

UNITED STATES OF AMERICA
POSTAL REGULATORY COMMISSION
WASHINGTON, DC 20268-0001

Before Commissioners:

Robert G. Taub, Chairman;
Michael Kubayanda, Vice Chairman;
Mark Acton;
Ann C. Fisher; and
Ashley E. Poling

Statutory Review of the System
for Regulating Rates and Classes
for Market Dominant Products

Docket No. RM2017-3

ORDER ADOPTING FINAL RULES FOR THE SYSTEM OF REGULATING RATES
AND CLASSES FOR MARKET DOMINANT PRODUCTS



Washington, DC 20268-0001
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Appendix A—Technical Appendix (Density and Retirement)

Appendix B—List of Commenters and Comments

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(Issued November 30, 2020)

I. INTRODUCTION

Pursuant to 39 U.S.C. § 3622(d)(3), the Commission adopts final rules modifying the ratemaking system for Market Dominant products. In 2006, Congress enacted the Postal Accountability and Enhancement Act (PAEA).¹ The PAEA required the Commission to promulgate regulations establishing a ratemaking system for Market

¹ Postal Accountability and Enhancement Act (PAEA), Pub. L. 109-435, 120 Stat. 3198 (2006).

Dominant products within 18 months after the law's enactment.² The PAEA mandated certain features that the ratemaking system in its initial form had to include, most prominently a price cap limiting rate increases to annual changes in the consumer price index for all urban consumers (CPI-U). See 39 U.S.C. § 3622(d)(1)(A). The PAEA also required the Commission to review the ratemaking system 10 years after the PAEA's enactment to determine if it had achieved 9 statutory objectives specified by the PAEA, taking into account 14 statutory factors. 39 U.S.C. § 3622(b), (c), and (d)(3). If the Commission determined that the ratemaking system had not achieved the statutory objectives, taking into account the statutory factors, then "the Commission may, by regulation, make such modification or adopt such alternative system...as necessary to achieve the objectives." 39 U.S.C. § 3622(d)(3).

On December 20, 2016, the Commission initiated its required review of the ratemaking system by issuing an advance notice of proposed rulemaking (ANPR).³ The ANPR established a framework for the review, appointed an officer of the Commission to represent the interests of the general public, and provided an opportunity for public comment. On December 1, 2017, the Commission issued its findings.⁴ In short, the Commission found that the ratemaking system was not achieving the statutory objectives, taking into account the statutory factors. Order No. 4257 at 275. The Commission therefore set about the task of "mak[ing] such modification or adopt[ing]

² 39 U.S.C. § 3622(a) instructs the Commission to establish "a modern system for regulating rates and classes for market-dominant products." This system for regulating rates and classes for Market Dominant products is collectively referred to as the "ratemaking system." The Commission promulgated regulations establishing the ratemaking system in 2007. See Docket No. RM2007-1, Order Establishing Ratemaking Regulations for Market Dominant and Competitive Products, October 29, 2007 (Order No. 43).

³ Advance Notice of Proposed Rulemaking on the Statutory Review of the System for Regulating Rates and Classes for Market Dominant Products, December 20, 2016 (Order No. 3673).

⁴ Order on the Findings and Determination of the 39 U.S.C. § 3622 Review, December 1, 2017 (Order No. 4257).

such alternative system...as necessary to achieve the objectives.” 39 U.S.C. § 3622(d)(3).

On the same day that it released its findings, the Commission issued a notice of proposed rulemaking (NPR) proposing a number of regulatory modifications to the ratemaking system intended to enable the system to achieve the statutory objectives.⁵ The NPR sought public comment on the Commission’s proposals, and the Commission received a wide range of comments in response. Based on the comments received, the Commission issued a revised notice of proposed rulemaking (Revised NPR) on December 5, 2019, again seeking public comment on the Commission’s revised proposals.⁶ The Commission once again received a wide range of comments, which are addressed in this Order.

⁵ Notice of Proposed Rulemaking for the System for Regulating Rates and Classes for Market Dominant Products, December 1, 2017 (Order No. 4258).

⁶ Revised Notice of Proposed Rulemaking, December 5, 2019 (Order No. 5337).

II. OVERVIEW

A. The Need for Modifications to the Ratemaking System

In Order No. 4257, the Commission identified specific aspects of the ratemaking system that had failed to achieve the PAEA's statutory objectives, taking into account the statutory factors. Prior to the enactment of the PAEA, the Postal Service operated under a cost-of-service ratemaking system with a break-even mandate, in which it was expected to generate sufficient revenue to cover its operating costs, but not retained earnings. Order No. 4257 at 24. Rates were set so that total estimated revenues would equal as nearly as practicable total estimated costs. *Id.* Proposed rate adjustments by the Postal Service were formally litigated before the Commission in quasi-judicial proceedings that were "complex, expensive, and time-consuming." *Id.* at 26.

The PAEA reformed postal ratemaking by ending the break-even mandate and encouraging the Postal Service to generate retained earnings. *Id.* at 31. It replaced the cost-of-service model for postal ratemaking with a price cap model in which rate increases were limited to annual changes in CPI-U. *Id.* at 32. It afforded the Postal Service greater pricing flexibility and enabled the Postal Service to implement new rates on a substantially shorter timeframe through a shorter and more streamlined process that did not require on-the-record hearings. *Id.* at 31-32. Other new features introduced by the PAEA included the requirement that the Postal Service establish service standards and publicly report on service performance, which it had not been required to do previously, as well as explicit requirements with regard to workshare discounts, which provide reduced prices to mailers who perform certain mail preparation activities prior to entering mail into the Postal Service's network.⁷

⁷ *Id.* at 33-34, 42-45, 130; see 39 U.S.C. §§ 3622(e), 3652(a)(2)(B), 3691.

At the time the PAEA was enacted, overall mail volume was increasing and the Postal Service's financial position appeared to be stable.⁸ Moreover, prior to the enactment of the PAEA, increases in Postal Service costs tended to track increases in the consumer price index (CPI). Order No. 4257 at 37. Given this environment, Congress anticipated that the PAEA's CPI-based price cap system would enable the Postal Service to generate sufficient revenues to cover all of its operating costs and statutorily mandated obligations, while at the same time motivating the Postal Service to cut costs and become more efficient. *Id.* at 32-33, 37. The PAEA was intended to allow the Postal Service to fund network expansion and necessary capital improvements because it removed the break-even restriction and allowed the Postal Service to generate retained earnings.⁹

However, the PAEA also established a significant new obligation for the Postal Service.¹⁰ It required the Postal Service to prefund future retiree health benefits (RHB), with the goal of reducing the Postal Service's future RHB liability by FY 2017. Order No. 4257 at 37 (citing PAEA, Pub. L. 109-435 § 803, 120 Stat. 3198 (2006)). These payments were to average \$5.6 billion per year.¹¹

The Commission found in Order No. 4257 that the Postal Service's operating environment changed rapidly after the PAEA was enacted. *Id.* at 35. The Great Recession, which began in 2007, had a substantial negative impact on Postal Service volume and revenues. *Id.* at 38. This economic downturn occurred in concert with

⁸ Order No. 4257 at 37. Market Dominant mail volume reached its peak in FY 2006—the year the PAEA was enacted. See Library Reference PRC-LR-RM2017-3/1, December 1, 2017, Excel file "PRC-LR-RM2017-3-1.xlsx," tab "Figure II-23," column F (displaying Market Dominant volume from FY 1997 through FY 2016).

⁹ *Id.* at 37 (citing S. Rep. 108-318 at 8, 11 (2004); H.R. Rep. 109-66, pt. 1, at 44, 118 (2005)).

¹⁰ Order No. 4257 at 37 (citing PAEA, Pub. L. 109-435 § 803, 120 Stat. 3198 (2006)).

¹¹ Order No. 4257 at 37 (citing PAEA, Pub. L. 109-435 § 803; 5 U.S.C. § 8909a(d)(3)(A)).

emergent technological trends (e.g., email, text messaging, and other electronic transmission of messages and information) that resulted in even greater volume declines for First-Class Mail, in particular—the Postal Service’s most profitable mail class.¹² Moreover, in the aftermath of the Great Recession there was a period of deflation, which constrained the Postal Service’s ability to raise rates given the CPI-based price cap.¹³

The first full fiscal year after implementation of the PAEA, FY 2008, was the first in which the Postal Service’s total revenue increased less than the CPI, and this trend continued every year thereafter. Order No. 4257 at 40. These reduced revenues were largely driven by volume declines. *Id.* Additionally, while historically increases in Postal Service costs had tended to track the CPI, beginning in FY 2006 that correlation began to diverge. *Id.* at 38. The Postal Service’s total costs increased dramatically in FY 2007, largely due to recognition of the RHB prefunding cost for the fiscal year as an expense, and then fluctuated up and down from year to year for reasons that the Commission determined “could [have been] the result of numerous factors, such as the [RHB] payments, expanding delivery network, reductions in total volume, and Postal Service cost saving initiatives.” *Id.* at 39-40. The result was that after the enactment of the PAEA the Postal Service’s total costs began exceeding its total revenues. *Id.* at 40.

The divergence between the Postal Service’s costs and revenues made it difficult for the Postal Service to accumulate retained earnings through sustained net income. The required RHB prefunding costs, increases in non-cash workers’ compensation

¹² *Id.*; see United States Government Accountability Office, Report No. GAO-20-385, U.S. Postal Service: Congressional Action is Essential to Enable a Sustainable Business Model, May 2020, at 8-9, available at: <https://www.gao.gov/assets/710/706729.pdf> (GAO-20-385).

¹³ Order No. 4257 at 38 (citing United States Department of Labor, Bureau of Labor Statistics, One Hundred Years of Price Change: The Consumer Price Index and the American Inflation Experience, April 2014, available at: <https://www.bls.gov/opub/mlr/2014/article/one-hundred-years-of-price-change-the-consumer-price-index-and-the-american-inflation-experience.htm>).

expenses,¹⁴ significant reductions in mail volume and revenue related to internet diversion, and the extensive business downturn and slow economic recovery following the Great Recession contributed to the inability to generate net income. *Id.* at 40-41. The Postal Service ultimately defaulted on the majority of the required annual RHB prefunding costs. Order No. 5337 at 82. Over the 10 years immediately preceding the enactment of the PAEA, the Postal Service reported a cumulative net income of \$11.3 billion. See Order No. 4257 at 30, Figure II-1. However, over the 10 years after the PAEA was enacted, the Postal Service suffered a cumulative net loss of \$59.1 billion. *Id.* at 171.

For purposes of organization, the Commission's analysis in Order No. 4257 grouped the PAEA's nine statutory objectives into three principal areas: (1) the structure of the ratemaking system; (2) the financial health of the Postal Service; and (3) service. *Id.* at 22. Each principal area was further divided into subtopics addressing relevant objectives and factors. *Id.*

Applying this framework, the Commission concluded that while the ratemaking system had fulfilled some of the PAEA's goals, the overall system had not achieved the statutory objectives, taking into account the statutory factors. *Id.* at 4. For the first principal area—the structure of the ratemaking system—the Commission found that the ratemaking system had resulted in predictable and stable rates, in terms of timing and magnitude (Objective 2); that it had reduced administrative burden and increased transparency (Objective 6); that it had provided the Postal Service with pricing flexibility (Objective 4); and that it had, on balance, maintained just prices (Objective 8). *Id.* at 142-145. However, the Commission found that the ratemaking system had not

¹⁴ The non-cash workers' compensation expense includes actuarial revaluations of existing cases and new cases, initial costs of new cases for the year, and any changes in the discount rate used to estimate the amount of current funds needed to settle all claims in the current year. This is separate from the cash payment which is made to the U.S. Department of Labor for the current year's cost of medical and compensation benefits and an administrative fee.

increased pricing efficiency (Objective 1). *Id.* at 145. This was because, first, the Commission determined that workshare discounts during the PAEA era had not been set as close as practicable to their avoided costs, despite the Postal Service having had the ability within the constraints of the price cap to have done so. *Id.* This failed to comport with the principles of Efficient Component Pricing (ECP), pursuant to which prices are most efficient when workshare discounts are set as closely as practicable to the avoided costs of particular workshare activities. *Id.* at 135-136. Second, the Commission found that multiple products had failed to cover their attributable costs during the PAEA era. *Id.* at 145. This failure did not comport with the principles of allocative pricing efficiency, pursuant to which prices are efficient when they are set at or above a product's marginal (or, in the Postal Service's case, "attributable") costs. *Id.* at 139-140.

For the second principal area—the financial health of the Postal Service—the Commission found that while the ratemaking system had been sufficient to provide for mail security and terrorism deterrence (Objective 7); had provided a sufficient mechanism to allocate institutional costs between Market Dominant products and Competitive products (Objective 9); and had generally enabled the Postal Service to achieve short-term financial stability, medium- and long-term financial stability had not been achieved (Objective 5). *Id.* at 247-249. This failure was evidenced by total revenue being inadequate to cover total costs, resulting in the Postal Service suffering a net loss every year during the PAEA era. *Id.* at 165-169. This accumulation of net losses resulted in accumulated deficits, which prevented the Postal Service from being able to achieve retained earnings. *Id.* at 169-171. The Commission determined that the Postal Service had not had any working capital (assets in excess of liabilities) during the PAEA era, its capital expenditure ratio had declined, and its debt ratio had steadily increased. *Id.* at 172-175.

The Commission also found that the Postal Service's costs had been reduced during the PAEA era, mostly in mail processing as a result of changes in the mail mix. *Id.* at 184-198. At the same time, however, the Commission found that "cost savings estimates from some of the Postal Service's initiatives are likely overstated and...the Postal Service could improve its quantitative measurement of the results of cost savings initiatives." *Id.* at 200. The Commission also noted that the Postal Service's unique cost structure constrained its ability to further reduce costs—specifically its pool of common ("institutional") costs; the labor-intensive nature of its business; its universal service obligation (USO); and its limited ability due to binding arbitration requirements to set wage rates, adjust its employee complement, and/or reduce workhours. *Id.* at 198-200.

The Commission found that the Postal Service's operational efficiency, as measured by total factor productivity (TFP), had generally increased during the PAEA era, although the Commission noted that operational efficiency may have been somewhat undermined by the Postal Service's failure to price workshare discounts as close as practicable to their avoided costs.¹⁵ Ultimately, the Commission concluded that while the Postal Service had been able to reduce costs and increase operational efficiency during the PAEA era, the results had been insufficient to achieve overall financial stability, and thus the incentives to reduce costs and increase operational efficiency had not been maximized as intended by the PAEA (Objective 1). *Id.* at 221-226. The Commission also found that there had not been an adequate mechanism under the ratemaking system to maintain reasonable rates (Objective 8) because the rates for certain products and mail classes had been insufficient to cover their

¹⁵ *Id.* at 203-208, 216-219. While workshare discounts and ECP, as previously detailed, generally implicate pricing efficiency, the Commission noted that workshare discounts set substantially below avoided costs may also necessitate the Postal Service's maintenance of a larger than necessary processing network, which implicates operational efficiency. *Id.* at 216.

attributable costs. *Id.* at 226-236. The Commission attributed this, at least in part, to the price cap limitation. *Id.* at 236.

Finally, for the third principal area—service (Objective 3)—the Commission found that service standards declined during the PAEA era because the Postal Service had reduced the high-quality service standards that were initially promulgated in 2007.¹⁶ With regard to service performance, the Commission concluded that the Commission’s *Annual Compliance Determination (ACD)* “has been and continues to be the proper vehicle for addressing [such issues].”¹⁷

Viewing the ratemaking system in the totality, the Commission concluded that “while some aspects...have worked as planned, overall, the system has not achieved the objectives of the PAEA.” Order No. 4257 at 5. This was largely due to the fact that “the operating environment on which the PAEA was designed changed quickly and dramatically after the PAEA was passed[],” and “this made it challenging for the ratemaking system under [the] PAEA to achieve the goals it was designed to achieve.” *Id.* at 45. As a result, “although the...CPI-based price cap system was anticipated, at the time of its implementation, to enable the Postal Service to produce sustained net income and generate retained earnings, that has not occurred.” *Id.* at 148. Based on

¹⁶ *Id.* at 273. The two major service standard changes in the first 10 years after the passage of the PAEA were reviewed by the Commission, prior to implementation, in Docket Nos. N2012-1 and N2014-1. The “Network Rationalization” initiative implemented by the Postal Service included changes to the service standards for First-Class Mail, Periodicals, USPS Marketing Mail, and Package Services. The “Load Leveling” initiative included changes to the service standards for USPS Marketing Mail. *Id.* at 264-273.

¹⁷ *Id.* The Commission is required by law to conduct a review every year in which it determines whether the Postal Service’s rates and fees for the previous fiscal year were in compliance with statutory and regulatory requirements, as well as whether the Postal Service met its service standards. This report is known as the “*Annual Compliance Determination*” or “ACD.” See 39 U.S.C. § 3653. If the Commission finds that the Postal Service is noncompliant, then it may take remedial action. Order No. 4257 at 273.

these findings, the Commission issued an NPR containing proposals to address the identified shortcomings of the ratemaking system.

B. Overview of Proposals in the NPR

In the NPR that the Commission issued concurrently with Order No. 4257, the Commission sought to maintain a CPI-based price cap system while proposing modifications to rectify those aspects of the ratemaking system that the Commission specifically determined had failed to achieve the PAEA's statutory objectives. The Commission's initial proposal consisted of five main elements.¹⁸ First, the Commission proposed a new rate authority mechanism called supplemental rate authority designed to address the Postal Service's inability to maintain medium-term financial stability consistent with Objective 5. Order No. 4258 at 38. This mechanism would provide the Postal Service with an additional 2 percentage points of rate authority per mail class for a period of 5 years. *Id.* at 41-43. The 2-percentage-point figure was based on the Postal Service's FY 2017 net loss, which was the most recent net loss figure available at that time. *Id.* at 40-41. The supplemental rate authority mechanism was designed so that after 5 years, the rate base would have been enlarged sufficiently that in the future CPI-only rate increases would be able to generate revenue sufficient to offset the annual net losses the Postal Service had been experiencing. *Id.* at 42. The Commission proposed to review the supplemental rate authority mechanism after 5 years in order to assess the Postal Service's financial performance. *Id.*

¹⁸ The Commission notes that the rules appearing in title 39 of the Code of Federal Regulations were re-organized effective April 20, 2020. See Docket No. RM2019-13, Order Reorganizing Commission Regulations and Amending Rules of Practice, January 16, 2020 (Order No. 5407). Prior to this reorganization, the rule revisions proposed in the NPR and Revised NPR were to have appeared primarily in 39 C.F.R. parts 3010, 3050, and 3055. There were also proposed changes to part 3020 to align with the proposed changes to part 3010. Under the new organizational scheme, part 3010 has been re-labeled part 3030, and part 3020 has been re-labeled part 3040. Parts 3050 and 3055 remain unchanged. The final rules adopted in this Order conform to this new organizational scheme.

Second, the Commission proposed a new rate authority mechanism called performance-based rate authority designed to address several of the ratemaking system's shortcomings simultaneously. *Id.* at 46-53. Specifically, the Commission found that three of the shortcomings it had identified in Order No. 4257 were interrelated. The failure to maintain long-term financial stability consistent with Objective 5 had led to an inability to invest in capital projects that could potentially have increased operational efficiency and reduced costs, which had led, in turn, to insufficient efficiency gains and cost reductions that undermined Objective 1. *Id.* At the same time, the failure to maintain long-term financial stability had also resulted in the Postal Service reducing its service standards, which undermined Objective 3. *Id.* To address these three interrelated problems holistically, the Commission proposed an additional 1 percentage point of rate authority per mail class annually. *Id.* at 56. The 1-percentage-point figure was based on a review of the Postal Service's net asset holdings, capital outlays, and borrowing authority. *Id.* at 53-54. In order to access this additional rate authority, the Postal Service would have to achieve distinct performance-based requirements for operational efficiency and service standard quality. *Id.* at 56. Specifically, 0.75 percentage points of the 1 percentage point in additional rate authority would be made available to the Postal Service if its most recent TFP growth, based on a rolling 5-year average, met or exceeded 0.606 percent.¹⁹ The remaining 0.25 percentage points of rate authority would be made available to the Postal Service if it had maintained its service standards at the same level of quality since its last rate proceeding. *Id.* at 70-72.

Third, the Commission issued a series of proposals with regard to non-compensatory products and mail classes, based on its finding that rates which failed to cover the attributable costs of the products or mail classes to which they applied

¹⁹ *Id.* at 61-63. The Commission determined that 0.606 percent reflected the average growth in TFP over the most recent 5-year period, from FY 2011 through FY 2016. *Id.*

undermined the Postal Service's financial integrity and were unreasonable and thus inconsistent with Objectives 5 and 8. See *id.* at 76. The Commission also determined that such rates undermined Objective 1 by failing to comport with the principles of allocative pricing efficiency. Order No. 4257 at 139-142. For non-compensatory products, the Commission's proposal consisted of rate requirements: in future rate proceedings the Postal Service would be required to propose rate increases for all such products that were at least 2 percentage points higher than the class average. Order No. 4258 at 77.

However, the Commission recognized that for mail classes for which the entire class was non-compensatory, meaning that class-level revenues were not sufficient to cover class-level attributable costs, the Postal Service would be faced with a dilemma. *Id.* at 81-82. Imposing rate requirements on individual products in such a class would not be sufficient to improve cost coverage because of the lack of products with positive cost coverage among which rates within the class could be rebalanced. *Id.* Therefore, the Commission proposed that the Postal Service be provided with an additional 2 percentage points in rate authority for non-compensatory mail classes. *Id.* at 84-85. If the Postal Service chose to adjust rates for such a class, it would be required to use all available rate authority. *Id.* at 84. If there were any products within a non-compensatory class for which product-level revenue exceeded product-level attributable costs, prices for such products could only be increased up to the level of the class average. *Id.* at 85. In addition, the Postal Service would not be permitted to reduce rates for products in a non-compensatory class. *Id.* Whether a product or class was properly classified as "non-compensatory" would be determined based on the most recent ACD. *Id.* at 77.

Fourth, the Commission issued a series of proposals with regard to workshare discounts designed to address practices the Commission had identified as undermining pricing efficiency and frustrating the achievement of Objective 1. *Id.* at 87-90. The

Commission proposed implementing workshare “bands”—ranges with upper and lower limits in which workshare discount passthroughs²⁰ would have to fall in order to be deemed compliant. *Id.* at 93. For workshare discounts in the Periodicals class, the Commission proposed a band between 75 percent and 125 percent. *Id.* For workshare discounts in all other classes, the Commission proposed a band between 85 percent and 115 percent. *Id.* The band for the Periodicals class was intended to take into account “the wider variance observed in passthroughs for Periodicals and ‘the educational, cultural, scientific, or informational value’ [(ECIS)] of those mailpieces.” *Id.* (quoting 39 U.S.C. § 3622(c)(11) and (e)(2)(C)). The Commission proposed a 3-year grace period during which existing passthroughs could be brought into compliance prior to enforcement. Order No. 4258 at 95.

²⁰ The relationship between workshare discounts and avoided costs is usually expressed as a percentage called a passthrough, which is calculated by dividing the discount by the avoided cost. A workshare discount that fully reflects ECP has a passthrough equal to 100 percent.

Finally, the Commission proposed a series of procedural improvements to its existing rules designed to improve aspects of the ratemaking system.²¹ The Commission proposed to enhance the schedule for regular and predictable rate adjustments by requiring the Postal Service to update it annually and provide certain information intended to increase transparency for mailers with regard to the Postal Service's planned price changes. Order No. 4258 at 101-102. The Commission also proposed extending the minimum notice period between the date the Postal Service filed a notice of proposed rate adjustment and the date the proposed rates could go into effect from 45 days to 90 days. *Id.* at 104-105. This was intended to codify the existing practice of the Postal Service and to allow adequate time for rate proceedings to be adjudicated so that proposed rates could take effect on its planned implementation date. *Id.* at 104. Commensurate with this, the Commission also proposed extending the periods for parties to comment on proposed rates, as well as the period for the

²¹ While the Commission found in Order No. 4257 that the ratemaking system had resulted in predictable and stable rates in terms of timing and magnitude, the Commission nevertheless noted two concerns. First, the PAEA required the Postal Service to "establish a schedule whereby rates, when necessary and appropriate, would change at regular intervals by predictable amounts." 39 U.S.C. § 3622(d)(1)(B). The Commission's implementing regulations required the Postal Service to maintain on file with the Commission a schedule for regular and predictable rate changes, which the Postal Service could revise "[w]henever [it] deem[ed] it appropriate." 39 C.F.R. § 3030.509(a), (e). In Order No. 4257, the Commission determined that while for the most part the Postal Service's notices had been consistent with its schedules for regular and predictable rate changes, there had been slight deviations based on external influences that were generally known to mailers. Order No. 4257 at 52-62. Thus, in practice the Commission found that the timing of price adjustments had been predictable and stable. *Id.* at 62. The Commission nevertheless noted, however, that the ratemaking system did not *require* the Postal Service to update its schedule of regular and predictable price changes, which resulted in mailers having to refer to other sources to get updated information when the schedules changed. *Id.*

Similarly, the PAEA required the Postal Service to provide public notice of proposed price adjustments at least 45 days before the implementation of new prices. 39 U.S.C. § 3622(d)(1)(C). The Commission incorporated this requirement in its implementing regulations. 39 C.F.R. § 3030.510(a). In Order No. 4257, however, the Commission noted that the Postal Service had, in practice, consistently provided at least 90 days—twice as much notice as required. Order No. 4257 at 63, 70. The Commission therefore concluded that the intervals between notices of proposed rate adjustments and implementation of new prices during the PAEA era had been predictable and stable. *Id.* at 65. The Commission noted, though, that during the PAEA era large-scale price adjustments had lasted an average of 62 days—more than the 45-day minimum requirement. *Id.* at 72. In practice, this had never been a problem because the Postal Service had always given at least 90 days' notice.

Commission to render its decision, which was intended to enable better evaluation of rate proceedings by the Commission. *Id.* In addition, the Commission proposed specifically enumerating the potential actions it could take if it determined that the Postal Service had failed to provide required information in a rate adjustment proceeding. *Id.* at 104-105.

C. Overview of Proposals in the Revised NPR

In response to the NPR, the Commission received and considered comments reflecting widely divergent views on all aspects of the Commission's proposed modifications to the ratemaking system. After considering these comments, the Commission revised several aspects of its initial proposal.

For the supplemental rate authority, the Commission was influenced by commenter concerns that the net loss for FY 2017 may not be a representative baseline for the amount of additional rate authority necessary. Order No. 5337 at 62. The Commission was also influenced by commenter concerns that the amount of additional rate authority under the Commission's initial approach was not tied to specific drivers of the Postal Service's net losses. *Id.* Some commenters endorsed the use of separate rate design elements (often called "X-," "Y-," or "Z-" factors) to modify the price cap and address issues such as cost drivers that are exogenous to the Postal Service. *Id.* at 64-70.

After considering these comments, the Commission dispensed with a singular mechanism for supplemental rate authority based on a fixed amount, as had initially been proposed, and replaced it with two separate mechanisms designed to provide revenue for costs that were largely outside of the Postal Service's control.²² These were: (a) the increase in per-unit cost resulting from declines in mail density and (b) statutorily mandated amortization payments for retirement costs. Order No. 5337 at 62. The Commission determined that these two sources of costs formed primary obstacles to the Postal Service's ability to generate net income. *Id.* The intent of this revision was to tie the amount of supplemental rate authority to the primary drivers of the Postal Service's net losses, as many of the commenters had suggested. *Id.*

To address mail density declines, the Commission proposed modifying the price cap to provide additional rate adjustment authority equal to the density-driven portion of increases in average cost-per-piece. *Id.* at 77-80. This amount would be calculated each year based on year-over-year changes in density. *Id.* at 77. This mechanism was dynamic and was meant to remain a permanent feature of the ratemaking system. *Id.*

To address the Postal Service's retirement amortization payments, the Commission proposed modifying the price cap to provide additional rate adjustment authority equal to the percentage by which total revenue would need to increase to provide sufficient revenue for the Postal Service to make its required retirement obligation payments. *Id.* at 95-103. This amount would be phased in over 5 years, after which time the rate base would be enlarged sufficiently such that CPI-only rate increases (if accompanied by an equivalent rate increase on Competitive products)

²² *Id.* at 62. In this document, the Commission's reference to costs largely outside of the Postal Service's control, or not directly within its control, is different from the costs the Postal Service refers to as "items over which we have no control" in its calculation of "controllable loss" on its Forms 10-K. See United States Postal Service, 2019 Report on Form 10-K, November 14, 2019, at 18 (Postal Service FY 2019 Form 10-K). The Postal Service excludes costs such as RHBf actuarial revaluation, retirement amortization expenses, workers' compensation expenses caused by actuarial revaluation and discount rate changes to calculate what it calls "controllable loss."

would be able to generate revenue sufficient to cover such obligations in the future. *Id.* at 95. The yearly amounts of additional rate authority would be recalculated annually to account for changing conditions, and the Postal Service would be required to remit any revenue generated as a result of such rate authority to its outstanding liability. *Id.* at 95-96. The Commission proposed to review the effect of this rate authority after 5 years to comprehensively analyze its impact. *Id.* at 94.

For the performance-based rate authority, the Commission was influenced by commenter concerns regarding the use of a 5-year rolling average for TFP and the unequal weighting of the efficiency and service standard mechanisms as initially proposed. *Id.* at 105. The Commission revised its proposal so that the Postal Service would only be required to exceed its prior-year TFP in order to be eligible for the additional rate authority. *Id.* at 134. In addition, the Commission removed the “split” between the 2 mechanisms—0.75 percentage points for efficiency gains and 0.25 percentage points for the maintenance of service standards—and proposed that the Postal Service be eligible for the additional 1 percentage point of rate authority in any given year if it met both the efficiency and service standard requirements. *Id.* at 144-145.

For non-compensatory products and mail classes, the Commission revised its proposal to make the use of the additional 2 percentage points in rate authority for non-compensatory mail classes optional on the Postal Service’s part. *Id.* at 172. This was done both in response to commenter concerns about the unknown effects of sharp price increases on mail volumes for non-compensatory classes and because of the Commission’s agreement with the Postal Service that the Postal Service as the operator is in the best position to assess demand and other market considerations. *Id.* The Commission also removed the procedural requirement that determinations as to which products and/or mail classes are non-compensatory be made in ACD proceedings. *Id.* at 173. The Commission found that this would give it more flexibility to address

products or classes that become non-compensatory without having to wait for the next ACD to specifically identify them as such. *Id.*

For workshare discounts, the Commission made a number of revisions to its initial proposal based on commenter feedback. The overall goal of the revisions was to encourage incremental improvement in pricing efficiency. *Id.* at 193. The Commission abandoned the passthrough bands and instead proposed to address excessive and below-avoided-costs workshare discounts separately. *Id.* at 201. With its “do no harm principle,” the Commission proposed that the Postal Service be prohibited from changing workshare discounts set equal to avoided costs, from reducing workshare discounts set below avoided costs, and from increasing workshare discounts set above avoided costs. *Id.* at 206-207. The Postal Service would only be permitted to propose a workshare discount with a passthrough below 85 percent if the proposed discount was new; the discount was at least 20-percent higher than the existing discount; or the Postal Service filed an application in advance of a rate adjustment proceeding showing by a preponderance of the evidence that it could not increase the discount by 20 percent without impeding operational efficiency. *Id.* at 200. Similarly, the Postal Service would only be permitted to propose an excessive workshare discount if the discount was new; the discount was at least 20 percent lower than the existing discount; the discount was justified under 39 U.S.C. § 3622(e)(2)(c) (pertaining to preferential rates for mailpieces having ECSI value) including an adequate rationale for the Postal Service being unable to reduce the discount; or the Postal Service filed an application in advance of a rate adjustment proceeding showing by a preponderance of the evidence that rate shock or operational efficiency concerns limited its ability to lower the discount, would lead to volume loss and reduced contribution to institutional costs, or would result in further increases in rates paid by mailers not able to take advantage of the discount. *Id.* at 203 (citing 39 U.S.C. § 3622(e)(2)(B)-(D) and (e)(3)). In light of the foregoing revisions, the Commission dispensed with the 3-year grace period initially proposed,

finding concerns about phasing in the new requirements to be addressed by the incremental improvement approach. Order No. 5337 at 206.

In response to commenter concerns regarding the potential of increased revenue to undermine the Postal Service's incentives to pursue cost reductions and efficiency increases, the Commission in the Revised NPR proposed a new set of cost-reduction reporting requirements. *Id.* at 212-231. These reporting requirements were designed to provide transparency with regard to the Postal Service's cost-reduction efforts and to ensure that the Postal Service remained focused on pursuing cost reductions and efficiency increases consistent with Objectives 1, 5, and 6. *Id.* at 221-226. The Commission proposed that the Postal Service report annually on unit costs for Market Dominant mail products. *Id.* at 227-229. Additional reporting would be required when unit costs for an individual Market Dominant product increased by more than the class average. *Id.* The Commission also proposed that the Postal Service be required to provide detailed reporting with regard to large-scale cost-reduction initiatives, including ongoing reporting to monitor the impact of such initiatives on performance metrics and unit costs. *Id.* at 229-231. In addition, the Commission proposed that the Postal Service be required to provide summary information with regard to smaller-scale projects. *Id.* at 231.

With regard to the procedural improvements in the Commission's initial proposal, there was one substantive change in the Revised NPR. Specifically, the Commission proposed to discontinue addressing the statutory objectives and factors in individual rate adjustment proceedings. *Id.* at 239-240. The Commission also proposed to review the modified ratemaking system in its entirety after 5 years to assess the effects of the changes and the evolving economic trends affecting the mailing industry. *Id.* at 243. The Commission added that if an unforeseen change occurred before the 5-year review period, the Commission would respond as necessary prior to the 5-year review. *Id.*

D. Final Rules

In response to the Revised NPR, the Commission once again received and considered a large number of comments. Based on consideration of these comments, the Commission has made further revisions to the final rules being adopted in this Order. The most significant revision is that the Commission has elected to withdraw the proposed performance-based rate authority from these rules. See Section VI.C., *infra*. The Commission intends to open a separate rulemaking to further study potential modifications to the ratemaking system that link financial incentives and/or consequences to efficiency gains, cost reductions, and the maintenance of service standards. See *id*. A separate rulemaking focused on these issues will permit the Commission to evaluate whether, when, and how to introduce a performance incentive mechanism. Moreover, it will allow the Commission to do so without delaying implementation of the remainder of these rules. See *id*. The Commission is, however, adopting two of the proposed reporting requirements related to the performance-based rate authority for purposes of transparency. Specifically, the Commission is requiring the Postal Service, at the time when it files its *Annual Compliance Report (ACR)*, provide the input data and calculations used to produce the annual TFP estimates, and to provide a description of and reason for any changes to the service standards (including relevant business rules), or certify that no changes have occurred. See Section VI.D., *infra*.

With regard to the density-based rate authority and retirement-based rate authority, the final rules contain a slight revision and a clarification. They permit the Postal Service to retain density-based rate authority as unused rate adjustment authority for purposes of 39 U.S.C. § 3622(d)(2)(C). See Section IV.C., *infra*. They also clarify that a minor rate change of one or two rate cells would not trigger the necessity of using the retirement-based rate authority in such an adjustment. See Chapter V. and Section XII.C.2, *infra*.

With regard to non-compensatory products and mail classes, the final rules contain slight revisions. The Commission has revised the rules with respect to non-compensatory products to permit the Postal Service to exclude from the mandatory rate increase requirements products for which it does not set rates (such as, for example, certain international mail products that have rates set by treaty).²³ The Commission has also revised the rules with respect to non-compensatory mail classes to permit the Postal Service to generate unused rate adjustment authority. See Section VII.B.3., *infra*.

With regard to workshare discounts, the final rules contain a slight revision. The Commission has expanded one of the bases for waiver to permit the use of waiver for below-avoided-costs workshare discounts that relate to non-compensatory products. See Section VIII.C.4., *infra*.

For the cost-reduction reporting requirements, the final rules contain a minor, clarifying revision. The Commission has revised the rules pertaining to summary reports for smaller-scale projects to clarify that the Postal Service does not have to prepare summary reports for prospective cost-reduction projects that have not yet been formalized. See Section IX.C.4., *infra*.

The final rules do not contain any changes with respect to the proposed procedural improvements or the Commission's proposal to review the modifications to the ratemaking system in 5 years (subject to Commission discretion to consider aspects of the system sooner, if needed). See Chapters X. and XI., *infra*. As a result, the

²³ See Section VII.A.3., *infra*. This exemption does not exempt these products from the price cap, but only the mandatory remedy for non-compensatory products. Should the Postal Service later gain control over setting rates for these products and the product is found to be non-compensatory, the mandatory price increase would apply. Moreover, this change would not affect the Commission's compliance determination; thus, the Commission may still find these products to be non-compliant and order appropriate remedial action to resolve the non-compliance. See *also* discussion at Section XII.C.4., *infra*.

Commission will undertake a holistic review of the system 5 years after the final rules go into effect, with the possibility of earlier review of discrete aspects of the system if necessary. See Chapter XI., *infra*. The Commission also makes a small number of minor corrections and clarifications. See Chapters XII., XIII., XIV., and XV., *infra*.

The modified ratemaking system that the Commission adopts in this Order is designed to achieve all of the PAEA's statutory objectives in conjunction with each other. The modifications address the deficiencies of the PAEA ratemaking system identified in Order No. 4257 while maintaining achievement of the remaining objectives. See Chapter XIII., *infra*. The density-based rate authority and retirement-based rate authority are designed to address the two underlying causes of the Postal Service's net losses that are largely outside of its control: the proportion of the increase in per-unit cost resulting from the decline in mail density and the statutorily mandated amortization payments for retirement costs. By addressing these two substantial and uncontrollable drivers of the Postal Service's financial distress, the final rules are intended to permit the Postal Service to improve its financial stability (Objective 5) and maintain existing service standards (Objective 3), without reducing the Postal Service's incentives to reduce costs and increase efficiency (Objective 1). See Chapter XIII., *infra*.

The rules with respect to non-compensatory products and mail classes are designed to incrementally address long-standing problems through a combination of rate-setting criteria for non-compensatory products and the provision of additional rate authority for non-compensatory mail classes. This is necessary to increase allocative pricing efficiency (Objective 1), address inefficient pricing practices that undermine the Postal Service's financial health (Objective 5), and rebalance rates to be just and reasonable to both mailers and to the Postal Service (Objective 8). See Chapter XIII., *infra*.

The workshare discount rules are designed to address inefficient pricing practices with regard to workshare discounts to make them better conform to the principles of ECP (Objective 1). See Chapter XIII., *infra*.

The cost-reduction reporting requirements are designed to incentivize the Postal Service to improve the robustness of its cost-benefit analyses (Objective 1) in order to facilitate financially sound decision-making (Objective 5). This should simultaneously improve the availability and comprehensibility of information with regard to the Postal Service's cost-reduction efforts to the Commission and postal stakeholders without imposing an undue administrative burden on the Postal Service (Objective 6). See Chapter XIII., *infra*.

The revisions to the Commission's procedural rules all take into account the competing priorities of increasing transparency and reducing administrative burden (Objective 6). These improvements are designed to make it easier for the public to comprehend and to participate in rate proceedings, as well as to facilitate the administration of the ratemaking process. See Chapter XIII., *infra*.

Taken together, the modifications adopted in these final rules are designed to remedy the deficiencies in the existing ratemaking system identified in Order No. 4257. The modified ratemaking system is intended to balance the PAEA's statutory objectives in order to place the Postal Service on a sustainable financial path for the future.

Two groups of commenters have sought to supplement the record in this docket with late-filed comments related to the effects of the ongoing COVID-19 pandemic on the Postal Service and the mailing industry.²⁴ They construe these effects as constituting a change in circumstances substantial enough to require reconsideration of aspects of the Commission's proposed rules. *MPA et al.* Proffered Supplemental Comments at 1-2; *NPPC et al.* Proffered Supplemental Comments at 1-2. They specifically take issue with the amount of rate authority that would be generated by the density-based rate authority mechanism in light of the volume shifts the Postal Service has experienced under pandemic conditions. *MPA et al.* Proffered Supplemental Comments *passim*; *NPPC et al.* Proffered Supplemental Comments *passim*. *NPPC et al.* also argue that \$10 billion in additional borrowing authority that Congress recently made available to the Postal Service as a result of the pandemic through the Coronavirus Aid, Relief, and Economic Security Act (CARES Act)²⁵ is relevant to the Commission's conclusions in Order No. 4257 regarding the Postal Service's liquidity. *NPPC et al.* Proffered Supplemental Comments at 14-15. The Postal Service opposes both motions to file supplemental comments.²⁶

²⁴ Supplemental Comments of MPA – the Association of Magazine Media, the Alliance of Nonprofit Mailers, and the Association for Postal Commerce, July 2, 2020 (*MPA et al.* Proffered Supplemental Comments); Motion for Late Acceptance of the Supplemental Comments of MPA – the Association of Magazine Media, the Alliance of Nonprofit Mailers, and the Association for Postal Commerce, July 2, 2020; Supplemental Comments of the National Postal Policy Council, the American Bankers Association, the American Catalog Mailers Association, the American Forest & Paper Association, the Association for Mail Electronic Enhancement, the Association for Postal Commerce, the Association for Print Technologies, the Envelope Manufacturers Association, the Greeting Card Association, the Major Mailers Association, the National Retail Federation, MPA – the Association of Magazine Media, the National Association of Presort Mailers, the News Media Alliance, the National Newspaper Association, the Parcel Shippers Association, Printing United Alliance, and the Saturation Mailers Coalition, July 6, 2020 (*NPPC et al.* Proffered Supplemental Comments); Motion for Late Acceptance of Supplemental Comments, July 6, 2020.

²⁵ Pub. L. No. 116-136 (2020).

²⁶ Opposition of the United States Postal Service to Motions for Late Acceptance of Supplemental Comments, July 13, 2020.

The Commission is cognizant of the ongoing COVID-19 pandemic and its effects on the Postal Service and the mailing industry. However, given what is currently known about the pandemic and its effects, the Commission finds that nothing specific to the pandemic undermines the findings the Commission made in Order No. 4257. In Order No. 4257, the Commission followed 39 U.S.C. § 3622(d)(3)'s directive to review the Market Dominant ratemaking system 10 years after the PAEA's enactment to determine if the existing ratemaking system was achieving the PAEA's statutory objectives, taking into account the statutory factors. The Commission determined that it was not. As discussed above, among the primary failings identified by the Commission were the existing ratemaking system's inability to enable the Postal Service to generate sufficient revenues to achieve medium- or long-term financial stability; its failure to maximize incentives for the Postal Service to reduce costs and increase pricing and operational efficiency; and its failure to maintain reasonable rates. Order No. 4257 at 135-136, 139-140, 145, 165-175, 203-208, 216-219, 221-236, 247-249.

All of these findings remain applicable today, because the existing ratemaking system remains in place. The Postal Service's finances remain unstable.²⁷ Its liabilities far exceed its assets, and its liquidity has been maintained only by defaulting on statutorily mandated payments.²⁸ Its working capital has declined even further since Order No. 4257 was issued. *Id.* at 29. The Postal Service's debt ratio has increased, and it still has very limited capacity for capital expenditure. *Id.* at 31-34. In addition, the problems identified in Order No. 4257 with respect to pricing and operational efficiency

²⁷ See Docket No. ACR2019, Postal Regulatory Commission, Financial Analysis of United States Postal Service Financial Results and 10-K Statement, Fiscal Year 2019, May 7, 2020, at 2-6 (FY 2019 Financial Analysis) (discussing the Postal Service's continuing financial instability).

²⁸ See FY 2019 Financial Analysis at 4, 27-38. The Postal Service has defaulted on most of the statutorily mandated RHB payments since FY 2008. Beginning in FY 2017, the Postal Service also improved its liquidity by defaulting on statutorily-mandated payments for the amortization of unfunded retirement benefits to the Federal Employees Retirement System (FERS) and the Civil Service Retirement System (CSRS).

and unreasonable rates have not abated.²⁹ These challenges, which all pre-date the pandemic, are expected to persist as long as the existing ratemaking system remains in effect, and nothing specific to the pandemic alters the Commission's findings with regard to these deficiencies.

That said, the pandemic has led to an unprecedented slowdown in economic activity in the United States and worldwide, across nearly all industries.³⁰ With regard to the Postal Service, the most pronounced effect thus far has been a shift in the mail mix due to changes in demand, with significant volume declines for some Market Dominant products and significant volume increases for packages, the majority of which are classified as Competitive products.³¹ There are both cost and revenue implications associated with such shifts that are not yet fully clear. It is also unclear if these shifts will be permanent or if volumes will return to their former levels in the future. However, the commenters seeking to supplement the record misconstrue the effects of these circumstances with respect to the Commission's proposals from Order No. 5337.

The density-based rate authority mechanism is designed to respond to exogenous increases in per-unit cost due to declines in the average volume of mail per delivery point. Order No. 5337 at 70-80. The Postal Service has no direct control over

²⁹ See Docket No. ACR2019, *Annual Compliance Determination*, March 25, 2020, at 12-23 (FY 2019 ACD) (discussing workshare discounts that continue to be set either above or below their avoided costs), 24-67 (discussing products and mail classes that continue to be non-compensatory), 155-175 (discussing the Postal Service's ongoing problems processing and delivering flat-shaped mail products, including its inability to improve operational efficiency with respect to flats processing).

³⁰ See, e.g., United States Department of Commerce, Bureau of Economic Analysis (August 27, 2020); Gross Domestic Product, 2nd Quarter 2020 (Second Estimate); Corporate Profits, 2nd Quarter 2020 (Preliminary Estimate), available at: <https://www.bea.gov/news/2020/gross-domestic-product-2nd-quarter-2020-second-estimate-corporate-profits-2nd-quarter>.

³¹ See United States Postal Service, Revenue, Pieces and Weight (RPW) Report by Rate Category and Special Service for Quarter 3, Fiscal Year 2020, August 7, 2020, available at: <https://www.prc.gov/dockets/document/114156>; United States Postal Service, Quarterly Report on Form 10-Q, August 7, 2020, at 10-11, available at: <https://www.prc.gov/docs/114/114136/2020%2008-06%20Form%2010-Q.pdf>.

the volume of mail that mailers send, or over growth in the number of delivery points that necessitates expanding its delivery network. Forcing it to internalize the proportion of per-unit costs that are largely outside of its control undermines its ability to achieve medium- and long-term financial stability. *Id.* at 77. The commenters concede that in terms of per-piece volume, the declines that have occurred with respect to Market Dominant mail far exceed the increases in packages. MPA *et al.* Proffered Supplemental Comments at 3; NPPC *et al.* Proffered Supplemental Comments at 4. Nevertheless, they point to the fact that the contribution per piece associated with packages is generally higher than it is with most Market Dominant mail (*i.e.*, packages are generally priced further above their costs than most Market Dominant mailpieces), and they maintain that the additional revenue realized from packages since the pandemic started has offset the revenue lost as a result of declines in Market Dominant mail. MPA *et al.* Proffered Supplemental Comments at 3; NPPC *et al.* Supplemental Comments at 3-4. They argue that the density component is flawed because it relies on changes in volume without taking into account associated changes in revenue or contribution. MPA *et al.* Proffered Supplemental Comments at 3; NPPC *et al.* Comments at 2-14.

However, the proportion of per-unit costs that the density component is designed to address are based on declines in volume per delivery point. Regardless of the contribution or revenue associated with packages versus other types of mail, the reality is that—as a result of the pandemic—there are fewer total mailpieces today over which the costs of servicing and maintaining the Postal Service’s network can be distributed, which causes the per-unit cost of delivering the remaining mailpieces to increase. It is

these costs, which are largely outside of the Postal Service's direct control in the short- and medium-term, that the density-based rate authority is designed to address.³² Moreover, with respect to commenters' arguments concerning the effect of price increases on mailers,³³ it is important to note that the final rules adopted in this Order permit the Postal Service to retain density-based rate authority as unused rate adjustment authority for purposes of 39 U.S.C. § 3622(d)(2)(C). See Section IV.C., *infra*. Thus, the Postal Service will be able to exercise its business judgment as to how much density-based rate authority to use in a given year. Given the need for the proposed changes notwithstanding any impacts from the pandemic and the Commission's commitment to conduct a full-scale review in 5 years, subject to Commission discretion to consider aspects of the system sooner if needed, the Commission does not find changes to the density component to be warranted at this time.

Likewise, with regard to NPPC *et al.*'s assertion that the CARES Act undermines the Commission's findings from Order No. 4257 concerning the Postal Service's liquidity, the increase in borrowing authority made available to the Postal Service in the CARES Act does not impact the Commission's analysis. The \$10-billion increase in borrowing authority is limited to addressing short-term operating needs due to the COVID-19 emergency. Pub. L. No. 116-136 § 6001(b). Such funds cannot be used to address the Postal Service's longer-term financial stability, outstanding debt, and capital expenses. See Pub. L. No. 116-136 § 6001(b)(1)(A)-(B) (additional borrowing authority

³² The Commission also notes that the density formula takes into account potential divergence of Competitive density and Market Dominant density. See Order No. 5337 at 72-73. Specifically, the formula takes the smaller of either the change in density overall or the change in density for Market Dominant (which prevents Competitive density losses from increasing the density factor, and requires the Competitive density gains to offset the Market Dominant density losses). *Id.*

³³ MPA *et al.* Proffered Supplemental Comments at 3-4; NPPC *et al.* Proffered Supplemental Comments at 14.

is “to be used for...operating expenses; and [...] not...to pay any outstanding debt of the Postal Service”).

Moreover, access to additional borrowing authority and any associated temporary increase in liquidity would at most improve the Postal Service’s short-term financial stability, meaning its ability to meet its immediate day-to-day operational needs. Order No. 4257 at 159-165. The Commission has never found that the Postal Service lacked short-term financial stability. *Id.* Borrowing more money to cover operating expenses, however, would do nothing to address the net losses and accumulated deficits that undermine the Postal Service’s medium- and long-term financial stability, which the Commission identified in Order No. 4257 as a primary deficiency in the existing ratemaking system. *Id.* at 247-249. It is these net losses that the density-based rate authority, retirement-based rate authority, and non-compensatory product/class modifications to the ratemaking system adopted in this Order are designed to address. As a result, the increase in borrowing authority resulting from the CARES Act does not impact the Commission’s findings of deficiencies with the existing ratemaking system, and the Commission does not find changes to these aspects of the final rules necessary at this time.

While an agency rule cannot “entirely fail[] to consider an important aspect of [a] problem...[,]”³⁴ agencies have discretion to exercise their expertise in order to determine whether supplementary comments on an existing record are necessary, and “[c]ourts normally reverse an agency’s decision not to reopen the record only for abuse of discretion.”³⁵ The Commission has reviewed the supplemental comments proffered by these commenters, but the Commission finds that the assertions contained in them do not affect the basis for the final rules the Commission is adopting in this Order. The

³⁴ *Motor Vehicle Mfrs. Ass’n of the United States v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43 (1983).

³⁵ *Eastern Carolinas Broad. Co. v. FCC*, 762 F.2d 95, 103 (D.C. Cir. 1985).

Commission determines that this matter can be adequately decided on the existing record. The Commission therefore denies both motions to supplement the record.

As a final matter, the Commission notes that it is committed to reviewing the modified ratemaking system in 5 years to assess its performance, and to reviewing specific components of the modified ratemaking system sooner than 5 years if needed. See Chapter XI., *infra*. The commenters themselves acknowledge that there is a great deal of uncertainty regarding the effects of the COVID-19 pandemic. MPA *et al.* Proffered Supplemental Comments at 7; NPPC *et al.* Proffered Supplemental Comments at 4-6. It is simply unknowable at present how long the downturn will persist or what the long-term economic effects will be, either for the Postal Service or for mailers. However, as stated above, the pandemic does not change any of the findings the Commission made in Order No. 4257 regarding the deficiencies of the current ratemaking system. Therefore, the Commission does not find any good cause to further delay implementation of the modified ratemaking system developed in this docket. The Commission will monitor the effects of the final rules on the Postal Service and on mailers in light of economic developments, and it will intervene as necessary if economic conditions prevent the final rules from operating as intended to achieve the objectives of section 3622.

III. STATUTORY AUTHORITY

A. Introduction and Background

The legal authority for the rules adopted in this docket derives from 39 U.S.C. § 3622, which was enacted as part of the PAEA in 2006.³⁶ Section 3622, which is titled “Modern rate regulation,” contains six subsections, which can be summarized as follows. Subsection (a), entitled “Authority generally,” provides that within 18 months after the PAEA’s enactment the Commission shall “by regulation establish (and may from time to time thereafter by regulation revise) a modern system for regulating rates and classes for market-dominant products.” 39 U.S.C. § 3622(a). Subsection (b) enumerates nine specific “objectives” that the ratemaking system shall be designed to achieve. 39 U.S.C. § 3622(b). Subsection (c) enumerates 14 specific “factors” that the Commission must take into account in establishing or revising the ratemaking system. 39 U.S.C. § 3622(c).

Subsection (d), titled “Requirements,” contains three paragraphs. Paragraph (d)(1), titled “In general,” provides that the ratemaking system shall: include an annual price cap on rate increases corresponding to the CPI-U; establish a schedule of rate changes; require public notice and an opportunity for Commission review of proposed rate adjustments; and establish procedures for rate adjustments. 39 U.S.C. § 3622(d)(1)(A)-(E).

³⁶ PAEA, Pub. L. No. 109-435, 120 Stat. 3198 (2006). The Commission also has general authority to “promulgate rules and regulations and establish procedures...and take any other action [it] deem[s] necessary and proper to carry out [its] functions and obligations to the Government of the United States and the people as prescribed under [Title 39 of the United States Code].” 39 U.S.C. § 503.

Paragraph (d)(2), titled “Limitations,” provides that the price cap is to be applied to mail products at the class level;³⁷ permits the Postal Service to round rates and fees as long as the overall rate increase does not exceed the price cap; and contains provisions regarding the use of unused rate authority.³⁸

Paragraph (d)(3), titled “Review,” provides the following specific language which is at the heart of the issue with regard to the Commission’s legal authority in this docket:

Ten years after the date of enactment of the [PAEA] and as appropriate thereafter, the Commission shall review the system for regulating rates and classes for market-dominant products established under this section to determine if the system is achieving the objectives in subsection (b), taking into account the factors in subsection (c). If the Commission determines, after notice and opportunity for public comment, that the system is not achieving the objectives in subsection (b), taking into account the factors in subsection (c), the Commission may, by regulation, make such modification or adopt such alternative system for regulating rates and classes for market-dominant products as necessary to achieve the objectives.

39 U.S.C. § 3622(d)(3).

Subsection (e) contains provisions related to workshare discounts, which are rate discounts provided to mailers who perform certain mail preparation activities prior to entering mail into the Postal Service’s network. 39 U.S.C. § 3622(e)(1). Subsection (e) generally requires (subject to certain exceptions) that such discounts not exceed the cost that the Postal Service avoids as a result of not having to perform the individual workshare activity in question. 39 U.S.C. § 3622(e)(2)-(4). Finally, subsection (f)

³⁷ A mail class is a grouping of Market Dominant mail products, “as defined in the Domestic Mail Classification Schedule as in effect on the date of enactment of the [PAEA].” 39 U.S.C. § 3622(d)(2)(A). There are five such mail classes: First-Class Mail; USPS Marketing Mail; Periodicals; Package Services; and Special Services.

³⁸ 39 U.S.C. § 3622(d)(2)(A)-(C). Unused rate authority is leftover rate authority that the Postal Service opts not to avail itself of in any given price adjustment. 39 U.S.C. § 3622(d)(2)(C)(i). Under the PAEA, the Postal Service is permitted to retain such rate authority for future use, subject to a number of conditions and limitations. 39 U.S.C. § 3622(d)(2)(C)(ii)-(iii).

provides for a 1-year transition period to the PAEA ratemaking system from the ratemaking system that preceded it. 39 U.S.C. § 3622(f).

The PAEA represented a compromise between two competing postal reform bills in Congress. Order No. 4258 at 19-21. The first bill, H.R. 22, was introduced in the House of Representatives by Representative John McHugh on January 4, 2005, and reported back to the House out of the House Committee on Government Reform with amendments on April 28, 2005.³⁹ On July 26, 2005, H.R. 22 as amended was passed by the House.⁴⁰ Under this bill proposed section 3622(d) was titled “Allowable Provisions.” 151 Cong. Rec. H6523 (daily ed. July 26, 2005). It provided that the ratemaking system could include one or more of several forms of regulation: incentive regulation (*e.g.*, price caps, revenue targets); cost-of-service regulation; or any other form of regulation that the Commission considered appropriate to achieve the bill’s listed objectives, consistent with its listed factors. *Id.* Proposed section 3622(e) under this bill was titled “Limitation.” *Id.* This provision would have capped annual product-level rate increases at the CPI, unless the Commission were to determine, after public notice and comment, that an above-CPI increase was reasonable, equitable, and necessary. *Id.*

The second bill, S. 662, was introduced in the Senate by Senator Susan Collins on March 17, 2005, and reported back to the Senate out of the Homeland Security and Governmental Affairs Committee with amendments on July 14, 2005.⁴¹ On February 9, 2006, the Senate considered these and additional amendments by unanimous consent, and the bill, as amended, was passed.⁴² Under this bill, proposed section 3622(d) was

³⁹ 151 Cong. Rec. H72 (daily ed. Jan. 4, 2005); 151 Cong. Rec. H2734 (daily ed. Apr. 28, 2005).

⁴⁰ 151 Cong. Rec. H6511, H6548-H6549 (daily ed. July 26, 2005) (Roll Call No. 430).

⁴¹ 151 Cong. Rec. S2994, S3012-S3031 (daily ed. Mar. 17, 2005); 151 Cong. Rec. S8301 (daily ed. July 14, 2005).

⁴² 152 Cong. Rec. S898-S927 (daily ed. Feb. 9, 2006).

titled “Requirements,” and was subdivided into paragraphs titled “In general” and “Limitations.” *Id.* at S913-S914. The content of these paragraphs employed similar language to that which was eventually used in the final version of the PAEA. *Compare id. with* 39 U.S.C. § 3622(d)(1) and (2). Specifically, they provided for an annual class-level price cap indexed to CPI-U, with a narrow exception for “unexpected and extraordinary circumstances.” *Id.*

Also on February 9, 2006, the Senate through unanimous consent passed H.R. 22 by replacing H.R. 22’s text with the text of S. 662.⁴³ Therefore, as passed by the Senate, H.R. 22 contained the same title structure as S. 662, with proposed section 3622(d)—titled “Requirements”—being subdivided into two paragraphs titled “In General” and “Limitations.” *Id.* at S929. The Senate then sent H.R. 22, as amended and passed by the Senate, back to the House and requested a conference to resolve the differences between the two versions.⁴⁴ None of the versions of the bills described above included the review provision that would eventually be codified at 39 U.S.C. § 3622(d)(3). Nor was this provision referenced in hearings, committee reports, or the presidential signing statement. Instead, paragraph (d)(3) was included only in the final version of the PAEA introduced on December 7, 2006—H.R. 6407.⁴⁵ Pursuant to a compromise between the Senate and the House, H.R. 6407 blended together concepts appearing in the separate versions of the bills described above, including combining each bill’s respective lists of objectives and factors.

⁴³ 152 Cong. Rec. at S927-S942 (daily ed. Feb. 9, 2006). H.R. 22 had been pending in the Senate since July 27, 2005. 151 Cong. Rec. S9155, S9156 (daily ed. July 27, 2005).

⁴⁴ *Id.* at S927, S942. For instance, as passed by the House on July 26, 2005, H.R. 22 provided for the ratemaking system to achieve 7 objectives and for the Commission to take into account 11 factors. 151 Cong. Rec. H6523 (daily ed. July 26, 2005). By contrast, as passed by the Senate on February 9, 2006, H.R. 22 provided for the ratemaking system to achieve 8 objectives and for the Commission to take into account 13 factors. 152 Cong. Rec. at S928-S929 (daily ed. Feb. 9, 2006).

⁴⁵ H.R. 6407, 109th Cong. § 3622(d)(3) (2006).

There is only one statement in the Congressional Record about the review provision contained at paragraph (d)(3), and it was made upon receipt of the final version of the bill on December 8, 2006. Senator Collins, the Senate sponsor of postal reform, remarked:

The Postal Service will have much more flexibility, but the rates will be capped at the CPI. That is an important element of providing 10 years of predictable, affordable rates, which will help every customer of the Postal Service plan. After 10 years, the Postal Regulatory Commission will review the rate cap and, if necessary, and following a notice and comment period, the Commission will be authorized to modify or adopt an alternative system.

While this bill provides for a decade of rate stability, I continue to believe that the preferable approach was the permanent flexible rate cap that was included in the Senate-passed version of this legislation. But, on balance, this bill is simply too important, and that is why we have reached this compromise to allow it to pass. We at least will see a decade of rate stability, and I believe the Postal [Regulatory] Commission, at the end of that decade, may well decide that it is best to continue with a CPI rate cap in place. It is also, obviously, possible for Congress to act to reimpose the rate cap after it expires. But this legislation is simply too vital to our economy to pass on a decade of stability. The consequences of no legislation would be disastrous for the Postal Service, its employees, and its customers.⁴⁶

The Commission's interpretation of section 3622, based on its plain language, its structure, and its purpose, and as confirmed by its legislative history, has been consistent throughout this docket. That interpretation, which is more fully articulated below, can be summarized as follows. Subsection (a) directed the Commission to promulgate rules establishing the ratemaking system following the PAEA's enactment. The ratemaking system was required to be designed to achieve the statutory objectives enumerated in subsection (b), taking into account the statutory factors enumerated in subsection (c).

⁴⁶ 152 Cong. Rec. S11,674, S11,675 (daily ed. Dec. 8, 2006) (statement of Sen. Collins).

In its initial form, the ratemaking system was also required to contain certain mandatory features, as embodied in paragraphs (d)(1) and (d)(2), as well as subsection (e). The most significant of these features was the CPI-U price cap. However, those mandatory features were the product of the legislative compromise that reconciled the competing postal reform bills in Congress. A central component of that legislative compromise was paragraph (d)(3), which directed the Commission to review the ratemaking system after 10 years and determine if the ratemaking system, including the mandatory features, was achieving the statutory objectives set out in subsection (b), taking into account the statutory factors set out in subsection (c). If the Commission determined that the ratemaking system was not achieving the statutory objectives, taking into account the statutory factors, then the Commission was empowered to “by regulation, make such modification or adopt such alternative system...as necessary to achieve the objectives.” 39 U.S.C. § 3622(d)(3).

The Commission conducted the required review and issued its findings on December 1, 2017. See *generally* Order No. 4257. The Commission determined that the ratemaking system has not achieved the statutory objectives, taking into account the statutory factors. Pursuant to paragraph (d)(3), the Commission thereafter set about the task of “mak[ing] such modification or adopt[ing] such alternative system...as necessary to achieve the objectives.” In doing so, the Commission interprets its authority as encompassing all aspects of the ratemaking system under section 3622, including the price cap provisions at paragraphs (d)(1) and (d)(2) and the workshare discount provisions in subsection (e).

Order No. 4258 addressed comments positing that the Commission lacks the statutory authority to modify or replace the CPI-U price cap. Order No. 4258 at 14-25. The Commission analyzed the three primary arguments raised by commenters to support this position: that the plain language of section 3622 clearly forecloses modification or replacement of the CPI-U price cap; that modification or replacement of the CPI-U price cap would be inconsistent with the PAEA's legislative history; and that modification or replacement of the CPI-U price cap would produce unconstitutional results. *Id.* The Commission also addressed comments objecting to the inclusion of workshare discounts as an issue in this proceeding. *Id.* at 18-19, 25.

Order No. 5337 addressed comments received in response to Order No. 4258 pertaining to the Commission's initial proposal to make additional rate adjustment authority available to the Postal Service. Order No. 5337 at 18-31, 32-57. The Commission also addressed comments concerning the statutory authority underlying the Commission's initial proposal to limit the setting of inefficient workshare discounts. *Id.* at 57-58. Many of the comments received in response to Order No. 4258 echoed prior remarks submitted in this proceeding. Order No. 5337 at 18-27. Some commenters reiterated their prior positions again with regard to the revised proposal presented in Order No. 5337.⁴⁷ Generally, no new arguments concerning statutory authority were introduced in response to Order No. 5337.⁴⁸

Primarily, commenters contending that the Commission lacks the statutory authority to adopt the final rules in this Order argue that a reviewing court would reject the Commission's interpretation of section 3622 under the two-step framework for

⁴⁷ See ANM *et al.* Comments at 91-99; ANM *et al.* Reply Comments at 16-17; ABA Comments at 4-5.

⁴⁸ Because no commenter re-raised arguments having to do with the constitutionality of modifying or replacing the CPI-U price cap in response to Order No. 5337, those arguments are not addressed in this Order. They were addressed in detail in Order Nos. 4258 and 5337. See Order No. 4258 at 23-25; Order No. 5337 at 53-57.

evaluating an agency's interpretation of its governing statute set forth in *Chevron, U.S.A., Inc. v. Nat. Res. Def. Council, Inc.*, 467 U.S. 837 (1984). Under *Chevron* step one, a court considers whether "Congress has directly spoken to the precise question at issue." *Chevron*, 467 U.S. at 842. If so, "that is the end of the matter; for the court, as well as the agency, must give effect to the unambiguously expressed intent of Congress." *Id.* at 842-843. If not, then the court proceeds to *Chevron* step two and considers whether the agency's interpretation "is based on a permissible construction of the statute." *Id.* at 843. The court must defer to the agency's interpretation if it is "reasonable." *Id.* at 844.

Because paragraph (d)(3) expressly authorizes the Commission to adopt regulations modifying the ratemaking system or adopting an alternative ratemaking system if necessary to achieve the statutory objectives, the final rules adopted in this Order would survive judicial scrutiny under *Chevron* step one. Moreover, even if there were any ambiguity as to whether the Commission had the authority to adopt the final rules, because the Commission's interpretation is based on a permissible and reasonable construction of section 3622, the Commission would be accorded deference under *Chevron* step two.

In the remainder of this section, the Commission first addresses the positions of commenters asserting that the Commission lacks the statutory authority to make additional rate adjustment authority available to the Postal Service. The Commission then addresses issues that pertain exclusively to the Commission's statutory authority to limit the setting of inefficient workshare discounts, as well as the Commission's authority to modify specific Postal Service reporting requirements.

B. Additional Rate Authority

1. The PAEA expressly authorizes the Commission to modify or replace all aspects of the existing ratemaking system, including the CPI-U price cap, if necessary to achieve the statutory objectives.

At *Chevron* step one, the question is whether the meaning of a statute is unambiguously clear. *Chevron*, 467 U.S. at 842-843. In order to determine this, a court must “exhaust the traditional tools of statutory construction to determine whether Congress has spoken to the precise question at issue[,...][which] include examination of the statute’s text, legislative history, and structure, as well as its purpose.”⁴⁹ Courts “consider not only the language of the particular statutory provision under scrutiny, but also the structure and context of the statutory scheme of which it is a part.”⁵⁰

The Commission’s interpretation of section 3622 begins with the text of paragraph (d)(3). Paragraph (d)(3) states:

If the Commission determines, after notice and opportunity for public comment, that the system is not achieving the objectives in subsection (b), taking into account the factors in subsection (c), the Commission may, by regulation, make such modification or adopt such alternative system for regulating rates and classes for market-dominant products as necessary to achieve the objectives.

39 U.S.C. § 3622(d)(3). In the absence of an express definition, a statutory phrase must be given its ordinary meaning.⁵¹ “May” is a permissive word, which indicates that the Commission has discretion under paragraph (d)(3) whether to take any action

⁴⁹ *Petit v. United States Dep’t of Educ.*, 675 F.3d 769, 781 (D.C. Cir. 2012) (quoting *Bell Atl. Tel. Cos. v. FCC*, 131 F.3d 1044, 1047 (D.C. Cir. 1997)) (internal marks omitted).

⁵⁰ *Petit*, 675 F.3d at 781-782 (quoting *Cty. of L.A. v. Shalala*, 192 F.3d 1005, 1014 (D.C. Cir. 1999)) (internal marks omitted).

⁵¹ *Smith v. United States*, 508 U.S. 223, 228 (1993).

following its 10-year review of the ratemaking system.⁵² “Or” is a disjunctive word, which indicates that the two options on either side of it have distinct meanings.⁵³

Of the two options presented in paragraph (d)(3), the word “modification” is defined as “the making of a limited change in something.”⁵⁴ Therefore, “make such modification” connotes the making of moderate changes to the existing ratemaking system.⁵⁵ On the other hand, “alternative” is defined as “a proposition or situation offering a choice between two or more things *only one of which may be chosen*.”⁵⁶ Therefore, the phrase “adopt such alternative system” contemplates replacement of the existing ratemaking system with a different ratemaking system.⁵⁷

Accordingly, if the Commission determines, after conducting its required review of the ratemaking system, that the ratemaking system is not achieving the statutory objectives, taking into account the statutory factors, then the Commission has discretion to, by regulation, either “make such modification [to the ratemaking system]...as necessary to achieve the objectives,” which connotes moderate change to the existing ratemaking system, or “adopt such alternative system...as necessary to achieve the

⁵² Order No. 4258 at 14; see *United States v. Rodgers*, 461 U.S. 677, 706 (1983) (“The word ‘may,’ when used in a statute, usually implies some degree of discretion.” (citations omitted)).

⁵³ Order No. 4258 at 14; see *Loughrin v. United States*, 573 U.S. 351, 357 (2014) (“[o]rdinary use [of the term ‘or’] is almost always disjunctive, that is, the words it connects are to be given separate meanings.” (internal marks and citation omitted)); *Chao v. Day*, 436 F.3d 234, 236 (D.C. Cir. 2006) (terms connected using the disjunctive “or” must be given separate meanings).

⁵⁴ See Merriam-Webster Dictionary, available at: <https://www.merriam-webster.com/dictionary/modification>.

⁵⁵ Order No. 4258 at 15 (quoting 39 U.S.C. § 3622(d)(3)); see *MCI Telecomms. Corp. v. Am. Tel. & Tel. Co.*, 512 U.S. 218, 228 (1994) (“‘Modify,’ in our view, connotes moderate change.”).

⁵⁶ See Merriam-Webster Dictionary, available at: <https://www.merriam-webster.com/dictionary/alternative> (emphasis added).

⁵⁷ Order No. 4258 at 15 (quoting 39 U.S.C. § 3622(d)(3)); see Merriam-Webster Dictionary, available at: <https://www.merriam-webster.com/dictionary/adopt> (“adopt” defined as “to accept formally and put into effect”).

objectives,” which contemplates replacement of the existing ratemaking system with a different ratemaking system. See Order No. 4258 at 14-15 (quoting 39 U.S.C. § 3622(d)(3)). In either instance, the only limit that paragraph (d)(3) imposes on the scope of any such changes is that they must be “necessary” to achieve the statutory objectives. Order No. 4258 at 15. “Necessary” means “logically unavoidable.”⁵⁸

The scope of the Commission’s authority under paragraph (d)(3) plainly extends to all aspects of the ratemaking system under section 3622, including the price cap provisions at paragraphs (d)(1) and (d)(2). Order No. 4258 at 25; Order No. 5337 at 35. This interpretation takes into account the text and structure of section 3622 as a whole, and properly gives the statutory language its ordinary meaning. Order No. 5337 at 35 (citing *Smith*, 508 U.S. at 228). Paragraph (d)(3) grants the Commission authority to modify the “system” or to adopt an “alternative system.” The word “system” is used throughout section 3622. Subsection (a) instructs the Commission to establish a “modern system for regulating rates and classes for market-dominant products.” 39 U.S.C. § 3622(a). Subsection (b) provides that the “system” shall be designed to achieve the statutory objectives. 39 U.S.C. § 3622(b). Subsection (c) provides that in establishing the “system” the Commission shall take into account the statutory factors. 39 U.S.C. § 3622(c). Subsection (d), at paragraphs (d)(1) and (d)(2), provides additional features that the “system” shall include, including the CPI-U price cap. 39 U.S.C. § 3622(d)(1)-(2). Subsection (d) also, at paragraph (d)(3), provides that if the Commission, after conducting its required 10-year review, determines that the “system” is not achieving the statutory objectives, taking into account the statutory factors, then the Commission may by regulation modify or replace the “system” as necessary to achieve the statutory objectives. 39 U.S.C. § 3622(d)(3). As ordinarily defined,

⁵⁸ Order No. 4258 at 15; see Merriam-Webster Dictionary, available at: <https://www.merriam-webster.com/dictionary/necessary>.

“system” is a general term referring to a set of connected things or parts forming a complete whole.⁵⁹ It is clear that all of the provisions within section 3622 relate to the same “system” of ratemaking, including the CPI-U price cap provisions, and that under paragraph (d)(3) all aspects of that “system” are subject to review and, if necessary to achieve the statutory objectives, potential modification or replacement. Order No. 5337 at 35-36.

The structure of subsection (d), specifically the relationship between paragraph (d)(3) and paragraphs (d)(1) and (d)(2), also serves to confirm this. Paragraph (d)(3)’s review provision follows the price cap provisions set out in paragraphs (d)(1) and (d)(2). Each of paragraph (d)(2)’s limitations modify the general provisions contained in paragraph (d)(1). *Id.* at 36. This structure reinforces the conclusion that the provisions at paragraphs (d)(1) and (d)(2) are part of the system subject to review and potential modification or replacement under paragraph (d)(3). *Id.*

Moreover, textual differences between paragraph (d)(3) and subsection (a) plainly demonstrate that the extent of regulatory action permissible under paragraph (d)(3) is broader than under subsection (a). *Id.* Subsection (a) provides that:

The Postal Regulatory Commission shall, within 18 months after the date of enactment of this section, by regulation establish (and may from time to time thereafter by regulation revise) a modern system for regulating rates and classes for market-dominant products.

39 U.S.C. § 3622(a). The definition of “establish” is “to institute (something, such as a law) permanently by action or agreement.”⁶⁰ The definition of “revise” is “to look over

⁵⁹ Order No. 5337 at 35; see Merriam-Webster Dictionary, available at: <http://www.merriam-webster.com/dictionary/system> (“system” defined as “a regularly interacting or interdependent group of items forming a unified whole”).

⁶⁰ Order No. 4258 at 16; see Merriam-Webster Dictionary, available at: <https://www.merriam-webster.com/dictionary/establish>.

again in order to correct or improve.”⁶¹ The use of parentheticals along with the conjunction “and” explains the relationship between “establish” and “revise”—the ratemaking system established pursuant to subsection (a) is subject to periodic revision by the Commission at the Commission’s discretion. Order No. 4258 at 16; Order No. 5337 at 36. Thus, “establish” and “revise” are connected powers under subsection (a)—any “revision” is to the ratemaking system “established” under subsection (a). Order No. 5337 at 36. This differs from the wording of paragraph (d)(3), which speaks of “modifying” the system *or* “adopt[ing] [an] alternative system”—two separate options with different meanings. Order No. 4258 at 17; Order No. 5337 at 36-37.

The conditions necessary to trigger the Commission’s authority under paragraph (d)(3) are more demanding than those under subsection (a). Subsection (a) required the Commission to set up the ratemaking system within a specified period after the PAEA was enacted, and it permits the Commission to improve or correct those regulations “from time to time thereafter” through normal rulemaking procedures. Order No. 4258 at 16. Paragraph (d)(3), by contrast, is not triggered until several separate and specific requirements are met: first, a review of the ratemaking system by the Commission 10 years after the PAEA’s enactment, following notice and an opportunity for public comment; and second, a determination by the Commission that the ratemaking system has not achieved the statutory objectives, taking into account the statutory factors.⁶²

⁶¹ Order No. 4258 at 16; see Merriam-Webster Dictionary, available at: <https://www.merriam-webster.com/dictionary/revise>.

⁶² 39 U.S.C. § 3622(d)(3); see Order No. 4258 at 16; Order No. 5337 at 37.

The different language used in subsection (a) compared to paragraph (d)(3), coupled with the existence of separate triggering mechanisms, and in conjunction with the overall structure of section 3622, in which any regulatory action under paragraph (d)(3) is premised on a finding that the ratemaking system established under subsection (a) has failed to achieve the statutory objectives, taking into account the statutory factors, demonstrates that Congress intended to create two separate but complementary processes. First, Congress provided for the Commission's general authority to set up and periodically recalibrate the ratemaking system in its initial form under subsection (a), which was required to include certain mandatory features.⁶³ Second, Congress provided for the Commission's specific authority pursuant to paragraph (d)(3) to review the ratemaking system established under subsection (a) after 10 years and modify or replace any part of it, including the mandatory features, as necessary to achieve the statutory objectives. Order No. 4258 at 17; Order No. 5337 at 36-37. Thus, it is plain that subsection (a) and paragraph (d)(3) serve different purposes within the statutory scheme of section 3622, and that the Commission's authority under paragraph (d)(3) is broader than the Commission's authority under subsection (a). Order No. 4258 at 17-18; Order No. 5337 at 36-37. The purpose of paragraph (d)(3) is plainly to ensure that the statutory objectives in subsection (b) are being met and, if needed, to empower the Commission to remedy any failure to meet the objectives. Order No. 5337 at 37.

⁶³ Historically, the Commission had not possessed such broad regulatory authority. Order No. 4258 at 17; Order No. 5337 at 43. Prior to the enactment of the PAEA, the Postal Rate Commission, as the Postal Regulatory Commission was formerly known, was limited to "review of rate, classification, and major service changes, unadorned by the overlay of broad FCC-esque responsibility for industry guidance and of wide discretion in choosing the appropriate manner and means of pursuing its statutory objective." Order No. 4258 at 17 n.30 (citing *Mail Order Ass'n of Am. v. U.S. Postal Serv.*, 2 F.3d 408, 415 (D.C. Cir. 1993 (quoting *Governors of U.S. Postal Serv. v. Postal Rate Comm'n*, 654 F.2d 108, 117 (D.C. Cir. 1981))). The PAEA transformed the Postal Rate Commission into the Postal Regulatory Commission, a separate independent agency with regulatory oversight of the Postal Service. *Id.* (citing *U.S. Postal Serv. v. Postal Reg. Comm'n*, 717 F.3d 209, 210 (D.C. Cir. 2013)).

Paragraph (d)(3) places only one limit on the features that a “modifi[ed]” or “alternative system” can contain: such features must be necessary to achieve the statutory objectives in subsection (b). There is no requirement that any other specific feature of the existing ratemaking system be retained, including the CPI-U price cap. Moreover, subsection (b), in which the statutory objectives are set out, states that the objectives are to be applied in conjunction with each other, not in conjunction with any other statutory provisions. Order No. 4258 at 15; Order No. 5337 at 40.

In reaching its interpretation of section 3622, the Commission has considered alternative interpretations and constructions offered by commenters.⁶⁴ Commenters have cited the title of subsection (d)—“Requirements”—as meaning that any modified or alternative ratemaking system promulgated pursuant to paragraph (d)(3) must contain the features specified in paragraphs (d)(1) and (d)(2).⁶⁵ Commenters have similarly cited the use of the word “shall” in paragraph (d)(1) (*i.e.*, “The system for regulating rates and classes for market dominant products *shall*...contain an annual limitation on the percentage change in rates...equal to the change in [CPI-U]...” (emphasis added)) as making the CPI-U price cap mandatory for any and all versions of the ratemaking

⁶⁴ In response to Order No. 5337, two of these commenters, ANM *et al.* and ABA, have renewed their previous arguments, which are addressed below. National Postal Policy Council, Major Mailers Association, National Association of Presort Mailers, and Association for Mail Electronic Enhancement (collectively, NPPC *et al.*) incorporate all of their prior arguments by reference. NPPC *et al.* Comments at 9. A new commenter, the Coalition for a 21st Century Postal Service (C21), also adopts by reference in its reply comments the general arguments advanced by other commenters in this proceeding that the Commission lacks the statutory authority to modify or replace the CPI-U price cap. C21 Reply Comments at 3.

⁶⁵ 2014 ANM *et al.* White Paper at 4-7; Comments of the Major Mailers Association, the National Association of Presort Mailers, and the National Postal Policy Council, March 20, 2017, at 14-15 (2017 MMA *et al.* Comments); Initial Comments of the Greeting Card Association, March 20, 2017, at 29-31 (2017 GCA Comments) (citing *Ratzlaf v. United States*, 510 U.S. 135, 143 (1994)); Comments of the National Postal Policy Council, the Major Mailers Association, and the National Association of Presort Mailers, March 1, 2018, at 22-23 (2018 NPPC *et al.* Comments); Comments of Alliance of Nonprofit Mailers, American Catalog Mailers Association, Inc., Association for Postal Commerce, Idealliance and MPA—the Association of Magazine Media, March 1, 2018, at 17, 21-22 (2018 ANM *et al.* Comments).

system that might be adopted.⁶⁶ Alliance of Nonprofit Mailers, Association for Postal Commerce, MPA—the Association of Magazine Media, American Catalog Mailers Association, Direct Marketing Association of Washington, Nonprofit Alliance, Envelope Manufacturers Association, Saturation Mailers Coalition, and Continuity Shippers Association (collectively, ANM *et al.*), and the American Bankers Association (ABA) continue to make these arguments in response to Order No. 5337. ANM *et al.* Comments at 91-92; ABA Comments at 4.

As an initial matter, the Commission has noted that section titles are not dispositive—they can aid in resolving an ambiguity but they cannot enlarge text or confer powers.⁶⁷ Nevertheless, the Commission maintains that its interpretation of paragraph (d)(3) is consistent with the “Requirements” title of subsection (d) and the use of “shall” in paragraph (d)(1), because it is the mandatory features—the “requirements”—of the ratemaking system established under subsection (a), which were put in place during the PAEA’s first decade, that are subject to review and potential modification or replacement under paragraph (d)(3). Order No. 5337 at 40. The structure of subsection (d), in which paragraph (d)(3) follows paragraphs (d)(1) and (d)(2), and the text of paragraph (d)(3), which does not impose any specific requirement on a modified or alternative ratemaking system other than that its features must be necessary to achieve the statutory objectives, both confirm this. Order No. 5337 at 36, 38-39.

⁶⁶ Alliance of Nonprofit Mailers; the Association for Postal Commerce; the Association of Marketing Service Providers; the Direct Marketing Association; EMA; MPA—the Association of Magazine Media; the National Association of Advertising Distributors, Inc.; and the Saturation Mailers Coalition, Limitations on the Commission’s Authority Under Section 3622(d)(3), October 28, 2014, at 6-7 (2014 ANM *et al.* White Paper); Comments of Alliance of Nonprofit Mailers, Association for Postal Commerce, and MPA—the Association of Magazine Media, March 20, 2017, at 9-10 n.2 (2017 ANM *et al.* Comments); Comments of American Bankers Association, March 20, 2017, at 8-9 (2017 ABA Comments); Comments of American Bankers Association, March 1, 2018, at 4-5 (2018 ABA Comments); 2018 ANM *et al.* Comments at 11; 2018 NPPC *et al.* Comments at 20-22.

⁶⁷ Order No. 4258 at 16 (citing *Pa. Dep’t. of Corr. v. Yeskey*, 524 U.S. 206, 212 (1998)).

ANM *et al.* argue in response to Order No. 5337 that paragraphs (d)(1), (d)(2), and (d)(3) are each requirements of the ratemaking system, and “[n]othing in the law’s structure states that paragraph (d)(3) eliminates the CPI cap from paragraph (d)(1).” ANM *et al.* Comments at 93-94. However, this argument ignores the statutory context on which the second sentence of paragraph (d)(3) is premised—a finding that the ratemaking system established under subsection (a), which included the provisions in paragraphs (d)(1) and (d)(2), has failed to achieve the statutory objectives, taking into account the statutory factors. Moreover, it ignores the fact that the only limit paragraph (d)(3) places on the Commission’s ability to modify the ratemaking system or to adopt an alternative ratemaking system is that such changes must be necessary to achieve the objectives in subsection (b). Paragraph (d)(3) does not say that a modified or alternative ratemaking system has to contain the features specified in paragraphs (d)(1) and (d)(2).

Commenters have argued that under general canons of statutory construction, specific provisions, such as the price cap provision at paragraph (d)(1)(A), trump general provisions, such as paragraph (d)(3).⁶⁸ However, the logic underlying this general principle does not hold with respect to paragraph (d)(3) because paragraph (d)(3) expressly contemplates the potential modification or replacement of other provisions of the ratemaking system under section 3622, including the provisions contained in paragraphs (d)(1) and (d)(2). In Order No. 4258, the Commission found that the language of paragraph (d)(3) was intentionally broad, stating that “Congress knew how to impose express limits on the scope of [an] ‘alternative system’ but chose not to do so with respect to the Commission’s authority under [paragraph] (d)(3).” Order No. 4258 at 15.

⁶⁸ 2014 ANM *et al.* White Paper at 15 (citing *Navarro-Miranda v. Ashcroft*, 330 F.3d 672, 676 (5th Cir. 2003)).

Commenters have contended that it was not necessary for paragraph (d)(3) to contain a textual modifier limiting the scope of what a modified or alternative system could consist of because the relevant restrictions appear in paragraphs (d)(1) and (d)(2). 2018 ANM *et al.* Comments at 21, 23. In response to Order No. 5337, ANM *et al.* continue to argue that paragraph (d)(3) does not specifically reference the price cap at all, and that “Congress clearly knew how to explicitly refer to the CPI cap....” ANM *et al.* Comments at 94. They maintain that “[paragraphs] (d)(1) and (d)(2) set forth the required parameters of the system[,]” and “it would have been superfluous for Congress to have [repeated them in paragraph (d)(3)].” *Id.* at 98-99. However, nothing in paragraph (d)(3) states that the Commission’s authority is limited by paragraphs (d)(1) or (d)(2), and the structure of subsection (d) reinforces the conclusion that paragraphs (d)(1) and (d)(2) are both part of the system subject to modification or replacement under paragraph (d)(3). Order No. 5337 at 38. The Commission continues to conclude that if Congress had intended to restrict the scope of the Commission’s authority in this way, it could have done so expressly.⁶⁹

Commenters have argued that if Congress had intended to enact a sunset date on the CPI-U price cap provision contained in paragraph (d)(1)(A) it would have done so explicitly. 2018 NPPC *et al.* Comments at 25-26. They have noted that paragraph

⁶⁹ Order No. 5337 at 38 (citing *Smith*, 508 U.S. at 228-229 (rejecting a *Chevron* step one challenge contending that the statutory phrase “use of a firearm” referred only to use as a weapon and did not include use of a firearm as an item of barter to receive drugs, holding that “[s]urely petitioner’s treatment of his [firearm] can be described as ‘use’ within the everyday meaning of that term[,]” and “[h]ad Congress intended the narrow construction petitioner urges, it could have so indicated.”)).

Notably, there are instances in the text of section 3622 where Congress explicitly restricted the scope of a particular provision. Paragraph (c)(4), for example, limits the scope of “alternative means of sending and receiving letters and other mail matter at reasonable costs” to alternative means which are “available.” 39 U.S.C. § 3622(c)(4); Order No. 4258 at 15. This confirms that Congress knew how to impose limits on the scope of what a modified or alternative ratemaking system could consist of, but it chose not to do so with respect to paragraph (d)(3), and instead drafted it to be intentionally broad. Order No. 4258 at 15-16; Order No. 5337 at 38. The plain language of paragraph (d)(3) leaves it to the Commission’s discretion to determine what regulatory changes to the existing ratemaking system, if any, are logically required to achieve the statutory objectives. Order No. 4258 at 15.

(d)(2) imposes specific limits on paragraph (d)(1), and they have asserted the general legal principle that where certain exceptions to a general prohibition (*i.e.*, the price cap provision at paragraph (d)(1)) are enumerated specifically, others are not to be implied.⁷⁰ As the Commission has explained, however, its interpretation does not rest on an implied exception to paragraph (d)(1); it rests on the express language of paragraph (d)(3), which contemplates that paragraph (d)(1) is part of the system that is to be reviewed and potentially modified or replaced. Order No. 5337 at 41. Moreover, no sunset provision was needed for the CPI-U price cap (or any other feature of the existing ratemaking system) because paragraph (d)(3) does not automatically remove the CPI-U price cap (or any other feature of the existing ratemaking system). *Id.* at 40-41. If the existing ratemaking system did not suffer from deficiencies that prevented it from achieving the statutory objectives, taking into account the statutory factors, the Commission's authority under paragraph (d)(3) would not have been invoked and the existing ratemaking system would have remained unchanged. *Id.*

Commenters have argued that the quantitative pricing standards (*i.e.*, paragraphs (d)(1) and (d)(2)) outrank the qualitative pricing standards (*i.e.*, the statutory objectives and factors listed in subsections (b) and (c)) within the hierarchy of pricing standards set out in section 3622.⁷¹ However, regardless of how one classifies the hierarchy of pricing standards for purposes of the existing ratemaking system, the plain language of paragraph (d)(3) states that the only criteria that a modified or alternative ratemaking system are required to meet are the statutory objectives in subsection (b). Order No. 5337 at 39-40.

⁷⁰ 2018 NPPC *et al.* Comments at 26 (citing *Andrus v. Glover Constr. Co.*, 446 U.S. 608, 616-617 (1980)).

⁷¹ 2014 ANM *et al.* White Paper at 12; 2017 MMA *et al.* Comments at 15-16; 2018 ANM *et al.* Comments at 18.

Commenters have asserted that for purposes of paragraph (d)(3) “adopt such alternative system” does not meaningfully differ from “make such modification,” and that “revise” in subsection (a) and “modify” in paragraph (d)(3) are synonymous—they are both ways to “adopt an alternative system.” 2018 ANM *et al.* Comments at 16-17. However, to interpret “adopt such alternative system” as no different than a “modification” would drain the ordinary meaning from the phrase “alternative system,” which connotes a far more fundamental degree of change than “modification.” Order No. 5337 at 41. It would also ignore the use of “or,” a disjunctive word separating the two phrases that connects terms with separate meanings. *Id.* at 41-42.

Likewise, to interpret “revise” in subsection (a) and “modify” in paragraph (d)(3) as synonymous would ignore the important textual differences between the provisions that provide necessary context to understanding their meaning. “Revise” in subsection (a) is joined to the “establishment” of the ratemaking system by the conjunction “and” and the use of a parenthetical. Hence, “revisions” under subsection (a) are revisions to the ratemaking system “established” under subsection (a). The “modification” and “alternative system” authorities in paragraph (d)(3), on the other hand, are not available unless the Commission has made a finding that the ratemaking system established under subsection (a) has not achieved the statutory objectives, taking into account the statutory factors. *Id.* Hence, the power to “modify” the ratemaking system under paragraph (d)(3) is plainly broader than the power to “revise” it under subsection (a). Therefore, a plain reading of the PAEA does not support the contention that “adopt such alternative system” is synonymous with, or merely intended to explicate the meaning of, “make such modification,” or that “revise” in subsection (a) is synonymous with “modify” in paragraph (d)(3). *Id.* at 42.

A large number of comments have cited the word “system” used throughout section 3622 and argued—invoking the presumption of consistent usage—that consistent use of the word “system,” without any qualifiers on it in paragraph (d)(3) such

as “the first system” or “the initial system,” implies that it should be given the same meaning in each instance in which it appears.⁷² These commenters have maintained that the “system” established under subsection (a) is the same “system” subject to modification or replacement under paragraph (d)(3), and as such, it is bound by the same requirements, including those contained in paragraphs (d)(1) and (d)(2). *Id.* These commenters have viewed the “system” subject to modification or replacement under paragraph (d)(3) as consisting only of the implementing regulations that the Commission adopted pursuant to subsection (a), and they maintain that the Commission may alter those regulations only to the extent that such alterations do not conflict with the text of section 3622, including paragraphs (d)(1) and (d)(2).⁷³ In sum, these commenters have argued that the scope of the Commission’s authority under paragraph (d)(3) is limited to the scope of the Commission’s authority under subsection (a).⁷⁴ ANM *et al.* and ABA continue to make these same arguments in response to Order No. 5337. ANM *et al.* Comments at 91-92; ABA Comments at 4-5.

These arguments are unpersuasive. First, the most straightforward reading of the consistent use of the word “system” is that all of the provisions of section 3622 are part of the “system” to be reviewed and potentially modified or replaced under paragraph (d)(3), including paragraphs (d)(1) and (d)(2). Order No. 5337 at 35-36. This reading takes into account the text and structure of section 3622 as a whole, and accords the word “system” its ordinary meaning, in which it refers to a set of connected things or parts forming a complete whole. *Id.* at 35. This reading gives equal recognition to each use of the word “system” in section 3622. Subsection (a) required

⁷² 2014 ANM *et al.* White Paper at 10; 2017 ABA Comments at 8-10; 2018 ABA Comments at 5; 2018 ANM *et al.* Comments at 13, 23 n.8, 24; 2018 NPPC *et al.* Comments at 23-25.

⁷³ 2017 ABA Comments at 9; 2017 MMA *et al.* Comments at 14-15; 2017 GCA Comments at 31-32; 2018 ANM *et al.* Comments at 2, 12-13; 2018 NPPC *et al.* Comments at 19.

⁷⁴ 2014 ANM *et al.* White Paper at 9-11; 2017 ABA Comments at 9; 2017 MMA *et al.* Comments at 14-15; 2018 ANM *et al.* Comments at 10-13; 2018 NPPC *et al.* Comments at 23-24.

the Commission to establish the “system of ratemaking;” that “system” was initially required to include certain mandatory features, including those in paragraphs (d)(1) and (d)(2), and under paragraph (d)(3) that “system” in its entirety is subject to review and potential modification or replacement. In arguing that the scope of the Commission’s authority under paragraph (d)(3) is limited to the scope of the Commission’s authority under subsection (a), these commenters ignore the use of the word “system” in the other subsections within section 3622. Paragraph (d)(1) is expressly identified as part of the “system.” 39 U.S.C. § 3622(d)(1). And the Commission has the authority to modify the “system” or adopt an “alternative system.” 39 U.S.C. § 3622(d)(3).

Second, even if the matter were not so straightforward, there are clear textual and structural differences between subsection (a) and paragraph (d)(3), which indicate that the Commission’s authority under paragraph (d)(3) is broader than under subsection (a). Order No. 5337 at 38. The presumption of consistent usage “is not rigid and readily yields whenever there is such variation in the connection in which the words are used as reasonably to warrant the conclusion that they were employed in different parts of the act with different intent.”⁷⁵ Had Congress intended only to allow the Commission to revise the regulations implementing the CPI-U price cap to make them more consistent with the PAEA’s statutory objectives, it would have been simpler (and

⁷⁵ Order No. 5337 at 38-39 (citing *Gen. Dynamics Land Sys., Inc. v. Cline*, 540 U.S. 581, 595 (2004) (internal citation omitted)). Applying the presumption mechanically would “ignore[] the cardinal rule that ‘[s]tatutory language must be read in context [since] a phrase ‘gathers meaning from the words around it.’” Order No. 5337 at 39 (citing *Cline*, 540 U.S. at 596 (internal citation omitted)). It would also ignore the rule that statutes should be read as a whole. *United States v. Atl. Research Corp.*, 551 U.S. 128, 135 (2007) (citing *King v. St. Vincent’s Hosp.*, 502 U.S. 215, 221 (1991)).

Notably, the presumption “relents when a word used has several commonly understood meanings among which a speaker can alternate in the course of an ordinary conversation, without being confused or getting confusing.” Order No. 5337 at 39 (citing *Cline*, 540 U.S. at 595-596 (noting that the word “age” can be readily understood to have different meanings depending on the context (internal footnote omitted))).

more natural) for Congress to have drafted the second sentence of paragraph (d)(3) accordingly. *Id.* at 42.

Several commenters have asserted that the purpose of paragraph (d)(3) was to mandatorily require (rather than simply permit at the Commission's discretion) a review of the performance of the implementing regulations the Commission adopted pursuant to subsection (a) after 10 years, followed by the making of any necessary changes to those. 2018 ANM *et al.* Comments at 19; 2018 NPPC *et al.* Comments at 27. These commenters have maintained that this interpretation would not render paragraph (d)(3) mere surplusage or an empty formality, because there are a number of regulatory options that the Commission could pursue while still retaining a CPI-U price cap.⁷⁶ Other commenters have argued that Congress must have concluded that the mandatory features such as the CPI-U price cap were necessary to achieve the statutory objectives since Congress established them all at the same time when it enacted the PAEA. 2017 MMA *et al.* Comments at 15-16; 2017 GCA Comments at 30-31.

However, the text of the relevant provisions does not support this interpretation. Subsection (a) and paragraph (d)(3) employ different language and feature different triggering mechanisms, which, in conjunction with the overall structure of section 3622 and the statutory context on which the Commission's authority under the second sentence of paragraph (d)(3) is premised (a finding that the system established under subsection (a) has not achieved the statutory objectives, taking into account the statutory factors), confirms that the two provisions serve different purposes. Order No. 4258 at 17-18; Order No. 5337 at 42. Moreover, the Commission has always had the

⁷⁶ 2018 ANM *et al.* Comments at 19 n.6; 2018 NPPC *et al.* Comments at 27 n.23. Examples these commenters have given include "using a Passche [i]ndex instead of a Laspeyres index"; changing how [the Commission] calculates CPI increases; modify[ing] the cap to subtract for periods of deflation; adopt[ing] an X-Factor to increase the incentive for cost reduction; modify[ing] the rules for below-cost products; defin[ing] more products and price points within classes and products; or us[ing] a quality-of-service adjusted price cap." 2018 NPPC *et al.* Comments at 27 n.23.

authority to revise its regulations under subsection (a). 39 U.S.C. § 3622(a). Given that, if the scope of the Commission's authority under paragraph (d)(3) were no greater than the scope of its authority under subsection (a), then paragraph (d)(3) would seem to serve no purpose. Likewise, if Congress had concluded that the mandatory features were necessary to achieve the statutory objectives and factors, then paragraph (d)(3) would seem to serve no purpose.⁷⁷ Such an interpretation would run counter to the fundamental principle that statutes should be read as a whole, and a statute should not be interpreted so as to render any part of it inoperative.⁷⁸ Construing paragraph (d)(3) as having no greater scope than subsection (a) would drain paragraph (d)(3) of any power independent of the standing discretionary authority the Commission already enjoys to change its implementing regulations under subsection (a). Order No. 5337 at 42-43.

Contrary to the arguments of commenters, both the text and structure of section 3622 make the purpose of paragraph (d)(3) clear. The Commission was provided general authority to set up and periodically recalibrate the ratemaking system in its initial form under subsection (a), which was required to include certain mandatory features. The Commission was also provided specific authority pursuant to paragraph (d)(3) to review the ratemaking system established under subsection (a) after 10 years and modify or replace any part of it, including the mandatory features, as necessary to

⁷⁷ The Commission does not find that it is reasonable to conclude that Congress required the Commission to conduct a detailed review of the ratemaking system in light of the statutory objectives and factors and make written findings with respect to that review using notice-and-comment rulemaking procedures if Congress did not simultaneously envision the possibility of the ratemaking system in its initial form being subject to change.

⁷⁸ Order No. 5337 at 42 (citing *Safeco Ins. Co. of Am. v. Burr*, 551 U.S. 47, 59-60 (2007) (rejecting an interpretation that would render a word superfluous and incompatible with the statutory structure); *Montclair v. Ramsdell*, 107 U.S. 147, 152 (1883) ("It is the duty of the court to give effect, if possible, to every clause and word of a statute, avoiding, if it may be, any construction which implies that the legislature was ignorant of the meaning of the language it employed.")).

achieve the PAEA's statutory objectives. Order No. 4258 at 17; Order No. 5337 at 36-37.

Moreover, paragraph (d)(3) was the result of a legislative compromise intended to obtain 10 years of rate stability, followed by a Commission-led review of the ratemaking system and, if warranted, modification of the ratemaking system or the adoption of an alternative ratemaking system in order to achieve the statutory objectives. Order No. 4258 at 17; Order No. 5337 at 43. Reading paragraph (d)(3) to confer authority on the Commission that is no greater than the scope of the Commission's authority under subsection (a) would be contrary to this purpose. Order No. 4258 at 17-18. Any suggested interpretation of a statute's plain language must give way if it would conflict with Congress's manifest purposes.⁷⁹

In disputing the Commission's authority under paragraph (d)(3) to modify or replace the CPI-U price cap, ANM *et al.* in response to Order No. 5337 assert that "Congress...does not alter the fundamental details of a regulatory scheme in vague terms or ancillary provisions..." and "[r]epeals by implication are very much disfavored."⁸⁰ However, for the reasons stated above, this characterization of paragraph (d)(3) and its role within the PAEA's regulatory scheme is fundamentally flawed. The text and structure of section 3622, as confirmed by its legislative history, demonstrate, quite to the contrary, that paragraph (d)(3) forms a central component of what Congress envisioned. As a result, the theoretical removal of the provisions contained in paragraphs (d)(1) and (d)(2) from the ratemaking system would not be a "repeal by implication." See ANM *et al.* Comments at 94-95. Paragraph (d)(3) does not

⁷⁹ Order No. 4258 at 18 (citing *Sullivan v. Hudson*, 490 U.S. 877, 890 (1989) ("Congress cannot lightly be assumed to have intended" a result that would "frustrat[e]...the very purposes" of the statute); *Dep't of Revenue of Or. v. ACF Indus. Inc.*, 510 U.S. 332, 340 (1994) (No sound approach to statutory interpretation would attribute to Congress an intent to "subvert the statutory plan[.]").

⁸⁰ ANM *et al.* Comments at 94-95 (quoting *Whitman v. Am. Trucking Ass'ns*, 531 U.S. 457, 468 (2001); *Fogg v. Gonzalez*, 492 F.3d 447, 453 (D.C. Cir. 2007) (citation omitted)).

repeal anything; it expressly *authorizes* the Commission to take action to execute the law by remedying a failure to achieve the PAEA's statutory objectives, including, if necessary, by adopting an alternative to the existing CPI-U price cap system.

ANM *et al.* also criticize Order No. 5337's explanation of the relationship between subsection (a), subsections (b) and (c), and paragraph (d)(3), stating that "[t]here is...nothing in the statute that relegates the objectives and factors to a mere 'background role' under subsection (a) and promotes them to a 'primary role' during the ten-year review required by paragraph (d)(3)." *Id.* at 95-97. However, as explained above, the purpose of paragraph (d)(3) is to ensure that the statutory objectives appearing in subsection (b) are being met. It was in this sense that the Commission in Order No. 5337 referred to the statutory objectives as occupying a more "primary" role in the paragraph (d)(3) context. See Order No. 5337 at 37.

In response to Order No. 5337, Mailers Hub LLC (Mailers Hub) suggests that while the Commission is legally required to develop remedial prescriptions if its paragraph (d)(3) review finds that the ratemaking system is not achieving the statutory objectives, taking into account the statutory factors, the Commission has discretion to defer implementation of those remedial measures if they "would be harmful and counterproductive." Mailers Hub Comments at 10-11. The Commission of course recognizes that by virtue of paragraph (d)(3)'s use of the word "may," the Commission has discretion as to whether to implement changes to the ratemaking system under paragraph (d)(3). However, the Commission disagrees with Mailers Hub's assertion that the modifications the Commission is adopting, which are relatively modest in scope, will be harmful or counterproductive. The Commission has appropriately balanced the statutory objectives and has considered arguments regarding the possibility that increased rate adjustment authority could lead to volume losses that could harm the Postal Service's finances. The Commission has found such concerns to be unwarranted. See Sections IV.C.1., V.C.1., and XIII.E., *infra*.

In sum, given the overwhelming consensus of section 3622's text, structure, purpose, and legislative history as to what Congress intended and envisioned, commenters opposing the Commission's interpretation of section 3622 have failed to demonstrate that their alternative interpretations are plausible at all, much less that they unambiguously foreclose the Commission's interpretation.⁸¹

Nevertheless, despite the Commission's clear legal authority to adopt an alternative ratemaking system, the final rules implemented in this Order serve to modify, rather than replace, the existing ratemaking system. See Order No. 5337 at 33-35. The relatively narrow approach that the Commission has taken seeks to preserve the ratemaking system in its initial form to the greatest extent possible, while at the same time making modifications necessary to achieve the statutory objectives that are responsive to the system's failings. The Commission is not jettisoning the CPI-U price cap; it is implementing adjustments to the CPI-U price cap that remain consistent with price cap theory. *Id.* at 34. Price cap formulas have generally started with a measure of

⁸¹ See, e.g., *Petit*, 675 F.3d at 781 (to prevail under *Chevron* step one, a challenger "must do more than offer a reasonable or, even the best, interpretation [of the statute in question]." (quoting *Village of Barrington, Ill. v. Surface Transp. Bd.*, 636 F.3d 650, 661 (D.C. Cir. 2011)) (internal marks omitted). "Instead, they 'must show that the statute *unambiguously* forecloses the [agency's] interpretation.'" *Petit*, 675 F.3d at 781 (emphasis in original) (quoting *Village of Barrington*, 636 F.3d at 661). "[T]hey must demonstrate that the challenged term is susceptible of only [one] possible interpretation." *Petit*, 675 F.3d at 781 (quoting *Shalala*, 192 F.3d at 1015 (internal marks and citation omitted)).

The Commission notes that other commenters have generally supported its interpretation of paragraph (d)(3), at least insofar as it pertains to section 3622's price cap provisions. See Comments of the United States Postal Service, March 20, 2017, at 19-20 (2017 Postal Service Comments); Comments of the Public Representative, March 21, 2017, at 29-30 (2017 PR Comments); Comments of the American Postal Workers Union, AFL-CIO, March 20, 2017, at 5-6 (2017 APWU Comments); Comments of the National Association of Letter Carriers, AFL-CIO, March 20, 2017, at 16-17 (2017 NALC Comments); Initial Comments of the United States Postal Service in Response to Order No. 4258, March 1, 2018, at 11-12 (2018 Postal Service Comments); Reply Comments of the United States Postal Service in Response to Order No. 4258, March 30, 2018, at 7-19 (2018 Postal Service Reply Comments); Reply Comments of the Public Representative, March 30, 2018, at 8-9 (2018 PR Reply Comments). In response to Order No. 5337, two separate commenters, NPMHU and the Postal Service, support the Commission's interpretation of paragraph (d)(3). NPMHU Comments at 2; Postal Service Reply Comments at 8.

inflation (called the inflation factor), such as the CPI-U index, which the final rules retain.⁸² Many of these price cap formulas have also included various adjustments to the inflation factor, which the final rules for the first time introduce into the ratemaking system's design.⁸³ Based on the Commission's findings in Order No. 4257, the Commission has determined that adjustment factors are now necessary to remedy the existing ratemaking system's failure to achieve the statutory objectives, taking into account the statutory factors. Order No. 5337 at 34. The adjustments being adopted in this Order generally maintain an inflation-based price cap using the CPI-U index, while also remediating aspects of the existing ratemaking system that have proven to be inadequate to achieve the statutory objectives. *Id.* at 35. However, as explained *supra*, even if the Commission's proposal were to be construed as an "alternative system," the Commission has the authority under paragraph (d)(3) to implement such a change.

⁸² *Id.* at 34 (citing United States Postal Service, Office of Inspector General, Report No. RARC-WP-13-007, Revisiting the CPI-Only Price Cap Formula, April 12, 2013, at 46, available at: https://www.uspsoig.gov/sites/default/files/document-library-files/2015/rarc-wp-13-007_0.pdf (RARC-WP-13-007)).

⁸³ Order No. 5337 at 34. As explained in Order No. 5337, most price cap formulas include an "X-factor" to offset productivity growth. See RARC-WP-13-007 at 45; United States Postal Service, Office of Inspector General, Risk Analysis Research Center, Report No. RARC-WP-17-003, Lessons in Price Regulation from International Posts, February 8, 2017, Appendix A at 16, available at: <https://www.uspsoig.gov/sites/default/files/document-library-files/2017/RARC-WP-17-003.pdf>; David E.M. Sappington, *Price Regulation and Incentives*, Body of Knowledge on Infrastructure Regulation (December 2000), at 14, available at: http://regulationbodyofknowledge.org/wp-content/uploads/2013/03/Sappington_Price_Regulation_and.pdf. Price cap plans also may regulate service quality using a reward- or penalty-style "Q-factor." See Sappington (2000) at 14-15, 51; Copenhagen Economics, *Postal Quality and Price Regulation*, March 29, 2017, at 18 n.19 (Copenhagen Economics Report). Other adjustment factors include a "Y-factor" to address recurring exogenous costs, or a "Z-factor" to address an exogenous one-time cost. See RARC-WP-13-007 at 16.

2. If any ambiguity exists, it is reasonable to construe the CPI-U price cap as part of the system subject to review and potential modification or replacement by the Commission.

In the alternative, the PAEA is at most ambiguous on the question of whether the adjustments to the CPI-U price cap proposed by the Commission are within the scope of the phrase “make such modification or adopt such alternative system for regulating rates and classes for market-dominant products as necessary to achieve the objectives.” See 39 U.S.C. § 3622(d)(3). At *Chevron* step two, courts “ask ‘whether the agency’s [interpretation] is based on a permissible construction of the statute.’” *Petit*, 675 F.3d at 785 (quoting *Chevron*, 467 U.S. at 843). Courts consider “whether the [agency] has reasonably explained how the permissible interpretation it chose is ‘rationally related to the goals of’ the statute.” *Petit*, 675 F.3d at 785 (quoting *Village of Barrington*, 636 F.3d at 665 (internal marks omitted)). “If the statute is ambiguous enough to permit the agency’s reading, ... [courts will generally] defer to that interpretation so long as it is reasonable.”⁸⁴

To the extent that paragraph (d)(3) may be ambiguous, the Commission’s interpretation articulated above is reasonable and thus would be entitled to *Chevron* deference.⁸⁵ The same analysis set out above with regard to *Chevron* step one would be equally applicable to explain how the Commission’s interpretation of section 3622 is

⁸⁴ *Nat’l Cable & Telecomms. Ass’n v. FCC*, 567 F.3d 659, 663 (D.C. Cir. 2009) (citing *Consumer Elecs. Ass’n v. FCC*, 347 F.3d 291, 299 (D.C. Cir. 2003)).

⁸⁵ An agency may argue in the alternative as to whether its reading of a statute is proper under *Chevron* step one or *Chevron* step two. See, e.g., *United Parcel Serv., Inc. v. Postal Reg. Comm’n*, 890 F.3d 1053, 1063 (D.C. Cir. 2018) (“Given our conclusion that the Commission’s reading of ‘institutional costs’ is reasonable and so merits our deference [under *Chevron* step two], we need not consider the Commission’s argument that, under *Chevron* [step one], its reading is not only permissible, but also unambiguously correct.”); *Decatur Cty. Gen. Hosp. v. Johnson*, 602 F. Supp. 2d 176, 186 n.6 (D.D.C. 2009) (holding that agency’s decision to apply cost reduction factors to base year costs was entitled to deference under *Chevron* step two, where the agency also provided an alternative justification under *Chevron* step one).

consistent with the statute's text, context, structure, purpose, and legislative history, and is thus reasonable.

Furthermore, to the extent that any ambiguity exists with regard to paragraph (d)(3), it is permissible to use Senator Collins' floor statement as an interpretative aid and reasonable to conclude from that statement that paragraph (d)(3) permits the Commission to modify or replace the price cap provisions. Order No. 5337 at 45. Following the passage of two different postal reform bills, key members of the House and the Senate (including Senator Collins) negotiated a compromise.⁸⁶ The final text of the PAEA was introduced in a new bill and was approved without amendment by both the House and the Senate.⁸⁷ As to the compromise nature of the PAEA, Senator Collins stated:

This *compromise* is not perfect and, indeed, earlier tonight, there were issues raised by the appropriators—legitimate issues—that threatened at one point to derail the bill again. It has been a delicate *compromise* to satisfy all of the competing concerns. Everyone has had to *compromise*, but I think we have come up with a good bill. This *compromise* will help ensure a strong financial future for the U.S. Postal Service and the many sectors of our economy that rely on its services, and it reaffirms our commitment to the principle of universal service that I believe is absolutely vital to this institution.⁸⁸

Senator Thomas Carper also confirmed that the final bill was “a difficult compromise.”⁸⁹

⁸⁶ 151 Cong. Rec. H6511, H6548-H6549 (daily ed. July 26, 2005) (Roll Call No. 430) (reflecting a vote of 410-20 in the House); 152 Cong. Rec. S898, S927-S942 (daily ed. Feb. 9, 2006) (reflecting approval by unanimous consent in the Senate); 152 Cong. Rec. H9160, H9179 (daily ed. Dec. 8, 2006) (statement of Rep. Tom Davis).

⁸⁷ 152 Cong. Rec. H9160-H9182 (daily ed. Dec. 8, 2006); 152 Cong. Rec. S11,821-S11,822 (daily ed. Dec. 8, 2006); see 152 Cong. Rec. D1153, D1162 (daily digest, Dec. 8, 2006).

⁸⁸ 152 Cong. Rec. S11,674, S11,675 (daily ed. Dec. 8, 2006) (statement of Sen. Collins) (emphasis added).

⁸⁹ 152 Cong. Rec. S11,674, S11,675 (daily ed. Dec. 8, 2006) (statement of Sen. Carper).

Paragraph (d)(3) first appeared in this final version, and it was not addressed in any hearings or committee reports.⁹⁰ Neither the presidential signing statement nor any other floor statements addressed paragraph (d)(3).⁹¹ Accordingly, Senator Collins' floor statement is the best source of legislative history to shed light on the purpose of paragraph (d)(3).⁹² Specifically, Senator Collins remarked:

The Postal Service will have much more flexibility, but the rates will be capped at the CPI. That is an important element of providing 10 years of predictable, affordable rates, which will help every customer of the Postal Service plan. After 10 years, the Postal Regulatory Commission will review the rate cap and, if necessary, and following a notice and comment period, the Commission will be authorized to modify or adopt an alternative system.

While this bill provides for a decade of rate stability, I continue to believe that the preferable approach was the permanent flexible rate cap that was included in the Senate-passed version of this legislation. But, on balance, this bill is simply too important, and that is why we have reached this compromise to allow it to pass. We at least will see a decade of rate stability, and I believe the Postal [Regulatory] Commission, at the end of that decade, may well decide that it is best to continue with a CPI rate cap in place. It is also, obviously, possible for Congress to act to reimpose the rate cap after it *expires*. But this legislation is simply too vital to our economy to pass on a decade of stability. The consequences of no legislation would be disastrous for the Postal Service, its employees, and its customers.⁹³

Senator Collins' statement confirms that paragraph (d)(3) was a part of a legislative compromise that required the price cap "Requirements" to remain in place for 10 years, and then allowed the Commission the opportunity to review the effectiveness

⁹⁰ H.R. 6407, 109th Cong., at 7 (2006); Order No. 4258 at 21; Order No. 5337 at 45-46.

⁹¹ Statement on Signing the Postal Accountability and Enhancement Act, 42 Weekly Comp. Pres. Doc. 2196-2197 (Dec. 20, 2006), 2006 U.S.C.C.A.N. S76 (2006); 152 Cong. Rec. H9160-H9182 (daily ed. Dec. 8, 2006); 152 Cong. Rec. S11,674-S11,677, S11,821-S11,822 (daily ed. Dec. 8, 2006).

⁹² Order No. 5337 at 46. Numerous commenters have expressed agreement with the Commission's interpretation of the PAEA's legislative history. See 2017 Postal Service Comments at 21-22; 2017 NALC Comments at 16; 2017 APWU Comments at 5-6; 2018 Postal Service Comments at 11-12; 2018 Postal Service Reply Comments at 14-15.

⁹³ 152 Cong. Rec. S11,674, S11,675 (daily ed. Dec. 8, 2006) (statement of Sen. Collins) (emphasis added).

of the ratemaking system and potentially design a modified or alternative ratemaking system.⁹⁴ Senator Collins' statement confirms that the congressional sponsors of the PAEA contemplated that the Commission would have broad discretion following its paragraph (d)(3) review—including deciding whether to maintain the price cap in its existing form, modify it, or replace it. Order No. 5337 at 46-47. That Senator Collins believed that Congress might need to “reimpose the rate cap after it expires” clearly evidences recognition that the Commission would have the authority following its paragraph (d)(3) review to eliminate the price cap through potential modification of the ratemaking system or through the adoption of an alternative ratemaking system. The statement also confirms that Congress did not consider the CPI-U price cap to be a permanent or immutable requirement of the ratemaking system.

Senator Collins' floor statement demonstrates that Congress contemplated the breadth of the Commission's authority to review and, if needed, to modify or replace the ratemaking system if the Commission determined that the existing system was not achieving the statutory objectives. Order No. 4258 at 22-23; Order No. 5337 at 46-47. Senator Collins' statement confirms that Congress considered the CPI-U price cap to be a part of the system subject to the Commission's authority under paragraph (d)(3). Order No. 4258 at 22-23; Order No. 5337 at 46-47. Moreover, the statement negates any interpretation that paragraph (d)(3) was intended to deny the Commission the authority to modify or replace the CPI-U price cap. Senator Collins explained that the PAEA guaranteed that the CPI-U price cap would exist for a minimum of 10 years.⁹⁵ Senator Collins explained that the 10-year review would occur and discussed potential outcomes: either the Commission would decide to retain the CPI-U price cap in its current form; the Commission would decide to modify the CPI-U price cap; or the

⁹⁴ It is worth noting that it was Senator Collins who introduced the initial bill in the Senate which contained the “requirement” language with regard to the CPI-U price cap. As a result, her statement in the Congressional Record is particularly probative as to the intended meaning of paragraph (d)(3).

⁹⁵ 152 Cong. Rec. S11,674-S11,675 (daily ed. Dec. 8, 2006) (statement of Sen. Collins).

Commission would decide to replace the CPI-U price cap system with an alternative system (subject, of course, to the possibility that Congress could elect to reinstate the CPI-U price cap through legislation). Order No. 5337 at 46-47. This statement directly rebuts any suggested interpretation that the drafters of the PAEA intended for the Commission's 10-year review to redress *only* technical or procedural issues with regard to implementing the CPI-U price cap, which would be the case if the scope of the Commission's rulemaking authority under paragraph (d)(3) were limited to the scope of its rulemaking authority under subsection (a). *Id.* at 47. Therefore, if section 3622 is deemed to be ambiguous, the legislative history confirms the reasonableness of the Commission's interpretation of its statutory authority to modify the ratemaking system or adopt an alternative ratemaking system. *Id.*

Commenters have asserted that Senator Collins' statement must be disregarded because it is not an authoritative expression of legislative intent (such as an official committee report).⁹⁶ They have also asserted that Senator Collins' statement is inconsistent with the longstanding role of Congress in managing the postal system. 2018 NPPC *et al.* Comments at 29. They have stated that the compromise embodied in the PAEA "could well have been to require the Commission to review the operation of the rate system after 10 years and evaluate how to modify it to improve performance while still retaining the CPI-based limitation." 2018 ANM *et al.* Comments at 25. In response to Order No. 5337, ANM *et al.* continue to argue that "regardless of what Senator Collins said on the Senate floor...[that] statement cannot override the plain text of the statute." ANM *et al.* Comments at 103.

However, floor statements by key individuals, such as legislative sponsors, especially where no legislators offered contrary views, help illuminate the purpose of a

⁹⁶ See 2018 ABA Comments at 6; 2018 ANM *et al.* Comments at 25-26; 2018 NPPC *et al.* Comments at 28-29.

piece of legislation.⁹⁷ Floor statements are particularly instructive in clarifying the purpose of language where no other evidence of legislative intent exists.⁹⁸ Moreover, “[s]ection 3622 fits within a history of Congressional delegations of decision-making authority concerning postal matters, including ratemaking.” Order No. 5337 at 47 (quoting 2018 Postal Service Reply Comments at 16). Furthermore, as Senator Collins expressly stated, Congress may re-impose the CPI-U price cap at any time.⁹⁹ Particularly in this instance where the sole source of legislative history is uncontradicted and is consistent with the Commission’s interpretation of the text and structure of section 3622, the Commission’s interpretation must be accorded substantial deference.

Commenters have also asserted that the Commission’s interpretation of paragraph (d)(3) conflicts with statements the Commission has made in the past.¹⁰⁰ In

⁹⁷ Order No. 5337 at 45; see *Fed. Energy Admin. v. Algonquin SNG, Inc.*, 426 U.S. 548, 564 (1976) (finding that an uncontradicted floor statement by one of the legislation’s sponsors “deserves to be accorded substantial weight in interpreting the statute”).

⁹⁸ Order No. 5337 at 45; see *North Haven Bd. of Educ. v. Bell*, 456 U.S. 512, 526-527 (1982) (finding remarks on the Senate floor by “the sponsor of the language ultimately enacted[] are an authoritative guide to the statute’s construction” where no committee report addressed the provisions at issue); *St. Louis Fuel & Supply Co. v. FERC*, 890 F.2d 446, 449 (D.C. Cir. 1989) (finding that sponsors’ floor statements were “the only evidence of congressional intent,” and concluding that such remarks “necessarily have some force” and “carry ‘substantial weight’” (internal citation omitted)).

⁹⁹ Order No. 5337 at 47 (citing 152 Cong. Rec. S11,674-S11,675 (daily ed. Dec. 8, 2006) (statement of Sen. Collins)).

¹⁰⁰ 2014 ANM *et al.* White Paper at 12-14 (citing Docket No. RM2009-3, Order Adopting Analytical Principles Regarding Workshare Discount Methodology, September 14, 2010 (Order No. 536); Docket No. ACR2010, *Annual Compliance Determination*, March 29, 2011 (FY 2010 ACD); Docket No. ACR2010R, Order on Remand, August 9, 2012 (Order No. 1427); Docket No. ACR2011, *Annual Compliance Determination*, March 28, 2012, at 17 (FY 2011 ACD)); 2017 ABA Comments at 8 (citing Docket No. R2010-4, Order Denying Request for Exigent Rate Adjustments, September 20, 2010 (Order No. 547); 2017 MMA *et al.* Comments at 15-16 (citing FY 2010 ACD); 2018 ABA Comments at 5 n.4 (citing Order No. 547); 2018 ANM *et al.* Comments at 13-15, 18, 27-29 (citing Docket No. RM2007-1, Regulations Establishing System of Ratemaking, August 15, 2007 (Order No. 26); Order No. 536; Order No. 547; Order No. 1427; Docket No. R2010-4R, Order Resolving Issues on Remand, September 20, 2011 (Order No. 864)); 2018 NPPC *et al.* Comments at 26 (citing Order No. 547; Order No. 536; FY 2010 ACD).

response to Order No. 5337, ANM *et al.* identify two additional such statements.¹⁰¹ They contend that “[a]n agency cannot typically abandon an earlier position..., but is instead ‘obligated to supply a reasoned analysis for the change.’”¹⁰²

In terms of the two-step *Chevron* framework, if a court were to decide this issue at *Chevron* step one, prior orders of the Commission would not be dispositive.¹⁰³ In the alternative that a court were to evaluate this issue under *Chevron* step two to determine whether the Commission should be accorded deference, it is important to recognize that “[a]n initial agency interpretation is not instantly carved in stone.” *Chevron*, 467 U.S. at 863. Agencies “must consider varying interpretations and the wisdom of [their] polic[ies] on a continuing basis.” *Id.* at 863-864. Nevertheless, the Commission has not changed its interpretation or its position because, as the Commission has explained in prior orders, none of the statements cited by commenters were an interpretation of paragraph (d)(3)—they were all statements addressing the contours of the ratemaking system promulgated under subsection (a) in its initial form. Order No. 4258 at 18; Order No. 5337 at 47-53.

This is also true of the two additional statements identified by ANM *et al.* They cite to statements from Order No. 547 and Order No. 1926 to the effect that changes in circumstances, such as volume declines, are generally to be accommodated within the CPI-U price cap “by reducing costs and increasing efficiencies.” ANM *et al.* Reply Comments at 16 (quoting Order No. 1926 at 175). However, as with the other prior Commission statements that ANM *et al.* have cited to in this proceeding, these statements were not interpretations of the Commission’s authority under paragraph

¹⁰¹ ANM *et al.* Comments at 103-104; ANM *et al.* Reply Comments at 16 (citing Order No. 547; Docket No. R2013-11, Order Granting Exigent Price Increase, December 24, 2013 (Order No. 1926)).

¹⁰² ANM *et al.* Comments at 104 (citing *Trunkline LNG v. FERC*, 921 F.2d 313, 320 (D.C. Cir. 1990) (internal citations omitted)).

¹⁰³ Order No. 5337 at 47; see *Chevron*, 467 U.S. at 842-843 (“If the intent of Congress is clear, that is the end of the matter....”).

(d)(3). They were made in the context of ratemaking system as it was initially established under subsection (a). Therefore, the Commission has not changed its interpretation or its position.

ANM *et al.* also argue, in response to Order No. 5337, that even if the meaning of paragraph (d)(3) is ambiguous, “[m]ere ambiguity in a statute is not evidence of congressional delegation of authority.”¹⁰⁴ They assert that the Commission’s interpretation will lead to “unprecedented” rate increases and volume losses, which cannot be what Congress intended.¹⁰⁵

However, explicit delegations of authority are typically found where “Congress has expressly delegated to [an agency] the authority to prescribe regulations containing ‘such...provisions’ as, in the judgment of the [agency], ‘are necessary or proper to effectuate the purposes of [the authorizing statute]....’”¹⁰⁶ Paragraph (d)(3) empowers the Commission to “*by regulation*, make such modification or adopt such alternative system for regulating rates and classes for market-dominant products as necessary to achieve the objectives.” 39 U.S.C. § 3622(d)(3) (emphasis added). This is a clear delegation of authority by Congress. Furthermore, as with Mailers Hub’s comments, the Commission disagrees with the assertion that the modifications the Commission is adopting, which are relatively modest in scope, will be harmful or counterproductive. The Commission has considered arguments regarding the possibility that increased rate adjustment authority could lead to volume losses that could harm the Postal Service’s

¹⁰⁴ ANM *et al.* Comments at 100 (citing *Am. Bar Ass’n v. FTC*, 430 F.3d 457, 469 (D.C. Cir. 2005) (internal citation and marks omitted)).

¹⁰⁵ ANM *et al.* Comments at 101 (citing *Bechtel Constr., Inc. v. United Bhd. of Carpenters & Joiners of Am.*, 812 F.2d 1220, 1225 (9th Cir. 1987) (court should avoid construction establishing illogical, unjust, or capricious statutory scheme)).

¹⁰⁶ *Household Credit Servs., Inc. v. Pfennig*, 541 U.S. 232, 238 (2004) (internal citations omitted).

finances, and has found such concerns to be unwarranted. See Sections IV.C.1., V.C.1., and XIII.E., *infra*.

In sum, even if paragraph (d)(3) were construed to be ambiguous, the Commission's interpretation of section 3622 is reasonable and permissible and thus would be entitled to *Chevron* deference.

C. Workshare Discounts

In addition to price cap adjustments, the Commission is also adopting modifications to the workshare discount provisions set out in subsection (e) of section 3622. A number of commenters have argued that the workshare discount provisions are outside the scope of the "system" subject to modification or replacement under paragraph (d)(3).¹⁰⁷ These commenters have argued that, structurally, the "system" subject to review and potential modification or replacement under section 3622 consists only of subsections (a) through (d), with paragraph (d)(3) coming at the tail end.¹⁰⁸ Because subsection (e) comes after paragraph (d)(3), they view it as being outside of that "system." *Id.* These commenters have also argued that the PAEA's legislative history demonstrates that Congress did not intend for the requirement that workshare discounts be prohibited from exceeding their avoided costs to be abrogated. 2017

¹⁰⁷ See, e.g., 2017 APWU Comments at 5; 2017 Postal Service Comments at 19, 28-30; 2017 GCA Comments at 36-37; Initial Comments of the Greeting Card Association, March 1, 2018 at 1 n.1 (2018 GCA Comments); 2018 Postal Service Reply Comments at 108 n.285, 111 n.292. Other commenters have supported the Commission's interpretation of its legal authority with regard to workshare discounts. See 2017 ABA Comments at 11; 2017 ANM *et al.* Comments at 11-12, 82; Comments of the Honorable Jason Chaffetz and the Honorable Mark Meadows of the U.S. House of Representatives Committee on Oversight and Government Reform, March 20, 2017, at 2 (2017 Chairman Chaffetz and Chairman Meadows Comments); 2017 MMA Comments at 19, 71; Comments of Pitney Bowes Inc., March 20, 2017, at 3-4 (2017 Pitney Bowes Comments); Comments of the Parcel Shippers Association Pursuant to Commission Order No. 3673, March 20, 2017, at 6 (2017 PSA Comments); 2018 ANM *et al.* Reply Comments at 73-74; 2018 NPPC *et al.* Reply Comments at 5; 2018 Pitney Bowes Comments.

¹⁰⁸ 2017 Postal Service Comments at 19, 28-29; 2017 APWU Comments at 5; 2017 GCA Comments at 37-38.

Postal Service Comments at 30-31; 2017 GCA Comments at 34. These commenters have cited prior statements by the Commission that they claim corroborate their view that the workshare discount provisions are separate and distinct from the other parts of the “system” under section 3622. 2017 Postal Service Comments at 32 (citing Order No. 536); 2017 GCA Comments at 36 (same).

However, subsection (e), like the other parts of section 3622, is part of the system subject to review and potential modification or replacement under paragraph (d)(3). Paragraph (d)(3) instructs the Commission to “review the system for regulating rates and classes for market-dominant products *established under this section....*” 39 U.S.C. § 3622(d)(3) (emphasis added). This phrase clearly and unambiguously encompasses section 3622 in its entirety, including subsection (e). Order No. 4258 at 18. This conclusion derives from both the plain meaning of the term “section,” as well as the fact that within section 3622 there is a clear differentiation made between “sections” and “subsections.”¹⁰⁹ If Congress had wished to limit the system subject to review and potential modification or replacement to subsections (a) through (d), it could have done so.

In addition, one of the statutory factors in subsection (c) that the Commission is required to consider when establishing or reviewing the ratemaking system is “the degree of preparation of mail for delivery into the postal system performed by the mailer and its effect upon reducing costs to the Postal Service....” 39 U.S.C. § 3622(c)(5). Subsection (e) defines workshare discounts as discounts mailers receive for additional preparation of mailpieces, such as “presorting, prebarcoding, handling, or transportation....” See 39 U.S.C. § 3622(e)(1). It is clear that Factor 5 is referring to workshare discounts. Thus, contrary to the structural arguments advanced by

¹⁰⁹ Order No. 4258 at 18-29; see 39 U.S.C. § 3622(d)(3) (“[T]he Commission shall review the system for regulating rates and classes for market-dominant products established under *this section* to determine if the system is achieving the objectives in *subsection* (b), taking into account the factors in *subsection* (c).”) (emphasis added).

commenters, the workshare discount provisions are expressly recognized within subsections (a) through (d), which even under the commenters' interpretation are part of the "system." Therefore, the workshare discount provisions are plainly part of the ratemaking system subject to review and possible modification or replacement under paragraph (d)(3), and any analysis of the issue need go no further than *Chevron* step one. Order No. 4258 at 19; Order No. 5337 at 57. However, even if the question were found to be ambiguous, the Commission would still be entitled to deference under *Chevron* step two given its reasonable and permissible construction of the PAEA. Order No. 5337 at 57.

In addition, even if a court found that paragraph (d)(3) did not authorize the worksharing modifications, the changes to the workshare discount provisions that the Commission is adopting are within the scope of the Commission's standing rulemaking authority (under 39 U.S.C. §§ 3622(a) and 503) and are consistent with the Commission's specific authority to regulate excessive workshare discounts under section 3622, subsection (e). *Id.* at 57-58. Subsection (e) is silent with regard to workshare discounts set lower than avoided costs and therefore does not clearly foreclose the regulation of workshare discounts set lower than avoided costs. *Id.* at 58. Furthermore, the Commission's interpretation "is 'rationally related to the goals of'" the PAEA. *Id.* (citing *Petit*, 675 F.3d at 781). Accordingly, the Commission has multiple sources of authority to support addressing workshare discounts in this proceeding. Order No. 5337 at 58.

D. Annual Compliance Reporting Requirements

The Commission is also modifying the reporting requirements codified at 39 C.F.R. parts 3050 (Periodic Reporting) and 3055 (Service Performance and Customer Satisfaction Reporting). These modifications both further the achievement of the PAEA's statutory objectives and conform with the changes proposed to 39 C.F.R. part 3030 (Regulation of Rates for Market Dominant Products). Additionally, they are

separately authorized under the Commission's specific authority to "prescribe the content and form of the public reports...to be provided by the Postal Service [as part of its ACR]." 39 U.S.C. § 3652(e)(1). These changes will ensure that the Commission can evaluate the Postal Service's compliance with the new regulations proposed in part 3030 and will further the public interest in transparency with respect to the Postal Service's finances, service standards, and efficiency. 39 U.S.C. § 3652(e)(2)(C).

IV. DENSITY-BASED RATE AUTHORITY

A. Introduction

In Order No. 5337, the Commission sought comments on its proposal to allocate additional Market Dominant rate authority based on the unavoidable increase in per-unit costs caused by the decline in mail density. See Order No. 5337 at 63-80. This additional density-based rate authority, along with the retirement-based rate authority, was created to address critical comments that the Commission's prior proposal to annually allocate 2 percentage points of supplemental rate authority was not tied to specific drivers of the Postal Service's losses. *Id.* at 60. The Commission has carefully considered the comments received on Order No. 5337, and now implements the density-based rate authority as proposed, with one change to permit banking of unused density-based rate authority.¹¹⁰

The Commission has identified the portion of the increase in per-unit costs caused by the decline of mail density as a specific driver of the Postal Service's net losses, and has determined that this increase is largely beyond the Postal Service's control. Order No. 5337 at 62-63; see *also* Section IV.C.1., *infra*. Put simply, when the Postal Service delivers fewer mailpieces to more delivery points, those costs which are driven by factors other than marginal changes in volume are spread over fewer pieces, necessarily increasing the per-unit cost. The loss of its economies of density means that the Postal Service's per-unit costs will be unavoidably higher than they were before the decline in density. See Section IV.B.1., *infra*.

The density-based rate authority modifies the existing price cap to include additional Market Dominant rate authority calculated to approximate the amount that per-unit costs would be expected to increase as mail density declines, using the prior

¹¹⁰ For a discussion of the change, see Section IV.C.1., *infra*.

year's decline in density to determine the amount of density-based rate authority.¹¹¹ The formula uses the negative of the institutional cost ratio as a proxy for the elasticity of per-unit costs with respect to density, and multiplies that ratio by the measured change in density to approximate the increase in per-unit costs driven by the prior year's decline in density.

While the loss of density the Postal Service experiences is directly observable, the exact change to network costs due to loss in density cannot be directly observed. The Commission's density-based rate authority formula, therefore, calculates the effect on network costs using a ratio that is a reasonable approximation of the elasticity of per-unit costs with respect to density, *i.e.*, the expected increase in unit costs that results from a loss in density.¹¹² Utilizing this proxy that provides the *expected* increase in per-unit costs, rather than an observed increase has an advantage, namely that the density-based rate authority retains the Postal Service's existing incentives to reduce costs. To the extent that the Postal Service is able to offset some of this unavoidable increase through efficiency improvements in other areas, the design of the density-based rate authority preserves its incentive to do so.

To protect Market Dominant mailers, the formula for the density-based rate authority looks at both the change in Market Dominant volume, and the change in total volume (including Competitive products) when calculating the density-based rate authority, and uses whichever measure provides less total rate authority. This permits Market Dominant mailers to benefit from reduced density-based rate authority when

¹¹¹ If volume increases at the same pace as delivery points, there will be no change in mail density, and thus the amount of density-based rate authority will be zero. If density increases, the formula for the density-based rate authority sets the amount of additional authority to zero. See Section IV.B.2., *infra*.

¹¹² To reiterate, the Commission's use of the term "expected" is due to this use of an approximation of a cost elasticity to estimate the increase in unit costs driven by the prior year's decline in density. It is not a forecast of future results. This temporal aspect of the density-based rate authority is similar to that of the CPI-U price cap, which provides rate authority based on the change in CPI-U over the prior 12 months, rather than a forecast of inflation.

Competitive products experience more favorable changes in volume than Market Dominant products, and protects Market Dominant mailers from increased density-based rate authority when Competitive products experience less-favorable changes in volume.

The Commission concludes that the density-based rate authority is a necessary improvement to the existing system for regulating rates and classes for Market Dominant products, with the other proposed modifications, in order to enable the system to achieve the objectives of 39 U.S.C. § 3622(b). See Chapter XIII., *infra*.

B. Background

1. Economies of Density in Network Industries

A network industry is one in which goods and services are provided over a geographic network of nodes and links.¹¹³ Delivery of a good or service involves transporting the good or service across one or more links to reach the destination node.¹¹⁴ The Postal Service is a multiproduct enterprise operating in a network industry. It provides mail service over a nationwide network of delivery points and delivery routes.

A characteristic feature of network industries is the fact that handling multiple products together leads to important cost advantages.¹¹⁵ These cost advantages are referred to as economies. RARC-WP-12-008 at 2. Economies of scale occur when a

¹¹³ Claude Crampes, "Network Industries and Network Goods" (September 1997), at 2-3, available at: <http://idei.fr/sites/default/files/medias/doc/by/crampes/network.pdf>.

¹¹⁴ Hans-Werner Gottinger, *Economies of Network Industries* (2003), at 3.

¹¹⁵ United States Postal Service, Office of Inspector General, Report No. RARC-WP-12-008, A Primer on Postal Costing Issues, March 20, 2012, at 2, available at: https://www.uspsaig.gov/sites/default/files/document-library-files/2015/rarc-wp-12-008_0.pdf (RARC-WP-12-008).

firm enjoys more efficiency from producing more services of the same type—per-unit costs decline as the scale of the operation increases.¹¹⁶ Economies of scope occur when the firm enjoys more efficiency by producing more types of goods and services—per-unit costs decline as shared costs are spread over more types of goods and services. Economies of density occur when a greater volume of goods and services is provided per network node (delivery points in the case of the Postal Service)—per-unit costs decline as the costs of reaching each node are spread over a larger volume of goods and services.¹¹⁷

Changes in the volume of mail and the number of delivery points to which the Postal Service provides service significantly impact the Postal Service's per-unit costs over time. As the network of delivery points grows larger, the costs of servicing the entire network (network costs) increase. These network costs are spread over the total volume of mailpieces delivered throughout the network. Accordingly, delivering a larger number of mailpieces within the same network of delivery points has the effect of spreading the costs of delivery over a larger number of pieces, lowering the per-unit cost. Increases in mail volume per delivery point therefore decrease per-unit cost, and conversely, decreases in mail volume per delivery point increase the per-unit cost. See RARC-WP-13-007 at 4-10.

In postal policy, the scope of delivery service is fixed by law and carved by custom into the bedrock of American commerce and daily life. Under the current law,

¹¹⁶ *Id.*; NERA Economic Consulting, "Economics of Postal Services: Final Report" (July 2004), at vii, available at: https://www.acm.nl/sites/default/files/old_publication/publicaties/11241_2004-nera-final-postal-report_en.pdf.

¹¹⁷ See Holmes, Thomas J., "The Diffusion of Wal-Mart and Economies of Density," *Econometrica*, Vol. 79, No. 1 (January, 2011), at 257-258, available at: <http://users.econ.umn.edu/~holmes/papers/ecta7699.pdf>.

mail shall be delivered 6 days per week to virtually every address.¹¹⁸ The mail volume being carried to each address must bear the entire costs of the network and the operations needed to serve it. By law, there is no operating subsidy nor is there an option to unilaterally change the delivery requirements established by statute.

2. Density-Based Rate Authority in the Revised Notice of Proposed Rulemaking

In Order No. 5337, the Commission responded to criticism that its original proposal to provide supplemental rate authority in Order No. 4258 was not tied to specific drivers of the Postal Service's net losses. Order No. 5337 at 62. Along with the statutorily mandated amortization payments for particular retirement costs,¹¹⁹ the Commission identified the portion of the increase in per-unit costs caused by the decline in mail density as a driver of the Postal Service's net losses and a primary obstacle to the Postal Service's ability to achieve net income.¹²⁰ To more precisely target these loss drivers, the Commission replaced its original supplemental rate authority proposal of a static 2 percentage points of Market Dominant rate adjustment authority per year with the density-based and retirement-based rate authorities, each of which use formulas to annually calculate the appropriate amount of additional rate authority for each loss driver.¹²¹

¹¹⁸ Specifically, appropriations language included as a rider in each appropriations bill since 1983 requires "that 6-day delivery and rural delivery [of mail] 'shall continue at not less than the 1983 level.'" Postal Regulatory Commission, Report on Universal Postal Service and the Postal Monopoly, December 19, 2008, at 69, available at: <https://www.prc.gov/docs/61/61628/USO%20Report.pdf>.

¹¹⁹ See Chapter V., *infra*.

¹²⁰ Order No. 5337 at 62; *see also id.* at 63 (describing the Postal Service and Public Representative as identifying declines in mail density as a driver of net losses). For an expanded discussion of the density as a driver of the Postal Service's net losses, *see* Section IV.C.1., *infra*

¹²¹ Order No. 5337 at 62-63. Unlike the density-based rate authority, the amount of the retirement-based rate authority is calculated on an annual basis only during the 5-year phase in period. *Id.* at 63.

The Commission noted that the Postal Service does not directly control the volume of mail entered into its network, nor does it control the number of delivery points it must service. *Id.* at 64. The Commission accordingly concluded that the Postal Service does not have direct control over the density of mail in its network. *Id.* The Commission also explained that volume and delivery points, both components of density, affect attributable and institutional costs differently and how the portion of increases in per-unit costs caused by the decline in mail density are not linked to the rate of inflation, and so the existing inflation-capped ratemaking system does not provide adequate ratemaking authority to offset the density-driven increase in per-unit costs. *Id.* at 70-71.

The Commission discussed how the differences in the way that changes in density affect attributable costs, which largely vary with volume but are insensitive to the number of delivery points, and institutional costs, which do not vary with volume but increase with the number of delivery points, makes the institutional cost ratio particularly useful for approximating the portion of an increase in per-unit costs that would be expected as a result of a decline in density.¹²²

Calculation and implementation. As proposed in Order No. 5337 and implemented here, the amount of the density-based rate authority would be determined annually based on the formula described below. As originally proposed, the density-based rate authority would be available to the Postal Service to use in any rate change that is implemented within 12 months of the date of the determination. See Order No. 5337 at 79. The Commission has removed that requirement, permitting the Postal Service to bank available density-based rate authority for use in future years. See Section IV.C.1., *infra*.

¹²² *Id.* at 71. For an expanded discussion of the role of the institutional cost ratio in the formula for the density-based rate authority, see Appendix A, Section I.A.

As described in Order No. 5337, the formula for the density-based rate authority calculates the percentage amount by which per-unit costs would be expected to increase as a result of the observed year-over-year change in density. Order No. 5337 at 79. That same percentage would then be authorized as additional rate authority for Market Dominant products. *Id.*

The year-over-year change in density is calculated in two different ways, once using total density and once using Market Dominant density—whichever produces less density-based rate authority will be used as the year-over-year change in density. *Id.* The Commission had previously mischaracterized this mechanism as intended to prevent cross-subsidization of Competitive products by Market Dominant products. See *id.* at 72. The term cross-subsidy is not technically accurate in this context, as it refers specifically to the regulatory oversight of Competitive products. See 39 U.S.C. § 3633(a)(1). However, the rationale behind the mechanism is akin to the rationale behind preventing cross-subsidy in that the mechanism protects Market Dominant mailers from being harmed by negative volume changes in Competitive products. The intent is to protect Market Dominant mailers from having to pay higher rates as the result of the density-based rate authority if changes in Competitive volume are less favorable than changes in Market Dominant volume. Conversely, this mechanism ensures that Market Dominant mailers benefit if changes in Competitive volume are more favorable than changes in Market Dominant volume. The mechanism also serves the purpose of more directly aligning the density-based rate authority with the statutory focus of this rulemaking – that is to make modifications to the Market Dominant system of ratemaking necessary for the system to achieve the objectives of section 3622.¹²³ This goal of protecting Market Dominant mailers overlaps with the purposes of the

¹²³ Specifically, this rulemaking adopts final rules modifying the system of ratemaking for Market Dominant products, and does not modify the regulatory oversight of Competitive products. Because the Postal Service's financial position is affected by both Market Dominant and Competitive density, the limitation of density-based authority described above is both a prudential and precautionary measure.

statutory prohibition against cross-subsidization found at 39 U.S.C. § 3633(a)(1), but the statutory authority to implement the density-based rate authority stems from 39 U.S.C. § 3622. See Chapter III., *supra*.

Formula. Formula IV-1 shows how the Commission annually calculates the available amount of density-based rate authority. The measured change in year-over-year density is multiplied by -1 multiplied by the institutional cost ratio. This product is the amount by which unit costs are expected to increase as a result of the measured decline in density. If density does not decline, the amount of density-based rate authority is zero. The year-over-year change in density is calculated using both total density and Market Dominant density, and the amount of density-based rate authority will be based on whichever figure produces less available rate authority.

Formula IV-1: The amount of the density-based rate authority is the greater of zero and:

$$-1 * \frac{IC_T}{TC_T} * \% \Delta D_{[T-1,T]}$$

Where,

T = most recently completed fiscal year;

T-1 = fiscal year prior to year T;

IC_T = institutional cost in fiscal year T;

TC_T = total cost in fiscal year T; and

%ΔD_[T-1,T] = Percentage change in density from fiscal year T-1 to fiscal year T.

A hypothetical example of the formula in operation can be found in the attached technical appendix. Appendix A, Section I.B.

C. Commission Analysis

Comments on the density-based rate authority fall into three categories: general conceptual objections to providing the density-based rate authority; general

methodological objections regarding how the density-based rate authority is implemented; and specific comments concerning the formula for the density-based rate authority. Each group of comments is discussed below.

1. Conceptual Objections to the Density-Based Rate Authority

Objections that the density-based rate authority does not go far enough. The Postal Service states that the proposed density-based rate authority is not a meaningful substitution for a recalibration of rates. Postal Service Comments at 7. It suggests that a rate reset should be based on a broader set of factors than density and retirement, and advocates for a net-loss based approach as more consistent with established regulatory practice. Postal Service Reply Comments at 32. APWU similarly suggests that the density-based rate authority is inadequate to provide financial stability. APWU Comments at 2-4. NALC recommends that the density proposal should be modified to account for declines in density since 2009 to address the shortcomings of the existing rate system and to make the Postal Service whole. NALC Comments at 5. GCA replies that the Commission makes clear that its proposal is not intended as a true-up, and instead targets two underlying causes of financial distress: volume erosion and retirement obligations. GCA Reply Comments at 10.

GCA is correct in stating that the Commission's proposal is not intended as a true-up. The intent is to address identified deficiencies in the current price cap system that contributed to the failure of that system to meet the objectives of 39 U.S.C. § 3622(b). The density-based rate authority is specifically intended to address the future rise in per-unit costs caused by declines in density, but is not intended to recalibrate rates to reflect the Postal Service's density at a specific point in time. The recalibration of rates suggested by the Postal Service goes beyond the scope of modifying the ratemaking system to address specific deficiencies.

*Objections that the density-based rate authority will counter-productively induce further volume loss.*¹²⁴ ABA objects to the proposed density-based rate authority on the grounds that resulting price increases will result in volume declines and be counterproductive. ABA Comments at 10. ANM *et al.* point out that a large feedback effect resulting from year-over-year rate increases is inherent in the density formula. ANM *et al.* Comments at 44. NPPC describes the density-based rate authority as discouraging volume growth and creating a death spiral.¹²⁵

As a foundational matter, the Governors of the Postal Service, not the Commission, set the rates for postal services, while the Commission establishes and administers the regulatory system. The law generally permits the Postal Service to set Market Dominant product prices as long as each product covers its attributable costs and the average price increase for each class is at or below the CPI-U price cap. The Postal Service may utilize all of the CPI-U price cap authority, regardless of its costs. 39 U.S.C. § 3642 defines Market Dominant products as those for which “the Postal Service exercises sufficient market power that it can effectively set the price of such product substantially above costs, raise prices significantly...without risk of losing a significant level of business....”¹²⁶ The paragraph continues, “[t]he competitive category of products shall consist of all other products.” *Id.* § 3642(b)(1). Prices for Competitive products are not subject to the price cap.

¹²⁴ For additional comments relating to induced volume loss relating to the retirement-based rate authority, and the retirement-based rate authority in combination with the density-based rate authority, see Section V.C.1., *infra*.

¹²⁵ NPPC Comments at 36; NPPC Reply Comments at 11. The concept of a “death spiral” refers to the idea that increased prices will induce losses in volume as price-sensitive mailers send less mail, and that loss of volume then triggers additional density-based rate authority, which will induce further volume losses when used.

¹²⁶ 39 U.S.C. § 3642(b)(1). Market Dominant products also include products covered by the postal monopoly. See *id.* § 3642(b)(2).

Thus, title 39 provides that as a general matter, if products are particularly price sensitive, such that potential price increases could cause significant customer flight, the correct regulatory response is lighter price regulation, not more.¹²⁷ Even if commenters opposing the cap modification were correct in their arguments regarding price sensitivity, their proposed solution is inconsistent with the regulatory approach of title 39. (In contrast, section 3642 provides for heavier price regulation where products have captive customers, *i.e.* when a significant price increase, quality decrease, or reduced offering does not result in a significant loss of business to other firms offering similar products, for example). In the Commission's experience, demand for Market Dominant products has been relatively price inelastic in both the pre-PAEA period and the PAEA period. Accordingly, the decrease in volume induced by the density-based rate authority is expected to be less in proportional terms than the amount of density-based rate authority.

A brief review of the recent history of price regulation is instructive. From 1971 through 2006, the prices for postal services were not capped, and volumes grew steadily. Starting in 2007, the PAEA price cap limited all Market Dominant classes to the rate of growth of CPI-U. Rather than preserving the volume of Market Dominant mail, volume subject to the price cap shrunk by 35 percent in the period covered by this review and has continued to decline. See Table IV-1, *infra*. The precise economic meaning that should be inferred from this decline, and the appropriate strategic response, is complicated by a number of factors including changes in communications technology, economic cycles, and consumer and business reactions to both. It would strain the bounds of the law and rationality, however, for the Commission to ignore its findings regarding the failure of the current system to achieve the objectives of § 3622(b) (taking into account the factors of § 3622(c)), and to overlook the disconnect

¹²⁷ "Products covered by the postal monopoly cannot be moved from the Market Dominant to the competitive category." 39 U.S.C. § 3642(b)(2).

between actual Postal Service costs and the CPI-U, in order to recast the CPI-U only cap as a tool to accomplish what it has not been able to do: preserve Market Dominant mail volume, and ensure the financial stability of the Postal Service.

The Postal Service has discretion to decide how much of the density-based rate authority to use on a year-to-year basis, and can choose not to use all of its available rate authority if it decides that doing so would be counterproductive. Additionally, in the event that price elasticity for Market Dominant products changes such that volume effects are outside the expected range, the Commission retains the authority to revisit the density-based rate authority sooner than the planned 5-year timeframe. See Chapter XI., *infra*.

As originally proposed in Order No. 5337, the density-based rate authority was only available for 12 months after the Commission's determination of the amount of authority, and would be forfeited if not used. Order No. 5337 at 79. The Commission recognizes, however, that preventing the Postal Service from banking unused density-based rate authority limits the Postal Service's ability to respond to potential changes in market and economic conditions, by providing an incentive to use all of the available authority in each year.

To provide added flexibility, the Commission modifies the final rules to state that the Postal Service may use the density-based authority to generate unused rate adjustment authority.¹²⁸ This change also takes into consideration the assumption that limiting the ability to use the additional authority to a particular year is equivalent to a requirement to use all of the authority in that year. Making the additional authority

¹²⁸ See Chapter XIV., *infra*. New unused rate authority generated by the density-based rate authority, if any, will be added to the total amount of banked authority, and will follow the existing operation of the rules governing banked authority, including the annual limitation on the use of banked authority per class and the expiration of unused banked authority. 39 U.S.C. § 3622(d)(2)(C).

bankable discourages the Postal Service from simply using it to avoid losing it. Rather, this change provides more incentive for the Postal Service, as the operator, to consider demand, amount of authority available, and other market conditions before determining whether to use the authority in its entirety in a particular year.¹²⁹

Objections that the density-based rate authority will disincentivize efficiency. ANM *et al.* and NPPC *et al.* object to the density-based rate authority on the grounds that it would reduce the Postal Service's incentive for efficiency. ANM *et al.* Comments at 41; NPPC *et al.* Comments at 35. ACMA objects to the idea that the density-based rate authority is designed to preserve contribution as volume is lost, discouraging the Postal Service from successfully transitioning from a high-volume service with high fixed costs to a low-volume service with low fixed costs. ACMA Reply Comments at 6.

Joint Commenters also argue that modifications to the price cap responding to the financial performance and economic conditions faced by the Postal Service are inconsistent with price cap theory and practice. This argument is part of a persistent line of criticism by some commenters that would have the Commission overlook the ongoing losses of the Postal Service in order to preserve the price cap "as is." Besides avoiding the Commission's responsibilities under section 3622, ignoring the impacts of the price cap would be irrational and at odds with regulatory practice.

As price caps have been implemented over the past 3 decades in several industries, the actual practice has been that "[w]hen the price cap plan is reassessed at its scheduled review, ongoing price regulations are often informed by realized costs and

¹²⁹ In addition to providing additional flexibility to respond to market conditions, permitting the Postal Service to bank unused density-based rate authority responds to the Postal Service's objections that Order No. 5337 did not adequately explain why the new forms of rate authority could not be banked. See Postal Service Comments at 64.

earnings.”¹³⁰ Furthermore “the stringency of stipulated price regulations is often influenced by the firm’s realized earnings in practice. In this sense, the price cap regimes that are observed in practice are seldom ‘pure’ price cap regimes.” Sappington December 2000 at 5.

The Commission, for its part, is authorized to—at a minimum—make modifications to the existing regulatory system, and indeed must make them due to the failure of the current regulatory system to meet the objectives of section 3622. Far from an *ad hoc* course correction, the Commission’s actions in this docket are required by any good faith effort to implement section 3622 and are consistent with regulatory best practices which require adjusting to, rather than ignoring, the economic realities of a regulated firm.

The density-based rate authority targets specific cost increases over which the Postal Service has minimal control. It does not reduce the Postal Service’s incentive for efficiency, because the Postal Service will need cost savings and efficiency gains to fully achieve financial health, and it will continue to be able to accrue the benefits of the cost savings it achieves through increased efficiency in other areas. Additionally, the formula for the density-based rate authority is designed as an estimate of how much per-unit costs would be *expected* to have increased as a result of the prior year’s decline in density, rather than on an observed increase in per-unit costs. To the extent the Postal Service is able to offset some of the realized increase in per-unit costs

¹³⁰ See *Price Regulation and Incentives*, David E. M. Sappington, at 21 (Sappington December 2000), available at: http://regulationbodyofknowledge.org/wp-content/uploads/2013/03/Sappington_Price_Regulation_and.pdf. See also Sappington December 2000 at 53–64, explaining some of the regulatory tools designed to take costs into account under price cap regulation. See RARC-WP-13-007, in which the United States Postal Service Office of Inspector General (Postal Service OIG) discusses at length the different ways that regulators are able to take exogenous costs into account under price cap regulation.

through efficiency improvements in other areas, the density-based rate authority preserves the Postal Service's incentive to do so.

ACMA's concern that the density-based rate authority will disincentivize the Postal Service from transitioning to a low-volume service with low fixed costs overlooks the fact that parts of the Postal Service's network continue to grow even as volume declines. The formula for the density-based rate authority is specifically designed to isolate the expected increase in per-unit costs caused by delivering fewer pieces to an expanding number of delivery points (*i.e.*, a growing network). Although this increase is largely unavoidable in the short and medium term, by focusing on expected cost increases rather than actual cost increases, the density-based rate authority fully maintains the Postal Service's incentive to reduce costs (including fixed costs) wherever possible.

Objections that the density-based rate authority is not rationally related to drivers of loss. ANM *et al.* claim that the density formula is not rationally related to the expenses it is intended to cover, and that it is arbitrary and capricious because it is not rationally related to Postal Service cost drivers. ANM *et al.* Comments at 44-49. NPPC *et al.* state that the density formula bears no relation to the actual costs of servicing additional delivery points. NPPC *et al.* Comments at 26.

The density-based rate authority is not designed to track the actual cost of servicing additional delivery points. Instead, the density-based rate authority is an approximation of the proportion of per-unit costs that would be *expected* to unavoidably increase in the short and medium term as density declines. If the Postal Service is able to achieve lower increases in the proportion of average per-unit costs that it controls, it retains those savings. Conversely, if the Postal Service experiences an increase in per-unit costs above those that are unavoidable in the short and medium term, it must absorb those costs. This mechanism specifically targets the increase in per-unit costs

that the Commission has identified as a driver of the Postal Service's net losses, while simultaneously not weakening the Postal Service's incentive to operate efficiently.

Additional Commission analysis. The Commission reiterates its determination that the increase in per-unit costs caused by the decline in mail density is a primary driver of its net losses and that these density-driven increases in per-unit costs are largely outside of the Postal Service's control.¹³¹

Since 2007, the total volume of Market Dominant mail has declined by 35 percent. See Table IV-I. Over the same time period, the number of delivery points has increased by 10 percent. See *id.* Together, these trends mean that the density of Market Dominant mail has decreased by 41 percent during the PAEA era. See *id.*

¹³¹ See Section IV.B.2., *supra* (citing Order No. 5337 at 62-64).

Table IV-1
Market Dominant Volume, Delivery Points, and Density, FY 2007–FY 2019

Fiscal Year	Market Dominant Volume (millions)	Delivery Points (millions)	Density
2007	210,603.10	127.02	1,658.03
2008	201,128.00	128.43	1,566.05
2009	175,677.24	129.51	1,356.48
2010	169,154.12	130.39	1,297.29
2011	166,460.88	131.14	1,269.34
2012	157,325.68	131.93	1,192.49
2013	155,114.14	132.72	1,168.73
2014	151,926.68	133.78	1,135.65
2015	150,197.94	134.86	1,113.73
2016	149,823.80	136.03	1,101.40
2017	144,387.07	137.32	1,051.46
2018	140,737.79	138.58	1,015.57
2019	136,897.53	139.96	978.12

Source: Please see Appendix A, Section I.C. for references to source data.

Over the same period, the per-unit costs of mail have increased by more than 54 percent.¹³² The existing ratemaking system, however, assumes that costs will rise in line with CPI-U or at minimum would be close enough to make up the difference with efficiency improvements and cost reductions. Since 2007, the cumulative rate authority generated by CPI-U has been only 27 percent.¹³³ In a hypothetical scenario where per-unit costs increased only in line with inflation, the Postal Service's financial position would have been greatly improved, as seen on Table IV-2.

¹³² *Id.* Because institutional costs are not attributed to either Market Dominant or Competitive products, the growth in per-unit costs specifically for Market Dominant products cannot be meaningfully calculated. Per-unit costs are the average cost per piece, calculated by dividing total costs by volume.

¹³³ The inflation series is obtained from the fiscal-year average of the Bureau of Labor Statistics' monthly CPI-U values, from January 2006 to December 2019, available at: <https://beta.bls.gov/dataViewer/view>.

Table IV-2
Postal Service Unit Costs and Net Losses, FY 2007– FY 2019

Fiscal Year	Actual Unit Cost	Actual Net Profit/Loss (Millions)	Hypothetical Unit Cost (CPI-U Only)	Hypothetical Net Profit/Loss (CPI-U Only)
2007	0.38	(5,142.38)	0.38	
2008	0.38	(2,805.65)	0.40	(5,481.67)
2009	0.41	(3,794.33)	0.40	(1,927.79)
2010	0.44	(8,505.39)	0.40	(1,539.11)
2011	0.42	(5,067.00)	0.41	(3,607.43)
2012	0.51	(15,905.97)	0.42	(2,358.84)
2013	0.46	(4,977.09)	0.43	(661.58)
2014	0.47	(5,507.60)	0.44	(6.89)
2015	0.48	(5,060.00)	0.44	1,412.47
2016	0.50	(5,591.00)	0.44	3,290.93
2017	0.48	(2,741.00)	0.45	2,236.85
2018	0.51	(3,913.00)	0.46	3,118.50
2019	0.56	(8,813.55)	0.47	4,190.66

Source: Please see Appendix A, Section I.C. for references to source data.

The Commission recognizes the above-inflation increase in per-unit costs has multiple causes, including the increasing role of Competitive products (increasing per-unit costs).¹³⁴ While it is not possible from the available data to precisely determine how much of the above-inflation increase in per-unit costs has been driven by the decline in mail density, the fact that the Postal Service operates in a network industry and enjoys economies of density necessarily means that losing those economies will increase real per-unit costs. See Section IV.B.1., *supra*. An estimate can be made, however, using the same methodology used by the Commission's formula for the density-based rate authority. Under that approach, the 41 percent decline in density since the end of FY

¹³⁴ There are also factors that have reduced per-unit costs over time, such as increases in worksharing.

2007, a period during which the institutional cost ratio varied between 0.40 and 0.50, would be expected to drive an increase in per-unit costs of between \$0.09 and \$0.11.¹³⁵

Because under the current ratemaking system Market Dominant rates are limited to growing at the rate of inflation, the Postal Service is forced to absorb the portion of the above-inflation increase in per-unit costs driven by the loss of density. See Order No. 5337 at 70-71. Moreover, the density-driven increase in per-unit costs cannot be avoided through operational changes, particularly not in the short- and medium-term. Costs that vary with volume can be avoided as volume falls, but the costs of servicing the growing network and other costs that only indirectly depend on volume will remain, and will necessarily be spread over fewer pieces of mail.

Under the constraints of the current ratemaking system, the Postal Service can neither avoid the density-driven increase in per-unit costs, nor can it raise additional revenue to cover the increase.

2. General Methodological Objections to Density-Based Rate Authority

Recommendations that the density-based rate authority should be forward-looking. ANM *et al.* recommend that any rate authority for volume loss should be prospective to avoid perverse incentives. ANM *et al.* Comments at 42. In the context of discussing that the proposed density formula bears no relation to the cost of servicing additional delivery points, NPPC *et al.* suggest that density decline is more properly measured by the well-established roll forward model. NPPC *et al.* Comments at 30.

¹³⁵ The minimum value for the institutional cost ratio since the end of 2007 was 0.40 in FY 2009. See Docket No. ACR2009, Library Reference USPS-FY09-1, December 29, 2009, Excel file "FY09PublicCRA.xlsx," tab "Cost3," cells F34:F35. The maximum value for the institutional cost ratio since the end of 2007 was 0.50 in FY 2012. See Docket No. ACR2012, Library Reference USPS-FY12-1, December 28, 2012, Excel file "FY12PublicCRA.xlsx," tab "Cost3," cells F36:F37.

By contrast, the Postal Service objects to basing the density-based rate authority on roll-forward methodologies on the grounds that the impact of delivery point growth on network costs is broader than cost segments and commenter-suggested methodologies. Postal Service Reply Comments at 33, Appendix B.

Similarly, the Public Representative disagrees with the declaration in support of ANM *et al.* that suggests annual volume losses should be replaced with predicted future declines. PR Reply Comments at 8. The Public Representative states that use of actual measured changes in density provide an “objective anchor” for price adjustment. *Id.* However, the Public Representative recommends including a forward-looking element to address concerns that the density-based rate authority is a true-up and to prevent excessive rate increases. *Id.* He recommends considering Dr. Brennan’s proposed methodology for adjusting volume declines for price elasticity of demand. *Id.*

Projecting future density would be more complicated than the Commission’s proposal, would entail more uncertainty, and would require an additional mechanism in later years to correct for inaccurate projections.¹³⁶ The Commission’s formula bases future rate increases on actual, measured declines in density,¹³⁷ similar to how the current price cap limits future rate increases based on actual, measured changes in CPI-U. The Public Representative’s proposal for adjusting for price elasticity of demand is discussed further below, in the context of induced declines in density.

¹³⁶ In particular, the complexity of forward-looking estimates imposes additional administrative burdens, and reduces the predictability of the resulting amount of rate authority, in opposition to Objectives 2 and 6. The transparency of the solution is also reduced if the mechanics are hidden behind complicated economic models that attempt to predict future volume losses. None of the commenters have shown that a forward-looking model would have sufficiently improved accuracy over the Commission’s backwards-looking estimate to justify these tradeoffs.

¹³⁷ As stated previously, “the density-based rate authority is an approximation of the proportion of per-unit costs that would be *expected* to unavoidably increase in the short and medium term as density declines.” See Section IV.C.1, *supra*.

Objections that the density-based rate authority does not distinguish between exogenous density declines and controllable or induced density declines. ANM *et al.* state that the density formula does not differentiate between density declines resulting from exogenous volume decreases and those that result from rate increases or factors within the Postal Service's control. ANM *et al.* Comments at 43. NPPC *et al.* object that the density-based rate authority treats as uncontrollable those costs that it asserts are actually within the Postal Service's control. NPPC *et al.* Comments at 25-26. ABA states that the density-based rate authority would convert the price cap regime back to cost of service, noting that not all density declines are exogenous. ABA Reply Comments at 5.

Additionally, the Public Representative suggests that price elasticity can be used to differentiate between controllable and non-controllable volume losses. PR Reply Comments at 9. The Public Representative notes that an analysis of elasticities suggests that the Commission should include a forward-looking component and that it is reasonable to assume certain products may become more elastic. *Id.* at 14. The Public Representative alternatively suggests a one-time adjustment for density, with periodic adjustments at 5-year intervals. *Id.* at 17.

When volume declines, the remaining costs of servicing the growing network are spread among fewer mailpieces, resulting in an unavoidable increase in per-unit costs in the short- and medium-term. As discussed above, this density-driven increase in per-unit costs is in addition to per-unit cost increases caused by inflation, which are addressed in an inflation-based price cap system. See Section IV.C.1., *supra*. The purpose of the density-based rate authority is therefore to provide additional Market Dominant ratemaking authority to offset this unavoidable increase in per-unit costs in the short- and medium-term.

These commenters do not allege that the relationship between declining density and increased per-unit costs is different depending on the cause(s) of the underlying

volume loss, and there is no evidence that it is. Similarly, the inability to offset the increase in per-unit costs under the existing price cap system is equally damaging to the Postal Service's ability to attain financial stability regardless of whether the volume loss was caused by technological shifts or price increases.

The Postal Service has limited options to address increases in per-unit costs that are outside of its direct control. The Commission has accordingly determined that the density-based rate authority is necessary to provide additional revenue to offset the density-driven increase in per-unit costs, and created a formula to calculate the expected increase in per-unit costs. Reducing the amount of additional rate authority below the expected increase in per-unit costs on the grounds that the decision to use that authority induces a further "controllable" volume loss would stymie the purpose of offsetting that increase in expected per unit costs. Accordingly, any induced volume loss is a necessary consequence of providing the offsetting revenue, rather than a reason to reduce the amount of density-based rate authority. The only hypothetical scenario where the rate increase would be counterproductive would be where the price-induced volume effect (price elasticity) is such that less revenue is collected from the increase than is forgone due to the loss in volume. As discussed in Section V.C.1., if such a scenario were to come to pass, the Postal Service as the operator may determine not to use any or all of its rate authority, or the Commission may review any component of the ratemaking system sooner than its planned 5-year review.

The formula for the density-based rate authority is designed to approximate the amount by which per-unit costs is *expected* to unavoidably increase in the short and medium term as a result of the decline in density as remaining costs are distributed over fewer pieces. This contrasts with a cost-of-service approach that would instead compensate the Postal Service for the *actual* increase in total costs. By focusing on the increase in per-unit costs expected to occur due to density declines, the density-based rate authority maintains the Postal Service's incentive to decrease costs wherever

possible. Additionally, the density-based rate authority only addresses declines in density calculated after the effective date of the rules (based upon the observed density decline experienced in the most recently ended fiscal year), and makes no attempt to compensate the Postal Service for prior density declines.

Finally, the Commission notes that if it were returning to a cost-of-service regime, it would necessarily have to address all outstanding costs. Instead, the Commission has targeted specifically identified costs that are driving the Postal Service's losses and are outside the Postal Service's direct control in the short and medium term.

Objections that the density-based rate authority does not address differences in the mail mix. ACMA objects to the density-based rate authority on the grounds that it ignores the evolution of the mail mix towards higher contribution pieces. ACMA Comments at 5.

The Public Representative notes that the density formula does not account for mail volume declines by either class or product, and that not all mail volume declines are equally harmful to the Postal Service's finances. PR Comments at 14-15. The Public Representative describes this failure to consider the mail mix as a serious flaw in the proposed density-based rate authority. *Id.* at 15. He notes that Package Services, for example, has never experienced declines, and states it is unclear why Package Service deserves density-based rate authority. *Id.* ACMA objects to the Public Representative's implication that specific classes of mail "deserve" additional rate authority to compensate for class-specific declines in density. ACMA Reply Comments at 6-7.

The extent to which density-decline driven increases in per-unit costs are affected by the mail mix is captured by the measured cost elasticities of each cost segment. Those cost elasticities are in turn indirectly captured by the institutional cost ratio, which the density formula uses as a proxy for the elasticity of unit costs with

respect to density.¹³⁸ This ratio will change as the mail mix changes.¹³⁹ Additionally, the size of the Postal Service's network is not measured by mail class. The density-based rate authority is designed to offset increases in per-unit costs that are unavoidable in the short- and medium-term, and is not designed to offset contribution changes from individual mail classes.

The Public Representative's suggestion that density declines should be measured on a class basis overlooks the fact that changes to per-unit costs are not isolated to specific classes. As overall volume decreases, remaining costs—those that are less responsive to volume—are borne by fewer pieces, driving an increase in per-unit costs, irrespective of class. Additionally, the effects of network size cannot be evaluated at a class level, as the number of delivery points is not a class-specific measure.

As the Commission discussed in Order No. 5337, factoring in revenue (or contribution) would not comport with the necessity of compensating the Postal Service for unavoidable increases in per-unit costs. Order No. 5337 at 76-77. The incentives for efficiency that the density-based rate authority preserves would be weakened if additional rate authority were tied to revenue or contribution, because calculating the density-based authority as a particular revenue or contribution level would inadvisably tie the amount of authority to the Postal Service's pricing decisions.

Other recommendations. NPPC *et al.* recommend that, if adopted, the density-based rate authority should include a reduction in rate authority if per-unit delivery costs decline. NPPC *et al.* Comments at 26. NPPC *et al.* also recommend that adoption of the density-based rate authority should preclude future exigent increases based on

¹³⁸ For an expanded discussion of the relationship between the cost elasticities of cost segments and the institutional cost ratio, please see Appendix A, Section I.A.

¹³⁹ Similarly, for an expanded discussion of the impact of changes in the mail mix on the institutional cost ratio, please see Appendix A, Section I.A.

volume loss. *Id.* Further, NPPC *et al.* recommend that the Postal Service should be required to report on its efforts to increase density. *Id.* at 74.

The density-based rate authority is an estimate. Year-to-year fluctuations in measured density are to be expected. If systemic shifts result in persistent increases in density, or cyclical increases are followed by decreases, that might be reason to reconsider the application of the density-based rate authority in the Commission's next review, or sooner, should the circumstances warrant.

Reducing the density-based rate authority if per-unit delivery costs decline would reduce the Postal Service's incentive to reduce costs to the maximum extent possible. Maintaining that incentive is why the density-based rate authority is based on the increase in per-unit costs expected as a result of density declines, rather than the actual increase.

Even with the additional density-based rate authority, the Postal Service still has a powerful incentive to increase volume and density. The density-based rate authority only provides additional revenue to cover the expected increase in average cost per piece, and does not otherwise compensate the Postal Service for lost volume and revenue. Maximizing volume is not an objective of 39 U.S.C. § 3622(b), and the Postal Service has both the business discretion to take actions to attempt to increase volume, and a powerful incentive to do so.¹⁴⁰ Accordingly, an additional reporting requirement is not necessary.

The Commission will be mindful of the density-based rate authority when considering future exigent requests.¹⁴¹ However, the Commission notes that exigent requests are fact-based and, by their nature, difficult to anticipate. The Commission

¹⁴⁰ By contrast, improving efficiency via maximizing incentives for cost reductions is an objective of 39 U.S.C. § 3622(b). See Chapter IX., *infra*.

¹⁴¹ Exigent rate adjustments are authorized by 39 U.S.C. § 3622(d)(1)(E).

therefore declines to explicitly preclude future exigent rate increases based on volume loss.

3. Specific Critiques of the Density-Based Rate Authority Formula

Recommendations to use different data sources as the input to the density-based rate authority formula. The Public Representative states concerns relating to the use of TFP reports as the input data for the number of delivery points, and Revenue, Piece, and Weight (RPW) reports for input data for volume. PR Comments at 14, 17. The Public Representative suggests that delivery points can instead be obtained from the figures on the Postal Service's website, and that volume data can be obtained from the Cost and Revenue Analysis (CRA) which is traditionally used to calculate per-unit costs. *Id.*

RPW data is the original input source to the CRA, so using the CRA instead would not provide any advantages. Similarly, the Commission has evaluated the figures the Public Representative proposes to use for delivery points, and has not identified any advantages to revising the input data source from what was proposed in Order No. 5337. Accordingly, the Commission declines to adopt the Public Representative's recommendations.

Objections relating to the formula's use of the institutional cost ratio as a proxy for the elasticity of unit costs with respect to density. ACMA states that the Commission has not adequately justified the use of the institutional cost ratio in the density formula. ACMA Comments at 5. ACMA also states that there is no reason that the institutional cost ratio or percent variability in costs each year should be the same as the base year. *Id.* at 7. The Public Representative states that the Commission is not fully consistent with its definition of the institutional cost ratio, and encourages the Commission to provide supporting workpapers to demonstrate how year-over-year decreases in density drive an increase in per-unit cost.

As volume declines, some costs (those that are dependent on volume) also decline. The remaining costs, however, are necessarily borne by a smaller number of pieces, and decreasing the denominator drives up the per-unit cost. At the same time, as the number of delivery points increases, the expansion of the network increases the costs of providing service to the entire nation, independent of volume. The inclusion of the institutional cost ratio in the formula is designed to reflect these different cost behaviors in the approximation of the effect of density changes on per-unit costs. To the extent that the overall variability of costs with respect to volume changes over time, that change will be reflected in changes in the institutional cost ratio in future years.

The attached technical appendix to this Order explains in more detail why the institutional cost ratio is a good proxy for the elasticity of unit cost with respect to density, as well as the constraints on using the institutional cost ratio for that purpose.

Objections to the formula's comparison of Market Dominant volume to total volume. The Postal Service describes the formula's use of the least favorable of Market Dominant volume change and total volume change as arbitrary, arguing that cross-subsidization should be prevented by the appropriate share formula. Postal Service Comments at 27. The Postal Service urges the Commission to pick one of the two options. *Id.* ACMA notes that the Commission does not explain why it does not calculate the percent change in density for Competitive products as a group. ACMA Comments at 5.

GCA contends that the use of the least favorable of the two volume change figures is rationally designed to maximize protections for users of Market Dominant products. GCA Reply Comments at 2. GCA notes that the Commission is not trying to prevent a Competitive product from being priced below incremental cost, but rather is trying to protect Market Dominant mailers from paying for unit delivery cost increases caused exclusively by a decline in competitive density. *Id.* at 3. GCA describes the Commission as not attempting to create a new method of enforcing 39 U.S.C.

§ 3633(a)(1) and (2), but instead redesigning the density rate authority to provide improved protection for captive mailers. *Id.*

GCA is correct that the purpose of comparing Market Dominant volume to total volume is to protect Market Dominant mailers, rather than to create a new method of enforcing statutory provisions against cross-subsidization. As discussed above, the references to cross-subsidization in Order No. 5337 were erroneous. See Section IV.B.2., *supra*. The purpose of this part of the formula is to protect Market Dominant mailers from being forced to pay higher rates if changes in Competitive volume are less favorable than changes in Market Dominant volumes. This built-in safeguard also allows Market Dominant mailers to benefit from increases in Competitive volumes that have the effect of reducing the overall density-based rate authority.

D. Conclusion

Having considered the comments received on its proposal in Order No. 5337, the Commission concludes that the density-based rate authority will be an effective mechanism for providing additional Market Dominant ratemaking authority to offset the unavoidable increase in per-unit costs caused by the decline in mail density, which the Commission has identified as a primary driver of the Postal Service's net loss.

The Commission therefore implements the density-based rate authority as proposed in Order No. 5337, with the revision to permit banking such authority, as described above.

V. RETIREMENT-BASED RATE AUTHORITY

A. Introduction

In Order No. 5337, the Commission sought comments on its proposal to allocate additional Market Dominant rate authority based on the amount of specific retirement liabilities of the Postal Service. Order No. 5337 at 95-103. This additional authority, along with the density-based rate authority, was created to address critical comments that the Commission's prior proposal to annually allocate 2 percentage points of supplemental rate authority was not tied to specific drivers of the Postal Service's losses. *Id.* at 60. The Commission has carefully considered the comments received on Order No. 5337, and now implements the retirement-based rate authority as proposed, with a minor non-substantive clarification.¹⁴²

The Commission has identified the Postal Service's retirement costs as a specific driver of the Postal Service's net losses, and determined that the amortization payments for those retirement costs are beyond the Postal Service's control. Order No. 5337 at 62-63, 89-90; *see also* Section V.C.1., *infra*. The retirement-based rate authority modifies the existing price cap to include additional Market Dominant rate authority calculated from the proportional increase in revenue per piece for all products (both Market Dominant and Competitive) needed to permit the Postal Service to make the targeted amortization payments. To protect Market Dominant mailers from a large initial rate shock, this additional rate authority will be phased in over 5 years, with annual recalculations to ensure ongoing accuracy during the phase-in period.

¹⁴² See Section XII.C.2. (clarifying that limited rate adjustments to one or two price cells will not preclude later use of the retirement-based rate authority).

The Postal Service must remit all revenue raised under the additional rate authority towards the targeted amortization payments to be eligible to continue to receive the retirement-based rate authority.

The Commission concludes that the retirement-based rate authority is a necessary improvement to the existing system for regulating rates and classes for Market Dominant products and is, with the other proposed changes, necessary to achieve the objectives of 39 U.S.C. § 3622(b) in conjunction with each other. See *generally* Chapter XIII., *infra*.

B. Background

1. Postal Service Retirement Costs

Components of Postal Service retirement costs. Postal Service retirement benefits include: retiree health benefits (RHB), pension benefits under CSRS, and pension benefits under FERS.

Prior to the PAEA, the Postal Service was required to pay the employer's share of health insurance premiums for all current postal retirees and their survivors on a pay-as-you-go basis. 5 U.S.C. § 8906(g)(2)(A) (1970). The PAEA, in addition to the pay-as-you-go payments, established the Postal Service Retiree Health Benefits Fund (RHBF) and required the Postal Service to prefund long-term retiree health benefits for current

postal employees, retirees, and their survivors. 5 U.S.C. § 8906a(2)(a)(b). This prefunding requirement is unique to the Postal Service.¹⁴³

For FY 2007 through FY 2016, costs for retiree health benefits consisted of (1) fixed annual payments required to prefund the RHBF; and (2) the employer's share of health insurance premiums for all current Postal retirees and their survivors who participate in the Federal Employee Health Benefits Program (FEHBP)—the pay-as-you-go payments. 5 U.S.C. §§ 8909a(3)(B) and 8906(g)(2)(A). The Postal Service contributed \$20.9 billion to the RHBF between years FY 2007 to FY 2011, including transfers from existing funds and payments made in accordance with the fixed payment schedule required by 5 U.S.C. § 8909a(3)(a). Postal Service FY 2019 Form 10-K at 6. From FY 2012 to FY 2016, the Postal Service defaulted on a total of \$33.9 billion of the prefunding portion of its RHB payments. *Id.*

Beginning in FY 2017, the pay-as-you go payments were paid out of the RHBF, and so the Postal Service's costs for retiree health benefits consisted of (i) the present value of estimated future retiree health benefits attributable to active employees' current year of service (normal costs), and (ii) annual amortization payments required to liquidate the remaining unfunded balance in the RHBF by FY 2056. 5 U.S.C. § 8909a(2)(B). The Postal Service defaulted on all of these payments in years FY 2017 to FY 2019. Postal Service FY 2019 Form 10-K at 6. As of September 30, 2019, the Postal Service has missed or defaulted on a total of \$47.2 billion in payments to the RHBF. *Id.*

¹⁴³ See U.S. Government Accountability Office, GAO-13-112, U.S. Postal Service: Status, Financial Outlook, and Alternative Approaches to Fund Retiree Health Benefits (2012), at 7, available at: <https://www.gao.gov/assets/660/650511.pdf> ("the [prefunding] payments required by PAEA were significantly 'frontloaded,' with the fixed payment amounts in the first 10 years exceeding what actuarially determined amounts would have been using a 50-year amortization schedule).” The same reported noted that: “Although other federal, state and local, and private sector entities generally are not required to prefund retiree health care benefits, a few do prefund at limited percentages of their total liability.” GAO-13-112 at 45.

The PAEA also significantly changed many of the funding requirements for the CSRS. It removed the requirement for actuarially determining the funding for the Postal Service's portion of CSRS, and it also transferred the military service time for postal employees back to the responsibility of the Federal government. 5 U.S.C. § 8334(a)(B)(ii), 5 U.S.C. § 8348(g)(2). Additionally, beginning in FY 2017, the U.S. Office of Personnel Management (OPM) was required to evaluate the CSRS pension liability by June 30 of each year. 5 U.S.C. § 8348(h)(2)(B). In case of a surplus in the fund, the surplus is to be transferred to the RHBF during certain years.¹⁴⁴ If there is an unfunded liability, the Postal Service is to pay into the fund the present value equivalent (amortization) of the unfunded liability with interest through FY 2043. 5 U.S.C. § 8348(h)(2)(B). OPM calculated and invoiced the Postal Service for amortization of unfunded CSRS liabilities in years FY 2017 to FY 2019 totaling \$4.8 billion. Postal Service FY 2019 Form 10-K at 7. The Postal Service has defaulted on each of these amortization payments.¹⁴⁵

Postal Service retirement obligations for FERS consists of normal costs,¹⁴⁶ the employer portion of Thrift Savings Plan (TSP) contributions, social security, and amortization of any unfunded retirement liabilities. Postal Service FY 2019 Form 10-K at 6. The Postal Service is required to annually pay the share of the total value of benefits allocated to the valuation year (normal costs) without regard to any surplus funding or deficit position for CSRS. 5 U.S.C. §§ 8423(a) (describing payment

¹⁴⁴ Transfers of any CSRS surplus to the RHBF occur at the close of FY 2015, 2025, 2035, and 2039. 5 U.S.C. § 8348(h)(2)(C).

¹⁴⁵ Postal Service FY 2019 Form 10-K at 63. CSRS was replaced by FERS. "The CSRS, implemented in 1921, is a stand-alone plan, providing benefits to most Federal employees hired before 1984.... The FERS was established in 1986 and when it became effective on January 1, 1987, CSRS Interim employees with less than 5 years of creditable civilian service on December 31, 1986, were automatically converted to FERS." United States Office of Personal Management, Agency Financial Report Fiscal Year 2019 (November 2019), at 51 (OPM Fiscal Year 2019 Agency Financial Report). The Postal Service is not assessed service (normal) costs for CSRS. 5 U.S.C. § 8334(a)(B)(ii).

¹⁴⁶ The employer portion of retirement benefits established by OPM, attributable to active employees' current year of service. Postal Service FY 2019 Form 10-K at 6.

requirement) and 8423(a)(2)(B)(iv) (exempting Postal Service from provisions related to the unfunded liability of CSRS). The Postal Service is also required to pay additional installment (supplemental) payments for FERS, but only in circumstances in which the prior and future contributions made by the Postal Service and its employees are inadequate to cover the benefits expected to be paid from the Postal Service's FERS account. 5 U.S.C. § 8423(b)(2). OPM calculated amortization payments of supplemental liabilities in years FY 2017 to FY 2019 totaling \$2.9 billion. Postal Service FY 2019 Form 10-K at 6. The Postal Service has annually paid its FERS normal costs, but defaulted on the supplemental payments in FY 2017 through FY 2019. *Id.*

The specific retirement costs targeted by the retirement-based rate authority are the annual amortization payments for the unfunded RHBF liability, the amortization payments for any unfunded CSRS liability, and the amortization payments for FERS supplemental liabilities (collectively, amortization payments).

2. Retirement-Based Rate Authority in the Revised Notice of Proposed Rulemaking

In Order No. 5337, the Commission responded to criticism that its original proposal to provide supplemental rate authority in its first NPR was not tied to specific drivers of the Postal Service's net losses. Order No. 5337 at 62. Along with the increase in per-unit costs caused by the decline in mail density,¹⁴⁷ the Commission identified the Postal Service's statutorily mandated amortization payments for particular

¹⁴⁷ See Chapter IV., *supra*.

retirement costs as a driver of the Postal Service's net losses and a primary obstacle to the Postal Service's ability to achieve net income.¹⁴⁸ To more precisely target these loss drivers, the Commission replaced its original supplemental rate authority proposal of a static 2 percentage points of Market Dominant rate adjustment authority per year with the Density-Based and Retirement-Based Rate Authorities, each of which use formulas to annually calculate the appropriate amount of additional rate authority for each loss driver.¹⁴⁹ The Commission noted that unlike other components of the Postal Service's retirement costs that in-principle vary with volume, the amortized components of the Postal Service's retirement costs are institutional costs,¹⁵⁰ the amount of which is determined by OPM based on prior year service costs that are beyond the Postal Service's control.¹⁵¹

Calculation and implementation. As proposed in Order No. 5337 and implemented here, the amount of the retirement-based rate authority will be determined annually based on the formulas described below, and would be available to the Postal Service to use in any rate change that is implemented within 12 months of the date of the determination. See Order No. 5337 at 91. The full additional rate authority will be phased in over 5 years, contingent upon the Postal Service's ongoing partial

¹⁴⁸ Order No. 5337 at 62; see *id.* at 89 (discussing GAO attribution of Postal Service financial instability to the statutorily mandated prefunding requirements and previous Commission findings related to RHBF payments as a major factor in net losses from FY 2012 to FY 2016). For an expanded discussion of the targeted amortization costs as a driver of the Postal Service's net losses, see Section V.C.1., *infra*.

¹⁴⁹ Order No. 5337 at 62-63. Unlike the Density-Based Rate Authority, the amount of the Retirement-Based Rate Authority is calculated on an annual basis only during the 5-year phase in period. *Id.* at 63. Beyond that period, no new authority is provided.

¹⁵⁰ The amortization payment for CSRS additionally includes a small portion of current-year costs related to remaining employees covered by CSRS. Summary Description of USPS Development of Costs by Cost Segments and Components Fiscal Year 2019, July 1, 2020, at 18-3.

¹⁵¹ *Id.* at 90. For an expanded discussion of the degree to which the targeted amortization payments are outside the Postal Service's control, see Section V.C.1., *infra*.

amortization payments towards its unfunded retirement liabilities. *Id.* The required minimum remittance for these payments in each year is equal to the amount of revenue raised from the additional rate authority during the previous fiscal year. *Id.*

As described in Order No. 5337, the formulas for the retirement-based rate authority calculate the percentage amount by which revenue on all products (both Market Dominant and Competitive) would need to increase to make the full payments (as calculated by OPM). *Id.* at 91-92. That same percentage is authorized as additional rate authority for Market Dominant products, spread out over the phase-in period.¹⁵² Each year during the 5-year phase-in period, the required percentage increase is recalculated based on the current amount of the OPM invoice, reduced by the actual amount of revenue collected under the retirement-based rate authority in the previous year, and the balance spread across the remainder of the phase-in period.¹⁵³

The Commission described how the annual recalculation ensures that the retirement-based rate authority accounts for volume changes during the phase-in period. *Id.* This recalibration protects the Postal Service from receiving too little additional revenue at the end of the phase-in period as a result of decreases in volume, and protects mailers against unnecessarily large price increases as a result of increases in volume. *See id.* The Commission also discussed other protections for mailers, including how calculating the amount of the rate authority as a fraction of total revenue rather than Market Dominant revenue ensures that the burden does not fall

¹⁵² *Id.* The Commission notes that implementing an equivalent rate increase on Competitive products is outside the scope of this docket and remains within the Postal Service's business discretion. Competitive products are subject to a different statutory and regulatory framework, and the Postal Service does not require additional rate authority to be granted by the Commission to implement the same increase on Competitive products.

¹⁵³ *Id.* at 92. Because OPM does not add the unpaid amount to the unfunded liability subject to amortization (instead treating the amount as currently due), the required percentage increase will not substantially change throughout the phase-in period as a result of the Postal Service making only partial payments. *See* Notice of Supplemental Information, August 10, 2017 (August 10, 2017 Notice of Supplemental Information).

disproportionately on Market Dominant mailers. *Id.* at 93. Additionally, to remain eligible for future retirement-based rate authority (and to avoid other equitable remedies at the discretion of the Commission), the Postal Service must remit the entire amount of revenue raised under this authority each year towards the targeted amortization payments, protecting mailers against the possibility that the Postal Service might use the additional rate authority and then spend it elsewhere. *Id.*

Formulas. Formula V-1 shows how the Commission calculates the retirement-based rate authority available during each year of the phase-in period. The first step is to divide the required amortization payment (as calculated by OPM) for the most recent fiscal year by the total revenue from that fiscal year. This proportion, expressed in percentage terms, is the amount by which total revenue would need to increase to make the full payment. From that proportion is subtracted the compounded amount of previously granted retirement-based rate authority (calculated in Formula V-2). The resulting difference is then amortized over the remainder of the phase-in period to determine the amount of retirement-based rate authority authorized that year.

(Formula V-1) Retirement rate authority available in fiscal year T+1 =

$$\left(1 + \frac{AP_T}{TR_T} - PARA_T\right)^{\frac{1}{5-N}} - 1$$

Where,

T = most recently completed fiscal year;

AP_T = total amortization payment for fiscal year T;

TR_T = total revenue in fiscal year T;

PARA_T = previously authorized retirement obligation rate authority, compounded through fiscal year T, expressed as a proportion of the Market Dominant rate base and calculated using the formula below; and

N = number of previously issued determinations in which retirement obligation rate authority was made available under this subpart.

Formula V-2 shows how the compounded amount of previously granted retirement-based rate authority is calculated. The sums of 1 plus each previous year's retirement-based rate authority are multiplied together to determine how much higher rates are than they would have been without any previously authorized retirement-based rate authority. The inverse of that product is then subtracted from 1 to express the result as a proportion of the Market Dominant rate base.

(Formula V-2) Previously authorized retirement obligation rate authority through fiscal year T =

$$1 - \left(\prod_{t=T-N}^T (1 + r_t) \right)^{-1}$$

Where,

T = most recently completed fiscal year;
 r_t = retirement obligation rate authority authorized in fiscal year t; and
 N = number of previously issued determinations in which retirement obligation rate authority was made available under this subpart.

Formula V-3 shows how the amount of revenue generated in a fiscal year by use of retirement-based rate authority is calculated, and thus the minimum amount that the Postal Service must remit towards its amortization payments to remain eligible for future retirement-based rate authority. As in Formula V-2, the sums of 1 plus each previous year's retirement-based rate authority are multiplied together, except that each previous year's rate authority is prorated (calculated in Formula V-4) if it came into effect partway during the fiscal year. The inverse of that product is then subtracted from 1 to express the result as the proportion of Market Dominant revenue resulting from use of retirement-based rate authority. Multiplying that proportion by Market Dominant revenue converts the result into a dollar amount.

(Formula V-3) Amount of revenue collected during fiscal year T as a result of the use of retirement-based rate authority =

$$MDR_T \left(1 - \left(\prod_{t=T-N}^T 1 + (p_t)(r_t) \right)^{-1} \right)$$

Where,

T = most recently completed fiscal year;
 MDR_T = Market Dominant revenue in fiscal year T;
 N = number of previously issued determinations in which retirement obligation rate authority was made available under this subpart;
 r_t = retirement obligation rate authority authorized in fiscal year t; and
 p_t = prorated fraction of r_t that was in effect during fiscal year T, calculated using the formula below.

Formula V-4 shows how each year's retirement-based rate authority is prorated when calculating its contribution to the total amount of revenue. If a particular year's authority was implemented prior to the start of the fiscal year, all of it is included in the calculation. Conversely, if a particular year's authority was not implemented prior to the end of the fiscal year, none of it is included in the calculation. If a particular year's authority was first implemented during the fiscal year, a volume-weighted average is taken to calculate how much of the fiscal year's volume was subject to that rate authority. To do so, the proportion of volume in the quarter of implementation occurring after the date of implementation is added to the volume for subsequent quarters, and the sum divided by the total Market Dominant volume for the fiscal year.

(Formula V-4) Prorated fraction of rate authority in effect during fiscal year T =

$$\begin{cases} 0, & \text{if } r_t \text{ was not in effect during fiscal year T} \\ 1, & \text{if } r_t \text{ was in effect for all of fiscal year T} \\ \frac{\left(\frac{E_Q}{D_Q}\right) (QMDV_Q) + \sum_{i=Q+1}^4 QMDV_i}{MDV_T}, & \text{if } r_t \text{ came into effect during fiscal year T} \end{cases}$$

Where,

T = most recently completed fiscal year;

r_t = retirement obligation rate authority authorized under this subpart in fiscal year t;

Q = the number of the quarter during the fiscal year of the effective date of the price increase including retirement obligation rate authority made available under this subpart;

E_Q = number of days in quarter Q subsequent to and including the effective date of the price increase;

D_Q = total number of days in quarter Q;

$QMDV_Q$ = Market Dominant volume in quarter Q; and

MDV_T = Market Dominant volume in fiscal year T.

A hypothetical example of the formulas in operation can be found in the attached technical appendix. Appendix A, Section II.A.

C. Commission Analysis

Comments on the retirement-based rate authority fall into three categories: general conceptual objections to providing the retirement-based rate authority, methodological objections regarding how the retirement-based rate authority is implemented, and comments concerning removal of the retirement-based rate authority from the rate base in the event of non-compliance. Each group of comments is discussed below.

1. Conceptual Objections to Retirement-Based Rate Authority

Objections that the retirement-based rate authority is—or is not—a true-up of rates. ANM *et al.* object to the retirement-based rate authority on the basis that it is a true-up of rates. ANM *et al.* Comments at 52-54. ANM *et al.* further claim that such a true-up violates congressional intent. *Id.* at 53. ANM *et al.* also characterize the density- and retirement-based rate authorities as resembling a cost-of-service regime that permits the Postal Service to recover prior-year cost-control shortfalls. *Id.* at 17.

Conversely, the Postal Service objects to the retirement-based rate authority on the basis that it is *not* a true-up of rates, stating “best practices of price-cap regulation would be to authorize a reset of the Postal Service’s revenue base to a compensatory level....” Postal Service Comments at 15.

The retirement-based rate authority is not a true-up of rates, nor is it intended to be.¹⁵⁴ To reiterate, the Commission has identified the amortization payments for particular retirement costs to be a “primary obstacle” to the Postal Service’s ability to achieve net income, and thus to satisfying the objectives of 39 U.S.C. § 3622(b). See Order No. 5337 at 60; Section V.C.1., *infra*. The retirement-based rate authority: (1) modifies the available rate cap authority to cover these specific costs; (2) only applies to future rates; and (3) is limited to specifically-identified exogenous costs required by statute and calculated by OPM.

Similarly, the Commission is not attempting to compensate the Postal Service for cost-control shortfalls by implementing the retirement-based rate authority. There are no short- or medium-term cost-control measures the Postal Service can take to meaningfully affect the amortization portion of its retirement costs. Missed payments are excluded from the amortization portion,¹⁵⁵ so the Commission is not compensating the Postal Service for its \$49.7 billion in missed payments.¹⁵⁶ The Postal Service has forgone the investment returns that would have accrued had the missed payments been contributed to the RHBF, but this does not affect the unfunded liability that arises in the

¹⁵⁴ A true-up for retirement expenses would, at a minimum, be designed to recover the revenue necessary to make the previously defaulted payments. A more general true-up would be designed to recover all cumulative losses since the enactment of the PAEA.

¹⁵⁵ See August 10, 2017 Notice of Supplemental Information.

¹⁵⁶ Postal Service FY 2019 Form 10-K at 29, 33 (showing \$2.7 billion past due for CSRS and FERS, and \$47.2 billion past due for RHB).

RHBF, FERS, and CSRS as a result of changes in actuarial assumptions and the discount rate.

Making necessary modifications to the system of ratemaking to achieve the objectives of 39 U.S.C. § 3622(b) is fully in keeping with the Congressional intent that the Commission modify or replace the price cap when it is found to not achieve those objectives. See 39 U.S.C. § 3622(d)(3); Section III.B., *supra*. While the existing ratemaking system does not distinguish among types of obligations (such as giving special status to any type of cost or obligation), it left the Postal Service limited means to meet those obligations. The Commission, in part due to the Postal Service's inability to meet its obligations (especially those largely outside of its control), has determined that the existing system failed to achieve the objectives of 39 U.S.C. § 3622(b), taking into account the factors of 39 U.S.C. § 3622(c). See Order No. 4257; Retirement-Based Rate Authority in the Revised Notice of Proposed Rulemaking, *supra*. The Commission is thus empowered by the terms of the statute to modify or replace the existing system, as necessary to achieve the objectives. See 39 U.S.C. 3622(d)(3). The retirement-based rate authority is a modification of the existing system that addresses the specific problem that retirement amortization costs are driving the Postal Service's net losses which are preventing the existing system from achieving Objective 5.

Objections that the retirement-based rate authority is an impermissible exercise in retroactive ratemaking. ANM *et al.* argue that the proposal "singles out and attempts to true up a single expense that the Postal Service was always intended to recover in its rates, an action that is contrary to incentive ratemaking theory and amounts to impermissible retroactive ratemaking." ANM *et al.* Comments at 51 (citing *Old Dominion Elec. Coop. v. FERC*, 892 F.3d 1223, 1227 (D.C. Cir. 2018)). However, the rule prohibiting retroactive ratemaking does not apply to the proposal nor to the Commission.

The rule against retroactive ratemaking “prohibits [the Federal Energy Regulatory Commission (FERC)] from adjusting current rates to make up for a utility's over- or under-collection in prior periods.”¹⁵⁷

As this rule is based on limits to FERC authority, it is not applicable here. In a recent case, the D.C. Circuit explained that the question of whether a particular method of ratemaking is retroactive, and thus impermissible, is a question of law rooted in the Interstate Commerce Act, the statute that governs FERC’s regulation of oil pipelines.¹⁵⁸ In particular, statutory language states that if FERC finds a rate unreasonable, it shall determine the just and reasonable rate to be thereafter observed and in force. See, e.g., 16 U.S.C. § 824e(a); 15 U.S.C. § 717d(a). The use of “thereafter” is what courts have used to find that FERC has no authority to alter a rate retroactively.¹⁵⁹ No similar language is found in 39 U.S.C. § 3622.¹⁶⁰

The Commission’s proposal to provide additional authority to the Postal Service to fulfill its statutorily mandated retirement obligations is not an adjustment of current rates. Interpreting the rules in a light most favorable to ANM *et al.*’s arguments, the

¹⁵⁷ *Old Dominion*, 892 F.3d at 1227 (citing *Towns of Concord, Norwood, & Wellesley v. FERC*, 955 F.2d 67, 71 n.2 (D.C. Cir. 1992)).

¹⁵⁸ See *SFPP, L.P. v. FERC*, 967 F.3d 788, 801-802 (D.C. Cir. 2020).

¹⁵⁹ See *City of Anaheim v. FERC*, 558 F.3d 521, 522 (D.C. Cir. 2009); *Ark. La. Gas Co. v. Hall*, 453 U.S. 571, 577 (1971).

¹⁶⁰ Notwithstanding the rule being rooted in the statutory limits on FERC’s authority, it also applies in that instance to rate adjustments within an existing system, not the creation or modification of a ratemaking system. The rule against retroactive ratemaking prohibits the adjustment of current rates to make up for a utility’s inadequate collection in prior periods. *Old Dominion*, 892 F.3d at 1227. It is a corollary of the filed rate doctrine. See *SFPP*, 967 F.3d at 801-802. This doctrine provides that a regulated entity may not charge, or be forced to charge, a rate different from the one on file with FERC for a particular good or service. *Id.* The considerations underlying the doctrine are preservation of the agency’s primary jurisdiction over reasonableness of rates and the need to ensure that regulated companies charge only those rates of which the agency has been made cognizant. See *Ark. La. Gas Co. v. Hall*, 453 U.S. 571, 577-578 (1971). Because it concerns current rates on file, this doctrine is also inapplicable here.

proposal provides advance notice that the Postal Service may have access to additional rate authority for future rate adjustment proceedings. Such notice does not constitute retroactive rulemaking.¹⁶¹

ANM *et al.* also argue that the proposal is contrary to incentive ratemaking theory. ANM *et al.* Comments at 51. However, the system for regulating rates and classes for Market Dominant products is not a system solely based on incentive ratemaking theory, which primarily emphasizes incentivizing cost reductions and efficiency improvements. The aim to incentivize cost reductions and increase efficiency, however, is only one of nine specific objectives that the Commission must apply in conjunction with each other when revising the ratemaking system. 39 U.S.C. § 3622; see Chapter XIII., *infra*. Accordingly, the ratemaking system must be revised in a way necessary to achieve all nine objectives, and cannot, given that mandate, adhere unequivocally to incentive ratemaking principles.

Objections that the retirement-based rate authority will not benefit the Postal Service while imposing an undue burden on mailers. The Postal Service, ANM *et al.*, ABA, and NPPC *et al.* argue that the retirement-based rate authority will not improve the financial position of the Postal Service.¹⁶² In particular, the Postal Service emphasizes that the retirement-based rate authority does not improve the Postal Service's liquidity because the revenue raised must in turn be remitted to OPM. See Postal Service Comments at 18. ANM *et al.* and ABA additionally argue that the retirement-based rate authority imposes an undue burden on mailers. ANM *et al.* Comments at 52-54; ABA Reply Comments at 6.

¹⁶¹ See *Columbia Gas Transmission Corp. v. FERC*, 895 F.3d 791, 796-797 (D.C. Cir. 1990).

¹⁶² Postal Service Comments at 18; ANM *et al.* Comments at 57-58; ABA Reply Comments at 6; NPPC *et al.* Reply Comments at 9.

The purpose of the retirement-based rate authority is to improve the Postal Service's ability to achieve net income rather than to improve the Postal Service's liquidity. The Postal Service cannot achieve net income if it does not generate sufficient revenue to be able to make its statutorily mandated payments. To address this problem, the retirement-based rate authority provides additional rate adjustment authority and the revenue derived must be remitted towards the portion of those payments that the Postal Service cannot control.

The retirement-based rate authority contains strong protections designed to limit the burden on mailers while also providing additional revenue to address the underlying driver of loss. Examples include: (1) using a phase-in period to create a predictable and stable schedule for rate increases; (2) limiting the amount of the rate authority for Market Dominant products to the percentage by which revenue would have to increase for all products (both Market Dominant and Competitive) to make the full amortization payments; and (3) requiring that all of the revenue generated under the retirement-based rate authority is actually remitted towards those payments. These protections help ensure that the retirement-based rate authority limits the effect on mailers while simultaneously improving the ability of the Postal Service to achieve net income.

The Commission is permitting the density-based rate authority to be banked on the grounds that doing so will assist the Postal Service in responding to potential changes in price elasticity. See Section IV.C.1., *infra*. In the case of the retirement-based rate authority, however, permitting banking would defeat the purpose of the phase-in period that protects mailers by smoothing out the rate increases, and overly-complicate the adjustment for mail-mix change and induced volume decline during the phase-in period. Given those countervailing factors, the Commission maintains the requirement that the retirement-based rate authority is only available for 12 months after the Commission's determination of the amount of retirement-based rate authority.

Objection that the retirement-based rate authority addresses a problem that should be fixed legislatively. ABA argues that the Postal Service's retirement obligations are a topic best addressed by Congress. ABA Reply Comments at 6.

While Congress certainly has the authority to act to address the retirement obligations of the Postal Service, in the absence of Congressional action, the Commission has the authority as explained above to take action to address the identified retirement costs, which remain a primary driver of the Postal Service's ongoing losses, thus preventing the Postal Service from achieving net income.¹⁶³ The Commission's modifications to the system of ratemaking are necessary to achieve the objectives, and as a corollary, the scope of the Commission's authority is limited to the system of ratemaking. The Commission cannot abdicate its responsibility to address a driver of the Postal Service's net loss (and thus a driver of the existing system's failure to achieve the objectives).

Objections that the retirement-based rate authority will counter-productively induce further volume loss. ANM *et al.*, Mailer's Hub, ABA, and NPPC *et al.* argue that the retirement-based rate authority will contribute to additional volume loss, especially when combined with the other sources of rate authority.¹⁶⁴

The Commission's experience demonstrates that demand for Market Dominant products has been price inelastic in both the pre-PAEA period and the PAEA period. Accordingly, the decrease in volume induced by the retirement-based rate authority is expected to be less in proportional terms than the amount of retirement-based rate authority.

¹⁶³ The Commission reiterates that the retirement-based rate authority does not provide the Postal Service with additional revenue to offset its previous (or future) missed payments. The payments do not affect the amortization portion of the Postal Service's retirement costs.

¹⁶⁴ ANM *et al.* Comments at 29-33, 59; Mailer's Hub Comments at 6-7; ABA Comments at 1; NPPC *et al.* Comments at 13.

ANM *et al.* argue that the Commission should anticipate that price elasticity will increase beyond the Postal Service's elasticity estimates as rates rise. ANM *et al.* Comments at 32-33. Unlike the density-based rate authority, where the Postal Service can decide on a year-to-year basis how much of the additional authority to use, if the Postal Service opts to make use of the retirement-based rate authority, it is required to continue to use the available additional authority throughout the phase-in period, or else forfeit the remaining authority. See Section IV.C.1., *infra*. Although this limits the Postal Service's flexibility to respond to observed changes in price elasticity, rate increases under the retirement-based rate authority are limited to the 5-year phase-in period, after which there will be no further rate increases that may induce further volume loss. If price elasticity were to change abruptly, the Commission may review the components of the ratemaking system sooner than the scheduled 5-year review. Additionally, the Postal Service could, as the operator, make the judgment to forfeit the additional authority should the circumstances warrant.

ANM *et al.* also argue that mailers will respond to the amount of price authority granted to the Postal Service, rather than the amount by which the Postal Service ultimately raises rates. ANM *et al.* Comments at 32. The Commission expects that mailers will behave rationally based on the best information they have available. In a situation where elasticity has increased to the point that using additional rate authority would hurt the Postal Service, it is reasonable to expect that the Postal Service will choose not to use all of its available rate authority. If the Postal Service has signaled an intent on such grounds, it is also reasonable to expect that mailers will respond rationally to the Postal Service's actions.

Objections that the retirement-based rate authority will disincentivize efficiency. ANM *et al.* argue that the retirement-based rate authority does not provide the Postal Service with the correct incentives to improve efficiency because it increases rates in reaction to increases in costs. See ANM *et al.* Comments at 51.

The retirement-based rate authority does not increase rates in response to general increases in costs and does not reduce the Postal Service's incentive for efficiency because the Postal Service cannot directly decrease the amount of its unfunded retirement liabilities through improved efficiency. See Order No. 5337 at 62-63; Section V.C.1., *infra*. The Postal Service will need cost savings and efficiency gains to fully achieve financial health, and cost savings it reaps from increased efficiency in other areas do not affect the amount of retirement-based rate authority. See Section XIII.E.1., *infra*.

Objections that the retirement-based rate authority arbitrarily targets specific retirement costs. The Postal Service and NALC argue that the Commission's distinction between normal retirement costs and the amortization portion of the Postal Service's retirement obligations is arbitrary. Postal Service Comments at 17; NALC Comments at 2. APWU recommends that the Commission consider including normal costs as part of the retirement-based rate authority. APWU Comments at 4-5. The Postal Service states that although normal retirement costs depend on headcount, which is within the control of the Postal Service, normal costs fluctuate in response to the same OPM actuarial assumptions that drive changes in amortization costs. Postal Service Comments at 17 n.7. The Postal Service also points out that some of the influences on its headcount are also outside its control, citing as examples labor arbitration and the Postal Service's universal service obligation. *Id.*

The retirement-based rate authority targets amortization costs rather than normal costs due to the same distinction acknowledged by the Postal Service. It has more control over normal costs than over amortization costs. Amortization costs are based on prior year service costs (in addition to actuarial and financial assumptions) and thus are outside of postal management's operational control. Reducing current or future headcount, for example, does not directly affect the amount of the Postal Service's amortization costs. By contrast, normal costs—the cost of the future retirement benefits

earned by employees in the current year—while also influenced by actuarial and financial assumptions, are affected by current-year operational decisions, including headcount. The fact that actuarial and financial assumptions also factor in to the Postal Service’s normal retirement costs does not eliminate this distinction between normal and amortization costs.¹⁶⁵

Additional Commission analysis. The Commission reiterates its determinations that the Postal Service’s retirement costs are a primary driver of its net losses and that the targeted amortization payments are outside the Postal Service’s control. See Section V.B.2., *supra* (citing Order No. 5337 at 62, 89-90).

As previously stated above and in Order No. 5337, the GAO has attributed the Postal Service’s financial instability to the statutorily mandated prefunding requirements,¹⁶⁶ and the Commission has previously found RHBF payments as a major factor in net losses from FY 2012 to FY 2016. Order No. 5337 at 89 (citing Order No. 4257 at 41). Additionally, as shown in Table V-1, the Commission notes that the PAEA was enacted at a time when the Postal Service was experiencing modest profits under the previous regulatory regime. In every year since the PAEA imposed new payment

¹⁶⁵ The Commission also notes that the density-based rate authority provides increased rate authority to offset the expected increase in per-unit costs (including retirement costs) caused by the decline in mail density. Thus, in the case where growth of the Postal Service’s delivery network is not accompanied by an equivalent growth in mail volume, the density-based rate authority ameliorates the Postal Service’s concern that its obligation to serve its entire network puts exogenous upwards pressure on its headcount (and thus its normal retirement costs).

¹⁶⁶ See Order No. 5337 at 89 n.171; GAO 13-112 2 (“We have previously reported that USPS cannot be financially viable until Congress and USPS address the cash flow problems that limit its immediate prefunding capability while also addressing how to pay for the long-term cost of USPS’s unfunded retiree health benefit liability”); U.S. Government Accountability Office, GAO-17-404T, U.S. Postal Service: Key Considerations for Restoring Fiscal Sustainability (Statement of Lori Rectanus, Director, Physical Infrastructure Issues) (2017), at 6, available at: <https://www.gao.gov/assets/690/682534.pdf> (“As previously discussed, USPS’s unfunded liabilities and debt have become a large financial burden, increasing from 99 percent of USPS revenues at the end of fiscal year 2007 to 169 percent of revenues at the end of fiscal year 2016. These unfunded liabilities and debt—totaling about \$121 billion at the end of fiscal year 2016—consist mostly of retiree health and pension benefit obligations for which USPS has not set aside sufficient funds to cover.” (footnote omitted)).

requirements for the newly established RHBF, revenue has not been adequate to cover the added costs, even in years when the Postal Service would have experienced net income but for the PAEA prefunding requirements (required by statute through 2016) and amortization payments (required by statute starting in 2017).

Table V-1
Net Loss With and Without PAEA-Imposed Expenses

Fiscal Year	Net Income (Loss) before PAEA mandated payments <i>(\$ in millions)</i>	Add: Statutory Prefunding to RHBF <i>(\$ in millions)</i>	Add: Amortization of unfunded RHBF obligation <i>(\$ in millions)</i>	Add: Amortization of unfunded CSRS obligation <i>(\$ in millions)</i>	Add: Amortization of unfunded FERS obligation <i>(\$ in millions)</i>	Total Net Income (Loss) <i>(\$ in millions)</i>
2006	\$ 900					\$ 900
2007	\$ 3,216	8,358				\$ (5,142)
2008	\$ 2,794	5,600				\$ (2,806)
2009	\$ (2,394)	1,400				\$ (3,794)
2010	\$ (3,005)	5,500				\$ (8,505)
2011	\$ (5,067)	-				\$ (5,067)
2012	\$ (4,806)	11,100				\$ (15,906)
2013	\$ 623	5,600				\$ (4,977)
2014	\$ 192	5,700				\$ (5,508)
2015	\$ 881	5,700			241	\$ (5,060)
2016	\$ 457	5,800			248	\$ (5,591)
2017	\$ 871		955	1,741	917	\$ (2,742)
2018	\$ (700)		815	1,440	958	\$ (3,913)
2019	\$ (5,347)		789	1,617	1,060	\$ (8,813)

Source: Please see Appendix A, Section II.B. for references to source data.

The Commission has also explained that the amount of the targeted amortization payments are calculated by OPM based largely on prior-year service costs. Order No. 5337 at 90. To elaborate, the amount the Postal Service is invoiced by OPM for its amortization payments is calculated based on the amount of the unfunded liability in the RHBF. For purposes of this calculation, the amount of the unfunded liability is reduced by the outstanding amounts of the missed payments. See August 10, 2017 Notice of

Supplemental Information. With that adjustment, the remaining unfunded liability subject to amortization is primarily the result of liability incurred in previous years for future retirees, which the Commission refers to as prior-year service costs.¹⁶⁷ Starting in 2017, however, the Postal Service was required to annually pay each year's service costs into the RHBF,¹⁶⁸ so since 2017 the amount of those costs no longer adds to the unfunded liability subject to amortization—if the Postal Service makes the payment, there is no additional unfunded liability, and if the Postal Service fails to make the payment, the amount of that payment will be deducted from the total unfunded liability before determining the amortization payment.¹⁶⁹ Accordingly, making changes to the size of its current workforce—the primary method the Postal Service has for controlling its retirement costs—would not in the near term affect the amount of its outstanding unfunded RHBF liabilities, and thus would not affect the amount it is invoiced by OPM for its amortization payments. At best, changing the size of its current and future workforce to reduce the amount of future normal costs could limit the growth of its unfunded liability, but would not affect the amount of unfunded liability already accrued.

The Postal Service similarly has no control over its amortization payments for FERS and CSRS. The Postal Service pays the normal costs of FERS but has defaulted on its amortization payments. The amortization payments consist solely of supplemental¹⁷⁰ payments for changes in liability due to actuarial re-evaluations. See Section V.B.1., *supra*. Reducing the size of its current workforce would thus have no

¹⁶⁷ The amount of the unfunded liability subject to amortization also includes actuarial changes, financial returns on the balance of the RHBF, and the discount rate applied to the total liability. See, e.g., Postal Service FY 2019 Form 10-K at 33.

¹⁶⁸ See Section V.B.1., *supra*.

¹⁶⁹ Instead, the missed payment remains as a past due balance. See August 10, 2017 Notice of Supplemental Information at 1-2.

¹⁷⁰ Additional installment payments are assessed when the prior and future contributions made by the Postal Service and its employees are inadequate to cover the benefits expected to be paid from the Postal Service's FERS account.

effect at all on the amount of the Postal Service's amortization payments for FERS. Similarly, CSRS which replaced FERS, has been frozen since 1987 and has a dwindling active employee population close to the end of their careers.¹⁷¹ As such, the amount of its amortization payments are again dependent almost entirely on actuarial re-evaluations.

2. Methodological Objections to Retirement-Based Rate Authority

Objections that the retirement-based rate authority does not account for changes in the OPM invoice after the phase-in period. The Postal Service argues that the retirement-based rate authority formula does not provide an adjustment for the amount of the OPM invoice after the phase-in period. Postal Service Comments at 20.

The retirement-based rate authority is intended as a phased-in one-time increase in the rate base, rather than as an ongoing surcharge. The purpose of the phase-in period is to avoid putting an undue burden on mailers by applying a one-time increase of the full amount of the 5-year retirement-based rate authority. Because the inputs to the retirement-based rate authority change during the phase-in period, it is reasonable to adjust the annual retirement-based rate authority to match the new inputs while the phase-in period lasts. After the phase-in period, should the amount of the OPM invoice change, or mail volumes decline, the Postal Service is still only required to remit to OPM the actual amount of revenue collected as a result of the retirement-based rate authority.

It is also reasonable to not build in provisions for additional adjustments after the phase-in period because the Commission will revisit the retirement-based rate authority at least 5 years after implementation, and sooner if it appears it is not working as intended, or should the magnitude of the obligations change in either direction. This

¹⁷¹ See Docket No. SS2018-1, Report to the Postal Regulatory Commission on Civil Service Retirement System Demographic and Salary Assumptions, May 16, 2018, at 3.

serves as an additional protection for mailers (and the Postal Service) and obviates the need for scheduled adjustments after the phase-in period.

Objections that the retirement-based rate authority does not fully compensate the Postal Service for the targeted retirement costs. The Postal Service claims that the retirement-based rate authority does not fully compensate it for the amortization portion of the identified retirement costs. Postal Service Comments at 16-17.

The retirement-based rate authority is not intended to provide full compensation. Instead, the formula calculates the revenue increase that would be required from all products (both Market Dominant and Competitive). The scope of the Commission's authority in the instant docket is limited to the Market Dominant rate system, and authorizing that percentage of increase on Market Dominant products will necessarily not recover the full amount of the identified retirement costs. This prevents Market Dominant mailers from being required to pay the entirety of the identified retirement costs. The Commission notes that the Postal Service is free to implement an equivalent rate increase on Competitive products and does not require additional rate authority to be granted by the Commission to do so, as long as the Competitive rate increase complies with all relevant statutory and regulatory requirements.

The amount of the retirement-based rate authority is determined based on actual, measured changes in the amount of the Postal Service's liability and actual, measured volume. This is consistent with the price cap, which bases rate authority on actual, measured changes in inflation, and the density-based rate authority, which is based on actual, measured changes in density. This consistent methodology has the substantial advantage of avoiding the need to predict future volumes and correct for inaccurate predictions. The advantage of avoiding the need to make predictions about volume outweighs the 1-year lag created by waiting to use actual, measured data.

Objections that the retirement-based rate authority does not account for \$3.1 billion already included in the rate base. NPPC *et al.* argue that the retirement-based

rate authority should take into account the \$3.1 billion per year added to the rate base in Docket No. R2005-1. NPPC *et al.* Comments at 44. Similarly, ANM *et al.* argue that RHB expenses should have always been compensated by postal rates. ANM *et al.* Comments at 51. Additionally, the Public Representative states that the Commission should determine whether the retirement-based rate authority is already provided for under the CPI-U price cap. PR Reply Comments at 21-22. Mailers Hub, by contrast, argues that last-minute changes in the prefunding schedule under the PAEA (compressing 40 years of prefunding payments into 10 years) suggest that little consideration was given at the time of the PAEA's enactment to whether the CPI-cap could generate sufficient revenue to cover the newly mandated retirement expenses. Mailers Hub Comments at 4-5.

The \$3.1 billion added to the rate base in Docket No. R2005-1 was part of the pre-PAEA cost-of-service ratemaking system. The funds were required to be escrowed, but there was no requirement that the escrowed funds be spent in any particular way. After the PAEA passed, the escrow requirement was removed. Additionally, the PAEA imposed the new RHBF liability.

The transition to the PAEA was a change to a new ratemaking system, with the existing rate base (including the \$3.1 billion from Docket No. R2005-1) as a starting point. The new ratemaking system was evaluated on its own terms, and using the data generated by experience under that system.¹⁷² Accordingly, the question of how much of the pre-PAEA rate base was originally intended to cover retirement costs is not relevant to the Commission's finding that the current ratemaking system has not achieved the specified objectives, or to the Commission's modifications to the ratemaking system necessary to achieve the objectives.

¹⁷² Congress, when modifying the retirement-related liabilities in the PAEA could have specified how any specific funds escrowed under the prior system would be utilized, but it did not do so.

Unlike the pre-PAEA ratemaking system, the current ratemaking system does not provide specific amounts of revenue to cover specific costs. Whether or not it was anticipated that the revenue raised under the current ratemaking system would be adequate to pay any particular cost is not relevant. The Commission has found the targeted retirement costs to be a driver of the Postal Service's inability to achieve net income, and it is therefore reasonable for the Commission's modifications to the current ratemaking system to address those costs.

Objections that the retirement-based rate authority does not cap the amount of additional rate authority. NPPC *et al.* object to the retirement-based rate authority on the grounds that it is excessive, fluctuates between years, and is not subject to any cap. NPPC *et al.* Comments at 42, 48. They state that a substantial drop in revenue would increase the amount of the retirement-based rate authority. *Id.* at 42.

It is only during the phase-in period that the retirement-based rate authority fluctuates, and it fluctuates only to the extent necessary to ensure that the Postal Service receives (as nearly as practicable) the full amount of rate authority at the end of the five years. While it is true that a substantial drop in Postal Service volume during the phase-in period would increase the amount of the retirement-based rate authority (in percentage terms) available in the remainder of the period, it is a trade-off that occurs due to protecting mailers by including a phase-in period. The Postal Service's obligation is denominated in dollars, and recovering the same amount of dollars from fewer pieces would require more rate authority per piece. After the phase-in period, mailers are no longer exposed to additional retirement-based rate authority under this rule.

Objections to the remittance requirement for the retirement-based rate authority. The Postal Service argues that requiring revenue collected under the retirement-based rate authority to be remitted towards its retirement liabilities prevents the Postal Service

from improving its liquidity and usurps the business discretion of Postal Service management. Postal Service Comments at 21.

The Public Representative agrees that remittance should not be required, stating that due to induced volume decline, the Postal Service would have no incentive to use the retirement-based rate authority. PR Comments at 32.

The purpose of the retirement-based rate authority is to improve the Postal Service's ability to achieve net income by making payments towards its unfunded liability, not to improve the Postal Service's liquidity. The remittance requirement helps prevent the retirement-based rate authority from imposing an undue burden on Market Dominant mailers by ensuring that the revenue raised under that authority actually goes towards paying down the Postal Service's unfunded liabilities. The retirement-based rate authority is a tool the Postal Service may use to raise revenue to remit towards its statutorily mandated payments, but the decision whether or not to make use of that authority to adjust rates remains within the business discretion of the Postal Service.

Comments on the formula for calculating the amount of revenue actually collected under the retirement-based rate authority. The Public Representative states that the Commission does not demonstrate or explain how the actual amount of additional revenue resulting from the retirement-based rate authority will be calculated. PR Comments at 25.

The Postal Service claims that the additional rate authority provided by Formula V-1 does not generate sufficient revenue to cover the remittance required under Formula V-3 because the formulas do not take into account induced volume decline.¹⁷³

¹⁷³ See Postal Service Comments at 22 and Appendix A at 1. The Postal Service's comments and Appendix refer to these as Formulas IV-1 and IV-3, consistent with how they were identified in Order No. 5337. In this document, they are identified as Formulas V-1 and V-3.

The Commission disagrees with the Postal Service's conclusion that the retirement-based rate authority provided by Formula V-1 does not generate sufficient revenue to cover the minimum required remittance.¹⁷⁴ The formula for calculating the amount of revenue generated by the retirement-based rate authority (and thus amount of the required remittance) is calculated by Formula V-3. This formula calculates the fraction of the previous year's rate base caused by all prior uses of retirement-based rate authority, and multiplies the fraction by the actual revenue of the previous year. Any induced volume decline caused by the higher rates will reduce the actual revenue used in the calculation of the required remittance.

The amount of revenue collected as a result of the retirement-based rate authority may be less than originally anticipated when the amount of retirement-based rate authority was calculated. However, during years 2 through 5 of the phase-in period, the formula accounts for the difference between the initial and subsequent revenue when determining the amount of retirement-based rate authority available in the next year. After the phase-in period ends, future declines in volume may continue to reduce the amount of revenue raised by the retirement-based rate authority, but the Postal Service will continue to only be required (for purposes of the retirement-based authority) to remit the amount collected.

The Postal Service suggests that instead of calculating the fraction of the rate base resulting from use of the retirement-based rate authority and then multiplying by actual revenue, the Commission should calculate the amount of revenue raised by this authority by estimating the amount of revenue the Postal Service hypothetically would

¹⁷⁴ The Commission notes that the minimum remittance requirement operates only in the context of the Postal Service's eligibility to receive the retirement-based rate authority. The Postal Service's statutory obligation to remit the full invoiced amount to OPM is not subject to Commission modification.

have raised absent the additional authority, and subtracting that estimate from actual revenue.¹⁷⁵

An estimate of the hypothetical revenue the Postal Service would have raised absent the retirement-based rate authority would be a counterfactual approximation necessarily involving the price-elasticity of Market Dominant mail, and a complex iterative process not unlike that applied in pre-PAEA rate cases where the Commission would design rates to achieve a break-even revenue target. The Postal Service uses its own estimates in the technical appendix attached to its comments, which show wildly varying elasticities among different classes of Market Dominant mail, and among products within each class. See Postal Service Comments, Excel file “USPS 2020 RRA workbook,” tab “Elasticity” (Technical Appendix). The Postal Service uses a volume-weighted average elasticity in the examples supporting its alternative proposal.

Any reliable estimate of the amount of revenue that hypothetically would have been raised absent the additional rate authority would require a class-by-class (and potentially a product-by-product) comparison of the amount of rate authority used to the price-elasticity of that class or product. Additionally, the Postal Service’s proposed volume-weighted average does not account for complexity introduced by interactions between price and volume across different products (cross-price elasticities), where a price change for one product may affect the volume of another product. Even if these additional complexities were to be taken into account, the reliability of the estimate would depend entirely on the accuracy of the estimates for price-elasticities.

¹⁷⁵ Postal Service Comments at 20; see Postal Service Comments, Technical Appendix. The Postal Service alternatively suggests revising the amount of the retirement-based rate authority to reflect the anticipated difference between actual revenue and the estimate of revenue absent the additional authority. See Postal Service Comments, Technical Appendix.

In addition, while the Postal Service's analysis of potential counterfactual scenarios include examples that incorporate density-based rate authority resulting from volume declines induced by retirement-based rate authority, these scenarios do not include an estimate of this additional revenue after the final year of the phase-in period.¹⁷⁶ Because of the lagged effect of induced volume losses, additional density-based rate authority would occur after the phase-in of retirement-based rate authority. More significantly, the Postal Service's scenarios also do not include any estimates of the effect that induced volume losses would have on the costs of the Postal Service. If retirement-based rate authority results in fewer pieces of mail being sent, then the attributable cost of the mail that is not sent would not be incurred. When considering the offsetting revenue effects of the density-based rate authority and the cost reductions that would accompany such loss of volume, the Commission finds that the Postal Service's proposals to alter the retirement-based rate authority or the required remittance risk increasing net revenue by more than the payments it is designed to fund, to the detriment of users of Market Dominant products.

The Commission declines to adopt the Postal Service's alternative methodology. If the Postal Service wishes to rely on its own internal estimates of elasticity when deciding whether or not to make use of the retirement-based rate authority, the Governors retain that authority.

3. Objections Concerning Removal of Retirement-Based Rate Authority

Objections that the retirement-based rate authority should instead be implemented as a surcharge. ACMA recommends that the retirement-based rate

¹⁷⁶ See Postal Service Comments; Appendix A; and Excel file "USPS 2020 RRA workbook.xlsx."

authority be implemented as a surcharge that can be easily removed when Congress acts. ACMA Comments at 3-4.

In the event that the Commission later determines that the retirement-based rate authority should be removed from the rate base, the rate base can be reduced by the percentage specified in Formula V-2. This is identical in effect to removing a surcharge, and avoids the possibility of an indefinite surcharge in the event that Congress does not act.

Comments on clawing back the retirement-based rate authority after forfeiture. NPPC *et al.* argue that there should be an automatic claw-back if the Postal Service fails to make the required remittance to OPM. NPPC *et al.* Comments at 48.

The Public Representative recommends that the Commission clarify whether forfeiture is immediate or would occur only after further Commission review. PR Comments at 33.

In the event that the Postal Service fails to make the required remittance to OPM, the Commission anticipates that the determination of whether or not to claw-back the existing retirement-based rate authority will be heavily fact-dependent. Rather than try to predict all possible scenarios and decide in advance which should trigger an automatic claw-back provision, the Commission will instead make a determination based on the facts at hand in the unlikely event that the Postal Service avails itself of the retirement-based rate authority and fails to comply with its requirements.

D. Conclusion

Having considered the comments received on its proposal in Order No. 5337, the Commission concludes that the retirement-based rate authority will be an effective tool for raising additional revenue toward the targeted retirement amortization payments,

which the Commission has identified as one of the primary drivers of the Postal Service's net loss.

The Commission therefore implements the retirement-based rate authority as proposed in Order No. 5337, with a clarification as discussed in Section XII.C.2.¹⁷⁷

¹⁷⁷ As discussed in that section, the requirement that the retirement-based rate authority be used in the first rate increase after it is available is clarified to exclude limited price changes that affect only one or two generally applicable price cells.

VI. PERFORMANCE-BASED RATE AUTHORITY

A. Introduction

The existing Market Dominant ratemaking system was unable to assure financial stability (including retaining earnings), maximize incentives to reduce costs and increase efficiency, and maintain service standards. See Order No. 4257 at 3-5, 274-275. In an effort to address these deficiencies, the Commission proposed to make available up to 1 percentage point of rate authority per class of mail per calendar year, conditioned on the Postal Service meeting or exceeding an operational efficiency-based standard and adhering to service standard quality criteria. See Order No. 4258 at 120. The Commission initially divided this 1 percentage point of performance-based rate authority between operational efficiency (0.75 percentage points), and service standards (0.25 percentage points). See *id.* The operational efficiency portion would be allocated if the average annual TFP growth over the most recent 5 years met or exceeded 0.606 percent. See *id.* The service standards portion would be allocated if all of the service standards (including the applicable business rules) for that class during the applicable year met or exceeded the service standards in place during the prior fiscal year on a nationwide or substantially nationwide basis. See *id.* at 120-121.

After consideration of the comments, the Commission simplified its approach in two ways. See Order No. 5337 at 149-150. First, rather than assign independent weights for operational efficiency and service standards, the Commission made the entire 1 percentage point of performance-based rate authority contingent on meeting both requirements. See *id.* at 149. Second, the Commission revised the TFP target: the Postal Service's TFP for the measured fiscal year must exceed the previous fiscal year to meet the operational efficiency-based requirement. See *id.* at 150.

The following discussion summarizes the comments received concerning the Commission's revised approach, provides analysis, and describes the resulting changes made to the proposed rules.

B. Comments

1. Overview

Multiple commenters oppose finalization of the rules relating to the performance-based rate authority.¹⁷⁸ In the alternative, some of these commenters suggest revisions to certain aspects of the final rules relating to the performance-based rate authority.¹⁷⁹ The Berkshire Company supports the finalization of the rules related

¹⁷⁸ See, e.g., ABA Comments at 13; ACI Comments at 3; ACMA Comments at 3; AF&PA Comments at 5-6; ANM *et al.* Comments at 61; Discover Comments at 1; eBay Comments at 4-5; Meredith Corporation Comments at 2; Mailers Hub at 5-8; NMA Comments at 8-9, 12; NPPC *et al.* Comments at 51-52, 78-79; NTU Comments at 2; PR Comments at 39-40; SBE Council Comments at 2.

Additionally, ANM *et al.* filed three declarations in support of their comments recommending that the Commission withdraw the rules relating to the performance-based rate authority. Expert Declaration of Robert D. Willig, PhD, In Support of Comments of the Alliance of Nonprofit Mailers, The Association for Postal Commerce, MPA - The Association of Magazine Media, The American Catalog Mailers Association, The Nonprofit Alliance, The Direct Marketing Association of Washington, The Envelope Manufacturers Association, and The Saturation Mailers Coalition, February 3, 2020, at ¶ 7 (Willig Decl.) (opining that the performance-based rate authority is “highly inconsistent with price cap theory,” “poorly designed,” “vulnerable to gainful counterproductive manipulation and fails to incentivize the Postal Service to maximize its productivity.”); Expert Declaration of Kevin Neels and Nicholas Powers, February 3, 2020, at ¶¶ 55, 62 (Brattle Decl.) (opining that the performance-based rate authority is inconsistent with the traditional theory of price cap regulation and that the financial health justification put forth by the Commission is significantly flawed); Declaration of Robert Fisher: TFP Accuracy for Performance-based Rate Authority, February 3, 2020, at 2 (Fisher Decl.) (opining that “TFP is not a valid or accurate operational efficiency-based measurement for performance-based rate authority as currently configured”).

Further, multiple commenters reiterate their opposition to the performance-based rate authority in their reply comments. See, e.g., ABA Reply Comments at 1-2, 6-7; ANM *et al.* Reply Comments at 1-3, 25-29; ACMA Reply Comments at 2-4; NPPC *et al.* Reply Comments at 33-39; PR Reply Comments at 34. One commenter made its first filing, expressing its opposition to all forms of additional rate authority through its reply comments. C21 Reply Comments at 1-2, 5-7.

¹⁷⁹ See, e.g., ABA Comments at 14 (suggesting to change: (1) the operational efficiency-based requirement to actual net productivity improvements since inception of the performance-based rate authority; and (2) the service standard-based requirement to actual service performance); ABA Reply Comments at 7 (same); AF&PA Comments at 5-6 (suggesting to develop: (1) a mechanism to validate that Postal Service management has fully leveraged all available tools to address cost and service issues prior to providing performance-based rate authority; (2) empirical criteria to define “efficiency” and “service;” and (3) a mechanism that would incentivize the Postal Service to align institutional costs with expected volume declines); ANM *et al.* Comments at 64-65, 82 (suggesting to change: (1) the amount of performance-based rate authority to correspond with future Postal Service capital needs; and (2) the performance-based rate authority to an “X-factor”); Meredith Corporation Comments at 2 (suggesting that any performance-based rate authority “must be tied to achieving future efficiencies that are not just

to the performance-based rate authority. Berkshire Co. Comments at 1. While generally supporting the provision of additional rate authority to the Postal Service to fund capital investments, APWU, NAPS, NPMHU, and the Postal Service suggest revising the performance-based rate authority rules to increase the likelihood that some amount of performance-based rate authority would be provided to the Postal Service.¹⁸⁰

marginal and are demonstrated through multi-year trends.”); Mailers Hub Comments at 8 (suggesting that “[i]f the [C]ommission finds that service performance is lagging because the Postal Service’s financial position inhibits it from doing what’s necessary to achieve expected performance, the [C]ommission has the latitude to authorize reductions in services to align reasonable operating costs to *available* revenue.”) (emphasis in original); NMA Comments at 12 (suggesting that the final workshare discount regulations and the Postal Service’s ongoing cost cutting initiatives be given time to improve the situation prior to providing additional rate authority); NPPC *et al.* Comments at 59-71 (suggesting to: (1) change the operational efficiency-based requirement to actual net productivity improvements since inception of the performance-based rate authority; (2) reduce rate authority for failure to achieve either operational efficiency-based or service standard-based requirement; (3) sunset the performance-based rate authority after 5 years; (4) change the service standard-based requirement to actual service performance; and (5) create a transparent and public process for review of Postal Service changes to its business rules); NPPC *et al.* Reply Comments at 12-13, nn.26-27 (suggesting that the Commission exert increased authority over the Postal Service’s cost reduction and investment decisions); NTU Comments at 2 (suggesting to ensure that the Postal Service is thoroughly measuring performance before establishing performance parameters); PR Comments at 40-45 (suggesting to change: (1) the amount of performance-based rate authority to correspond with future Postal Service capital needs; and (2) the operational efficiency-based requirement to multi-year TFP growth).

¹⁸⁰ APWU Comments at 5-12 (suggesting to replace the operational efficiency-based requirement with a capital investment plan and increase the amount of performance-based rate authority above 1 percentage point per annum); NAPS Comments at 2 (supporting the performance-based rate authority in principle as a “postage-for-performance” incentive mechanism but asserting that it “falls short”); NPMHU Comments at 1, 3-4 (supporting the performance-based rate authority but suggesting to independently allocate some amount for achieving the service standard-based requirement); Postal Service Comments at 29-31, 40 n.24 (suggesting to: (1) provide performance-based rate authority unconditionally for a period of time; (2) adjust the service standard-based requirement; (3) provide 0.25 percentage points of performance-based rate authority for independent achievement of the adjusted service standard-based requirement; or (4) provide partial credit for slowing the rate of TFP decline); Postal Service Reply Comments at 34-42 (reiterating suggestion to provide performance-based rate authority unconditionally for a period of time); see Postal Service Reply Comments, Appendix A, Declaration of A. Thomas Bozzo and Mark E. Meitzen, Christensen Associates, March 4, 2020, at 17 (Christensen Decl.) (opining that providing “a limited (but unconditional) amount of revenue towards a capital funding goal would be a more appropriate method than a TFP-linked price cap component.”).

In the reply comments, some participants expressly oppose¹⁸¹ the suggestions of other commenters.

2. Incentive Regulation

Asserting that the performance-based rate authority is unnecessary, inconsistent with, and/or in conflict with the theoretical principles of incentive regulation, multiple commenters urge the Commission to withdraw the performance-based rate authority.¹⁸²

With respect to concerns of theoretical necessity, ABA, ANM *et al.*, and Meredith Corporation assert that the performance-based rate authority unnecessarily duplicates the existing price cap mechanism's inherent incentive to increase efficiency and reduce costs.¹⁸³ ABA, ANM *et al.*, and NPPC *et al.* contend that the existing system richly rewards the Postal Service for gains in TFP and that it is unexplained why giving an

¹⁸¹ ABA Reply Comments at 6-7 (opposing the suggestions of the Postal Service and the unions to provide additional rate authority to fund investments that are necessary to improve efficiency and service, and opposing the Postal Service's suggestion to provide performance-based rate authority unconditionally); ANM *et al.* Reply Comments at 27-29 (opposing the Postal Service's suggestion to provide performance-based rate authority unconditionally for 5 years); ACMA Reply Comments at 2-4 (opposing APWU's suggestion to replace the operational efficiency-based requirement with a capital investment plan); C21 Reply Comments at 2, 5 (opposing the suggestions of the Postal Service, Public Representative, and the unions to provide additional rate authority in any form); NPPC *et al.* Reply Comments at 33-39 (opposing the Postal Service's suggestions to: (1) provide performance-based rate authority unconditionally for a period of time; (2) adjust the service standard-based requirement; (3) provide 0.25 percentage points of performance-based rate authority for independent achievement of the adjusted service standard-based requirement; or (4) provide partial credit for slowing the rate of TFP decline); Postal Service Reply Comments at 37-41 (opposing ANM *et al.*'s suggestion to transform the performance-based rate authority to an "X-factor" and the suggestions by ABA and NPPC *et al.* to change the operational efficiency-based requirement to actual net productivity improvements since inception of the performance-based rate authority).

¹⁸² See ABA Comments at 2, 13; ABA Reply Comments at 6-7; AF&PA Comments at 6; ANM *et al.* Comments at 61-68; ANM *et al.* Reply Comments at 25-29; Discover Comments at 15-16; Meredith Corporation Comments at 2; NMA Comments at 8-9, 12; NPPC *et al.* Comments at 51-52, 55; NPPC *et al.* Reply Comments at 35-36, 47-48.

¹⁸³ See ABA Comments at 2, 13; ABA Reply Comments at 6; ANM *et al.* Comments at 61 (citing Willig Decl. at ¶ 27 (opining that "the extra [reward of] 1percent of pricing authority [for any incremental improvement in productivity] 'is largely redundant and unnecessary.'")); ANM *et al.* Reply Comments at 28; Meredith Corporation Comments at 2.

additional reward through the performance-based rate authority would increase efficiency.¹⁸⁴

With respect to concerns of theoretical consistency, ANM *et al.* assert that the performance-based rate authority “does not similarly provide an ‘economically efficient connection between productivity gains, their financial benefits, and the cost of the investments needed to accomplish them’” and therefore there is no basis to conclude that the Postal Service will respond appropriately to it. ANM *et al.* Comments at 68 (quoting Willig Decl. at ¶ 32). ANM *et al.* contend that mailers would be better off if Postal Service productivity declined by 0.1 percent so that mailers could avoid the additional 1-percentage-point increase.¹⁸⁵ AF&PA contends that the performance-based rate authority is inconsistent with theory because there is no business model where a firm’s cost control and efficiency measures translate into an ability to charge customers more. AF&PA Comments at 6.

With respect to concerns of theoretical contradictions, NMA and NPPC *et al.* assert that implementing the performance-based rate authority would be contrary to theory because it would weaken the Postal Service’s existing incentive to reduce costs and increase efficiency.¹⁸⁶

The Public Representative agrees with these commenters that the observed deficiencies are not due to a lack of incentive and maintains that the performance-based

¹⁸⁴ See ABA Reply Comments at 6; ANM *et al.* Comments at 64, 68 (citing Brattle Decl. ¶ 56 (opining that “[i]f the Postal Service has failed to respond to [these inherent cost savings] incentives [under the current] price cap [system,] ... it is not clear why the Postal Service needs an additional reward in order to motivate it to reduce costs,”) or why it can be expected to respond to additional incentives beyond those it already faces.; NPPC *et al.* Comments at 55; NPPC *et al.* Reply Comments at 35-36.

¹⁸⁵ ANM *et al.* Comments at 62 (citing Willig Decl. at ¶ 27; Brattle Decl. ¶¶ 55, 59); see Willig Decl. ¶ 7 (opining that the performance-based rate authority is “highly inconsistent with price cap theory,” “poorly designed,” “vulnerable to gainful counterproductive manipulation and fails to incentivize the Postal Service to maximize its productivity.”); Brattle Decl. ¶¶ 55, 59, 61 (opining that the performance-based rate authority is inconsistent with the traditional theory of price cap regulation).

¹⁸⁶ See NMA Comments at 9; NPPC *et al.* Comments at 12; NPPC *et al.* Reply Comments at 36.

rate authority should be withdrawn. PR Comments at 39-42. He asserts that due to long-standing financial duress, the Postal Service has operated under significant incentives to increase efficiency and does not require additional incentives to operate efficiently. *Id.* at 41. He adds that any incentives created by the performance-based rate authority will be inadequate to induce improvement, until the Postal Service achieves financial health. *Id.* at 42. Similarly, the Postal Service asserts that the Commission's analysis established that the underinvestment problem is due to insufficient capital rather than insufficient incentive. Postal Service Comments at 39.

3. Amount of Rate Authority

a. Method to Derive the Amount

The Public Representative, ANM *et al.*, and NPPC *et al.* disagree with the Commission's usage of historic capital investment data as reference points to derive the proposed amount of the performance-based rate authority (1 percentage point per annum).¹⁸⁷ The Public Representative asserts that this amount is not adequately justified because there has been no demonstration that returning net asset holdings to FY 2006 levels is the appropriate target and that 5 years is the appropriate time span to reach that target.¹⁸⁸ Additionally, NPPC *et al.* assert that the pre-PAEA level of capital investment is the improper starting point because the price cap system was intended to reduce the level of capital investment compared to the cost-of-service system and past examples of capital investment, such as the Flats Sequencing System (FSS), do not indicate that greater capital investment would improve performance. NPPC *et al.* Comments at 53-54. The Public Representative and NPPC *et al.* contend that the

¹⁸⁷ See PR Comments at 40-41; ANM *et al.* Comments at 64-65; NPPC *et al.* Comments at 54-55.

¹⁸⁸ PR Comments at 40; Initial Comments of the Public Representative, Refiled March 7, 2018, at 31 (2018 PR Comments).

Commission must explain how it analyzed the reference points to derive the amount of 1 percentage point per annum.¹⁸⁹

The Public Representative and ANM *et al.* suggest that the amount of any performance-based rate authority be based on future Postal Service capital investment needs.¹⁹⁰ Similarly, NPPC *et al.* assert that the Commission incorrectly disclaims any effort to determine how much capital the Postal Service actually needs or review the Postal Service's capital investment decisions going forward.¹⁹¹ By contrast, the Postal Service opposes the Commission making any projections or assumptions concerning the Postal Service's future capital expenditures, claiming that doing so would risk unduly influencing the Postal Service's business discretion as to its capital deployment. Postal Service Comments at 37.

b. Necessity of the Amount

ABA, ACMA, Discover, and NPPC *et al.* argue that the performance-based rate authority is unnecessary to generate revenue and fund investments that would improve the Postal Service's financial health.¹⁹² ABA urges the Commission to "reject the arguments...that additional rate authority is necessary in advance to make the investments necessary to improve efficiency and service." ABA Reply Comments at 6 (footnote omitted). ACMA contends that the performance-based rate authority is

¹⁸⁹ See PR Comments at 41; NPPC *et al.* Comments at 54 (quoting Order No. 5337 at 122).

¹⁹⁰ PR Comments at 41; ANM *et al.* Comments at 64-65 (citing Willig Decl. at ¶ 30); ANM *et al.* Reply Comments at 26.

¹⁹¹ NPPC *et al.* Comments at 54 (citing Order No. 5337 at 121); *id.* at 54 n.60 (citing Order No. 5337 at 122).

¹⁹² See ABA Reply Comments at 6; ACMA Comments at 3; ACMA Reply Comments at 2-3; Discover Comments at 6, 15; see also NPPC *et al.* Reply Comments at 34-35.

unnecessary to fund capital investment because the Postal Service can borrow the funds. ACMA Comments at 3; ACMA Reply Comments at 2-3.

Similarly, NPPC *et al.* assert that the Postal Service has ample cash-on-hand and available borrowing authority to fund investments and that a lack of retained earnings is insufficient to establish that additional rate authority is needed to fund investment. NPPC *et al.* Reply Comments at 34-35. They emphasize that the Postal Service had \$8.9 billion in cash on hand and \$4 billion in borrowing authority at the end of FY 2019.¹⁹³ Additionally, they echo their prior position that the performance-based rate authority is premised on the misconception that the Postal Service is entitled to retained earnings.¹⁹⁴

Discover asserts that the justification for the performance-based rate authority is flawed because it relies on the unexplained assumption that a lack of capital investment has diminished service and/or volume and fails to identify any capital investments that would reduce costs, improve service, or increase volume. Discover Comments at 6, 15. Discover contends that the lack of capital investment is not a cause of the Postal Service's problems. *Id.* at 15. Further, Discover asserts that the justification for the performance-based rate authority is flawed because the Commission fails to address rising costs other than retirement obligations and actions the Postal Service can take to reduce costs under the existing system. *Id.* Discover asserts that the Commission fails

¹⁹³ NPPC *et al.* Comments at 53 (citing Docket No. ACR2019, Library Reference USPS-FY19-17, December 27, 2019, at 11). The actual cash on hand figure reported by the Postal Service is \$8.795 billion. Docket No. ACR2019, United States Postal Service *FY 2019 Annual Report to Congress*, December 27, 2019, at 11 (*FY 2019 Annual Report*), Library Reference USPS-FY19-17, December 27, 2019.

¹⁹⁴ Compare NPPC *et al.* Comments at 52-53, with Comments of the National Postal Policy Council, the Major Mailers Association, and the National Association of Presort Mailers, March 1, 2018, at 49-83 (2018 NPPC *et al.* Comments).

to consider if the Postal Service can reenter the financial health cycle under the existing system. *Id.* at 6.

Additionally, some commenters assert that the amount of the performance-based rate authority is too large.¹⁹⁵ NPPC *et al.* suggest that the Commission allow the performance-based rate authority to sunset at the 5-year review, rather than allow performance-based rate authority to be generated during the 5-year review. NPPC *et al.* Comments at 61. Similarly, ANM *et al.* assert that granting the performance-based rate authority in perpetuity runs counter to the Commission's theory that the performance-based rate authority is needed only until the Postal Service has reentered the financial health cycle. ANM *et al.* Comments at 68-69; see Brattle Decl. ¶ 64 (opining that "the liquidity problem identified by the Commission is only a temporary constraint created by the fact that the Postal Service has reached its borrowing limit" and "any additional rate authority awarded to address liquidity constraints need only be temporary"). NPPC *et al.* and eBay assert that the performance-based rate authority is flawed because prior usage is incorporated into the rate base and compounded. See NPPC *et al.* Comments at 12; eBay Comments at 5.

c. Sufficiency of the Amount

By contrast, other commenters assert that the amount of the performance-based rate authority is insufficient.¹⁹⁶ APWU asserts that the performance-based rate authority may not provide sufficient additional rate authority to return the Postal Service to the pre-PAEA level of capital investment. APWU Comments at 10. Additionally, APWU asserts that the pre-PAEA level of capital investment may not be the right level for the

¹⁹⁵ See ANM *et al.* Comments at 68-69; eBay Comments at 5; NPPC *et al.* Comments at 12, 61.

¹⁹⁶ See APWU Comments at 10-12; NAPS Comments at 2; PR Comments at 45-46; Postal Service Comments at 34.

future.¹⁹⁷ APWU opposes the 1-percentage-point limitation on the annual amount of the performance-based rate authority and argues that rate authority should be provided to raise revenues needed for the Postal Service's capital investment plan. APWU Comments at 12. NAPS characterizes the performance-based rate authority, even when combined with the other forms of rate authority, as insufficient to restore and maintain the financial integrity of the Postal Service. NAPS Comments at 2. The Public Representative asserts that the Postal Service's immediate capital needs remain unaddressed because the performance-based rate authority is designed "to put the Postal Service 'on the path to long-term stability'" and will not provide sufficient revenue to fund investment capital until the revenue accumulates for years. PR Comments at 46 (quoting Order No. 4258 at 53). He adds that the other forms of rate authority are aimed to address medium-term financial stability, which as defined by the Commission, also do not address immediate capital needs. *Id.* at 45-46. Similarly, the Postal Service contends that the other forms of rate authority are insufficient to generate retained earnings. Postal Service Comments at 34.

d. Potential Negative Effects

Multiple commenters assert that the performance-based rate authority would fail to allow the Postal Service to reenter the financial health cycle.¹⁹⁸ NPPC *et al.* express doubt that performance-based rate authority would allow the Postal Service to reenter the financial health cycle because they disagree that more revenue would lead to increased efficiency via wise investing. NPPC *et al.* Comments at 55. Additionally, they assert that history has shown that increased revenue can worsen TFP and past Postal

¹⁹⁷ APWU Comments at 10-11; see ACMA Reply Comments at 2 (agreeing with APWU on this point but disagreeing regarding the provision of additional rate authority to fund capital investments).

¹⁹⁸ NPPC *et al.* Comments at 55, 59-60; ANM *et al.* Comments at 66-69; PR Comments at 39-46; Postal Service Reply Comments at 34; APWU Comments at 5-6.

Service investments such as the FSS have not fulfilled their alleged promise of increased efficiency. *Id.* at 12, 55, 59-60.

APWU, ANM *et al.*, the Public Representative, and the Postal Service assert that the performance-based rate authority would fail to allow the Postal Service to reenter the financial health cycle based on their contention that any lack of funding for productivity-enhancing investments would not be addressed because the provision of the performance-based rate authority is contingent on the realization of productivity gains first.¹⁹⁹ As detailed below, while each of these commenters characterize this as a flaw, they recommend different regulatory approaches.

APWU asserts that “the requirement of positive TFP growth to get the performance-based rate authority puts the cart before the horse”. APWU Comments at 5-6. APWU recommends that the Commission replace the TFP achievement requirement with a capital investment plan requirement. *Id.* at 5-11. ACMA opposes this recommendation and argues that the Postal Service should use its borrowing authority to make essential investments with a likely payoff. ACMA Reply Comments at 2-3.

ANM *et al.* contend that “the explanation offered by the Commission for why costs have not fallen more—namely, that the Postal Service has not been able to generate the needed investment funds—would not be addressed by this [performance-based rate authority] proposal.” ANM *et al.* Comments at 69; see Brattle Decl. ¶ 66 (opining that “the Commission’s proposal would not by itself enable the Postal Service ‘to reenter the financial health cycle.’ Instead, it would only reward the Postal Service once it had managed to get there on its own.”). ANM *et al.* recommend that the performance-based rate authority be withdrawn, reiterating their position that the

¹⁹⁹ ANM *et al.* Comments at 69; PR Comments at 46; Postal Service Reply Comments at 34; APWU Comments at 5-6.

performance-based rate authority relies on the unexplained assumption that a lack of capital investment has resulted in the Postal Service being unable to restrain cost increases. ANM *et al.* Comments at 66-67; see Brattle Decl. ¶¶ 62 (opining that the financial health justification put forth by the Commission is significantly flawed). Additionally, ANM *et al.* assert that the Commission fails to explain how capital investment(s) would impact efficiency and volume. ANM *et al.* Comments at 67; see Brattle Decl. ¶¶ 63 (opining that “[t]he Commission fails to demonstrate that productivity improvements by the Postal Service have been hindered by a shortage of funds for productivity enhancing investments”). ANM *et al.* further express concern regarding the lack of any after-the-fact oversight to confirm that the revenue generated by the performance-based rate authority is used to fund productivity-enhancing investments. ANM *et al.* Comments at 68.

Arguing that designing the performance-based rate authority to function over the long term will frustrate its intent, the Public Representative also recommends withdrawing the performance-based rate authority. PR Comments at 39-40. He contends that the performance-based rate authority will not provide sufficient revenue to fund investment capital until after years of accumulation. *Id.* at 46. He asserts that the performance-based rate authority is misdirected at the symptoms of the Postal Service’s past revenue shortfalls rather than the causes, which he identifies as the exogenous costs of the health benefit and pension funds requirements. *Id.* at 39; 2018 PR Comments at 31.

The Postal Service asserts that “[t]here is agreement that conditioning additional rate authority on productivity gains (the ‘earn it first’ approach) is irreconcilable with the Commission’s stated rationale of providing additional liquidity in order to invest in productivity gains (the ‘financial-health cycle’ rationale).” Postal Service Reply Comments at 34 (emphasis omitted). Instead, the Postal Service recommends that the

performance-based rate authority be provided unconditionally until the 5-year review or until an activation point to be determined through a separate proceeding.²⁰⁰

Multiple commenters oppose this recommendation by the Postal Service.²⁰¹ Urging the Commission to “reject the Postal Service’s proposal to further dilute” the performance-based rate authority, ABA characterizes the Postal Service’s objection that conditioning additional rate authority on the Postal Service’s performance impermissibly infringes on operational decision-making as “meritless.” ABA Reply Comments at 7 (citing Postal Service Comments at 30). ANM *et al.* characterize several of the Postal Service’s remarks as “grous[ing] that the Commission’s proposal will make it harder for the Postal Service to *reduce* its service standards”²⁰² and assert that the Postal Service’s statements demonstrate that it will continue to reduce its service standards without stricter regulation. See ANM *et al.* Reply Comments at 26-27 (quoting Postal Service Comments at 30-31, 43). Additionally, ANM *et al.* characterize several of the Postal Service’s remarks as “mak[ing] clear that [the Postal Service] has become wholly uninterested in even feigning interest in a system that achieves Objective 1”²⁰³ and assert that the Postal Service’s statements demonstrate that it will not make operational decisions that would improve productivity in response to the performance-based rate authority. See ANM *et al.* Reply Comments at 27-28 (quoting Postal Service Comments at 32). NPPC *et al.* contend that the Postal Service contradicts itself by claiming that it needs unconditional revenue upfront to improve productivity and service quality and

²⁰⁰ See *id.* at 34-42; Postal Service Comments at 3; see also Christensen Decl. at 17 (opining that “[i]mplementing a K-factor to provide a limited (but unconditional) amount of revenue towards a capital funding goal would be a more appropriate method than a TFP-linked price cap component.”).

²⁰¹ See ABA Reply Comments at 7; ANM *et al.* Reply Comments at 26-29; NPPC *et al.* Reply Comments at 33-39.

²⁰² ANM *et al.* Reply Comments at 26 (citing Postal Service Comments at 30) (emphasis in original).

²⁰³ ANM *et al.* Reply Comments at 27.

also claiming that it does not need a price cap to incentivize cost reductions and efficiency improvements. See NPPC *et al.* Reply Comments at 34 (citing Postal Service Comments at 33, 56).

ABA, Discover, ACI, and Meredith Corporation assert that the provision of the performance-based rate authority to the Postal Service will negatively affect the system in various ways.²⁰⁴ ABA questions whether the Postal Service will actually use the revenue generated from the performance-based rate authority to increase efficiency and reduce costs. ABA Comments at 7-8. ABA adds that without the Postal Service making meaningful cost reductions and efficiency improvements, the additional revenues will only give the appearance of stability and may actually be counterproductive over the long term. *Id.* Similarly, Discover asserts that the Commission fails to provide evidence to suggest that additional revenues would fund adequate capital investment to improve efficiency and service. Discover Comments at 6. ACI contends that provision of the performance-based rate authority would create rewards for the Postal Service “that invite further pricing distortions.” ACI Comments at 3. Meredith Corporation asserts that the performance-based rate authority would reward the Postal Service for engaging in behavior that fails to adjust costs to economic realities. Meredith Corporation Comments at 2.

4. Operation of the Rate Authority Adjustment Mechanism

a. Progressive (Upward Adjusting) Mechanism

Multiple commenters assert that the performance-based rate authority is flawed because the incentive mechanism is entirely progressive—providing an upward

²⁰⁴ ABA Comments at 7-8; ACI Comments at 3; Discover Comments at 6; Meredith Corporation Comments at 2.

adjustment to rate authority that is incorporated into the rate base—rather than partially or entirely regressive—providing a downward adjustment to rate authority.²⁰⁵

AF&PA characterize the proposed mechanism as improperly rewarding the Postal Service and penalizing mail users. AF&PA Comments at 6. NPPC *et al.* contend that the performance-based rate authority is counterproductive and arbitrary because the adjustments to rate authority are upward only, the failure to meet either the operational efficiency-based or service standard-based requirement merely results in the inability to be eligible for the performance-based rate authority for 1 year, and prior usage of rate authority is incorporated into the rate base. See NPPC *et al.* Comments at 12-13.

ANM *et al.*, eBay, and NPPC *et al.* suggest revising the performance-based rate authority to adjust rate authority downward. ANM *et al.* suggest replacing the performance-based rate authority with a downward adjusting productivity offset referred to as an “X-factor.” See ANM *et al.* Comments at 81-82 (citing Brattle Decl. at ¶ 71). The Postal Service opposes this suggestion. Postal Service Reply Comments at 37-40. eBay asserts that the Commission errs by declining to reduce the available rate authority if efficiency or service decreases. eBay Comments at 5. NPPC *et al.* suggest that performance-based rate authority provided in prior years should be rescinded if TFP falls below the base year level or if service standards are reduced. NPPC *et al.* Comments at 59, 68.

b. Split Between Operational Efficiency and Service Standard-Based Requirements

Commenters express differing views on whether the achievement of the operational efficiency and service standard-based requirements should be linked to a

²⁰⁵ See AF&PA Comments at 6; ANM *et al.* Comments at 82; eBay Comments at 5; NPPC *et al.* Comments at 12-13, 59, 68.

single amount of rate authority as proposed in Order No. 5337 or to separate amounts of rate authority as proposed in Order No. 4258.

The Postal Service and NPMHU support Order No. 4258's initial proposal to provide 0.25 percentage points for achievement of the service standard-based requirement and 0.75 percentage points for achievement of the operational efficiency-based requirement.²⁰⁶ The Postal Service asserts that the service standard-based requirement "would impose an unwarranted gloss on Objective 3." Postal Service Comments at 31. The Postal Service argues that Order No. 4258's initial proposal is preferable because it would minimize the Commission's exercise of what the Postal Service characterizes as "unprecedented and undue influence over decisions that Congress expressly delegated to the Postal Service" under 39 U.S.C. § 3691. *Id.* at 30. Additionally, the Postal Service suggests that the Commission allow the performance-based rate authority to be earned for each class of mail for which service standards have not changed. *Id.* at 62.

By contrast, the Public Representative and NPPC *et al.* support Order No. 5337's revision to require the Postal Service to achieve both the operational efficiency-based requirement and the service standard-based requirement to be eligible for the entire 1 percentage point of performance-based rate authority. PR Comments at 42; NPPC *et al.* Comments at 52. NPPC *et al.* assert that "[t]he Postal Service overstates its argument" regarding 39 U.S.C. § 3691 and that this provision does not prohibit the Commission's proposed service standard-based requirement. NPPC *et al.* Reply Comments at 38. Additionally, NPPC *et al.* object to the Postal Service's suggestion to allow the performance-based rate authority to be earned for each class of mail for which service standards have not changed, asserting that doing so would create perverse

²⁰⁶ See Postal Service Comments at 29-31; NPMHU Comments at 1, 4; see also Christensen Decl. at 18 (opining that "the separate component of the authority for maintaining service standards is arguably closer to regulatory practice than the combined authority proposed in Order No. 5337.").

incentives to devote Postal Service managerial attention to a certain class at the expense of others. *Id.* at 39.

5. Operational Efficiency-Based Requirement

a. Use of TFP as the Benchmark

Multiple commenters oppose using TFP as the benchmark for measuring the achievement of the operational efficiency-based requirement.²⁰⁷

ABA characterizes the other comments as “confirm[ing] that total factor productivity is a flawed metric” (ABA Reply Comments at 6) and states that “[n]o party supports using total factor productivity.” *Id.* at 7 (citing Postal Service Comments at 39; Fisher Decl. at [31]). ACMA asserts that TFP is too weak an indicator to guide adjustments to the price cap. ACMA Comments at 3. AF&PA suggests developing empirical criteria to define “efficiency” to evaluate its achievement objectively. AF&PA Comments at 6. AF&PA suggests developing a mechanism to incentivize the Postal Service to align institutional costs with expected volume declines. *Id.* Stating that TFP growth can be affected by rapid volume decline, lack of capital expenditure, or when the Postal Service commits a lot of resources to fix a problem, APWU asserts that TFP growth is a flawed benchmark. APWU Comments at 6. APWU recommends that the Commission continue to address the issues surrounding TFP in other proceedings. *Id.* at 11. eBay asserts that the accuracy of TFP is debatable and can significantly vary. eBay Comments at 4.

ANM *et al.* assert that TFP is inaccurate for three primary reasons and overstates growth by about 1 percent per year from FY 2015 to FY 2018. ANM *et al.* Comments

²⁰⁷ ABA Reply Comments at 6-7; ACMA Comments at 3; AF&PA Comments at 6-7; ANM *et al.* Comments at 8, 76-81; APWU Comments at 6; eBay Comments at 6; NPPC *et al.* Comments at 56; NPPC *et al.* Reply Comments at 36-37; Postal Service Comments at 39-40; Postal Service Reply Comments at 35.

at 7-8, 76; see Fisher Decl. at 2 (opining that “TFP is not a valid or accurate operational efficiency-based measurement for performance-based rate authority as currently configured”). First, ANM *et al.* assert that TFP can produce “false positive” results in which TFP increases, but productivity has not. ANM *et al.* Comments at 76 (citing Fisher Decl. at 2). ANM *et al.* attribute this inaccuracy to the inclusion of inappropriate factors and issues with the component values used to calculate TFP. ANM *et al.* Comments at 76-79 (citing Fisher Decl. at 2, 4, 8, 14, 18-19, 21). Second, ANM *et al.* assert that TFP is not transparent and cannot be independently validated. ANM *et al.* Comments at 76, 79-80 (citing Fisher Decl. at 2, 26, 28; Brattle Decl. at ¶¶ 68, 70). Third, ANM *et al.* assert that TFP’s use of inputs that are beyond the control of the Postal Service renders it inappropriate to use as a basis for providing the performance-based rate authority. ANM *et al.* Comments at 76, 80-81 (citing Fisher Decl. at 2, 13, 31).

The Postal Service characterizes the comments received by the Commission as demonstrating agreement that “TFP is not a suitably precise metric on which to base a consequential award of rate authority.”²⁰⁸ The Postal Service asserts that productivity is an inappropriate and atypical requirement for performance-based rate authority. Postal Service Comments at 39. The Postal Service claims that TFP is too comprehensive, such that it detracts from its appropriateness to use as a measure. *Id.* Claiming that most performance-based rate authority benchmarks are specific (such as safety, service, or reliability-based), the Postal Service asserts that TFP is sensitive to exogenous factors (such as business cycles and net trends) and endogenous factors that are unrelated to operational performance (such as efficiency gains unrelated to capital expenditures, and capital expenditures unrelated to operations). *Id.*

²⁰⁸ Postal Service Reply Comments at 35 (citing ACMA Comments at 3; ANM *et al.* Comments at 76-81; APWU Comments at 6-7; eBay Comments at 4; Postal Service Comments at 38-40).

NPPC *et al.* agree with the Postal Service that TFP should not be used as a benchmark for providing performance-based rate authority. NPPC *et al.* Reply Comments at 36-37. NPPC *et al.* assert that “[a] review of the comments indicates that almost no one thinks that the TFP criterion is either appropriate or likely to have the desired effect.” *Id.* at 12 n.25. NPPC *et al.* question whether adding the TFP criterion and related reporting requirements would be consistent with Objective 6. NPPC *et al.* Comments at 20. NPPC *et al.* assert that TFP is an imperfect indicator because it does not account directly for changes in factor input prices and therefore excessive inflation in factor input prices (including wages) can increase TFP without costs decreasing. NPPC *et al.* Comments at 56; 2018 NPPC *et al.* Comments at 73. Asserting that using TFP as the benchmark incentivizes the Postal Service to shift costs to mailers, such as by imposing mail preparation requirements, NPPC *et al.* assert that the Commission must monitor the Postal Service pushing uncompensated costs on mailers.²⁰⁹ NPPC *et al.* support using a controllable cost approach rather than TFP as a benchmark. NPPC *et al.* Comments at 57 n.64 (citing 2018 NPPC *et al.* Comments at 73). Observing that cost problems with Periodicals and flat-shaped mail remain unresolved and that labor costs remain above 75 percent of total postal costs and have risen as volume fell, NPPC *et al.* urge the Commission to exert increased authority over the Postal Service’s cost-reduction and investment decisions. NPPC *et al.* Reply Comments at 12-13 nn.26-27.

²⁰⁹ NPPC *et al.* Comments at 56 (citing United States Postal Service, Office of the Inspector General, Report No. MS-AR-11-006, Effects of Compliance Rules on Mailers, August 24, 2011, available at: <https://www.uspsaig.gov/sites/default/files/document-library-files/2015/MS-AR-11-006.pdf> (MS-AR-11-006)); 2018 NPPC *et al.* Comments at 73.

b. Year-Over-Year Growth as the Target

Multiple commenters oppose setting the performance target for achievement of the operational efficiency-based requirement as exceeding the prior fiscal year's TFP.²¹⁰

APWU, the Public Representative, the Postal Service, and NPPC *et al.* raise concerns that year-to-year changes in TFP growth would not produce useful information regarding whether the Postal Service is actually maximizing efficiency.²¹¹ APWU and the Public Representative assert that year-over-year TFP growth is an inappropriate target because of the lag between expenditure and realization of productivity gains. APWU Comments at 10; PR Comments at 42-43. Similarly, the Postal Service asserts that efficiency improving investments affect TFP with variable and long lags. Postal Service Comments at 40. The Postal Service claims that a Postal Service response to a recession would not be fully reflected in TFP until recovery boosts workload. *Id.* NPPC *et al.* agree with the Postal Service that year-to-year changes in TFP growth are not particularly informative. NPPC *et al.* Comments at 57 (citing Docket No. ACR2019, Library Reference USPS-FY19-17 (*FY 2019 Annual Report*)); 2018 NPPC *et al.* Comments at 73.

ABA, ACI, Meredith Corporation, the Postal Service, and eBay argue that this target would send incorrect signals and/or create perverse incentives.²¹² ABA asserts that using this target would allow the Postal Service to be eligible for the performance-based rate authority “even if its net productivity declined over the 5-year period.” ABA Comments at 13. ACI asserts that the target would discourage maximization of Market

²¹⁰ ABA Comments at 14; ACI Comments at 3; ANM *et al.* Comments at 65-75; APWU Comments at 10; eBay Comments at 4; Meredith Corporation Comments at 2; NPPC *et al.* Comments at 57-59; Postal Service Comments at 40; PR Comments at 39-46.

²¹¹ See APWU Comments at 10; PR Comments at 42-43; Postal Service Comments at 40; NPPC *et al.* Comments at 57.

²¹² ABA Comments at 14; ACI Comments at 3; eBay Comments at 4; Meredith Corporation Comments at 2; Postal Service Comments at 40.

Dominant productivity. ACI Comments at 3. Meredith Corporation asserts that this target allows for “easy manipulation of year-over-year productivity comparisons” in order to be eligible for the performance-based rate authority. Meredith Corporation Comments at 2. The Postal Service asserts that the proposed target of year-over-year TFP growth would be inconsistent with the goal of maximizing efficiency incentives and would perversely incentivize the Postal Service to spread TFP gains over multiple years. Postal Service Comments at 40. eBay objects to the year-over-year TFP growth target, characterizing it as awarding the Postal Service with extra rate authority for doing “virtually nothing.” eBay Comments at 4.

Similarly, ANM *et al.* oppose using year-over-year TFP growth as the target, asserting that this target would be too low and would create incorrect incentives. ANM *et al.* Comments at 65-75. ANM *et al.* assert that the targets underlying the performance-based rate authority are set so low as to effectively authorize the provision of the 1 percent such that “[t]he ‘performance-based’ incentive is a misnomer.” *Id.* at 69. Comparing the year-over-year TFP growth target with TFP growth over different historical periods (average annual TFP growth was 0.72 percent from 1990 through 2006, and 0.75 percent from 2007 through 2015), ANM *et al.* assert that the operational efficiency-based requirement would result in the Postal Service reaping a reward for TFP growth below these historical levels. *Id.* at 70-71 n.24.

ANM *et al.* argue that the target creates an incentive for counterproductive manipulation, to spread TFP gains over multiple years and thereby obtain the performance-based rate authority for multiple years. *Id.* at 65-66, 72-75; Willis Decl. ¶¶ 27-29; Brattle Decl. ¶¶ 59-61, 67. ANM *et al.* hypothesize that in a situation where the Postal Service is near the target, it might make a capital investment that would boost TFP in the short term (to reach the target) but that would be inefficient in the long term. ANM *et al.* Comments at 75 (citing Brattle Decl. ¶ 67). Observing that the performance-based rate authority does not differentiate between changes in TFP, other

than an increase over the prior fiscal year, ANM *et al.* assert that the operational efficiency-based requirement would incentivize the Postal Service to aim for low positive TFP growth contrary to Objective 1. ANM *et al.* Comments at 70-71. ANM *et al.* assert that mailers would be better off if Postal Service productivity declined by 0.1 percent so that mailers could avoid the additional 1-percentage-point increase. *Id.* at 62 (citing Willig Decl. at ¶ 27). ANM *et al.* assert that the performance-based rate authority “does not similarly provide an ‘economically efficient connection between productivity gains, their financial benefits, and the cost of the investments needed to accomplish them’” and therefore there is no basis to conclude that the Postal Service will respond appropriately to the proposal. ANM *et al.* Comments at 68 (quoting Willig Decl. at ¶ 32).

c. Potential Alternative Target: Tiers of Achievement

The Postal Service and NPPC *et al.* debate the merits of introducing tiers of rewards. Postal Service Comments at 40; NPPC *et al.* Reply Comments at 37. The Postal Service contends that using year-over-year TFP growth as the target is flawed because the Postal Service would not receive any partial credit for controlling negative growth better than expected nor additional credit for exceeding the target. Postal Service Comments at 40. The Postal Service observes that record evidence concerning trends affecting TFP growth, the Postal Service’s operational efficiency opportunities, and historic results tend to suggest that year-over-year TFP growth is an overly ambitious target.²¹³ NPPC *et al.* oppose the Postal Service’s suggestion to provide partial credit for decreasing TFP results that are not as low as expected and express concern that doing so would allow for manipulation by the Postal Service’s

²¹³ Postal Service Reply Comments at 40-41 (citing Northwest Postal Consulting (NWPC) for the Postal Regulatory Commission, Report 2, Comparison of Postal Service Productivity Measurement: Before and After PAEA Enactment, March 27, 2017, at 8-11 (NWPC Report 2); see Comments of the United States Postal Service, March 20, 2017, Appendix C (A&M Cost Report); United States Postal Service, USPS Annual Tables, FY 2019 TFP (Total Factor Productivity), February 27, 2020, Excel file “Table Annual 2019 Public.xlsx,” tab “Tfp-52,” column K).

management given the lack of transparency into “expectations.” NPPC *et al.* Reply Comments at 37.

d. Potential Alternative Target: Multi-Year Growth

ABA, Meredith Corporation, NPPC *et al.*, and the Public Representative suggest changing the target to reflect multi-year trends of efficiency increases rather than year-to-year TFP growth,²¹⁴ to which the Postal Service objects. Postal Service Comments at 31-32.

While ABA and Meredith Corporation urge the Commission to withdraw the performance-based rate authority, they assert that a shift to actual net improvement in productivity since inception of the new authority would represent an improvement over the target proposed in Order No. 5337.²¹⁵ Similarly, while NPPC *et al.* and the Public Representative recommend that the Commission decline to adopt the performance-based rate authority, in the alternative, they prefer Order No. 4258’s proposal to use the 5-year rolling average as the target instead of the year-over-year target proposed in Order No. 5337. NPPC *et al.* Comments at 51-52, 57-59; PR Comments at 39-42.

Reviewing the past history of TFP growth from FY 2013 through FY 2019, NPPC *et al.* assert that the target proposed in Order No. 5337 would allow the Postal Service to earn performance-based rate authority in the early year(s) and keep those gains as baked into the rate base, but then lose all of those TFP gains in later year(s). NPPC *et al.* Comments at 57. Therefore, NPPC *et al.* suggest that performance-based rate authority should not be provided unless TFP is cumulatively higher than when the new system is put into place. *Id.* at 59. NPPC *et al.* suggest using the 5-year rolling average

²¹⁴ See ABA Comments at 14; ABA Reply Comments at 7; Meredith Corporation Comments at 2; NPPC *et al.* Comments at 57; PR Comments at 39-46.

²¹⁵ ABA Comments at 14; ABA Reply Comments at 7; Meredith Corporation Comments at 2.

for the TFP target, on an interim basis until a better metric is developed. *Id.* at 51-52, 57.

The Public Representative asserts that Order No. 5337's proposal to use a year-over-year target for TFP growth is inferior to Order No. 4258's proposal to use a 5-year rolling average method because TFP is designed to function over a lengthy period. PR Comments at 39-40. He states that the year-over-year target does not take into account the lag between productivity growth and innovations or short-term operating decisions. *Id.* at 42-43. He adds that year-over-year TFP growth is less reliable than the multi-year rolling average method because year-over-year growth may vary substantially and uses fewer data points. *Id.* at 43. Therefore, he suggests allowing a significantly longer period of 7 to 8 years to measure TFP growth. *Id.* He asserts that the Commission acknowledges these deficiencies and fails to adequately rebut them. *Id.* at 43-44 (quoting Order No. 5337 at 135). He asserts that although the year-over-year method may be marginally more straightforward than the multi-year rolling average method, the Commission's contention that the year-over-year method renders annual operational performance to be more visible does not justify its use over the multi-year rolling average method. *Id.* at 44. He asserts that visibility into annual operational performance can be obtained through reporting requirements; however, a multi-year lookback is needed to produce reliable measurement incentives for longer-term capital investments. *Id.* at 44-45. Overall, he asserts the change to the year-over-year method accounts for short-term productivity improvements rather than measuring efficiency. *Id.* at 45. Further, he hypothesizes that if the Postal Service generates revenue from the performance-based rate authority in the short-term, then the Postal Service might use the revenue to make longer-term capital investments that subsequently lower TFP for future years. *Id.* at 46.

The Postal Service opposes using multi-year TFP growth as the target, asserting that it is irrational to reward or punish the Postal Service based on TFP growth prior to the implementation of the rule. Postal Service Comments at 32.

6. Service Standard-Based Requirement

ACMA, AF&PA, Mailers Hub, NMA, and the Public Representative object to the requirement that the Postal Service meet or exceed the service standards in place during the prior fiscal year.²¹⁶ ACMA cautions that maintaining the Universal Service Obligation as volume continues to decline will lead to costs rising to prohibitive levels and eventual network collapse. ACMA Comments at 1. AF&PA suggests developing empirical criteria to define “service” to evaluate its achievement objectively. AF&PA Comments at 6. Mailers Hub opposes providing additional rate authority to incentivize the Postal Service to consistently achieve its service standards and asserts that the performance-based rate authority implies that the existing regulatory tools are insufficient to yield that result. Mailers Hub Comments at 8. Mailers Hub asserts that if the Commission finds that service performance is declining because the Postal Service’s financial challenges inhibit it from taking the actions necessary to achieve the expected performance, the Commission should authorize reductions in service that would align operating costs with available revenue. *Id.* NMA characterizes the performance-based rate authority as a reward for the Postal Service not officially reducing published standards. NMA Comments at 8-9. The Public Representative asserts that the performance-based rate authority is misdirected at the symptoms of service problems rather than the causes, which he identifies as inadequate

²¹⁶ ACMA Comments at 1; AF&PA Comments at 6; Mailers Hub Comments at 8; NMA Comments at 8-9; PR Comments at 41.

capitalization. PR Comments at 41-42 (citing 2018 PR Comments at 36 (quoting Kwoka and Wilson Decl. at 15)).

Opposing the service standard-based requirement,²¹⁷ the Postal Service suggests that any diminution of service standards trigger a qualitative evaluation of:

(1) whether the reduced service standards remain of 'high quality' for purposes of Objective 3; and (2) if the new service standards are not 'high quality,' whether the change, on balance, nonetheless furthers other Section 3622 criteria (e.g., reducing costs and increasing efficiency (Objective 1)) that outweigh the impact on Objective 3.

Postal Service Comments at 43. NPPC *et al.* object and characterize the Postal Service as "seek[ing] to weaken [Order No. 5337's] already inadequate proposal [even] more." NPPC *et al.* Reply Comments at 38 (citing Postal Service Comments at 42-43).

ABA, eBay, and NPPC *et al.* suggest incorporating service performance achievement into the service standard-based requirement.²¹⁸ ABA asserts that providing performance-based authority even if the Postal Service fails to meet its published service standards is arbitrary and capricious. ABA Reply Comments at 7; ABA Comments at 14. eBay asserts that maintaining service standards without evaluating achievement lacks value. eBay Comments at 4. NPPC *et al.* suggest that the Commission base the provision and reduction of performance-based rate authority on the achievement of service standards (service performance results). NPPC *et al.* Comments at 62-65. NPPC *et al.* assert that not linking the provision of performance-based rate authority with service performance results fails to achieve Objective 3 and take into account Factors 1, 4, and 9. *Id.* at 12, 63-64. NPPC *et al.* assert that the annual compliance review process has been and will continue to be insufficient to

²¹⁷ As summarized, Section VI.B.4.b., *supra*, the Postal Service provides suggestions that would affect the amount of rate authority earned or foregone by achievement such as: reducing the amount of rate authority earned by the achievement of this requirement (see Postal Service Comments at 30-31) and allowing rate authority to be earned on a class-by-class basis (see *id.* at 62).

²¹⁸ See, e.g., ABA Comments at 14; ABA Reply Comments at 7; eBay Comments at 4; NPPC *et al.* Comments at 62-66.

address declining service and that a rate authority consequence must be imposed. *Id.* at 65-66.

NPPC *et al.* and the Postal Service debate the merits of introducing reporting requirements associated with changes to service standards. *Id.* at 12, 69-71; Postal Service Comments at 42. NPPC *et al.* support the inclusion of changes in the business rules as part of the evaluation of whether the service standards have been maintained and state that the Commission should have a process to assess such changes transparently so that mailers may evaluate such changes. NPPC *et al.* Comments at 12, 69-71. By contrast, asserting that the changes to the service standards are already transparent, the Postal Service argues that the certification requirement is an unnecessary administrative burden. Postal Service Comments at 42.

C. Commission Analysis of Comments

1. Overview

The Commission appreciates the commenters' efforts in preparing their critiques of the performance-based rate authority. Upon consideration of the comments received, the Commission declines to implement the proposed rules relating to performance-based rate authority at this time and will defer consideration of the related issues to a new rulemaking docket.

The existing Market Dominant ratemaking system did not achieve the PAEA's objectives during the 10 years following the PAEA's enactment. See Order No. 4257 at 3-5, 274-275. The Commission's findings were premised on the existing ratemaking system's inability to assure financial stability (including retaining earnings), maximize incentives to reduce costs and increase efficiency, and maintain service standards. See *id.* at 3-5, 274-275. During the PAEA era, the existing ratemaking system was

inadequate, which resulted in an accumulated deficit,²¹⁹ maximum use of the Postal Service's borrowing authority and a sharp decline in capital investments,²²⁰ operational efficiency increases and cost reductions that were insufficient to achieve overall financial stability and/or retained earnings,²²¹ and reduction of the high quality service standards that were set in 2007. Order No. 4257 at 273.

The Commission's approach to designing a system that meets the PAEA's objectives in conjunction with each other is to make principled adjustments to the existing ratemaking system. The Commission makes principled adjustments to the existing price cap that targets two underlying drivers of the Postal Service's net losses that are largely outside of its direct control: (1) the increase in per-unit cost resulting from the decline in mail density for each fiscal year under final subpart D of 39 C.F.R. part 3030; and (2) the statutorily mandated amortization payments for particular retirement costs under final subpart E of 39 C.F.R. part 3030. This allows the Postal Service the opportunity to capture revenue to address these two underlying drivers of the Postal Service's near-term financial distress.

The Commission also provides additional rate authority of 2 percentage points per fiscal year for each non-compensatory class of mail and defines rate-setting criteria for non-compensatory products in classes for which overall class revenue exceeds overall class attributable cost under final subpart G of 39 C.F.R. part 3030. The additional 2 percentage points of rate authority made available for non-compensatory

²¹⁹ See *id.* at 171-172 (describing how the consecutive net losses resulted in an accumulated deficit).

²²⁰ The Postal Service lacks shareholders and instead must finance capital investments through revenue or through borrowing. Order No. 4258 at 48-49. Therefore, as consecutive years of net losses resulted in an accumulated deficit, the Postal Service relied heavily on its borrowing authority, deferred capital investments, and increased its cash reserves. See *id.* at 46-52.

²²¹ Order No. 4257 at 222, 274-275 (summarizing that while some cost reductions and efficiency gains were achieved post-PAEA, they were insufficient to achieve financial stability in the medium term and long term).

classes is aimed at narrowing the cost coverage gap over time and is not projected to produce positive returns within 5 years. See Order No. 5337 at 168-170. By taking an incremental approach to addressing these long-standing issues, the final rules are designed to ensure that the ratemaking system would not incentivize the Postal Service to *solely* raise rates to address non-compensatory classes and products.

In addition to providing new forms of rate authority and introducing rate-setting criteria, the Commission finalizes two other types of regulations. One type is directly aimed at maximizing the Postal Service's incentives to increase pricing efficiency, and the other type is designed to increase transparency into the Postal Service's efforts to increase efficiency and reduce costs. To address the inefficient pricing practices observed during the PAEA era, the Commission enhances its regulation of workshare discounts under final subpart J of 39 C.F.R. part 3030. To monitor the effects of all of the finalized regulatory changes, particularly with respect to planned and realized cost reductions, the Commission codifies additional reporting requirements in final 39 C.F.R. § 3050.55.

Based on the record in this proceeding, the Commission finds that it is neither necessary nor prudent to implement the proposed rules relating to performance-based rate authority at this juncture. The performance-based rate authority proposal was designed to maximize the incentives to increase efficiency and reduce costs while maintaining service standards by introducing a performance incentive mechanism.²²² Because the final rules adopted in this Order, which are directly aimed at preventing the

²²² Performance-based regulation is a broad concept referring to a regulatory system that applies incentives to promote targeted behavior by the regulated entity. See William Zarakas, A New Face for PBR: Aligning Incentives in the Electric Utility System, PUB. UTILS. FORT., December 2017 (Zarakas), available at: <https://www.fortnightly.com/fortnightly/2017/12/new-face-pbr?authkey=e0a4230ee85eb602f123c1e633c0e5b5260f9bd3f297c094c055e7868e5a4589>. More specifically, a performance incentive mechanism (PIM), also referred to as a targeted performance incentive (TPI), is used by regulators to set a target for acceptable performance by the regulated entity for a specific area and attach a financial incentive to ensure compliance. See *id.*

Postal Service from succumbing to its near-term financial challenges, contain numerous safeguards in their design,²²³ the Commission acknowledges that implementation of the performance-based rate authority proposal is not an immediate need. Moreover, as numerous commenters have highlighted potential issues with the design and implementation of the performance-based rate authority, further careful deliberation on whether, when, and how to introduce a performance incentive mechanism is warranted.

The aim of the Commission's approach in removing the performance-based rate authority from the final rules is to realign the existing system in a balanced, measured manner. To ensure that this realignment occurs and the objectives remain properly balanced until the next system review in 5 years or earlier if necessary, the Commission will initiate a separate rulemaking to consider a number of issues—most particularly the exact nature of what additional adjustments (if any) would be beneficial to the system's achievement of Objectives 1, 3, and 5.²²⁴ The following considerations lead the Commission to decline to implement the performance-based rate authority at this time and defer consideration of related issues to a new rulemaking docket.

²²³ Particular discussion of how each of the three new forms of rate adjustment authority (the density rate authority, retirement obligation rate authority, and non-compensatory rate authority) are designed to account for such concerns appears in Section XIII.E.1., *infra*. Particular discussion of the nature and extent of the financial instability of the Postal Service appears in Section XIII.E.5., *infra*. Particular discussion of how the modified rate system is designed to enable the Postal Service to set rates that would be "just and reasonable"—neither a threat to the Postal Service's financial integrity nor excessive to ratepayers—appears in Section XIII E.8., *infra*.

²²⁴ The discussion of the performance-based authority in prior orders and in this Order focuses on the most direct impacts regarding issues encapsulated under Objectives 1, 3, and 5. This focus should not be viewed as implying that the Commission is unaware of, or unconcerned with, the other objectives appearing in the PAEA. See NPPC *et al.* Comments at 10. The Commission remains cognizant of the need to balance all nine objectives with respect to the design of the ratemaking system. To promote clarity, the Commission provides a summary in Chapter XIII., *infra*, organized by objective, of how finalizing the other changes, and declining to finalize the performance-based rate authority at this time, are necessary to achieve the objectives of 39 U.S.C. § 3622(b) in conjunction with each other. Any changes that may be undertaken in the new rulemaking docket will also consider all of the objectives in conjunction with each other.

The final rules, even without the performance-based rate authority, introduce numerous changes to the existing ratemaking system simultaneously. These changes include the introduction of three new forms of rate adjustment authority that would allow the Postal Service to raise rates in excess of the existing annual limitation (the annual percentage change in the CPI-U). The deficiencies of the existing system are complex and necessarily require complex solutions that act in concert with each other. To mitigate against potential shocks and unintended consequences of introducing multiple complex changes simultaneously, the Commission finds it is prudent to tailor the focus of the final rules implemented at this time.²²⁵

Moreover, the Commission determines that it should exercise particular caution in introducing performance-based rate authority to the existing ratemaking system. As proposed in Order No. 5337, the performance-based rate authority interconnects complex, longer-term challenges concerning finances, operational efficiency, cost reductions, and service. While the theoretical literature and experiences of other regulators relating to incentive regulation may not exactly correspond to the Postal Service,²²⁶ these sources tend to confirm that designing incentive based rate authority

²²⁵ See, e.g., NPPC *et al.* Comments at 14 (“Given these many moving parts, it would be prudent for the Commission to move incrementally.”).

²²⁶ For instance, the Postal Service is unique in that it is a government agency and therefore “...has no shareholders and may not invest in stocks, bonds, or other financial instruments.” Order No. 4258 at 48. Additionally, the Postal Service’s borrowing capacity is restrained. See Order No. 4257 at 33 (describing the \$15 billion limitation on borrowing imposed by 39 U.S.C. § 2005); Order No. 4258 at 49 (describing the Postal Service’s use of its borrowing authority post-PAEA); FY 2019 Financial Analysis at 36 (explaining that as of FY 2019, the Postal Service has \$4 billion in available borrowing authority.). Therefore, unlike private companies, the Postal Service must finance capital investments through revenue or using its nearly exhausted borrowing authority. See Order No. 4258 at 48-49.

should be done cautiously as implementing incentive regulation is complicated and may have unintended consequences.²²⁷ Moreover, as reflected above, multiple commenters in this docket also have raised practical concerns with implementing the proposed versions of performance-based rate authority. Upon consideration of the record in this

²²⁷ See Synapse Energy Economics, Inc., Melissa Whited, Tim Woolf, & Alice Napoleon, *Utility Performance Incentive Mechanisms: A Handbook for Regulators*, Prepared for the Western Interstate Energy Board, March 9, 2015, at 13, available at: https://www.synapse-energy.com/sites/default/files/Utility%20Performance%20Incentive%20Mechanisms%2014-098_0.pdf, (describing the difficulties of establishing the right productivity factor when there are few comparable peer operators, the operator needs to replace aging infrastructure, the operator or the industry is in a period of rapid transition, and historical costs and practices are not a good indication of what future costs and practices will be); *id.* at 53-56 (describing potential pitfalls when designing performance incentive mechanisms such as providing disproportionate rewards or penalties, unintended consequences, regulatory burden, uncertainty, and gaming and manipulation by the regulated entity); Paul L. Joskow, *Incentive Regulation and its Application to Electricity Networks*, *Review of Network Economics* Vol. 7, Issue 4, at 547, 554 (Dec. 2008) (2008 Joskow), available at: https://siliconflatirons.org/documents/initiatives/IRLEdaythree/Joskow_Incentive_Regulation.pdf, (“... the implementation of price cap mechanisms is more complicated and their efficiency properties more difficult to evaluate than is often implied and places a significant information collection, auditing and analysis burden on regulators.”); Paul L. Joskow, *Incentive Regulation in Theory & Practice: Electricity Distribution & Transmission Networks*, January 21, 2006, at 8-9 (2006 Joskow), available at: <https://economics.mit.edu/files/1181>, (“Some mechanisms can provide both good pricing and performance (cost, quality) incentives, but typically, the desire to get prices as well as performance incentives right creates another constraint that moves us further from first-best outcomes.”); General Oversight of the U.S. Postal Service: Hearings Before the Subcomm. on the Postal Service of the H. Comm. on Gov’t Reform, 105th Cong. 33-51 (1997) (statement of John E. Kwoka, Jr., Professor of Economics, George Washington University) (Kwoka Congressional Testimony) (opining that caution should be exercised in adjusting for past performance and describing other regulators’ efforts to correct for errors in prior productivity calculations); Peter Navarro, *The Simple Analytics of Performance-Based Ratemaking: A Guide for the PBR Regulator*, 13 *Yale J. on Reg.* 105, 109 (1996) (Navarro), available at: <https://core.ac.uk/download/pdf/72838797.pdf> (“...PBR is neither good nor bad--but that application, design, and implementation make it so. We shall also argue that PBR is sufficiently flawed as a concept that would-be reformers should approach it with far less zeal and much more caution than is now being exhibited in many quarters.”); Navarro at 110 (“...*a poorly designed PBR experiment can actually make the economic situation worse.*”) (emphasis in original); Navarro at 125-144 (describing the potential pitfalls of setting the amount of revenue at stake too high or too low, the tradeoffs involved in selecting a progressive versus regressive mechanism for incentivizing efficiency gains and cost savings, and the difficulties in establishing a mechanism to link cost savings with maintaining quality); *Ass’n of Oil Pipe Lines v. FERC*, 83 F.3d 1424, 1437 (D.C. Cir. 1996) (*Oil Pipelines I*) (upholding the Federal Energy Regulatory Commission’s price cap regulation for oil pipelines despite the lack of a productivity offset); *Time Warner Entertainment Co. v. FCC*, 56 F.3d 151, 173 (D.C. Cir. 1995) (upholding the Federal Communication Commission’s price cap regulation for cable television despite the lack of a productivity offset).

proceeding, the Commission finds that it should engage in additional study before deciding whether, when, or how to introduce performance-based rate authority into the ratemaking system.

While multiple system designs could potentially satisfy the objectives of the PAEA in conjunction with each other, the Commission aims to produce a balanced system. In balancing the tradeoffs, the Commission finds that it is reasonable to focus on near-term issues first.²²⁸ The performance-based rate authority is aimed at addressing longer-term challenges. See Order No. 5337 at 114-116; Order No. 4258 at 38-39, 53. While 39 U.S.C. § 3622(d)(3) requires that the Commission engage in rulemaking, subject to notice and opportunity for public comment, it also allows the Commission broad discretion with regard to determining which (if any), how, and when any regulatory changes may be adopted to achieve the objectives, in conjunction with each other.²²⁹ In determining the timing or schedule of how to address the many challenges faced by the Postal Service, the Commission finds it prudent to address immediate term pricing and uncontrollable cost issues first and then consider the potential impact of imposing additional adjustments to the price cap that would further incentivize efficiency, cost reductions, and maintenance of service standards. While the

²²⁸ See *City of Las Vegas v. Lujan*, 891 F.2d 927, 935 (D.C. Cir. 1989) (“Since agencies have great discretion to treat a problem partially, we would not strike down the listing if it were a first step toward a complete solution”); *Nat’l Ass’n of Broads. v. FCC*, 740 F.2d 1190, 1210 (D.C. Cir. 1984) (“We have therefore recognized the reasonableness of the Commission’s decision to engage in incremental rulemaking and to defer resolution of issues raised in a rulemaking even when those issues are ‘related’ to the main ones being considered.”).

²²⁹ See 39 U.S.C. § 3622(d)(3); see also NPPC *et al.* Reply Comments at 16 (“That the Commission ‘may’ modify the system to better achieve the Objectives does not mean that it *must* make changes.” (emphasis in original)); *Env’tl. Integrity Project v. McCarthy*, 139 F. Supp. 3d 25, (D.D.C. 2015) (withdrawing a proposed rule after a notice and comment period is subject to a more deferential standard of judicial review than a decision to issue a new rule or rescind an existing rule “because a decision that ‘alters the regulatory status quo’ requires ‘more persuasive justification than does the decision to retain an existing rule’ and “must also be guided by appropriate deference to an agency’s discretion to set the ‘timing and priorities of its regulatory agenda.’”) (quoting *Williams Nat’l Gas Co. v. FERC*, 872 F.2d 438, 443 (D.C. Cir. 1989) and *WildEarth Guardians v. EPA*, 751 F.3d 649, 651 (D.C. Cir. 2014)).

Commission could opt to finalize such issues in a single rulemaking, the PAEA does not require it. Moreover, given the issues that require refinement, prudence counsels against it. Therefore, at this juncture, the Commission adopts a cautious approach with respect to adding a direct financial incentive (such as the addition of 1 percentage point of performance-based rate authority) contingent on year-over-year TFP growth and maintenance of existing service standards. This approach is further reinforced by the comments filed in this proceeding expressing widespread opposition to finalizing the performance-based rate authority as proposed at this time²³⁰ and urging the Commission to conduct additional study prior to implementing this or another type of proposal.²³¹

The Commission acknowledges that stakeholders may have concerns related to timing and certainty. Notice and comment rulemaking allows an agency, after consideration of comments, to choose to adopt or withdraw its proposals.²³² While implementing the additional 1 percentage point of performance-based rate authority now would provide more certainty, reasoned decision-making also requires the Commission to ensure that any changes to the existing ratemaking system are

²³⁰ See n.177, *supra*; see also ANM *et al.* Reply Comments at 29 (“More generally, however, the initial comments to Order No. 5337 show that even commenters with widely divergent opinions uniformly agree that the Commission’s performance-based rate authority cannot stand and should not be enacted”); NPPC *et al.* Reply Comments at 36 (“The Commission should acknowledge that almost no one supports the *Revised NPRM*’s proposed use of TFP as a partial basis for additional ‘service performance’ rate authority.”); Postal Service Reply Comments at 34 (“Despite some unfounded criticisms, there is remarkable consensus that the proposed performance-based rate authority is problematic”).

²³¹ See AF&PA Comments at 5-6 (suggesting to develop a mechanism to validate that Postal Service management has fully leveraged all available tools to address cost and service issues prior to providing performance-based rate authority); APWU Comments at 11 (suggesting that the Commission continue to address the issues surrounding TFP in other proceedings); NMA Comments at 12 (suggesting that the final workshare discount regulations and the Postal Service’s ongoing cost cutting initiatives be given time to improve the situation prior to providing additional rate authority); NTU Comments at 2 (suggesting to ensure that the Postal Service is thoroughly measuring performance before establishing performance parameters).

²³² See *Long Island Care at Home, Ltd. v. Coke*, 551 U.S. 158, 175 (2007).

measured. At this juncture, withdrawing the rules relating to the performance-based rate authority and deferring these issues for further study represents the best procedural method to ensure that any changes that the Commission implements to the existing ratemaking system are measured. Doing so is also consistent with the Administrative Procedure Act, which requires the Commission to address significant public comments.²³³

The Commission finds that further study would produce useful information concerning a number of issues, including many raised in the comments. Because the Commission remains committed to exploring ways to enhance the regulatory system to promote longer-term financial stability, increased efficiency and cost reductions, while maintaining high quality service standards, the Commission intends to initiate a new rulemaking in the coming months. The Commission also commits to conducting such a proceeding via a notice and comment rulemaking to ensure that sufficient notice and opportunity for comment is given to all stakeholders.

2. Areas for Further Refinement in the New Rulemaking

The comments received in this docket have been instructive in highlighting key areas for additional study that will be analyzed in the new rulemaking, such as what amount(s) of rate authority(ies) should be put at stake (if any), and what benchmark(s) and incentive mechanism(s) should be used to incentivize desired behavior(s).

The Commission acknowledges that further analysis would be particularly helpful to determine whether additional incentives should be added to further enhance the ratemaking system. Multiple commenters express concerns that additional incentives may be unneeded and suggest differing regulatory approaches: stricter limitations on

²³³ See *U.S. Postal Serv. v. Postal Reg. Comm'n*, 963 F.3d 137, 141 (D.C. Cir. 2020) (citing *Int'l Fabricare Inst. v. EPA*, 972 F.2d 384, 389 (D.C. Cir. 1992)).

rate increases to promote discipline by the Postal Service in containing costs²³⁴ versus fewer limitations on rate increases to generate additional revenue to fund the Postal Service's operating needs and capital investments.²³⁵ The Commission wishes to further explore whether connecting direct financial consequences with efficiency gains, cost reductions, and maintained service standards would benefit the ratemaking system, and if so, how to best design these potential measures.

Numerous commenters express concerns regarding the method used to approximate the amount of the financial incentive.²³⁶ The Commission intends to explore whether there is a method that would better set the amount(s) of the financial consequence to enhance the incentives for the Postal Service to increase efficiency, reduce costs, and maintain high quality service standards in the current environment. The Commission finds that additional study would ensure that counterproductive outcomes do not occur and would better connect the change(s) in or level(s) of efficiency, cost reductions, and service standards with the financial incentive(s) at stake. The Commission also intends to further explore whether the amount(s) at stake would translate to an increase of rate authority(ies),²³⁷ a reduction of rate authority(ies), a combination mechanism, or a surcharge(s).

²³⁴ See, e.g., ABA Comments at 2, 13; ABA Reply Comments at 6; ANM *et al.* Comments at 61-68; ANM *et al.* Reply Comments at 28; Meredith Corporation Comments at 2; NPPC *et al.* Comments at 55; NPPC *et al.* Reply Comments at 35-36.

²³⁵ See, e.g., PR Comments at 39-42; Postal Service Comments at 39.

²³⁶ See, e.g., ANM *et al.* Comments at 64-69; APWU Comments at 10-12; eBay Comments at 5; NAPS Comments at 2; NPPC *et al.* Comments at 12, 54-55, 61; PR Comments at 40-46; Postal Service Comments at 34.

²³⁷ Upward adjustments (such as a negative "X-factor") are not foreclosed by price cap theory. See Postal Service Reply Comments at 37-38; PR Reply Comments at 3 n.9; Willig Decl. at ¶ 12 n.5; see also Zarakas, *supra*.

Numerous commenters express particular concerns regarding the reliability, accuracy, and transparency of TFP.²³⁸ The Commission intends to further explore whether TFP is an appropriate benchmark to use for the basis of connecting a direct financial incentive and how TFP (or an alternative) could be refined methodologically to produce sufficiently reliable, accurate, and transparent results. Observing that there have been some changes in the TFP methodology over the years and that TFP results have been revised after-the-fact on occasion,²³⁹ the Commission intends to ensure that TFP, particularly if it is selected as a benchmark for provision of additional rate authority, is methodologically stable and sound. A critical step to enable this study of TFP will be to require the Postal Service to file the documentation and linked workpapers for its TFP methodology in the new rulemaking. Engaging in additional study will also somewhat mitigate the existing information asymmetry, particularly with respect to cost reductions, which tends to advantage the Postal Service (which has better information about the actual extent of achievable cost reductions) and disadvantage the ratepayers (who have less information on this issue).²⁴⁰

²³⁸ See, e.g., ABA Reply Comments at 6-7; ACMA Comments at 3; AF&PA Comments at 6-7; ANM *et al.* Comments at 8, 76-81; APWU Comments at 6; eBay Comments at 6; NPPC *et al.* Comments at 56; NPPC *et al.* Reply Comments at 36-37; Postal Service Comments at 39-40; Postal Service Reply Comments at 35.

²³⁹ Compare, e.g., United States Postal Service, USPS Annual Tables, FY 2017 TFP (Total Factor Productivity), February 28, 2018, Excel file "table annual 2017 public (2017 cra).xlsx," tab "Tfp-52" (updating FY 2016 TFP result to 1.262), with United States Postal Service, USPS Annual Tables, FY 2016 TFP (Total Factor Productivity), March 1, 2017, Excel file "table annual 2016 public (2016 cra).xlsx," tab "Tfp-52" (reporting FY 2016 TFP result as 1.260). While the Postal Service did not provide an explanation for the updated FY 2016 TFP result, Commission analysis identified updated source data for FY 2016. Additional technical changes to the TFP are detailed in the NWPC paper provided by the Commission in conjunction with Order No. 5337. See generally NWPC Report 2.

²⁴⁰ See Order No. 5337 at 224-226 (describing opportunities to improve transparency and reduce information asymmetries relating to cost reduction initiatives or explanations for significant changes in costs); see also 2008 Joskow, *supra* at 550-551 (observing that regulators have imperfect information relating to the operator's cost, quality, and demand attributes and that such information asymmetries favor the operator and may disadvantage customers).

This need for additional information and study is particularly applicable to exploring potential alternatives to using a TFP benchmark. While some parties have provided their general positions regarding potential alternatives, the record in this docket does not contain much detail regarding how to potentially operationalize an alternative to using TFP.²⁴¹ The new rulemaking will provide an opportunity for parties to focus on these potential alternatives (and others) and provide operationalization suggestions.

Numerous commenters have expressed particular concerns regarding the performance target for efficiency gains that would be connected with a direct financial consequence.²⁴² As proposed in Order No. 5337, the amount of performance-based rate authority provided for low positive TFP growth would not differ from the amount of performance-based rate authority provided for higher positive TFP growth. Similarly, the amount of performance-based rate authority would not differ along the spectrum of possible negative TFP growth results. In the new rulemaking, the Commission is interested in exploring whether this performance incentive mechanism can and should be refined to provide tiers of financial consequences based on particular achievements. This need for additional information and study is particularly applicable to exploring potential alternatives to using a single performance target derived from past performance and potentially shifting to an approach that would connect direct financial consequences with tiers of performance targets. With regard to the concerns regarding setting an achievable target,²⁴³ the Commission intends for any incentive mechanism it may finalize to be effective; therefore, selection of an achievable target(s) will be

²⁴¹ See, e.g., ACMA Reply Comments at 2-4; AF&PA Comments at 5-6; APWU Comments at 5-11; NPPC *et al.* Reply Comments at 12-13.

²⁴² See, e.g., ABA Comments at 14; ACI Comments at 3; ANM *et al.* Comments at 65-75; APWU Comments at 10; eBay Comments at 4; Meredith Corporation Comments at 2; NPPC *et al.* Comments at 57-59; Postal Service Comments at 40; PR Comments at 39-46.

²⁴³ See Postal Service Comments at 40; NPPC *et al.* Reply Comments at 37.

explored in the new rulemaking.²⁴⁴ The comments regarding the use of a shorter-term or longer-term measure of the change in TFP growth²⁴⁵ raise important issues, and the Commission intends to further explore whether the target should be measured over the shorter-term or longer-term (or both) and whether any safeguards should be adopted to avoid perverse effects such as attaining occasional small, shorter-term gains at the expense of longer-term declines.

Some commenters take the position that the ratemaking system should introduce direct financial consequences with further degradation of the existing service standards. See NPMHU Comments at 1, 3-4. By contrast, other commenters oppose the introduction of such a mechanism because it would impose a large cost burden on the Postal Service and some users may not desire to pay extra to maintain existing service standards. See Mailers Hub Comments at 5, 8. The Commission will explore in the new rulemaking if introducing such a mechanism would enhance the system, and if so, how to calibrate that mechanism. To the extent that such a mechanism would enhance the ratemaking system's achievement of the objectives, the Commission disagrees with the Postal Service's new argument that introducing such a mechanism would be inconsistent with 39 U.S.C. § 3691.²⁴⁶ Previously, the Commission proposed to

²⁴⁴ See Zarakas, *supra* (opining that performance targets set in performance-based regulation should be achievable because "setting unachievable targets, in effect, extracts any meaning from the incentive mechanism.").

²⁴⁵ See, e.g., ABA Comments at 14; ABA Reply Comments at 7; Meredith Corporation Comments at 2; NPPC *et al.* Comments at 57; PR Comments at 39-46; Postal Service Comments at 32.

²⁴⁶ See Postal Service Comments at 30 (claiming that linking 1 percentage point of performance-based rate authority to maintenance of service standards is contrary to 39 U.S.C. § 3691); see also NPPC *et al.* Reply Comments at 38 (asserting that the Postal Service overstates its argument); Initial Comments of the United States Postal Service in Response to Order No. 4258, March 1, 2018, at 130 (2018 Postal Service Comments) (claiming that linking 0.25 percentage points of performance-based rate authority to maintenance of service standards is appropriately limited); Comments of the United States Postal Service, March 20, 2017, at 219 n.428 (2017 Postal Service Comments) ("Indeed, the Commission would always have the authority to fashion a prospective remedy to remedy any unlawful action by the Postal Service, which could include reduced pricing authority and the imposition of more burdensome regulation.").

introduce the service standard-based requirement as a necessary condition for availability of the performance-based rate authority as an effort to counterbalance the potential perverse incentives that might occur as a result of tying a financial incentive to operational efficiency gains and cost reductions. See Order No. 5337 at 142, 144; see *also* Order No. 4257 at 255. Because the Commission determines that additional examination is needed prior to codifying a performance incentive mechanism related to operational efficiency and that potential reductions in service standards may be linked with such a mechanism, such issues will be addressed in the new rulemaking.

These reasons also apply to the Commission's determination, at this juncture, not to partially codify its initial proposal in Order No. 4258 to provide 0.25 percentage points of rate authority based solely on the maintenance of existing service standards. Additionally, attempting to codify a portion of the performance-based rate authority conditioned solely on the service standard-based requirement, without having determined the final action related to any performance-based rate authority conditioned on an operational efficiency-based requirement, may disrupt the balancing of operational efficiency and cost-reduction goals.

Accordingly, the Commission finds that further refinement is warranted for these areas, and as a result, the Commission declines to implement its performance-based rate authority proposal at this time.

3. Analysis of Alternatives

The Commission declines to adopt the Postal Service's suggestion that the performance-based rate authority should be implemented now and that the operational efficiency and service standard-based requirements be deferred (effectively providing 1 percentage point of rate authority per annum unconditionally for a period of time). See Postal Service Comments at 29, 32-40; Postal Service Reply Comments at 36-37, 42. The Commission aims to ensure that the ratemaking system does not incentivize the

Postal Service to *solely* raise rates to respond to its challenges.²⁴⁷ Declining to finalize the performance-based rate authority at this time further ensures that this outcome is avoided. The final rules are intended to encourage prudent pricing *and* operational decision-making by the Postal Service. This properly balances all of the objectives of the PAEA, which strive to achieve systemic benefits for both the Postal Service and its ratepayers. Tending to be more conservative with the provision of additional rate authority remains in the spirit of the PAEA given that, as a practical matter, ratepayers lack a means of recovery for a rate increase that results in overpayment to the Postal Service. See 39 U.S.C. § 3681 (prohibiting reimbursement for any amount paid pursuant to a rate later determined to be unlawful).

Similarly, the Public Representative's concern regarding immediate capital needs fails to consider the effect of the Commission's approach as a whole. See PR Comments at 45-46. The Postal Service has been funding its immediate capital commitments from its "operating activities and defaults or non-payment on certain retirement and retiree healthcare obligations." Postal Service FY 2019 Form 10-K at 40. Revenue collected from the Postal Service's use of the rate authority provided under the final rules based upon declining density and non-compensatory classes (in addition to the rate authority provided by the change in the CPI-U) can be used by the Postal Service to finance capital investments directly or indirectly (*e.g.*, reduce its debt and thereby increase its available borrowing authority, which could be used to fund capital

²⁴⁷ Allowing an operator to passthrough all of its capital investment expenditures to ratepayers, may have adverse consequences; an increased incentive to gold-plate and a diminished incentive to innovate. See, *e.g.*, *Nat'l Rural Telecom Ass'n v. FCC*, 988 F.2d 174, 178 (D.C. Cir. 1993) (describing perverse incentives under a rate-of-return regulatory system arising from allowing a firm to pass any cost along to ratepayers, including "gold-plat[ing]"—using equipment or services that are not justifiable in purely economic terms, especially when their use improves the lot of management (elegant offices, company jets, etc.).") (quoting *In the Matter of Policy & Rules Concerning Rates for Dominant Carriers*, 5 F.C.C. Rcd. 6786, 6853 n. 450 (1990)). This aim is consistent with the spirit of the PAEA's reforms to postal rate-setting. See H. Rep. No. 109-66, pt. 1, at 48 (2005) ("The [PRA-era cost-of-service] rate-setting process provides little or no incentive for the Postal Service to control its costs because all costs are ultimately passed through to the consumer regardless of how efficiently or inefficiently the Postal Service operates.").

investments). The Commission's principled adjustments to the existing price cap provide opportunities for the Postal Service to raise revenue that would somewhat offset these imminent financial pressures and allow the Postal Service to address capital needs that, while important, have been deferred to allow the Postal Service to continue to operate in the near-term.

The Commission also declines to defer implementation of the remaining final rules until the conclusion of the new rulemaking. The principled adjustments to the existing CPI-U price cap based on declining density and retirement obligations increase the amount of rate authority available to the Postal Service and target two underlying drivers of the Postal Service's net losses that are largely outside of its direct control, thereby realigning the existing price cap system. The principled adjustment providing 2 percentage points of rate authority per annum for non-compensatory classes of mail continues, by regulation, the Commission's ongoing approach to address long-standing issues concerning non-compensatory rates, which cumulatively threaten the financial integrity of the Postal Service. The enhanced regulation of workshare discounts formally requires the Postal Service to adhere to the Commission's past recommendations regarding the Postal Service's inefficient pricing practices. The additional reporting requirements are directly aimed at promoting transparency and accountability regarding the Postal Service's cost benefit analyses concerning planned and actual operational initiatives. None of these approaches are dependent on the outcome of the issues being examined in the new rulemaking.

The Commission does not find it is necessary to delay the finalization of the remaining forms of rate authority to coincide with the potential application of performance-based rate authority. The claim that the Postal Service's collection of increased revenue would lead to a decrease in TFP is based on correlation without any evidence of causation. See *NPPC et al.* Comments at 12, 55, 59-60. TFP cumulative growth was comparatively lower when the exigent surcharge was in place than

compared to other time periods.²⁴⁸ Taken in isolation, this result might suggest that providing the Postal Service with an opportunity to generate additional revenue by raising rates might negatively affect the systemic achievement of Objective 1; however, the record contains evidence that other issues may have contributed to this result. NWPC opines that the Postal Service's decision to reduce its service standards (in an aggressive effort to reduce costs) negatively affected service performance, to which the Postal Service responded by diverting resources in a manner that decreased TFP cumulative growth.²⁴⁹ NWPC's opinion tends to confirm the Commission's repeated concerns regarding the robustness of the Postal Service's analysis of its projected cost savings, efficiency gains, and service performance impacts. See Order No. 4257 at 201-203 (summarizing the Commission's past advice regarding the Postal Service's planned changes to its service standards and during the joint Periodicals Mail Study). The Commission maintains its position that the Postal Service must comprehensively analyze the costs and benefits of potential operational changes and the additional reporting requirements in the final rules at 39 C.F.R. § 3050.55 are directly aimed at addressing this past deficiency.

Moreover, delaying implementation of the remaining final rules until the issues related to the performance-based rate authority are resolved would deprive the

²⁴⁸ The exigent surcharge, which added 4.3 percent overall, was effective from January 26, 2014 (FY 2014 Quarter 2) through April 10, 2016 (FY 2016 Quarter 3). Docket No. R2013-11, Order Granting Exigent Price Increase, December 24, 2013, at 1, 193 (Order No. 1926); Docket No. R2013-11, Order on Removal of the Exigent Surcharge and Related Changes to the Mail Classification Schedule, March 29, 2016, at 1-2, 4-5 (Order No. 3186). Using updated TFP data provided in FY 2018, TFP cumulative growth from FYs 2014 through 2016 was 0.25 percent. See United States Postal Service, USPS Annual Tables, FY 2017 TFP (Total Factor Productivity), February 28, 2018, Excel file "table annual 2017 public (2017 cra).xlsx," tab "Tfp-52" (updating FY 2016 TFP result from 1.260 to 1.262). This growth rate is lower than most of the other time periods described by NWPC. NWPC Report 2 at 16-17. To clarify, NWPC calculated this rate as 0.04 percent using the most current TFP data available at the time of writing its report, which was finalized on March 27, 2017. See *id.*

²⁴⁹ NWPC Report 2 at 17, 87-88; see Declaration of John Kwoka, March 20, 2017, at 18-19, 21 (2017 Kwoka Decl.).

ratemaking system of changes that are necessary for the achievement of the objectives in the near-term, and represent a significant improvement over the status-quo. Thus, from a purely practical perspective, the Commission has concerns that such an alternative may result in the ratemaking system continuing to fall further out of alignment with the objectives. The 10-year review period set by the PAEA could be considered longer than typical price cap regimes and the lack of a review and course-correction at the 4- or 5-year mark likely exacerbated the extent of the observed deficiencies.²⁵⁰ The Commission acknowledges that attempting to realign the price cap system with the objectives, after over a decade of operation, presents complicated issues that may require further refinement. Therefore, in an effort to prioritize the near-term issues and engage in sufficient refinement of longer-term issues, the Commission will focus on issues related to the performance-based rate authority separately and finalizes the remainder of its proposal herein.

With regard to the comments reiterating issues with service performance, as previously explained, the Commission took into account the findings of Copenhagen Economics in deciding not to link the provision of performance-based rate authority with service performance results. See Order No. 5337 at 141-142. Generally, Copenhagen Economics found that “dynamic markets, such as the postal market, where user needs are changing over time and where the regulated operator’s cost of providing a high

²⁵⁰ See Christensen Decl. at 6:

Even if the PAEA price cap was properly calibrated at the beginning of the plan, with a formal (and not merely implied) determination that CPI – 0 was an appropriate calibration of the X factor at the time, a ten-year period without a mechanism to perform mid-course corrections is outside the realm of standard practice.

2017 Kwoka Decl. at 28-29 (opining that the 10-year period before the first review was unusually long, and thereby allowed for design defects and changed circumstances to contribute to the Postal Service’s financial problems and inflict persistent harm on the Postal Service and its customers); see *a/so* Willig Decl. at ¶¶ 12, 14 (describing price cap plans as typically running for 4 to 5 years between adjustments).

quality of service is highly dependent on market developments” call for a cautious regulatory approach.²⁵¹ Where the postal operator is already under financial stress, the risk of regulatory failure associated with applying a penalty Q-factor²⁵² (downward adjustment to the rate authority based on service performance) is higher. See Copenhagen Economics Report at 78. Additionally, in an environment of declining volumes, “if, for example, the operator is instructed to provide a very high level of quality, then this will lead to even higher [unit] costs on top of those already caused by the volume decline.”²⁵³ Therefore, creating the right formulation for a service performance incentive will require a better understanding of the relationship between cost and quality of service. The Commission must balance Objective 3 in conjunction with Objective 1’s cost-reduction component.

Additionally, the Commission recognizes that very few postal regulatory systems use a Q-factor at all. See Copenhagen Economics Report at 6 (describing that two

²⁵¹ Copenhagen Economics, *Postal Quality and Price Regulation*, March 29, 2017, at 7 (Copenhagen Economics Report); see *id.* at 22 (“It can be particularly challenging to assess the benefits and costs of a change in service quality in settings where the market is in dynamic transition and user needs are changing over time.”).

²⁵² Price cap plans may regulate service quality using a reward- or penalty-style “Q-factor.” See David E. M. Sappington, *Price Regulation and Incentives*, December 2000, at 14-15, 51, available at: http://regulationbodyofknowledge.org/wp-content/uploads/2013/03/Sappington_Price_Regulation_and.pdf; Copenhagen Economics Report at 18 n.19.

²⁵³ Copenhagen Economics Report at 24; see United States Postal Service, Office of Inspector General, Report No. 19XG013NO000-R20, *U.S. Postal Service’s Processing Network Optimization and Service Impacts*, October 15, 2018, at 2, available at: <https://www.uspsoig.gov/sites/default/files/document-library-files/2020/19XG013NO000-R20.pdf> (finding that “[g]enerally, management prioritized high-quality service above the financial health of the Postal Service and is making decisions daily to attempt to meet service performance goals that are significantly increasing costs[]”); Office of Inspector General, Report No. NO-AR-19-008, *Assessment of the U.S. Postal Service’s Service Performance and Costs*, October 15, 2018, at 2, available at: <https://www.uspsoig.gov/sites/default/files/document-library-files/2019/NO-AR-19-008.pdf> (NO-AR-19-008) (finding that “[w]hen the Postal Service’s processes are not completed as designed or when delays occur, management can, and often does, take actions outside the normal process to keep the mail moving and meet service targets; however, these actions can result in additional costs[]”).

countries presently use Q-factors under a price cap and that two countries have abandoned using Q-factors under a price cap).²⁵⁴ With respect to the countries that used or use service performance benchmarks, the Commission observes that the scope of the products subject to the Universal Service Obligation (USO) in the United States is far broader than the scope of products of international postal operators subject to a similar obligation. *Compare* 39 U.S.C. §§ 403(a), 403(b)(2), 404(b), and 404(c), *with* Copenhagen Economics Report at 28. These experiences further confirm the Commission's cautious and measured approach to creating rules that would directly link service performance with rate authority at this time without further review and consideration.

D. Revisions to Proposed Rules

The Commission withdraws the proposed rules relating to performance-based rate authority. Accordingly, all text associated with and cross-references to these provisions are deleted from the final rules. See final 39 C.F.R. §§ 3030.101 (deleting definition of performance-based rate authority, adjusting subsequent paragraph letter designations, and conforming cross-reference); 3030.127(a) (deleting cross-reference and adjusting subsequent subparagraph number designations). In order to maintain the letter designations of the other subparts, final subpart F of 39 C.F.R. part 3030 is reserved.

²⁵⁴ Belgium and Portugal have used Q-factors as a part of their price caps for 14 years and 25 years, respectively. See Copenhagen Economics Report at 28. Italy used a Q-factor for nearly 20 years and stopped in 2015 once service consistently reached the targets imposed by the regulator, although fines for failure to meet targets remain in place. See *id.* at 32-38. The United Kingdom (UK) applied a Q-factor-type adjustment to the revenue cap for Royal Mail from 2003 through 2010 and formally stopped using this adjustment when it abandoned a revenue cap model altogether in 2012. See *id.* at 38-43. Both Italy and the UK still impose a financial penalty on their respective postal operators for failing to meet service quality standards. See *id.* at 38, 43.

However, the Commission codifies the two reporting changes relating to TFP and service standards, which affect final 39 C.F.R. §§ 3050.21(m), 3050.60, and 3055.2(c), as previously proposed.²⁵⁵ As described below, finalizing these changes provides information that is helpful to the public and the Commission in monitoring the system. The information will be particularly helpful in the new rulemaking and the system review undertaken in 5 years.

First, final 39 C.F.R. § 3050.21(m) requires the provision of the input data and calculations used to produce the annual TFP estimates at the time of filing the Postal Service's ACR, which is due to be filed 90 days after the close of the fiscal year ending on September 30. Corresponding changes are finalized for existing § 3050.60: delete existing § 3050.60(e); modify the cross-reference appearing in existing § 3050.60(a); and redesignate existing § 3050.60(f) and (g) as final § 3050.60 (e) and (f), respectively. The Postal Service objects that TFP depends heavily on cost data in the Cost and Revenue Analysis (CRA) and International Cost and Revenue Analysis reports, both of which are filed with the Postal Service's ACR, and contends that it is not feasible to provide the TFP data at that same time. Postal Service Comments at 52. In response to a prior request, the Postal Service has provided the TFP data as early as two weeks after filing the Postal Service's ACR.²⁵⁶ Therefore, revising the deadline to require the Postal Service to file TFP data along with the Postal Service's ACR is reasonable, and, on a case-by-case basis and with adequate justification, the Postal Service can seek reasonable and brief extensions of time in its efforts to provide the TFP data as close in

²⁵⁵ See Order No. 4258 at 73, Attachment A at 42; Order No. 5337 at 273-276, Attachment A at 66, 70-71.

²⁵⁶ Docket No. ACR2018, Responses of The United States Postal Service to Questions 1-15, 17-50 of Chairman's Information Request No. 1, question 2, January 11, 2019 (providing all supporting workpapers for derivation of TFP for FY 2018). This information was sought by the Chairman, on behalf of the Commission, 1 week after filing of the Postal Service's ACR for FY 2018. Docket No. ACR2018, Chairman's Information Request No. 1, January 4, 2019, question 2.

time as possible to the filing of the Postal Service's ACR. Additionally, the Commission finds that the rule change, which would require the provision of the TFP data approximately 2 months earlier than the existing March 1 deadline, would improve the transparency of TFP to the public because it would facilitate the ability of commenters to incorporate assessments and analysis of changes in TFP into their comments on the Postal Service's ACR.²⁵⁷

Second, final 39 C.F.R. § 3055.2(c) adds a requirement that the Postal Service's ACR provide a description of and reason for any changes to the service standards (including relevant business rules), or certify that no changes have occurred. Asserting that the changes to the standards are already transparent, the Postal Service claims that the certification requirement is an unnecessary administrative burden. Postal Service Comments at 42. NPPC *et al.* indicate that more transparency surrounding service standard changes would be helpful to the public. See NPPC *et al.* Comments at 12, 69-71. In response to the specific question posed by NPPC *et al.* concerning how to access the most recent version of the business rules appearing in section 10, Appendix provided in the Postal Service's Service Performance Measurement (SPM) Plan (see NPPC *et al.* Comments at 70), the Commission observes that a more recent version of this document has been filed with the Commission.²⁵⁸ The difficulty that this commenter encountered in tracking this information tends to suggest that requiring certification in the ACR would benefit the public. Further, the Commission observes that the Postal Service has included a footnote in past ACRs asserting that in the applicable fiscal year

²⁵⁷ Further, the predictability and transparency of the density formula are also increased because an input to the density formula is included in this earlier filing. See final 39 C.F.R. § 3030.161(d).

²⁵⁸ See Docket No. PI2019-1, Library Reference USPS-LR-PI2019-1/1, May 21, 2019, file "iSPM RevPlan RED-LINE 52119.pdf" (May 20, 2019 Postal Service SPM Plan). Additionally, the Commission has provided standing instructions to the Postal Service regarding filing updates to its SPM Plan, on an as-needed basis. See Docket No. PI2018-2, Order Closing Docket, December 27, 2018, at 2 (Order No. 4945).

under review, “the Postal Service did not change market dominant product service standards for any class of mail on a nationwide or substantially nationwide basis.”²⁵⁹ Generally, the Commission allows the Postal Service to present the information as it sees appropriate and does not impose detailed form requirements; however, the purpose of requiring service standard information to be certified in the future is to ensure that the information will be reported in a manner that is clear, consistent, and useful to the public. Because the certification requirement improves transparency for the public by condensing information into a readily comprehensible, accessible, and public summary on an annual basis and does not appreciably increase the administrative burden, the Commission will codify final 39 C.F.R. § 3055.2(c).

²⁵⁹ *E.g.*, Docket No. ACR2017, United States Postal Service *FY 2017 Annual Compliance Report*, December 29, 2017, at 49 n.39 (FY 2017 ACR); Docket No. ACR2018, United States Postal Service *FY 2018 Annual Compliance Report*, December 28, 2018, at 46 n.55 (FY 2018 ACR); Docket No. ACR2019, United States Postal Service *FY 2019 Annual Compliance Report*, December 29, 2019, at 38 n.37 (FY 2019 ACR).

VII. NON-COMPENSATORY PRODUCTS AND CLASSES

This section describes changes to the ratemaking system regarding non-compensatory products and classes. The Commission previously proposed rules for non-compensatory products and classes in Order Nos. 4258 and 5337. In Order No. 4258, the Commission proposed additional rate authority for non-compensatory classes and products to increase revenue and improve cost coverage. See Order No. 4258 at 77, 84-85. In Order No. 5337, the Commission revised its proposal such that the additional rate authority for non-compensatory classes be optional rather than mandatory and that the determination of whether a product or class is non-compensatory may be made outside of the Annual Compliance Review proceeding. See Order No. 5337 at 151. The following discussion summarizes the comments received concerning the Commission's revised proposed rules, provides analysis, and describes additional changes made to the proposed rules.

A. Non-Compensatory Products

1. Introduction

The Commission defines non-compensatory products as those products for which attributable costs exceed revenue. Order No. 4258 at 77. The Commission identified eight non-compensatory products in the FY 2019 ACD: (1) Periodicals In-County, (2) Periodicals Outside County, (3) USPS Marketing Mail Flats, (4) USPS Marketing Mail Parcels, (5) USPS Marketing Mail Carrier Route, (6) Inbound Letter Post, (7) Media Mail/Library Mail, and (8) Stamp Fulfillment Services. FY 2019 ACD at 2, 24-67. With the exception of the two Periodicals products, which will be addressed in Section VII.B., *infra*, all of these non-compensatory products are included within classes of mail for which the overall class revenue exceeds overall class attributable cost. This distinction is relevant because Market Dominant price increases are capped at the class

level, but the Postal Service has flexibility to vary product prices and price increases within each class.

In its evaluation of the ratemaking system, the Commission found that non-compensatory products are not reasonably or efficiently priced and therefore threaten the financial integrity of the Postal Service because revenue from these products fails to cover costs. See Order No. 4257 at 139-142, 235-236. To improve the cost coverage for non-compensatory products, the Commission proposed several modifications to the system. Order No. 4258 at 77.

First, the Commission proposed to define “non-compensatory products” as products for which attributable cost exceeds revenue, as determined by the most recent ACD. *Id.* The Commission also proposed to prohibit the reduction of rates for non-compensatory products. *Id.* In addition, the Commission proposed to require minimum product-level price increases for each non-compensatory product. *Id.* Under the proposal, whenever the Postal Service files a notice of rate adjustment applicable to any class of mail, it will be required to propose to increase the rate for any non-compensatory product within that class by a minimum of 2 percentage points above the percentage increase for the class. *Id.* This proposed rate increase would not create additional rate authority for the entire class and must comply with the other rate-setting criteria proposed by the Commission. *Id.*

After addressing any non-compensatory product(s), the Postal Service retains pricing flexibility with regard to use of the remaining authority under the price cap for that class. *Id.* The Commission explained that the proposal allows for continued achievement of Objective 4 (allowing the Postal Service pricing flexibility) while making changes necessary to achieve Objective 1 (maximize incentives to increase pricing efficiency) and Objective 8 (establishing and maintaining reasonable rates). *Id.* Moreover, the Commission noted that the price increase would maintain stability and predictability in rates as required by Objective 2. *Id.* at 78. The Commission reasoned

that, although the proposal does not mandate immediate full cost coverage for non-compensatory products, the proposal sought to narrow the coverage gap and move non-compensatory products toward full cost coverage over time. *Id.*

Commenters provided mixed responses to the proposal, with some commenters citing concerns that price increases will create a hardship on mailers who may move mail out of the system and others expressing concern that the proposal does not consider the Postal Service's failure to contain costs. See Order No. 5337 at 154-156 (summarizing comments).

Noting the need to increase revenue and its limited tools that directly affect costs, the Commission did not propose any substantive changes to its proposal. *Id.* at 156-157. However, the Commission revised its proposal so that determinations as to which products were non-compensatory could be made outside of the Annual Compliance Review proceedings. *Id.* at 151.

2. Comments

The Commission again received varied responses to its proposal, including discussions on potential volume declines, cost reductions, and recommended clarifications.

AF&PA agrees that the system should address the related financial consequences of non-compensatory products. AF&PA Comments at 7. However, AF&PA suggests caution in the approach to "catch up" the cost coverage of these products so that rate increases are so high as to push mailers to other alternatives. *Id.* As part of the solution, AF&PA expects the Postal Service to more closely examine opportunities to reduce its costs associated with delivering these products, and to accurately proportion its cost allocation to these products to ensure that current cost estimates are not overstated. *Id.*

ANM *et al.* ask that the Commission consider whether the proposal will “drive all this mail out of the system, and whether doing so is necessary to ensure the financial health of the Postal Service.” ANM *et al.* Comments at 85. They observe that Postal Service operations have become more efficient as co-mailing has increased, and suggest that the Commission focus on designing a system that encourages this type of activity rather than focusing on squeezing revenue out of the remaining volume in USPS Marketing Mail Flats. *Id.* at 84-85.

ACMA asserts that rate increases of the magnitude contemplated in this docket, if implemented by the Postal Service, will cause volume declines and economic dislocations that go well beyond those suggested by the official elasticity estimates. ACMA Comments at 2. Repeating its comments from Docket No. ACR2019, ACMA explains that it would be detrimental to the viability of the overall postal system to continue to force higher rates on mail in the USPS Marketing Mail class that is less dense than the arbitrary thresholds of the Enhanced Carrier Route categories. *Id.* at 3; see ACMA Reply Comments at 1.

Mailers Hub comments that providing the Postal Service additional rate authority beyond what the CPI-based cap or other provisions may allow would improve cost coverage but states that lowering the attributable costs would have the same effect. Mailers Hub Comments at 9. In addition, Mailers Hub explains that, though the price sensitivity of most non-compensatory mail will be challenged by an additional 2-percent-per-year rate increase above the CPI cap, requiring that seems like the least that can be done. *Id.* Mailers Hub suggests that any additional rate authority should be confined to the class or product currently “underwater” and should be separate from, not offset by, decreases in the rate authority available to other products in the class. *Id.*

PSA states that the key to financial stability is “keeping mailbags full” and asserts that the price increases projected by the Commission in its proposal would result in significant volume declines. PSA Revised Comments at 6-7.

The Public Representative comments that the Commission's proposal for non-compensatory products in a compensatory class appears reasonable. PR Comments at 47. He explains that the Commission's proposed adjustments to the price cap for declines in volume density and exogenous retirement obligations, if properly structured, should give the Postal Service significant additional authority to increase prices for non-compensatory products. *Id.* at 48. Thus, the Public Representative states that he would support the proposal, provided the Postal Service is given enough additional price cap authority by the proposed adjustment for density declines and uncontrollable retirement obligations to raise prices by the amount that the Commission proposed to require. *Id.*; see PR Reply Comments at 34-35.

The Postal Service does not expressly support or oppose the proposal for non-compensatory products. However, it makes several observations. First, the Postal Service states that the text of proposed §§ 3030.220 and 3030.221 do not make clear that the rules for non-compensatory products are limited to classes for which overall class revenue exceeds overall class attributable cost. Postal Service Comments at 63 (citing Order No. 5337 at 163, Attachment A at 38). Second, the Postal Service suggests that prices set by the Universal Postal Union (UPU) should be excluded from the Commission's proposed rate-rebalancing rules for underwater products because it would not be rational to hold the Postal Service responsible for any lack of compliance. Postal Service Comments at 46. The Postal Service also suggests that prices set by the UPU be excluded from the price cap. *Id.*

3. Commission Analysis of Comments

The Commission shares the commenters' concern regarding potential volume declines and the need to focus on cost reductions. However, the issue of non-compensatory products is a complicated one. The Commission has previously stated that it has limited tools that directly affect costs, and the tools it has used have not eliminated the problem of non-compensatory products. Order No. 5337 at 156-157.

Thus, the Commission must consider competing concerns regarding price increases and balance them with the pressing need to increase revenue.

As an initial matter, cost coverage would further decline if revenue is not increased. *Id.* at 160. Gradual above-average price increases for non-compensatory products, along with cost reductions, will bring those products to full cost coverage over time and thereby achieve reasonable and efficient rates as envisioned by the PAEA. *Id.* at 163.

The proposed rules addressing non-compensatory products are designed to stop the trend of declining cost coverage for these products and move cost coverage toward 100 percent. *Id.* at 157-158. The Commission performed a scenario-based analysis to determine the appropriate level of price increases for non-compensatory products and found that price adjustments of this type are likely to have positive results on cost coverage. *Id.* at 158-161; see Order No. 4258 at 78-80. The Commission determined that the above-average price increase requirement is appropriate because it balances the need for mailers to pay reasonable rates (rates that do not threaten the financial integrity of the Postal Service) with the need for the Postal Service to reduce costs. Order No. 5337 at 161.

Moreover, the minimum product-level price increases are not so large to give the Postal Service the ability to address its financial challenges solely by raising rates. Regarding the proposed requirements for above-average price increases for non-compensatory products, commenters (specifically users of non-compensatory products) have consistently raised the specter of large volume losses and wholesale substitution to non-postal methods. The evidence provided on the record concerning the relationship between price and volume for all non-compensatory products has

consistently shown that price increases do not lead to large volume decreases.²⁶⁰ The Commission will monitor the impact of the pricing requirements for non-compensatory products to ensure that these requirements do not have a direct and unexpected negative impact on overall contribution. If such results do occur, the Commission will take appropriate action (and may, if warranted, revisit portions of the ratemaking system sooner than the 5 year review). Similarly, the Commission will continue to expect and encourage the Postal Service to work to reduce costs.²⁶¹ The Commission will also continue to monitor the performance of these products, including volume and cost coverage trends in the Annual Compliance Review proceeding. Thus, the Commission does not make any substantive changes to the proposed rules.

The Commission declines to modify the rules such that the additional authority be confined to an individual product and be separate from decreases in the rate authority available to other products in the class, as suggested by Mailers Hub. The price cap is applied at the class level to allow for Postal Service pricing flexibility, and price cap changes are based on the volume and prices of all products within a class. Thus, there is no mechanism for providing additional authority to individual products. Furthermore, creating such a mechanism while imposing mandatory rate requirements would further restrict pricing flexibility, hindering the achievement of Objective 4.

In response to the Postal Service's suggestion for clarity, the Commission revises final §§ 3030.220 and 3030.221 to clarify that these rules apply to non-

²⁶⁰ See United States Postal Service, *Econometric Estimates of Demand Elasticity for All Postal Products*, FY 2019, January 21, 2020.

²⁶¹ The Postal Service recently agreed with several recommendations made by Postal Service OIG to reduce costs. See United States Postal Service, Office of Inspector General, Report No. 20-088-R20, *Cost Reduction Initiatives for Mail Products*, August 3, 2020, available at: <https://www.uspsoidg.gov/sites/default/files/document-library-files/2020/20-088-R20.pdf>.

compensatory products in compensatory classes. Non-compensatory products in non-compensatory classes are addressed in final § 3030.222.

In addition, the Commission modifies final § 3030.221 to exclude products where prices are not set by the Postal Service.²⁶² The exclusion is specifically limited to rates that are set by treaty obligation and does not extend to any product subject to UPU deliberations and to which the United States has the authority to establish self-declared rates.²⁶³ The Commission acknowledges the difficulty with requiring rate increases where the Postal Service does not exercise complete control over the pricing and would be unable to unilaterally implement the remedy. Products covered under this exclusion would be determined by the Commission. The only Market Dominant product that met this definition in FY 2019 was the First-Class Mail inbound international product “Inbound Letter Post.” See FY 2019 ACD at 52. The Commission continues to encourage the Postal Service to endeavor to improve the pricing of this product, in conjunction with the U.S. Department of State. See *id.* at 59. Should the Postal Service later gain control over these rates and the product is found non-compensatory, the mandatory price increase would apply. This change would not affect the Commission’s compliance determination; thus, the Commission may still find these products to be non-compliant and order appropriate remedial action to resolve the non-compliance.

While the Postal Service also suggests that the Commission exclude from the price cap products where the Postal Service does not exercise complete control over the pricing, as discussed further in Section XII.C.4., these products remain on the Market Dominant product list and their prices remain subject to the price cap.

²⁶² This exemption does not exempt these products from the price cap, but only the mandatory remedy for non-compensatory products.

²⁶³ These are products where the Postal Service negotiates with foreign posts for rates higher than terminal dues, e.g., Inbound Market Dominant Multi-Service Agreements with Foreign Postal Operators.

4. Revisions to Proposed Rules

The Commission adopts the proposed rules, modified as described below. The final rules incorporate several of the suggestions identified in the comments. However, the substance of the rules remains unchanged.

The Commission revises final §§ 3030.220 and 3030.221 to clarify that these rules apply to non-compensatory products in compensatory classes. The Commission also revises final § 3030.221 to exclude products where the Commission has determined that the Postal Service lacks independent authority to set rates.

B. Non-Compensatory Classes

1. Introduction

Non-compensatory classes are classes for which the costs of all products exceed the revenues of all products. The overall financial results of such classes are dominated by non-compensatory products. Like non-compensatory products, non-compensatory classes threaten the financial integrity of the Postal Service. Order No. 4257 at 274. However, non-compensatory classes create unique issues in a ratemaking system that limits price increases at the class level to the average change in CPI-U over the preceding 12 months. Order No. 4258 at 81. Cost coverage cannot improve unless the Postal Service is able to constrain class costs below the price cap level. *Id.*

Moreover, improved cost coverage for products within non-compensatory classes cannot be attained by rebalancing rates among products within such classes because increasing the rates for one product generally requires offsetting decreases to the rates for other products. *Id.* at 84; see Order No. 5337 at 164. In non-compensatory classes, there are usually no products with positive cost coverage against which such offsets can be made. Order No. 5337 at 164. For example, the Periodicals class has consistently

failed to cover its costs. FY 2019 ACD at 25. The Periodicals class is comprised of two products—In-County Periodicals and Outside County Periodicals—and each of those products is non-compensatory. *Id.* at 24.

In Order No. 4258, the Commission proposed modifications to the ratemaking system that will provide 2 percentage points of additional rate authority to non-compensatory classes in order to improve cost coverage. See Order No. 4258 at 84-85. The Commission proposed that the Postal Service, when seeking to raise rates for a non-compensatory class, must use all available rate authority for non-compensatory classes as part of the first generally applicable rate adjustment in a calendar year. *Id.* at 84. If there are any products within a non-compensatory class for which product-level revenue exceeds the product-level attributable cost, then prices for such products may only be increased up to the amount of the class average. *Id.* at 85. Moreover, the Commission proposed to prohibit the reduction of rates for non-compensatory products. *Id.*

The Commission reasoned that the requirement that the Postal Service increase the rates for any non-compensatory class by an additional 2 percentage points is appropriate because it balances the need for mailers to pay a more reasonable rate with the need for the Postal Service to achieve cost reductions and improvements in operational efficiency. *Id.* at 86. Without a change to the ratemaking system, the Commission found that non-compensatory classes would continue the trend of negative class contribution and continue to hinder the achievement of Objective 1 (maximize incentives to increase pricing efficiency), Objective 5 (assure adequate revenues, including retained earnings, to maintain financial stability), and Objective 8 (establish and maintain reasonable rates). *Id.* at 85. The Commission explained that the proposed solution sought to stop the trend of declining cost coverage and move toward full cost coverage over time. *Id.*

Some commenters supported the Commission's goal to improve cost coverage, while others cautioned the Commission regarding potential volume declines. See Order No. 5337 at 165-167 (summarizing comments). Several commenters proposed alternative solutions, such as utilizing exigent surcharge capability to provide additional revenue, instituting a one-time reset to collect rates as close as possible to estimated total costs, or providing the additional authority on a trial basis. *Id.* at 166-167.

After consideration of the comments, the Commission proposed that the 2 percentage points of additional rate authority for non-compensatory classes be optional. *Id.* at 168. The Commission stated that the Postal Service's caution about unknown effects appeared to be in alignment with other commenters. *Id.* at 172. Agreeing that the Postal Service is in the best position to "assess demand and other market forces," the Commission found that the Postal Service should have flexibility to determine if and when this additional authority should be used. *Id.* (quoting 2018 Postal Service Reply Comments at 31). As with non-compensatory products, the Commission also revised its proposal so that determinations as to which classes were non-compensatory could be made outside of Annual Compliance Review proceedings. Order No. 5337 at 173.

2. Comments

Similar to comments for non-compensatory products, the Commission received a variety of responses to its proposal for non-compensatory classes, including discussions regarding potential volume declines, alternative solutions, and clarifications as to certain aspects of the proposed rules.

ANM *et al.* state the change to the proposal, while welcome, ignores that the Postal Service's inefficient management is the root cause of this issue. ANM *et al.* Comments at 82. ANM *et al.* also assert that the proposal "fails to further Objective 1 of the PAEA by reducing incentives for the Postal [S]ervice to eliminate inefficiencies and reduce the costs of processing and delivering these products; the proposal violates

Objective 4 by limiting the Postal Service's pricing flexibility, hampering its ability to recognize the multiplier effect this type of mail can create; and the proposal ignores Factors 3 (impact of increases on mailers), 8 (value of the different kinds of mail entered into the system), and 11 (the educational, cultural, scientific, [or] informational [ECSI] value to the recipient of the mail matter)." *Id.* Further, ANM *et al.* assert that, in this context, the ability of the Postal Service to use its full authority is equivalent to a requirement that it do so. *Id.* at 83.

NMA states that postage increases of the sizes contemplated by the proposal will drive newspaper marketing and periodicals mail out of the system as newspaper mailers will have no option but to reduce their distribution or shift to more affordable alternatives. NMA Comments at 11. NMA concludes that the Postal Service must continue to engage in serious cost-cutting, just as many newspapers have had to do. *Id.* NMA describes the efforts of the Postal Service along with news publications to address operational problems and efficiencies. *Id.* at 11-12. NMA recommends that the Commission give these initiatives, along with the Commission's proposed worksharing requirements, a chance to improve matters before authorizing rate increases. *Id.* at 12.

C21 comments that the additional rate authority will "put further stress on what are in many ways the most vulnerable products in the system, imperiling the viability of many periodicals, catalogs, and more." C21 Reply Comments at 11. C21 states that postal pricing in the 1970s ignored the impact on periodicals and actively contributed to their demise. *Id.* C21 cautions that the same could happen again, and catalogs, periodicals, and other industry segments could be "killed off entirely." *Id.*

Meredith Corporation states that it strongly opposes the proposal. Meredith Corporation Comments at 1. It explains that imposing price increases will negatively impact business mail users and will impede the ability of mail with ECSI value to reach its readers. *Id.* at 2. Meredith Corporation also comments that making the additional authority optional provides little comfort because the Postal Service has shown no

restraint in using the rate authority provided by the Commission, and thus it must plan for price increases. *Id.* Meredith Corporation suggests that the Postal Service must be required to reduce its flats processing costs before it is allowed to charge any surcharges on underwater products or classes. *Id.* at 3.

NNA urges the Commission to recognize the impact of rate increases on: community newspapers that serve America's rural areas; the communities they serve; and the Postal Service's universal service mission. NNA Comments at 3. NNA provides that if the Commission has the discretion to remove the price cap and rearrange the rate system set out in the PAEA, it also has the discretion to give ECSI values sufficiently high weight to protect this mail, even if it allows some degree of non-compensatory mailing for the Periodicals class. *Id.* at 15. NNA suggests that if any pricing penalties are to be applied, the Commission owes it to the small newspapers of America to require more precise costing data than those which the In-Office Cost System (IOCS) and other sampling systems presently provide for this small mail subclass. *Id.* at 17.

The Public Representative states that the Commission's proposal is inadequate. PR Comments at 49. He explains that 2 percentage points would do very little to reduce the large negative contribution of Periodicals revenue. *Id.* The Public Representative explains that an increase of the price cap for the Periodicals class should allow for the recovery of costs and can be designed to balance the objectives of increased revenues with price stability and reasonableness. *Id.* at 50. He states that the Commission's proposal accords too much weight to stability and reasonableness and far too little weight to producing adequate revenue. *Id.*

The Public Representative continues to support a one-time reset of the price cap that would permit the Postal Service to collect rates as near as possible to estimated total costs. *Id.* at 49. The Public Representative asserts that when the Commission rejected his proposal, the Commission ignored his assertion that a multi-year phase-in

mechanism could be used to moderate the impact of an increase in the cap to cover costs. *Id.* at 50. He states that he also emphasized that his proposal did not relieve the Postal Service of its obligation to reduce costs; that statutory provisions recognize the special place of Periodicals in the postal system; that raising the price cap for Periodicals would not, by itself, raise prices for Periodicals; and that, if Periodicals require subsidization because of perceived societal benefits, such subsidies should come from taxpayers, not the Postal Service or other customers. *Id.* The Public Representative also asserts that the one-time reset is consistent with generally applicable price cap principles. PR Reply Comments at 27. He further recommends that questions from other commenters regarding the validity of costs be examined and addressed by the Commission. *Id.* at 28.

The Postal Service states that the Commission improved its proposal by making the additional authority optional rather than mandatory. Postal Service Comments at 1. The Postal Service suggests that the Commission clarify its intent regarding the availability of the rate authority because it appears that the Commission intends to make the authority available upon issuance of the final rule, yet the rules appear to require an announcement as a condition precedent to the rate authority's availability. *Id.* at 51 n.37.

3. Commission Analysis of Comments

The Commission acknowledges the concern regarding the potential effect of price increases on mailers and on mail volume. The Commission also acknowledges that reducing costs will improve cost coverage. The Commission further acknowledges that the Periodicals class, in particular, comprises mailpieces that offer ECSI value.

However, as discussed in Section VII.A.1., the Commission has limited tools that directly affect costs. The Commission will continue to encourage cost reductions and efficient operations. To date, however, cost-reduction and efficiency improvements

have not staunched the growing negative contribution caused by non-compensatory products. As previously discussed in this section, the trend of negative class contribution would continue if the Postal Service does not have access to additional pricing authority. See Section VII.B.1. The Commission proposed the 2-percentage-point increase because this amount moves prices toward full coverage. This amount also appropriately balances the goal of improving cost coverage with maintaining stability and predictability in rates. See Order No. 5337 at 168. By making the use of the additional authority optional, the Commission recognized that there are a significant number of cumulative changes to the ratemaking system and there may be unknown effects on volume and revenue if prices were to increase in these classes. *Id.* at 172.

To provide added flexibility, the Commission modifies final § 3030.222 such that the Postal Service may use the additional authority to generate unused rate adjustment authority.²⁶⁴ This change also takes into consideration the assumption that the ability to use the additional authority is equivalent to a requirement. Making the additional authority bankable discourages the Postal Service from simply using it to avoid losing it. Rather, this change provides more incentive for the Postal Service to consider demand, ECSI value, and other market conditions before determining whether to use the additional authority.

The Commission declines to require more precise costing data in this proceeding that are specific to non-compensatory products.²⁶⁵ The Commission adopted cost reporting requirements in an effort to improve flats transparency and analyzed the first

²⁶⁴ See Chapter XIV., *infra*. New unused rate authority generated by the non-compensatory class-based authority, if any, will be added to the total amount of banked authority, and will follow the existing operation of the rules governing banked authority, including the annual limitation on the use of banked authority per class and the expiration of unused banked authority. 39 U.S.C. § 3622(d)(2)(C).

²⁶⁵ The Commission is adopting detailed cost reporting requirements for all Market Dominant classes and products as part of this rulemaking. The cost reporting requirements initiated by this proceeding are discussed, in general, in Chapter IX., *infra*.

set of data in response to these requirements in the FY 2019 ACD.²⁶⁶ Commenters may request that a separate rulemaking proceeding be initiated if they believe improvements can be made over the current costing models and estimates.

The Commission also declines to institute a one-time rate reset, as proposed by the Public Representative. The Commission previously found that the one-time reset results in 35 to 40 percent in additional authority and prioritizes adequate revenue (Objective 5) over stability and reasonableness in rates (Objectives 2 and 8). Order No. 5337 at 171. Given the concern regarding the effect of price increases on mailers and mail volume, the Commission must fashion a solution that increases revenue while maintaining stability and predictability in rates. The Commission's proposal strikes an appropriate balance between maintaining stable and reasonable prices and producing improvements in cost coverage.

The Commission clarifies two aspects of the proposed rule. First, because the additional authority is optional, the Commission clarifies that the Postal Service is not required to use all available rate authority for non-compensatory classes as part of the first generally applicable rate adjustment.

Second, the Commission declines to modify the text of final § 3030.222 to clarify its intent regarding the availability of the rate authority. The proposed rules are clear that the additional authority would be made available upon the Commission's announcement. The Postal Service appears interested in learning when the authority would first be available once these rules are finalized. The Commission will require the Postal Service to file a notice by December 31, 2020, of its intent to use this available authority. This date is consistent with the determination date for the density- and retirement-based authority presented in this Order.

²⁶⁶ See Docket No. RM2018-1, Order Adopting Final Rules on Reporting Requirements Related to Flats, May 8, 2019 (Order No. 5086); FY 2019 ACD at 155-175.

4. Revisions to Proposed Rules

The Commission adopts the proposed rules, modified as described below. However, the substance of the rules remains unchanged. The Commission revises final § 3030.222 to permit the use of the additional authority to generate unused authority.

VIII. WORKSHARE DISCOUNTS

A. Introduction

As it relates to workshare discounts,²⁶⁷ in Order No. 4258, the Commission determined that Objective 1's goal of pricing efficiency could be achieved when "prices adhere as closely as practicable" to ECP. Order No. 4258 at 87 (citing Order No. 4257 at 136). Under ECP, workshare discounts are equal to avoided costs and produce passthroughs equal to 100 percent. Order No. 4258 at 87-89.

The Commission identified and proposed to phase out the two practices impeding pricing efficiency: workshare discounts set substantially below avoided costs and workshare discounts set substantially above avoided costs. *Id.* at 93. In Order No. 4258, the Commission proposed the use of passthrough bands—ranges with upper and lower limits—in order to evaluate workshare discount compliance.²⁶⁸ The bands were subject to a 3-year grace period, providing the Postal Service with time to bring workshare discounts in compliance with applicable ranges. *Id.* at 95.

In Order No. 5337, the Commission refined its initial approach by dispensing with the 3-year grace period and instead proposing an incremental path to bring existing workshare discounts closer to ECP. Order No. 5337 at 176. The revised approach prohibits workshare discounts that are equal to avoided cost from being changed (that is, set below or above avoided cost). *Id.* Moreover, the revised approach prohibits

²⁶⁷ A workshare discount is a discount that a mailer receives for additional preparation of a mailpiece, such as presorting, prebarcoding, handling, or transportation, and relieves the Postal Service of the cost of performing those activities. Order No. 4257 at 130; Order No. 4258 at 19; 39 U.S.C. § 3622(e)(1).

²⁶⁸ The Commission's initial approach included percentage passthrough bands ranging from 75 percent to 125 percent for Periodicals and 85 percent to 115 percent for all other classes. *Id.*

workshare discounts that are below avoided cost from being reduced and workshare discounts that exceed avoided cost from being increased. *Id.*

Under this approach, compliance would still be determined in each ACD by identifying which workshare discounts during the previous fiscal year resulted in passthroughs that either exceeded 100 percent or fell below 85 percent (also referred to as the passthrough floor). *Id.* at 207. The Commission would also identify those workshare discounts that are equal to their avoided costs.²⁶⁹

In its next rate adjustment proceeding, the Postal Service would have several options to address any non-compliant workshare discounts identified in the most recent ACD or any discount being proposed in the rate adjustment proceeding that is low or excessive. *See id.* at 207-209.

In rate adjustment proceedings, the revised approach permits the Postal Service to propose to set a workshare discount below its avoided costs or above its avoided costs under certain circumstances. *Id.* at 207. A low workshare discount or an excessive workshare discount would be permitted if it was new, if it would represent an improvement of 20 percent over the existing workshare discount passthrough, or if it was set in accordance with a prior Commission order (via the proposed waiver process). *Id.* A low workshare discount would also be permitted if the proposed workshare discount would produce a passthrough of at least 85 percent. *Id.* Additionally, an excessive workshare discount would be permitted if it would be provided in connection with a subclass of mail (product), consisting exclusively of mail matter of educational, cultural, scientific, or informational (ECSI) value (39 U.S.C. § 3622(e)(2)(C)) and accompanied by certain information to ensure transparency. *Id.*

²⁶⁹ During its next rate adjustment proceeding, the Postal Service would not be able adjust a discount that the Commission identified in the most recent ACD as being equal to its avoided cost. *Id.*

As it relates to the waiver process, the Postal Service would have the opportunity to apply for a waiver for non-compliant workshare discounts via the Commission's proposed waiver process prior to a rate adjustment proceeding. *Id.* at 208-209. Under the existing ratemaking system, the Commission is unable to scrutinize in detail the Postal Service's claims regarding the statutory exceptions of 39 U.S.C. § 3622(e) prior to excessive workshare discounts going into effect due to the short timeframe for review of rate adjustment filings. *Id.* at 208. The waiver process allows the Postal Service to use the statutory exceptions of 39 U.S.C. § 3622(e), and also requires the Postal Service to submit the necessary data so that the Commission has the opportunity to analyze why the Postal Service is unable to set the discount consistent with or closer to ECP. *Id.* at 208-209. In addition, the use of one of the exceptions found in 39 U.S.C. § 3622(e) was expanded to include below-avoided-costs workshare discounts. *Id.* at 209.

The Commission received several comments on its rules related to worksharing as a result of Order No. 5337, which are discussed below. Following a discussion of the comments, the Commission provides its analysis of the comments and resulting revisions to the proposed rules.

B. Comments

1. Comments Supporting Commission's Revised Rules without Modifications

Greeting Card Association (GCA), Discover Financial Services (DFS), the Parcel Shippers Association (PSA), the News Media Alliance (NMA), and the Alliance of Nonprofit Mailers *et al.* (ANM *et al.*) support the Commission's revised rules related to worksharing.

GCA supports the Commission's waiver application process in proposed § 3030.286 stating that it would "relocate any disputes over justification for keeping a

noncompliant workshare discount to a pre-rate-adjustment timeframe.” GCA Comments at 3-4 (footnote omitted).

DFS supports the Commission’s focus on workshare discounts that result in passthroughs below 100 percent, indicating the Commission’s proposal is a “positive step” toward ECP. Discover Comments at 16 n.5. DFS states that if the Commission’s rules are “properly implemented, it should encourage the most efficient division of costs between the Postal Service and private industry, reducing the overall cost burden of the Postal Service.” *Id.*

PSA supports the proposed regulations that establish a passthrough floor for workshare discounts. PSA Revised Comments at 8. PSA states that it has “long argued” workshare discounts should be set equal to avoided costs as it would “promote efficiency by ensuring that work is performed by the least cost provider.” *Id.* PSA further states that when workshare discounts are set below avoided costs, it results in the Postal Service “maintaining an inappropriately large network” by performing work “that can be better performed by the private sector.” *Id.* at 8-9.

NMA states that the Commission’s worksharing proposals could help the Postal Service engage in “serious cost-cutting,” by “encouraging the Postal Service to implement fully improvements in pricing efficiency and operations for Periodicals.” NMA Comments at 11-12.

ANM *et al.* appear to support the Commission’s revised rules related to worksharing when it states that “[t]he correct course of action is clear,” and recommends the Commission “focus on those aspects of the proposed rule[s]—such as revisions to workshare discounts—that will actually lead to a more efficient and successful Postal Service.” ANM *et al.* Reply Comments at 29.

2. Comments Recommending Modifications to the Commission's Revised Rules

Mailers Hub LLC (Mailers Hub), ABA, the National Postal Policy Council *et al.* (NPPC *et al.*), Pitney Bowes, Inc. (Pitney Bowes), and the Postal Service each recommend modifications to the Commission's revised rules. The suggested modifications fall into six categories: (1) the elimination of the 85 percent passthrough floor (proposed § 3030.284(e));²⁷⁰ (2) the inclusion of an 85 percent passthrough floor as part of the waiver application process (proposed § 3030.286);²⁷¹ (3) the additional flexibility for below-avoided-costs workshare discounts (proposed § 3030.282);²⁷² (4) the expansion of an exception to include below-avoided-costs workshare discounts (proposed § 3030.286(c)(7));²⁷³ (5) the consideration of pending cost avoidance methodology dockets; and (6) exceptions related to mail matter with ECSI value (proposed § 3030.283(e)).²⁷⁴

a. Elimination of Passthrough Floor

ABA, NPPC *et al.*, and Pitney Bowes recommend the elimination of the 85 percent passthrough floor as proposed in § 3030.284(e). See Order No. 5337, Attachment A at 51.

In general, ABA supports the Commission's revised rules related to worksharing and notes that the Commission made "positive changes to workshare pricing," that "meaningfully incentivize[d] efficiency and cost reductions" by the Postal Service. ABA Comments at 1, 2, 14, 15. However, ABA states that the 85 percent passthrough floor

²⁷⁰ Order No. 5337, Attachment A at 51.

²⁷¹ *Id.* Attachment A at 53-57.

²⁷² *Id.* Attachment A at 49-50.

²⁷³ *Id.* Attachment A at 55-56.

²⁷⁴ See 39 U.S.C. § 3622(e)(2)(C); see also Order No. 5337, Attachment A at 51.

for discounts below avoided costs is unnecessary and that “[i]t risks frustrating the Commission’s stated intent to encourage incremental improvement in pricing efficiency...by always moving workshare discounts closer to 100 percent.” *Id.* at 15. ABA further states that the passthrough floor would “cure the worst abuses of passthroughs set below avoided costs,” but would “likely result in the systematic understatement of many workshare discounts.” *Id.* at 15-16. In its reply comments, ABA reiterates its concern that the 85 percent passthrough floor represents a “standalone safe harbor.” ABA Reply Comments at 2. ABA notes its and other commenters’ position that the passthrough floor “will frustrate the Commission’s stated intent to move workshare discounts closer to full [ECP] rates.” *Id.*

NPPC *et al.* contend that the Commission’s revised rules are “too permissive,” and could “allow the Postal Service to continue to avoid pricing according to ECP, thus defeating their very purpose.” NPPC *et al.* Comments at 17. NPPC *et al.* contend that the 85 percent passthrough floor creates a “safe harbor” for some workshare discounts and that “in practice it will tend to migrate discounts to 85 percent instead of the desired 100 percent.” *Id.* NPPC *et al.* suggest that workshare discounts with passthroughs between 85 percent and 99 percent “should be increased in the same manner” as all other passthroughs that exceed or are below avoided costs (*i.e.*, improvements of 20 percent). *Id.* at 18. In their reply comments, NPPC *et al.* reiterate the same concerns and recommendations related to the 85 percent passthrough floor. NPPC *et al.* Reply Comments at 18.

Pitney Bowes states that the Commission’s revised rules as they relate to worksharing “are improvements,” but suggests “slight modifications to promote efficiency.” Pitney Bowes Comments at 1. Similar to ABA and NPPC *et al.*, it states that the 85 percent passthrough floor as a “stand-alone safe harbor” is unnecessary, “will invite inefficient pricing,” and recommends its removal. *Id.* at 3, 7. Pitney Bowes further states that “[a]n 85 percent passthrough floor does not maximize incentives to

reduce costs or increase efficiency and does not encourage prices to be set as close as ‘practicable’ to full ECP rates.” *Id.* at 5. Pitney Bowes also contends that the 85 percent passthrough floor is inconsistent with the Commission’s “do no harm” principle and that, because the passthrough floor would not be “time-limited or transitional,” it would “allow inefficient pricing to remain over time.” *Id.* at 6. Pitney Bowes maintains that workshare discounts with passthroughs between 85 percent and 99 percent “should be treated the same as all other discounts” and “moved closer to full ECP rates unless there is adequate justification not to do so.” *Id.* at 7.

The Postal Service disagrees with those commenters who describe the passthrough floor as a “safe harbor” and points out that proposed § 3030.282(c) prevents it from “adjusting passthroughs freely within an 85 percent to 100 percent passthrough range.”²⁷⁵

b. Inclusion of Passthrough Floor in Waiver Application Process for Below-Avoided-Costs Workshare Discounts

ABA views the Commission’s proposed waiver process as providing “sufficient flexibility” to the Postal Service and contends the 85 percent passthrough floor “should operate as a constraint on the waiver process—not as a general safe harbor.” ABA Comments at 16.

Similar to ABA, NPPC *et al.* recommend an addition to the waiver application rule that would prevent waiver requests for passthroughs below 85 percent. NPPC *et al.* Comments at 18. NPPC *et al.* continue to recommend that the 85 percent passthrough

²⁷⁵ Postal Service Reply Comments at 42. Having said that, the Postal Service does request modifications to the Commission’s revised rules that would provide the Postal Service with the flexibility to increase or decrease workshare discounts with passthroughs between 85 percent and 100 percent, as necessary. *See id.* (“As explained in our initial comments, the Commission should establish this passthrough range as a safe harbor, by relaxing rules [§ 3030.]282(a) and (c)”). (emphasis in original).

floor “serve as the minimum passthrough applicable to any waiver request by the Postal Service” in their reply comments. NPPC *et al.* Reply Comments at 18.

Pitney Bowes maintains that the 85 percent passthrough floor should be included only “as a limitation on [] waiver authority” and not as an exception to the Commission’s focus of moving workshare discounts closer to ECP. Pitney Bowes Comments at 4. For that reason, Pitney Bowes recommends the 85 percent passthrough floor be used as “a lower bound on [workshare] discounts set below costs avoided” in any application for waiver pursuant to proposed § 3030.286(g) and recommends related changes to the rule. *Id.* at 4, 5. Pitney Bowes states that “[s]trict enforcement of the waiver provisions will be essential” to achieving the goals of the Commission’s revised rules. *Id.* at 4. It reiterates its position as part of its reply comments. See Pitney Bowes Reply Comments at 2, 5.

c. Flexibility for Passthroughs Between 85 Percent and 100 Percent

Proposed § 3030.282 prohibits changes to passthroughs of 100 percent and reductions to passthroughs less than 100 percent.²⁷⁶ As a result of the limitations in proposed § 3030.282, the Postal Service requests additional flexibility for workshare discounts resulting in passthroughs between 85 percent and 100 percent. Postal Service Comments at 48.

The Postal Service maintains that “the prices associated with these discounts might affect other workshare discounts,” and requests that reductions in workshare discounts be permitted so long as the resulting passthrough meets the 85 percent passthrough floor. *Id.* at 48-49. The Postal Service asserts that in order to better balance pricing flexibility with maximizing efficiency, the 85 percent passthrough floor

²⁷⁶ See Order No. 5337, Attachment A at 49-50.

should be implemented without the additional limitations in proposed § 3030.282 for passthroughs between 85 percent and 100 percent. *Id.* at 49. The Postal Service presents four arguments in support of its request for more flexibility.

First, the Postal Service states that increases and decreases to workshare discounts with passthroughs between 85 percent and 100 percent could allow for predictable and stable rates by “smooth[ing] out the normal ups and downs of estimated avoided costs.” *Id.* Second, the Postal Service states that “prohibiting a decrease in the size of the discount works against utilizing price cap space.” *Id.* It notes that “[t]o the extent that volume is concentrated in workshared rate cells [or] in a limited number of rate cells ... the Postal Service could at times find it difficult to fully exercise its rate authority if no decrease in size of a workshare discount is permitted.” *Id.* Third, the Postal Service indicates that there may be situations when it may require passthroughs of less than 100 percent, such as when the “longer-run marginal cost curve is downward-sloping” and “unit attributable cost [are] pushed up (beyond inflation) after work is outsourced to workshare partners” or when “attributable costs are not as volume-variable as measured.” *Id.* at 49-50. Fourth, the Postal Service contends that the flexibility to set workshare discounts that result in passthroughs below 100 percent (but above 85 percent) would help mitigate the “real risk” of overstated cost avoidances unnecessarily transferring work from the Postal Service to a workshare partner. *Id.* at 50. The Postal Service states that such an occurrence would be inconsistent with “optimizing economic efficiency” and would deprive the Postal Service (and its customers) of economies of scale and density. *Id.* In its reply comments, the Postal Service reiterates that proposed § 3030.282(c), as well as, proposed § 3030.282(a) should be “relax[ed]” in reaction to cost avoidance fluctuation. Postal Service Reply Comments at 42-43.

NPPC *et al.* respond to the Postal Service’s comments related to the passthrough floor and its request “to weaken” portions of proposed § 3030.282 by

“allow[ing] it to reduce discount passthroughs to 85 percent in *any* instance.” (emphasis in original). NPPC *et al.* Reply Comments at 18. NPPC *et al.* contend that the Postal Service’s request would “gut the central goal” of the Commission’s revised rules. *Id.* As it relates to the Postal Service’s argument that it may require passthroughs of less than 100 percent when attributable costs are not as volume-variable as measured, NPPC *et al.* describe the argument as “curious.” *Id.* at 19; see Postal Service Comments at 50. NPPC *et al.* maintain that the Postal Service’s argument “amounts to a request that the Commission ignore established costing principles when the Postal Service says it does not trust its own analyses.” NPPC *et al.* Reply Comments at 19. NPPC *et al.* also respond to the Postal Service’s argument that a passthrough of 100 percent could transfer work from the Postal Service to a workshare partner if avoided costs are overestimated. NPPC *et al.* Reply Comments at 20; see Postal Service Comments at 50. They state that the Postal Service’s argument “ignores the likelihood that the workshare partners may still be more efficient than the Postal Service.” NPPC *et al.* Reply Comments at 20. Finally, NPPC *et al.* recommend more precise language to ensure that workshare discounts that equal avoided costs are maintained despite annual changes in costs avoided. NPPC Comments at 17; see *also* Order No. 5337, Attachment A at 50.

ABA similarly objects to the Postal Service’s request for more flexibility for workshare discounts with passthroughs below 100 percent, which it asserts “confirm[s] that [the Postal Service] do[es] not want to change its behavior to promote more efficient operations.” ABA Reply Comments at 3. ABA further states that the Postal Service’s “pricing behavior for the past thirteen years has demonstrated that it will not set efficient workshare prices unless forced to do so.” *Id.* ABA recommends that the Commission “reject the litany of excuses offered by the Postal Service.” *Id.*

Pitney Bowes recommends the Commission reject the Postal Service’s requests as “inconsistent with Objective 1 and the Commission’s ‘do no harm’ principle,” and

asserts that it deviates from more efficient workshare pricing. Pitney Bowes Reply Comments at 3, 6. Similar to NPPC *et al.*, Pitney Bowes also disagrees with the Postal Service's "generalized concern regarding the risk of overestimating the modeled cost avoidance." *Id.* at 6. Pitney Bowes states that the Postal Service failed to cite any specific issues within the approved cost models and that "[h]and-waving concerns regarding overestimation" does not justify a "risk premium' that would bias [workshare] discounts downward." *Id.*

d. Expansion of 39 U.S.C. § 3622(e)(3)(B) Exception

The Postal Service contends that the waiver basis provided in § 3030.286(c)(7), which, as proposed, applies to excessive workshare discounts, should be expanded to include discounts that fall below their avoided costs.²⁷⁷ The Postal Service notes that all In-County, Periodicals workshare discounts fall below avoided costs. *Id.* It further notes that the Commission's revised rules related to non-compensatory products would prohibit the Postal Service from decreasing the products' rates and so below-avoided-costs workshare discounts "could be increased only by raising benchmark prices," and "unduly harm[ing] mailers not able to take advantage of the discounts." *Id.*

In response, Pitney Bowes contends there is "no basis" to expand the 39 U.S.C. 3622(e)(3)(B) exception and permit its use as a waiver from setting workshare discounts that are below avoided costs closer to "full ECP rates." Pitney Bowes Reply Comments at 4. Pitney Bowes cites to the Commission's initial findings related to the use of the exception for a waiver related to below-avoided-costs workshare discounts. *Id.* Pitney Bowes notes that the Commission "considered and rejected" the Postal Service's

²⁷⁷ Postal Service Comments at 48. Section 3030.286(c)(7) incorporates the statutory exception described in 39 U.S.C. § 3622(e)(3)(B), which permits excessive workshare discounts if reducing or eliminating the excessive workshare discount would result in a further increase in the rates paid by mailers not able to take advantage of the workshare discount. See 39 U.S.C. § 3622(e)(3)(B). The Postal Service seeks expansion of the exception to below-avoided-costs workshare discounts. Other conforming changes would be required in § 3030.286(g).

argument and that the Postal Service “offers no reason for the Commission to revisit its prior determination.” *Id.* Pitney Bowes maintains that the Postal Service’s example is “substantially overstate[d]” and that broadening the exception “would create significant efficiency losses because there are many important, high-volume discounts ... with passthroughs set well below 100 percent of the modeled costs avoided.” *Id.* at 4-5. Pitney Bowes argues that, should the Commission consider expanding the 39 U.S.C. 3622(e)(3)(B) exception, “it should be narrowly tailored to apply only to discounts that affect small volume rate categories where the rate impact would be substantial.” *Id.* at 4.

NPPC *et al.* recommend that the Commission reject the Postal Service’s proposal to permit waivers when increasing discounts could raise benchmark prices. NPPC *et al.* Reply Comments at 19. They state that it “amounts to a request to maintain the *status quo* in setting workshare discounts that the Commission has already found has not achieved Objective 1.” *Id.*

ABA recommends that the waiver process be strictly enforced and asserts that the process already provides sufficient flexibility to the Postal Service. ABA Reply Comments at 2-3. ABA recommends that the Commission “tighten the exceptions and waiver process” in order to maximize efficiency and reject the Postal Service’s request for “more expansive waiver authority.” *Id.* at 4.

e. Pending Cost Avoidance Methodology Dockets

The Postal Service contends that the Commission’s revised rules related to worksharing are “too restrictive” and may lead to pricing decisions that focus on workshare discounts and not on improving operational efficiency or meeting other business goals. Postal Service Comments at 46-47. The Postal Service notes that there may be instances where changes to the cost avoidance methodology are pending before the Commission. *Id.* at 47. The Postal Service recommends that the “pendency

of such a rulemaking” should be either grounds for a waiver pursuant to proposed § 3030.286 or included as an exception in proposed §§ 3030.283 and 3030.284. *Id.*

NPPC *et al.* respond that the Commission should reject the Postal Service’s proposal to approve a waiver when a costing methodology docket is pending. NPPC *et al.* Reply Comments at 19. NPPC *et al.* state that the Postal Service’s proposal “opens a potential loophole ... rife for abuse” because “[n]ot all costing methodology changes necessarily are adopted.” *Id.* NPPC *et al.* contend it would be “more prudent” for a change to be “adopted before it may be used as the basis for a discount.” *Id.*

Similarly, Pitney Bowes states “[t]here is no basis for a waiver or exception for workshare discounts subject to a pending cost methodology change” because the timing of any changes “is entirely within the Postal Service’s control.” Pitney Bowes Reply Comments at 3. It further states that “the exception for pending rulemakings would subvert the statutory delegation of responsibility to the Commission to establish approved costing methodologies.” *Id.* Pitney Bowes indicates that it would “support a separate procedural rule specifying the time for filing proposed changes to analytical principles to ensure timely resolution” prior to the next rate adjustment.²⁷⁸

f. Mail Matter with ECSI Value

Mailers Hub supports the Commission’s intentions to move workshare discount passthroughs toward 100 percent, but contends that “doing so should be done only when ‘desirable mailer behavior’ can be maintained.” Mailers Hub Comments at 9. Mailers Hub contends the permitted exceptions for above- or below-avoided-costs workshare discounts “should be limited.” *Id.* In light of “today’s postal finances,” Mailers Hub questions the appropriateness of the exception found in proposed § 3030.283(e)

²⁷⁸ *Id.* at 3-4. It is unclear whether Pitney Bowes is suggesting a “separate rule” as part of the revised rules in the instant docket related to worksharing or as part of another part of title 39.

related to mail matter with ECSI value.²⁷⁹ Specifically, Mailers Hub questions why costs and workshare discounts would be different for two identical pieces “simply because one has ECSI ‘value.’” Mailers Hub Comments at 10. Mailers Hub suggests that such deference is of “increasingly questionable appropriateness” and unfair to other ratepayers not producing such material. *Id.* Mailers Hub maintains that worksharing “in any form” should be “perpetuated” only at the lowest combined cost, including “mailer cost, postage, and [Postal Service] costs.” *Id.*

In its reply comments, the Postal Service disagrees with Mailers Hub’s criticisms related to ECSI mailpieces. Postal Service Reply Comments at 44. The Postal Service maintains that ECSI value preference “is relevant whenever changing a passthrough requires price increases for mailers who send material with ECSI value.” *Id.*

C. Commission Analysis

1. Elimination of Passthrough Floor

In Order No. 5337, the Commission stated that workshare discounts less than their avoided costs run counter to pricing efficiency and that it has consistently encouraged the Postal Service to improve workshare discounts that are less than avoided costs. Order No. 5337 at 195. The Commission found that the passthrough floor was necessary to address the Commission’s finding that the Postal Service had the ability to adhere to ECP throughout the PAEA era but did not do so. *Id.* Additionally, the Commission acknowledged that a higher passthrough floor would come closer to achieving ECP. *Id.* at 200. Indeed, the elimination of the passthrough floor as suggested by commenters, coupled with the incremental improvements required by final § 3030.284(c), would likely result in below-avoided-costs workshare discounts moving closer toward achieving ECP.

²⁷⁹ See *id.* at 9-10; see also 39 U.S.C. § 3622(e)(2)(C); Order No. 5337, Attachment A at 51.

However, the Commission notes that the regulatory requirements related to below-avoided-costs workshare discounts are new. The PAEA prohibits passthroughs above 100 percent (with some exceptions), but it does not address workshare discounts with passthroughs below 100 percent. See 39 U.S.C. § 3622(e)(2-3). The Commission also notes that the consequences of below-avoided-costs workshare discounts are less detrimental to the Postal Service than excessive workshare discounts. This is because, with excessive workshare discounts, the Postal Service is providing excessive discounts to mailers, hurting its bottom line and affecting its financial stability. Therefore, given that below-avoided-costs workshare discounts will be regulated for the first time under these rules and the Commission seeks to provide continued pricing flexibility, the Commission has elected to implement less restrictive rules related to these workshare discounts, including the implementation of an 85 percent passthrough floor.

Furthermore, the 85 percent passthrough floor phases out the most inefficient of the Postal Service's pricing practices related to below-avoided-costs workshare discounts. The Commission finds that the 85 percent passthrough floor in final § 3030.284(e) (in conjunction with the other regulations for below-avoided-costs workshare discounts) strikes an appropriate balance between improving pricing efficiency and providing sufficient pricing flexibility for below-avoided-costs workshare discounts that were not previously regulated.

Additionally, commenters contend that the Postal Service may use the passthrough floor as a "safe harbor" and fail to move discounts with passthroughs between 85 percent and 100 percent closer to ECP. As the Postal Service notes, that concern is mitigated by final § 3030.282(c), which prevents the Postal Service from decreasing the amount of a workshare discount that is less than the avoided cost. Postal Service Reply Comments at 42. The Commission notes that, over time, should it appear that the Postal Service is attempting to use the 85 percent passthrough floor as a "safe harbor" for below-avoided-costs workshare discounts and is not taking steps to

move those workshare discounts toward ECP, the Commission may revisit its rules on workshare discounts as part of its planned review in 5 years.

For these reasons, the Commission rejects commenters' request to eliminate the passthrough floor.

2. Inclusion of Passthrough Floor in Waiver Application Process for Below-Avoided-Costs Workshare Discounts

Commenters' suggestion to include the 85 percent passthrough floor as part of the waiver process would impose substantially more limitations on below-avoided-costs workshare discounts. As noted above, the implementation of new regulations as it applies to below-avoided-costs workshare discounts, which had no previous limitations, necessitates that the Commission proceed cautiously in implementing such regulations. The Commission intends to require the Postal Service to move workshare discounts that are less than their avoided costs closer to ECP in order to improve pricing efficiency, but also provide some flexibility to the Postal Service at the outset of these new regulations.

Additionally, commenters provide no rationale for including the 85 percent passthrough floor as part of the waiver process, only asserting that, if a passthrough floor must exist, it should be a limitation on a request for a waiver in proposed § 3030.286.²⁸⁰ However, the Commission finds that the limitations on below-avoided-costs workshare discounts imposed by the waiver process are appropriate as they allow the Postal Service to set below-avoided-costs workshare discounts that do not meet the requirements of final § 3030.284(b), (c), or (e) only in limited circumstances and after a thorough Commission review. The Commission intends for the waiver process to be used in exceptional circumstances, where waiver applications are considered on a

²⁸⁰ See generally ABA Comments at 16; NPPC *et al.* Comments at 18; Pitney Bowes Comments at 4, 5.

case-by-case basis, focusing on the specific discounts in question and the characteristics of the relevant categories of mail associated with the discounts. The appropriateness of waiving, in full or in part, the requirements of other regulations will be based on the Commission's findings regarding the Postal Service's ability to adjust the discounts in question, and not the resulting passthrough. Although the Commission finds waivers for discounts less than avoided costs are necessary to provide the Postal Service with sufficient flexibility for potentially problematic below-avoided-costs workshare discounts, the Commission intends to ensure the Postal Service's strict adherence to the waiver regulation (final § 3030.286).

For the reasons discussed above, the Commission rejects commenters' request to include the 85 percent passthrough floor as part of the waiver application process in final § 3030.286.

3. Flexibility for Passthroughs Between 85 Percent and 100 Percent

The Postal Service suggests the Commission grant additional flexibilities to workshare discounts between 85 percent and 100 percent, specifically suggesting that such discounts should not have to comply with proposed § 3030.282(a) and (c).

Final § 3030.282 codifies the Commission's "do no harm" principle, which is intended to prohibit the Postal Service from making workshare discounts more inefficient. Order No. 5337 at 193. Final § 3030.282 prohibits workshare discounts that are equal to avoided cost from being changed (that is, set below or above avoided cost). *Id.* at 206. Moreover, the rule prohibits workshare discounts that are below avoided cost from being reduced and workshare discounts that exceed avoided cost from being increased. *Id.* at 206-207. The purpose of these limitations is to address the Commission's previous finding that, during the PAEA era, the Postal Service had the ability to set workshare discounts in accordance with ECP, yet failed to do so. Order No. 4257 at 139.

NPPC *et al.* recommend that more precise language be included in the rules to ensure that workshare discounts that equal avoided costs are maintained as equal to avoided costs despite annual changes in costs avoided. NPPC *et al.* Comments at 17. The Commission disagrees that more precise language is needed as NPPC *et al.*'s suggested changes would alter the final rules' intended limitations on workshare discounts. The Commission acknowledges that changes in cost avoidances occur annually, causing passthroughs to fluctuate. As it relates to excessive passthroughs, the Commission notes that when changes in avoided costs result in passthroughs above 100 percent, under some circumstances, the Postal Service may be able to easily return the passthrough to 100 percent of avoided costs in the next rate adjustment proceeding. However, that may not always be the case. Therefore, in the next rate adjustment proceeding, the final rules would only require a 20 percent improvement to the excessive passthrough or the workshare discount to otherwise meet the requirements of final § 3030.283.²⁸¹ As it relates to low passthroughs, the Commission notes that when changes to avoided costs result in passthroughs below 100 percent, the final rules do not require that the Postal Service return the passthrough to 100 percent of avoided costs as long as the passthrough is above 85 percent or otherwise meets the requirements of final § 3030.284.

The Postal Service asserts that in order to better balance pricing flexibility with maximizing efficiency, the 85 percent passthrough floor should be implemented without the additional limitations in proposed § 3030.282 for passthroughs between 85 percent

²⁸¹ The Commission maintains that this does not conflict with the "do no harm" principle conveyed in final § 3030.282(a) as it relates to workshare discounts set equal to avoided costs. If the Postal Service reports a workshare discount passed through 100 percent of avoided costs in the ACR (as confirmed by the Commission in the ACD), then the Postal Service is prohibited from proposing to adjust a rate associated with that workshare discount that may alter the resulting passthrough in the next rate adjustment proceeding. This prohibition also applies to excessive and below-avoided-costs workshare discounts pursuant to final § 3030.282(b) and (c). Indeed, final § 3030.282 prevents the Postal Service from proposing a rate adjustment to a workshare discount that would push the related passthrough further from ECP. The Commission notes that even the waiver process described in final § 3030.286 cannot be used to evade the "do no harm" requirements of final § 3030.282.

and 100 percent. Postal Service Comments at 49. The Postal Service presents four arguments in support of its request for more flexibility, and the Commission addresses each in turn.

First, the Postal Service maintains that added flexibility for workshare discounts with passthroughs between 85 percent and 100 percent would allow for more predictable and stable rates while also satisfying the pricing flexibility objective. *Id.* The Commission acknowledges that the worksharing regulations constrain the Postal Service's pricing flexibility to some extent. However, 39 U.S.C. § 3622(b) instructs that each objective "shall be applied in conjunction with the others." 39 U.S.C. § 3622(b). Thus, the Commission's modification to the ratemaking system overall must appropriately balance all of the PAEA's objectives in conjunction with each other. In order to achieve more efficient pricing as it relates to workshare discounts, an element of Objective 1 that was not achieved during the PAEA era, some of the Postal Service's pricing flexibility must be sacrificed. Allowing the Postal Service to decrease a workshare discount that already passes through less than its avoided cost would lead to less efficient pricing, which runs counter to Objective 1. See 39 U.S.C. § 3622(b)(2). As noted above, improved pricing efficiency as it relates to workshare discounts is the main focus of the Commission's "do no harm" principle.

Additionally, it does not follow that the proposed rules related to below-avoided-costs workshare discounts provide the Postal Service with no pricing flexibility. By including an 85 percent passthrough floor (instead of no passthrough floor at all), the Commission provides the Postal Service with some flexibility for workshare discounts. Other elements of the final rules related to worksharing also allow for pricing flexibility. They contain specific provisions to allow for transitional flexibility, particularly for new workshare discounts and by setting minimum thresholds for movement towards ECP (improving the existing workshare discount by 20 percent or producing a passthrough between 85 percent and 100 percent). Additionally, the Commission allows for pricing

flexibility to deviate from the new requirements for setting discounts in final § 3030.283 and § 3030.284, if adequately justified via the waiver process. Finally, these final rules limit only the workshare discount aspect of pricing and do not restrict the setting of the benchmark prices, thereby continuing to allow pricing flexibility. As it relates to the predictability and stability of rates, the Commission notes that the incremental nature and modest magnitude of the improvements to workshare discount in final §§ 3030.283(c) and 3030.284(c) are consistent with Objective 2. See 39 U.S.C. § 3622(b)(2); Section XIII.E.2., *infra*.

Second, the Postal Service states that “prohibiting a decrease in the size of the discount works against utilizing price cap space.” Postal Service Comments at 49. To the Postal Service’s point, the Commission acknowledges that the limitations provided in the revised rules may require more technical precision in the price setting process for the Postal Service to utilize all price cap space. However, the Commission finds that the additional flexibility requested by the Postal Service would be detrimental to ensuring that workshare discounts are improved toward ECP and that it should be possible in most circumstances to use all or nearly all available pricing authority while adhering to the final rules.²⁸² In addition, the Commission notes that the final rules will permit the Postal Service to bank unused pricing authority that can be used in the future.

Third, the Postal Service indicates that there may be situations that require passthroughs of less than 100 percent such as when the “longer-run marginal cost curve is downward-sloping” and “unit attributable cost [are] pushed up (beyond inflation) after work is outsourced to workshare partners” or when “attributable costs are not as volume-variable as measured.” *Id.* at 49-50. The Postal Service’s contentions are

²⁸² Although the Commission’s workshare discounts rules constrain the pricing relationships between worksharing tiers of a particular product, the rules do not prevent the Postal Service from setting other pricing relationships between products, which provides the Postal Service with the flexibility necessary to achieve its pricing objectives.

speculative as it provides no support or examples to show why under the identified conditions a passthrough of less than 100 percent would be preferable. The Postal Service also fails to explain the relevance of increases in unit attributable costs. The Commission notes that cost avoidances reflect differences in attributable costs associated with the applicable workshare activity, not differences in unit attributable cost. The cost segments involved in the calculation of cost avoidances are only a subset of the cost segments involved in the calculation of unit attributable cost. Therefore, no conclusions can be drawn about the behavior of cost avoidances from changes in unit attributable cost.

Fourth, the Postal Service contends that the flexibility to set workshare discounts that result in passthroughs below 100 percent (but above 85 percent) would help mitigate the “real risk” that overstated cost avoidances could unnecessarily transfer work from the Postal Service to a workshare partner, impacting efficiency. *Id.* at 50. The Commission is not persuaded by the Postal Service’s assertion that more flexibility is necessary to mitigate the risk of overstated cost avoidances and unnecessarily transferring work from the Postal Service to a workshare partner. Pitney Bowes correctly notes that the Postal Service did not cite any specific examples of cost avoidances being overstated. See Pitney Bowes Reply Comments at 6. If the Postal Service believes a cost avoidance model systematically overestimates or underestimates avoided costs, the Commission encourages the Postal Service to revise the model to better reflect operational realities and petition the Commission for a change in analytical principles pursuant to 39 C.F.R. § 3050.11. Additionally, the Commission notes that should a change in a below-avoided-costs workshare discount affect the Postal Service’s operational efficiency, the Postal Service may address that through the waiver process.

For the reasons discussed above, the Commission rejects the Postal Service's request to provide additional flexibility for passthroughs that fall between 85 percent and 100 percent.

4. Expansion of 39 U.S.C. § 3622(e)(3)(B) Exception

Section 3622(e)(3)(B) of title 39 permits workshare discounts with passthroughs above 100 percent to not be reduced if such a reduction would "result in a further increase in the rates paid by mailers not able to take advantage of the discount." See 39 U.S.C. § 3622(e)(3)(B). This exception was included as grounds for a waiver in the waiver application process in proposed § 3030.286(c)(7) as it relates to excessive discounts. However, this exception was not included as grounds for a waiver as it relates to below-avoided-costs workshare discounts.

The Postal Service had previously noted that increasing workshare discounts that are presently below their avoided costs may force the Postal Service to choose between harming its finances or increasing the rates of other mailers to a level that is not just and reasonable.²⁸³ However, in Order No. 5337, the Commission noted that "[t]he Postal Service fail[ed] to provide any explanation of how such harm is likely to occur." Order No. 5337 at 196. The Commission further noted that the Postal Service retained the flexibility to adjust below-avoided-costs workshare discounts in order to comply with the revised rules and had several methods of doing so. *Id.* The Commission acknowledged that, although the limitations related to below-avoided-costs workshare discounts may lead to an increase in rates for some mailers, "there [was] no evidence that increasing the size of workshare discounts [with passthroughs] under 100 percent [would] cause other rates to reach a level that is not just and reasonable." *Id.* at 196-197. Without an explanation of how such harm is likely to occur, the

²⁸³ See Reply Comments of the United States Postal Service in Response to Order No. 4258, March 30, 2018, at 108-109.

Commission saw no reason to allow the application of the exception found in 39 U.S.C. § 3622(e)(3)(B) to below-avoided-costs workshare discounts.

In response to Order No. 5337, the Postal Service presented a valid explanation for why the waiver process for the exception found in 39 U.S.C. § 3622(e)(3)(B) should be extended to below-avoided-costs workshare discounts for non-compensatory products. See Postal Service Comments at 48. The Commission acknowledges the validity of the Postal Service's assertion that for non-compensatory products, the only option to increase a passthrough is to increase the benchmark rate because the rules regarding non-compensatory products (39 C.F.R. part 3030, subpart G) prohibit lowering rates.

The Commission disagrees with Pitney Bowes' assertion that the Postal Service's example is overstated. Pitney Bowes Reply Comments at 4-5. However, the Commission also finds it unnecessary and inappropriate to extend the exception to *all* below-avoided-costs workshare discounts as suggested by the Postal Service. For below-avoided-costs workshare discounts unrelated to non-compensatory products, the Postal Service would be able to make the adjustments to a workshare discount without also substantially increasing the rates paid by mailers not able to take advantage of the discount, because the Postal Service could adjust other prices downward to bring workshare discounts closer to avoided costs. See 39 U.S.C. § 3622(e)(3)(B). However, for discounts related to non-compensatory products, the potential for substantial increases on mailers not able to take advantage of the discounts does exist because the rules regarding non-compensatory products (39 C.F.R. part 3030, subpart G)

prohibit lowering the rates associated with those products, which in turn would force the Postal Service to increase benchmark rates to improve the associated passthroughs.²⁸⁴ As such, the Commission will expand the waiver application process in final § 3030.286(c)(7) (with corresponding changes to final § 3030.286(g)) and permit the Postal Service to apply for a waiver based on the statutory exception found in 39 U.S.C. § 3622(e)(3)(B) for below-avoided-costs workshare discounts associated with non-compensatory products only.²⁸⁵

As it relates to commenters' concerns that expanding the exception provides for a more expansive waiver process, the Commission reiterates that Postal Service submission of a waiver application does not equate to the Commission granting the waiver. In order to be exempt from the requirements of final § 3030.284(c) (assuming the below-avoided-costs workshare discount does not qualify under final § 3030.284(b) or (e)), the Postal Service would have to demonstrate that it is unable to increase the workshare discount by the amount specified in final § 3030.284(c), without raising the benchmark rate for those mailers that are unable to qualify for the discount. The Commission notes that, for each basis for waiver including final § 3030.286(c)(7), the rules list a number of explanations the Postal Service must provide in order to show, by a preponderance of the evidence, that an application for waiver should be granted. With each of the explanations required, the Commission seeks to obtain information that

²⁸⁴ The least workshared mail category is considered the benchmark category. Each benchmark category has a benchmark rate that is based on the level of preparation of the mail, or where the mail is entered. Workshare discounts are set in relation to the benchmark rate. Because a workshare discount is measured as the difference in the price of the benchmark rate and the discounted rate, the workshare discount can be increased by either increasing the benchmark rate, or reducing the discounted rate.

²⁸⁵ The Commission could have provided a similar level of flexibility by expanding the waiver process for below-avoided-costs workshare discounts based on the statutory exception related to rate shock found in 39 U.S.C. § 3622(e)(2)(B). As part of the waiver process, both exceptions require a showing of harm or impact that would result from certain price changes. However, the Postal Service requests the expansion of the exception found in 39 U.S.C. § 3622(e)(3)(B), thus the Commission makes conforming changes to final § 3030.286(c)(7) (with corresponding changes to final § 3030.286(g)).

shows, absent a waiver, a change to a workshare discount at issue meets one of the narrow exceptions provided in the PAEA.

For the reasons discussed above, the Commission revises proposed § 3030.286(c)(7) to allow the 39 U.S.C. § 3622(e)(3)(B) exception to be used for below-avoided-costs workshare discounts related to non-compensatory products only.

5. Pending Cost Avoidance Methodology Dockets

The Commission notes several issues related to the Postal Service's proposal to include pending cost avoidance methodology dockets as part of the waiver process in § 3030.286 or in the limitations on workshare discounts in §§ 3030.283 and 3030.284. First, Commission approval of new cost avoidance methodologies is necessary prior to implementation and adoption is not guaranteed. Second, due to the complex nature of some proposed changes in cost avoidance methodologies, Commission review can take a significant amount of time to complete. As such, to delay the improvement of workshare discounts closer to ECP for a significant amount of time for a proposal that may not be approved would be inappropriate and counterproductive to objectives underlying the worksharing regulations. The Commission notes that, if a proposed change in cost avoidance methodology pending before the Commission would

somehow impede operational efficiency, the Postal Service can request relief through the waiver application process in final § 3030.286.²⁸⁶

It should also be noted that the Postal Service controls the timing of its filings for proposed changes in cost avoidance methodologies. The Postal Service is experienced in the level of complexity for these types of filings and the likely duration of a Commission review. The Postal Service also controls the timing of rate adjustment filings. Thus, the Commission finds it is unnecessary to add a separate procedural rule related to the timing of changes in methodology filings as suggested by Pitney Bowes. Instead, the Commission encourages the Postal Service to keep in mind case complexity as well as the potential duration of Commission review, and to submit changes in cost avoidance methodologies well in advance of a Postal Service rate adjustment filing.

For the reasons discussed above, the Commission rejects the Postal Service's request to include pending costing methodology dockets as part of the waiver process in § 3030.286 or the limitations on workshare discounts in §§ 3030.283 and 3030.284.

²⁸⁶ For example, if the Postal Service makes an operational change that increases the avoided costs for a destination delivery unit (DDU) dropship workshare discount, but under the accepted methodology the discount appears excessive, the Postal Service would be required to decrease the discount in order to comply with final §§ 3030.282(b) and 3030.283, unless a basis for waiver applies. The Commission notes that, even if the Postal Service petitioned the Commission to implement a conforming change to the associated cost avoidance model, if the Commission's review process is ongoing, the applicable avoided cost is based on the accepted methodology at that time. However, if reducing the workshare discount would shift volume from the DDU to the destination sectional center facility (DSCF), overwhelming the DSCF (or causing some other undesirable operational outcome), then the Postal Service could request a waiver under the operational efficiency exception (§ 3030.286(c)(5)), citing concerns of shifting volume and the likelihood that the avoided cost is understated, even though the exact amount of understatement is still under Commission review.

6. Mail Matter with ECSI Value

The Commission notes that Mailers Hub did not propose any specific rule changes, but appears to disagree with the exception in § 3030.283(e), which permits excessive workshare discounts for mail matter with ECSI value.

As part of the PAEA, Congress unambiguously intended to provide additional flexibility to workshare discounts greater than avoided costs for mail matter with ECSI value because of the value of that type of mail. See 39 U.S.C. § 3622(e)(2)(C). The same may be said about the various exceptions Congress permitted for different types of workshare discounts. See 39 U.S.C. § 3622(e). The Commission incorporates all of the statutory exceptions provided in 39 U.S.C. § 3622(e) into its revised rules for workshare discounts. The Commission finds that, final § 3030.283(e) is consistent with the PAEA's exception related to excessive workshare discounts for mail matter with ECSI value.

For the reasons discussed above, the Commission declines to adopt Mailers Hub's suggestion to remove or otherwise revise the inclusion of the exception for mail matter with ECSI value related to excessive workshare discounts.

D. Revisions to Proposed Rules

As noted above, the Commission revises § 3030.286(c)(7) in order to expand the 39 U.S.C. § 3622(e)(3)(B) exception to below-avoided-costs workshare discounts associated with non-compensatory products.

As discussed in Order No. 5337, proposed § 3030.286(c)(7) set forth the requirements specific to an application for waiver for excessive workshare discounts based on a further increase in rates paid by mailers not able to take advantage of the discount. See 39 U.S.C. § 3622(e)(3)(B); Order No. 5337, Attachment A at 55-56.

The Commission revises the language in final § 3030.286(c)(7) to include below-avoided-costs workshare discounts associated with non-compensatory products. The revised language is necessary in order to account for the prohibitions on reducing the rate for any product where the attributable cost exceeded the revenue imposed by final §§ 3030.127(b) and 3030.129(g). If a workshare discount is offered for a non-compensatory product and is so far below its avoided cost to produce a passthrough of less than 85 percent, then final §§ 3030.127(b) and 3030.129(g) prohibit the Postal Service from increasing that workshare discount because that would reduce the rate for a non-compensatory product. Therefore, in that situation, the Postal Service may seek a waiver under final § 3030.286(c)(7). Additionally, the Commission makes corresponding changes to final § 3030.286(g), which lists each basis for a waiver that the Postal Service may use related to below-avoided-costs workshare discounts. The Commission otherwise adopts the proposed rules from Order No. 5337 related to worksharing without changes.

IX. COST-REDUCTION REPORTING REQUIREMENTS

A. Introduction

In Order No. 4257, the Commission found that while the Postal Service's costs had been reduced during the PAEA era, the Postal Service's incentives to reduce costs and increase efficiency had not been maximized because the results had not been sufficient to achieve overall financial stability. Order No. 4257 at 191, 222. The Commission also found that the Postal Service's costs decreased less during the PAEA era than during the 10 years preceding the PAEA era. *Id.* at 224-25. Moreover, the Commission determined that cost savings estimates from some of the Postal Service's cost savings initiatives "[were] likely overstated," and that the Postal Service could improve its quantitative measurement of the results of cost savings initiatives. *Id.* at 200.

In Order No. 4258, cost reductions were addressed in a general manner as an aspect of the Postal Service's overall financial health. Order No. 4258 at 35-36, 39-40, 46-53. The Commission took as its starting point its conclusion from Order No. 4257 that the Postal Service was not financially stable because the current ratemaking system had not assured the Postal Service adequate revenues. Order No. 4258 at 33. The Commission noted that adequate revenues are necessary to achieve net income, which over time should lead to retained earnings, which can be used to fund capital investments that improve operational efficiency. *Id.* at 35-36. The Commission found that "improvements in medium- and long-term financial stability and increased operational efficiency should lead to cost reductions when the [financial health] cycle is functioning normally[,] and the Commission accordingly stated its "expect[ation] that its proposal [would] incentivize the Postal Service to take necessary steps to reduce costs." *Id.* at 36.

However, many of the comments received in response to Order No. 4258 raised concerns that price increases in excess of the CPI-U could undermine the Postal

Service's incentives to reduce costs and increase efficiency. Order No. 5337 at 214-217. Commenters also expressed criticism of the Postal Service's past efforts at reducing costs and increasing efficiency, and complained that there had been lack of transparency and accountability with regard to such efforts. *Id.* at 217-221.

In considering these comments, the Commission noted that "[t]he price cap and the potential for retained earnings were intended by the PAEA to be the primary incentives for cost reduction..." and that "[u]nder the rules [being] proposed..., the price cap will continue to exist, albeit in a modified form." *Id.* at 223. Nevertheless, the Commission concluded that "[t]o the extent that any additional rate adjustment authority might weaken the Postal Service's incentives with regard to cost reductions..." it was prudent to implement reporting requirements that could "serve as a counterbalance by requiring the Postal Service to focus its efforts on identifying the underlying causes of cost increases and developing concrete plans to reduce costs." *Id.*

The Commission also considered the issues of transparency and accountability. It found that the current ratemaking system has provided a general level of transparency through the ACR, in which the Postal Service files cost data for all of its products after the end of each fiscal year.²⁸⁷ It also found that the current ratemaking system has provided a general level of accountability through the ACD, in which the Commission determines compliance with title 39 and its related regulations after the end of each fiscal year and is empowered to take action in the event of a finding of non-compliance.²⁸⁸ Nevertheless, the Commission noted that "the current Commission rules do not require the Postal Service to specifically report on individual cost reduction initiatives or to explain significant changes in costs between years." Order No. 5337 at 224 (footnote omitted). The Commission determined that "[r]eceiving contemporary

²⁸⁷ *Id.* at 223-224. See 39 U.S.C. § 3652.

²⁸⁸ *Id.* See 39 U.S.C. § 3653.

information and explanations about cost reduction initiatives and changes in costs would allow the Commission to investigate these issues more consistently as part of the annual compliance review process.” *Id.* (footnote omitted). Furthermore, “[t]he information gleaned from such inquiries could lead to further investigation in other proceedings, such as rulemakings or public inquiries, to promote transparency and accountability.” *Id.* Therefore, the Commission “[found] it prudent to require the Postal Service, for the purposes of transparency and the ability of the Commission and other stakeholders to monitor these issues, to begin reporting on changes in costs and the status of cost reduction initiatives.” *Id.* at 222-223.

Based on the foregoing, the Commission proposed new reporting requirements designed to facilitate the tracking of costs and monitoring of the Postal Service’s efforts to reduce costs. These requirements consisted of three separate components: (1) a consolidated cost analysis; (2) detailed information regarding planned and active large-scale cost-reduction initiatives; and (3) summary information pertaining to approved Decision Analysis Reports (DARs), which are internal Postal Service documents used to justify and obtain approval for certain proposed capital spending projects.

The first component, proposed § 3050.55(b), would require the Postal Service to annually provide a consolidated cost analysis report detailing costs for Market Dominant products collectively,²⁸⁹ for individual Market Dominant products, and for the entire postal system. *Id.* at 227. For Market Dominant products collectively, the Postal Service would be required each year to report the percentage change in total unit attributable cost for all Market Dominant products collectively. *Id.* Attachment A at 67.

For individual Market Dominant products, the Postal Service would be required each year to provide unit cost data for each Market Dominant product, along with a

²⁸⁹ The Commission’s proposal excluded the Special Services class from reporting due to the unique nature of the products in that class. See Order No. 5337 at 227 n.315.

comparison of that data to the previous fiscal year, and a specific analysis evaluating the effect of any mail mix changes on unit costs. *Id.* at 227-228. For individual Market Dominant products for which unit costs had increased faster than the average for all Market Dominant products collectively, the Commission proposed additional reporting. *Id.* at 228. In such cases, the Postal Service would be required to disaggregate the total unit costs for each such product into six separate categories: (1) mail processing unit cost; (2) delivery unit cost; (3) vehicle service driver unit cost; (4) purchased transportation unit cost; (5) window service unit cost; and (6) other unit cost. *Id.* The Commission also proposed that for each such product the Postal Service provide a narrative identifying the drivers of changes in unit costs between fiscal years, and a plan to reduce the product's unit attributable costs. *Id.*

For the entire postal system, the Postal Service would be required each year to provide the percentage change in system-wide total unit cost per piece, defined as the sum of Market Dominant product attributable cost, Competitive product attributable cost, and institutional costs, divided by the sum of Market Dominant product volume and Competitive product volume. *Id.* at 228-229.

The second component of the proposed reporting requirements, proposed § 3050.55(c) and (d), would require the Postal Service to file specific information regarding planned and active cost-reduction initiatives. *Id.* at 229. Specifically, the Commission would require reporting with regard to cost-reduction initiatives expected to cost the Postal Service at least \$5 million over the duration of the initiative. *Id.* For each such initiative, the Postal Service would be required to file a narrative including an overview of the initiative, its status, the expected Postal Service expenditure on the initiative, the start date, the end date, and any intermediate deadlines. *Id.* at 230. The Postal Service would also be required to identify a metric to be used to measure the expected impact of each cost-reduction initiative in future years, as well as a timeline detailing when the Postal Service expected to see the impact. *Id.* Using its selected

metric, the Postal Service would be required to estimate the cost-reduction initiative's impact on Market Dominant products' unit costs, as well as total unit costs, in future years. *Id.*

Once a cost-reduction initiative was underway, the Postal Service would be required to file data detailing the impact of the initiative measured by its selected metric, as well as the impact on Market Dominant unit costs and total unit costs. *Id.* The Postal Service would be required to compare the actual results to the expected results and provide a narrative explaining any variance, along with a specific statement as to whether the initiative actually achieved the expected impact as measured by the selected metric. *Id.* Finally, the Postal Service would be required to provide a description of any mid-implementation adjustments made to align the actual results to expected results, as well as to identify any revisions to expected results for future fiscal years. *Id.* at 230-231.

The final component of the proposed reporting requirements, proposed § 3050.55(e) and (f), would require the provision of summary information pertaining to approved DARs. *Id.* at 231. A DAR is an internal Postal Service document required for each capital spending project that has total costs over \$1 million. *Id.* The Commission proposed that the Postal Service be required to provide the following information for all projects associated with a DAR in the current and next fiscal year: a description of the project; the status of the project; an estimate of cost savings or additional revenues from the project; and the expected return on investment from the project. *Id.*

The following discussion summarizes the comments received concerning the Commission's proposed cost-reduction reporting requirements, provides analysis, and describes the resulting changes made to the proposed rules.

B. Comments

Comments received in response to the proposed cost-reduction reporting requirements generally cover five topics: (1) the necessity of the new reporting requirements; (2) the risk of commercial harm to the Postal Service; (3) whether reporting requirements alone provide a sufficient incentive; (4) whether there should be changes made to the proposed reporting requirements; and (5) the tension between the proposed reporting requirements and Objective 6 of the PAEA.

1. The Necessity of the Proposed Reporting Requirements

The Postal Service argues that the proposed reporting requirements are not necessary. First, it asserts that “[e]ven without a price cap, [it] has a strong, inherent incentive to reduce costs and improve efficiency given market realities and persistent volume and density declines...” Postal Service Comments at 56. Second, regardless of what the Postal Service’s incentives would be in the absence of a price cap, it argues that “the [Commission’s] proposal is still fundamentally a price-cap system, maintaining an inflation-based cap within which the Postal Service must manage its operating costs.” *Id.* at 57. The Postal Service maintains that “price caps...create inherent incentives to reduce costs without the need for regulatory scrutiny of cost-reduction efforts.” *Id.* The Postal Service acknowledges that “the proposed rules...provide additional rate adjustment authority to offset exogenous pressures and correct economic imbalances...,” but it states that “the additional rate authority is proposed [in order] to make the price-cap structure work as intended.” *Id.* While the Postal Service allows that “[r]egulatory review of capital investments and cost-reduction efforts could perhaps be justifiable in cost-of-service regulation or in a deregulated environment without market-based efficiency incentives[,]” it maintains that “a fundamental purpose of price-cap regulation and incentive mechanisms is to reduce the need for regulatory scrutiny by shifting efficiency risks to the regulated entity.” *Id.* at 59.

NPPC *et al.*, on the other hand, assert that “[t]o the extent the Commission attaches cost-of-service factors, such as the density and retirement factors[,] onto the nominal structure of a price cap system, it adopts cost-of-service regulation.” NPPC *et al.* Reply Comments at 46. As such, “a commitment by the regulator to the regulatory reviews appropriate in a cost-of-service system[]” is called for. *Id.* at 47.

2. Risk of Commercial Harm

The Postal Service argues that “the Commission fails to consider any potential commercial harm to the Postal Service if these reports are made public.” Postal Service Comments at 60. The Postal Service states that:

The Cost Reduction Initiative Report and the...DAR summary reports cover a wide range of projects and almost inevitably involve some combination of procurement information that would not yet be available to potential suppliers; sensitive intellectual property information; information related to real estate decisions that could harm the Postal Service’s negotiating position; and predecisional, confidential information....

Id. The Postal Service maintains that “[s]ome of this information could impact future procurements and is information that potential suppliers should not be allowed to use to their benefit when participating in competitive solicitations.” *Id.* at 60-61. While the Postal Service acknowledges that with regard to DARs “the proposed rules require summaries, not the full [reports]...,” it nevertheless argues that “even the summary data could carry the same risks, as could responses to follow-up inquiries related to the summary reports.” *Id.* at 61. Furthermore, “if a DAR relates to an innovation for which the Postal Service wants to pursue intellectual-property protection, premature release of that information could interfere with the Postal Service’s future attempts to implement and monetize the innovation.” *Id.* In sum, the Postal Service argues that “[g]iven the potential for commercial injury and the lack of clear justification, the Commission should eliminate the Cost Reduction Initiative Report and the DAR summary report requirements.” *Id.*

3. Whether Reporting Requirements Alone Provide a Sufficient Incentive

Multiple commenters argue that reporting requirements, in and of themselves, are insufficient to incentivize the Postal Service to pursue cost reductions and efficiency improvements. ABA states that “reporting alone [will not] satisfy the pro-efficiency objectives and factors of the PAEA.” ABA Comments at 16. It advocates that the Commission “use the enhanced reporting data to meaningfully regulate [the Postal Service] []” by “condition[ing] new rate authority on real cost, productivity and service performance.” *Id.* ANM *et al.* similarly state that increased reporting requirements will accomplish nothing unless they are coupled with sanctions. ANM *et al.* Reply Comments at 19 n.15.

Although they do not oppose the proposed reporting requirements, NPPC *et al.* likewise “wonder[] about the utility of reports in the absence of more rigorous enforcement.” NPPC *et al.* Comments at 74. They express the view that reporting requirements have not proven to be an effective means of improving postal performance.²⁹⁰ They are concerned that the Commission’s proposal will undermine the incentive to control costs by replacing “the strong cost-reducing effect of a firm price cap with toothless reporting requirements.” NPPC *et al.* Comments at 24. They state that “[t]he Postal Service’s inadequate progress in reducing costs to efficient levels is not a problem of transparency, it is a problem of managerial effectiveness and lack of sustained focus.” NPPC *et al.* Reply Comments at 46. They maintain that “[t]he Postal Service’s continued inability to reduce costs should require a stronger remedy than simply more transparency and additional reports.” NPPC *et al.* Comments at 75. They advocate for financial penalties, in the form of reduced rate authority, for unsuccessful initiatives.²⁹¹

²⁹⁰ NPPC *et al.* Comments at 13; NPPC *et al.* Reply Comments at 13.

²⁹¹ NPPC *et al.* Comments at 76; NPPC *et al.* Reply Comments at 46.

4. Recommended Changes to Proposed Reporting Requirements

Both NPPC *et al.* and the Postal Service suggest changes to the proposed reporting requirements. NPPC *et al.* state that reporting on mid-implementation adjustments, which as initially proposed only applied to Cost-Reduction Initiative Reports, should be required for DAR summary reports as well. NPPC *et al.* Comments at 75. They also state that the Commission should conduct prior review of major cost reduction initiatives or capital investment programs. *Id.*

The Postal Service argues that the Commission should apply the \$5 million threshold proposed for Cost-Reduction Initiative Reports to DAR summary reports as well. Postal Service Comments at 61. Because the Postal Service prepares DARs for any capital spending project valued at \$1 million or more, it argues that requiring summary reports for all DARs would result in a lower effective threshold for having to prepare DAR summary reports than the \$5 million threshold for having to prepare Cost-Reduction Initiative Reports. *Id.* NPPC *et al.*, on the other hand, state that “[the Postal Service’s] repeated failures to achieve anticipated returns on major investments is a long-standing problem[,]” and “[the Postal Service] [does not] have the type of history of successfully-implemented capital investments that would warrant the level of deference it wants.” NPPC *et al.* Reply Comments at 47.

The Postal Service also argues that the Commission should remove the requirement that the Postal Service prepare summary reports for “planned projects that will require a [DAR] in the next fiscal year.” Postal Service Comments at 60, 61. The Postal Service states that “[a]ny project that the Postal Service is considering, but that does not yet have a DAR, would not yet be developed in a meaningful way.” *Id.* at 61. Therefore, disclosure of such projects “would have no utility.” *Id.* at 62.

5. Tension with Objective 6

Several commenters note potential tension between the proposed reporting requirements and Objective 6 of the PAEA, which is focused on “reduc[ing] the administrative burden and increas[ing] the transparency of the ratemaking process.” 39 U.S.C. § 3622(b)(6). With regard to transparency, ABA and NPPC *et al.* both concede that reporting requirements generally promote transparency, although both commenters believe that reporting requirements alone are not sufficient with regard to the Postal Service’s cost-reduction and efficiency improvement efforts.²⁹²

With regard to administrative burden, NPPC *et al.* state that “more reporting requirements are in tension with Objective 6’s goal of minimizing administrative burdens.” NPPC *et al.* Comments at 24. ANM *et al.* assert that “without...sanctions, reporting requirements simply increase the administrative burden on [the Postal Service] and distract it from efforts to improve its service performance.” ANM *et al.* Reply Comments at 19 n.15. The Postal Service likewise asserts that “oversight of [its] capital investments and cost-reduction initiatives would serve little purpose but to increase administrative burden.” Postal Service Comments at 59. The Postal Service states that this is particularly true with regard to planned projects that will require a DAR, but do not yet have one. Postal Service Comments at 61-62. The Postal Service explains that “[p]rojects that are under consideration but do not yet have a DAR are so predecisional that the information is not ‘already collected’ or ‘already produced internally’...,” as contemplated in Order No. 5337. *Id.* at 62 (citing Order No. 5337 at 229, 231). Therefore, the Postal Service maintains that having to prepare summary reports with regard to such projects would result in administrative burden. *Id.* at 61-62.

²⁹² ABA Comments at 16; NPPC *et al.* Reply Comments at 13.

C. Commission Analysis of Comments

1. The Necessity of the Proposed Reporting Requirements

The Postal Service maintains that it does not need any additional incentive to pursue cost reductions and/or efficiency improvements under a price cap-based ratemaking system. However, the Postal Service has been operating under a price cap-based ratemaking system throughout the PAEA era, but, as the Commission has found, cost reductions and efficiency improvements have not been maximized.²⁹³ This undermines the Postal Service's argument that the price cap alone has been sufficient to maximize the incentive to reduce costs and increase efficiency. Given that the price cap adjustments being adopted in this order will result in additional rate authority for the Postal Service, the Commission finds that additional cost monitoring is prudent in order to ensure that the Postal Service is focusing on maximizing all possible cost reductions. This cost monitoring is also intended to provide additional transparency to the Commission and postal stakeholders as to why the Postal Service has struggled to

²⁹³ Order No. 4257 at 226. As discussed in Order No. 4257, the Postal Service's cost reduction initiatives have repeatedly failed to realize the level of cost savings projected by the Postal Service. Order No. 4257 at 200-203. See, e.g., Docket No. N2012-1, Advisory Opinion on Mail Processing Network Rationalization Service Changes, September 28, 2012, at 92, 111, (concluding that the Postal Service overestimated the potential for transportation cost savings as part of its Network Rationalization initiative); United States Postal Service Office of Inspector General, *Operational Window Change Savings*, Report Number NO-AR-19-001, October 15, 2018, at 1 (finding that the Postal Service only achieved about 18 percent of the cost savings it projected from the second phase of its Network Rationalization initiative in FY 2016 and FY 2017, and that the Officer of Inspector General was only able to verify 5.6 percent of that amount).

achieve adequate cost reductions, as well as to address past concerns regarding the quality of the Postal Service's cost savings estimates.²⁹⁴ Although the Commission disagrees with NPPC *et al.*'s characterization of the proposed price cap adjustment factors that are intended to address exogenous costs and are consistent with price cap theory as "convert[ing] the regulatory system into a cost-of-service system," the Commission finds merit in the call for additional oversight of this issue by the regulator. NPPC *et al.* Reply Comments at 46. The cost-reduction reporting requirements are intended to facilitate such oversight.

2. Risk of Commercial Harm

The Commission finds the concerns the Postal Service raises with regard to the risk of commercial harm stemming from public disclosure of sensitive commercial information to be potentially valid. However, under existing Commission procedures, the Postal Service can file such information nonpublicly and request that it be held under seal. See 39 C.F.R. part 3011. The Commission finds that its current rules in 39 C.F.R. part 3011 provide adequate protection for Postal Service information filed with the Commission that the Postal Service identifies as commercially sensitive.

²⁹⁴ The Postal Service also argued in its comments that the reporting requirements were unnecessary in light of the Performance-Based Rate Authority proposed in Order Nos. 4258 and 5337, which was also intended to provide the Postal Service with an incentive to reduce costs and increase efficiency. Postal Service Comments at 58-59. As discussed in Section VI.C., *supra*, the Commission has determined to defer consideration of the proposed Performance-Based Rate Authority to a separate strategic rulemaking proceeding. Nevertheless, the Commission notes that the cost-reduction reporting requirements addressed in this section and the issues to be considered in the strategic rulemaking serve different, albeit related, purposes. The cost-reduction reporting requirements are designed to incentivize the Postal Service to improve the robustness of its cost-benefit analyses, which is intended to provide a mechanism to better ensure that the Postal Service's operational decisions are supported by thorough analysis, thereby encouraging prudent and financially sound decision-making. The strategic rulemaking proceeding that the Commission is initiating will focus on further enhancements to the ratemaking system that not only amplify the Postal Service's incentives to reduce costs and increase efficiency, but also enhance the Postal Service's ability to address its longer-term financial challenges. See Section VI.C., *supra*.

3. Whether Reporting Requirements Alone Provide a Sufficient Incentive

With regard to comments that the Postal Service should be penalized in the form of sanctions or reduced rate authority for failing to achieve sufficient cost reductions or efficiency improvements, as stated in Section VI.C., *supra*, the Commission will be initiating a strategic rulemaking proceeding in a separate docket to consider such issues. Specifically, that proceeding will focus on cost-reduction issues in conjunction with service, efficiency, and long-term finances in order to determine if further modifications to the ratemaking system are desirable. The purpose of these reporting requirements is to provide transparency over the breadth of the Postal Service's innovative projects.

Moreover, the Commission disagrees with commenters who assert that the reporting requirements the Commission is adopting will not provide any incentive to reduce costs. While the primary purpose of the cost-reduction reporting requirements is to increase transparency and incentivize the Postal Service to improve the robustness of its cost-benefit analyses,²⁹⁵ the reporting requirements will also drive the Postal Service to identify underlying causes of cost increases, which should enable it to undertake targeted responses to those causes. The reporting requirements have the additional benefit of allowing the Commission to investigate cost increases more thoroughly as part of the annual ACD process or as part of a rulemaking proceeding,

²⁹⁵ As discussed in Order No. 4257, the Postal Service's cost reduction initiatives have repeatedly failed to realize the level of cost savings projected by the Postal Service, and the Postal Service has struggled at measuring cost savings from its initiatives. Order No. 4257 at 200-203. See, e.g., Periodicals Mail Study, Joint Report of the United States Postal Service and Postal Regulatory Commission, September 2011, at 97, available at: https://www.prc.gov/docs/76/76767/Periodicals%20Mail%20Study_final_2131_2149.pdf (noting the Postal Service's "inability to capture efficiencies in flat mail processing," and stating that "[o]ver the past decades the Postal Service has introduced many programs to capture some of these efficiencies," but it was "unclear how successful these programs had been."); Docket No. RM2018-5, Order Approving In Part Proposal Two, January 8, 2019, at 30 (Order No. 4972) (denying proposed methodological components because the Postal Service was unable to determine the impact of the proposed changes).

which could lead to further information requests or proceedings if the Commission identifies areas where cost-reduction efforts have been insufficient or have not been realized as intended.²⁹⁶

4. Recommended Changes to Proposed Reporting Requirements

Commenters proposed changes to the cost-reduction reporting requirements that include prior review of cost-reduction initiatives by the Commission, increased reporting thresholds and mid-implementation reports with respect to DARs, and an exemption from required summary reporting for planned DARs. With regard to comments asserting that the Commission should engage in prior review of the Postal Service's cost-reduction initiatives and capital expenditure programs, the Commission explained in Order No. 5337 that it did not intend to engage in such prior review. Regulators have imperfect information about the cost-reduction efforts available to a regulated firm, and as a result, the Commission found that requiring prior approval could hinder, rather than improve, the efficiency of cost-reduction efforts. Order No. 5337 at 226.

With regard to comments that mid-implementation reports should be required for DAR summary reports, under the rules being adopted, the Commission intends to use DAR summary reports mainly as supplements to the more in-depth Cost-Reduction Initiative Reports. The Cost-Reduction Initiative Reports will address larger and more substantial projects with greater opportunities for cost savings and efficiency improvements, while the DAR summary reports will give the Commission visibility at a high level into smaller cost-reduction projects. It is for this reason that the Commission is limiting DAR reporting requirements to summary information, while more extensive

²⁹⁶ For example, the Postal Service in Docket No. RM2016-11 withdrew its petition for a proposed methodological change having to do with costs after the Commission identified several potential issues with the proposal, including that it could potentially understate or misallocate time and associated costs, possibly resulting in a large increase in training costs. See Docket No. RM2016-11, Order Closing Docket, October 7, 2016, at 8 (Order No. 3559).

reporting is being required for Cost-Reduction Initiative Reports. For example, for a Cost-Reduction Initiative Report, the Postal Service will be required to file data comparing actual changes in unit costs with expected changes in unit costs throughout the duration of a project, while for DAR summary reports, the Postal Service will only be required to detail the expected cost savings (or additional revenues) of a capital spending project in the current and next fiscal year, without providing analysis of the project's impact on Market Dominant costs or any reasons for deviations between projections and actual figures.²⁹⁷ Because of the detail required for Cost-Reduction Initiative Reports and the differing levels of depth expected for Cost-Reduction Initiative Reports and DAR summary reports, the Commission finds it unnecessary to expand the scope of DAR summary reports at this time, by, for example, requiring mid-implementation reports. Information requests can, if warranted, be issued to gather more information about a specific DAR project.

Likewise, because DAR summary reports are not intended to be as in-depth as Cost-Reduction Initiative Reports, and because the administrative burden associated with producing DAR summary reports is considerably less, the Commission does not find it necessary to implement an increased threshold for having to disclose DAR summary reports as the Postal Service suggests. Additionally, if the reporting threshold for DAR summary reports were increased to \$5 million, it is likely that the same projects

²⁹⁷ Specifically, the Postal Service will be required to provide the following information for all projects associated with a DAR in the current or next fiscal year: descriptions of the projects; status of projects; estimates of cost savings or additional revenues for each project; and the expected return on investment from each project. Order No. 5337 at 231. For each active cost-reduction initiative above the \$5 million threshold, however, the proposed rules will require the Postal Service to file actual data detailing the impact of the cost-reduction initiative on its selected metric, as well as the impact on Market Dominant unit costs and total unit costs. Then, the Postal Service will be required to compare the actual results to the expected results, and to provide a narrative explaining any variance along with a specific statement as to whether the initiative actually achieved the expected impact as measured by the selected metric. Finally, the Postal Service will be required to provide a description of any mid-implementation adjustments made to align actual results to expected results, as well as identify any revisions to expected results for future fiscal years. *Id.* at 230-231.

would be identified under both reports. This would eliminate transparency with regard to smaller projects.

With regard to the Postal Service's concern about having to prepare summary reports for planned DARs, the Commission finds the Postal Service's position to be reasonable. It was not the intent of the Commission for the Postal Service to be required to provide pre-decisional information. The Commission has therefore revised § 3050.55(f) to clarify that the Postal Service will only be required to provide summary information with regard to projects that have an approved DAR for the next fiscal year.

5. Tension with Objective 6

With respect to comments concerning administrative burden, administrative burden must be balanced with increased transparency, which is also a goal of Objective 6. See 39 U.S.C. § 3622(b)(6). The Commission has concluded that the benefits to be gained from increased transparency with respect to the Postal Service's cost-reduction initiatives outweigh the burden associated with having to compile reports containing data and information that are already produced and available to the Postal Service. The sole potential exception to this—planned projects which have not yet been formalized into a final DAR—is addressed by the revision the Commission is making to § 3055.55(f). Those revisions clarify that the Postal Service does not have to provide information with regard to planned projects that have not yet been formalized into a final DAR, which should eliminate any concern about having to provide information that is not “already produced internally[.]” Postal Service Comments at 62.

D. Revisions to Proposed Rules

The Commission is revising § 3050.55(f) to clarify that the Postal Service will only be required to provide summary information with regard to projects that have an approved DAR for the next fiscal year. The Commission otherwise adopts the proposed rules from Order No. 5337 related to cost-reductions reporting without changes.

X. PROCEDURAL IMPROVEMENTS

A. Introduction

Order No. 4258 proposed two procedural changes to improve the ratemaking process related to planned rate adjustments of general applicability. These changes are within the scope of the Commission's general authority to revise its regulations under 39 U.S.C. §§ 3622(a) and 503. Order No. 4258 at 98. First, the Commission proposed to enhance rules regarding the Schedule for Regular and Predictable Rate Adjustments (Schedule). *Id.* at 99-102. Existing 39 C.F.R. § 3030.509 requires the Postal Service to "maintain on file with the Commission a Schedule for Regular and Predictable Rate Adjustments." 39 C.F.R. § 3030.509(a). The Schedule must be updated "[w]henever the Postal Service deems it appropriate to change" by filing a revised Schedule and explanation with the Commission. *Id.* § 3030.509(e).

In Order No. 4258, the Commission proposed requiring the Postal Service to update the Schedule at least once a year (at a minimum, when it files the ACR). Order No. 4258 at 101. The proposed rules required the Schedule to (1) schedule rate adjustments at specific regular intervals and (2) include plans to adjust rates that may occur over the next 3 years, at a minimum. *Id.*; *id.* Attachment A at 5-6. Specifically, the Postal Service must include the estimated filing and implementation dates (month and year), as well as an explanation that would allow mailers to predict with reasonable accuracy, by class, the amounts of future rate adjustments. Order No. 4258 at 101. The Postal Service would retain the flexibility to file a new Schedule at any time and may deviate from the anticipated rate changes if it provides an explanation in its rate adjustment filing. *Id.*

Second, the Commission proposed revising the procedural schedule for rate adjustment proceedings. *Id.* at 102-106. The proposed rules lengthened the notice period for rate adjustments and made conforming adjustments to the timing requirements for the comments and a Commission decision. *Id.* The proposed rules

extended the notice period for rate adjustments from 45 days to 90 days before the planned implementation of rates. *Id.* at 104. The proposed rules extended the comment deadline from 20 to 30 days for an initial request to review planned rate adjustments. *Id.* For an amended request, the proposed rules extended the comment deadline from 7 to 10 days. *Id.*

The proposed rules also lengthened the time period for rendering a Commission decision from 14 to 21 days after the comment period ends for both initial and amended requests. *Id.* The proposed rules enumerated potential actions the Commission may take following its determination that the Postal Service's rate adjustment filing failed to include the information required by the Commission's rules. *Id.* at 104-105.

In Order No. 5337, the Commission issued revised proposed rules concerning the two procedural changes described above. Order No. 5337 at 238-239. The revised proposed rules retained the substance and structure of the rules proposed in Order No. 4258 and only included non-substantive changes made for clarity, global consistency, and terminology. *Id.* The Commission revised other proposed procedural rules to conform to changes proposed in Order No. 5337. *Id.* at 239. For example, the revised definitions, which appear in revised § 3030.101, reflected the new forms of rate authority proposed in Order No. 5337 (density-based rate authority and retirement obligation rate authority). *Id.* Revised § 3030.123 described the supporting technical documentation the Postal Service must include with its rate adjustment filing, which contained the same requirements as the proposed rules, but added the requirement that the Postal Service designate how much of each type of rate adjustment authority it plans to use for each class. *Id.*

The revised proposed rules in Order No. 5337 also proposed to discontinue addressing the objectives and factors of 39 U.S.C. § 3622(b) and (c) in individual rate adjustment proceedings. *Id.* at 239-240. While the Commission proposed to require the Postal Service to consider the provisions of 39 U.S.C. chapter 36 in its rate design,

the Commission also proposed to discontinue requiring the Postal Service to report its underlying justification for proposed rates vis-à-vis the objectives and factors of 39 U.S.C. § 3622(b) and (c). *Id.* at 245.

The following discussion summarizes the comments received concerning the Commission's revised proposed procedural rules, provides analysis responding to comments received, and describes the changes made to the proposed rules.

B. Comments

None of the commenters discuss the proposed enhancements to the Schedule. Several commenters discuss the proposed revisions to the rate adjustment notice period, the Commission review periods, the discussion of objectives and factors, and other changes to the procedural schedule for rate adjustment proceedings. Each topic is discussed below.

1. Rate Adjustment Notice Period

Pitney Bowes, NPPC *et al.*, and GCA support extending the rate adjustment notice period from 45 to 90 days.²⁹⁸ Pitney Bowes and NPPC *et al.* observe that codifying the 90-day notice requirement largely conforms to the Postal Service's current practice. Pitney Bowes Comments at 8; NPPC *et al.* Comments at 76. PSA comments that extending the notice period to 90 days would somewhat reduce the Postal Service's pricing flexibility. PSA Revised Comments at 9.

²⁹⁸ Pitney Bowes Comments at 8; NPPC *et al.* Comments at 76; GCA Comments at 3.

2. Commission Review Periods

Pitney Bowes states that extending the Commission's review period "will enable a more thorough review by the Commission and, thus, will facilitate improved accountability consistent with Objectives 2 and 6." Pitney Bowes Comments at 8.

The Postal Service opposes the proposed changes to the Commission review periods for initial and amended rate adjustment filings. Postal Service Comments at 53. It observes that the proposed rules would create a separate pre-rate adjustment filing proceeding to consider waiver requests for workshare discounts. *Id.* The Postal Service notes that interested persons would have at least 7 days to submit comments, and the pre-rate adjustment filing proceeding would resolve issues related to workshare discounts before the rate adjustment proceeding. *Id.* The Postal Service comments that the proposed rules would streamline rate adjustment proceedings because they would not require an analysis of the statutory objectives and factors. *Id.* Because the proposed rules would address workshare discount issues in a separate proceeding and remove the requirement to consider the objectives and factors, the Postal Service asserts that the subject matter of rate adjustment proceedings under the proposed rules would be substantially narrower compared to the current rules. *Id.* Thus, it concludes that the Commission should maintain or reduce rather than extend the rate adjustment filing review periods. *Id.* at 54-55.

The Postal Service asserts that extending the Commission review period for amended rate adjustment filings would not provide sufficient time for rate certainty before implementation. *Id.* at 54. It comments that both mailers and the Postal Service need a final order on rate adjustments before programming and testing the software changes necessary to implement a rate adjustment. *Id.* The Postal Service notes that under the current rules, it must file a notice of rate adjustment at least 106 days before rates are implemented to ensure that the Commission issues a final order at least 45 days before implementation. *Id.* It observes that the proposed rules would require the

Postal Service to file a notice of rate adjustment at least 130 days before rates are implemented. *Id.* It asserts that filing a notice that far in advance could push back the hybrid year used in the rate filing, which could result in a loss of billing determinant data reflecting current prices and shorten the time for preparing and presenting the filing to the Board of Governors. *Id.* at 54-55. It concludes that lengthening the procedural schedule for rate adjustment proceedings “either would cause a cascade of disruptive effects on mailers and the Postal Service or could deprive the Postal Service Governors and the Commission of important data.” *Id.* at 55.

The Postal Service asserts that Order No. 5337 fails to justify the proposed extensions of the Commission review periods for initial and amended rate adjustment filings. *Id.* at 53-54. It acknowledges that some parties may support the proposed changes to the procedural rules, but notes that no interested person sought to extend the rate adjustment review periods or provided a clear justification for doing so. *Id.* at 55. It asks that the Commission either retain or shorten the review periods for initial and amended rate adjustment filings. *Id.* at 54-55.

3. Discussion of Objectives and Factors

ABA, GCA, NPPC *et al.*, and Pitney Bowes argue that *Carlson v. Postal Regulatory Commission*²⁹⁹ does not allow the Commission to disregard the objectives and factors when reviewing proposed rate adjustments, asserting that *Carlson* did not find the PAEA to be ambiguous on this issue.³⁰⁰ NPPC *et al.* assert that “the Court only partly relied on the text of the current regulation, but also rested its decision on the text of the PAEA and the APA^[301].” NPPC *et al.* Comments at 77 n.75. Therefore, they

²⁹⁹ *Carlson v. Postal Reg. Comm’n*, 938 F.3d 337 (D.C. Cir. 2019).

³⁰⁰ ABA Comments at 17-18; GCA Comments at 2-3, 5; NPPC *et al.* Comments at 77-78; Pitney Bowes Comments at 9-10.

³⁰¹ Administrative Procedure Act, Pub. L. 79-404, 60 Stat. 237 (1946) (codified at 5 U.S.C. §§ 500 *et seq.*).

contend that “even if the Commission were to delete from its procedures governing market-dominant rate adjustments the specific references to the Objectives and Factors, it would continue to have an obligation to address them in approving rates, and particularly those raised in public comments.” *Id.* at 77. GCA and NPPC *et al.* assert that relieving the burden on the Postal Service to provide a justification of its proposed rate adjustments improperly shifts the burden of proof to the ratepayer to show that an approved rate (post-implementation) is unreasonable, contrary to an express concern of *Carlson*.³⁰²

GCA also comments that extending the notice period to 90 days “means that consideration of the objectives and factors is not infeasible” and that the Commission cannot postpone addressing these issues in complaint or Annual Compliance Review proceedings. GCA Comments at 3, 5. It states that considering the objectives and factors “will become even more practicable” if the Commission adopts the revised proposed rules concerning waivers for workshare discounts. *Id.* at 3-4.

Further, multiple commenters find it difficult to reconcile discontinuance of reviewing the objectives and factors in individual rate adjustment proceedings with the thrust of the Commission’s modified system: granting additional forms of rate authority above the existing CPI-U price cap.³⁰³ ABA and Pitney Bowes express concern that discontinuing review for consistency with the relevant objectives and factors is incompatible with the PAEA’s titular aim to enhance accountability. See ABA Comments at 17; Pitney Bowes Comments at 10-11. They also argue that the Commission has not provided an adequate policy rationale for reversing its position with

³⁰² Compare GCA Comments at 5, and NPPC *et al.* Comments at 78 n.76, with *Carlson*, 938 F.3d at 350.

³⁰³ See ABA Comments at 18; GCA Comments at 4; Pitney Bowes Comments at 10-11.

regard to the breadth of the review of rate adjustments. See ABA Comments at 18; Pitney Bowes Comments at 10.

The Postal Service supports the Commission's proposal to discontinue addressing the objectives and factors because it contends that *Carlson* should be interpreted as narrowly as possible and that review by the Commission prior to implementation of the planned rates (pre-implementation review) is unnecessary. See Postal Service Reply Comments at 45-48.

4. Other Procedural Changes to Rate Adjustment Proceedings

Pitney Bowes comments that the proposed procedural changes to rate adjustment proceedings should be adopted as proposed because they will improve procedural regularity and transparency. Pitney Bowes Comments at 2, 11. It observes that extending the public comment period will encourage more meaningful participation by interested persons. *Id.* at 8. Pitney Bowes also supports the proposed changes clarifying Commission responses to incomplete filings because they will help facilitate the administration of the ratemaking process. *Id.*

C. Commission Analysis of Comments

1. Rate Adjustment Notice Period

Pitney Bowes, NPPC *et al.*, and GCA support extending the rate adjustment notice period from 45 to 90 days.³⁰⁴ Pitney Bowes and NPPC *et al.* observe that codifying the 90-day notice requirement in the revised proposed rules largely conforms to the Postal Service's current practice. Pitney Bowes Comments at 8; NPPC *et al.* Comments at 76.

³⁰⁴ Pitney Bowes Comments at 8; NPPC *et al.* Comments at 76; GCA Comments at 3.

To facilitate the administration of rate adjustment proceedings, the final rules extend the rate adjustment notice period to 90 days. In Order No. 4257, the Commission determined that rate adjustment proceedings were consistently able to be adjudicated within 90 days. Order No. 4257 at 72. In eight of the rate adjustments for all classes during the PAEA era, the Postal Service filed the notice of rate adjustment at least 90 days before the planned implementation date. *Id.* at 63. Pitney Bowes and NPPC *et al.* note that extending the notice period from 45 to 90 days codifies this existing practice and facilitates the administration of rate adjustment proceedings.³⁰⁵ Ninety days' advance notice should also facilitate mailers' ability to generate budgets, allow adequate time for rate adjustment proceedings to be adjudicated, and give mailers time to implement the rates as planned. Order No. 4258 at 104.

PSA comments that extending the notice period to 90 days would somewhat reduce the Postal Service's pricing flexibility. PSA Revised Comments at 9. In Order No. 4257, the Commission found that the pricing flexibility may be limited "as long as the Postal Service has some flexibility to set prices, the price structure, and the timing of price changes." Order No. 4257 at 91. The final rules continue to allow the Postal Service pricing flexibility. Under the final rules, the Postal Service has the authority to propose rates, determine the magnitude of rate increases, and decide the timing and frequency of rate adjustments. Final § 3030.509 reflects the Postal Service's pricing flexibility to revise the Schedule and vary the magnitude with an explanation. See Order No. 5337 at 238. Given that a 90-day notice period is consistent with past practice, the Commission finds any effects on the Postal Service's pricing flexibility to be negligible and outweighed by the benefits to the mailers and adjudicative process.

³⁰⁵ Pitney Bowes Comments at 8; NPPC *et al.* Comments at 76; see Order No. 4258 at 104.

2. Commission Review Periods

In Order No. 4257, the Commission analyzed the duration of eight non-exigent Market Dominant rate adjustment proceedings during the PAEA era. Order No. 4257 at 71. The Commission found that these large-scale rate adjustment proceedings lasted an average of 62 days. *Id.* at 72. In six of these eight proceedings, there were significant issues with the Postal Service's rate adjustment filings resulting in durations of between 58 and 112 days. *Id.*

The Postal Service asserts that the subject matter of rate adjustment proceedings under the revised proposed rules would be narrower compared to the existing rules because workshare discount issues would be addressed in a separate proceeding, and the objectives and factors would not need to be considered.³⁰⁶ However, longer Commission review periods during the PAEA era were necessary due to deficiencies in the Postal Service's filings that required corrections to resolve the proceedings—not issues specific to worksharing or consideration of the objectives and factors. See Order No. 4257 at 98. For example, in Docket No. R2017-1, the Postal Service filed a notice of rate adjustment on October 12, 2016.³⁰⁷ On November 15, 2016, the Commission issued an order approving the rate adjustments for each class of mail except for Special Services.³⁰⁸ Rate adjustments for Special Services were not approved until December 15, 2016, "[d]ue to delays in receiving the information

³⁰⁶ Postal Service Comments at 53. The Commission notes that the Postal Service is only partially correct that workshare discount issues would be addressed in a separate proceeding. The worksharing rules create a waiver process that would adjudicate some workshare discounts in advance of a rate adjustment proceeding. Proposed § 3030.286. However, review of workshare discounts for compliance with other Commission regulations would continue to occur within a rate adjustment proceeding. See, e.g., proposed §§ 3030.283, .284, .285.

³⁰⁷ Docket No. R2017-1, United States Postal Service Notice of Market Dominant Price Adjustment, October 12, 2016.

³⁰⁸ Docket No. R2017-1, Order on Price Adjustments for First-Class Mail, Standard Mail, Periodicals, and Package Services Products and Related Mail Classification Changes, November 15, 2016 (Order No. 3610).

necessary to complete [the Commission's] review and the complexity of classification changes proposed by the Postal Service...." Order No. 3610 at 2. There were other delays because the Postal Service filed two errata to the notice of rate adjustment and did not finalize its rate adjustment until December 6, 2016.³⁰⁹ The Postal Service also submitted imprecise and inadequate workpapers, which included billing determinants that differed from those submitted to the Commission in quarterly reports. Order No. 3670 at 2. Consequently, this proceeding lasted 64 days. See Order No. 4257 at 72.

As another example, in Docket No. R2015-4, the Commission remanded rates for USPS Marketing Mail, Periodicals, and Package Services twice because the proposed rate adjustments did not comply with certain statutory and regulatory requirements, and the Postal Service did not provide the information necessary to calculate the average rate increase for Package Services.³¹⁰ The Postal Service's first two rate adjustment filings contained many errors and inconsistencies, lacked the information required by title 39 and the Commission's regulations, and required 16 Chairman's Information Requests to attempt to cure the deficiencies.³¹¹ Also, before

³⁰⁹ *Id.* at 1 n.1; Docket No. R2017-1, Order on Price Adjustments for Special Services Products and Related Mail Classification Changes, December 15, 2016, at 2 (Order No. 3670).

³¹⁰ Docket No. R2015-4, Order on Price Adjustments for Standard Mail, Periodicals, and Package Services Products, March 6, 2015, at 2-3 (Order No. 2378); Docket No. R2015-4, Order on Amended Price Adjustments for Standard Mail, Periodicals, and Package Services Products, March 18, 2015, at 2 (Order No. 2398).

³¹¹ See Docket No. R2015-4, Order on Revised Price Adjustments for Standard Mail, Periodicals, and Package Services Products and Related Mail Classification Changes, May 7, 2015, at 5-6 (Order No. 2472).

the Commission remanded the rate adjustments, the Postal Service filed several revisions to the initial notice of rate adjustment, which caused further delays.³¹² These issues were caused by the insufficiency of the Postal Service's filings rather than the need to analyze workshare discounts and the objectives and factors. This proceeding lasted 112 days.

The revised proposed rules were designed to address the issues encountered during the previous large-scale rate adjustment proceedings. Under proposed § 3030.126, the Commission completes its initial review of a proposed rate adjustment within 51 days. If the planned rate adjustments are consistent with applicable law, they may take effect. Proposed § 3030.126(c). If, however, the planned rate adjustments are found inconsistent with applicable law, the Commission would have 31 days to review an amended rate adjustment filing. Proposed § 3030.126(f), (g). These timelines balance the needs of the Postal Service for expeditious review with the need to allow adequate time for thorough vetting of the planned rate adjustments by commenters and the Commission.

Further, there is no question that the Commission has the discretion to determine such timelines. In *Carlson*, the court stated that “[t]he PAEA is silent about the amount of time the Commission may take *during* its review...[and] Congress did not limit the scope and duration of the Commission’s review....” *Carlson*, 938 F.3d at 349 (emphasis in original).

³¹² Docket No. R2015-4, Notice of Revision to United States Postal Service Notice of Market-Dominant Price Adjustment, Attachment A, Part II -- Errata, February 27, 2015; Docket No. R2015-4, Notice of Revision to United States Postal Service Notice of Market-Dominant Price Adjustment, Attachment A, Part II -- Errata, February 20, 2015; Docket No. R2015-4, Notice of Revisions to United States Postal Service Notice of Market-Dominant Price Adjustment, Attachments A and D -- Errata, February 6, 2015; Docket No. R2015-4, Notice of Revisions to United States Postal Service Notice of Market-Dominant Price Adjustment, Attachment A -- Errata, February 4, 2015.

The Postal Service asserts that extending the Commission review period for amended rate adjustment filings would not provide sufficient time for rate certainty before implementation. Postal Service Comments at 54. It states that the lengthened procedural schedule could either disrupt mailers' and the Postal Service's implementation of the new rates or deprive the Board of Governors and the Commission of important data. *Id.* at 55. With regard to potential disruption to rate implementation, as the Commission noted above, historically, rate adjustment proceedings have been lengthened due to the Postal Service's prior notices of rate adjustment being deficient. Amended rate adjustment filings will likely be unnecessary if the Postal Service submits all required information in the initial filings and that information is precise and accurate. Also, the revised proposed rules provide the Postal Service the option to submit a rate adjustment filing with more than 90 days' notice. By exercising this option, the Postal Service will be able to address its concern that it has sufficient time to address a remand prior to the planned implementation date.

The Postal Service asserts that filing a notice that far in advance could result in a loss of billing determinant data reflecting current prices and shorten the time for preparing and presenting the filing to the Board of Governors. Postal Service Comments at 54-55. First, under the current filing requirements, more recent billing determinant data can become available during rate adjustment proceedings.³¹³ As a practical matter, the time necessary to compile and report billing determinants, prepare and present a filing to the Board of Governors, and provide customers with advance notice of a price change limit the availability of billing determinant data that reflect current prices. The Postal Service has not raised this issue during PAEA-era rate adjustment proceedings, which suggests that this is not a major issue. The billing

³¹³ See Order No. 2472; United States Postal Service, Market Dominant Billing Determinants, Quarter 1, FY 2015, March 27, 2015.

determinants used in a rate case cover a 12-month period that typically ends more than 60 to 90 days prior to the filing.³¹⁴ In this context, increasing the time between filing and implementation by 24 days is unlikely to substantially reduce the availability of billing determinant data that reflect current prices.³¹⁵ Furthermore, the Postal Service provides no evidence that shifting one quarter of billing determinant data will have a major impact on the price cap calculations.

One of the important questions the Commission had to determine when implementing the regulations required by the PAEA was whether to apply the price cap to a forward-weighted or backward-weighted index of prices. From a technical perspective, the Commission had to choose between using the most recent historical billing determinant information and developing a forecast of future volumes at the proposed prices to calculate the aggregate percentage increase in prices for each class of mail. The vast majority of the commenters, including the Postal Service, supported

³¹⁴ 39 C.F.R. § 3030.523(d)(1) instructs the Postal Service to use “the most recent available 12 months of Postal Service billing determinants” to calculate the percentage change in rates. The Commission’s periodic reporting rules require the Postal Service to provide “[b]illing determinants within 60 days of the close of Quarters 1, 2, and 3 of the fiscal year and 90 days after Quarter 4.” 39 C.F.R. § 3050.25(e).

³¹⁵ The Postal Service asserts that the proposed timeline for review would necessitate filing 130 days before implementation, in contrast to 106 days under the current review timeline. Postal Service Comments at 54.

using a backward-weighted index that applied the most recent historical billing determinants.³¹⁶ The Commission has periodically evaluated the impact of using historical information compared to the actual volumes at the new prices. See FY 2008-FY 2012 ACD, Appendix A. This evaluation showed that the differential between the two sets of billing determinants was minimal. *Id.* Although there is no reason to expect that the reasonableness of using the historical determinants would be changed by the modified system implemented by these rules, the Postal Service may petition the Commission for a rulemaking should it find the billing determinants are no longer the most appropriate weights to use.

3. Discussion of Objectives and Factors

Multiple commenters contend that the PAEA unambiguously requires the Commission's pre-implementation review of the Postal Service's planned rate adjustments to explicitly consider the objectives and factors of 39 U.S.C. § 3622(b) and (c).³¹⁷ There is no textual support for this proposition. As reiterated below, the Commission has authority to construe how to apply the provisions of 39 U.S.C. § 3622, including paragraphs (b), (c), and (d)(3). Order No. 5337 at 239-240.

³¹⁶ See Docket No. RM2007-1, Order Proposing Regulations to Establish a System of Ratemaking, August 15, 2007, ¶¶ 2071-2072 (Order No. 26); Docket No. RM2007-1, Errata to Order No. 26, August 16, 2007 (Order No. 27); see also Docket No. RM2007-1, Initial Comments of Pitney Bowes Inc. in Response to Advance Notice of Proposed Rulemaking on Regulations Establishing A System of Ratemaking, April 6, 2007, at 7-8; Docket No. RM2007-1, Initial Comments of the United States Postal Service, April 6, 2007, at 27-28; Docket No. RM2007-1, Direct Marketing Association, Inc. Initial Comments Pursuant to PRC Order No. 2, April 6, 2007, at 4; Docket No. RM2007-1, Comments of Advo, Inc. in Response to Advance Notice of Proposed Rulemaking on Regulations Establishing A System of Ratemaking; April 6, 2007, at 4; Docket No. RM2007-1, Initial Comments of Pitney Bowes Inc. in Response to Second Advance Notice of Proposed Rulemaking on Regulations Establishing a System of Ratemaking, June 18, 2007, at 3-4.

³¹⁷ See GCA Comments at 2; NPPC *et al.* Comments at 77; see also ABA Comments at 17-18; Pitney Bowes Comments at 9-10.

The PAEA charges the Commission with the establishment and periodic revision of the contours of a modern ratemaking system. 39 U.S.C. § 3622(a). On October 29, 2007, the Commission established the system through a notice-and-comment rulemaking proceeding³¹⁸ and has periodically revised the system through subsequent rulemakings.³¹⁹ The PAEA also requires that the Commission conduct a 10-year review of the existing system to determine if the system is achieving the objectives of § 3622(b). 39 U.S.C. § 3622(d)(3). The factors of § 3622(c) must be taken into account in the determination of whether the system is achieving the objectives. *Id.* If the Commission determines that the system is not achieving the objectives, taking into account the factors, then the Commission may modify or adopt an alternative system as necessary to achieve the objectives. *Id.* The Commission initiated the review in this docket and determined that the ratemaking system has not achieved the objectives, taking into account the factors. Order No. 4257 at 275.

The qualitative criteria encapsulated in the objectives and factors are unambiguously relevant to the design of the Market Dominant ratemaking system as a whole and have been taken into account in past rulemaking proceedings under 39 U.S.C. § 3622(a) and the instant proceeding under 39 U.S.C. § 3622(d)(3). The PAEA does not require the objectives and factors to be considered in the Commission's pre-implementation review of the Postal Service's planned rate adjustments. Additionally, the PAEA does not unambiguously require the Commission to issue regulations that would require the Commission's pre-implementation review of the Postal Service's planned rate adjustments to explicitly consider the objectives and factors.

³¹⁸ See generally Order No. 43.

³¹⁹ See, e.g., Docket No. RM2009-8, Order Amending the Cap Calculation in the System of Ratemaking, September 22, 2009 (Order No. 303) (amending the rounding convention for the price cap calculation from using one decimal place to using three decimal places). Such periodic revisions are not as far-reaching or extensive as the undertaking pursuant to 39 U.S.C. § 3622(d)(3).

The Commission also disagrees with the arguments that the ruling in *Carlson* precludes the Commission from adopting these regulatory changes.³²⁰ “A court’s prior judicial construction of a statute trumps an agency construction otherwise entitled to *Chevron* deference only if the prior court decision holds that its construction follows from the unambiguous terms of the statute and thus leaves no room for agency discretion.”³²¹ *Carlson* did not rest on the premise that the PAEA unambiguously required the Commission to apply the objectives and factors in rate adjustments or to issue regulations that would require the Commission’s pre-implementation review of the Postal Service’s planned rate adjustments to explicitly consider the objectives and factors.

Carlson focused on the APA violation (finding failure to substantively engage with public comment and rejecting the premise that the 45-day period specified in 39 U.S.C. § 3622(d)(1)(C) could be relied upon to limit the scope of review) and the Commission’s existing regulations,³²² which made the objectives and factors relevant to individual rate adjustments. See *Carlson*, 938 F.3d at 343, 345, 348. Notwithstanding this decision, the Commission has authority to interpret the ambiguity in 39 U.S.C. § 3622 regarding the role of the objectives and factors in pre-implementation rate review, including paragraphs (b), (c), and (d)(3) in promulgating regulations for a modified ratemaking system. *Carlson* acknowledged the discretion of the Commission with regard to setting up a regulatory process to apply the objectives and factors to individual rate

³²⁰ See ABA Comments at 17-18; GCA Comments at 2-3, 5; NPPC *et al.* Comments at 77-78; Pitney Bowes Comments at 9-10.

³²¹ *Nat’l Cable & Telecomms. Ass’n v. Brand X Internet Servs.*, 545 U.S. 967, 982 (2005).

³²² Effective April 20, 2020, the Commission renumbered the applicable regulations, which formerly appeared in 39 C.F.R. part 3010. See Order No. 5407 at 21, Appendix B at 6 (renumbering former 39 C.F.R. §§ 3010.10, .11, and .12 to existing 39 C.F.R. §§ 3030.510, .511, and .512, respectively).

adjustments.³²³ Further, *Carlson* did not evaluate the impact of the Commission's authority under 39 U.S.C. § 3622(d)(3). The Commission's authority under § 3622(d)(3), which includes modification and extends to adoption of an alternative system, is far broader than its authority under § 3622(a).³²⁴ Streamlining the process for rate adjustment dockets is well within the bounds of this authority. Accordingly, it is permissible for the Commission to conclude that its modified ratemaking system will achieve the PAEA's objectives as required under 39 U.S.C. § 3622(d)(3). Therefore, review for consistency with the objectives and factors is unnecessary in individual rate adjustments under the Commission's modified system, which already takes account of the objectives and factors in Docket No. RM2017-3.

ABA, GCA, NPPC *et al.*, and Pitney Bowes assert that particular statements appearing in *Carlson* preclude the Commission from adopting the modified regulatory approach. ABA references that "the Commission must apply the relevant objectives and factors to individual rate adjustments." ABA Comments at 17 (quoting *Carlson*, 938 F.3d at 344) (internal marks omitted). Similarly, NPPC *et al.* assert that the Commission may not "disregard the objectives and factors" when approving rates, because its orders must satisfy the APA requirement to be "reasonably explained," (NPPC *et al.* Comments at 77 (quoting *Carlson*, 938 F.3d at 344) (internal marks omitted); see Pitney Bowes Comments at 9), and that the Commission must "[o]f course" consider "all relevant statutory objectives and factors" raised in public comments. NPPC *et al.* Comments at 78 (quoting *Carlson*, 938 F.3d at 345) (internal marks omitted). However, these statements were based on the existing regulations allowing the objectives and factors to be deemed as relevant to individual rate adjustments, and the particular facts underlying *Carlson* involving the Commission's failure to substantively engage with a commenter

³²³ See *Carlson*, 938 F.3d at 344 ("Congress left the Commission leeway to establish, through regulation, a process for considering the PAEA's objectives and factors. 39 U.S.C. § 3622(a)-(c).").

³²⁴ See Section III.B.1., *supra*; Order No. 5337 at 35-37; Order No. 4258 at 15, 17-18.

that had raised issues with relevant objectives and factors. These statements are inapplicable under the final regulations appearing in this Order, which effectively modify the scope of individual rate dockets to render the objectives and factors to be irrelevant in individual rate dockets and instead address such issues systemically, as intended by the PAEA.

GCA and Pitney Bowes contend certain statements in *Carlson* indicate that the PAEA unambiguously requires the Commission to apply the objectives and factors in rate adjustments. These commenters reference that “[b]ased on the text and structure of the PAEA, [the court] conclude[s] that the PAEA requires consideration of all relevant statutory objectives and factors as part of the regulatory process and does not authorize the Commission to defer evaluation of those objectives and factors until after it approves a rate change.”³²⁵ Similarly, Pitney Bowes references that *Carlson* rejected the premise that consideration of the objectives and factors could be deferred to the annual compliance review process or a complaint as “contrary to the plain language of the statute when read as a whole.” Pitney Bowes Comments at 10 (quoting *Carlson*, 938 F.3d at 350) (internal marks omitted). As described above, the narrow underlying facts and circumstances at issue in *Carlson* support a narrow interpretation of the applicability of these statements.³²⁶

Moreover, this underlying premise rejected in *Carlson* is not at issue in the Commission’s modified ratemaking system. These statements in *Carlson* were directed at examining whether the existing ratemaking system created under 39 U.S.C.

³²⁵ Pitney Bowes Comments at 9 (quoting *Carlson*, 938 F.3d at 343) (internal marks omitted); see GCA Comments at 2 (same); see also *Carlson*, 938 F.3d at 343.

³²⁶ The Commission further observes that no statutory authority was provided for a fundamental mischaracterization underlying *Carlson*: that the Commission sets rates for the Postal Service’s Market Dominant products. See *Carlson*, 938 F.3d at 349 (“Congress did not limit the scope and duration of the Commission’s review, but did charge the Commission with setting rates through rulemaking (rather than adjudication), with the due consideration required by the APA.”). It is plain that the Governors of the Postal Service set rates under the PAEA. See 39 U.S.C. § 404(b).

§ 3622(a) permitted the Commission to defer consideration of the objectives and factors (which under the existing system are relevant to rate adjustment proceedings) to a post-implementation proceeding such as the annual compliance review or complaint process. However, the modified ratemaking system created under 39 U.S.C. § 3622(d)(3) would not defer consideration of the objectives and factors to post-implementation proceedings. Instead, the Commission has specifically designed a modified ratemaking system that properly balances the objectives *in advance* of individual rate adjustments. Therefore, rather than defer consideration to a time after the rates have already been implemented, the Commission has adequately given consideration to the relevant objectives and factors in Docket No. RM2017-3. The regulatory output of this proceeding—the final rules implementing the modified ratemaking system—will govern the Postal Service’s future rate design. Accordingly, each planned rate adjustment governed by that modified system need not be justified individually. Further, as a policy matter, the Commission undertook extensive analysis of the objectives and factors in its 10-year review and the Commission will review the system again in 5 years, subject to Commission discretion to consider aspects of the system sooner, if needed.³²⁷

The Commission disagrees that its modified ratemaking system would improperly shift the burden of proof to the ratepayer to show that an approved rate (post-implementation) is unreasonable, contrary to an express concern raised in *Carlson*. See GCA Comments at 5; NPPC *et al.* Comments at 78 n.76. The final rules implement a modified ratemaking system that adequately gives consideration to the qualitative issues presented by the relevant objectives and factors. These considerations have been balanced by the Commission in this extensive notice-and-comment rulemaking

³²⁷ To clarify, as detailed in Chapter XIII., *infra*, the Commission acknowledges that attempting to realign the price cap system with the objectives, after more than a decade of operation, presents complicated issues that may require further refinement. The Commission maintains that the changes implemented by the final rules are necessary to achieve the objectives and that subsequent review will serve as an adequate safeguard mechanism as well as a checkpoint that is consistent with typical price cap systems.

proceeding in advance of the Postal Service proposing rate adjustments. If the Postal Service proposes a rate adjustment compliant with the final rules, then that planned rate adjustment would be consistent with the objectives and factors. The Postal Service's rate adjustment filing must substantially comply with the requirements of final §§ 3030.122 and 3030.123. See final 39 C.F.R. § 3030.126. A Postal Service proposal to adjust a workshare discount must be supported by substantial evidence and demonstrate compliance with the applicable provisions appearing in 39 U.S.C. § 3622(e) and final subpart J of 39 C.F.R. part 3030. See final 39 C.F.R. § 3030.285(a). A Postal Service application for waiver regarding a workshare discount must be supported by a more rigorous standard: a preponderance of the evidence. See final 39 C.F.R. § 3030.286(b). The modified ratemaking system does not impose any additional burden of proof on ratepayers.

ABA and Pitney Bowes argue that the Commission has not put forth an adequate reason for the change in policy from applying the objectives and factors to individual rate adjustments. See ABA Comments at 18; Pitney Bowes Comments at 10. "Agencies are free to change their existing policies as long as they provide a reasoned explanation for the change."³²⁸ The agency must explain "that the new policy is permissible under the statute, that there are good reasons for it, and that the agency believes it to be better."³²⁹ As stated above, in the description of the narrow applicability of *Carlson*, which was based on a unique set of facts and on the existing regulations, the change is permissible because *Carlson* did not foreclose the Commission from restructuring the regulatory process for applying the objectives and factors to individual rate adjustments and did not consider the Commission's authority under 39 U.S.C. § 3622(d)(3). The Commission's existing system of regulations, which essentially codified

³²⁸ *Encino Motorcars, LLC v. Navarro*, 136 S. Ct. 2117, 2125 (2016) (citing *Brand X Internet Servs.*, 545 U.S. at 981-982).

³²⁹ *FCC v. Fox Television Stations, Inc.*, 556 U.S. 502, 515 (2009) (emphasis omitted); see also *Nat'l Ass'n of Home Builders v. EPA*, 682 F.3d 1032, 1038 (D.C. Cir. 2012).

the quantitative parameters of 39 U.S.C. § 3622 and would not be reviewed for 10 years, needed to incorporate the objectives and factors as a safeguard; however, the modified system does not require such a safeguard. The modified system achieves the objectives as required under 39 U.S.C. § 3622(d)(3). This change simplifies the existing ratemaking process and reduces the administrative burden, consistent with an aim of Objective 6.

The Commission disagrees that discontinuing review for consistency with the relevant objectives and factors is incompatible with the PAEA's titular aim to enhance accountability. See ABA Comments at 17; Pitney Bowes Comments at 10-11. The Commission's design of the modified system specifically includes numerous provisions directly aimed at enhancing accountability. The new forms of rate authority (density rate authority under final subpart D of 39 C.F.R. part 3030, retirement obligation rate authority under final subpart E of 39 C.F.R. part 3030, and non-compensatory rate authority under final § 3030.222) are designed with specific criteria to ensure that any planned usage would be consistent with the PAEA. The rate-setting criteria for non-compensatory products and workshare discounts directly ensure accountability of the Postal Service's pricing decisions with the PAEA. See final subparts G and H of 39 C.F.R. part 3030.

Finally, the contrast between the text of the existing and former statutory provisions supports the interpretation that the PAEA does not require the existing Postal Regulatory Commission to perform pre-implementation adjudications similar to the level of review required by the former Postal Rate Commission under the cost-of-service system of the former Postal Reorganization Act (PRA).³³⁰

Under former 39 U.S.C. § 3621, the Governors of the Postal Service were authorized "to establish reasonable and equitable classes of mail and reasonable and

³³⁰ Pub. L. 91-375, 84 Stat. 719-787 (1970).

equitable rates of postage and fees for postal services.” But, this authority was severely circumscribed by the active role given to the Postal Rate Commission (the predecessor to the existing Postal Regulatory Commission). 39 U.S.C. § 3621 (2000). Former § 3622(a) stated that “[t]he Postal Service may submit such suggestions for rate adjustments as it deems suitable.” 39 U.S.C. § 3622(a) (2000). Under former § 3624(a) and (b), rate adjustments were formally litigated before the Postal Rate Commission in quasi-adjudicatory proceedings taking 10 to 18 months to complete. 39 U.S.C. § 3624(a) and (b) (2000); see Order No. 4257 at 25-31 (describing rate cases under the PRA).

After submission of suggestions by the Postal Service, former § 3622(b) required the Postal Rate Commission to make a “recommended decision” in accordance with the policies of title 39 and eight specific statutory factors. 39 U.S.C. § 3622(b) (2000). Former § 3624(c) required that the Postal Rate Commission’s recommended decision “include a statement specifically responsive to the criteria established under [former] section 3622....” 39 U.S.C. § 3624(c) (2000). For each rate suggested by the Postal Service, the Postal Rate Commission was obliged to exercise its best judgment as to which among a spectrum of lawful rates or classifications was the outcome most consistent with the PRA’s criteria. In almost all cases, the Postal Rate Commission’s decision was a final determination because the PRA provided little scope for change by the Governors under former § 3625. 39 U.S.C. § 3625 (2000).

The Supreme Court characterized PRA-era postal ratemaking as follows:

Although the Postal Reorganization Act divides ratemaking responsibility between two agencies, the legislative history demonstrates “that ratemaking...authority [was] vested primarily in [the] Postal Rate Commission.” S. Rep. No. 91–912, p. 4 (1970) (Senate Report); see *Time, Inc. v. United States Postal Service*, 685 F.2d 760, 771 (CA2 1982); *Newsweek, Inc. v. United States Postal Service*, 663 F.2d at 1200–1201; *NAGCP III*, 197 U.S.App.D.C. at 87, 607 F.2d, at 401. The structure of the Act supports this view.¹⁶

¹⁶ It is the Rate Commission, not the Postal Service, that conducts extensive hearings, § 3624, and applies the ratemaking factors enumerated in § 3622(b). The Postal Service may modify a Rate Commission recommendation only if the recommended rates will not produce revenues equal to the Postal Service's estimated costs. § 3625(d)(2).³³¹

On December 20, 2006, the PAEA was signed into law. Among other things, the PAEA transformed the roles of the Postal Service and the oversight agency—renamed the Postal Regulatory Commission. The PAEA streamlined the Commission's pre-implementation role and expanded the Commission's post-implementation rate review role. The PAEA does not carry forward the former PRA requirements for Commission review of planned rates to be based on the factors enumerated in the statute. *Compare* 39 U.S.C. § 3622, *with* 39 U.S.C. §§ 3622(b), 3624(c) (2000).

Interpreting these differences to support the Commission's decision not to consider the objectives and factors in pre-implementation review is logical because under existing § 404(b), the authority to establish reasonable and equitable classes of mail and rates of postage is vested primarily in the Governors of the Postal Service rather than the Commission. The numerous differences between the PRA and PAEA, which are described above, indicate that the PAEA was intended to streamline the nature and scope of the Commission's pre-implementation review of rates, and that

³³¹ *Nat'l Ass'n of Greeting Card Publishers v. U.S. Postal Serv.*, 462 U.S. 810, 821 (1983).

under the PAEA, consideration of the objectives and factors is required in rulemakings concerning the design of the ratemaking system.

4. Other Procedural Changes to Rate Adjustment Proceedings

Pitney Bowes recommends that the proposed procedural changes to rate adjustment proceedings be adopted as proposed because they will improve procedural regularity and transparency. Pitney Bowes Comments at 2, 11. It also supports the proposed changes clarifying Commission responses to incomplete filings because they will help facilitate the administration of the ratemaking process. *Id.*

Pitney Bowes observes that extending the public comment period will encourage more meaningful participation by interested persons. *Id.* at 8. PSA comments that extending the public comment period will somewhat reduce the Postal Service's pricing flexibility. PSA Revised Comments at 9. As previously discussed, the final rules continue to allow the Postal Service pricing flexibility. Any effects of the final rules on the Postal Service's pricing flexibility would be negligible and outweighed by the benefits to the mailers and adjudicative process. See Section X.C.1., *supra*.

Except as noted below, the final rules adopt the other procedural changes to rate adjustment proceedings as proposed.

D. Revisions to Proposed Rules

The Commission revises final §§ 3030.101 and 3030.127(a) to reflect the withdrawal of the performance-based rate authority. See Section VI.D., *supra*. The Commission otherwise adopts the proposed rules from Order No. 5337 related to procedural improvements without changes.

XI. 5-YEAR REVIEW

A. Introduction

In Order No. 5337, the Commission proposed a 5-year review period for reviewing the effects of the Commission's final changes to its regulations. Order No. 5337 at 241. The Commission stated that it viewed the 5-year review period as most appropriate despite the Public Representative's request to shorten the period to 3 years "because it balances the competing needs of sufficient time to allow the effects of the changes to be fully known with a review period short enough to protect postal stakeholders from unintended consequences stemming from the changes." *Id.* at 243. It noted that a 3-year review period "would only show the effects of two rate cycles, which would not allow the cumulative effects to be fully explored." *Id.*

B. Comments

The Public Representative is the only party who commented on the 5-year review period. First, he reiterates his position that a review period that is shortened to 3 years would allow the Commission to act more quickly in the event of deleterious effects to Postal Service stakeholders. PR Comments at 52. He suggests that if the 3-year period turns out to provide inadequate data for the Commission's review, the review period could always be delayed. *Id.* at 53. He maintains that allegations of serious potential harm by mailers provide additional support for shortening the review period. *Id.* at 52.

Second, the Public Representative states that the exact timing of the 5-year review period should be clarified. *Id.* at 50-51. He states that the language setting forth a review period 5 years after "implementation" of the proposed rules could mean 5 years after the effective date of the regulations, the date of the first Postal Service rate filing under the final rules, or the date on which rate changes first go into effect. *Id.* at 50.

C. Commission Analysis

The Commission's initial rationale for retaining the 5-year review period remains unchanged from Order No. 5337. A thorough and insightful review must provide more than two rate cycles as data points to assess the impact of the changes to the Market Dominant ratemaking system. An abbreviated review period would not provide the Commission with sufficient data to evaluate the final rules in operation, account for outlying data, and determine the impact on mailers. The Commission retains the flexibility to review and adjust certain components of the system sooner than 5 years if serious ill effects are evident. Even if such a scenario were to occur, a holistic review of the system would also take place 5 years after implementation. Such an approach provides more predictability and transparency than the Public Representative's suggested solution.

As for clarifying the timeline, the Commission intends "5 years after implementation" to mean 5 years after the date the final rules go into effect. This approach possesses the advantage of being more predictable for all parties and not wholly dependent on when the Postal Service decides to make its first rate increase filing under the new rules.

For the reasons discussed above, the Commission concludes that it will retain the 5-year review period proposed in Order No. 5337.

XII. OTHER ISSUES

A. Introduction

Several commenters raise other issues that do not relate to a specific component of the proposed rules. These comments fall into two broad categories. First, parties submitted comments regarding the proposed rules generally, including their overall effects and impact on the postal community. Second, commenters put forward specific suggestions they would like the Commission to incorporate into its final rules. To the extent that these comments are not addressed in other sections, the Commission discusses these issues below.

B. General Comments

1. Impact on Mailers of Cumulative Proposal

Many Postal Service customers state that above-inflation rates would be detrimental to their ability to carry out their respective missions. See, e.g., Feed the Children Comments at 1; CBF at 1; ChimpHaven Comments at 1; HRC Comments at 1. In remarks representative of many of the comments received, the American Kidney Fund states that it “relies on the U.S. mail to raise funds and communicate with [its] supporters and constituents” and goes on to state that its “fundraising budget will not be able to keep pace with the increase in postage costs” resulting from the proposed rules, leading to “a reduction in our use of the mail, a reduction in our revenue, and in turn, a reduction in our ability to serve patients, and will not reform the Postal Service.” AKF Comments at 1. Similarly, the March of Dimes asserts that it “is not able to increase [its] budget to continue to keep pace with postage increases over the next five years” and “[a]ny expense, such as postage, that exceeds our means will result in necessary reductions in our use of mail... [that will] lead to less revenue, limiting our reach and reducing the amount our organization can spend on maternal and infant health programs, advocacy, and research funding.” March of Dimes Comments at 1.

Additionally, the Public Representative urges the Commission to consider the cumulative volume and price impacts of the proposed modifications before adopting them into a final rule. PR Reply Comments at 29.

As a threshold matter, the Commission notes that an analysis of the impact of its proposal as a whole is discussed below in its evaluation of how the modification to the ratemaking system appropriately balances all of the PAEA's objectives in conjunction with each other. See Chapter XIII., *infra*. As discussed therein, the Commission has considered how the modifications to the ratemaking system are necessary to achieve the objectives in conjunction with each other, and as they apply to the system as a whole. See *id*. It has determined that "although some aspects of the final rules may be in tension with particular components of certain objectives ... the weight of the balance favors implementation of the final rules." Section XIII.A., *infra*.

Accordingly, the Commission has considered the impact of above CPI price increases on mailers as well as the Postal Service and has balanced these considerations with all of the objectives.³³² The Commission has determined that additional pricing authority is necessary. It has determined that under the parameters set forth in the final rules, the Postal Service will be able to obtain necessary revenue while minimizing the burden on mailers. For a more detailed discussion of the Commission's finding that the final rules are "just and reasonable" to mailers and to the Postal Service as required by Objective 8, see Section XIII.E.8., *infra*. For a discussion on reductions in mail volume leading to a potential "death spiral" for the Postal Service, see Chapter IV., *supra*. Additionally, the final rules provide safeguards to protect mailers from deleterious effects of the increased rates – not only will the Commission perform a holistic review of the revised Market Dominant ratemaking system in 5 years,

³³² The arguments that the Commission has not considered the effect of above CPI increases on mailers and the Postal Service overlaps substantially with the commenter positions that *only* the existing ratemaking system would appropriately balance all of the PAEA's objectives in conjunction with each other that are addressed in Section XIII.B., *infra*.

it also possesses the ability to adjust components of that system sooner than 5 years if serious ill effects are alleged and proven. Finally, the Commission also notes that while the system of ratemaking limits the maximum pricing authority the Postal Service may utilize, it does not generally mandate a specific price level.³³³ The Postal Service's Board of Governors is vested with managing the Postal Service, and is in the best position to determine how to best utilize the pricing authority and make decisions about specific price increases for Market Dominant products. The Commission expects the Postal Service to use its business judgment in utilizing the tools provided in the system of ratemaking to craft pricing schemes and specific prices.

2. Lack of Incentives for Efficiency

Several commenters express concern that allowing the Postal Service additional rate authority, even if it fails to maximize cost reductions and efficiencies, sends the wrong message and fails to incentivize efficiency. See NMA Comments at 8; Mailers Hub Comments at 7. The Commission evaluates these claims in its discussion of Objective 1 in Section XIII.E.1., *infra*. There, the Commission concludes that principled modifications to the existing CPI-U price cap system are tailored to deficiencies in the ratemaking system as experienced during the PAEA era. See *id.* Adding these additional targeted sources of pricing authority but retaining the existing price cap does not allow the Postal Service to respond to its financial challenges through rate increases alone. See *id.* The final rules are intended to provide the correct incentives for the Postal Service by encouraging prudent pricing and operational decision-making to allow the system to achieve the objectives of 39 U.S.C. § 3622(b) in conjunction with each other. See *id.* The modifications to the ratemaking system pertaining to rate authority are designed to address cost drivers outside of the Postal Service's control. The

³³³ In limited circumstances, such as loss making products and inefficient workshare discounts, the Commission constrains the Postal Service's pricing flexibility. See *generally* Chapters VII., and VIII., *supra*.

additional rate authority related to those cost drivers will not be sufficient to achieve necessary financial health without meaningful action and success by the Postal Service on the cost drivers it can control. The Postal Service will still need to employ significant and ambitious cost reductions and efficiency improvements under the revised system.³³⁴ The Postal Service will need to utilize its pricing authority to begin to return to financial health, and in turn make necessary investments and reduce costs to maximize efficiency in furtherance of Objective 1. 39 U.S.C. § 3622(b)(1). For a more extensive discussion of how the new sources of rate authority will continue to incentivize efficiency, refer to Section XIII.E.1., *infra*.

3. Lack of Productivity Growth Target

ANM *et al.* suggest that the Commission include a productivity growth target in the final rules that both allows the Postal Service to retain a portion of the benefits resulting from productivity growth and innovation and allows customers to share in the benefits of productivity growth. ANM *et al.* Comments at 88-89.

The Commission has previously found that the Postal Service's overall financial health is poor and that financial stability has not been maintained throughout the PAEA era. Order No. 4257 at 274. The final rules are designed to allow the ratemaking system to achieve the objectives, in conjunction with each other. This includes the financial stability of the Postal Service, which is intended to function as a financially viable and efficient public service for the benefit of mailers and society in general. The Postal Service's financial health is necessary for it to make investments to achieve efficiency improvements and rational cost reductions. As the Postal Service begins to remedy its existing challenges, mailers primarily benefit from the continued existence of

³³⁴ See Order No. 4258 at 35-37. The Commission previously noted that it "expects that its proposal will incentivize the Postal Service to take necessary steps to reduce costs." *Id.* at 36. Likewise, the Postal Service "will need to realize cost reductions in order for the system to achieve financial stability." *Id.* at 37.

a vital mail system, and in the future, from a Postal Service able to pursue efficiency gains and cost reductions in a rational and planned manner, as opposed to operating in an ongoing, short-term-focused state of crisis.

As for efficiency gains created by innovations within the Postal Service, the additional rate authority provided in the final rules would remain within the Postal Service's discretion to use. The Governors have the discretion to share the financial benefits of any efficiency gains via unused rate authority. As discussed further in Chapter XI., *supra*, the Commission will continue to closely monitor the operation of the modified Market Dominant ratemaking system. If it is evident that the Postal Service is consistently using its additional authority in a way that subsidizes inefficiency, the Commission retains the authority to adjust the system earlier than the scheduled 5-year review.

4. Effect on Competitive Product Prices

eBay expresses concern that the proposed price increases will reduce volume for Market Dominant mail and create a corresponding increase (or "spillover effect") on Competitive prices as those products are forced to bear a greater share of the Postal Service's operating costs. eBay Comments at 2.

The Commission notes that Competitive product prices, and the market for these prices, are outside the scope of the current review as the final rules relate only to objectives in the Market Dominant ratemaking system. 39 U.S.C. § 3622(d)(3). Further, Competitive prices are set in a competitive market environment and are not directly impacted by fluctuations in Market Dominant volume. As explained in Section XIII.E.9., *infra*, the Commission has determined that the finalized changes are designed to allow the system to "allocate the total institutional costs of the Postal Service appropriately between market-dominant and competitive products," as provided by Objective 9. See 39 U.S.C. § 3622(b)(9). Should the impact of the proposed rules

create serious ill effects on Competitive product mailers, the Commission retains the authority to adjust components of the Market Dominant ratemaking system without waiting for the 5-year review.

C. Specific Suggestions for Final Rules

1. Market Dominant Negotiated Service Agreement (NSA) Rules

Discover suggests that the Commission should revise the Market Dominant NSA rules to allow for volume discounts whenever the discounted volume would still cover its attributable costs. Discover Comments at 12. Such a revision, according to Discover, would be consistent with the PAEA and “would recognize that the Postal Service and its customers are in a better position to determine how mailers will react to incentives provided by NSAs, and how they would act in the absence of an NSA” than the Commission. *Id.* at 13.

The Commission is open to suggestions on how to improve the Postal Service’s financial position and better serve the needs of mailers through revisions to Market Dominant NSA rules. As noted in Section XIII.E.5., *infra*, the Commission finds that this suggestion is purely aimed at increasing certain volumes and is wholly undeveloped in terms of what changes are requested and how those changes would represent an improvement in furtherance of the objectives of 39 U.S.C. § 3622(b). As such, Discover may propose a more robust proposal in a petition for a rulemaking in a separate docket with adequate support.

2. Clarification in Language of Final Rules

The Postal Service highlights several ambiguities in the text of the proposed rules, and suggests that the Commission provide explicit clarification on four specific issues. Each is discussed in turn here, with the requisite clarification immediately following.

First, the Postal Service seeks to ensure that it can retain the flexibility to file limited rate adjustment cases without triggering the application of rules requiring the use of new forms of price cap authority. Postal Service Comments at 63. It requests clarification that:

[A] limited price-change case for less than all classes, such a stand-alone change to one or two (generally applicable) price cells, would not be considered a 'generally applicable rate adjustment,' if such a case were to be followed by a broader rate adjustment in the class later in the same calendar year.

Id. The Commission agrees that this distinction should be made in the final rules. The Commission clarifies that a limited price change which changes one or two generally applicable price cells will be exempted from the rules for a generally applicable rate adjustment requiring the use of new price cap authority.

Second, the Postal Service requests clarification on which additional authority can be banked for future use. *Id.* at 5.

The Commission clarifies that the Postal Service will have the ability to bank rate authority generated via the density and non-compensatory pricing authority mechanisms. The Postal Service will be limited to use no more than 2 percentage points of banked rate authority per class per year and banked rate authority will expire after 5 years. The retirement rate authority, however, will not be bankable due to the computation of this authority as a self-adjusting amount to be remitted to cover the Postal Service retirement obligations.

Third, the Postal Service seeks further explanation from the Commission on whether legacy mail classes can be modernized. *Id.*

In response, the Commission notes that the proposed rules do not affect the Postal Service's ability to petition for an MCS change in a separate docket whenever it seeks to modify existing mail classes.

Finally, the Postal Service and APWU seek an explanation from the Commission as to why it has proposed to maintain a price cap system rather than adopting an alternative form of rate regulation. *Id.*; APWU Comments at 2.

The Commission has given extensive consideration to the alternative proposals put forth by the Postal Service and other commenters. After considering how these proposals would affect the achievement of all the PAEA's objectives enumerated in 39 U.S.C. § 3622(b), it has determined that retaining the price cap system with the modifications set forth in the final rules best achieves balance among the (sometimes competing) objectives. The Commission does not take the position that the Market Dominant ratemaking system must cover all historic net losses or reset all rates to be compensatory, as this would disregard considerations enumerated by some of the objectives. Section XIII.E.5., *infra*. Instead, the final rules redesign the system in a way necessary to address the Postal Service's primary drivers of loss that are largely outside of its direct control while continuing to encourage prudent pricing and operational decision-making by the Postal Service. *See id.* This balance allows the Postal Service, as well as mailers, to derive benefits from the system in a way that the other proposals fail to do.

3. Timing

The Postal Service states that rate authority under the proposed rules should be available sooner, as there is too much time between the final rule and when rates under the new system become effective. Postal Service Comments at 50-51. The Postal Service interprets the implementation of the proposed rules as follows:

Order No. 5337 proposes that the Postal Service file proposed determinations of rate authority at the end of December, whereupon the Commission will take an unspecified amount of time to validate them. After that validation, the Postal Service will have another year to 'use' the rate authority. If a final rule in this docket is issued later in 2020, the new rate authority would not actually manifest in rates until January 2022, because the Commission would not even have received the proposed rate-authority determinations, let alone validated them, until after its review of the January 2021 price change.

Id. (internal citations omitted).

The Postal Service is correct that given the timing of this final rule, the Postal Service's proposed January 2021 Market Dominant price change was recently approved by the Commission and therefore cannot include any new authority made available after the effective date of these final rules. See *generally* Docket No. R2021-1.

The final rules would require the Postal Service to file proposed calculations of the amount of the density-based and retirement-based rate authorities by the end of December. See Attachment §§ 3030.160(b) and 3030.181(b). The Commission would then validate these proposed calculations and determine the amount of the density-based and retirement-based rate authorities, as well as the amount of the non-compensatory-based rate authority. Presuming the Commission makes its determinations no later than the issuance of the ACD in March of 2021, any additional rate authority would be available to the Postal Service in March of 2021.

The Postal Service's assertion that it would not be able to include any new authority until January of 2022 is incorrect, as it is premised upon the Postal Service waiting to propose a Market Dominant product price adjustment until October of 2021. The Postal Service retains the flexibility to propose an out-of-sequence price adjustment at any time. The rate authority provided by the final rules is available for the Postal Service to use shortly after the effective date of the rules, and following the Commission's determination.

4. Price Cap Exclusion of UPU Prices

The Postal Service suggests that products over which it does not exercise complete pricing control should be excluded from the price cap. Postal Service Comments at 46.³³⁵ The Postal Service explains that the “incentives and effects” that may be imposed on it by a price cap are “nonexistent where an unregulated third party sets the prices.” Postal Service Comments at 45.

The Postal Service’s comments concerning these rates appear concurrent and comingled with its comments on the Commission’s proposals concerning non-compensatory products. The Commission separately addresses the Postal Service’s suggestion concerning these products and the non-compensatory product regulations in Section VII.A.3.

At the outset, 39 U.S.C. §§ 3621 and 3631 establish Market Dominant and Competitive products. The Commission is empowered to make changes to either list pursuant to 39 U.S.C. § 3642.³³⁶

Excluding these rates from the price cap would require the creation of a new tier of rates that are subject to neither the regulatory scheme governing Market Dominant

³³⁵ The Postal Service first suggested this proposal in this docket in March 2018. See Initial Comments of the United States Postal Service in Response to Order No. 4258, March 1, 2018, at 154-158 (stating that this docket presents an opportunity for the Commission to revisit its decision in Order No. 43 to include terminal dues for inbound international mail within the price cap). Several commenters urged the Commission to reject the proposal. See, e.g., Reply Comments of United Parcel Service, Inc., March 30, 2018 (stating that the proposal would undermine the efficiency goals of the system and suggesting that the Commission reclassify Inbound Letter Post as a Competitive product); Reply Comments of the Greeting Card Association, March 30, 2018, at 16 (stating that section 3621(a)(10) includes single-piece international mail and this definition is not subject to this review). In the same month, the Commission issued an order in a separate docket, reaffirming its initial determination that inbound international products must be categorized as Market Dominant or Competitive. See Docket No. ACR2017, Determination to Unseal the Postal Service’s Response to Chairman’s Information Request No. 15, March 28, 2018, at 5 (Order No. 4551).

³³⁶ See also 39 U.S.C. §§ 3621(a) and 3631(a) (“subject to any changes the Postal Regulatory Commission may make under section 3642”).

products nor the scheme governing Competitive products, and the Commission previously rejected this argument in 2007.³³⁷ Moreover, in March 2018, the Commission reaffirmed its finding in Order No. 43. See Order No. 4551 at 5. There, the Commission explained that in Order No. 43, it found the Postal Service's arguments for exceptional treatment of inbound international mail as neither Market Dominant nor Competitive unpersuasive and inconsistent with section 3642. *Id.* The Commission further explained that "the PAEA unambiguously requires the Commission to classify inbound international mail as either market dominant or competitive." *Id.* The Commission noted that no party had requested a transfer or partial transfer of the product from the Market Dominant to the Competitive product list. *Id.* at 6. The Commission's reiterates this interpretation and, in this proceeding, the Commission declines to modify the classification of specific products. The Postal Service may petition the Commission to change the classification of any product pursuant to 39 C.F.R. §§ 3040.130 *et seq.*³³⁸

As a result, the Commission declines the Postal Service's suggestion to remove these prices from the price cap and they remain on the Market Dominant product list and their prices remain subject to the price cap.

³³⁷ See Docket No. RM2007-1, Order Establishing Ratemaking Regulations for Market Dominant and Competitive Products, October 29, 2007, at 78 (Order No. 43).

³³⁸ Such a request to add, remove, or transfer a product must address the criteria set forth in 39 U.S.C. § 3642(b), and conform to 39 C.F.R. §§ 3040.130 *et seq.*

XIII. THE OBJECTIVES OF THE PAEA

A. Introduction

The Commission must review the Market Dominant ratemaking system 10 years after the PAEA's enactment. 39 U.S.C. § 3622(d)(3). The purpose of the review is to determine whether the system is achieving the objectives appearing in subsection (b), taking into account the factors appearing in subsection (c). *Id.* "If the Commission determines, after notice and opportunity for public comment, that the system is not achieving the objectives in subsection (b), taking into account the factors in subsection (c), the Commission may, by regulation, make such modification or adopt such alternative system for regulating rates and classes for market-dominant products as necessary to achieve the objectives." *Id.* The nine objectives are:

- (1) To maximize incentives to reduce costs and increase efficiency.
- (2) To create predictability and stability in rates.
- (3) To maintain high quality service standards established under section 3691.
- (4) To allow the Postal Service pricing flexibility.
- (5) To assure adequate revenues, including retained earnings, to maintain financial stability.
- (6) To reduce the administrative burden and increase the transparency of the ratemaking process.
- (7) To enhance mail security and deter terrorism.
- (8) To establish and maintain a just and reasonable schedule for rates and classifications, however the objective under this paragraph shall not be construed to prohibit the Postal Service from making changes of unequal magnitude within, between, or among classes of mail.
- (9) To allocate the total institutional costs of the Postal Service appropriately between market-dominant and competitive products.

Id. § 3622(b).

As a starting point, the Commission responds to the position that *only* the existing ratemaking system would appropriately balance all of the PAEA's objectives in

conjunction with each other. Next, the Commission summarizes how its modification to the ratemaking system overall would appropriately balance all of the PAEA's objectives in conjunction with each other. Then, the Commission summarizes the comments asserting that the Commission's final rules (as a whole)³³⁹ fail to meet an objective(s). The Commission's analysis of these comments considers and applies the statutory objectives to the final rules. Where relevant and in response to comments, this Order provides analysis of particular final rules that demonstrate that the regulatory changes overall are consistent with the objectives. Comments focusing upon a particular proposal's consistency with a particular objective are already addressed above.³⁴⁰ Similarly, comments focusing upon a particular alternative proposal (that is, a suggestion by a commenter that was not adopted by the Commission) are already addressed above.³⁴¹ Finally, to provide clarity, the Commission discusses its treatment of the factors of 39 U.S.C. § 3622(c) in this proceeding.

The PAEA commits the balancing of the objectives to the Commission's discretion. See 39 U.S.C. § 3622(d)(3). Determinations of which objectives are relevant to the particular modifications implemented in this rulemaking, how much

³³⁹ The performance-based rate authority proposal has been withdrawn. See Section VI.D., *supra*. Comments asserting that the performance-based rate authority was inconsistent with the objectives are therefore not analyzed in this section. Issues related to whether the outcome of the Commission's evaluation of whether, when, and how to introduce a performance incentive mechanism produces rules that would be consistent with the objectives will be addressed in a separate rulemaking docket. See Section VI.C.1., *supra*.

³⁴⁰ See, e.g., Section IX.C.5., *supra* (considering arguments that the cost-reduction reporting requirements are contrary to Objective 6); Section X.C.1. and 4., *supra* (considering whether the procedural improvements are consistent with allowing pricing flexibility).

³⁴¹ See, e.g., Chapter VIII., *supra* (rejecting suggestions to remove the safe harbor for passthroughs between 85 and 100 percent); Section XII.C.2., *supra* (rejecting the Postal Service's suggestion that *ex ante* pricing rules are unnecessary to achieve the objectives of the PAEA and that replacing the price cap system with an alternative system of regulatory monitoring would better achieve the objectives); Section IV.C.3., *supra* (rejecting the Postal Service's suggestion to use a single density formula incorporating both Market Dominant and Competitive products rather than the Commission's two-formula approach); Section XII.C.1., *supra* (rejecting Discover's suggestion to revise the rules for Market Dominant NSAs).

weight to apply to particular objectives, the timing in which to implement proposed modifications, and how to balance the objectives are all committed to the discretion of the Commission.³⁴² In “applying the plain meaning of the [statutory] term ‘in conjunction,’ the Commission considers the objectives together as they apply to the system as a whole.”³⁴³ The Commission also observes that some aspects of the objectives are in tension with each other, whereas other aspects may overlap. See, e.g., Order No. 4257 at 18, 65-66, 260; Order No. 5337 at 94, 161, 168, 173, 194, 204. Therefore, as discussed below, although some aspects of the final rules may be in tension with particular components of certain objectives, ultimately, the Commission determines that the weight of the balance favors implementation of the final rules. While commenters may disagree with the final balance struck,³⁴⁴ upon consideration of all of the comments submitted in this rulemaking, the Commission has reasonably explained the nature and extent of the interrelated deficiencies and proposed a targeted regulatory solution necessary to address these issues. Further, the Commission has given specific and thorough consideration to all of the PAEA’s objectives in this proceeding. To explain its position, the Commission organizes its comment summary and analysis by objective below.

³⁴² See *id.*; see also Docket No. ACR2009, *Annual Compliance Determination*, March 29, 2010, at 15 (FY 2009 ACD).

³⁴³ Order No. 4257 at 17; see *Ass’n of Am. Publishers, Inc. v. Governors of U.S. Postal Serv.*, 485 F.2d 768, 774 (D.C. Cir. 1973) (“Like most other factors sheets, whether in statutes, A.L.I. Restatements, or comparable compilations, the factors listed are not analogous to a table of atomic weights, or to the multiplication table. The factors are reminders of relevant considerations, not counters to be placed on scales or weight-watching machines.”).

³⁴⁴ “[Judicial] review of agency decisions based on multi-factor balancing tests...is necessarily quite limited. [The appellate court] may not merely substitute the balance [it] would strike for that the agency reached.” *U.S. Postal Serv. v. Postal Reg. Comm’n*, 963 F.3d 137, 141 (D.C. Cir. 2020) (quoting *USAir, Inc. v. Dep’t of Transp.*, 969 F.2d 1256, 1263 (D.C. Cir. 1992)).

B. The Existing Ratemaking System

Before addressing each objective, the Commission addresses the position that *only* the existing ratemaking system, which generally does not allow annual rate increases for each class of Market Dominant products to exceed the corresponding change in the CPI-U, would be capable of balancing all of the PAEA's objectives in conjunction with each other.³⁴⁵ The Commission disagrees. As the Commission previously determined, "the operating environment on which the PAEA was designed changed quickly and dramatically after the PAEA was passed[]," and "this made it challenging for the ratemaking system under the PAEA to achieve the goals it was designed to achieve." Order No. 4257 at 45.

"At the time it created the new PAEA system, Congress anticipated that the CPI-U price cap would enable the Postal Service to achieve sufficient revenues to cover all of its operating costs and statutorily mandated obligations while at the same time motivate the Postal Service to cut costs and become more efficient." *Id.* at 3. This judgment was based on the appearance of the Postal Service's financial position being relatively stable in FY 2006 and the observable PRA-era correlation between increases in Postal Service expenses, Postal Service's revenues, and the CPI. *See id.* at 37. Generally, Market Dominant volume had been increasing from FY 1997, reaching its peak in FY 2006.³⁴⁶

However, after the enactment of the PAEA, a number of converging macro-level circumstances such as the Great Recession, a rare period of deflation post-Great Recession, and emergent technological trends contributed to the Postal Service's inability to adequately respond to Postal Service-specific challenges such as declining

³⁴⁵ Compare ANM *et al.* Comments at 13-22, and ANM *et al.* Reply Comments at 2, 9, 16, with 2018 ANM *et al.* Comments at 30-31.

³⁴⁶ See *id.* at 35-36; Library Reference PRC-LR-RM2017-3/1, Excel file "PRC-LR-RM2017-3-1.xlsx," tab "Figure II-23," column F (displaying Market Dominant volume from FY 1997 through FY 2016).

mail density, the newly imposed statutory retirement obligations, and long-standing issues with non-compensatory rates. See Order No. 4257 at 3, 37-41, 148, 236. While the nature of these Postal Service-specific challenges such as the longer-term diversion of mail to electronic forms of communication may have been somewhat foreseeable, their coincident impact was accelerated by the circumstances occurring after the PAEA's enactment, rendering the speed and extent of their impact unforeseeable at the time of the PAEA's enactment.³⁴⁷ Therefore, during the PAEA era,³⁴⁸ "the correlation between the growth in Postal Service expenses and revenue and the growth in CPI began to diverge."³⁴⁹ This sudden divergence "made it extremely challenging for the Postal Service to manage retained earnings through sustained net income." Order No. 4257 at 40.

³⁴⁷ See, e.g., RARC-WP-13-007 at ii ("When the current price cap formula was enacted in 2006, postal volumes had been trending upward.... Few analysts or policymakers foresaw the recent steep decline in mail volume, or contemplated the impact on the Postal Service of such a decline combined with the price cap."); United States Postal Service, Office of the Inspector General, Report No. RARC-WP-12-010, State of the Mail, April 27, 2012, at 13-19, available at: https://www.uspsoig.gov/sites/default/files/document-library-files/2015/rarc-wp-12-010_0.pdf (RARC-WP-12-010) (summarizing how the impact of electronic diversion on the Postal Service was exacerbated by the Great Recession followed by the slow economic recovery referred to as the Great Slump).

³⁴⁸ Order No. 4257 uses the phrase "PAEA era" to refer to FY 2007 through FY 2016. See Order No. 4257 at 22 n.40.

³⁴⁹ *Id.* at 38-41; see Library Reference PRC-LR-RM2017-3/1, Excel file "PRC-LR-RM2017-3-1.xlsx," tab "Figure II-2" (displaying CPI-U, total cost, and total revenue indices from FY 1995 through FY 2016). The correlation remains weak from FY 2016 to the present. Total Cost and Total Revenue figures are derived from the applicable Public Cost and Revenue Analysis Reports. See *id.*; Docket No. ACR2019, Library Reference USPS-FY19-1, December 27, 2019, PDF file "FY19-1 Public CRA and preface.pdf," Public Cost and Revenue Analysis Fiscal Year 2019: Finance, at 3 (displaying FY 2019 total cost and total revenue); Docket No. ACR2018, Library Reference USPS-FY18-1, December 28, 2018, revised February 11, 2019, PDF file "USPS-FY18-1 Preface.Rev.2.11.19.pdf," Public Cost and Revenue Analysis Fiscal Year 2018: Finance, at 3 (displaying FY 2018 total cost and total revenue, as revised); Docket No. ACR2017, Library Reference USPS-FY17-1, December 29, 2017, PDF file "USPS-FY17-1 Preface.pdf," Public Cost and Revenue Analysis Fiscal Year 2017: Finance, at 3 (displaying FY 2017 total cost and total revenue). The CPI-U data are published on the Commission's website, available at: <http://www.prc.gov>; hover over "References" and follow the "CPI Figures" hyperlink.

The existing ratemaking system was unable to adequately respond to this confluence of circumstances. The Postal Service was unable to generate sufficient revenue to cover its total costs, thereby resulting in a net loss for each and every year of the PAEA era.³⁵⁰ The consecutive net losses resulted in an accumulated deficit. See Order No. 4257 at 170-171. The Postal Service was unable to cover the revenue shortfall despite maximum use of its borrowing authority and a sharp decline in capital investments.³⁵¹ While some cost reductions and efficiency gains were achieved post-PAEA, they were insufficient to achieve overall financial stability and/or retained earnings. Order No. 4257 at 222, 274-275. In an effort to restrain costs and account for declining demand, the Postal Service reduced the high-quality service standards that were set in 2007. See *id.* at 273; Sections II.A. and VI.C.3., *supra*. Overall, the existing ratemaking system was unable to achieve the PAEA's objectives in conjunction with each other. See Order No. 4257 at 3-5, 274-275.

In light of these circumstances, the Commission determines that it would be unreasonable and inappropriate to retain the existing ratemaking system unchanged. Rectifying the system's inability to adequately respond to these coincident trends occurring after the PAEA's enactment and making necessary modifications to achieve the objectives of the PAEA is a reasonable and appropriate way for the Commission to fulfill the purpose of 39 U.S.C. § 3622(d)(3).

³⁵⁰ See Order No. 4257 at 168, Table II-10. The consecutive net losses also persist from FY 2016 to the present. See FY 2019 Financial Analysis at 3 ("As seen in Figure I-1 [of the FY 2019 Financial Analysis], the Postal Service has not had a profitable year in the last decade [FY 2010 through FY 2019].").

³⁵¹ See Order No. 4257 at 168-169, 172-174. The Postal Service lacks shareholders and instead must finance capital investments through revenue or through borrowing. Order No. 4258 at 48-49. Therefore, as consecutive years of net losses resulted in an accumulated deficit, the Postal Service relied heavily on its borrowing authority, deferred capital investments, and increased its cash reserves. See *id.* at 46-52.

C. The Modified Ratemaking System

The final rules modify the ratemaking system's design to encourage and enable the Postal Service to address its complex challenges by making prudent pricing and operational decisions. The final rules directly aim to address two underlying drivers of the Postal Service's net losses that are largely outside of its direct and near-term control: (1) the increase in per-unit cost resulting from the decline in mail density for each fiscal year under final subpart D of 39 C.F.R. part 3030 and (2) the statutorily mandated amortization payments for particular retirement costs under final subpart E of 39 C.F.R. part 3030. In order to incrementally address long-standing problems concerning non-compensatory classes and products, the Commission also provides 2 percentage points per fiscal year for each non-compensatory class of mail and defines rate-setting criteria for non-compensatory products in classes for which overall class revenue exceeds overall class attributable cost under final subpart G of 39 C.F.R. part 3030. To address the inefficient pricing practices observed after the PAEA's enactment, the Commission enhances its regulation of workshare discounts under final subpart J of 39 C.F.R. part 3030. To improve transparency into the Postal Service's efforts to increase efficiency and reduce costs as well as to monitor the effects of all of the finalized regulatory changes, particularly with respect to planned and realized cost reductions, the Commission codifies additional reporting requirements in final § 3050.55.

The Commission structures these adjustments to rate authority and rate-setting criteria in a manner that would allow for the Postal Service to exercise pricing flexibility to set rates that would be predictable and stable. The Commission has balanced the competing priorities enumerated in the PAEA to ensure that modifications to the design of the ratemaking system will better enable the Postal Service to set rates that are just and reasonable to the mailers and to the Postal Service. Finally, in improving its rate adjustment procedural rules, the Commission considered how the modified ratemaking

system would achieve the competing priorities to increase transparency and reduce administrative burden.

D. Comments

1. Objective 1

Multiple commenters object to providing *any* additional rate authority to the Postal Service so that it may adjust rates above the percentage change in the CPI-U, arguing that doing so would remove the financial pressure to reduce costs and increase efficiency imposed on the Postal Service by the existing CPI-U price cap.³⁵² ABA and ANM *et al.* assert that the proposed rules are irreconcilable with Objective 1 because they fail to hold the Postal Service accountable for cost reductions and instead allow the Postal Service to raise prices to fix its failure to control costs.³⁵³ ANM *et al.* object that the existing price cap is designed to operate in situations of declining volume (see ANM *et al.* Reply Comments at 16 (quoting Order No. 1926 at 175)) and that Congress intended for the retirement prefunding to be recovered under the existing price cap. See ANM *et al.* Reply Comments at 23, 54.

Additionally, ABA and ANM *et al.* assert that the proposed rules retain a price cap in name only and effectively represent a return to cost-of-service rate regulation. ABA Comments at 11; ANM *et al.* Comments at 17. AF&PA asserts that the proposed rules would “make mailers pay for USPS management failures to improve performance.” AF&PA Comments at 4. C21 argues that the Commission relegates Objective 1 to secondary status compared to Objective 5. C21 Reply Comments at 5.

³⁵² See, e.g., ABA Comments at 7-8, 11; AF&PA Comments at 4-5; ANM *et al.* Comments at 4, 14-17; C21 Reply Comments at 5; NMA Comments at 8-9; NPPC *et al.* Comments at 24, 35.

³⁵³ See ABA Comments at 7-8; ANM *et al.* Comments at 13-16, 82; see also ANM *et al.* Reply Comments at 11.

NMA asserts that the provision of additional rate authority would “send the wrong message to the Postal Service by assuring that it will recoup revenue even if it fails to maximize cost reductions and efficiencies.” NMA Comments at 8. NPPC *et al.* disagree with the Commission’s statement that the density rate authority “maintains the efficiency incentives created by a price cap.”³⁵⁴

Additionally, multiple commenters direct their concerns regarding Objective 1 at the withdrawn performance-based rate authority proposal, which are summarized³⁵⁵ and analyzed above.³⁵⁶ Further, multiple commenters focus on Objective 1 with respect to workshare discounts; these issues are summarized and analyzed above.³⁵⁷

2. Objective 2

Multiple commenters object to providing *any* additional rate authority to the Postal Service so that it may adjust rates above the percentage change in the CPI-U, arguing that doing so would be contrary to Objective 2.³⁵⁸ ABA argues that allowing rate increases to exceed inflation would render future rate increases uncertain and unconstrained. ABA Comments at 7. ANM *et al.* object that allowing the Postal Service

³⁵⁴ NPPC *et al.* Comments at 35 (quoting Order No. 5337 at 76); see NPPC *et al.* Reply Comments at 5; ABA Comments at 11.

³⁵⁵ See Section VI.B.2., *supra* (summarizing comments asserting that the performance-based rate authority is inconsistent with incentivizing efficiency gains and cost reductions); Section VI.B.3., *supra* (summarizing comments asserting that the performance-based rate authority is unnecessary, insufficient, or unlikely to result in efficiency gains and cost reductions); Section VI.B.5., *supra* (summarizing objections and suggested alternatives to the operational-efficiency based requirement).

³⁵⁶ Issues relating to any performance-based rate authority and any connected operational efficiency-based requirement will be further addressed in a separate rulemaking. See Section VI.C., *supra*. The Commission will implement the reporting requirement changes in final §§ 3050.21(m), 3050.60. See Section VI.D., *supra*.

³⁵⁷ See Chapter VIII., *supra* (maintaining the Commission’s prior position with respect to the safe harbor for passthroughs between 85 and 100 percent).

³⁵⁸ See, e.g., ABA Comments at 7; ANM *et al.* Comments at 19-21, 57; NMA Comments at 7-9; NPPC *et al.* Comments at 20; see also 2018 ANM *et al.* Comments at 5, 58, 60-62.

to increase rates multiple times the rate of inflation would not create rate stability.³⁵⁹ ANM *et al.*, C21, and NPPC *et al.* assert that the additional rate authorities would impair ratepayers' ability to predict rates and plan their mailing budgets, thereby jeopardizing the achievement of Objective 2.³⁶⁰ NMA argues that the provision of additional rate authority through a formula that does not limit the maximum amount of rate authority does not meet Objective 2. NMA Comments at 7-9. Additionally, C21 argues that Order No. 5337 relegates Objective 2 to secondary status compared to Objective 5 and that the final rules would produce a system that no longer achieves Objective 2. C21 Reply Comments at 5, 7; see ABA Comments at 2-3.

3. Objective 3

Generally, the commenters direct their concerns regarding Objective 3 at the withdrawn performance-based rate authority proposal, which are summarized³⁶¹ and analyzed above.³⁶²

³⁵⁹ ANM *et al.* Comments at 20-21, 57. Additionally, approximately 138 comments (listed in Appendix A) were filed by non-profit organizations and related entities that object to the magnitude of the potential allowable rate increases and urge the Commission to retain the existing CPI-U price cap asserting that doing so would maintain stability of rates. See, e.g., AFA *et al.* Comments at 1.

³⁶⁰ ANM *et al.* Comments at 19-20; C21 Reply Comments at 7; NPPC *et al.* Comments at 20. Similarly, AF&PA, Discover, and NTU contend that multiple overlapping layers of rate authority render it difficult for ratepayers to plan their mailing budgets. AF&PA Comments at 4; Discover Comments at 7-8, NTU Comments at 2. Additionally, approximately 138 comments (listed in Appendix A) were filed by non-profit organizations and related entities urge the Commission to retain the existing CPI-U price cap asserting that doing so would maintain predictability of rates. See, e.g., AFA *et al.* Comments at 1.

³⁶¹ See Section VI.B.4.b., *supra* (summarizing comments regarding the amount of performance-based rate authority connected with achievement of the service standard-based requirement); Section VI.B.6., *supra* (summarizing objections to the service-standard based requirement, the suggestion that achievement of the service standard-based requirement triggers a qualitative evaluation process, the suggestion to add new rules to connect direct financial consequence with service performance achievement, and commenting on the reporting requirement of final § 3055.2(c)).

³⁶² Issues relating to any performance-based rate authority and any connected service standard-based requirement will be further addressed in a separate rulemaking. See Section VI.C., *supra*. The Commission will implement final § 3055.2(c)'s reporting requirement. See Section VI.D., *supra*.

4. Objective 4

The primary commenter with regard to Objective 4 was the Postal Service. Generally, the Postal Service directs its concerns regarding pricing flexibility at the limitations concerning the usage of the additional forms of rate authority, rate-setting criteria for non-compensatory products, and workshare discounts, which are summarized and analyzed above, where relevant.³⁶³ ANM *et al.* assert that authorizing above-average rate increases on non-compensatory classes and products is inconsistent with Objective 4 and fails to recognize that the types of mail at issue can create a multiplier effect. See ANM *et al.* Comments at 82.

5. Objective 5

Multiple commenters base their objections to the additional forms of rate authority on their previously stated opposition to prior findings of the Commission. ABA restates its prior assertion that the Commission's analysis of the Postal Service's financial stability was unsound and incomplete because the financial impact of the retiree obligations was overstated and the value of the Postal Service's real estate portfolio was understated. Compare ABA Comments at 8-9, with 2018 ABA Comments at 10-11. AF&PA reiterates that the Commission's analysis of the Postal Service's financial stability should be limited to revenues needed to support ongoing operations and that "[t]he underlying deficit on the USPS balance sheet due to the RHB [p]refunding requirements should be up to Congress to solve."³⁶⁴ Similarly, NPPC *et al.*

³⁶³ See Chapters VII. and VIII., *supra*.

³⁶⁴ AF&PA Comments at 2; Comments of the American Forest & Paper Association, March 1, 2018, at 6 (2018 AF&PA Comments).

restate their prior assertion that the Commission applied an improper definition of financial stability.³⁶⁵

ABA, AF&PA, ANM *et al.*, and C21 argue that the Commission has improperly elevated Objective 5 above all other objectives.³⁶⁶ Additionally, ANM *et al.* reiterate their prior position that the Commission has incorrectly interpreted Objective 5 to set the regulatory goal as providing retained earnings and has improperly elevated that goal above all other objectives (in lieu of properly balancing the objectives). ANM *et al.* Reply Comments at 3; see 2018 ANM *et al.* Comments at 1-2. ANM *et al.* restate their position that the Commission's analysis in Order No. 4257 supporting the determination that the existing system, including the CPI-U price cap, has not achieved the objectives (particularly with respect to Objective 1's efficiency component and Objective 5's retained earnings component) is improper because it "is entirely results-based...and lacks any analysis of causality." ANM *et al.* Reply Comments at 9-10 (emphasis omitted); see 2018 ANM *et al.* Comments at 36, 55 n.31. Further, they restate their position that the net losses are attributable to the Postal Service's operational decisions, specifically the failure to reduce costs, rather than the system or pricing issues. ANM *et al.* Reply Comments at 10-11; see 2018 ANM *et al.* Comments at 85.

Multiple commenters assert that providing additional rate authority to the Postal Service would be unnecessary and counterproductive to achieving financial stability, arguing that additional rate authority weakens the financial pressure imposed on the Postal Service by the existing CPI-U price cap to reduce costs and increase

³⁶⁵ See NPPC *et al.* Comments at 9-10, 53; 2018 NPPC *et al.* Comments at 48-50; see also Comments of the Major Mailers Association, the National Association of Presort Mailers, and the National Postal Policy Council, March 20, 2017, at 33-48 (2017 NPPC *et al.* Comments); ANM *et al.* Reply Comments at 22-23 (asserting that the Commission improperly "*defined* the Postal Service into financial instability") (emphasis in original).

³⁶⁶ ABA Comments at 2-3, 6; AF&PA Comments at 3; ANM *et al.* Reply Comments at 3; C21 Reply Comments at 5.

efficiency.³⁶⁷ ANM *et al.* restate their position that the contribution from the Postal Service's Competitive products should sufficiently offset losses sustained due to declining Market Dominant volumes. See ANM *et al.* Comments at 24-25, 48-49; 2018 ANM *et al.* Comments at 6.

NPPC *et al.* and the Postal Service object that the retirement obligation rate authority conflicts with Objective 5, arguing that it would have no real effect on the Postal Service's financial stability because it would not support operations and instead would remit revenue to the U.S. Department of the Treasury. NPPC *et al.* Comments at 46; see Postal Service Comments at 19. Similarly, ANM *et al.* object that there is no need for the Postal Service to recover the retirement obligation prefunding at all because its retirement funding level is sufficient and the Postal Service will suffer no penalty for continued default. ANM *et al.* Reply Comments at 23-24.

Further, multiple commenters contend that any additional rate authority (that is, beyond that included in the existing ratemaking system) will lead to price increases that are not sustainable for users of the mail and thereby will result in irreversible volume declines that would harm the Postal Service's financial viability.³⁶⁸

Finally, the Postal Service asserts a contrary view: that the final rules, which do not provide sufficient rate authority to cover the Postal Service's net losses and do not reset rates to levels that are fully compensatory, do not achieve Objective 5. Postal Service Comments at 6, 11, 15.

³⁶⁷ See, e.g., ABA Comments at 7-8, 11; AF&PA Comments at 4-5; NPPC *et al.* Comments at 5-8.

³⁶⁸ See, e.g., ABA Comments at 1-2, 10-11; AFPA Comments at 3; ANM *et al.* Comments at 38 (citing Brattle Decl. ¶ 40); ANM *et al.* Reply Comments at 2; Discover Comments at 4; eBay Comments at 3-4; NPPC *et al.* Comments at 22-23, 36-38; PSA Comments at 6.

6. Objective 6

ANM *et al.* assert that the final rules are inconsistent with Objective 6. ANM *et al.* Reply Comments at 2. AF&PA and NPPC *et al.* contend that the additional rate authorities, by increasing the complexity of the calculation of the maximum rate adjustment authority, would jeopardize the achievement of Objective 6. AF&PA Comments at 4; NPPC *et al.* Comments at 20. NPPC *et al.* assert that cost-reduction reporting requirements are in tension with Objective 6's goal of reducing administrative burden. NPPC *et al.* Comments at 24.

7. Objective 7

No commenters reference Objective 7.

8. Objective 8

Multiple commenters contend that the final rules would conflict with Objective 8, arguing that the magnitude of the additional rate authority would lead to rates that would be excessive to mailers.³⁶⁹ ABA asserts that allowing the Postal Service to raise prices because of declining volume would effectively tax ratepayers that continue to use the mail over electronic communication. ABA Comments at 6-7. NNA contends that the Commission should not authorize increases in rate authority that would lead to rate increases that will likely drive Periodicals out of the mail. NNA Comments at 10, 14-15.

Finally, the Postal Service asserts a contrary view: that the final rules, which do not provide sufficient rate authority to cover the Postal Service's net losses and do not reset rates to levels that are fully compensatory, do not achieve Objective 8. Postal Service Comments at 6, 11, 15. The Postal Service objects that the retirement obligation rate authority further conflicts with Objective 8 because it would require that

³⁶⁹ See, e.g., ABA Comments at 6; ANM *et al.* Comments at 4-5, 18; C21 Reply Comments at 5; NMA Comments at 9; NPPC *et al.* Comments at 20.

the revenue collected be remitted to the U.S. Department of the Treasury. *See id.* at 19.

9. Objective 9

Generally, the commenters direct their concerns regarding Objective 9 at the approach to calculating the density rate authority by using the volume input that experiences the lesser decline (either Market Dominant or total volume), which are summarized and analyzed above. *See* Section IV.C.3., *supra*.

E. Commission Analysis of Comments

The Commission organized Order No. 4257's analysis of the PAEA's nine statutory objectives into three principal areas: (1) the structure of the ratemaking system; (2) the financial health of the Postal Service; and (3) service. Order No. 4257 at 22. Each principal area was further divided into subtopics addressing relevant objectives and factors. *Id.* The Commission concluded that while the existing ratemaking system had achieved some of the PAEA's goals, the overall system had not achieved the statutory objectives, taking into account the statutory factors. *Id.* at 3-4.

For the first principal area—the structure of the ratemaking system—the Commission found that the existing ratemaking system has resulted in predictable and stable rates (Objective 2); reduced administrative burden and increased transparency (Objective 6); allowed the Postal Service pricing flexibility (Objective 4); and maintained prices that were not excessive to mailers (Objective 8).³⁷⁰

³⁷⁰ *See id.* at 113, 116-118, 142-145. For organizational purposes, Order No. 4257 disaggregated the discussion of Objective 8 into two prongs in Order No. 4257. *See id.* at 114-115. Therefore, Order No. 4257 also discusses Objective 8 in the context of the second principal area of discussion—the financial health of the Postal Service. *See id.*

However, the Commission found that the existing ratemaking system has not increased pricing efficiency (Objective 1). Order No. 4257 at 145. This finding was based on the failure to adhere to the two principles of pricing efficiency during the PAEA era: ECP and allocative efficiency. See *id.* at 130, 145. First, the Commission determined that workshare discounts have not been set as close as practicable to their avoided costs, despite the Postal Service having the ability to do so under the price cap. *Id.* at 145. This failed to comport with the principles of ECP because prices are most efficient when workshare discounts are set equal to the avoided costs of particular workshare activities. *Id.* at 135-136. Second, the Commission concluded prices for multiple products did not cover their attributable costs. *Id.* at 141, 145. This failure did not comport with the principles of allocative pricing efficiency because “[p]rices that adhere to the principles of allocative efficiency are set at or above marginal (or in the Postal Service’s case, attributable) costs, meaning they would have a cost coverage of 100 percent or greater.” *Id.* at 139-140 (internal footnotes omitted).

For the second principal area—the financial health of the Postal Service—the Commission found that there were safeguards to protect the mail and deter terrorism and sufficient funds to pay for those safeguards (Objective 7) and that the existing ratemaking system contained a mechanism to allocate institutional costs between Market Dominant products and Competitive products (Objective 9). *Id.* at 247-249. However, applying the objectives in conjunction with each other, the Commission described the overall picture of the Postal Service’s financial health as “poor” and found that the existing ratemaking “system has not maintained the financial health of the Postal Service as intended by the PAEA.” *Id.* at 249. The deficiencies identified by the Commission related to financial health pertain to the goals encapsulated by Objectives 1, 5, and 8. See *id.* at 247-249.

With regard to Objective 1, the Commission extensively reviewed cost reductions and operational efficiency and their relative effects on the Postal Service’s finances

during the PAEA era. See *id.* at 178-226. The Commission found that the Postal Service's overall costs had been reduced during the PAEA era, mostly in mail processing as a result of changes in the mail mix. *Id.* at 184-198. At the same time, however, the Commission found that "cost savings estimates from some of the Postal Service's initiatives are likely overstated and...the Postal Service could improve its quantitative measurement of the results of cost savings initiatives." *Id.* at 200. The Commission also noted that the Postal Service's unique cost structure constrained its ability to further reduce costs—specifically its pool of institutional costs; the labor-intensive nature of its business; its USO; and its limited ability due to binding arbitration requirements to set wage rates, adjust its employee complement, and/or reduce workhours. *Id.* at 198-200.

The Commission found that the Postal Service's operational efficiency, as measured by TFP, generally increased during the PAEA era, although the Commission noted that operational efficiency may have been somewhat undermined by the Postal Service's failure to price workshare discounts as nearly as practicable to their avoided costs.³⁷¹ Ultimately, the Commission concluded that while the Postal Service was able to reduce costs and increase operational efficiency during the PAEA era, the results had been insufficient to achieve overall financial stability and did not generate retained earnings. *Id.* at 222.

With regard to Objective 5, the Commission found that while the existing ratemaking system generally enabled the Postal Service to achieve short-term financial stability, medium- and long-term financial stability had not been achieved. *Id.* at 247-249. This failure was evidenced by total revenue being inadequate to cover total costs,

³⁷¹ *Id.* at 203-208, 216-219. While workshare discounts and ECP, as previously detailed, generally implicate pricing efficiency, which was organized under the first principal area of discussion—structure of the ratemaking system—the Commission noted that workshare discounts set substantially below avoided costs may also necessitate the Postal Service's maintenance of a larger than necessary processing network, which implicates operational efficiency. *Id.* at 216.

resulting in the Postal Service incurring a net loss each and every year during the PAEA era. *Id.* at 165-169. This persistent accumulation of net losses resulted in accumulated deficits, which also prevented the Postal Service from being able to achieve retained earnings. *Id.* at 169-171.

With regard to Objective 8, the Commission determined that the existing ratemaking system lacked an adequate mechanism to maintain rates that cover attributable costs and enable a positive contribution to institutional costs.³⁷² Attributing this deficiency, in part, to the existing price cap limitation, the Commission found that this deficiency threatened the financial integrity of the Postal Service. See Order No. 4257 at 236, 274-275.

Finally, for the third principal area—service (Objective 3)—the Commission found that service standards declined during the PAEA era because the Postal Service had reduced the high-quality service standards that were initially promulgated in 2007. *Id.* at 273. Objective 3 also implicitly requires consistent achievement of service standards, otherwise known as “service performance.” See *id.* at 262-263. The Commission found that the existing regulatory system has a mechanism to hold the Postal Service accountable for its service performance. See *id.* at 264.

Analyzing the ratemaking system in its totality, the Commission concluded that “while some aspects...have worked as planned, overall, the system has not achieved the objectives of the PAEA.” *Id.* at 5. This result was largely due to the fact that “the operating environment on which the PAEA was designed changed quickly and dramatically after the PAEA was passed[],” and “this made it challenging for the ratemaking system under [the] PAEA to achieve the goals it was designed to achieve.”

³⁷² See *id.* at 235-236. As described above, for organizational purposes, the Commission disaggregated the discussion of Objective 8 into two prongs in Order No. 4257; therefore, Order No. 4257 also discusses Objective 8 under the first principal area of discussion—structure of the ratemaking system. See n.330, *supra*.

Id. at 45. As a result, “although the...CPI-based price cap system was anticipated, at the time of its implementation, to enable the Postal Service to produce sustained net income and generate retained earnings, that has not occurred.” *Id.* at 148. Based on these findings and having given consideration to the comments received in response to the proposals and revised proposals appearing in Order Nos. 4258 and 5337, the Commission implements the final rules in this Order to address the deficiencies identified above within the ratemaking system.

Commenters generally focus their remarks on framing how a proposed regulatory change would affect a single statutory objective aligned with the commenters’ interests. The Commission observes that comments arguing that the Commission should adopt or reject particular changes to advance a certain objective necessarily fail to consider the impact that adoption or rejection would have on the achievement of other objectives. The Commission, however, is required by statute to consider the impact of proposed changes on the achievement of other objectives. This necessarily involves the Commission’s exercise of reasoned, expert judgment to determine which tradeoffs should be made from a holistic view of the system’s design.

Several of these tradeoffs are described in the Commission’s analysis below, which discusses each objective. For instance, declining to provide any additional rate authority would further the achievement of Objective 2 somewhat (by generally preventing rates on a class level from exceeding the change in the CPI-U); but would continue to frustrate the achievement of multiple other relevant objectives, including Objectives 5 and 8. On the other hand, resetting all Market Dominant rates to a level that would be sufficient to recover all costs would further the achievement of Objectives 5 and 8 but would likely represent a regression in the progress already made after the enactment of the PAEA toward achieving Objective 2.

Multiple ratemaking system designs could potentially satisfy the objectives of the PAEA when evaluated in conjunction with each other. Ultimately, in these final rules the

Commission has made modifications that in its expert judgment produce a balanced system. In balancing the tradeoffs, the Commission finds that it is reasonable to focus first on issues that frustrate achievement of the objectives in the near term.³⁷³ In doing so, the Commission incorporates moderation into its design so as not to introduce problems related to objectives that were generally being achieved after the PAEA's enactment. For deficiencies that can be addressed later, the Commission will open a separate rulemaking docket to consider possible refinements to its regulatory approach.

In the near term, modifying the system's design to better equip Postal Service management with additional pricing tools to respond to its challenges (such as declining density, statutorily imposed retirement obligations, and non-compensatory products and classes) is necessary, proper, and consistent with the PAEA. Therefore, the adjustments to the price cap made in this Order are necessary to achieve the objectives of the PAEA, in conjunction with each other, and are focused on vital near-term improvements. Because the near-term financial instability of the Postal Service is a source of imminent peril, it is reasonable for the Commission to exercise its considerable expert policy judgment, authority, and experience to address those more time-sensitive issues first and then evaluate how the longer-term financial stability issues should be addressed, in conjunction with the other objectives, under the modified ratemaking system.

1. Objective 1

The finalized changes are designed to address the systemic issues underlying the existing system's failure to "maximize incentives to reduce costs and increase

³⁷³ See *Lujan*, 891 F.2d at 935 ("Since agencies have great discretion to treat a problem partially, we would not strike down the listing if it were a first step toward a complete solution") (internal footnote omitted); *Nat'l Ass'n of Broads.*, 740 F.2d at 1210 ("We have therefore recognized the reasonableness of the Commission's decision to engage in incremental rulemaking and to defer resolution of issues raised in a rulemaking even when those issues are 'related' to the main ones being considered.").

efficiency,” as provided by Objective 1. 39 U.S.C. § 3622(b)(1). The Commission determined that under the existing ratemaking system, the Postal Service was able to reduce costs and increase operational efficiency but the results were insufficient to achieve overall financial stability for the Postal Service and did not generate retained earnings. Order No. 4257 at 222. The Commission observed that real unit Market Dominant attributable cost decreased less during the PAEA era than during the preceding 10 years. *Id.* at 225. Additionally, the Commission observed that TFP increased less during the PAEA era than during the preceding 10 years. *Id.* at 226.

Further, the Commission determined that the existing ratemaking system has not increased pricing efficiency. *Id.* at 274. Pricing efficiency encompasses two principles: ECP and allocative efficiency. *Id.* at 130. First, prices are most efficient when workshare discounts are set equal to avoided costs in accordance with the principles of ECP, and the Commission concluded that the Postal Service failed to set most workshare discounts in accordance with ECP during the 10 years following the enactment of the PAEA. *Id.* at 131, 136-138. Second, the Commission concluded prices for multiple products during the PAEA era did not cover costs and as a result were not priced in accordance with the principles of allocative efficiency. *Id.* at 141. “Prices that adhere to the principles of allocative efficiency are set at or above marginal (or in the Postal Service’s case, attributable) costs, meaning they would have a cost coverage of 100 percent or greater.” *Id.* at 139-140 (internal footnotes omitted).

Multiple commenters express concerns that providing additional rate authority to the Postal Service may lead the Postal Service to simply rely on rate increases to respond to its financial challenges and weaken the existing incentives for the Postal Service to increase efficiency and reduce costs.³⁷⁴ Considerable focus has been given

³⁷⁴ See, e.g., ABA Comments at 7, 11; AF&PA Comments at 4-5; ANM *et al.* Comments at 4; ANM *et al.* Comments at 17; NMA Comments at 8-9; NPPC *et al.* Comments at 24.

to the use of the verb “maximize” in the text of Objective 1 throughout this review and in comments advocating against allowing any adjustments above the percentage change in the CPI-U.³⁷⁵ The Commission’s prior approaches to addressing Objective 1 included a proposal to make available 1 percentage point of performance-based rate authority, conditioned on the Postal Service exceeding an operational efficiency-based requirement and adhering to service standard-based criteria. See Section VI.A., *supra*. After considering the numerous comments opposed to this proposal, including those claiming that it would not address Objective 1 in a meaningful way and would violate other objectives, the Commission finds that this proposal requires further study. See Section VI.B.-C., *supra*.

Deferring such issues to a new rulemaking is reasonable given the importance of having a good design for a performance incentive mechanism to be successful. See Section VI.C., *supra*. Moreover, the Postal Service’s efforts, which increased operational efficiency after the PAEA’s enactment (see Order No. 4257 at 226), tend to suggest that while systemic incentives to increase operational efficiency could be increased, the need to do so is less pressing than addressing the imminent financial challenges faced by the Postal Service. Accordingly, the Commission’s final rules focus on what can be improved in the near term and defer other issues to a new rulemaking. As applied to Objective 1, this Order implements a number of rules directly aimed at producing near-term improvement towards achieving the pricing efficiency component of Objective 1, while deferring other rule changes aimed at the operational efficiency component of Objective 1 for further refinement.

Additionally, the objectives “to *maximize* incentives to increase efficiency and reducing costs” and “to *assure* adequate revenues, including retained earnings, to maintain financial stability” set forth ambitious goals that may not be achieved

³⁷⁵ See, e.g., ACI Comments at 3; ANM *et al.* Comments at 4; ANM *et al.* Reply Comments at 17; NMA Comments at 8.

instantaneously. 39 U.S.C. § 3622(b)(1) and (5) (emphasis added). To explore whether additional changes may also be necessary to achieve these goals, and if there is a way to implement such changes in a manner that would appropriately balance competing priorities such as “[t]o maintain high quality service standards,” as provided by 39 U.S.C. § 3622(b)(3), the Commission will initiate a separate rulemaking proceeding.

As noted previously, the Commission has the flexibility to balance the objectives in a reasonable manner. In addressing Objective 1, the Commission must balance maximizing incentives to increase efficiency and reduce costs with the other relevant objectives. Continued financial pressure, particularly in the near term, may hinder the Postal Service’s ability to make investments that would increase efficiency, reduce costs, maintain high-quality service standards, and assure adequate revenues, as provided by Objectives 1, 3, and 5. The Commission’s density-based rate authority and retirement-based rate authority are designed to relieve financial pressure due to costs largely outside of the Postal Service’s direct control. The trend of negative class contribution continues to hinder pricing efficiency, assuring adequate revenues, and establishing and maintaining rates in a range that are just and reasonable, as provided by Objectives 1, 5, and 8. The Commission’s adjustment to the existing price cap for non-compensatory classes addresses this relevant issue.

Theoretically, a price cap system contains inherent incentives for the regulated entity to increase efficiency and reduce costs.³⁷⁶ At the time it enacted the PAEA, Congress anticipated that setting the price cap equal to the percentage change in the CPI-U would provide these incentives: the Postal Service would be able to generate retained earnings by restraining cost increases below the pace of inflation. See Order No. 4257 at 37. These retained earnings would, in turn, allow the Postal Service to fund

³⁷⁶ See Order No. 4257 at 32-33 (describing the economic theory for using price cap regulation to incentivize the Postal Service to reduce costs and increase efficiency).

network expansion and capital improvements and incentivize employees with bonuses. *See id.* This judgment was based on the appearance of the Postal Service's financial position being relatively stable in FY 2006 and the observable PRA era correlation between increases in Postal Service expenses, the Postal Service's revenues, and the consumer price index. *See id.* However, circumstances occurring after the enactment of the PAEA accelerated trends that led to total costs increasing more than CPI-U and a sudden divergence between total Postal Service costs and total Postal Service revenues. *See id.* at 38-41; *see also* Section XIII.B., *supra*. As the Commission has previously explained, Postal Service-specific challenges such as declining mail density, the statutory retirement obligations, and long-standing issues with non-compensatory rates exacerbated those trends. *See* Section XIII.B., *supra*.

Accordingly, the existing CPI-U price cap system requires modifications to achieve the objectives of the PAEA in conjunction with each other. The principled adjustments to the existing CPI-U price cap based on declining density, retirement obligations, and non-compensatory classes increase the amount of rate authority available to the Postal Service. However, contrary to commenters' assertions, they are not designed to allow the Postal Service to respond to its financial challenges through rate increases alone. These modifications address the deficiencies highlighted by the challenges experienced after the PAEA's enactment. By closely tailoring the modifications to the identified deficiencies, these modifications are designed to provide correct incentives and to encourage prudent pricing and operational decision-making by the Postal Service that will allow the system to achieve the objectives of 39 U.S.C. § 3622(b) in conjunction with each other.

The PAEA was intended to provide the Postal Service with the opportunity to retain earnings (rather than merely break-even as limited by the PRA) as an incentive

for the Postal Service to increase its efficiency and reduce its costs.³⁷⁷ By providing the Postal Service with the needed pricing tools to narrow the existing formidable gap between revenues and costs, the ability for the Postal Service to bridge that gap fully via efficiency gains and cost reductions is more meaningful than under the existing ratemaking system. The final rules, which modify the implementation of the existing price cap, take into account Objective 1 as described below.

As previously explained, the density rate authority is aimed at addressing the unique financial dilemma of declining density that was created by the decline in volume combined with the statutorily imposed universal service obligation to deliver to an increasing number of delivery points.³⁷⁸ These final rules are designed to help the system to achieve Objective 5 while also considering the need to be consistent with Objective 1 in the following ways. First, the density rate authority targets the portion of per-unit cost increases that is caused by the decline in density (rather than cost increases caused by inflation).³⁷⁹ There is no evidence that adjusting for declining

³⁷⁷ See Order No. 4257 at 32 (citing S. Rep. No. 108-318 at 9 (2004)). Notably, the legislative history indicates that the Senate recognized that “[i]f retained earnings are not permitted, that is if revenues must equal costs [as required under the PRA], the incentive to control costs and thus generate funds for long-term capital investments, network growth or other needs will not exist.” S. Rep. No. 108-318 at 9 (2004). Further, the Senate acknowledged the link between efficiency gains and cost reductions with “[t]he long term financial viability of the Postal Service.” *Id.* at 8.

³⁷⁸ See Order No. 5337 at 70; *see also* United States Postal Service, USPS Annual Tables, FY 2018 TFP (Total Factor Productivity), July 16, 2019, Excel file "Table Annual 2018 - 2018 CRA Public.xlsx," tab "Out-46," cells K52:69 (showing increasing number of delivery points for FYs 2001-2018); United States Postal Service, USPS Annual Tables, FY 2019 TFP (Total Factor Productivity), February 27, 2020, Excel file "Table Annual 2019 Public.xlsx," tab "Out-46," cells K52:70 (showing increasing number of delivery points for FYs 2001-2019).

³⁷⁹ Order No. 5337 at 70. As previously explained, the Commission’s formula targets costs outside of the Postal Service’s direct control in the short to medium term and focuses on the specific costs increases due to declining density (volume per delivery point) and thereby maintains the efficiency incentives created by a price cap. *Id.* at 75-76. The Commission rejected targeting a net revenue position as proposed by the Public Representative and rejected using revenue-weighted volume measurement as proposed by the Postal Service and its OIG, because those formulations may weaken efficiency incentives. *Id.* at 75-77.

density, a main driver of the Postal Service's net losses that is largely outside of its direct control,³⁸⁰ would undermine the price cap's incentives for the Postal Service to achieve efficiencies and cost reductions.³⁸¹ Modifying the implementation of the price cap to account for the exogenous increase in average cost per piece caused by declining density does not reduce the Postal Service's incentives to increase efficiency and reduce costs, because the Postal Service will still be able to retain 100 percent of costs avoided through increased efficiency. Second, the formula for the density rate authority is based on a conservative estimate of how much average cost per piece is *expected* to increase as a result of the decline in density. It does not compensate the Postal Service for the *actual* increase in average cost per piece. Accordingly, the Postal Service is incentivized to assure that actual costs do not rise faster than the formula's expectation. Conversely, to the extent the Postal Service is able to offset some of that expected increase through efficiency improvements and/or reductions to costs within its control, the density rate authority preserves the Postal Service's incentive to do so. Third, the density rate authority adjusts for declines calculated after the effective date of final subpart D of 39 C.F.R. part 3030 (based upon the observed density decline experienced in the most recently ended fiscal year) and does not adjust for prior declines. Because the density rate authority does not include previous losses due to

³⁸⁰ See Order No. 5337 at 64 (describing why the Postal Service does not have direct control over density); Christensen Decl. at 14 ("The exogenous nature of the forces driving changes in mail density, and of the constraints on the Postal Service's ability to adapt to those changes, justifies the Commission's adjustment of the cap for such changes on a Y or Z factor basis."); PR Comments at 5-6 ("[T]he record in this proceeding supports exogenous factor adjustments to the price cap that respond to continuing declines in mail density....").

³⁸¹ See *Sw. Bell Tel. Co. v. FCC*, 28 F.3d 165, 167 (D.C. Cir. 1994) (stating that adjustments for costs that are not controlled by the regulated firm would not undermine the incentive structure of the price cap); PR Reply Comments at 3 (citing Declaration of John Kwoka and Robert Wilson, March 1, 2018, at 8 (Kwoka and Wilson Decl.)) (asserting that the Commission's adjustment to the price cap for declining density is a Z-factor that adjusts for costs that are not under the Postal Service's control and thereby would not affect the Postal Service's incentive to be efficient); Christensen Decl. at 6 ("the exogenous nature of the costs means Y and Z factors do not affect the efficiency incentives of price caps").

declines in density and reflects only the portion of the increase in per-unit costs that would be expected as a result of decline in density, in order to retain earnings the Postal Service will have to reduce costs within its control and increase efficiency in addition to using rate authority.

Because the retirement obligation rate authority targets a driver of the Postal Service's net losses that is outside of its direct control,³⁸² the Commission finds that adequate incentives for the Postal Service to achieve efficiencies and cost reductions remain with the existing levers and approach outlined in the final rule.³⁸³ Additionally, all revenue collected as a result of the retirement obligation rate authority must be remitted towards the corresponding statutory liabilities, as provided under final subpart E of 39 C.F.R. part 3030. This further ensures that this adjustment does not diminish the price cap's inherent incentives to increase efficiency and reduce costs.³⁸⁴

Similarly, the Commission recognizes that the principled adjustment to the existing CPI-U price cap for non-compensatory classes of mail also increases the amount of rate authority available to the Postal Service. This adjustment aims to

³⁸² See Order No. 5337 at 90 ("these congressionally mandated payments are outside of the Postal Service's direct control"); Christensen Decl. at 15 ("Retirement expenses change for reasons either entirely external to the Postal Service (e.g., decisions by the Office of Personnel Management Board of Actuaries) or with only an indirect connection to Postal Service performance.."); PR Comments at 19-20 ("these are exogenous costs and the authority to collect them by means of an adjustment to the price cap is fully supported by established price cap theory and the record in this proceeding.") (omitting internal footnote).

³⁸³ See *Sw. Bell Tel. Co.*, 28 F.3d at 167 ("Because of the [firm's] lack of control, adjustments for such changes [exogenous cost triggered by administrative, legislative or judicial action beyond the control of the firm] presumably do not undermine the price caps' incentive structure."); PR Reply Comments at 3 (citing Kwoka and Wilson Decl. at 8) (asserting that the Commission's adjustment to the price cap for the statutory retirement obligations is a Z-factor that adjusts for costs that are not under the Postal Service's control and thereby would not affect the Postal Service's incentive to be efficient); Christensen Decl. at 6 ("the exogenous nature of the costs means Y and Z factors do not affect the efficiency incentives of price caps").

³⁸⁴ See Christensen Decl. at 15 ("The proposed retirement authority implements a pass-through of exogenous costs and has no adverse incentive properties[.]").

address long-standing issues concerning non-compensatory rates, particularly for Periodicals, which as a class has not covered its attributable costs since the enactment of the PAEA.³⁸⁵ From FY 2007 to FY 2019, the cumulative contribution losses for Periodicals amount to negative \$7.4 billion (FY 2019 ACD at 25), an outcome patently contrary to the PAEA's goals of maximizing the incentives to increase pricing efficiency, assuring financial stability, and establishing and maintaining rates in a range that are just and reasonable, as provided by Objectives 1, 5, and 8.

The final rules addressing non-compensatory classes are consistent with the achievement of Objective 1. The application of the existing CPI-U price cap at a class level limited the Postal Service's ability to set prices for Periodicals that adhered to the principles of allocative efficiency (*i.e.*, compensatory prices). Order No. 4257 at 142. Therefore, the 2 percentage points of rate authority made available for non-compensatory classes is particularly focused on increasing pricing efficiency, a component of Objective 1. See *id.* at 140-142; Order No. 4258 at 85; Order No. 5337 at 164, 168.

Additionally, to clarify the record, the Commission does not take the view that the provision or reduction of rate authority is the only tool that the ratemaking system can use to further the achievement of Objective 1. As explained below, three additional aspects of the existing ratemaking system's design are modified to promote the systemic achievement of Objective 1.

First, under the existing ratemaking system, the Postal Service had flexibility to set prices for non-compensatory products in compensatory classes in a manner that would have increased allocative efficiency. See Order No. 4257 at 141-142. With respect to the most egregious examples (USPS Marketing Mail Flats and Parcels), the

³⁸⁵ See Order No. 4257 at 233-234; Order No. 4258 at 81; Order No. 5337 at 164; see also FY 2019 ACD at 25.

Commission has made efforts to direct the Postal Service to remedy the situation by addressing both costs and prices.³⁸⁶ As the cost-coverage situation for Flats and Parcels has worsened over time, the Commission has escalated its initial regulatory approach of more flexible-style recommendations and directives to more prescriptive rate-setting criteria that would require the rates for Flats and Parcels to increase at least 2 percentage points above the percentage increase for the USPS Marketing Mail class

³⁸⁶ After repeatedly encouraging the Postal Service to use its intra-class price flexibility to reduce the cost-coverage shortfall of Flats, in the FY 2010 ACD, the Commission directed the Postal Service to increase the cost coverage of Flats through a combination of above-average price adjustments and cost reductions. See FY 2010 ACD at 105-106. For a number of years, the Commission monitored the Postal Service's progress and provided additional recommendations. See FY 2011 ACD at 119 (determining not to require remedial action due to the Postal Service's then-pending appeal regarding the FY 2010 directive); Docket No. ACR2012, *Annual Compliance Determination* (Revised May 7, 2013), May 7, 2013, at 116 (FY 2012 ACD) (finding the Postal Service's pricing changes to be responsive to the FY 2010 directive and recommending that the Postal Service derive elasticity estimates to provide for a more realistic assessment of the impact of price changes on contribution); Docket No. ACR2013, *Annual Compliance Determination*, March 27, 2014, at 54-55 (FY 2013 ACD) (same); Docket No. ACR2014, *Annual Compliance Determination*, March 27, 2015, at 47-48 (FY 2014 ACD) (same and further recommending that the Postal Service better quantify cost savings resulting from operational initiatives). Observing some regression of the prior progress toward improving Flats cost coverage, starting with the FY 2015 ACD, the Commission increased its scrutiny of the Postal Service's cost-reduction efforts at an operational level and with regard to quantifying the cost savings of operational initiatives. See Docket No. ACR2015, *Annual Compliance Determination*, March 28, 2016, at 51-65 (FY 2015 ACD) (addressing the continued applicability of the FY 2010 directive and further recommending that the Postal Service better quantify cost savings resulting from operational initiatives for Flats); *id.* at 160-182 (evaluating long-standing cost and service efficiency issues for flat-shaped mailpieces and requiring the Postal Service to provide information aimed at quantifying the results of its operational initiatives); Docket No. ACR2016, *Annual Compliance Determination*, March 28, 2017, at 57 (FY 2016 ACD) (addressing the continued applicability of the FY 2010 directive and further recommending that the Postal Service better quantify cost savings resulting from operational initiatives for Flats); *id.* at 158-171 (evaluating long-standing cost and service efficiency issues for flat-shaped mailpieces and initiating a separate strategic rulemaking to develop enhanced periodic reporting requirements); Docket No. ACR2017, *Annual Compliance Determination*, March 29, 2018, at 59-60 (FY 2017 ACD) (addressing the continued applicability of the FY 2010 directive and further recommending that the Postal Service better quantify cost savings resulting from operational initiatives for Flats); *id.* at 174-182 (evaluating long-standing cost and service efficiency issues for flat-shaped mailpieces and describing the status of the separate strategic rulemaking focused on the development of enhanced periodic reporting requirements).

For a number of years, the Commission approved the Postal Service's approach to improve Parcels cost coverage through above-average price increases. See FY 2010 ACD at 107-108; FY 2011 ACD at 119-120; FY 2012 ACD at 117; FY 2013 ACD at 56; FY 2014 ACD at 50; FY 2015 ACD at 66-67; FY 2016 ACD at 59; FY 2017 ACD at 63.

in the next general Market Dominant rate adjustment.³⁸⁷ The finalized rate-setting criteria for non-compensatory products, which require the Postal Service to increase the rate for any non-compensatory product by a minimum of 2 percentage points above the percentage increase for the class (see final 39 C.F.R. § 3030.221), and prohibit the Postal Service from reducing the rates of non-compensatory products (see final 39 C.F.R. §§ 3030.127(b) and 3030.129(g)) expand the existing incremental approach for improving the allocative efficiency of pricing for Flats and Parcels to each non-compensatory product in a compensatory class. Accordingly, the finalized rate-setting criteria for non-compensatory products are necessary to increase pricing efficiency, consistent with Objective 1.

Second, under the existing ratemaking system, the Postal Service's pricing practices with respect to workshare discounts frustrated the achievement of Objective 1. See Order No. 5337 at 194. Phasing out these inefficient pricing practices under final

³⁸⁷ Starting with the FY 2018 ACD, the Commission accelerated its approach for Flats. See Docket No. ACR2018, *Annual Compliance Determination*, April 12, 2019, at 71 (FY 2018 ACD) (directing the Postal Service to propose a price increase for Flats that is at least 2 percentage points above the class average for USPS Marketing Mail in the next Market Dominant rate adjustment); FY 2019 ACD at 43 (same).

Additionally, in the FY 2018 ACD, the Commission recommended that the Postal Service accelerate its pricing approach to propose a price increase for Parcels that is at least 2 percentage points above the class average for USPS Marketing Mail in the next Market Dominant rate adjustment. See FY 2018 ACD at 78. In the FY 2019 ACD, the Commission made this pricing approach mandatory. See FY 2019 ACD at 46 (directing the Postal Service to propose a price increase for USPS Marketing Mail Parcels that is at least 2 percentage points above the class average for USPS Marketing Mail in the next Market Dominant rate adjustment).

subpart J of 39 C.F.R. part 3030 is also necessary for the ratemaking system to achieve Objective 1.³⁸⁸ As previously stated, this “approach aims to adhere as closely to ECP principles as practicable and therefore achieves the pricing and operational efficiency components of Objective 1 (maximize incentives to increase efficiency).”³⁸⁹

Third, the 10-year review period set by the PAEA was considerably longer than those under several other price cap regimes and the lack of an ability to course-correct at the more typical 4- or 5-year mark likely exacerbated the extent of the observed deficiencies.³⁹⁰ Therefore, the Commission is attentive to ensuring that the ratemaking system will have procedures in place to monitor and safeguard against the system falling out of alignment with the objectives after the implementation of the final rules. To monitor planned and realized cost reductions, and thereby incentivize the Postal Service to improve the robustness of its cost-benefit analyses, the Commission codifies additional reporting requirements in final § 3050.55. These reporting requirements also

³⁸⁸ See Order No. 5337 at 194; see also ABA Comments at 15 (asserting that the workshare discount proposal would “require that USPS move workshare discounts closer to 100 percent of the cost savings to maximize incentives to reduce costs and increase efficiency as required by Objective 1”); NPPC *et al.* Reply Comments at 11 (asserting that “adopting rules designed to move discounts closer to economically efficient levels...will have a beneficial effect on cost reduction and efficiency”); Pitney Bowes Comments at 3 (asserting that “[a] rule requiring that all workshare discounts must be moved successively closer to ECP is consistent with the pricing and operational components of Objective 1”); ANM *et al.* Reply Comments at 29 (asserting that the proposed revisions to workshare discounts “will actually lead to a more efficient and successful Postal Service.”). Additionally, the Postal Service asserts that setting the passthrough floor at 85 percent would be consistent with Objective 1. Postal Service Comments at 49.

³⁸⁹ Order No. 5337 at 193. The Commission also described the benefits of its approach in terms of sending more efficient pricing signals to mailers, improving productive efficiency in the postal sector, and dismissed concerns regarding harms to allocative efficiency. See *id.* at 193, 195-197.

³⁹⁰ See Christensen Decl. at 6 (“Even if the PAEA price cap was properly calibrated at the beginning of the plan, with a formal (and not merely implied) determination that CPI – 0 was an appropriate calibration of the X factor at the time, a ten-year period without a mechanism to perform mid-course corrections is outside the realm of standard practice.”); 2017 Kwoka Decl. at 28-29 (opining that the 10-year period before the first review was unusually long and thereby allowed for design defects and changed circumstances to contribute to the Postal Service’s financial problems and inflict persistent harm on the Postal Service and its customers); see also Willig Decl. ¶¶ 12, 14 (describing price cap plans as typically running for 4 to 5 years between adjustments).

have ancillary benefits that promote the achievement of Objective 1; requiring the Postal Service to identify underlying causes of cost increases would enable the Postal Service to undertake targeted responses to those causes and would allow the Commission to investigate cost increases and evaluate the effectiveness of the Postal Service's operational initiatives more thoroughly. See Section IX.C.3., *supra*. These reporting requirements, which tend to encourage the Postal Service to conduct robust cost-benefit analyses of potential operational changes that may involve the reduction of service standards, engage in prudent and financially sound decision-making, and increase the availability and comprehensibility of information on a regular basis are consistent with Objectives 3, 5, and 6. See Section XIII.E.3., 5., and 6., *infra*. Additionally, the initiation of the separate rulemaking proceeding will focus on whether any enhancements to the ratemaking system can be made to amplify incentives to reduce costs and increase efficiency by introducing a performance incentive mechanism. See Section VI.C., *supra*. Taken together, these changes would afford the Commission important information that would enhance oversight, and thereby promote the Postal Service to make progress on reducing costs and increasing efficiency. Further, the Commission's commitment to conduct a full-scale review in 5 years, subject to Commission discretion to consider aspects of the system sooner (if needed), helps to safeguard against a situation where the system falls out of alignment due to the occurrence of unforeseen circumstances.

2. Objective 2

The changes in the final rules are designed to continue to allow the system to "create predictability and stability in rates," as provided by Objective 2. 39 U.S.C. § 3622(b)(2). The Commission determined that the existing system has generally created predictable and stable rates. Order No. 4257 at 143-144. This determination was based on an evaluation of the timing and magnitude of rate changes. *Id.* at 143-144. The Commission found that the timing of rate changes has been relatively

predictable and consistent, with some timing deviations due to external circumstances that were reasonably forecastable by ratepayers. *Id.* at 143. The Commission found that the magnitude of rate changes “were ‘capable of being consistently forecast’ and did ‘not include sudden or extreme fluctuations’” during the PAEA era. *Id.* at 144.

Some comments appear to suggest that because the existing ratemaking system, which generally limits the annual percentage change in rates to the corresponding percentage change in CPI-U, achieves Objective 2, a system that raises the amount of the annual limitation would necessarily thwart the achievement of Objective 2. *See, e.g.*, C21 Reply Comments at 7; ANM *et al.* Comments at 54. To clarify the record, the Commission does not take the view that limiting the annual percentage change in rates to the corresponding percentage change in CPI-U is the only tool that the ratemaking system can use to achieve Objective 2. As previously explained, this existing annual limitation is a part of the system that *must* be reviewed and *may* potentially be changed or replaced in order to achieve the objectives of 39 U.S.C. § 3622(b) in conjunction with each other. *See* Order No. 5337 at 40-41. The Commission recognizes that the principled adjustments to the existing CPI-U price cap based on declining density, retirement obligations, and non-compensatory classes increase the amount of rate authority available to the Postal Service. These principled adjustments are aimed at addressing the existing ratemaking system’s failure to achieve all of the objectives of 39 U.S.C. § 3622(b) in conjunction with each other.

Multiple commenters express concerns that the finalization of a formula-based approach with components that add rate authority would create more uncertainty and volatility for future rate increases.³⁹¹ With regard to objections to adding three new forms of rate authority to the system after over a decade of operation under the CPI-U annual limitation, it is useful context to note that generally price cap systems allow

³⁹¹ *See, e.g.*, ABA Comments at 7; ANM *et al.* Comments at 19-21; NMA Comments at 7-9; NPPC *et al.* Comments at 20.

rebasing and restructuring after 4 to 5 years. See n.389, *supra*. “The need for adjustments to price caps arises from the fact that price cap formulae are based upon predictions of costs and, over time, divergences between prices and costs are inevitable.”³⁹² Trends outside the direct control of the Postal Service accelerated and exacerbated this divergence and the corresponding impact on the Postal Service after the PAEA’s enactment. See Section XIII.B., *supra*. The longer timeframe between the establishment of the existing system and the implementation of the changes in these final rules tends to exacerbate the misperception that raising the annual limitation would necessarily disrupt predictability and stability. However, the final rules, which modify the implementation of the existing price cap to address the observed systemic deficiencies, account for the achievement of Objective 2 as described below.

An important starting point for this analysis is that the rate authority formula will set the maximum allowable annual rate increase for each class of mail (annual limitation) based on the various components. As the Commission has emphasized, “it would be inappropriate to design a system that lacks a mechanism to limit the magnitude of price adjustments” because doing so would run counter to Objective 2. Order No. 4258 at 34; see Order No. 4257 at 103. Numerous commenters express concern that the final rules, by increasing the annual limitation, would necessarily produce rate increases of a magnitude that would harm ratepayers and the mail system

³⁹² PR Reply Comments 4 (citing 2017 Kwoka Decl. at 9); see PR Comments at 50 (“Price cap theory anticipates the need to adjust price caps when they fail to permit the recovery of costs.”); 2017 Kwoka Decl. at 7 (stating that a price cap “plan that leaves prices unchanged in the face of costs that rise or fall over time—as they surely will—results in the same windfalls or shortfalls that compromise plan objectives in the initialization of prices. Accordingly, price cap plans need to adjust the level of price to reflect changes over time in the economic factors that cause underlying costs to change.”); Kwoka Congressional Testimony at 38 (“even the best-designed formula will inevitably diverge from underlying costs over time raising the question of whether, and how, the regulator should intervene. Failure to intervene may result in persistent, substantial profit windfalls or shortfalls that are unacceptable on both economic and political grounds.”); see *also* Christensen Decl. at 6.

(drive away volume).³⁹³ This concern fails to account for the Commission's findings and analysis, which extensively discusses the deficiencies of the existing ratemaking system and examines these deficiencies by applying the objectives in conjunction with each other. See *generally* Order No. 4257. Notably, the persistent net losses and resulting accumulated deficit significantly impede the financial stability of the Postal Service, contrary to Objective 5. See *id.* at 170-171 (describing how the consecutive net losses resulted in an accumulated deficit); Order No. 4258 at 46-52 (describing how the consecutive net losses resulted in an accumulated deficit and that capital investments declined sharply as the accumulated deficit increased). Moreover, rates under the existing ratemaking system were not excessive to the mailers; instead, rates threatened the financial integrity of the Postal Service, contrary to Objective 8. See Order No. 4257 at 274-275.

Additionally, this concern omits a critical intervening fact: the Postal Service retains discretion not to use all of the rate authority provided by the final rules. The Postal Service has this discretion under the existing system; however, given the relatively low amount of rate authority generated under the existing price cap, the Postal Service's exercise of this discretion (such as by banking rate authority, proposing

³⁹³ See, e.g., ABA Comments at 1-2, 10-11; AFPA Comments at 3; ANM *et al.* Comments at 38 (citing Brattle Decl. ¶ 40); ANM *et al.* Reply Comments at 2; Discover Comments at 4; eBay Comments at 3-4; NPPC *et al.* Comments at 22-23; PSA Comments at 6; NPPC *et al.* Comments at 22-23, 36-38.

promotional or discount rates, proposing rate decreases, or forbearing increases) has been limited.³⁹⁴ The larger amount of rate authority available for use increases the Postal Service's opportunity and capacity to use its business judgment to smooth out rate adjustments. The authority to establish reasonable and equitable classes of mail and rates of postage is vested primarily in the Governors of the Postal Service. 39 U.S.C. § 404(b). The Postal Service has indicated that it is attentive to not allowing rates to increase too sharply, notwithstanding its market power.³⁹⁵ Therefore, the combination of a price cap and the Postal Service's inherent incentives to exercise business judgment combine to promote predictability and stability of rates overall under the final rules, while also allowing for additional rate authority that the Commission finds to be necessary for the achievement of other objectives. Further, the Commission commits to monitoring for any evidence that pricing decisions are exacerbating volume declines and evaluating if such results would justify adjusting these final rules in the next system review in 5 years.

Additionally, it is important to observe that public utility regulators have accepted rates based on formulae since the early 1970s.³⁹⁶ "[A]cceptance of formula rates is

³⁹⁴ See Library Reference PRC-LR-RM2017-3/1, Excel file "PRC-LR-RM2017-3-1.xlsx," tab "Figure II-3" (average annual percentage change in the CPI-U of 1.83 percentage points, ranging as low as -0.634 percentage points in October 2009 and as high as 4.5 percentage points in October 2008); *id.* tab "Table II-3" (cumulatively the Postal Service has not banked more than 0.25 percentage points for First-Class Mail, USPS Marketing Mail, Periodicals, and Package Services).

Even over a longer period of time, the trend holds. From January 2005 to September 2020, the annual percentage change in the CPI-U has been on average 1.83 percentage points, and the Postal Service has not banked more than 0.4 percentage points for First-Class Mail, USPS Marketing Mail, Periodicals, and Package Services. The CPI-U data are published on the Commission's website, available at: <http://www.prc.gov>; hover over "References" and follow the "CPI Figures" hyperlink.

³⁹⁵ See Postal Service Reply Comments at 18 ("The risk that using too much pricing authority will permanently harm the Postal Service's financial position will necessarily be an important consideration in the Governors' pricing decisions.").

³⁹⁶ See *Pub. Utils. Comm'n v. FERC*, 254 F.3d 250, 254 (D.C. Cir. 2001) (citing *Me. Yankee Atomic Power Co.*, 42 F.E.R.C. ¶ 61,307, 61,923 (1988)).

premised on the rate design's 'fixed, predictable nature,' which both allows a utility to recover costs that may fluctuate over time and prevents a utility from utilizing excessive discretion in determining the ultimate amounts charged to customers."³⁹⁷ Public utility regulators evaluate if the various components of the formula are predictable and adjustments to the numerical values assigned to the components of the formula can be made in essentially a mechanical fashion. See *Ocean State Power II*, 69 F.E.R.C. at 61,552. Below, the Commission evaluates the predictability and stability of each component of the formula for calculating the maximum amount of rate adjustment authority. Each of these new forms of rate authority that raise the amount of the existing annual limitation are designed to enable the modified ratemaking system to achieve predictable and consistent timing of rate changes, a forecastable magnitude of rate changes, and minimization of sudden or extreme fluctuation.

While a number of commenters express concern that the Postal Service may vary the magnitude and/or timing of rate adjustments for certain products and/or rate cells,³⁹⁸ it is also important to reiterate that Objective 2 cannot be read in isolation. The system of ratemaking, as modified by this Order, will continue to apply the price cap at the class level.³⁹⁹ This class-level application remains consistent with Objective 8, which "shall not be construed to prohibit the Postal Service from making changes of unequal magnitude within, between, or among classes of mail." 39 U.S.C. § 3622(b)(8).

³⁹⁷ *Pub. Utils. Comm'n*, 254 F.3d at 254 (quoting *Ocean State Power II*, 69 F.E.R.C. ¶ 61,146, 61,552 (1994)) (internal citation omitted).

³⁹⁸ Each of the Market Dominant classes consists of multiple products. The term product "means a postal service with a distinct cost or market characteristic for which a rate or rates are, or may reasonably be, applied." 39 U.S.C. § 102(6). Within each product, there may be multiple rate cells, which refer to each price.

³⁹⁹ Because certain Postal Service pricing practices were identified as being inefficient and therefore contrary to Objective 1, particular rate-setting criteria that apply below the class level are adopted to maximize the Postal Service's incentives to increase pricing efficiency for non-compensatory products and workshare discounts. See final 39 C.F.R. §§ 3030.127(b), 3030.129(g), and 3030.221, and subpart J of 39 C.F.R. part 3030. These rate-setting criteria do not affect the amount of rate authority available.

Moreover, this class-level application continues to allow the Postal Service pricing flexibility to vary the size of rate changes at the product and rate cell levels, consistent with Objective 4.

The Commission has given due consideration to how the modified ratemaking system would achieve predictability and stability of rates in the design of its density rate authority formula component. First, the density rate authority formula is designed to conservatively approximate the amount by which average cost per piece is expected to *unavoidably* increase in the near term as a result of the decline in density as remaining costs are distributed over fewer pieces, thereby reigning in the magnitude of potential rate increases.⁴⁰⁰ Second, annual fluctuations in the resulting amount of rate authority made available each fiscal year are expected to occur due to the operation of the formula. The formula is designed to limit such fluctuations to reflect the expected unavoidable cost increases resulting from density declines.⁴⁰¹ The Commission commits to monitoring for any evidence that pricing decisions are exacerbating volume declines and evaluating if such results would be reason to adjust these final rules in the next system review. Moreover, the Commission will allow the Postal Service to bank unused density rate authority so as to give the operator the ability to smooth out the rate increases over time.⁴⁰² Third, basing the density rate authority formula on actual measured per-unit cost increases caused by the corresponding actual measured annual decline in density rather than on projections avoids the need to design an additional adjustment to correct for inaccurate projections, further reducing fluctuation. Fourth, the

⁴⁰⁰ See Order No. 5337 at 70, 75-76 (explaining how the Commission's approach is more conservative than targeting a net revenue position as suggested by the Public Representative or a revenue-weighted measurement of declines as suggested by the Postal Service); see also Section IV.A., IV.B.2., IV.C.1., and IV.C.2., *supra* (discussing how the formula estimates the expected increase in per-unit costs rather than an observed increase in actual per-unit costs).

⁴⁰¹ See Order No. 5337 at 75; see also Section IV.B.2., *supra*.

⁴⁰² As described previously, the existing annual limitation, which generates rate authority based on the percentage change in the CPI-U, has provided a relatively low amount of rate authority. See n.393, *supra*.

density rate authority formula is designed to approximate declining density for Market Dominant products as a whole rather than focusing on individual mail classes, which would produce more fluctuation. Fifth, the inputs to the density rate authority formula are transparent, and the corresponding calculation of the rate authority eligible for use in a particular fiscal year will be publicly knowable on a predictable basis. By December 31 of each year, the Postal Service must file a notice with the Commission demonstrating whether or not density rate authority is eligible for authorization, and the Commission will announce its final determination on eligibility.

The Commission has given consideration to how the modified ratemaking system would achieve predictability and stability of rates in the design of its retirement obligation rate authority formula component. First, the retirement obligation rate authority is designed to phase in the increase to the rate base over 5 years. This phase-in mechanism is designed to encourage regular and stable timing and a smaller magnitude of rate increases each year over the 5-year period rather than apply a one-time increase of the full amount of the retirement obligation rate authority. Second, annual fluctuations in the amount of retirement obligation rate authority are limited to the extent such fluctuations are necessary to ensure that the Postal Service receives the appropriate amount of revenue at the end of the 5-year phase-in period. After the 5-year phase-in period, ratepayers are no longer subject to additional fluctuation in rate increases based on the retirement obligation rate authority. Third, basing the retirement obligation rate authority formula on the actual measured changes in the amount of the Postal Service's liability and actual measured volume rather than on projections avoids

the need to design an additional adjustment to correct for inaccurate projections, further reducing fluctuation.⁴⁰³ Fourth, the retirement obligation rate authority is designed to limit the amount of the rate authority eligible for use for each class of Market Dominant products to the amount that rates would have to increase on all products (both Market Dominant and Competitive products) to generate enough revenue to make the full amortization payments. Consequently, the formula design presumes that an equal rate increase will be applied to Competitive products and thus further limits the magnitude of the potential rate increases applied to Market Dominant products. Fifth, the inputs to the retirement obligation rate authority formula are transparent, and the corresponding calculation of the rate authority eligible for use in a particular fiscal year will be publicly knowable on a predictable basis. By December 31 of each year, the Postal Service must file a notice with the Commission demonstrating whether or not retirement obligation authority is eligible for authorization and the Commission will announce its final determination on eligibility.

The Commission has given consideration to how the modified ratemaking system would achieve predictability and stability of rates in providing 2 percentage points of rate authority for non-compensatory classes. First, the amount of rate authority made available is designed as an incremental approach to conservatively narrow the long-standing cost-coverage gap.⁴⁰⁴ Second, allowing a finite amount of rate authority over a finite period of time strikes a reasonable balance among Objectives 1, 2, 5, and 8, which

⁴⁰³ With regard to the suggestion that the Commission should not take any action on this issue due to pending legislative action (see NMA Comments at 14; NNA Comments at 18), in the event that Congress takes action that would alter OPM's payment calculation, the formula's inputs are designed to incorporate such updates through the annual recalculation. Transparently adjusting for such changes would be a reasonable fluctuation. If Congressional action warrants reexamination of the final rules sooner, the Commission commits to exercising its rulemaking authority to do so. See 39 U.S.C. § 3622(d)(3).

⁴⁰⁴ See Order No. 5337 at 168-170. Notably, the Public Representative in advocating for a one-time reset of the price cap for Periodicals characterizes the Commission's approach as "accord[ing] too much weight to stability and reasonableness and far too little weight to producing adequate revenue." PR Comments at 50.

require the system to provide predictability and stability to ratepayers, improve allocative efficiency, promote the Postal Service to focus on increasing operational efficiency and cost reductions, improve financial integrity, and move rates into the range of prices that is just and reasonable. Moreover, the Commission will allow the Postal Service to bank unused rate authority for non-compensatory classes so as to give the operator the ability to smooth out the rate increases over time. Third, the primary source of fluctuation will be if a class changes from compensatory to non-compensatory, which will be made known to the public transparently on a predictable basis. By December 31 of each year, the Postal Service must file a notice with the Commission demonstrating whether or not rate authority is eligible for authorization for a particular class and the Commission will announce its final determination on eligibility.

The existing rate authority provided by the change in the CPI-U with limited ability to bank such authority for future use does not disrupt predictability and stability. Moreover, providing the Postal Service with the limited ability to bank additional forms of rate authority for declining density and for non-compensatory classes for future use ensures that the system will not create a perverse incentive for the Postal Service to raise rates faster than the market can bear. Consistent with the existing requirements, the Postal Service would still be limited to using no more than 2 percentage points of banked rate authority per class per year and banked rate authority would still expire after 5 years.

Additionally, the Commission has demonstrated consideration for the achievement of Objective 2 in other aspects of its final rules. Final § 3030.221, which requires the Postal Service to increase the rate for any non-compensatory product by a minimum of 2 percentage points above the percentage increase for the class, represents a natural expansion of the Commission's existing approach to USPS

Marketing Mail Flats⁴⁰⁵ and Parcels⁴⁰⁶ to all non-compensatory products. Maintaining this steady incremental approach,⁴⁰⁷ rather than adopting alternatives such as accelerating required increases to be at least 3 percentage points above the percentage increase for the class or raising the price cap to specifically address this issue (see Order No. 5337 at 158-161), demonstrates the balancing of predictability and stability with the need to increase cost coverage for non-compensatory products, consistent with the aims of Objectives 1, 5, and 8. Final §§ 3030.127(b) and 3030.129(g), which prohibit the Postal Service from reducing the rates of non-compensatory products, are baseline rules that also promote stability and predictability of rates.

Final subpart J of 39 C.F.R. part 3030 also takes an incremental approach to phase out inefficient pricing practices. The Commission's approach to regulating workshare discounts gives consideration to promoting price changes that would be incremental in timing and magnitude and provides customers sufficient advance notice to plan their mailing budgets, consistent with the purpose of Objective 2. The final rules encourage the Postal Service to phase out excessive workshare discounts incrementally by 20 percent in each rate adjustment. For rare cases where reducing an excessive workshare discount by 20 percent could lead to rate shock, there is a process in place by which the Postal Service can seek a waiver of this rule. Similarly, to promote incremental improvement (and eventual phase out) of workshare discounts that

⁴⁰⁵ See FY 2018 ACD at 71 (directing the Postal Service to propose a price increase for USPS Marketing Mail Flats that is at least 2 percentage points above the class average for USPS Marketing Mail in the next Market Dominant rate adjustment); FY 2019 ACD at 43 (same).

⁴⁰⁶ See FY 2018 ACD at 78 (recommending that the Postal Service propose a price increase for USPS Marketing Mail Parcels that is at least 2 percentage points above the class average for USPS Marketing Mail in the next Market Dominant rate adjustment); FY 2019 ACD at 46 (making the prior directive mandatory for FY 2020).

⁴⁰⁷ Reaching the mandatory minimum rate increase of 2 percentage points above the class average for USPS Marketing Mail Flats and Parcels (two of the most egregious examples of a non-compensatory product in a compensatory class) was itself an incremental process, as detailed in notes 385 and 386, *supra*.

are below their avoided costs, the final rules encourage the Postal Service to gradually increase the workshare discounts by at least 20 percent or increase the workshare discount to produce a passthrough of at least 85 percent.⁴⁰⁸ For rare cases where raising the proposed workshare discount by at least 20 percent (or to produce a passthrough of at least 85 percent) could impede the Postal Service's operational efficiency, there is a process in place by which the Postal Service can seek a waiver of this rule.

Additionally, the Commission will finalize procedural changes that are aimed at improving mailers' ability to predict rate changes (and thereby generate their mailing budgets) by enhancing the schedule for regular and predictable rate adjustments and requiring the Postal Service to file a rate adjustment filing at least 90 days prior to planned implementation.⁴⁰⁹ Furthermore, committing to review the system in 5 years, subject to Commission discretion to consider aspects of the system sooner (if needed), balances the competing priorities of setting a review period that would be both short enough to safeguard against any potential unintended consequences (by contrast the 10-year review period set by the PAEA was, in hindsight, too long⁴¹⁰) and long enough to allow the effects of the changes to be observed. Finally, declining to implement the provision of 1 percentage point of performance-based rate authority will allow for less potential fluctuation in rate increases than if the Commission implemented the performance-based rate authority at this time. The Commission will undertake a rulemaking to evaluate whether, when, and how to introduce a performance incentive mechanism (see Section VI.C., *supra*) through notice-and-comment procedures in order

⁴⁰⁸ The Postal Service asserts that setting the passthrough floor at 85 percent would be consistent with Objective 2. Postal Service Comments at 49.

⁴⁰⁹ See final 39 C.F.R. §§ 3030.102 and 3030.121. Pitney Bowes supports these extensions of the procedural schedule as consistent with Objective 2. Pitney Bowes Comments at 8.

⁴¹⁰ See n.389, *supra*.

to ensure that its outcome would not be sudden or disruptive to the ratemaking system, thereby further showing consideration for the continued achievement of Objective 2.

3. Objective 3

The finalized changes are designed to address the systemic issues underlying the existing system's failure to "maintain high quality service standards established under section 3691," as provided by Objective 3. 39 U.S.C. § 3622(b)(3). The Commission determined that the PAEA's goals relating to service were not achieved under the existing system. Order No. 4257 at 250. More specifically, the Commission found that the existing system did not effectively encourage the maintenance of high-quality service standards. *Id.* The Commission observed that service standards declined during the PAEA era, because the Postal Service reduced the high-quality service standards that were set in 2007. *Id.* at 273.

As described below, past experience evidences that the existing system lacked an effective mechanism to incentivize the Postal Service to perform a meaningful analysis of the potential service performance effects and cost savings prior to implementing changes to its service standards. *See id.* at 201-203. This deficiency

was especially compounded by the focus on aggressively managing costs, which did have an impact on service.⁴¹¹ The Postal Service proceeded to implement both its “Mail Processing Network Rationalization” initiative beginning in FY 2012,⁴¹² and its “Standard Mail Load Leveling” initiative beginning in FY 2014,⁴¹³ notwithstanding the conclusions and recommendations of the Commission that the Postal Service should perform additional analysis of the potential effects before proceeding.⁴¹⁴ The Postal Service’s exercise of its authority to change the service standards in the past has not realized the

⁴¹¹ See, e.g., Order No. 4257 at 255 (“There is ‘the potential to cut costs by way of service reductions to comply with price cap requirements.’”) (quoting Postal Regulatory Commission, Section 701 Report, Analysis of the Postal Accountability and Enhancement Act of 2006, September 22, 2011, at 58); NWPC Report 2 at 87 (“This matching of resources can be indirectly attributed to cost management strategies, including ones that traded service downgrades for cost savings.”); NWPC Report 2 at 88 (“However, the focus on aggressively managing costs did have an impact on service. The Service Standard Realignment first reduced Overnight First Class Mail coverage, then eliminated it almost entirely. The service performance did not generally meet goals after the change, leading to the suspension of the Network Consolidation program and additional resources to improve service performance.”); 2017 Kwoka Decl. at 18-19 (describing the reduction of First-Class Mail service standards as one of the Postal Service’s efforts to reduce its costs post-PAEA); 2017 Kwoka Decl. at 21 (“As noted earlier, price cap plans generally have some incentives to reduce quality in order to lower cost, but in the present case these shortfalls seem more likely the result of the financial difficulties of the Postal Service and the need to conserve on current expenditures. Deferred vehicle replacement, workforce reductions, and capital expenditure cutbacks are all suggestive of a setting where service quality as well as everything else has been pre-empted by the overriding need for cost cutting. Service quality would appear to be an issue of on-going concern.”); 2006 Joskow at 29 (“Deferred maintenance (e.g. tree trimming) and deferred capital expenditures may lead to the deterioration of service quality in either the short run or the long run or both.”).

⁴¹² See Revised Service Standards for Market-Dominant Mail Products, 77 Fed. Reg. 31,190 (May 25, 2012) (codified at 39 C.F.R. pt. 121).

⁴¹³ See Service Standards for Destination Sectional Center Facility Rate Standard Mail, 79 Fed. Reg. 12,390, 12,393 (March 5, 2014) (codified at 39 C.F.R. pt. 121).

⁴¹⁴ See Docket No. N2012-1, Advisory Opinion on Mail Processing Network Rationalization Service Changes, September 28, 2012, at 45-46 (concluding that “it is possible for the Postal Service to undertake significant network rationalization and realize substantial cost savings while preserving most current service levels” and encouraging “the Postal Service to consider the advice in this opinion and study the effects of the service standard changes implemented on July 1, 2012, before going forward with Phase 2, and its further reductions in service”); Docket No. N2014-1, Advisory Opinion on Service Changes Associated with Standard Mail Load Leveling, March 26, 2014, at 1 (recommending that the Postal Service “undertake a more rigorous cost-benefit analysis, additional field testing and service performance analysis, and volume impact studies before committing to a nationwide rollout of the Load Leveling Plan”).

planned cost savings or efficiency gains⁴¹⁵ and has altered its network in ways that have resulted in a decreased level of service performance results for some Market Dominant products.⁴¹⁶

The final rules realign the system to address these deficiencies, and thereby promote the achievement of Objective 3. The Commission's prior approaches to addressing Objective 3 included a proposal to make available 1 percentage point of performance-based rate authority, conditioned on the Postal Service exceeding an operational efficiency-based requirement and adhering to service standard-based criteria. See Section VI.A., *supra*. After considering the numerous comments opposed to this proposal, including those claiming that it would not address Objective 3 in a meaningful way, the Commission finds that this proposal requires further study. See Section VI.B.-C., *supra*. As discussed above, the Commission will initiate a new rulemaking proceeding that will evaluate potential refinements to this proposal, including

⁴¹⁵ The revisions to the First-Class Mail service standards enabled the Postal Service to expand its mail processing operational window to process mail on fewer machines, thus using less facility square footage. United States Postal Service, Office of the Inspector General, Report No. NO-AR-19-001, Operational Window Change Savings, October 15, 2018, at 1, available at: <https://www.uspsoig.gov/sites/default/files/document-library-files/2018/NO-AR-19-001.pdf> (NO-AR-19-001). The Postal Service OIG determined that the Postal Service did not achieve its projected cost savings or efficiency gains from this change, referred to as the Operational Window Change (OWC). See *id.* (determining that the Postal Service achieved only \$323.48 million of its projected \$1.61-billion savings in FYs 2016 and 2017 and that mail processing costs increased by \$153 million and mail processing productivity declined by 14 percent since the OWC); United States Postal Service, Office of the Inspector General, Report No. NO-AR-16-009, Mail Processing and Transportation Operational Changes, September 2, 2016, at 9, available at: <https://www.uspsoig.gov/sites/default/files/document-library-files/2016/NO-AR-16-009.pdf> (NO-AR-16-009) (determining that in the first year after the OWC, the Postal Service achieved only approximately 10 percent of its projected \$805-million savings, transportation costs exceeded the planned budget by over \$200 million, and mail processing productivity decreased by 4.5 percent).

⁴¹⁶ See, e.g., FY 2015 ACD at 133 (citing Docket No. ACR2015, Library Reference USPS-FY15-29, December 29, 2015, at 8, 9; Docket No. ACR2015, Responses of the United States Postal Service to Questions 15-26 of Chairman's Information Request No. 2, January 19, 2016, question 19.a.); NO-AR-19-001 at 3; NO-AR-16-009 at 1-2.

the aspect aimed at maintaining service standards, applying the objectives in conjunction with each other. See Section VI.C., *supra*.

The principled adjustments to the price cap made in this Order are necessary to achieve the objectives of the PAEA, in conjunction with each other, and are focused on vital near-term improvements. The Commission provides rate authority to account for underlying drivers of the financial distress, to which the Postal Service responded with an aggressive attempt to cut costs by reducing service standards. For instance, rate authority addressing underlying financial pressures puts the Postal Service in a position to increase its revenue and thereby generate funds that would otherwise not be available. While the density-based rate authority and retirement-based rate authority are designed to address only cost effects outside of the direct control of the Postal Service, in the absence of the revenue it will generate, the Postal Service may offset those cost increases by further reducing service standards if it is unable to sufficiently reduce costs within its control. This aspect of the modified ratemaking system serves to reinforce the goals of Congress.⁴¹⁷

Moreover, the reporting requirements address the concerns regarding the Postal Service's past decisions to implement such changes based on its overly ambitious estimates of cost savings, against the advice of the Commission. The Commission finds that regulations in final § 3050.55, which help ensure the robustness of the Postal Service's cost-benefit analyses of potential operational changes that may involve the reduction of service standards, would further the achievement of Objective 3, in conjunction with the other objectives, particularly Objectives 1, 5, and 6. See Section XIII.E.1., *supra*; Section XIII.E.5. and 6., *infra*. In the new rulemaking it will be initiating, the Commission will invite commenters to include views on whether additional

⁴¹⁷ Legislative history indicates that the Senate recognized that providing the Postal Service with the opportunity to retain earnings (rather than merely break-even as limited by the PRA) would provide the Postal Service with a resource to meet service standards and its universal service obligation. S. Rep. No. 108-318 at 8-9 (2004).

information would be helpful in the rulemaking to evaluate whether, when, and how to introduce a performance incentive mechanism (see Section VI.C., *supra*), as the Commission considers whether further rulemaking adjustments would be beneficial to maintain high-quality service standards.

With respect to service standards, the Commission notes that the PAEA and federal regulations require the Postal Service to give advance notice of plans to change its service standards.⁴¹⁸ Additionally, in the separate rulemaking the Commission will

⁴¹⁸ 39 U.S.C. § 3661(b) (requiring the Postal Service to “submit a proposal [to change the nature of postal services that will generally affect service on a nationwide or substantially nationwide basis], within a reasonable time prior to the effective date of such proposal, to the Postal Regulatory Commission requesting an advisory opinion on the change.”); 39 C.F.R. § 3020.112 (requiring the Postal Service to file notice of any changes to the nature of postal services that will generally affect service on a nationwide or substantially nationwide basis at least 90 days in advance); 39 C.F.R. § 3055.5 (requiring the Postal Service to file notice of any changes to service standards at least 30 days in advance).

Further, the Postal Service acknowledges that “...there arguably is already a process for third parties to seek Commission adjudication of whether the Postal Service somehow implemented a service standard change without proper notice: namely, the complaint process.” Postal Service Comments at 42 n.25 (citations omitted). A complaint may be filed with the Commission if the Postal Service is not operating in conformance with the requirements of chapter 36 of title 39 of the United States Code; 39 U.S.C. §§ 101(d), 401(2), 403(c), 404a, or 601; or any rule, order, or other regulatory requirement based on any of those statutory provisions. 39 U.S.C. § 3662(a); 39 C.F.R. § 3022.2. The Commission further observes that a complaint may be filed by “[a]ny interested person (including a duly appointed officer of the [Postal Regulatory Commission] representing the interests of the general public).” 39 C.F.R. § 3022.2; see 39 U.S.C. § 3662(a). The Postal Service’s compliance with 39 U.S.C. § 3661(b) has also been directly enforced through the federal courts. See *Buchanan v. U.S. Postal Serv.*, 508 F.2d 259, 265-267 (5th Cir.1975) (affirming issuance of preliminary injunction pending hearing and issuance of an advisory opinion by the Postal Rate Commission as to implementation of the retail access program, alleged to be a decision-making process to relocate and alter postal facilities on a nationwide or substantially nationwide basis); see also *Am. Postal Workers Union, AFL-CIO v. U.S. Postal Serv.*, No. CIV.A.06 726 CKK, 2007 WL 2007578, at *7 (D.D.C. July 6, 2007) (finding that the court may exercise jurisdiction, pursuant to 39 U.S.C. § 409, to review a claim that the Postal Service violated § 3661 by allegedly implementing a change prior to issuance of the applicable advisory opinion); *Nat’l Ass’n for the Advancement of Colored People v. U.S. Postal Serv.*, No. 20-CV-2295(EGS), 2020 WL 5995032, at *8-11 (D.D.C. Oct. 10, 2020) (exercising jurisdiction over a claim relating to the alleged failure of the Postal Service to undertake the process mandated under 39 U.S.C. § 3661(b) in making nationwide changes to service and entering preliminary injunction); *Commonwealth of Penn. v. Dejoy*, No. CV 20-4096, 2020 WL 5763553, at *14, 22, 39 (E.D. Pa. Sept. 28, 2020) (exercising jurisdiction over a claim relating to the alleged failure of the Postal Service to undertake the process mandated under 39 U.S.C. § 3661(b) in making nationwide changes to service and based on a finding that Congressional intent to preclude district courts from hearing claims relating to 39 U.S.C. § 3661(b) is not fairly discernible from the statutory text, structure, or legislative history and entering preliminary injunction); *New York v. Trump*, No.

explore if further rule changes would be beneficial to maintaining high-quality service standards, such as the potential impact of introducing a performance incentive mechanism into the ratemaking system. See Section VI.C., *supra*.

As previously stated, Objective 3 also implicitly requires consistent achievement of service standards, otherwise known as “service performance.” See Order No. 4257 at 262-263. The existing regulatory system has a mechanism to hold the Postal Service accountable for its service performance.⁴¹⁹ Additionally, other aspects of the final rules make changes to the system that would tend to promote service performance achievement. The rate authority addressing near-term financial pressures puts the Postal Service in a position to increase its revenue and thereby potentially have additional funds to address service performance. Additionally, final § 3050.55, which helps ensure the robustness of the Postal Service’s cost-benefit analyses of potential operational changes that may affect service performance, would further the achievement of Objective 3, in conjunction with the other objectives, particularly Objectives 1, 5, and 6. See Section XIII.E.1., *supra*; Section XIII.E.5. and 6., *infra*.

20-CV-2340(EGS), 2020 WL 5763775, at *6-10 (D.D.C. Sept. 27, 2020) (exercising jurisdiction over a claim relating to the alleged failure of the Postal Service to undertake the process mandated under 39 U.S.C. § 3661(b) in making nationwide changes to service and entering preliminary injunction); *Washington v. Trump*, No. 1:20-CV-03127-SAB, 2020 WL 5568557, at *3 (E.D. Wash. Sept. 17, 2020) (exercising jurisdiction over a claim relating to the alleged failure of the Postal Service to undertake the process mandated under 39 U.S.C. § 3661(b) in making nationwide changes to service and entering preliminary injunction). Further, 39 C.F.R. § 3055.5 reserves the Commission’s ability to initiate a proceeding at any time regarding planned changes to service standards, noting as an example that a planned reduction in service standards might change the nature of a product and thereby amount to a classification change. Docket No. RM2009-11, Order Establishing Final Rules Concerning Periodic Reporting of Service Performance Measurements and Customer Satisfaction, May 25, 2010, at 38 n.25 (Order No. 465).

⁴¹⁹ See Order No. 4257 at 264. The Commission’s ACD aims to promote the Postal Service’s identification and implementation of best practices that drive local facilities’ adherence to the existing multi-year national data-driven strategies and processing targets. See FY 2019 ACD at 107-115, 118-121.

Accordingly, the Commission's rules demonstrate adequate consideration of how the modified ratemaking system would achieve Objective 3, in conjunction with the other objectives.

4. Objective 4

The finalized changes are designed to continue to allow the system to "allow the Postal Service pricing flexibility," as provided by Objective 4. 39 U.S.C. § 3622(b)(4). The Commission found that the existing system has allowed for pricing flexibility on a number of dimensions by allowing the Postal Service to exercise broad discretion over the prices, the price structure, and the timing of price changes. Order No. 4257 at 144.

The new forms of rate authority (density rate authority under final subpart D of 39 C.F.R. part 3030, retirement obligation rate authority under final subpart E of 39 C.F.R. part 3030, and non-compensatory rate authority under final § 3030.222) will provide the Postal Service with considerably more ability to adjust rates than provided under the existing CPI-U price cap: increases may be higher and vary more between rate cells and products than allowed under the existing CPI-U price cap. Therefore, to some extent, these final rules increase pricing flexibility. However, each of these new forms of rate authority is subject to limitations. The amount of density rate authority is limited by a formula designed to approximate the amount by which average cost per piece is expected to unavoidably increase in the near term, as a result of the decline in density, as remaining costs are distributed over fewer pieces. The amount of retirement obligation rate authority is limited by a formula designed to approximate the amount of specifically identified exogenous costs required by the PAEA and calculated by OPM, over which the Postal Service has minimal control. Two percentage points of rate authority may also be allocated to each non-compensatory class per annum, at the Postal Service's discretion.

The retirement obligation rate authority is subject to a further limitation requiring revenue collected to be remitted towards the Postal Service's retirement liabilities to improve the Postal Service's ability to achieve net income by making payments towards its outstanding liability. Market Dominant ratepayers asked to pay higher rates for the purposes of making payments toward the Postal Service's retirement liabilities have a reasonable expectation that the funds will be used for that purpose. This rate authority is a tool the Postal Service may use to raise revenue to remit toward its statutorily mandated payments, but the decision whether or not to make use of that authority to raise rates is entirely within the business discretion of the Postal Service. Therefore, this limitation rationally balances the competing priorities of allowing pricing flexibility, improving the Postal Service's ability to achieve net income by making payments toward its outstanding liability, and ensuring that the schedule of rates would be in the range that is just and reasonable, as provided by Objectives 4, 5, and 8.

Under the existing ratemaking system, the Postal Service may only bank rate authority provided by the change in the CPI-U for future use, expiring after 5 years and using no more than 2 percentage points per class per year. Because on average, the change in the CPI-U has provided less than 2 percentage points of rate authority per annum, the Postal Service has generally exhausted that rate authority.⁴²⁰ The modified ratemaking system would allow the Postal Service to also bank additional forms of rate authority for declining density and for non-compensatory classes, thereby increasing the Postal Service's pricing flexibility compared to the existing ratemaking system.

⁴²⁰ See Library Reference PRC-LR-RM2017-3/1, Excel file "PRC-LR-RM2017-3-1.xlsx," tab "Figure II-3" (average annual percentage change in the CPI-U of 1.83 percentage points); *id.* tab "Table II-3" (cumulatively the Postal Service has not banked more than 0.25 percentage points for First-Class Mail, USPS Marketing Mail, Periodicals, and Package Services).

Even over a longer period of time, the trend holds. From January 2005 to September 2020, the annual percentage change in the CPI-U has been on average 1.83 percentage points, and the Postal Service has not banked more than 0.4 percentage points for First-Class Mail, USPS Marketing Mail, Periodicals, and Package Services. The CPI-U data are published on the Commission's website, available at: <http://www.prc.gov>; hover over "References" and follow the "CPI Figures" hyperlink.

Additionally, allowing this pricing flexibility would give the operator increased ability to smooth out rate increases over time, thereby demonstrating that the modified ratemaking system is designed to achieve Objectives 2 and 8. Consistent with the existing requirements, the Postal Service would still be limited to using no more than 2 percentage points of banked rate authority per class per year and banked rate authority would still expire after 5 years, so as to further reinforce Objectives 2 and 8.

The Commission recognizes that stricter regulation of non-compensatory products limits the Postal Service's pricing flexibility. However, the PAEA did not intend for the Postal Service to have unrestrained pricing authority for its Market Dominant products as evidenced by the competing goals of increased efficiency, assuring financial stability, and maintaining a just and reasonable rate schedule encapsulated by Objectives 1, 5, and 8. The finalized rate-setting criteria for non-compensatory products, which require the Postal Service to increase the rate for any non-compensatory product by a minimum of 2 percentage points above the percentage increase for the class, represent a natural expansion of the Commission's existing approach for USPS Marketing Mail Flats and Parcels to all non-compensatory products. As the cost-coverage situation for Flats and Parcels has worsened over time, the Commission has escalated its regulatory approach from more flexible-style recommendations and directives to more prescriptive rate-setting criteria.⁴²¹

The argument that final subpart G of 39 C.F.R. part 3030 violates Objective 4 because it does not appropriately recognize the multiplier effect of non-compensatory products (the theory that non-compensatory products may lead to increased compensatory product volume such as invoices and bill payments) (*see ANM et al.*

⁴²¹ The history regarding the escalation to the present mandatory minimum rate increase of 2 percentage points above the class average for USPS Marketing Mail Flats and Parcels (two of the most egregious examples of a non-compensatory product in a compensatory class) is detailed in notes 385 and 386, *supra*.

Comments at 82) lacks adequate support. First, assuming without deciding that any multiplier effect does exist, such effect is already likely in decline due to largely exogenous trends that reduce volume.⁴²² Second, no evidence suggests that any potential compensatory product volume gain linked with the non-compensatory products would outweigh the quantifiably increasing losses sustained by non-compensatory products. From FY 2007 to FY 2019, the cumulative contribution losses are negative \$7.4 billion for Periodicals and negative \$6.7 billion for USPS Marketing Mail Flats.⁴²³ Declining to take an affirmative step to address the long-standing quantifiable losses sustained by non-compensatory products because of a purely speculative concern about the effect on compensatory product volumes would allow for ongoing harm to the Postal Service's financial condition. This would also overly weight the pricing flexibility *allowed* by Objective 4 against the goals of Objectives 1 (increased pricing efficiency), 5 (assured financial stability), and 8 (just and reasonable rates). Moreover, declining to continue the Commission's existing incremental approach to remedying non-compensatory products in a compensatory class would exacerbate the existing cross-subsidy. Third, the Postal Service would retain discretion to exercise business judgment to moderate price increases if market conditions did suggest that a rate increase would harm its financial condition or drive away profitable mail.

Additionally, the Commission recognizes that stricter regulation of workshare discounts limits the Postal Service's pricing flexibility. However, it is also important to acknowledge that the Postal Service had the ability to set workshare discounts in accordance with ECP under the existing ratemaking system, yet chose not to do so.⁴²⁴ The final rules aim to strike a balance between maximizing pricing efficiency and

⁴²² See United States Postal Service, *The Household Diary Study: Mail Use & Attitudes in FY 2019*, May 29, 2020, at 48.

⁴²³ FY 2019 ACD at 25, 34. Flats did not exist as a product in FY 2007; therefore, the losses for Flats were incurred from FY 2008 through FY 2019.

⁴²⁴ See Order No. 4257 at 136-139; Order No. 4258 at 87; Order No. 5337 at 195.

unreasonably restricting the Postal Service's pricing decisions. The final rules will produce passthroughs more in line with ECP principles than the existing rules in place since the PAEA's enactment. The final rules aim for incremental improvement in pricing efficiency and contain specific provisions to allow for transitional flexibility, particularly for new workshare discounts and by setting minimum thresholds for movement towards ECP (improving the existing workshare discount by 20 percent or producing a passthrough between 85 and 100 percent).⁴²⁵ Additionally, the Commission allows for pricing flexibility to deviate from moving towards ECP as required by final §§ 3030.283 and 3030.284, if adequately justified via the waiver process. Finally, these final rules limit only the workshare discount aspect of pricing and do not restrict the setting of the benchmark prices, thereby continuing to allow pricing flexibility.

The Commission recognizes that procedural improvements serve to limit the Postal Service's pricing flexibility with respect to timing of rate adjustment filings. Final § 3030.121, which would require the Postal Service to file a rate adjustment filing at least 90 days prior to planned implementation, is aimed at addressing mailers' concerns about predictability and stability (Objective 2) while also balancing flexibility concerns by using the Postal Service's historic and suggested timeframe. See final 39 C.F.R. § 3030.121. Given that the additional rate authorities increase the amount of rate authority available to the Postal Service, greater transparency and more advance notice would facilitate mailers' ability to plan for increases. Similarly, final § 3030.102, which would enhance the schedule for regular and predictable rate adjustments, would give mailers better advance information to generate mailing budgets and preserve the Postal Service's flexibility to deviate as needed. See final 39 C.F.R. § 3030.102. Taken together, these procedural improvements demonstrate that the modified ratemaking

⁴²⁵ The Postal Service asserts that setting the passthrough floor at 85 percent would be consistent with Objective 4. See Postal Service Comments at 49.

system is designed to achieve Objectives 2 (predictability and stability of rates), 4 (pricing flexibility), and 6 (increased transparency).

5. Objective 5

The finalized changes are designed to address the systemic issues underlying the existing system's failure to "assure adequate revenues, including retained earnings, to maintain financial stability," as provided by Objective 5. 39 U.S.C. § 3622(b)(5).

With respect to the definition of financial stability, measurement metrics used, and scope of the financial analysis, multiple commenters reiterate their position that the Commission's findings are flawed. The Commission has thoroughly considered the issues raised by the commenters and has explained its rationale to: reject using the exigent provision standard as a measurement metric, value real estate in a manner that follows Generally Accepted Accounting Principles, include the statutory obligations of the Postal Service in the financial analysis, and use retained earnings as a key, measurable concept. See Order No. 4257 at 153-159, 169-170.

With respect to the assertions that providing any additional rate authority is unnecessary, the Commission refers to its prior financial analysis, which extensively discusses the deficiencies of the existing ratemaking system and examines these deficiencies by applying the objectives in conjunction with each other. See *generally* Order No. 4257. Multiple commenters claim that the financial instability of the Postal Service is an exaggerated balance sheet issue. For instance, according to NPPC *et al.*, the Commission mischaracterizes the Postal Service's "phantom accounting losses stemming from the retiree obligations" as "'vast net losses' and an 'accumulated deficit.'" NPPC *et al.* Comments at 53 (quoting Order No. 5337 at 106). However, these consecutive net losses and this accumulated deficit significantly impede the financial stability of the Postal Service. See Order No. 4257 at 170-171 (describing how the consecutive net losses resulted in an accumulated deficit); Order No. 4258 at 46-52

(describing how the consecutive net losses resulted in an accumulated deficit and that capital investments declined sharply as the accumulated deficit increased). Notwithstanding the repetition of the claims that the Postal Service's financial problems are illusory and/or exaggerated, analysis from outside experts confirms the Commission's assessment.⁴²⁶

As previously explained, the Postal Service lacks shareholders and instead must finance capital investments through revenue or through borrowing. Order No. 4258 at 48-49. Therefore, as consecutive years of net losses resulted in an accumulated deficit, the Postal Service relied heavily on its borrowing authority, deferred capital investments, and increased its cash reserves.⁴²⁷ Essentially, the Postal Service has used these existing mechanisms to address its more urgent financial challenges driven largely by

⁴²⁶ See, e.g., GAO-20-385 at 13 ("USPS's unfunded liabilities and debt, which consist mostly of unfunded liabilities for retiree health and pension benefits, have become a significant financial burden, increasing from 99 percent of USPS's annual revenues at the end of fiscal year 2007 to 226 percent of its fiscal year 2019 revenues." (footnote omitted)); United States Government Accountability Office, Report to the Chairman, Committee on Oversight and Government Reform, House of Representatives, Report No. GAO-13-112, U.S. Postal Service: Status, Financial Outlook, and Alternative Approaches to Fund Retiree Health Benefits, December 2012, at 2, available at: <https://www.gao.gov/assets/660/650511.pdf> (GAO-13-112) ("We have previously reported that USPS cannot be financially viable until Congress and USPS address the cash flow problems that limit its immediate prefunding capability while also addressing how to pay for the long-term cost of USPS's unfunded retiree health benefit liability."); United States Government Accountability Office, Testimony Before the Committee on Oversight and Government Reform, House of Representatives, GAO-17-404T, U.S. Postal Service: Key Considerations for Restoring Fiscal Sustainability (Statement of Lori Rectanus, Director, Physical Infrastructure Issues), February 7, 2017, at 6, available at: <https://www.gao.gov/assets/690/682534.pdf> (GAO-17-404T) ("As previously discussed, USPS's unfunded liabilities and debt have become a large financial burden, increasing from 99 percent of USPS revenues at the end of fiscal year 2007 to 169 percent of revenues at the end of fiscal year 2016. These unfunded liabilities and debt—totaling about \$121 billion at the end of fiscal year 2016—consist mostly of retiree health and pension benefit obligations for which USPS has not set aside sufficient funds to cover." (footnote omitted)).

⁴²⁷ See Order No. 4258 at 46-52; FY 2019 Financial Analysis at 5 ("The Postal Service built up its cash by taking extraordinary actions to preserve liquidity, including defaulting on its prefunding obligations and failure to make payments towards [the Federal Employees Retirement System (FERS)] and [the Civil Service Retirement System (CSRS)], cutting operating costs, and suspending all but the most essential capital investments."); Postal Service FY 2019 Form 10-K at 40 (The Postal Service has been funding its capital commitments from its "operating activities and defaults or non-payment on certain retirement and retiree healthcare obligations.").

declining density and the statutory obligations related to retirement.⁴²⁸ The new forms of rate authority add mechanisms to the existing ratemaking system that would directly address underlying drivers of these adverse trends.

The apparent improvement in liquidity observed during FY 2019 underscores the extraordinary measures that the Postal Service has had to take to respond to this challenging situation. During FY 2019, the Postal Service reduced its cash and cash equivalents to \$8.8 billion and paid \$2.2 billion to the U.S. Department of the Treasury, which increased its available borrowing authority to \$4 billion.⁴²⁹ As the Commission explains, this improved liquidity is because the Postal Service had not made a payment to the RHBFB since FY 2010, the Postal Service had not made a payment toward the amortization of the unfunded retirement benefits for the FERS and CSRS since FY 2017, and the Postal Service had suspended all but the most essential capital investments. *Id.* at 4, 5. Forcing the Postal Service to take such extraordinary measures to preserve liquidity is patently inconsistent with the PAEA's goal of "assur[ing] adequate revenues, including retained earnings, to maintain financial stability." 39 U.S.C. § 3622(b)(5).

Further, although commenters argue that the Postal Service's financial situation is much better than reflected on its balance sheet, the negative impacts of its challenging situation are real. For example, years of deferring capital investments has

⁴²⁸ See, e.g., 2017 Kwoka Decl. at 28; GAO-20-385 at 8 ("USPS's current business model is not financially sustainable due to declining mail volumes, increased compensation and benefits costs, and increased unfunded liabilities and debt. USPS's costs continue to rise faster than its revenues, and although USPS has made changes over the years to address these challenges, its efforts have been limited by stakeholder opposition and statutory requirements.").

⁴²⁹ FY 2019 Financial Analysis at 4-5. At the end of FY 2019, the Postal Service's cash and cash equivalents total, excluding \$0.3 billion in restricted cash, was \$1.3 billion lower than at the end of FY 2018. *Id.* at 5. "In September 2018, the Postal Service paid down its debt by \$1.8 billion, the first reduction in its annual debt since 2005." *Id.* at 5 n.8. Therefore, combined with the additional \$2.2 billion paid in FY 2019, the resulting available borrowing authority is \$4 billion. *Id.*

resulted in dated, worn out, and malfunctioning facilities, vehicles, and equipment that may negatively impact efficiency and cost-reduction efforts.⁴³⁰ The Commission analyzed the impact of the lack of capital investment in prior reports.⁴³¹ Additionally, the

⁴³⁰ See, e.g., Order No. 4257 at 216 (“Some of this decline [in processing productivities] may, however, be due to aging machines and a lack of capital investment during the PAEA era.”) (citing Docket No. ACR2013, Responses of the United States Postal Service to Questions 1-11 of Chairman’s Information Request No. 2, January 23, 2014, question 1)); 2017 Kwoka Decl. at 19 (“While this [deferral of scheduled investments, such as its truck fleet] may have conserved on current expenditures, this deferred investment strategy has likely increased both current maintenance costs as well as future costs of replacing the vehicles.”); *id.* at 21 (noting that deferred vehicle replacement, workforce reductions, and capital expenditure cutbacks may lead to a decline in service quality); United States Postal Service, Office of the Inspector General, Report No. 19-002-R20, Delivery Vehicle Acquisition Strategy, August 12, 2020, at 1, 5, available at: <https://www.uspsoig.gov/sites/default/files/document-library-files/2020/19-002-R20.pdf> (OIG Rep. No. 19-002-R20) (observing that the expected service life of the right-hand-drive Long Life Vehicle (LLV) is 24 years, and 69 percent of the current fleet is between 25 and 32 years old, leading to higher maintenance costs and eventual retirement as they become too costly to maintain or repair); see also 2006 Joskow, *supra* at 29 (“Deferred maintenance (e.g. tree trimming) and deferred capital expenditures may lead to the deterioration of service quality in either the short run or the long run or both.”).

⁴³¹ See, e.g., FY 2019 Financial Analysis at 5 (“Financial sustainability continues to erode due to large personnel-related liabilities and the slow replacement of fully depreciated capital assets.”); *id.* at 30 (“Aging capital assets and the continued restriction in capital investment resulted in a decline in net property, plant, and equipment of \$0.3 billion...[and] resulted from FY 2009 in a net decrease in fixed assets of \$8.3 billion.”); *id.* at 33 (“This [FY 2019 debt] ratio is indicative of the Postal Service’s inability to possess sufficient resources that would allow it the ability to invest in capital and pay down its obligations.”). These findings were relatively consistent with prior findings. See, e.g., Docket No. ACR2018, Financial Analysis of United States Postal Service Financial Results and 10-K Statement, April 19, 2019, at 3 (FY 2018 Financial Analysis) (“Financial sustainability continues to erode due to large personnel related liabilities and the slow replacement of fully depreciated capital assets.”); *id.* at 27-28 (“Aging capital assets and the continued restrictions on capital investment resulted in depreciation costs in excess of investments, which resulted in a net decrease in fixed assets of \$0.3 billion.”); *id.* at 73 (“After taking depreciation into account, FY 2018 net property, plant, and equipment values decreased 36.7 percent from the base year. This is primarily due to reduced capital investments and because fully-depreciated assets have not been replaced or are being replaced at a slower rate than the estimated life of the predecessor asset.”); Docket No. ACR2017, Financial Analysis of United States Postal Service Financial Results and 10-K Statement, April 5, 2018, at 6 (FY 2017 Financial Analysis) (“Financial sustainability continues to erode due to large personnel related liabilities and the slow replacement of fully depreciated capital assets.”); *id.* at 29 (“Because of its existing outstanding debt, the Postal Service must finance all current activity with internally generated cash. This limits its ability to invest in much needed equipment and other productive assets.”); *id.* at 30 (“Aging capital assets and the continued restrictions on capital investment resulted in depreciation costs in excess of investments, which resulted in a net decrease in fixed assets of \$0.4 billion.”); *id.* at 72 (The negative fixed asset to net worth ratio “signifies an inability to rapidly respond to financial emergencies or easily obtain cash for further investment and growth.”); *id.* at 75 (“After taking depreciation into account, FY 2017 net property, plant, and equipment

Postal Service explains that it “will need to increase [its] capital expenditures in order to address [its] aging facilities and delivery fleet and to upgrade [its] equipment to remain competitive in the marketplace and to ensure that [it] will be able to continue to meet [its] statutory obligation to provide prompt, efficient and reliable postal services to the nation.” Postal Service FY 2019 Form 10-K at 40. In order to maintain delivery services, increase efficiency, and reduce costs, the Postal Service identifies its funding needs: to repair and maintain aging facilities; to upgrade aging processing equipment and deploy new equipment; to replace and maintain the aging delivery fleet; and to upgrade and enhance information technology and Postal Support Equipment.⁴³² The modifications to the existing ratemaking system adopted in this Order are targeted at addressing underlying drivers of this challenging situation and relieve financial pressure due to costs outside of the Postal Service’s direct control.

values decreased 35.5 percent from the base year. This is primarily due to reduced capital investments and because fully-depreciated assets have not been replaced.”).

⁴³² United States Postal Service, Revised Integrated Financial Plan, Fiscal Year 2020, March 9, 2020, at 7-8; see United States Postal Service, Ready-Now → Future-Ready — The U.S. Postal Service Five-Year Strategic Plan FY2020-FY2024, at 25-26, available at <https://about.usps.com/strategic-planning/five-year-strategic-plan-2020-2024.pdf> (planning to optimize network transportation and processing and delivery and retail platforms to improve reliability, speed, and efficiency); Postal Service FY 2019 Form 10-K at 41 (“Our delivery fleet includes approximately 144,000 vehicles that are at least 20 years old and need significant maintenance to continue in service. As a result, repair and maintenance costs, including applicable labor costs, have risen significantly in recent years. We purchased approximately 4,000 new vehicles to add to our fleet during 2019, at a cost of approximately \$289 million. Additionally, we continue to invest in upgrades of letter sorting equipment that is at or near the end of its useful life, while also investing in equipment to fully capitalize on business opportunities in the growing package delivery market. To conserve cash, we have deferred facilities maintenance in instances where this could be done without adversely impacting employee and customer health or safety.”); *id.* at 64 (“The Postal Service continues to pursue strategies within its control to increase operational efficiency and improve liquidity. The Postal Service has managed capital in recent years by spending only what it believed essential to maintain its existing facilities and service levels, and to increase efficiencies. However, continued increases in capital investment are necessary to upgrade its facilities, fleet of vehicles and processing equipment in order to remain operationally viable. Aggressive management of the business operations, as well as legislative and regulatory reforms that will enable it to increase revenue and reduce costs, will all be necessary to restore the Postal Service to financial health.”).

The increase to the Postal Service's borrowing authority provided via the enactment of the CARES Act⁴³³ does not impact the Commission's analysis in a material fashion. The \$10-billion increase to the Postal Service's borrowing authority is limited to addressing short-term operating needs due to the COVID-19 emergency.⁴³⁴ The express limitations prohibit the Postal Service from using the additional borrowing authority to address its longer-term financial stability, outstanding debt, and capital expenses.⁴³⁵

With respect to ANM *et al.*'s contentions that there is no demonstrable causal link between the existing ratemaking system and the observed deficiencies (see ANM *et al.* Reply Comments at 10) nor an identifiable decline in the Postal Service's financial situation that was unanticipated when the PAEA was enacted (see ANM *et al.* Comments at 54 (quoting Order No. 5537 at 90)), the Commission refers to its prior analysis. Additionally, the Commission refers to the summary of key circumstances and underlying drivers of the deficiencies above. See Section XIII.B., *supra*. Rectifying the system's ability to adequately respond to these coincident trends occurring after the PAEA's enactment and making necessary modifications to achieve the objectives of the PAEA is a reasonable and appropriate way for the Commission to fulfill the purpose of 39 U.S.C. § 3622(d)(3). The final rules directly aim to modify the ratemaking system's design to encourage and enable the Postal Service to address its complex challenges by making prudent pricing and operational decisions. Final subpart D of 39 C.F.R. part

⁴³³ Pub. L. No. 116-136 (2020).

⁴³⁴ Pub. L. No. 116-136 § 6001(b) (Additional borrowing authority is available only "if the Postal Service determines that, due to the COVID-19 emergency, the Postal Service will not be able to fund operating expenses without borrowing money[.]").

⁴³⁵ See Pub. L. No. 116-136 § 6001(b)(1)(A)-(B) (Additional borrowing authority is "to be used for such operating expenses; and [...] not [to] be used to pay any outstanding debt of the Postal Service[.]"); see also Term Sheet: Loan by U.S. Department of the Treasury to U.S. Postal Service, July 28, 2020, at 1, available at: <https://oversight.house.gov/sites/democrats.oversight.house.gov/files/2020-07-29%20UST%20Production%20summary%20of%20terms.pdf> (stating that the funds may be used for operating expenses, and not for debt service nor capital expenses).

3030 introduces a mechanism into the ratemaking system that will provide the Postal Service with both the means and incentive to respond to density declines, and thereby improve its financial health. Final subpart E of 39 C.F.R. part 3030 introduces a mechanism into the ratemaking system that will provide the Postal Service with both the means and incentive to begin to meet its statutory obligations, liquidate its unfunded retirement liabilities, and improve its financial health. Final subpart G of 39 C.F.R. part 3030 introduces a mechanism into the ratemaking system that will provide the Postal Service with both the means and incentive to improve the cost coverage of non-compensatory classes and products, and thereby improve its financial health.

The observable divergence between the changes in CPI-U and the growth in Postal Service expenses and revenue after the PAEA's enactment tends to undermine the argument that retaining the existing annual limitation of the percentage change in the CPI-U is necessary to drive the Postal Service to fully respond to its financial challenges by reducing costs and increasing efficiency.⁴³⁶ In order to realign the ratemaking system to correct for this divergence, which was exacerbated by trends that are largely outside of the Postal Service's direct control, the Commission must adjust the system to allow for additional rate authority. While price caps are designed to

⁴³⁶ See, e.g., ABA Comments at 7-8, 11; AF&PA Comments at 4-5; NPPC *et al.* Comments at 5-8.

encourage efficiency, they do not do so by holding the regulated entity's prices chronically underwater, which would run counter to Objectives 5 and 8.⁴³⁷

Some commenters express concern that the final rules would allow the Postal Service management to simply rely on rate increases to respond to its challenges and absolve them from taking other prudent steps (such as increasing efficiency and reducing costs). See ANM *et al.* Reply Comments at 10-11. It would not. See Section XIII.E.1., *supra*. The final rules appropriately balance the competing priorities encapsulated by the objectives (such as maintaining service standards, assuring financial stability, and establishing just and reasonable rates) in the near term. These modifications to the ratemaking system are intended to provide correct incentives—that the Postal Service not *solely* raise rates to respond to its challenges—and are intended to encourage prudent pricing and operational decision-making by the Postal Service that are necessary for the system to achieve the objectives of 39 U.S.C. § 3622(b) in conjunction with each other.

The evidence submitted in this docket tends to support the Commission's conclusion. On March 20, 2017, the Postal Service submitted the A&M Cost Report, prepared by an independent consultant—Alvarez & Marsal (A&M)—identifying the scope and magnitude of the cost-saving opportunities for the Postal Service from FY

⁴³⁷ To the contrary, the PAEA was intended to provide the Postal Service with the opportunity to retain earnings (rather than merely break-even as limited by the PRA) as an incentive for the Postal Service to increase its efficiency and reduce its costs. See Section XIII.E.1., *supra*. By making the opportunity to retain earnings more achievable, the modified ratemaking system would provide a more meaningful incentive for the Postal Service to increase its efficiency and reduce its costs. Moreover, the Senate recognized that the ability to retain earnings would serve the goal of maintaining financial stability. S. Rep. No. 108-318 at 8 (2004).

The Commission further observes that as a general matter, “[t]he enduring feature of ratesetting from *Smyth v. Ames* to the institution of price caps was the idea that calculating a rate base and then allowing a fair rate of return on it was a sensible way to identify a range of rates that would be just and reasonable to investors and ratepayers.” See *Verizon Commc'ns, Inc. v. FCC*, 535 U.S. 467, 487-488 (2002). Even when trying to encourage novel rate-setting models, price caps do not aim to set rates below costs. See *id.* at 489.

2017 through FY 2021. See 2017 Postal Service Comments at 2; see also 2018 Postal Service Comments at 66 (citing A&M Cost Report at 4-5). A&M's review did not identify any wholly new cost-saving opportunities that Postal Service management was not pursuing and instead categorized all identified initiatives as either recommended to continue or recommended to be accelerated, expanded, or modified. See 2018 Postal Service Comments at 66; A&M Cost Report at 4. Additionally, the independent consultant retained by the Commission—Northwest Postal Consulting—opined that existing and future opportunities to replace Postal Service labor with automation are more limited than in the past. NWPC Report 2 at 88. The Postal Service has already quantified the known annual cost savings within management's control from FY 2017 through FY 2021 as approximately \$0.8 billion. See 2018 Postal Service Comments at 66 (citing A&M Cost Report at 4-5). This evidence tends to support that cost reductions alone are unlikely to be enough. Rather, providing additional rate authority to mitigate the near-term financial pressure on the Postal Service is also necessary to lead to financial stability. By declining to implement the performance-based rate authority at this time and exploring whether and how to introduce a performance incentive mechanism in a separate rulemaking, the Commission further reinforces the Postal Service's incentive to demonstrate that it is exercising reasonable business judgment by taking advantage of the identified cost-saving opportunities.

With respect to the concern that the cause of the Postal Service's consecutive net losses are *solely* its operational and pricing decisions rather than its lack of pricing authority and that providing additional rate authority would be improper (see ANM *et al.* Reply Comments at 10-11, 14-15; see also 2018 ANM *et al.* Comments at 85), the Commission declines to engage in an overly facile exercise of suggesting that there is a single "but for" cause of the complex challenges facing the Postal Service. Doing so would oversimplify the complex issues facing the Postal Service. For instance, as detailed previously, the Postal Service was able to reduce costs and increase operational efficiency somewhat during the PAEA era, but the results were insufficient

to achieve overall financial stability, including retained earnings. Order No. 4257 at 222. The evidence suggests that additional cost reductions and operational efficiency efforts by the Postal Service are still necessary, but additional tools are required to help it achieve financial stability. In the near term, modifying the system's design to better equip Postal Service management with additional pricing tools to respond to its challenges (such as declining density, statutorily imposed retirement obligations, and non-compensatory products and classes) is necessary, proper, and consistent with the PAEA. Further, the rate-setting criteria for non-compensatory products (final 39 C.F.R. § 3030.221) aim to correct pricing practices that were inefficient, thereby increasing cost coverage. Similarly, stricter adherence to ECP (as required by final subpart J) would generally improve the Postal Service's finances by leading to more efficient pricing signals.⁴³⁸ Additionally, the reporting requirements for workshare discounts that exceed their avoided costs justified solely by 39 U.S.C. § 3622(e)(2)(C) better enable the Commission to monitor any potential negative impacts of such excessive discounts.

The enhanced reporting requirements of final § 3050.55 will provide a mechanism to better ensure that the Postal Service's operational decisions are supported by robust analysis, which also tends to encourage prudent and financially sound decision-making, consistent with the achievement of Objective 5, in conjunction with the other objectives, particularly Objectives 1, 3, and 6.⁴³⁹ Additionally, in the rulemaking regarding whether, when, and how to introduce a performance incentive mechanism (see Section VI.C., *supra*), the Commission plans to explore whether

⁴³⁸ See Order No. 4258 at 89-90. NPPC *et al.* support the Commission's proposal regarding workshare discounts as consistent with Objective 5. NPPC *et al.* Comments at 16.

⁴³⁹ See Section XIII.E.1. and 3., *supra*; Section XIII.E.6., *infra*. In addition to external oversight from the Commission, the Postal Service remains subject to external oversight from Congress, the U.S. Government Accountability Office (GAO), and the Postal Service OIG. Furthermore, the Governors also oversee Postal Service management.

additional changes to the ratemaking system would enhance the Postal Service's ability to address longer-term financial challenges.

With respect to the assertion that the Commission did not consider if the Postal Service can reenter the financial health cycle under the existing system, without providing any additional rate authority (see Discover Comments at 6), the Commission reiterates its prior finding that retaining the existing ratemaking system without any changes would be inappropriate and contrary to the goals of Objective 5 ("assure adequate revenues, including retained earnings, to maintain financial stability"). See 39 U.S.C. § 3622(b)(5). Notwithstanding the assertions by Discover that the Postal Service's financial challenges can be remediated by retaining the existing system and merely relaxing the rules regarding Market Dominant NSAs (see Discover Comments at 1), the record in this docket suggests that those financial challenges are far more pervasive. See Order No. 4257 at 170-171 (describing how the consecutive net losses resulted in an accumulated deficit); Order No. 4258 at 46-52 (describing how the consecutive net losses resulted in an accumulated deficit and that capital investments declined sharply as the accumulated deficit increased). Specific to Discover's suggestion that changes to the Market Dominant NSA rules replace the provision of any additional rate authority, the Commission finds that this alternative is purely aimed at increasing certain volumes and is wholly undeveloped in terms of what changes are requested and how those changes would represent an improvement in terms of the Postal Service's financial position, cost reductions, or efficiency, or in furtherance of any other objectives of 39 U.S.C. § 3622(b). See Section XII.C.1., *supra*. Discover may propose such rule changes in a separate petition with adequate support pursuant to existing 39 C.F.R. § 3010.201(b)(1).

The contention that additional rate authority is unnecessary due to the contribution from the Postal Service's Competitive products (see ANM *et al.* Comments at 24-25, 48-49; 2018 ANM *et al.* Comments at 6) misapprehends the command of the

PAEA. Objective 5 is a goal to be achieved via the design of the Market Dominant ratemaking system. 39 U.S.C. § 3622(a)-(b). The final rules are directly aimed at the Market Dominant ratemaking system, and the design of each new form of rate authority properly accounts for the role of Competitive products in contributing to financial stability of the Postal Service.

First, the eligibility and usage of 2 percentage points of additional rate authority for a non-compensatory class (final 39 C.F.R. § 3030.222) would be focused on the Market Dominant class at issue. The amount at issue is aimed at narrowing the cost-coverage gap for the applicable class over time. See Order No. 5337 at 168-170.

Second, the density rate authority formula is designed to properly account for the role of Competitive products. Using the volume input that experiences the lesser decline (either Market Dominant or total volume) in the formula benefits Market Dominant ratepayers. As an example, if Market Dominant volume declines proportionally faster than Competitive product volume, the formula input will use total volume rather than Market Dominant volume (see final 39 C.F.R. § 3030.162(b)(2)), which reduces the resulting density rate authority eligible for use for each Market Dominant class.⁴⁴⁰ Therefore, by design, healthy Competitive product volume would translate to a direct benefit to Market Dominant ratepayers.⁴⁴¹

Third, the retirement obligation rate authority formula properly accounts for the contribution of Competitive products. For the retirement obligation rate authority, the

⁴⁴⁰ A more detailed technical explanation is provided. See Sections IV.B.2. and IV.C.3., *supra*. Additionally, in a counter-hypothetical situation where Competitive product volume declines proportionally faster than Market Dominant volume, the formula input will use Market Dominant volume rather than total volume (see final 39 C.F.R. § 3030.162(b)(2)), which reduces the resulting density rate authority eligible for use for each Market Dominant class. Thus, potential declines in the relative health of Competitive product volumes would not translate to additional Market Dominant rate authority.

⁴⁴¹ See NPPC *et al.* Comments at 36 n.44 (“The First-Class Business Mailers appreciate that the proposed formula would allow market-dominant mail to benefit from growth in Competitive volume. This is a necessary improvement over the previous Phase II proposals, which had placed the entire burden of higher rates on market-dominant mailers.”) (internal citation omitted).

formula is designed to limit the amount of the rate authority eligible for use for each class of Market Dominant products to the amount that rates would have to increase on all products (both Market Dominant and Competitive products) to generate enough revenue to make the full amortization payments. Consequently, this formula design—by presuming that an equal rate increase will be applied to Competitive products—limits the amount of the potential rate increases applied to Market Dominant products.

Multiple commenters claim that the continued default on the statutory retirement obligations is essentially harmless and that remitting the owed payments to the U.S. Department of the Treasury would not improve the financial stability of the Postal Service.⁴⁴² Notwithstanding the claims that the Postal Service's funding of benefits for future retirees is sufficient,⁴⁴³ the PAEA imposed prefunding requirements⁴⁴⁴ that the Postal Service has not been able to meet. The identified retirement costs remain a primary driver of the Postal Service's ongoing losses and prevent the Postal Service from achieving net income, thereby undermining achievement of financial stability including retained earnings.

Multiple commenters express concern that the final rules increase the amount of rate authority to a level that the Postal Service will increase rates at a speed and

⁴⁴² See, e.g., NPPC *et al.* Comments at 46; NPPC *et al.* Reply Comments at 8; ANM *et al.* Reply Comments at 23-24.

⁴⁴³ The GAO reported that the financial outlook for the RHBF was poor—the Office of Personnel Management forecasted the fund would be depleted by 2030, if the Postal Service continued nonpayment. United States Government Accountability Office, Report to the Ranking Member, Committee on Homeland Security and Governmental Affairs, U.S. Senate, Report No. GAO-18-602, *Postal Retiree Health Benefits: Unsustainable Finances Need to be Addressed*, August 2018, at 6, available at: <https://www.gao.gov/assets/700/694188.pdf> (GAO-18-602).

⁴⁴⁴ The Postal Service's annual amortization payments for RHB and for CSRS and FERS benefits are legal obligations. See 5 U.S.C. §§ 8909a(d)(3)(B) (retirement and health benefits funding), 8348(h)(2)(E) (CSRS funding), and 8423(b)(4)(B) (FERS funding).

magnitude that will drive away volume and ultimately harm its finances.⁴⁴⁵ The arguments that the Postal Service would be likely to use the full amount of the additional rate authority based on its past history of using the near-maximum amount of authority provided under the existing system and excerpts of statements arguing for deregulation are not persuasive. See ANM *et al.* Comments at 38 (citing Brattle Decl. ¶ 40). As explained in Section XIII.E.2., *supra*, this disregards the relatively small amount of rate authority provided under the existing rules and the inherent incentives of the Postal Service to exercise reasonable business judgment to avoid such an outcome. These reasons support a reasonable expectation that the Postal Service would behave rationally and in its own best interests, as guided by the incentives and means provided by the modified ratemaking system.

Additionally, the Commission has accounted for concerns that the Postal Service might behave in a manner that would be rational *vis a vis* its near-term interests but potentially threaten its longer-term interests. First, providing the Postal Service with the limited ability to bank additional forms of rate authority for declining density and for non-compensatory classes for future use ensures that the modified ratemaking system would not create a perverse incentive for the Postal Service to raise rates faster than the market can bear. Consistent with the existing requirements, the Postal Service would still be limited to use no more than 2 percentage points of banked rate authority per class per year, and banked rate authority would still expire after 5 years, so as to further reinforce Objectives 2 and 8. Second, the separate rulemaking regarding whether, when, and how to introduce a performance incentive mechanism (see Section VI.C., *supra*), in which the Commission plans to explore additional changes to the ratemaking system, will allow for further consideration of issues affecting the Postal Service's incentives and ability to address longer-term financial challenges. Third, the

⁴⁴⁵ See, e.g., ABA Comments at 1-2, 10-11; AFPA Comments at 3; ANM *et al.* Comments at 38 (citing Brattle Decl. ¶ 40); ANM *et al.* Reply Comments at 2; Discover Comments at 4; eBay Comments at 3-4; NPPC *et al.* Comments at 22-23, 36-38; PSA Comments at 6.

Commission plans to review the system in 5 years, subject to Commission discretion to consider aspects of the system sooner (if needed). Moreover, the Postal Service has sufficient controls concerning the exercise of reasonable business judgment regarding its financial viability.⁴⁴⁶

Finally, the Commission considers the competing argument raised by the Postal Service, that the Commission's modified ratemaking system fails to accord sufficient weight to Objective 5 because the final rules do not provide sufficient rate authority to cover the Postal Service's net losses and do not reset rates to levels that are fully compensatory. See Postal Service Comments at 6, 11, 15. To clarify the Commission's position, the Commission has never asserted that the Market Dominant ratemaking system must immediately recover all of the historic net losses or reset all rates to a level sufficient to cover all costs. This would fail to balance the competing priorities of rate stability and predictability, as provided by Objective 2, and maximizing incentives to reduce costs and increase efficiency, as provided by Objective 1. The persistent accumulation of net losses demonstrate that the existing ratemaking system did not work as intended. Bridging the gap between revenue and expenses must be achieved through a combination of prudent pricing and operational decisions over time. To do otherwise would fail to achieve Objectives 1 and 2. The final rules redesign the system in a way necessary to achieve this outcome through the provision of additional rate authority in an amount and form that would mitigate the imminent financial pressure on the Postal Service, correct certain harmful pricing practices, and retain sufficient incentives to pursue cost reductions and efficiency gains.

The Commission aims to ensure that the ratemaking system does not incentivize the Postal Service to *solely* raise rates to respond to its challenges. Declining to

⁴⁴⁶ While the Postal Service lacks shareholders, it does not lack outside oversight to hold the Postal Service accountable for its financial and operational performance. Such oversight comes not only from the Commission, but also from Congress, the GAO, and the Postal Service OIG. Furthermore, the Governors also oversee Postal Service management.

provide rate authority that would fully cover the historic net losses (such as allowing the density factor to compensate for declines occurring before the implementation of the final rules) and declining to implement the performance-based rate authority at this time further ensure that that this outcome is avoided. The final rules are intended to encourage prudent pricing and operational decision-making by the Postal Service. This properly balances all of the objectives of the PAEA, which strive to achieve systemic benefits for both the Postal Service and its ratepayers. Given that the near-term financial instability is a source of imminent peril, it is within the Commission's considerable discretion and up to its reasonable, expert policy judgment to address those more time-sensitive issues first and then evaluate how the longer-term financial stability issues should be addressed, in conjunction with the other objectives, under the modified ratemaking system.

6. Objective 6

The finalized changes are designed to continue to allow the system to “reduce the administrative burden and increase the transparency of the ratemaking process,” as provided by Objective 6. 39 U.S.C. § 3622(b)(6). The Commission found that the existing system “has reduced the administrative burden and increased the transparency of the ratemaking system.” Order No. 4257 at 274.

AF&PA and NPPC *et al.* raise concerns that multiple overlapping layers of rate authority would render it difficult for ratepayers to comprehend and that the formula-based approach to calculating rate authority would be inconsistent with Objective 6. AF&PA Comments at 4; NPPC *et al.* Comments at 20. However, the existing ratemaking system already uses a formula to compute the maximum rate authority per annum. The maximum rate authority provided by the existing ratemaking system's formula (the percentage change in the CPI-U plus a limited amount of banked rate authority) is inadequate to allow the system to achieve the objectives of the PAEA. Adjusting that formula to address underlying drivers of the existing system's deficiencies

such as declining density would not make the system less transparent because the Commission has provided a thorough, publicly available explanation and the formula uses inputs from publicly available data and information. The Commission will announce the maximum amount of rate authority per annum on a regular basis (see final 39 C.F.R. § 3030.160(c)) and commits to maintaining the underlying calculations on its public website, similar to existing practice.⁴⁴⁷ Any additional administrative burden associated with the calculation is minimal and justified by the need to address underlying drivers of the existing system's deficiencies.

The enhanced cost-reduction reporting requirements are consistent with Objective 6. See final 39 C.F.R. § 3050.55; see *also* ABA Comments at 16. Final § 3050.55 would improve the availability and comprehensibility of information on a regular basis, thereby increasing transparency. Increased transparency relating to cost reductions would mitigate the existing information asymmetry that tends to advantage the Postal Service and disadvantage ratepayers.⁴⁴⁸ Any resulting increase in administrative burden to the Postal Service associated with having to compile reports containing data and information that are already generated and available to the Postal Service internally would be outweighed by the benefits of the increased transparency. See Section IX.C.5., *supra*. This balancing is consistent with the achievement of Objective 6, applied in conjunction with the other objectives, particularly Objectives 1, 3, and 5. See Section XIII.E.1., 3., and 5., *supra*.

⁴⁴⁷ On a monthly basis, the available price cap authority for each class is calculated and published on the Commission's website, available at: <http://www.prc.gov>; hover over "References" and follow the "CPI Figures" hyperlink.

⁴⁴⁸ See Order No. 5337 at 224-226 (describing opportunities to improve transparency and reduce information asymmetries relating to cost-reduction initiatives or explanations for significant changes in costs); see *also* 2008 Joskow at 550-551 (observing that regulators have imperfect information relating to the operator's cost, quality, and demand attributes and that such information asymmetries favor the operator and may disadvantage customers); 2006 Joskow, *supra*, at 3 (same).

Additionally, the Commission finalizes procedural changes that are aimed at improving the transparency and accountability of the ratemaking process by enhancing the schedule for regular and predictable rate adjustments and extending the time period for advance notice, public comment, and Commission review of rate proceedings. See final 39 C.F.R. §§ 3030.102 and 3030.121; see *also* Pitney Bowes Comments at 8. These improvements would make it easier for the public to comprehend and participate in rate adjustment proceedings. Further, the procedural improvements that clarify Commission responses to incomplete rate adjustment filings would help facilitate the administration of the ratemaking process, consistent with Objective 6. See final 39 C.F.R. § 3030.126; see *also* Pitney Bowes Comments at 8.

Finally, because the existing system does not include the 1 percentage point of performance-based rate authority, withdrawing these proposed rules at this time does not implicate Objective 6. A separate rulemaking to refine related issues will be undertaken through notice-and-comment procedures, which balances the need for transparent examination with minimizing the administrative burden imposed on participants, thereby further showing consideration for the continued achievement of Objective 6. This rulemaking will explore whether any additional adjustments to the price cap aimed at further incentivizing increasing efficiency, reducing costs, and maintaining service standards can be operationalized in a manner that would be sufficiently transparent and impose minimal administrative burden.

7. Objective 7

The finalized changes are designed to continue to allow the system to “enhance mail security and deter terrorism,” as provided by Objective 7. 39 U.S.C. § 3622(b)(7). The Commission determined that the existing ratemaking system “provided sufficient funds to maintain safeguards to protect the mail system and deter terrorism and provided a mechanism permitting additional funds for unforeseen security or terrorism emergencies.” Order No. 4257 at 274-275. Nothing on the record would suggest the

finalized changes would undermine the system's existing safeguards (such as the ability to seek a rate adjustment due to extraordinary or exceptional circumstances under 39 U.S.C. § 3622(d)(1)(E)) to address unexpected mail security or terrorist threats. The finalized changes would not have any negative effects on the achievement of Objective 7. Additionally, the finalized changes are aimed at increasing revenue, which is generally consistent with the achievement of Objective 7.⁴⁴⁹

8. Objective 8

The finalized changes are designed to address the systemic issues underlying the existing system's failure to "establish and maintain a just and reasonable schedule for rates and classifications," as provided by Objective 8. 39 U.S.C. § 3622(b)(8). The Commission concluded that rates under the existing ratemaking system fell below the range of what would be "just and reasonable" as required by Objective 8—finding that rates were not excessive to the mailers but threatened the financial integrity of the Postal Service.⁴⁵⁰

Multiple commenters contend that the final rules would conflict with Objective 8: several ratepayers express concern that the magnitude of the additional rate authority would lead to rates that would be excessive to mailers,⁴⁵¹ whereas the Postal Service argues that the rate authority is insufficient to reset rates to levels that are fully

⁴⁴⁹ See Order No. 4257 at 248-249 (evaluating whether the Postal Service had the ability to pay for mail security and terrorism deterrence efforts).

⁴⁵⁰ See Order No. 4257 at 274-275. Order No. 4257 disaggregated the discussion of Objective 8 into two prongs. See nn.369 and 371, *supra*. It is well established that "just and reasonable" refers to zone, rather than a fixed price, that achieves both prongs. See Order No. 4257 at 114-115, 117, 228-229; see also *Farmers Union Cent. Exch., Inc. v. FERC*, 734 F.2d 1486, 1502 (D.C. Cir. 1984) ("an agency may issue, and courts are without authority to invalidate, rate orders that fall within a 'zone of reasonableness,' where rates are neither 'less than compensatory' nor 'excessive'").

⁴⁵¹ See, e.g., ABA Comments at 6; ANM *et al.* Comments at 4-5, 18; C21 Reply Comments at 5; NMA Comments at 9; NPPC *et al.* Comments at 20.

compensatory. See Postal Service Comments at 6, 11, 15. In designing a system that would allow for rates to be adjusted so as to fall within the range of “just and reasonable,” the Commission must balance these differing views.

The Commission determines that any concerns that the provision of the additional forms of rate authority would unjustly enrich the Postal Service at the expense of the ratepayers are largely overstated. The significance of the financial pressures faced by the Postal Service is well documented.⁴⁵² The design of the modified ratemaking system would raise the annual limitation and thereby improve the ability of the Postal Service to set rates that would not threaten its financial integrity. At the same time, the modifications are designed to limit the accrual and use of rate authority to correct particular systemic deficiencies that threaten the financial integrity of the Postal Service. Therefore, narrowly tailoring the modifications to these identified deficiencies, rather than resetting rates as the Postal Service suggests, also protects mailers from excessive rates.⁴⁵³ The final rules, which modify the implementation of the existing price cap, account for the achievement of Objective 8 as described below.

The Commission’s overall design of the modified ratemaking system gives consideration to the achievement of Objective 8 by targeting a range of prices that

⁴⁵² See Order No. 4257 at 170-171 (describing how the consecutive net losses resulted in an accumulated deficit); Order No. 4258 at 46-52 (describing how the consecutive net losses resulted in an accumulated deficit and that capital investments declined sharply as the accumulated deficit increased); GAO-13-112 at 2; GAO-17-404T at 6; FY 2019 Financial Analysis at 5, 27-29; FY 2018 Financial Analysis at 3, 27-29, 69, 73-74; FY 2017 Financial Analysis at 6, 29-30, 72, 75-76.

⁴⁵³ See *Verizon Commc'ns, Inc.*, 535 U.S. at 481 (“The traditional regulatory notion of the ‘just and reasonable’ rate was aimed at navigating the straits between gouging utility customers and confiscating utility property.”) (quoting *Fed. Power Comm'n v. Hope Nat. Gas Co.*, 320 U.S. 591, 603 (1944)); *Jersey Cent. Power & Light Co. v. FERC*, 810 F.2d 1168, 1177 (D.C. Cir. 1987) (“[T]here is a zone of reasonableness within which rates may properly fall. It is bounded at one end by the investor interest against confiscation and at the other by the consumer interest against exorbitant rates.”) (quoting *Wash. Gas Light Co. v. Baker*, 188 F.2d 11 (D.C. Cir. 1950), *cert. denied*, 340 U.S. 952 (1951)); *Farmers Union Cent. Exch., Inc.*, 734 F.2d at 1502 (“[W]hen the inquiry is whether a given rate is just and reasonable to the consumer, the underlying concern is whether it is *low* enough so that exploitation [of the consumer] by the [regulated entity] is prevented.” (quoting *City of Chicago, Ill. v. Fed. Power Comm'n*, 458 F.2d 731, 750-751 (D.C. Cir. 1971) (emphasis in original))).

would be just and reasonable to the Postal Service and its mailers. Consistent with Objective 8, which “shall not be construed to prohibit the Postal Service from making changes of unequal magnitude within, between, or among classes of mail” (39 U.S.C. § 3622(b)(8)), and Objective 4, which “allow[s] the Postal Service pricing flexibility” (39 U.S.C. § 3622(b)(4)), the additional forms of rate authority made available by this Order apply at the class level. See Section XIII.E.2., *supra*.

By way of example, for a compensatory class, the final rules would provide rate authority based on the percentage change in the CPI-U, declining density formula, and the retirement obligation formula. These final rules would allow the Postal Service to raise rates based on factors that are largely outside of the Postal Service’s direct control: the change in inflation, the increase in per-unit cost resulting from the decline in mail density for each fiscal year, and the statutorily mandated amortization payments for particular retirement costs. The Postal Service would have the ability to bank unused rate authority based on the percentage change in the CPI-U and the declining density formula to mitigate against increases that would be excessive to mailers.

The Commission’s method of adjusting the price cap for declining density balances the need to allow for the Postal Service to adjust rates in a manner that would neither threaten its financial integrity nor would be excessive to mailers. The density rate authority is aimed at improving the Postal Service’s financial integrity by adjusting the price cap for the per-unit cost increases caused by the decline in density. At the same time, the Commission has also given consideration to designing the formula to safeguard against excessive rate increases. Three aspects of the formula’s design demonstrate consideration for ensuring that rates could not rise above the range that would be just and reasonable. First, as the Postal Service observes, the density rate authority (even in combination with all of the other forms of rate authority) would not constitute a rate reset or a true-up. Rather, the density rate authority adjusts for declines calculated *after* the effective date of final subpart D of 39 C.F.R. part 3030 and

based upon the observed density decline experienced in the most recently ended fiscal year and does not adjust for prior declines. Second, the formula is designed based on a conservative estimate of how much average cost per piece is *expected* to unavoidably increase in the near term as a result of the decline in density as remaining costs are distributed over fewer pieces. It does not compensate the Postal Service for the *actual* increased costs of servicing its network. Therefore, the formula's design limits the magnitude of the potential rate increase in a manner that encourages the Postal Service to continue to reduce costs to improve its financial integrity. Third, the formula has a safeguard mechanism that prevents excessive Market Dominant rates resulting from a disproportionately greater decline in Market Dominant volumes compared to Competitive product volumes. In a hypothetical situation where Market Dominant volume declines proportionally faster than Competitive product volume, the formula input will use *total* volume rather than Market Dominant volume (see final 39 C.F.R. § 3030.162(b)(2)), which reduces the resulting density rate authority eligible for use for each Market Dominant class.

The Commission's design of the retirement obligation rate authority formula also gives consideration to targeting a range of prices that would be just and reasonable to the Postal Service and its mailers. First, the formula to compute the retirement obligation rate authority is designed to limit the amount of the rate authority eligible for use for each class of Market Dominant products to the percentage by which average revenue per piece for all products (both Market Dominant and Competitive products) would need to increase to generate enough revenue to make the full amortization payments. See Section V.C.2., *supra*. By including the volume of Competitive products in the calculation of the amount of retirement obligation rate authority made available to each class of mail, this formula design safeguards against the Postal Service's setting rates at a level that would be excessive to Market Dominant ratepayers.

Second, all revenue collected as a result of the retirement obligation rate authority must be remitted towards the corresponding statutory liabilities, as provided under final subpart E of 39 C.F.R. part 3030. The remittance requirement is necessary because Market Dominant ratepayers asked to pay higher rates for the purposes of making payments towards the Postal Service's retirement liabilities have a reasonable expectation that the funds will be used for that purpose. Moreover, the identified retirement costs remain a primary driver of the Postal Service's ongoing losses that are outside of its control and prevent the Postal Service from achieving net income, thereby undermining its financial integrity.

Additionally, the final rules would require the Postal Service to increase the rate for any non-compensatory product in a compensatory class by a minimum of 2 percentage points above the percentage increase for the class. This modification is just and reasonable to both the mailers and the Postal Service. No additional rate authority is provided for this specific purpose; instead, the Postal Service must rebalance rate increases within a compensatory class to apply a larger increase to the non-compensatory products, thereby reducing the existing cross-subsidy over time. Several of the products at issue have been non-compensatory for many years, which is inconsistent with rates that are within the range of just and reasonable, impedes pricing efficiency, and threatens the Postal Service's financial integrity, thereby undermining the ratemaking system's achievement of Objectives 1, 5, and 8. The most egregious example, USPS Marketing Mail Flats, has not covered its attributable costs since the enactment of the PAEA and has sustained \$6.7 billion in cumulative contribution losses from FY 2007 to FY 2019.⁴⁵⁴

⁴⁵⁴ Order No. 4257 at 234; Order No. 4258 at 75; Order No. 5337 at 153; FY 2019 ACD at 34. Flats did not exist as a product in FY 2007; therefore, the losses for Flats were incurred from FY 2008 through FY 2019.

As the cost-coverage for Flats worsened over time, the Commission has incrementally escalated its regulatory approach from more flexible-style recommendations and directives to more prescriptive rate-setting criteria that would require the rates for Flats to increase at least 2 percentage points above the percentage increase for the USPS Marketing Mail class in the next general Market Dominant rate adjustment. See nn.346 and 347, *supra*. Subsequently, the Commission applied this requirement to USPS Marketing Mail Parcels as well. See n.347, *supra*. The finalized rate-setting criteria for non-compensatory products expand the existing incremental approach for improving the cost coverage of Flats and Parcels to each non-compensatory product in a compensatory class. This incremental 2–percentage-point increase would narrow the cost-coverage gap over time. See Order No. 5337 at 159-160. The rate-setting criteria are designed to operate only as long as necessary to achieve cost coverage; if cost coverage for a particular product does rise to provide a positive contribution, the Postal Service would no longer be required to apply the additional 2-percentage-point increase. See final 39 C.F.R. § 3030.221. Therefore, the rate-setting criteria strike a reasonable balance of providing predictability and stability to ratepayers, improving allocative efficiency, promoting the Postal Service to focus on increasing operational efficiency and cost reductions, improving financial integrity, and moving rates into the range of prices that is just and reasonable, as encapsulated by Objectives 1, 2, 5, and 8.⁴⁵⁵

For each non-compensatory class of mail, the Commission’s design of the modified ratemaking system provides an additional 2 percentage points of rate authority. This modification to the ratemaking system is needed to provide the Postal

⁴⁵⁵ The Commission further observes that certain mailpieces are accorded statutory pricing preferences, which remain unaffected by the final rules. See 39 U.S.C. § 3626(a)(6)(A) (requiring nonprofit rates to yield per-piece revenues that equal, as nearly as practicable, 60 percent of commercial per-piece revenues); 39 U.S.C. § 3626(a)(7) (requiring prices for Library Mail to be set as nearly as practicable to 95 percent of Media Mail prices). The Commission will continue to review planned price adjustments for compliance with these requirements.

Service with the tools to address the unique challenge faced by the Periodicals class of mail: both products in the class are non-compensatory, and therefore rebalancing rates within the class would be insufficient to improve cost coverage. See Order No. 5337 at 163-164.

Periodical mailers have argued that the rate authority provided by the final rules would lead to excessive rate increases. See NNA Comments at 10, 14-15. First, it is important to observe that this modification is necessary to allow the Postal Service to raise these historically non-compensatory rates to incrementally approach the range of rates that would be just and reasonable to both the Postal Service and the mailers. The Periodicals class has not covered its attributable costs since the enactment of the PAEA.⁴⁵⁶ From FY 2007 to FY 2019, Periodicals sustained \$7.4 billion in cumulative contribution losses. FY 2019 ACD at 25. The percentage change in the CPI-U has been unable to provide sufficient rate authority to allow the Postal Service to set compensatory rates for Periodicals.⁴⁵⁷ Therefore, a systemic modification is needed to remediate this threat to the Postal Service's financial integrity.

Second, the final rules produce a reasonable balancing of the PAEA's objectives as applied to Periodicals. The Commission explored the possibility of providing additional rate authority in the amounts of 1, 2, or 3 percentage points per annum. See Order No. 5337 at 168-170. The additional 2 percentage points is aimed only at narrowing the cost-coverage gap over time. See *id.* It is important to observe that the Commission has already incorporated an automatic safeguard for mailers into the

⁴⁵⁶ See Order No. 4257 at 233-234; Order No. 4258 at 81; Order No. 5337 at 164; see also FY 2019 ACD at 25.

⁴⁵⁷ Generally, the Postal Service has nearly exhausted all of the rate authority provided by the percentage change in the CPI-U for Periodicals. See Library Reference PRC-LR-RM2017-3/1, Excel file "PRC-LR-RM2017-3-1.xlsx," tab "Table II-3," rows 4 and 7. Even over a longer period of time, from January 2005 to now, the trend holds. The CPI-U data are published on the Commission's website, available at: <http://www.prc.gov>; hover over "References" and follow the "CPI Figures" hyperlink.

design of the final rules. If cost coverage for Periodicals does rise to provide a positive contribution, the Postal Service would no longer be eligible to apply the additional 2-percentage-point increase. See final 39 C.F.R. § 3030.222. Moreover, incrementally applying no more than an additional 2 percentage points annually, rather than allowing a one-time rate reset, further ameliorates against a magnitude and speed of rate increases that would be excessive to ratepayers.⁴⁵⁸ The additional rate authority provided for each non-compensatory class strikes a reasonable balance of providing predictability and stability to ratepayers, improving allocative efficiency, promoting the Postal Service to focus on increasing operational efficiency and cost reductions, improving financial integrity, and moving rates into the range of prices that is just and reasonable, as encapsulated by Objectives 1, 2, 5, and 8.

Third, the Periodicals class is accorded several statutory pricing preferences, which remain unaffected by the final rules. See 39 U.S.C. § 3626. The Commission will continue to review planned price adjustments for compliance with these requirements.

There are also sufficient safeguards in place to ensure that modifications in the final rule based on the Commission's expert economic judgment would not produce rates that are excessive to mailers. As explained in Section XIII.E.2., *supra*, the Postal Service has inherent incentives to exercise reasonable business judgment to avoid such an outcome. The Postal Service would have the ability to bank unused rate authority based on the percentage change in the CPI-U, the declining density formula, and non-compensatory classes to mitigate against increases that would be excessive to the mailers. Consistent with the existing requirements, the Postal Service would still be limited to use no more than 2 percentage points of banked rate authority per class per year and banked rate authority would still expire after 5 years, so as to further reinforce

⁴⁵⁸ Notably, the Public Representative in advocating for a one-time reset of the price cap for Periodicals characterizes the Commission's approach as "accord[ing] too much weight to stability and reasonableness and far too little weight to producing adequate revenue." PR Comments at 50.

Objectives 2 and 8. Moreover, committing to review the system in 5 years, subject to Commission discretion to consider aspects of the system sooner (if needed), balances the competing priorities of setting a review period that would be both short enough to safeguard against any potential unintended consequences (by contrast the 10-year review period set by the PAEA was, in hindsight, too long⁴⁵⁹) and long enough to allow the effects of the changes to be observed. Additionally, declining to implement the provision of 1 percentage point of performance-based rate authority further limits the magnitude of potential rate increases at this time. The Commission's determination to engage in further study on this topic remains in line with the goal of Objective 8, producing rates that are just and reasonable to both the ratepayers and the Postal Service. While a separate rulemaking is aimed at the Postal Service's longer-term financial integrity, any potential outcome would be evaluated *vis a vis* all of the PAEA's objectives, in conjunction with each other. The Commission further observes that although rates set in compliance with the final rules would presumptively be below a level that would constitute excessive rates, a complaint may be filed by "[a]ny interested person (including a duly appointed officer of the Commission representing the interests of the general public)."⁴⁶⁰

9. Objective 9

The finalized changes are designed to continue to allow the system to "allocate the total institutional costs of the Postal Service appropriately between market-dominant

⁴⁵⁹ See n.389, *supra*.

⁴⁶⁰ 39 C.F.R. § 3022.2. Price cap systems used by other U.S. regulators incorporate complaint procedures as a systemic safeguard against individual rates rising to a level that would be excessive to the consumer. See *Env'tl. Action v. FERC*, 996 F.2d 401, 409 (D.C. Cir. 1993) (rejecting argument that the price cap system was not just and reasonable, noting the presence of a complaint mechanism to hear challenges against individual rates); *Nat'l Rural Telecom Ass'n v. FCC*, 988 F.2d 174, 178 (D.C. Cir. 1993) (same). Further, the annual compliance review is a regular process by which the Commission may intervene if the Postal Service's pricing decisions would contravene relevant statutory policies such as 39 U.S.C. §§ 101(a), 101(d), and 403(e). See 39 U.S.C. § 3653.

and competitive products,” as provided by Objective 9. 39 U.S.C. § 3622(b)(9). The Commission determined that the existing ratemaking system has an adequate mechanism to ensure the appropriate allocation of total institutional costs. Order No. 4257 at 275. Nothing on the record would suggest the finalized changes would undermine the system’s existing mechanism and the finalized changes do not have any negative effect on the achievement of Objective 9. The withdrawal of the performance-based rate authority is also not expected to impact the continued achievement of Objective 9.

F. Factors

Issues raised relating to the factors of 39 U.S.C. § 3622(c) are addressed herein.

The fourteen factors are:

- (1) the value of the mail service actually provided each class or type of mail service to both the sender and the recipient, including but not limited to the collection, mode of transportation, and priority of delivery;
- (2) the requirement that each class of mail or type of mail service bear the direct and indirect postal costs attributable to each class or type of mail service through reliably identified causal relationships plus that portion of all other costs of the Postal Service reasonably assignable to such class or type;
- (3) the effect of rate increases upon the general public, business mail users, and enterprises in the private sector of the economy engaged in the delivery of mail matter other than letters;
- (4) the available alternative means of sending and receiving letters and other mail matter at reasonable costs;
- (5) the degree of preparation of mail for delivery into the postal system performed by the mailer and its effect upon reducing costs to the Postal Service;
- (6) simplicity of structure for the entire schedule and simple, identifiable relationships between the rates or fees charged the various classes of mail for postal services;
- (7) the importance of pricing flexibility to encourage increased mail volume and operational efficiency;
- (8) the relative value to the people of the kinds of mail matter entered into the postal system and the desirability and justification for special classifications and services of mail;
- (9) the importance of providing classifications with extremely high degrees of reliability and speed of delivery and of providing those that do not require high degrees of reliability and speed of delivery;

(10) the desirability of special classifications for both postal users and the Postal Service in accordance with the policies of this title, including agreements between the Postal Service and postal users, when available on public and reasonable terms to similarly situated mailers, that—

(A) either—

(i) improve the net financial position of the Postal Service through reducing Postal Service costs or increasing the overall contribution to the institutional costs of the Postal Service[,] or

(ii) enhance the performance of mail preparation, processing, transportation, or other functions[,] and

(B) do not cause unreasonable harm to the marketplace[;]

(11) the educational, cultural, scientific, and informational value to the recipient of mail matter;

(12) the need for the Postal Service to increase its efficiency and reduce its costs, including infrastructure costs, to help maintain high quality, affordable postal services;

(13) the value to the Postal Service and postal users of promoting intelligent mail and of secure, sender-identified mail; and

(14) the policies of this title as well as such other factors as the Commission determines appropriate.

39 U.S.C. § 3622(c).

NPPC *et al.* assert that the Commission failed to address any of these factors and that failure to consider the effects of the final rules on all of these factors is an error. NPPC *et al.* Comments at 10, 19-20. The factors appearing in 39 U.S.C. § 3622(c) are considerations to be taken into account when establishing or revising the system under subsection (a) and in making the determination of whether the system is achieving the objectives appearing in subsection (b). See 39 U.S.C. § 3622(a), (c), and (d)(3). These factors were explicitly considered, as required by 39 U.S.C. § 3622(d)(3) in the determination of whether the system is achieving the objectives appearing in subsection (b). Order No. 4257 at 18-21. With regard to the treatment of these factors in promulgation of these final rules, 39 U.S.C. § 3622(d)(3) grants the Commission discretion to “by regulation, make such modification or adopt such alternative system for regulating rates and classes for market-dominant products as necessary to achieve the objectives.” 39 U.S.C. § 3622(d)(3). Paragraph (d)(3) does not set forth the factors as

policy goals to be achieved. *Id.* In any event, to the extent that the issues encapsulated by these factors are relevant, the Commission has fully addressed them. See *Carlson*, 938 F.3d at 344. The Commission provides the following responses to comments that raise particular factors as either being inconsistent with a particular rule or alternative.⁴⁶¹

ABA, ANM *et al.*, and NPPC *et al.* assert that providing additional rate authority would be inconsistent with particular factors. Linking Factor 12 with Objective 1, ABA asserts that providing *any* additional rate authority to the Postal Service so that it may adjust rates above the percentage change in the CPI-U would remove the financial pressure imposed on the Postal Service by the existing CPI-U price cap to reduce costs and increase efficiency. ABA Comments at 7-8. This concern is addressed in Section XIII.1., *supra*. Linking Factor 4 with Objective 8, ABA asserts that allowing the Postal Service to raise prices because of declining volume would effectively tax ratepayers that continue to use the mail over electronic communication. ABA Comments at 6-7. The Commission has extensively explained that this rate authority corresponds to changes in the per-unit cost increases caused by the decline in *density* (the decline in volume combined with the statutorily imposed universal service obligation to deliver to every address) and specifically considers whether potential rate increases would be excessive to mailers. See Sections IV.B.2., IV.C.1., IV.C.3., and XIII.8., *supra*.

Invoking Factor 7, ANM *et al.* take issue with the Postal Service's characterizations of pricing flexibility under the existing CPI-U price cap system. ANM *et al.* Reply Comments at 12. The Commission has already evaluated pricing flexibility under the existing CPI-U price cap system and that impact of its use. See Order No. 4257 at 50-51, 86-99, 137-139, 141-142, 144-145, 150. Linking Factor 3 with Objective 2, ANM *et al.* assert that the Commission has failed to consider the impact on business

⁴⁶¹ NPPC *et al.* and Pitney Bowes assert that particular factors support implementation of the final rules regarding workshare discounts. NPPC *et al.* Comments at 16 (asserting that Factors 4, 5, 6, and 11 support the Commission's authority to regulate workshare discounts); Pitney Bowes Comments at 3 (asserting that the workshare discount rules properly take into account Factors 5 and 12).

mailers of the magnitude of the rate increases connected with the retirement obligation rate authority. ANM *et al.* Comments at 57. The Commission has given consideration to the magnitude of the potential rate increases and the effects on ratepayers. See Chapter V.; Section XIII.E.2., 5., and 8., *supra*.

NPPC *et al.* assert that providing *any* additional rate authority to the Postal Service so that it may adjust rates above the percentage change in the CPI-U “could readily impair the system’s achievement of, at least, Factors 1, 3, 4, 9, 12, and 13.” NPPC *et al.* Comments at 20. They add that Factors 1, 3, and 4 “require[] the Commission to consider how the potential rate increases – which exceed any past rate increases since enactment of the PAEA by well more than 100 percent -- could affect mailers and their volumes.” *Id.* at 21. No further explanation regarding these six factors is provided. The Commission has given consideration to the magnitude of the potential rate increases and the effects on ratepayers and volume. See Sections IV.B.2., IV.C.1., IV.C.3., V.A., V.B.2., V.C.1., V.C.2., XIII.E.2., XIII.E.5., and XIII.E.8., *supra*.

ANM *et al.*, C21, NMA, and NNA assert that the final rules regarding non-compensatory products and classes are inconsistent with particular factors. ANM *et al.* assert that providing additional rate authority for Periodicals ignores Factors 3, 8, and 11. ANM *et al.* Comments at 82. Similarly, NMA asserts that the Commission must consider the effects of potential rate increases on mailers pursuant to Factor 3 and that the potential rate increases would be harmful for news media ratepayers. NMA Comments at 9. Additionally, NNA contends that the Commission should not give undue weight to Factor 2 given the concerns of Factors 3 and 11, and that Order No. 5337 would lead to rate increases that will likely drive Periodicals out of the mail. NNA Comments at 10, 14-15. C21 compares the additional rate authority for non-compensatory classes to the postal pricing decisions of the 1970s, asserting that the Commission must consider Factors 1, 8, and 11. C21 Reply Comments at 11. The Commission has given consideration to the effect of the potential rate increases on

ratepayers and the value of the mail matter at issue. See Chapter VII.; Section XIII.E.2., 5., and 8., *supra*.

NPPC *et al.* assert that not linking the provision of performance-based rate authority with service performance results fails to take into account Factors 1, 4, and 9. NPPC *et al.* Comments at 63-64. The Commission maintains its position that introducing a rule providing for a direct financial consequence associated with service performance appears to be premature at this time. See Order No. 4258 at 72; Sections VI.C.2. and XIII.3., *supra*.

Favoring the revision of the existing rules on Market Dominant NSAs, Discover asserts that the Commission has given insufficient weight to Factor 10. Discover Comments at 12. The Commission has determined that Discover's proposed alternative is undeveloped in terms of what rule changes are requested and how those rule changes would further the objectives. See Sections XII.C.1. and XIII.E.5., *supra*.

G. Conclusion

The Commission appreciates the thoughtful input of commenters, which has promoted refinement of the Commission's analysis over the course of this proceeding. The Postal Service faces complex challenges, the speed and extent of which have been exacerbated by trends and circumstances after the enactment of the PAEA. Retaining the existing ratemaking system is unsustainable. The PAEA authorizes the Commission to modify the design of the ratemaking system to address deficiencies that frustrate the achievement of the objectives of the PAEA. The modifications to the ratemaking system adopted in this Order are designed to provide the incentive and the means for the Postal Service to address its complex challenges by making prudent pricing and operational decisions. Those changes are necessary for the system of ratemaking to achieve the objectives enumerated in section 3622(b). The PAEA charges the Board of Governors and management of the Postal Service with the

responsibility to exercise reasonable business judgment, as guided by the incentives and means provided by the modified ratemaking system, to sustain a viable and vibrant Postal Service. The Commission will continue to monitor the challenges ahead and support the Postal Service's successful implementation of these rules.

XIV. CHANGES TO THE FINAL RULES

For clarity, the changes to the final rules are summarized below.

A. Renumbering Consistent with Amended Rules of Practice

As explained previously, the Commission renumbers the final rules to conform with the changes made in Docket No. RM2019-13. See Order No. 5337 at 3 n.6. Accordingly, the final rules renumber 39 C.F.R. part 3010 to 39 C.F.R. part 3030 (Regulation of Rates for Market Dominant Products) and 39 C.F.R. part 3020 to 39 C.F.R. part 3040 (Product Lists and the Mail Classification Schedule).⁴⁶² A cross-reference appearing in final § 3030.264(b) is updated to reflect the renumbering as existing § 3010.120. The Commission also corrects a cross-reference appearing in existing § 3045.15(a) to reflect the renumbering of the final rule identifying the CPI-U data source to final § 3030.141(a).

B. Other Non-Substantive Clarifications and Corrections

Additional changes are made to the final rules to improve clarity and internal consistency and to correct typographical errors.

The Commission corrects an internal cross-reference appearing in § 3030.162(a)(1).

For clarity, final § 3030.181(b) is reworded to place the phrase “[u]ntil the conclusion of the phase-in period,” at the beginning of the text.

Final § 3030.181(c) is rephrased to clarify that it is not intended to prohibit the Postal Service from filing limited rate adjustment cases, such as a stand-alone

⁴⁶² The numbering of 39 C.F.R. parts 3050 (Periodic Reporting) and 3055 (Service Performance and Customer Satisfaction Reporting), and the sections within those parts, were not altered by Order No. 5407.

adjustment to one or two rate cells, followed by a broader adjustment to the remainder of the class later in the same fiscal year. See Section XII.C.2., *supra*.

The Public Representative suggests corrections to the paragraph numbering, internal cross-references, and typographical errors appearing in the text of the proposed rules. PR Comments at 53. The Commission agrees and adopts his suggestions in final §§ 3030.182(c), 3030.183(b), and 3030.184(c)(1).

Final §§ 3030.220 and 3030.221 are rephrased to clarify that the requirement for the Postal Service to increase rates by a minimum of 2 percentage points above the percentage increase for that class applies only for a non-compensatory product that is in a class that is compensatory overall.

Final § 3050.55(f) is rephrased to clarify that the Commission is not seeking information with regard to planned projects that do not have a Decision Analysis Report yet. See Section IX.D., *supra*.

C. Withdrawal of Performance-Based Rate Authority

As explained in Section VI.D., *supra*, the Commission withdraws the proposed rules relating to performance-based rate authority.⁴⁶³ Accordingly, all text associated with and cross-references to these provisions are deleted from the final rules. See final 39 C.F.R. §§ 3030.101 (deleting definition of performance-based rate authority, adjusting subsequent paragraph letter designations, and conforming cross-reference); 3030.127(a) (deleting cross-reference and adjusting subsequent subparagraph number

⁴⁶³ Previously, these provisions appeared as proposed subpart F of 39 C.F.R. part 3010. See Order No. 4258, Attachment A at 23-24; Order No. 5337, Attachment A at 36-38. As explained previously, the Commission renumbers the final rules to conform with the changes made in Docket No. RM2019-13. See Order No. 5337 at 3 n.6. Accordingly, the final rules renumber 39 C.F.R. part 3010 to 39 C.F.R. part 3030 (Regulation of Rates for Market Dominant Products).

designations). In order to maintain the letter designations of the other subparts, final subpart F of 39 C.F.R. part 3030 is reserved.

D. Generation of Unused Rate Authority and Banking

The Commission withdraws the proposed rules that prohibited a non-compensatory class from being able to generate unused rate authority.⁴⁶⁴ The Commission also withdraws the proposed rules that prohibited banking of density rate authority and the rate authority for non-compensatory classes.⁴⁶⁵ These changes are reflected in final §§ 3030.160, 3030.222, 3030.242, 3030.243, and 3030.244. Accordingly, unused rate authority accrued pursuant to final subpart C—Consumer Price Index Rate Authority, final subpart D—Density Rate Authority, or final § 3030.222 may be generated and banked for any class of mail, at the Postal Service’s discretion. Otherwise, the operation of remaining rules concerning the calculation of unused rate authority and application of banked rate authority is not intended to be altered. Consistent with the existing requirements, the Postal Service would still be limited to use no more than 2 percentage points of banked rate authority per class per year and banked rate authority would still expire after 5 years.

E. Interaction with the Non-Compensatory Products Rate-Setting Criteria

Two changes are made to accommodate interaction with the non-compensatory product rate-setting criteria. The first change pertains to a non-compensatory product for which the Commission has determined that the Postal Service lacks independent authority to set rates (such as rates set by treaty obligation). A sentence is added to final § 3030.221 that would exclude such a non-compensatory product from the

⁴⁶⁴ Previously, these provisions appeared as proposed 39 C.F.R. §§ 3010.242(b) and 3010.243(d). See Order No. 5337, Attachment A at 41-42.

⁴⁶⁵ Previously, these provisions appeared as proposed 39 C.F.R. §§ 3010.160(c)(4) and 3010.222(b)(4). See Order No. 5337, Attachment A at 24, 39.

requirement to raise such rates by a minimum of 2 percentage points above the percentage increase for that class.

The second change pertains to the interaction between the workshare discount and non-compensatory product rules. Final § 3030.286(c)(7) and (g) are rephrased to account for the prohibitions on reducing the rate for any product where the attributable cost exceeded the revenue imposed by final §§ 3030.127(b) and 3030.129(g). See Section VIII.D., *supra*.

F. Changes Related to Rate Incentives

On May 15, 2020, the Commission finalized changes to its rules related to rate incentives for Market Dominant products.⁴⁶⁶ These changes are reflected in final §§ 3030.101(j) (definition of rate of general applicability); 3030.123(j) (content requirements for inclusion of a rate incentive in a percentage change in rates calculation); and 3030.128(f)(2) (criteria for inclusion of a rate incentive in a percentage change in rates calculation). An appeal on these changes remains pending; however, on August 26, 2020, the Commission issued a notice of its intent to initiate a new rulemaking in the docket at issue here and reconsider Order No. 5510, and on September 11, 2020, the Commission and the Postal Service filed a joint motion for voluntary dismissal of the appeal and vacatur of these rules.⁴⁶⁷

⁴⁶⁶ Docket No. RM2020-5, Order Adopting Final Rules Regarding Rate Incentives for Market Dominant Products, May 15, 2020 (Order No. 5510).

⁴⁶⁷ See *generally* Docket No. RM2020-5, Notice of Intent to Reconsider, August 26, 2020 (Order No. 5655); *U.S. Postal Serv. v. Postal Reg. Comm'n*, No. 20-1208 (D.C. Cir. Sept. 11, 2020), ECF Document No. 1861005.

XV. REGULATORY FLEXIBILITY ACT ANALYSIS

The Regulatory Flexibility Act requires federal agencies, in promulgating rules, to consider the impact of those rules on small entities. See 5 U.S.C. §§ 601 *et seq.* If the proposed or final rules will not, if promulgated, have a significant economic impact on a substantial number of small entities, the head of the agency may certify that the initial and final regulatory flexibility analysis requirements of 5 U.S.C. §§ 603 and 604 do not apply. See 5 U.S.C. § 605(b). In the context of this rulemaking, the Commission's primary responsibility is in the regulatory oversight of the United States Postal Service. The rules that are the subject of this rulemaking have a regulatory impact on the Postal Service, but do not impose any regulatory obligation upon any other entity. Based on these findings, the Chairman of the Commission certifies that the rules that are the subject of this rulemaking will not have a significant economic impact on a substantial number of small entities. Therefore, pursuant to 5 U.S.C. § 605(b), this rulemaking is exempt from the initial and final regulatory flexibility analysis requirements of 5 U.S.C. §§ 603 and 604.

XVI. ORDERING PARAGRAPHS

It is ordered:

1. Parts 3030, 3040, 3045, 3050, and 3055 of title 39, Code of Federal Regulations, are revised as set forth below the signature of this Order, effective 30 days after publication in the *Federal Register*.
2. The Secretary shall arrange for publication of the final rules and general statement as to the basis and purpose of the final rules in the *Federal Register*.

By the Commission.

Erica A. Barker
Secretary

List of Subjects

39 CFR Part 3030

Administrative practice and procedure, Fees, Postal Service.

39 CFR Part 3040

Administrative practice and procedure, Foreign relations, Postal Service.

39 CFR Part 3045

Administrative practice and procedure, Postal Service.

39 CFR Part 3050

Administrative practice and procedure, Postal Service, Reporting and recordkeeping requirements.

39 CFR Part 3055

Administrative practice and procedure, Reporting and recordkeeping requirements.

For the reasons discussed in the preamble, the Commission amends Chapter III of title 39 of the Code of Federal Regulations as follows:

1. Revise part 3030 to read as follows:

PART 3030—REGULATION OF RATES FOR MARKET DOMINANT PRODUCTS

Subpart A—General Provisions

Sec.

3030.100 Applicability.

3030.101 Definitions.

3030.102 Schedule for regular and predictable rate adjustments.

Subpart B—Rate Adjustments

- 3030.120 General.
- 3030.121 Postal Service rate adjustment filing.
- 3030.122 Contents of a rate adjustment filing.
- 3030.123 Supporting technical documentation.
- 3030.124 Docket and notice.
- 3030.125 Opportunity for comments.
- 3030.126 Proceedings.
- 3030.127 Maximum rate adjustment authority.
- 3030.128 Calculation of percentage change in rates.
- 3030.129 Exceptions for de minimis rate increases.

Subpart C—Consumer Price Index Rate Authority

- 3030.140 Applicability.
- 3030.141 CPI-U data source.
- 3030.142 CPI-U rate authority when rate adjustment filings are 12 or more months apart.
- 3030.143 CPI-U rate authority when rate adjustment filings are less than 12 months apart.

Subpart D—Density Rate Authority

- 3030.160 Applicability.
- 3030.161 Density calculation data sources.
- 3030.162 Calculation of density rate authority.

Subpart E—Retirement Obligation Rate Authority

- 3030.180 Definitions.
- 3030.181 Applicability.
- 3030.182 Retirement obligation data sources.
- 3030.183 Calculation of retirement obligation rate authority.
- 3030.184 Required minimum remittances.
- 3030.185 Forfeiture.

Subpart F—[Reserved]

Subpart G—Non-compensatory Classes or Products

- 3030.220 Applicability.
- 3030.221 Individual product requirement.
- 3030.222 Class requirement and additional class rate authority.

Subpart H—Accumulation of Unused and Disbursement of Banked Rate Adjustment Authority

3030.240 General.

3030.241 Schedule of banked rate adjustment authority.

3030.242 Calculation of unused rate adjustment authority for rate adjustments that involve a rate increase which are filed 12 months apart or less.

3030.243 Calculation of unused rate adjustment authority for rate adjustments that involve a rate increase which are filed more than 12 months apart.

3030.244 Calculation of unused rate adjustment authority for rate adjustments that only include rate decreases.

3030.245 Application of banked rate authority.

Subpart I—Rate Adjustments Due to Extraordinary and Exceptional Circumstances

3030.260 General.

3030.261 Contents of a rate adjustment filing.

3030.262 Supplemental information.

3030.263 Docket and notice.

3030.264 Public hearing.

3030.265 Opportunity for comments.

3030.266 Deadline for Commission decision.

3030.267 Treatment of banked rate adjustment authority.

Subpart J—Workshare Discounts

3030.280 Applicability.

3030.281 Calculation of passthroughs for workshare discounts.

3030.282 Increased pricing efficiency.

3030.283 Limitations on excessive discounts.

3030.284 Limitations on discounts below avoided cost.

3030.285 Proposal to adjust a rate associated with a workshare discount.

3030.286 Application for waiver.

Authority: 39 U.S.C. 503; 3622.

Subpart A—General Provisions.**§ 3030.100 Applicability.**

(a) The rules in this part implement provisions in 39 U.S.C. chapter 36, subchapter I, establishing the modern system of ratemaking for regulating rates and

classes for market dominant products. These rules are applicable whenever the Postal Service proposes to adjust a rate of general applicability for any market dominant product, which includes the addition of a new rate, the removal of an existing rate, or a change to an existing rate. Current rates may be found in the Mail Classification Schedule appearing on the Commission's website at *www.prc.gov*.

(b) Rates may be adjusted either subject to the rules appearing in subpart B of this part, which includes a limitation on rate increases, or subject to the rules appearing in subpart I of this part, which does not include a limitation on rate increases but requires either extraordinary or exceptional circumstances. The rules applicable to the calculation of the limitations on rate increases appear in subparts C through H of this part. The rules for workshare discounts, which are applicable whenever market dominant rates are adjusted, appear in subpart J of this part.

§ 3030.101 Definitions.

(a) The definitions in paragraphs (b) through (l) of this section apply to this part.

(b) "Annual limitation" means the annual limitation on the percentage change in rates equal to the change in the Consumer Price Index for all Urban Consumers (CPI-U) unadjusted for seasonal variation over the most recently available 12-month period preceding the date the Postal Service files a request to review its notice of rate adjustment, as determined by the Commission.

(c) "Banked rate authority" means unused rate adjustment authority accumulated for future use pursuant to these rules.

(d) A “class” of mail means the First-Class Mail, USPS Marketing Mail, Periodicals, Package Services, or Special Services groupings of market dominant Postal Service products or services. Generally, the regulations in this part are applicable to individual classes of mail.

(e) “Density rate authority” means rate authority that is available to all classes to address the effects of decreases in density of mail.

(f) “Maximum rate adjustment authority” means the maximum percentage change in rates available to a class for any planned increase in rates. It is the sum of: the consumer price index rate authority, and any available density rate authority, retirement obligation rate authority, banked rate authority, and rate authority applicable to non-compensatory classes.

(g) “Rate authority applicable to non-compensatory classes” means rate authority available to classes where revenue for each product within the class was insufficient to cover that product’s attributable costs as determined by the Commission.

(h) “Rate cell” means each and every separate rate identified as a rate of general applicability.

(i) “Rate incentive” means a discount that is not a workshare discount and that is designed to increase or retain volume, improve the value of mail for mailers, or improve the operations of the Postal Service.

(j) “Rate of general applicability” means a rate applicable to all mail meeting standards established by the Mail Classification Schedule, the Domestic Mail Manual,

and the International Mail Manual. A rate is not a rate of general applicability if eligibility for the rate is dependent on factors other than the characteristics of the mail to which the rate applies, including the volume of mail sent by a mailer in a past year or years. A rate is not a rate of general applicability if it benefits a single mailer. A rate that is only available upon the written agreement of both the Postal Service and a mailer, a group of mailers, or a foreign postal operator is not a rate of general applicability.

(k) "Retirement obligation rate authority" means rate authority that is available to all classes to provide revenue for remittance towards the statutorily mandated amortization payments for unfunded liabilities.

(l) A "seasonal or temporary rate" is a rate that is in effect for a limited and defined period of time.

§ 3030.102 Schedule for regular and predictable rate adjustments.

(a) The Postal Service shall develop a Schedule for Regular and Predictable Rate Adjustments applicable to rate adjustments subject to this part. The Schedule for Regular and Predictable Rate Adjustments shall:

- (1) Schedule rate adjustments at specific regular intervals of time;
- (2) Provide estimated filing and implementation dates (month and year) for future rate adjustments for each class of mail expected over a minimum of the next 3 years; and
- (3) Provide an explanation that will allow mailers to predict with reasonable accuracy, by class, the amounts of future scheduled rate adjustments.

(b) The Postal Service shall file a current Schedule for Regular and Predictable Rate Adjustments annually with the Commission at the time of filing the Postal Service's section 3652 report. The Commission shall post the current schedule on the Commission's website at *www.prc.gov*.

(c) Whenever the Postal Service deems it appropriate to change the Schedule for Regular and Predictable Rate Adjustments, it shall file a revised schedule.

(d) The Postal Service may vary the magnitude of rate adjustments from those estimated by the Schedule for Regular and Predictable Rate Adjustments. In such case, the Postal Service shall provide an explanation for such variation with its rate adjustment filing.

Subpart B—Rate Adjustments

§ 3030.120 General

This subpart describes the process for the periodic adjustment of rates subject to the percentage limitations specified in § 3030.127 that are applicable to each class of mail.

§ 3030.121 Postal Service rate adjustment filing.

(a) In every instance in which the Postal Service determines to exercise its statutory authority to adjust rates for a class of mail, the Postal Service shall comply with the requirements specified in paragraphs (b) through (d) of this section.

(b) The Postal Service shall take into consideration how the planned rate adjustments are in accordance with the provisions of 39 U.S.C. chapter 36.

(c) The Postal Service shall provide public notice of its planned rate adjustments in a manner reasonably designed to inform the mailing community and the general public that it intends to adjust rates no later than 90 days prior to the planned implementation date of the rate adjustments.

(d) The Postal Service shall file a request to review its notice of rate adjustment with the Commission no later than 90 days prior to the planned implementation date of the rate adjustment.

§ 3030.122 Contents of a rate adjustment filing.

(a) A rate adjustment filing under § 3030.121 shall include the items specified in paragraphs (b) through (j) of this section.

(b) A representation or evidence that public notice of the planned changes has been issued or will be issued at least 90 days before the effective date(s) for the planned rate adjustments.

(c) The intended effective date(s) of the planned rate adjustments.

(d) A schedule of the planned rate adjustments, including a schedule identifying every change to the Mail Classification Schedule that will be necessary to implement the planned rate adjustments.

(e) The identity of a responsible Postal Service official who will be available to provide prompt responses to requests for clarification from the Commission.

(f) The supporting technical documentation as described in § 3030.123.

(g) A demonstration that the planned rate adjustments are consistent with 39 U.S.C. 3626, 3627, and 3629.

(h) A certification that all cost, avoided cost, volume, and revenue figures submitted with the rate adjustment filing are developed from the most recent applicable Commission accepted analytical principles.

(i) For a rate adjustment that only includes a decrease in rates, a statement of whether the Postal Service elects to generate unused rate adjustment authority.

(j) Such other information as the Postal Service believes will assist the Commission in issuing a timely determination of whether the planned rate adjustments are consistent with applicable statutory policies.

§ 3030.123 Supporting technical documentation.

(a) Supporting technical documentation shall include the items specified in paragraphs (b) through (k) of this section, as applicable to the specific rate adjustment filing. This information must be supported by workpapers in which all calculations are shown and all relevant values (*e.g.*, rates, CPI-U values, billing determinants) are identified with citations to original sources. The information must be submitted in machine-readable, electronic format. Spreadsheet cells must be linked to underlying data sources or calculations (not hard-coded), as appropriate.

(b) The maximum rate adjustment authority, by class, as summarized by § 3030.127 and calculated separately for each of subparts C through H of this part, as appropriate.

(c) A schedule showing the banked rate adjustment authority available, by class, and the available amount for each of the preceding 5 years calculated as required by subpart H of this part.

(d) The calculation of the percentage change in rates, by class, calculated as required by § 3030.128.

(e) The planned usage of rate adjustment authority, by class, and calculated separately for each of subparts C through H of this part, as appropriate.

(f) The amount of new unused rate adjustment authority, by class, if any, that will be generated by the rate adjustment calculated as required by subpart H of this part, as applicable.

(g) A schedule of the workshare discounts included with the planned rate adjustments, and a companion schedule listing the avoided costs that underlie each such discount.

(h) Whenever the Postal Service establishes a new workshare discount rate, it must include with its filing:

- (1) A statement explaining its reasons for establishing the workshare discount;
- (2) All data, economic analyses, and other information relied on to justify the workshare discount; and

(3) A certification based on comprehensive, competent analyses that the discount will not adversely affect either the rates or the service levels of users of postal services who do not take advantage of the workshare discount.

(i) Whenever the Postal Service establishes a new discount or surcharge rate it does not view as creating a workshare discount, it must include with its filing:

(1) An explanation of the basis for its view that the discount or surcharge rate is not a workshare discount; and

(2) A certification that the Postal Service applied accepted analytical principles to the discount or surcharge rate.

(j) Whenever the Postal Service includes a rate incentive with its planned rate adjustment, it must include with its filing:

(1) Whether the rate incentive is being treated under § 3030.128(f)(2) or under § 3030.128(f)(1) and (g);

(2) If the Postal Service seeks to include the rate incentive in the calculation of the percentage change in rates under § 3030.128(f)(2), whether the rate incentive is available to all mailers equally on the same terms and conditions;

(3) If the Postal Service seeks to include the rate incentive in the calculation of the percentage change in rates under § 3030.128(f)(2), sufficient information to demonstrate that the rate incentive is a rate of general applicability, which at a minimum includes: the terms and conditions of the rate incentive; the factors that determine eligibility for the rate incentive; a statement that affirms that the rate incentive will not

benefit a single mailer; and a statement that affirms that the rate incentive is not only available upon the written agreement of both the Postal Service and a mailer, or group of mailers, or a foreign postal operator.

(k) For each class or product where the attributable cost for that class or product exceeded the revenue from that class or product as determined by the Commission, a demonstration that the planned rate adjustments comply with the requirements in subpart G of this part.

§ 3030.124 Docket and notice.

(a) The Commission will establish a docket for each rate adjustment filed by the Postal Service under § 3030.121, promptly publish notice of the filing in the **Federal Register**, and post the filing on its website. The notice shall include the items specified in paragraphs (b) through (g) of this section.

(b) The general nature of the proceeding.

(c) A reference to legal authority under which the proceeding is to be conducted.

(d) A concise description of the planned changes in rates, fees, and the Mail Classification Schedule.

(e) The identification of an officer of the Commission to represent the interests of the general public in the docket.

(f) A period of 30 days from the date of the filing for public comment.

(g) Such other information as the Commission deems appropriate.

§ 3030.125 Opportunity for comments.

Public comments should focus on whether planned rate adjustments comport with applicable statutory and regulatory requirements.

§ 3030.126 Proceedings.

(a) If the Commission determines that the rate adjustment filing does not substantially comply with the requirements of §§ 3030.122 and 3030.123, the Commission may:

(1) Inform the Postal Service of the deficiencies and provide an opportunity for the Postal Service to take corrective action;

(2) Toll or otherwise modify the procedural schedule until such time the Postal Service takes corrective action;

(3) Dismiss the rate adjustment filing without prejudice; or

(4) Take other action as deemed appropriate by the Commission.

(b) Within 21 days of the conclusion of the public comment period the Commission will determine whether the planned rate adjustments are consistent with applicable law and issue an order announcing its findings. Applicable law means only the applicable requirements of this part, Commission directives and orders, and 39 U.S.C. 3626, 3627, and 3629.

(c) If the planned rate adjustments are found consistent with applicable law, they may take effect.

(d) If the planned rate adjustments are found inconsistent with applicable law, the Commission will notify and require the Postal Service to respond to any issues of noncompliance.

(e) Following the Commission's notice of noncompliance, the Postal Service may submit an amended rate adjustment filing that describes the modifications to its planned rate adjustments that will bring its rate adjustments into compliance. An amended rate adjustment filing shall be accompanied by sufficient explanatory information to show that all deficiencies identified by the Commission have been corrected.

(f) The Commission will allow a period of 10 days from the date of the amended rate adjustment filing for public comment.

(g) The Commission will review the amended rate adjustment filing together with any comments filed for compliance and issue an order announcing its findings within 21 days after the comment period ends.

(h) If the planned rate adjustments as amended are found to be consistent with applicable law, they may take effect. However, no amended rate shall take effect until 45 days after the Postal Service transmits its rate adjustment filing specifying that rate.

(i) If the planned rate adjustments in an amended rate adjustment filing are found to be inconsistent with applicable law, the Commission shall explain the basis for its determination and suggest an appropriate remedy. Noncompliant rates may not go into effect.

(j) A Commission finding that a planned rate adjustment is in compliance with the applicable requirements of this part, Commission directives and orders, and 39 U.S.C. 3626, 3627, and 3629 is decided on the merits. A Commission finding that a planned rate adjustment does not contravene other policies of 39 U.S.C. chapter 36, subchapter I is provisional and subject to subsequent review.

§ 3030.127 Maximum rate adjustment authority.

(a) The maximum rate adjustment authority available to the Postal Service for each class of market dominant mail is limited to the sum of the percentage points developed in:

- (1) Subpart C—Consumer Price Index Rate Authority;
- (2) Subpart D—Density Rate Authority;
- (3) Subpart E—Retirement Obligation Rate Authority;
- (4) Subpart G—Non-compensatory Classes or Products; and
- (5) Subpart H—Accumulation of Unused and Disbursement of Banked Rate

Adjustment Authority.

(b) For any product where the attributable cost for that product exceeded the revenue from that product as determined by the Commission, rates may not be reduced.

§ 3030.128 Calculation of percentage change in rates.

(a) For the purpose of calculating the percentage change in rates, the current rate is the rate in effect at the time of the rate adjustment filing under § 3030.121 with the following exceptions.

(1) A seasonal or temporary rate shall be identified and treated as a rate cell separate and distinct from the corresponding non-seasonal or permanent rate. When used with respect to a seasonal or temporary rate, the current rate is the most recent rate in effect for the rate cell, regardless of whether the seasonal or temporary rate is available at the time of the rate adjustment filing.

(2) When used with respect to a rate cell that corresponds to a rate incentive that was previously excluded from the calculation of the percentage change in rates, the current rate is the full undiscounted rate in effect for the rate cell at the time of the rate adjustment filing, not the discounted rate in effect for the rate cell at such time.

(b) For the purpose of calculating the percentage change in rates, the volume for each rate cell shall be obtained from the most recently available 12 months of Postal Service billing determinants with the following permissible adjustments.

(1) The Postal Service shall make reasonable adjustments to the billing determinants to account for the effects of classification changes such as the introduction, deletion, or redefinition of rate cells. The Postal Service shall identify and explain all adjustments. All information and calculations relied upon to develop the adjustments shall be provided together with an explanation of why the adjustments are appropriate.

(2) Whenever possible, adjustments shall be based on known mail characteristics or historical volume data, as opposed to forecasts of mailer behavior.

(3) For an adjustment accounting for the effects of the deletion of a rate cell when an alternate rate cell is not available, the Postal Service should adjust the billing determinants associated with the rate cell to 0. If the Postal Service does not adjust the billing determinants for the rate cell to 0, the Postal Service shall include a rationale for its treatment of the rate cell with the information required under paragraph (b)(1) of this section.

(c) For a rate adjustment that involves a rate increase, for each class of mail and product within the class, the percentage change in rates is calculated in three steps. First, the volume of each rate cell in the class is multiplied by the planned rate for the respective cell and the resulting products are summed. Second, the same set of rate cell volumes is multiplied by the corresponding current rate for each cell and the resulting products are summed. Third, the percentage change in rates is calculated by dividing the results of the first step by the results of the second step and subtracting 1 from the quotient. The result is expressed as a percentage.

(d) For rate adjustments that only involve a rate decrease, for each class of mail and product within the class, the percentage change in rates is calculated by amending the workpapers attached to the Commission's order relating to the most recent rate adjustment filing that involved a rate increase to replace the planned rates under the most recent rate adjustment filing that involves a rate increase with the corresponding

planned rates applicable to the class from the rate adjustment filing involving only a rate decrease.

(e) The formula for calculating the percentage change in rates for a class, described in paragraphs (c) and (d) of this section, is as follows:

Percentage change in rates =

$$\left(\frac{\sum_{i=1}^N (R_{i,n})(V_i)}{\sum_{i=1}^N (R_{i,c})(V_i)} \right) - 1$$

Where,

N = number of rate cells in the class

i = denotes a rate cell (i = 1, 2, ..., N)

R_{i,n} = planned rate of rate cell i

R_{i,c} = current rate of rate cell i (for rate adjustment involving a rate increase) or rate from most recent rate adjustment involving a rate increase for rate cell i (for a rate adjustment only involving a rate decrease)

V_i = volume of rate cell i

(f) Treatment of rate incentives.

(1) Rate incentives may be excluded from a percentage change in rates calculation. If the Postal Service elects to exclude a rate incentive from a percentage change in rates calculation, the rate incentive shall be treated in the same manner as a rate under a negotiated service agreement (as described in § 3030.128(g)).

(2) A rate incentive may be included in a percentage change in rates calculation if it meets the following criteria:

(i) The rate incentive is in the form of a discount or can be easily translated into a discount;

(ii) Sufficient billing determinants are available for the rate incentive to be included in the percentage change in rate calculation for the class, which may be adjusted based on known mail characteristics or historical volume data (as opposed to forecasts of mailer behavior);

(iii) The rate incentive is a rate of general applicability; and

(iv) The rate incentive is made available to all mailers equally on the same terms and conditions.

(g) Treatment of volume associated with negotiated service agreements and rate incentives that are not rates of general applicability.

(1) Mail volumes sent at rates under a negotiated service agreement or a rate incentive that is not a rate of general applicability are to be included in the calculation of the percentage change in rates under this section as though they paid the appropriate rates of general applicability. Where it is impractical to identify the rates of general applicability (e.g., because unique rate categories are created for a mailer), the volumes associated with the mail sent under the terms of the negotiated service agreement or the rate incentive that is not a rate of general applicability shall be excluded from the calculation of the percentage change in rates.

(2) The Postal Service shall identify and explain all assumptions it makes with respect to the treatment of negotiated service agreements and rate incentives that are not rates of general applicability in the calculation of the percentage change in rates and provide the rationale for its assumptions.

§ 3030.129 Exceptions for de minimis rate increases.

(a) The Postal Service may request that the Commission review a de minimis rate increase without immediately calculating the maximum rate adjustment authority or banking unused rate adjustment authority. For this exception to apply, requests to review de minimis rate adjustments must be filed separately from any other request to review a rate adjustment filing.

(b) Rate adjustments resulting in rate increases are de minimis if:

(1) For each affected class, the rate increases do not result in the percentage change in rates for the class equaling or exceeding 0.001 percent; and

(2) For each affected class, the sum of all rate increases included in de minimis rate increases since the most recent rate adjustment resulting in a rate increase, or the most recent rate adjustment due to extraordinary and exceptional circumstances, that was not a de minimis rate increase does not result in the percentage change in rates for the class equaling or exceeding 0.001 percent.

(c) If the rate adjustments are de minimis, no unused rate adjustment authority will be added to the schedule of banked rate adjustment authority maintained under subpart G of this part as a result of the de minimis rate increase.

(d) If the rate adjustments are de minimis, no rate decreases may be taken into account when determining whether rate increases comply with paragraphs (b)(1) and (2) of this section.

(e) In the next rate adjustment filing proposing to increase rates for a class that is not a de minimis rate increase:

(1) The maximum rate adjustment authority shall be calculated as if the de minimis rate increase had not been filed; and

(2) For purposes of calculating the percentage change in rates, the current rate shall be the current rate from the de minimis rate increase.

(f) The Postal Service shall file supporting workpapers with each request to review a de minimis rate increase that demonstrate that the sum of all rate increases included in de minimis rate increases since the most recent rate adjustment resulting in a rate increase that was not de minimis, or the most recent rate adjustment due to extraordinary and exceptional circumstances, does not result in a percentage change in rates for the class equaling or exceeding 0.001 percent.

(g) For any product where the attributable cost for that product exceeded the revenue from that product as determined by the Commission, rates may not be reduced.

Subpart C—Consumer Price Index Rate Authority

§ 3030.140 Applicability.

The Postal Service may adjust rates based upon changes in the Consumer Price Index for all Urban Consumers (CPI-U) identified in § 3030.141. If rate adjustment filings involving rate increases are filed 12 or more months apart, rate adjustments are subject to a full year limitation calculated pursuant to § 3030.142. If rate adjustment filings involving rate increases are filed less than 12 months apart, rate adjustments are subject to a partial year limitation calculated pursuant to § 3030.143.

§ 3030.141 CPI-U data source.

The monthly CPI-U values needed for the calculation of rate adjustment limitations under this section shall be obtained from the Bureau of Labor Statistics (BLS) Consumer Price Index—All Urban Consumers, U.S. All Items, Not Seasonally Adjusted, Base Period 1982-84 = 100. The current Series ID for the index is “CUUR0000SA0.”

§ 3030.142 CPI-U rate authority when rate adjustment filings are 12 or more months apart.

(a) If a rate adjustment filing involving a rate increase is filed 12 or more months after the most recent rate adjustment filing involving a rate increase, then the calculation of an annual limitation for the class (full year limitation) involves three steps. First, a simple average CPI-U index is calculated by summing the most recently available 12 monthly CPI-U values from the date of the rate adjustment filing and dividing the sum by 12 (Recent Average). Second, a second simple average CPI-U index is similarly calculated by summing the 12 monthly CPI-U values immediately preceding the Recent Average and dividing the sum by 12 (Base Average). Third, the full year limitation is

calculated by dividing the Recent Average by the Base Average and subtracting 1 from the quotient. The result is expressed as a percentage, rounded to three decimal places.

(b) The formula for calculating a full year limitation for a rate adjustment filing filed 12 or more months after the last rate adjustment filing is as follows: Full Year Limitation = (Recent Average/Base Average)-1.

§ 3030.143 CPI-U rate authority when rate adjustment filings are less than 12 months apart.

(a) If a rate adjustment filing involving a rate increase is filed less than 12 months after the most recent rate adjustment filing involving a rate increase, then the annual limitation for the class (partial year limitation) will recognize the rate increases that have occurred during the preceding 12 months. When the effects of those increases are removed, the remaining partial year limitation is the applicable restriction on rate increases.

(b) The applicable partial year limitation is calculated in two steps. First, a simple average CPI-U index is calculated by summing the 12 most recently available monthly CPI-U values from the date of the rate adjustment filing and dividing the sum by 12 (Recent Average). Second, the partial year limitation is then calculated by dividing the Recent Average by the Recent Average from the most recent previous rate adjustment filing (Previous Recent Average) applicable to each affected class of mail and subtracting 1 from the quotient. The result is expressed as a percentage, rounded to three decimal places.

(c) The formula for calculating the partial year limitation for a rate adjustment filing filed less than 12 months after the last rate adjustment filing is as follows: Partial Year Limitation = (Recent Average/Previous Recent Average) – 1.

Subpart D—Density Rate Authority

§ 3030.160 Applicability.

(a) This subpart allocates rate authority to address the effects of decreases in the density of mail as measured by the sources identified in § 3030.161. The calculation of the additional rate authority corresponding to the change in density is described in § 3030.162.

(b) The Postal Service shall file a notice with the Commission by December 31 of each year that calculates the amount of density rate authority that is eligible to be authorized under this subpart.

(c) The Commission shall review the Postal Service's notice and determine how much, if any, rate authority will be authorized under this subpart. Any rate authority allocated under this subpart:

(1) Shall be made available to the Postal Service as of the date of the Commission's determination;

(2) Must be included in the calculation of the maximum rate adjustment authority in the first generally applicable rate adjustment filed after the Commission's determination; and

(3) May be used to generate unused rate authority, if unused, within 12 months of the Commission's announcement.

§ 3030.161 Density calculation data sources.

(a) The data needed for the calculation of the density rate authority in § 3030.162 shall be obtained from the values reported by the Postal Service as specified in paragraphs (b) through (d) of this section. When both originally filed and annually revised data are available, the originally filed data shall be used. When the originally filed data are corrected through a refile or in the Commission's Annual Compliance Determination report, the corrected version of the originally filed data shall be used.

(b) Market dominant volume and total volume from the Revenue, Pieces, and Weight report, filed by the Postal Service under § 3050.25 of this chapter;

(c) Institutional costs and total costs from the Cost and Revenue Analysis report, filed with the Postal Service's section 3652 report; and

(d) The number of delivery points, from the input data used to produce the Total Factor Productivity estimates, filed with the Postal Service's section 3652 report.

§ 3030.162 Calculation of density rate authority.

(a) *Formulas*—(1) The formula for calculating the amount of density rate authority, in conformance with paragraph (b)(1) of this section, is as follows:

Density rate authority = the greater of 0 and

$$-1 * \frac{IC_T}{TC_T} * \% \Delta D_{[T-1,T]}$$

Where,

T = most recently completed fiscal year

T-1 = fiscal year prior to fiscal year T

IC_T = institutional cost in fiscal year T

TC_T = total cost in fiscal year T

%ΔD_[T-1,T] = Percentage change in density from fiscal year T-1 to fiscal year T

(2) The formula for calculating the percentage change in density, in conformance with paragraph (b)(2) of this section, is as follows:

Percentage change in density from prior fiscal year =

$$\frac{\frac{V_T}{DP_T}}{\frac{V_{T-1}}{DP_{T-1}}} - 1$$

Where,

T = most recently completed fiscal year

T-1 = fiscal year prior to fiscal year T

V_T = volume in fiscal year T (either market dominant volume or total volume as discussed in paragraph (b)(2) of this section)

DP_T = delivery points in fiscal year T

(b) *Calculation*—(1) The amount of density rate authority available under this section shall be calculated in three steps. First, the percentage change in density during the most recently completed fiscal year shall be calculated using the formula in paragraph (a)(2) of this section as described in paragraph (b)(2) of this section.

Second, this percentage change shall be multiplied by the institutional cost ratio, which is calculated as institutional costs for the most recently completed fiscal year divided by total costs for that fiscal year. Finally, this product shall be multiplied by negative 1 so that declines in density correspond to a positive increase in rates. If the result of this calculation is less than 0, the amount of additional rate authority shall be 0.

(2) The percentage change in density from the prior fiscal year shall be calculated as the ratio of volume to delivery points for the most recently completed fiscal year, divided by the same ratio for the prior fiscal year, and subtracting 1 from the quotient. The result is expressed as a percentage, rounded to three decimal places. To ensure that decreases in competitive product volume will not result in the Postal Service receiving greater additional rate adjustment authority under this subpart, the percentage change in density shall be calculated two ways: using market dominant volume and using total volume. The greater of the two results (not using absolute value) shall be used as the percentage change in density from the prior fiscal year.

Subpart E—Retirement Obligation Rate Authority

§ 3030.180 Definitions.

(a) The definitions in paragraphs (b) through (e) of this section apply to this subpart.

(b) “Amortization payments” mean the amounts that the Postal Service is invoiced by the U.S. Office of Personnel Management to provide for the liquidation of

the specific and supplemental unfunded liabilities by statutorily predetermined dates, as described in § 3030.182(a).

(c) “Phase-in period” means the period of time spanning the fiscal years of issuance of the first five determinations following the effective date of this subpart, as specified by the timing provisions in § 3030.181.

(d) “Required minimum remittance” means the minimum amount the Postal Service is required to remit during a particular fiscal year, as calculated under § 3030.184.

(e) “Revenue collected under this subpart” means the amount of revenue collected during a fiscal year as a result of all previous rate increases authorized under this subpart, as calculated under § 3030.184.

§ 3030.181 Applicability.

(a) This subpart allocates additional rate authority to provide the Postal Service with revenue for remittance towards the statutorily mandated amortization payments for supplemental and unfunded liabilities identified in § 3030.182. As described in § 3030.184, for retirement obligation rate authority to be made available, the Postal Service must annually remit towards these amortization payments all revenue collected under this subpart previously. The full retirement obligation rate authority, calculated as described in § 3030.183, shall be phased in over 5 fiscal years, taking into account changes in volume during the phase-in period. If combined with an equal rate increase on Competitive products, the compounded rate increase resulting from retirement

obligation rate authority is calculated to generate sufficient additional revenue at the end of the phase-in period to permit the Postal Service to remit the entire invoiced amount of its amortization payments.

(b) Until the conclusion of the phase-in period, the Postal Service shall file a notice with the Commission by December 31 of each year that calculates the amount of retirement obligation rate authority that is eligible to be authorized under this subpart.

(c) The Commission shall review the Postal Service's notice and determine how much, if any, rate authority will be authorized under this subpart. Any rate authority allocated under this subpart:

(1) Shall be made available to the Postal Service as of the date of the Commission's determination;

(2) Must be included in the calculation of the maximum rate adjustment authority in the first generally applicable rate adjustment filed after the Commission's determination;

(3) Shall lapse if not used in the first generally applicable rate adjustment filed after the Commission's determination;

(4) Shall lapse if unused, within 12 months of the Commission's determination, however this subparagraph shall not prohibit the Postal Service from making a stand-alone adjustment to one or two generally applicable rate cells, if such a case were to be followed by a broader rate adjustment in the class later in the same fiscal year; and

(5) May not be used to generate unused rate authority, nor shall it affect existing banked rate authority.

§ 3030.182 Retirement obligation data sources.

(a) The amounts of the amortization payments needed for the calculation of retirement obligation rate adjustment authority in § 3030.183 shall be obtained from notifications to the Postal Service by the Office of Personnel Management of annual determinations of the funding amounts specific to payments at the end of each fiscal year for Retiree Health Benefits as computed under 5 U.S.C. 8909a(d)(2)(B) and (d)(3)(B)(ii); the Civil Service Retirement System as computed under 5 U.S.C. 8348(h)(2)(B); and the Federal Employees Retirement System as computed under 5 U.S.C. 8423(b)(1)(B), (b)(2) and (b)(3)(B), filed with the Postal Service's section 3652 report.

(b) The values for market dominant revenue, total revenue and market dominant volumes needed for the calculation of retirement obligation rate authority in § 3030.183 shall be obtained from values reported in the Revenue, Pieces, and Weight report, filed by the Postal Service under § 3050.25 of this chapter.

(c) The values for additional rate authority previously provided under this subpart, if any, needed for the calculation of retirement obligation rate authority in § 3030.183 and the calculation of required minimum remittances under § 3030.184 shall be obtained from the Commission's prior determinations.

§ 3030.183 Calculation of retirement obligation rate authority.

(a) *Formulas*—(1) The formula for calculating the amount of retirement obligation rate authority available under this subpart, described in paragraph (b)(1) of this section, is as follows:

Additional rate authority in fiscal year T+1 =

$$\left(1 + \frac{AP_T}{TR_T} - PARAT\right)^{\frac{1}{5-N}} - 1$$

Where,

T = most recently completed fiscal year

AP_T = total amortization payment for fiscal year T

TR_T = total revenue in fiscal year T

PARA_T = previously authorized retirement obligation rate authority, compounded through fiscal year T, expressed as a proportion of the market dominant rate base and calculated using the formula in paragraph (a)(2) of this section as described in paragraph (b)(2) of this section

N = number of previously issued determinations in which retirement obligation rate authority was made available under this subpart

(2) The formula for calculating the amount of previously authorized retirement obligation rate authority through fiscal year T, described in paragraph (b)(2) of this section, is as follows:

Previously authorized retirement obligation rate authority through fiscal year T =

$$1 - \left(\prod_{t=T-N}^T (1 + r_t) \right)^{-1}$$

Where,

T = most recently completed fiscal year

r_t = retirement obligation rate authority authorized in fiscal year t

N = number of previously issued determinations in which retirement obligation rate authority was made available under this subpart

(b) *Calculations*—(1) The amount of retirement obligation rate authority available for a fiscal year shall be calculated in four steps. First, the ratio of the total amortization payment for the fiscal year under review to the total revenue in the fiscal year under review shall be added to 1. This sum represents the factor by which an equal increase in market dominant and competitive rates in the fiscal year under review would generate sufficient additional revenue to make the full amortization payment. It does not account, however, for any previous rate authority authorized under this subpart. The second step is therefore to subtract the proportion of the market dominant rate base resulting from previously authorized retirement obligation rate authority. That proportion is calculated using the formula in § 3030.183(a)(2) as described in § 3030.183(b)(2) Third, to amortize the resulting amount of retirement obligation rate authority over the remainder of the phase-in period, the difference shall be raised to the power of the inverse of the number of determinations remaining in the phase-in period,

including the current determination. Finally, 1 shall be subtracted from the result to convert from a proportional change in rates to a percentage of rate adjustment authority.

(2) The amount of previously authorized retirement obligation rate authority shall be calculated in two steps. First, the sums of 1 and the amount of retirement obligation rate authority authorized in each of the previous fiscal years shall be multiplied together. This product represents the compounded amount of such rate authority, expressed as a net rate increase. To express this product as a proportion of the market dominant rate base, the second step is to subtract the inverse of this product from 1.

§ 3030.184 Required minimum remittances.

(a) *Minimum remittances.* During each fiscal year subsequent to the year of the effective date of this subpart, the Postal Service shall remit towards the liabilities identified in § 3030.182 an amount equal to or greater than the amount of revenue collected as a result of all previous rate increases under this subpart during the previous fiscal year, as calculated using the formulas in paragraph (b) of this section, as described in paragraph (c) of this section.

(b) *Formulas*—(1) The formula for calculating the amount of revenue collected under this subpart during a fiscal year, described in paragraph (c)(1) of this section, is as follows:

Amount of revenue =

$$MDR_T \left(1 - \left(\prod_{t=T-N}^T 1 + (p_t)(r_t) \right)^{-1} \right)$$

Where,

T = most recently completed fiscal year

MDR_T = market dominant revenue in fiscal year T

N = number of previously issued determinations in which retirement obligation rate authority was made available under this subpart

r_t = retirement obligation rate authority authorized in fiscal year t

p_t = prorated fraction of r_t that was in effect during fiscal year T, calculated using the formula in paragraph (a)(2) of this section, as described in paragraph (b)(2) of this section

(2) The formula for calculating the prorated fraction of retirement obligation rate authority authorized in a particular fiscal year t that was in effect during the most recently completed fiscal year, described in paragraph (c)(2) of this section, is as follows:

Prorated fraction =

$$\begin{cases} 0, & \text{if } r_t \text{ was not in effect during fiscal year T} \\ 1, & \text{if } r_t \text{ was in effect for all of fiscal year T} \\ \frac{\left(\frac{E_Q}{D_Q}\right) (QMDV_Q) + \sum_{i=Q+1}^4 QMDV_i}{MDV_T}, & \text{if } r_t \text{ came into effect during fiscal year T} \end{cases}$$

Where,

T = most recently completed fiscal year

r_t = retirement obligation rate authority authorized under this subpart in fiscal year t

Q = the number of the quarter during the fiscal year of the effective date of the price increase including retirement obligation rate authority made available under this subpart

E_Q = number of days in quarter Q subsequent to and including the effective date of the price increase

D_Q = total number of days in quarter Q

$QMDV_Q$ = market dominant volume in quarter Q

MDV_T = market dominant volume in fiscal year T

(c) *Calculations*—(1) The amount of revenue collected under this subpart during a fiscal year, as calculated by the formula in paragraph (b)(1) of this section, shall be calculated in three steps. First, the sums of 1 and the amount of retirement obligation rate authority made available under this subpart during each previous fiscal year—prorated to account for mid-year price increases as described in paragraph (b)(2) of this section—shall be multiplied together. This product represents the proportion by which prices were higher during the most recently completed fiscal year as a result of retirement obligation rate authority. Second, to express this net price increase as a proportion of market dominant revenue, the inverse of this product shall be subtracted from 1. Finally, the result shall be multiplied by market dominant revenue for the fiscal year to change the proportion into a dollar amount.

(2) The prorated fraction of retirement obligation rate authority authorized in a particular fiscal year that was in effect during the most recently completed fiscal year, as calculated by the formula in paragraph (b)(2) of this section, shall be a piecewise

function of three parts. First, if the retirement obligation rate authority authorized in a particular year was not in effect during the most recently completed fiscal year, the prorated fraction shall be 0. Second, if the retirement obligation rate authority authorized in a particular year was in effect during the entirety of the most recently completed fiscal year, the prorated fraction shall be 1. Finally, if the retirement obligation rate authority authorized in a particular fiscal year was used to raise prices during the most recently completed fiscal year, the prorated fraction shall be the proportion of volume sent during the fiscal year after that rate increase went into effect.

This proportion shall be calculated in four steps. First, the number of days of the fiscal quarter after and including the effective date of the price adjustment including the retirement obligation rate authority shall be divided by the total number of days in that fiscal quarter. This quotient determines the proportion of days in that quarter in which the higher rates were in effect. Second, that quotient shall be multiplied by the market dominant volume from that fiscal quarter to determine the amount of volume during the quarter receiving the higher rates. Third, that product shall be added to the market dominant volume from any subsequent quarters of the fiscal year because the volume in those quarters was also sent under the higher rates. Finally, this sum shall be divided by the total market dominant volume from the fiscal year to determine the proportion of annual volume sent after the rate increase went into effect.

§ 3030.185 Forfeiture.

(a) If any of the circumstances described in paragraphs (b) through (d) of this section occur, the Postal Service shall not be eligible for future retirement obligation rate authority under this subpart, and the Commission may commence additional proceedings as appropriate.

(b) If, subsequent to 45 calendar days after the effective date of this subpart and prior to the end of the phase-in period, the Postal Service fails to timely file the notice required under § 3030.181(b);

(c) In any fiscal year in which retirement obligation rate authority was determined to be available under this subpart, the Postal Service fails to timely file under § 3030.122 for a rate increase including the full amount of retirement obligation rate authority authorized under this subpart during that fiscal year, to take effect prior to the end of that fiscal year; or

(d) In any fiscal year including or subsequent to the first fiscal year in which rate authority under this subpart was used to adjust market dominant rates, the Postal Service's total payments towards the supplemental and unfunded liabilities identified in § 3030.182 are not equal to or greater than the minimum remittance required for that fiscal year under § 3030.184(a).

Subpart F—[Reserved]

Subpart G—Non-compensatory Classes or Products

§ 3030.220 Applicability.

This subpart is applicable to a class or product where the attributable cost for that class or product exceeded the revenue from that class or product as determined by the Commission. Section 3030.221 is applicable where the attributable cost for a product within a class exceeded the revenue from that particular product where the product is classified within a class where the overall class revenue exceeded the attributable cost for that class. Section 3030.222 is applicable where the attributable cost for an entire class exceeded the revenue from that class.

§ 3030.221 Individual product requirement.

Whenever the Postal Service files a rate adjustment filing affecting a class of mail which includes a product where the attributable cost for that product exceeded the revenue from that product, as determined by the Commission, the Postal Service shall increase the rates for each non-compensatory product by a minimum of 2 percentage points above the percentage increase for that class. This section does not create additional rate authority applicable to any class of mail. This section only applies to products classified within classes for which the overall class revenue exceeded the attributable cost for that class. This section does not apply to a non-compensatory product for which the Commission has determined that the Postal Service lacks independent authority to set rates (such as rates set by treaty obligation).

§ 3030.222 Class requirement and additional class rate authority.

(a) This section provides 2 percentage points of additional rate authority for any class of mail where the attributable cost for that class exceeded the revenue from that class as determined by the Commission. This additional rate authority is optional and may be used at the Postal Service's discretion.

(b) The Commission shall announce how much, if any, rate authority will be authorized under this subpart. Any rate authority allocated under this subpart:

(1) Shall be made available to the Postal Service as of the date of the Commission's announcement;

(2) Must be included in the calculation of the maximum rate adjustment authority change in rates in the first generally applicable rate adjustment filed after the Commission's announcement; and

(3) May be used to generate unused rate authority, if unused, within 12 months of the Commission's announcement.

Subpart H—Accumulation of Unused and Disbursement of Banked Rate

Adjustment Authority

§ 3030.240 General.

Unless a specific exception applies, unused rate adjustment authority, on a class-by-class basis, shall be calculated for each rate adjustment filing. Unused rate adjustment authority shall be added to the schedule of banked rate authority in each

instance, and be available for application to rate adjustments pursuant to the requirements of this subpart.

§ 3030.241 Schedule of banked rate adjustment authority.

Upon the establishment of unused rate adjustment authority, the Postal Service shall devise and maintain a schedule that tracks the establishment and subsequent use of banked rate authority on a class-by-class basis. At a minimum, the schedule must track the amount of banked rate authority available immediately prior to the rate adjustment filing and the amount of banked rate authority available upon acceptance of the rates included in the rate adjustment filing. It shall also track all changes to the schedule, including the docket numbers of Commission decisions affecting the schedule, the dates and amounts that any rate authority was generated or subsequently expended, and the expiration dates of all rate adjustment authority. The schedule shall be included with any rate adjustment filing purporting to modify the amount of banked rate adjustment authority.

§ 3030.242 Calculation of unused rate adjustment authority for rate adjustments that involve a rate increase which are filed 12 months apart or less.

(a) When rate adjustment filings that involve a rate increase are filed 12 months apart or less, unused rate adjustment authority for a class is equal to the difference between the maximum rate adjustment authority as summarized by § 3030.127 and calculated pursuant to subparts C through H of this part, as appropriate, and the

percentage change in rates for the class calculated pursuant to § 3030.128, subject to the limitations described in paragraph (b) of this section.

(b) For rate adjustment filings that involve a rate increase, unused rate adjustment authority cannot exceed the unused portion of rate authority calculated pursuant to subparts C and D of this part, and § 3030.222.

§ 3030.243 Calculation of unused rate adjustment authority for rate adjustments that involve a rate increase which are filed more than 12 months apart.

(a) When rate adjustment filings that involve a rate increase are filed more than 12 months apart, any interim rate adjustment authority must first be added to the schedule of banked rate authority before the unused rate adjustment authority is calculated.

(b) Interim rate adjustment authority for a class is equal to the Base Average applicable to the second rate adjustment filing (as developed pursuant to § 3030.142) divided by the Recent Average utilized in the first rate adjustment filing (as developed pursuant to § 3030.142) and subtracting 1 from the quotient. The result is expressed as a percentage and immediately added to the schedule of banked rate authority as of the date the rate adjustment filing is filed. If the Commission announces that rate authority calculated pursuant to subpart D of this part or § 3030.222 are available and no rate adjustment is filed before the Commission subsequently announces that further rate authority calculated pursuant to subpart D of this part or § 3030.222 are available, then the amount of rate authority calculated pursuant to subpart D of this part and

§ 3030.222 in the first Commission announcement shall be added to the interim rate adjustment authority.

(c) Unused rate adjustment authority for a class is equal to the difference between the maximum rate adjustment authority as summarized by § 3030.127 and calculated pursuant to subparts C through H of this part, as appropriate, and the percentage change in rates for the class calculated pursuant to § 3030.128, subject to the limitations described in paragraph (d) of this section.

(d) For rate adjustment filings that involve a rate increase, unused rate adjustment authority cannot exceed the unused portion of rate authority calculated pursuant to subparts C and D of this part, and § 3030.222.

§ 3030.244 Calculation of unused rate adjustment authority for rate adjustments that only include rate decreases.

(a) For rate adjustment filings that only include rate decreases, unused rate adjustment authority for a class is calculated in two steps. First, the difference between the maximum rate adjustment authority as summarized by § 3030.127 and calculated pursuant to subparts C through H of this part, as appropriate, for the most recent rate adjustment that involves a rate increase and the percentage change in rates for the class calculated pursuant to § 3030.128(d) is calculated. Second, the unused rate adjustment authority generated in the most recent rate adjustment that involves a rate increase is subtracted from that result.

(b) Unused rate adjustment authority generated under paragraph (a) of this section for a class shall be added to the unused rate adjustment authority generated in the most recent rate adjustment that involves a rate increase on the schedule maintained under § 3030.241. For purposes of § 3030.244, the unused rate adjustment authority generated under paragraph (a) of this section for a class shall be deemed to have been added to the schedule maintained under § 3030.241 on the same date as the most recent rate adjustment filing that involves a rate increase.

(c) For rate adjustment filings that only include rate decreases, the sum of unused rate adjustment authority generated under paragraph (a) of this section and the unused rate adjustment authority generated in the most recent rate adjustment that involves a rate increase cannot exceed the unused portion of rate adjustment authority calculated pursuant to subparts C and D of this part, and § 3030.222 in the most recent rate adjustment that involves a rate increase.

(d) Unused rate adjustment authority generated under paragraph (a) of this section shall be subject to the limitation under § 3030.245, regardless of whether it is used alone or in combination with other existing unused rate adjustment authority.

(e) For rate adjustment filings that only include rate decreases, unused rate adjustment authority generated under this section lapses 5 years from the date of filing of the most recent rate adjustment filing that involves a rate increase.

(f) A rate adjustment filing that only includes rate decreases that is filed immediately after a rate adjustment due to extraordinary or exceptional circumstances

(i.e., without an intervening rate adjustment involving a rate increase) may not generate unused rate adjustment authority.

§ 3030.245 Application of banked rate authority.

(a) Banked rate authority may be applied to any planned rate adjustment subject to the limitations appearing in paragraphs (b) through (f) of this section.

(b) Banked rate authority may only be applied to a proposal to adjust rates after applying rate authority as described in subparts C through F of this part and in § 3030.222, Class requirement and additional class rate authority.

(c) A maximum of 2 percentage points of banked rate authority may be applied to a rate adjustment for any class in any 12-month period. If banked rate authority is used, it shall be subtracted from the schedule of banked rate adjustment authority as of the date of the final order accepting the rates.

(d) Subject to paragraphs (b) and (c) of this section, interim rate adjustment authority may be used to make a rate adjustment pursuant to the rate adjustment filing that led to its calculation. If interim rate adjustment authority is used to make such a rate adjustment, the interim rate adjustment authority generated pursuant to the rate adjustment filing shall first be added to the schedule of banked rate adjustment authority pursuant to § 3030.241 as the most recent entry. Then, any interim rate adjustment authority used in accordance with this paragraph shall be subtracted from the existing banked rate adjustment authority using a first-in, first-out (FIFO) method, beginning 5 years before the instant rate adjustment filing.

(e) Banked rate authority for a class must be applied, using a first-in, first-out (FIFO) method, beginning 5 years before the instant rate adjustment filing.

(f) Banked rate adjustment authority calculated under this section shall lapse 5 years from the date of the rate adjustment filing leading to its calculation.

Subpart I—Rate Adjustments Due to Extraordinary and Exceptional Circumstances

§ 3030.260 General.

The Postal Service may request to adjust rates for market dominant products due to extraordinary or exceptional circumstances pursuant to 39 U.S.C. 3622(d)(1)(E). The rate adjustments are not subject to rate adjustment limitations or the restrictions on the use of unused rate adjustment authority. The rate adjustment request may not include material classification changes. The request is subject to public participation and Commission review within 90 days.

§ 3030.261 Contents of a request.

(a) Each exigent request shall include the items specified in paragraphs (b) through (i) of this section.

(b) A schedule of the planned rates.

(c) Calculations quantifying the increase for each affected product and class.

(d) A full discussion of the extraordinary or exceptional circumstances giving rise to the request, and a complete explanation of how both the requested overall increase and the specific rate adjustments requested relate to those circumstances.

(e) A full discussion of why the requested rate adjustments are necessary to enable the Postal Service, under best practices of honest, efficient, and economical management, to maintain and continue the development of postal services of the kind and quality adapted to the needs of the United States.

(f) A full discussion of why the requested rate adjustments are reasonable and equitable as among types of users of market dominant products.

(g) An explanation of when, or under what circumstances, the Postal Service expects to be able to rescind the exigent rate adjustments in whole or in part.

(h) An analysis of the circumstances giving rise to the exigent request, which should, if applicable, include a discussion of whether the circumstances were foreseeable or could have been avoided by reasonable prior action.

(i) Such other information as the Postal Service believes will assist the Commission in issuing a timely determination of whether the requested rate adjustments are consistent with applicable statutory policies.

§ 3030.262 Supplemental information.

The Commission may require the Postal Service to provide clarification of its request or to provide additional information in order to gain a better understanding of the circumstances leading to the request or the justification for the specific rate adjustments

requested. The Postal Service shall include within its request the identification of one or more knowledgeable Postal Service official(s) who will be available to provide prompt responses to Commission requests for clarification or additional information.

§ 3030.263 Docket and notice.

(a) The Commission will establish a docket for each request to adjust rates due to extraordinary or exceptional circumstances, publish notice of the request in the **Federal Register**, and post the filing on its website. The notice shall include the items specified in paragraphs (b) through (g) of this section.

(b) The general nature of the proceeding.

(c) A reference to legal authority under which the proceeding is to be conducted.

(d) A concise description of the proposals for changes in rates, fees, and the Mail Classification Schedule.

(e) The identification of an officer of the Commission to represent the interests of the general public in the docket.

(f) A specified period for public comment.

(g) Such other information as the Commission deems appropriate.

§ 3030.264 Public hearing.

(a) The Commission will hold a public hearing on the Postal Service's request. During the public hearing, responsible Postal Service officials will appear and respond under oath to questions from the Commissioners or their designees addressing previously identified aspects of the Postal Service's request and supporting information.

(b) Interested persons will be given an opportunity to submit to the Commission suggested relevant questions that might be posed during the public hearing. Such questions, and any explanatory materials submitted to clarify the purpose of the questions, should be filed in accordance with § 3010.120 of this chapter, and will become part of the administrative record of the proceeding.

(c) The timing and length of the public hearing will depend on the nature of the circumstances giving rise to the request and the clarity and completeness of the supporting materials provided with the request.

(d) If the Postal Service is unable to provide adequate explanations during the public hearing, supplementary written or oral responses may be required.

§ 3030.265 Opportunity for comments.

(a) Following the conclusion of the public hearings and submission of any supplementary materials, interested persons will be given the opportunity to submit written comments on:

- (1) The sufficiency of the justification for an exigent rate adjustment;
- (2) The adequacy of the justification for adjustments in the amounts requested by the Postal Service; and
- (3) Whether the specific rate adjustments requested are reasonable and equitable.

(b) An opportunity to submit written reply comments will be given to the Postal Service and other interested persons.

§ 3030.266 Deadline for Commission decision.

Requests under this subpart seek rate relief required by extraordinary or exceptional circumstances and will be treated with expedition at every stage. It is Commission policy to provide appropriate relief as quickly as possible consistent with statutory requirements and procedural fairness. The Commission will act expeditiously on the Postal Service's request, taking into account all written comments. In every instance, a Commission decision will be issued within 90 days of the filing of an exigent request.

§ 3030.267 Treatment of banked rate adjustment authority.

(a) Each request will identify the banked rate adjustment authority available as of the date of the request for each class of mail and the available amount for each of the preceding 5 years.

(b) Rate adjustments may use existing banked rate adjustment authority in amounts greater than the limitations described in § 3030.245.

(c) Increases will exhaust all banked rate adjustment authority for each class of mail before imposing additional rate adjustments in excess of the maximum rate adjustment for any class of mail.

Subpart J—Workshare Discounts**§ 3030.280 Applicability.**

This subpart is applicable whenever the Postal Service proposes to adjust a rate associated with a workshare discount. For the purpose of this subpart, the cost avoided by the Postal Service for not providing the applicable service refers to the amount identified in the most recently applicable Annual Compliance Determination, unless the Commission otherwise provides.

§ 3030.281 Calculation of passthroughs for workshare discounts.

For the purpose of this subpart, the percentage passthrough for any workshare discount shall be calculated by dividing the workshare discount by the cost avoided by the Postal Service for not providing the applicable service and expressing the result as a percentage.

§ 3030.282 Increased pricing efficiency.

(a) For a workshare discount that is equal to the cost avoided by the Postal Service for not providing the applicable service, no proposal to adjust a rate associated with that workshare discount may change the size of the discount.

(b) For a workshare discount that exceeds the cost avoided by the Postal Service for not providing the applicable service, no proposal to adjust a rate associated with that workshare discount may increase the size of the discount.

(c) For a workshare discount that is less than the cost avoided by the Postal Service for not providing the applicable service, no proposal to adjust a rate associated with that workshare discount may decrease the size of the discount.

§ 3030.283 Limitations on excessive discounts.

(a) No proposal to adjust a rate may set a workshare discount that would exceed the cost avoided by the Postal Service for not providing the applicable service, unless at least one of the following reasons provided in paragraphs (b) through (e) of this section applies.

(b) The proposed workshare discount is associated with a new postal service, a change to an existing postal service, or a new workshare initiative.

(c) The proposed workshare discount is a minimum of 20 percent less than the existing workshare discount.

(d) The proposed workshare discount is set in accordance with a Commission order issued pursuant to § 3030.286.

(e) The proposed workshare discount is provided in connection with a subclass of mail, consisting exclusively of mail matter of educational, cultural, scientific, or informational value (39 U.S.C. 3622(e)(2)(C)) and is in compliance with § 3030.285(c).

§ 3030.284 Limitations on discounts below avoided cost.

(a) No proposal to adjust a rate may set a workshare discount that would be below the cost avoided by the Postal Service for not providing the applicable service, unless at least one of the following reasons provided in paragraphs (b) through (e) of this section applies.

(b) The proposed workshare discount is associated with a new postal service, a change to an existing postal service, or a new workshare initiative.

(c) The proposed workshare discount is a minimum of 20 percent more than the existing workshare discount.

(d) The proposed workshare discount is set in accordance with a Commission order issued pursuant to § 3030.286.

(e) The percentage passthrough for the proposed workshare discount is at least 85 percent.

§ 3030.285 Proposal to adjust a rate associated with a workshare discount.

(a) Each proposal to adjust a rate associated with a workshare discount shall be supported by substantial evidence and demonstrate that each proposed workshare discount has been set in compliance with 39 U.S.C. 3622(e) and this subpart. Substantial evidence means such relevant evidence as a reasonable mind might accept as adequate to support a conclusion.

(b) For each proposed workshare discount that would exceed the cost avoided by the Postal Service for not providing the applicable service, the rate adjustment filing shall indicate the applicable paragraph of § 3030.283 under which the Postal Service is justifying the excessive discount and include any relevant analysis supporting the claim.

(c) For each proposed workshare discount that is provided in connection with a subclass of mail, consisting exclusively of mail matter of educational, cultural, scientific, or informational value (39 U.S.C. 3622(e)(2)(C)), would exceed the cost avoided by the Postal Service for not providing the applicable service, and would not be set in accordance with at least one specific provision appearing in § 3030.283(b) through (d),

the rate adjustment filing shall provide the information specified in paragraphs (c)(1) through (3) of this section:

(1) The number of mail owners receiving the workshare discount during the most recent full fiscal year and for the current fiscal year to date;

(2) The number of mail owners for the applicable product or products in the most recent full fiscal year and for the current fiscal year to date; and

(3) An explanation of how the proposed workshare discount would promote the public interest, even though the proposed workshare discount would substantially exceed the cost avoided by the Postal Service.

(d) For each proposed workshare discount that would be below the cost avoided by the Postal Service for not providing the applicable service, the rate adjustment filing shall indicate the applicable paragraph of § 3030.284 under which the Postal Service is justifying the discount that is below the cost avoided and include any relevant analysis supporting the claim.

§ 3030.286 Application for waiver.

(a) In every instance in which the Postal Service determines to adjust a rate associated with a workshare discount in a manner that does not comply with the limitations imposed by §§ 3030.283 through 3030.284, the Postal Service shall file an application for waiver. The Postal Service must file any application for waiver at least 60 days prior to filing the proposal to adjust a rate associated with the applicable

workshare discount. In its application for waiver, the Postal Service shall indicate the approximate filing date for its next rate adjustment filing.

(b) The application for waiver shall be supported by a preponderance of the evidence and demonstrate that a waiver from the limitations imposed by §§ 3030.283 through 3030.284 should be granted. Preponderance of the evidence means proof by information that, compared with that opposing it, leads to the conclusion that the fact at issue is more probably true than not.

(c) The application for waiver shall include a specific and detailed statement signed by one or more knowledgeable Postal Service official(s) who sponsors the application and attests to the accuracy of the information contained within the statement. The statement shall set forth the information specified in paragraphs (c)(1) through (8) of this section, as applicable to the specific workshare discount for which a waiver is sought:

(1) The reason(s) why a waiver is alleged to be necessary (with justification thereof), including all relevant supporting analysis and all assumptions relied upon.

(2) The length of time for which a waiver is alleged to be necessary (with justification thereof).

(3) For each subsequent rate adjustment filing planned to occur during the length of time for which a waiver is sought, a representation of the proposed minimum amount of the change to the workshare discount.

(4) For a claim that the amount of the workshare discount exceeding the cost avoided by the Postal Service for not providing the applicable service is necessary in order to mitigate rate shock (39 U.S.C. 3622(e)(2)(B)), the Postal Service shall provide an explanation addressing all of the items specified in paragraphs (c)(4)(i) through (iii) of this section:

(i) A description of the customers that the Postal Service claims would be adversely affected.

(ii) Prices and volumes for the workshare discount at issue (the benchmark and workshared mail category) for the last 10 years.

(iii) Quantitative analysis or, if not available, qualitative analysis indicating the nature and extent of the likely harm to the customers that would result from setting the workshare discount in compliance with § 3030.283(c).

(5) For a claim that setting an excessive or low workshare discount closer or equal to the cost avoided by the Postal Service for not providing the applicable service would impede the efficient operation of the Postal Service, the Postal Service shall provide an explanation addressing all of the items specified in paragraphs (c)(5)(i) through (iii) of this section:

(i) A description of the operational strategy at issue.

(ii) Quantitative analysis or, if not available, qualitative analysis indicating how the workshare discount at issue is related to that operational strategy.

(iii) How setting the workshare discount in compliance with § 3030.283(c) or § 3030.284(c), whichever is applicable, would impede that operational strategy.

(6) For a claim that reducing or eliminating the excessive workshare discount would lead to a loss of volume in the affected category of mail and reduce the aggregate contribution to the Postal Service's institutional costs from the mail that is subject to the discount (39 U.S.C. 3622(e)(3)(A)), the Postal Service shall provide an explanation addressing all of the items specified in paragraphs (c)(6)(i) through (iii) of this section:

(i) A description of the affected category of mail.

(ii) Quantitative analysis or, if not available, qualitative analysis indicating the expected loss of volume and reduced contribution that is claimed would result from reducing or eliminating the excessive workshare discount.

(iii) How setting the excessive workshare discount in compliance with § 3030.283(c) would lead to the expected loss of volume and reduced contribution.

(7) For a claim that reducing or eliminating the excessive workshare discount would result in a further increase in the rates paid by mailers not able to take advantage of the workshare discount (39 U.S.C. 3622(e)(3)(B)), or a claim that increasing or eliminating a low workshare discount for a non-compensatory product would result in a further increase in the rates paid by mailers not able to take advantage of the workshare discount, the Postal Service shall provide an explanation addressing all of the items specified in paragraphs (c)(7)(i) through (iii) of this section:

(i) A description of the mailers not able to take advantage of the discount.

(ii) Quantitative analysis or, if not available, qualitative analysis indicating the expected size of the rate increase that is claimed would result in the rates paid by mailers not able to take advantage of the discount.

(iii) How setting the excessive workshare discount in compliance with § 3030.283(c) or the low workshare discount for a non-compensatory product in compliance with § 3030.284(c) or § 3030.284(e), whichever is applicable, would result in a further increase in the rates paid by mailers not able to take advantage of the discount.

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

(d) Unless the Commission otherwise provides, commenters will be given at least 7 calendar days to respond to the application for waiver after it has been filed by the Postal Service.

(e) To better evaluate the waiver application, the Commission may, on its own behalf or by request of any interested person, order the Postal Service to provide experts on the subject matter of the waiver application to participate in technical conferences, prepare statements clarifying or supplementing their views, or answer questions posed by the Commission or its representatives.

(f) For a proposed workshare discount that would exceed the cost avoided by the Postal Service for not providing the applicable service, the application for waiver

shall be granted only if at least one provision appearing in 39 U.S.C. 3622(e)(2)(A) through (e)(2)(D) or 39 U.S.C. 3622(e)(3)(A) through (e)(3)(B) is determined to apply.

(g) For a proposed workshare discount that would be set below the cost avoided by the Postal Service for not providing the applicable service, the application for waiver shall be granted only if setting the workshare discount closer or equal to the cost avoided by the Postal Service for not providing the applicable service would impede the efficient operation of the Postal Service or if increasing or eliminating a low workshare discount for a non-compensatory product would result in a further increase in the rates paid by mailers not able to take advantage of the workshare discount.

(h) The Commission will issue an order announcing, at a minimum, whether the requested waiver will be granted or denied no later than 21 days following the close of any comment period(s). An order granting the application for waiver shall specify all conditions upon which the waiver is granted, including the date upon which the waiver shall expire.

PART 3040—PRODUCT LISTS AND THE MAIL CLASSIFICATION SCHEDULE

2. The authority citation for part 3040 continues to read as follows:

Authority: 39 U.S.C. 503; 3622; 3631; 3642; 3682.

3. Amend § 3040.132 by revising paragraphs (a) and (b) to read as follows:

§ 3040.132 Supporting justification.

* * * * *

(a) Explain the reason for initiating the docket and explain why the change is not inconsistent with the applicable requirements of this part and any applicable Commission directives and orders;

(b) Explain why, as to market dominant products, the change is not inconsistent with the policies and the applicable criteria of chapter 36 of title 39 of the United States Code;

* * * * *

4. Amend § 3040.152 by revising paragraphs (a) and (b) to read as follows:

§ 3040.152 Supporting justification.

* * * * *

(a) Explain the reason for initiating the docket and explain why the change is not inconsistent with the applicable requirements of this part and any applicable Commission directives and orders;

(b) Explain why, as to market dominant products, the change is not inconsistent with the policies and the applicable criteria of chapter 36 of title 39 of the United States Code;

* * * * *

5. Amend § 3040.172 by revising paragraphs (a) and (b) to read as follows:

§ 3040.172 Supporting justification.

* * * * *

(a) Explain the reason for initiating the docket and explain why the change is not inconsistent with the applicable requirements of this part and any applicable Commission directives and orders;

(b) Explain why, as to market dominant products, the change is not inconsistent with the policies and the applicable criteria of chapter 36 of title 39 of the United States Code;

* * * * *

6. Amend § 3040.181 by revising paragraph (b)(1) to read as follows:

§ 3040.181 Supporting justification for material changes to product descriptions.

* * * * *

(b)(1) As to market dominant products, explain why the changes are not inconsistent with the policies and the applicable criteria of chapter 36 of title 39 of the United States Code, the applicable requirements of this part, and any applicable Commission directives and orders; or

* * * * *

7. Amend § 3040.182 by revising paragraph (e) to read as follows:

§ 3040.182 Docket and notice of material changes to product descriptions.

* * * * *

(e) Provide interested persons with an opportunity to comment on whether the proposed changes are consistent with the policies and the applicable criteria of chapter

36 of title 39 of the United States Code, the applicable requirements of this part, and any applicable Commission directives and orders.

8. Amend § 3040.190 by revising paragraph (c)(2) to read as follows:

§3040.190 Minor corrections to product descriptions.

* * * * *

(c) * * *

(2) Explain why the proposed corrections are consistent with the policies and the applicable criteria of chapter 36 of title 39 of the United States Code, the applicable requirements of this part, and any applicable Commission directives and orders; and

* * * * *

9. Amend § 3040.191 by revising paragraph (e) to read as follows:

§3040.191 Docket and notice of minor corrections to product descriptions.

* * * * *

(e) Provide interested persons with an opportunity to comment on whether the proposed corrections are consistent with the policies and the applicable criteria of chapter 36 of title 39 of the United States Code, the applicable requirements of this part, and any applicable Commission directives and orders.

10. Add subpart G to read as follows:

Subpart G—Requests for Market Dominant Negotiated Service Agreements

Sec.

3040.220 General.

3040.221 Additional supporting justification for negotiated service agreements.

3040.222 Data collection plan and report for negotiated service agreements.

§ 3040.220 General.

This subpart imposes additional requirements whenever there is a request to add a negotiated service agreement to the market dominant product list. The additional supporting justification appearing in § 3040.221 also should be provided whenever the Postal Service proposes to modify the terms of an existing market dominant negotiated service agreement. Commission findings that the addition of a special classification is not inconsistent with 39 U.S.C. 3622 are provisional and subject to subsequent review. No rate(s) shall take effect until 45 days after the Postal Service files a request for review of a notice of a new rate or rate(s) adjustment specifying the rate(s) and the effective date.

§ 3040.221 Additional supporting justification for negotiated service agreements.

(a) Each request shall also include the items specified in paragraphs (b) through (j) of this section.

(b) A copy of the negotiated service agreement.

(c) The planned effective date(s) of the planned rates.

(d) The identity of a responsible Postal Service official who will be available to provide prompt responses to requests for clarification from the Commission.

(e) A statement identifying all parties to the agreement and a description clearly explaining the operative components of the agreement.

(f) Details regarding the expected improvements in the net financial position or operations of the Postal Service (39 U.S.C. 3622(c)(10)(A)(i) and (ii)). The projection of

the change in net financial position as a result of the agreement shall be based on accepted analytical principles. The projection of the change in net financial position as a result of the agreement shall include for each year of the agreement:

(1) The estimated mailer-specific costs, volumes, and revenues of the Postal Service absent the implementation of the negotiated service agreement;

(2) The estimated mailer-specific costs, volumes, and revenues of the Postal Service which result from implementation of the negotiated service agreement;

(3) An analysis of the effects of the negotiated service agreement on the contribution to institutional costs from mailers not party to the agreement;

(4) If mailer-specific costs are not available, the source and derivation of the costs that are used shall be provided, together with a discussion of the currency and reliability of those costs and their suitability as a proxy for the mailer-specific costs; and

(5) If the Postal Service believes the Commission's accepted analytical principles are not the most accurate and reliable methodology available:

(i) An explanation of the basis for that belief; and

(ii) A projection of the change in net financial position resulting from the agreement made using the Postal Service's alternative methodology.

(g) An identification of each component of the agreement expected to enhance the performance of mail preparation, processing, transportation, or other functions in each year of the agreement, and a discussion of the nature and expected impact of each such enhancement.

(h) Details regarding any and all actions (performed or to be performed) to assure that the agreement will not result in unreasonable harm to the marketplace (39 U.S.C. 3622(c)(10)(B)).

(i) A discussion in regard to how functionally similar negotiated service agreements will be made available on public and reasonable terms to similarly situated mailers.

(j) Such other information as the Postal Service believes will assist the Commission in issuing a timely determination of whether the requested changes are consistent with applicable statutory policies.

§ 3040.222 Data collection plan and report for negotiated service agreements.

(a) The Postal Service shall include with any request concerning a negotiated service agreement a detailed plan for providing data or information on actual experience under the agreement sufficient to allow evaluation of whether the negotiated service agreement operates in compliance with 39 U.S.C. 3622(c)(10).

(b) A data report under the plan is due 60 days after each anniversary date of implementation and shall include, at a minimum, the following information for each 12-month period the agreement has been in effect:

(1) The change in net financial position of the Postal Service as a result of the agreement. This calculation shall include for each year of the agreement:

(i) The actual mailer-specific costs, volumes, and revenues of the Postal Service;

(ii) An analysis of the effects of the negotiated service agreement on the net overall contribution to the institutional costs of the Postal Service; and

(iii) If mailer-specific costs are not available, the source and derivation of the costs that are used shall be provided, including a discussion of the currency and reliability of those costs and their suitability as a proxy for the mailer-specific costs.

(2) A discussion of the changes in operations of the Postal Service that have resulted from the agreement. This shall include, for each year of the agreement, identification of each component of the agreement known to enhance the performance of mail preparation, processing, transportation, or other functions in each year of the agreement.

(3) An analysis of the impact of the negotiated service agreement on the marketplace, including a discussion of any and all actions taken to protect the marketplace from unreasonable harm.

PART 3045—RULES FOR MARKET TESTS OF EXPERIMENTAL PRODUCTS

11. The authority citation for part 3045 continues to read as follows:

Authority: 39 U.S.C. 3641.

12. Amend § 3045.15 by revising paragraph (a) to read as follows:

§ 3045.15 Dollar amount limitation.

(a) The Consumer Price Index used for calculations under this part is the CPI-U index, as specified in § 3030.141(a) of this chapter.

* * * * *

PART 3050—PERIODIC REPORTING

13. The authority citation for part 3050 continues to read as follows:

Authority: 39 U.S.C. 503; 3651; 3652; 3653.

14. Amend § 3050.20 by revising paragraph (c) to read as follows:

§ 3050.20 Compliance and other analyses in the Postal Service’s section 3652 report.

* * * * *

(c) It shall address such matters as non-compensatory rates and failures to achieve stated goals for on-time delivery standards. A more detailed analysis is required when the Commission observed and commented upon the same matter in its Annual Compliance Determination for the previous fiscal year.

15. Amend § 3050.21 by:

- a. Revising paragraphs (a), (e), and (m); and
- b. Adding paragraphs (n) and (o).

The revisions and additions read as follows:

§ 3050.21 Content of the Postal Service's section 3652 report.

(a) No later than 90 days after the close of each fiscal year, the Postal Service shall submit a report to the Commission analyzing its cost, volume, revenue, rate, and service information in sufficient detail to demonstrate that all products during such year comply with all applicable provisions of title 39 of the United States Code. The report shall provide the items in paragraphs (b) through (o) of this section.

* * * * *

(e) For each market dominant workshare discount offered during the reporting year:

- (1) The per-item cost avoided by the Postal Service by virtue of such discount;
- (2) The percentage of such per-item cost avoided that the per-item workshare discount represents;
- (3) The per-item contribution made to institutional costs;
- (4) The factual and analytical bases for any claim that one or more of the exception provisions of 39 U.S.C. 3622(e)(2)(A) through (e)(2)(D) or 39 U.S.C. 3622(e)(3)(A) through (e)(3)(B) apply; and

(5) For each workshare discount that is provided in connection with a subclass of mail, consisting exclusively of mail matter of educational, cultural, scientific, or informational value (39 U.S.C. 3622(e)(2)(C)), exceeded the cost avoided by the Postal Service for not providing the applicable service, and was not set in accordance with at least one specific provision appearing in § 3030.262(b) through (d) of this chapter, the information specified in paragraphs (5)(i) through (iii) of this section:

(i) The number of mail owners receiving the workshare discount;

(ii) The number of mail owners for the applicable product or products; and

(iii) An explanation of how the workshare discount promotes the public interest, even though the workshare discount substantially exceeds the cost avoided by the Postal Service.

* * * * *

(l) For the Inbound Letter Post product, provide revenue, volume, attributable cost, and contribution data by Universal Postal Union country group and by shape for the fiscal year subject to review and each of the preceding 4 fiscal years;

(m) Input data and calculations used to produce the annual Total Factor Productivity estimates;

(n) Copies of notifications to the Postal Service by the Office of Personnel Management (OPM) of annual determinations of the funding amounts specific to payments at the end of each fiscal year computed under 5 U.S.C. 8909a(d)(2)(B) and 5 U.S.C. 8909a(d)(3)(B)(ii); 5 U.S.C. 8348(h)(2)(B) and 5 U.S.C. 8423(b)(3)(B); 5 U.S.C. 8423(b)(1)(B) and 5 U.S.C. 8423(b)(2); and

(o) Provide any other information that the Postal Service believes will help the Commission evaluate the Postal Service's compliance with the applicable provisions of title 39 of the United States Code.

16. Add § 3050.55 to read as follows:

§ 3050.55 Information pertaining to cost reduction initiatives.

(a) The reports in paragraphs (b) through (f) of this section shall be filed with the Commission at the times indicated.

(b) Within 95 days after the end of each fiscal year, the Postal Service shall file a financial report that analyzes cost data from the fiscal year. For purposes of this paragraph, the percentage change shall compare the fiscal year under review to the previous fiscal year. At a minimum, the report shall include:

(1) For all market dominant mail, the percentage change in total unit attributable cost;

(2) For each market dominant mail product, the percentage change in unit attributable cost;

(3) For the system as a whole, total average cost per piece, which includes all Postal Service competitive and market dominant attributable costs and institutional costs,

(4) The percentage change in total average cost per piece;

(5) Market dominant unit attributable cost by product;

(6) If the percentage change in unit attributable cost for a market dominant mail product is more than 0.0 percent and exceeds the percentage change in total market dominant mail unit attributable cost, then the following information shall be provided:

(i) Unit attributable cost workpapers for the product disaggregated into the following cost categories: mail processing unit cost, delivery unit cost, vehicle service

driver unit cost, purchased transportation unit cost, window service unit cost, and other unit cost;

(ii) A narrative that identifies cost categories that are driving above average increases in unit attributable cost for the product and explains the reason for the above-average increase; and

(iii) A specific plan to reduce unit attributable cost for the product.

(7) An analysis of volume trends and mail mix changes for each market dominant mail product from fiscal year 2017 through the end of the fiscal year under review, which shall include at a minimum:

(i) A comparison of actual unit attributable costs and estimated unit attributable costs for each market dominant mail product, using the volume distribution from fiscal year 2017;

(ii) A narrative that identifies the drivers of change in volume trends and the mail mix; and

(iii) A narrative that explains the methodology used to calculate the estimated unit attributable costs as required by paragraph (b)(7)(i) of this section.

(c) Within 95 days after the end of each fiscal year, the Postal Service shall file a report with analysis of each planned cost reduction initiative that is expected to require Postal Service total expenditures of \$5 million or more over the duration of the initiative. At a minimum, the report shall include:

(1) A narrative that describes each cost reduction initiative planned for future fiscal years, including the status, the expected total expenditure, start date, end date, and any intermediate deadlines;

(2) Identification of a metric to measure the impact of each planned cost reduction initiative identified in paragraph (c)(1) of this section, a narrative describing the selected metric, a narrative explaining the reason for selecting that metric, and a schedule approximating the months and fiscal years in which the cost reduction impact is expected to be measureable;

(3) Estimates of the expected impact of each planned cost reduction initiative, with supporting workpapers, using the metric identified in paragraph (c)(2) of this section, total market dominant mail attributable unit cost, and total unit cost as calculated pursuant to paragraph (b)(3) of this section.

(d) Within 95 days after the end of each fiscal year, the Postal Service shall file a report that describes each active cost reduction initiative during the fiscal year which incurred or is expected to incur Postal Service expenditures of \$5 million or more over the duration of the initiative. At a minimum, the report shall include:

(1) The information described in paragraphs (c)(1) through (c)(3) of this section, based on actual data for the fiscal year, and a specific statement as to whether the initiative actually achieved the expected impact as measured by the selected metric;

(2) An explanation of the trends, changes, or other reasons that caused any variance between the actual information provided under paragraph (d)(1) of this section

and the estimated information previously provided under paragraphs (c)(1) through (c)(3) of this section, if applicable;

(3) A description of any mid-implementation adjustments the Postal Service has taken or will take to align the impacts with the schedule; and

(4) Any revisions to the schedule of cost reduction impacts for future fiscal years.

(e) Within 95 days after the end of each fiscal year, the Postal Service shall file a report that summarizes all projects associated with a Decision Analysis Report for the fiscal year. At a minimum, the report shall include:

(1) A description of each project;

(2) The status of each project;

(3) An estimate of cost savings or additional revenues from each project; and

(4) The return on investment expected from each project.

(f) Within 95 days after the end of each fiscal year, the Postal Service shall file a report that summarizes all planned projects that have an approved Decision Analysis Report for the next fiscal year. At a minimum, the report shall include:

(1) A description of each planned project;

(2) The status of each project;

(3) An estimate of the cost savings or additional revenues expected from each project; and

(4) The return on investment expected from each project.

17. Amend § 3050.60 by:

- a. Revising paragraph (a);
- b. Removing paragraph (e);
- c. Redesignating paragraphs (f) and (g) as paragraphs (e) and (f).

The revision reads as follows:

§ 3050.60 Miscellaneous reports and documents.

(a) The reports in paragraphs (b) through (f) of this section shall be provided at the times indicated.

* * * * *

**PART 3055—SERVICE PERFORMANCE AND CUSTOMER SATISFACTION
REPORTING**

18. The authority citation for part 3055 continues to read as follows:

Authority: 39 U.S.C. 503; 3622(a); 3652(d) and (e); 3657(c).

19. Amend § 3055.2 by revising paragraph (c) to read as follows:

§ 3055.2 Contents of the annual report of service performance achievements.

* * * * *

(c) The applicable service standard(s) for each product. If there has been a change to a service standard(s) since the previous report, a description of and reason for the change shall be provided. If there have been no changes to service standard(s) since the previous report, a certification stating this fact shall be provided.

* * * * *

APPENDIX A TECHNICAL APPENDIX (DENSITY AND RETIREMENT)

I. DENSITY-BASED RATE AUTHORITY

A. Density-Based Rate Authority Formula

1. Introduction

As discussed in Chapter IV. of the Order, the density-based rate authority is intended to approximate the increase in per-unit costs that would be expected¹ as a result of the decline in mail density. The amount of the expected increase is governed by the concept of elasticity, which measures the proportional change in one variable in response to a proportional change in another variable. The Commission's estimate of the expected proportional increase in per-unit costs in response to a measured change in density thus requires a reasonable approximation of the elasticity of per-unit costs with respect to density.

The Commission has determined that the institutional cost ratio, multiplied by negative 1, is a reasonable proxy for the elasticity of per-unit costs with respect to density. See Order, Section IV.C.1. The mathematical basis for that choice, along with the corresponding definitions and assumptions, are detailed below.

2. Definitions and Assumptions

Definition of density. The estimate of the amount that per-unit costs would be expected to increase in response to a measured decline in density is contingent upon several assumptions, the first of which is how density is defined. In the most general

¹ As discussed in Chapter IV., the Commission's use of the term "expected" is due to this use of an approximation of a cost elasticity to estimate the increase in unit costs driven by the prior year's decline in density. It is not a forecast of future results. This temporal aspect of the density-based rate authority is similar to that of the CPI-U price cap, which provides rate authority based on the change in CPI-U over the prior 12 months, rather than a forecast of inflation.

case, the concept of density measures the volume of goods and services provided per network node, but there are several possible methods for measuring volume, and several possible methods for counting network nodes. For purposes of the density-based rate authority, the Commission has chosen to measure volume and network nodes using the definitions that most closely align with the root problem the density-based rate authority is designed to address: the unavoidable increase in per-unit costs as less mail is delivered to more places.

Per-unit costs are measured as total costs divided by the number of mailpieces. Thus, the Commission finds it logical and reasonable to similarly measure the change in mail volume based on the number of mailpieces. Alternative approaches to measuring the change in volume, such as weighting volume by revenue, would introduce revenue as a confounding factor that would complicate the analysis of how a change in revenue-weighted volume would be expected to drive a change in (not-revenue-weighted) per-unit costs. See Order, Section IV.C.2. (rejecting commenter suggestions to consider differences in revenue or contribution in the mail mix).

Similarly, the number of places that mail is delivered to is directly measured by the number of delivery points. Thus, the number of delivery points is the logical and reasonable measure of the size of the network for purposes of calculating mail density. One limitation of using the raw number of delivery points is that it does not capture differences in the cost of servicing different types of delivery points.² However, in the current environment, the increase in the number of delivery points is driven mainly by population growth adding new nodes to the network. As long as this trend continues, the increasing cost of servicing the growing network will inevitably be spread over the remaining mailpieces, driving an increase in per-unit costs regardless of whether the

² For example, the Postal Service has estimated delivery costs to differ significantly between door delivery, curbside delivery, and the use of centralized delivery to cluster boxes to apartment buildings. See United States Government Accountability Office, U.S. Postal Service: Delivery Mode Conversions Could Yield Large Savings, but More Current Data Are Needed, May, 2014, at 11, available at: <https://www.gao.gov/assets/670/663107.pdf>.

new delivery points tend to have above-average or below-average costs to service. The Commission concludes that delivery points are the best measure of the number of network nodes for purposes of the density-based rate authority.

Assumptions. The derivation of the density-based rate authority formula presented in the next section is based on the Postal Service's existing costing methodology. This approach highlights how the formula takes into account much of the nuance of the existing costing system, while also requiring fewer assumptions than alternative derivations. These assumptions are detailed below. The Commission emphasizes that it finds these assumptions reasonable only in the specific context of estimating the effect of changes in density on changes in unit costs for the Postal Service as a whole, and not for purposes of cost attribution (which requires product-level causation).

The Commission notes that it is common in economic analysis to assume that cost functions in network industries, including the Postal Industry, take on a

Cobb-Douglas form.³ Cobb-Douglas cost functions are homogeneous functions of degree one, but require the additional assumption of locally constant elasticity. The commonplace use of the Cobb-Douglas form in economic analysis supports the assumption of homogeneity of degree one of the generalized cost functions of each cost segment, but by not assuming that those cost functions take a Cobb-Douglas form, the derivation below avoids the need to assume locally constant elasticity.⁴

³ See, e.g., NERA Consulting, *Economics of Postal Services*, June 2004, available at: https://www.acm.nl/sites/default/files/old_publication/publicaties/11241_2004-nera-final-postal-report_en.pdf, with an appendix at: <https://ec.europa.eu/docsroom/documents/14108/attachments/2/translations/en/renditions/native> (developing an econometric model of postal costs in Europe and finding that the best data fit can be obtained by using the Cobb-Douglas form); J.F. Banos and Ana Rodriguez-Alvarez, *Estimating Technical and Allocative Efficiency by Means of a Bayesian Approach: An Application to the Postal Sector*, February 2015, available at: https://www.researchgate.net/publication/291115601_ESTIMATING_TECHNICAL_AND_ALLOCATIVE_EFFICIENCY_BY_MEANS_OF_A_BAYESIAN_APPROACH_AN_APPLICATION_TO_THE_POSTAL_SECTOR (analyzing technical and allocative efficiency using an econometric estimate based on a Cobb-Douglas form); Denis Lawrence, *et al.*, Memorandum, January 22, 2014, available at: <https://www.accc.gov.au/system/files/Economic%20Insights%20memo%20on%20Australia%20Post%E2%80%99s%20mail%20and%20delivery%20centre%20cost%20elasticities.pdf> (conducting an econometric analysis of the effect of declining mail volume using a Cobb-Douglas form); Francois Destandau and Serge Garcia, *Service Quality, Scale Economies, and Ownership: An Econometric Analysis of Water Supply Costs*, *Journal of Regulatory Economics* 46(2), October 2015, available at: https://www.researchgate.net/publication/264086779_Service_quality_scale_economies_and_ownership_An_econometric_analysis_of_water_supply_costs making an econometric estimate of water supply costs using a Cobb-D); Michael Kuenzle, *Cost Efficiency in Network Industries: Application of Stochastic Frontier Analysis*, ETH Zurich Research Collection 2005, pages 17-32), available at: <https://www.research-collection.ethz.ch/handle/20.500.11850/53059> (discussing use of the Cobb-Douglas cost function in the context of cost efficiency).

⁴ Were the Commission to additionally assume that the cost function of the Postal Service as a whole takes on a Cobb-Douglas form, an alternative derivation of the density-based rate authority formula is possible. This derivation follows from the observations that in a Cobb-Douglas function the cost elasticities of volume and delivery points would sum to one, and that the cost elasticity of volume can be approximated as the ratio of volume-variable costs to total costs, because when volume declines, it is primarily volume-variable costs that decline. The Commission finds that the assumption that the cost function of the Postal Service as whole takes on a Cobb-Douglas form would be reasonable for the purposes of the density-based rate authority, and thus the alternative derivation described in this footnote would justify use of the density-based rate authority. The Commission instead presents the more-detailed derivation in the following section because it shows how the density-based rate authority formula can be derived even without the assumption of locally constant elasticity, and because the derivation presented shows in more depth how the formula is consistent with much of the nuance of the existing costing system. Allowing for variable elasticity ensures that the conclusions hold for a wide set of cost functions, including the Cobb-Douglas function, and therefore increases the robustness of these conclusions.

For the specific purpose of the density-based rate authority the Commission starts by assuming that the cost functions of each cost segment, when generalized to include network size, are homogeneous functions of degree one over a local domain.⁵ In practical terms, this means that the generalized cost functions of each cost segment exhibit constant returns to scale, which means that changing the value of all inputs to the generalized cost function by some factor will also change the output by the same factor. In the context of the mail density, this means assuming that changing both the number of cost driver units and the size of the network by some factor would result in costs changing by the same factor.⁶ This assumption is consistent with the idea that changes in density drive changes in per-unit costs: were both volume and delivery points to increase by 10 percent, the assumption of constant returns to scale says that costs would also increase by 10 percent, leaving both density and per-unit costs constant. By contrast, if density changes, then volume and delivery points necessarily change at different rates and, under the assumption of constant returns to scale, total costs will change by a different factor than volume, resulting in a change in per-unit costs.

The Postal Service's cost segments measure costs in relationship to cost drivers that are chosen to capture the relationship between the activities in each cost segment and the costs incurred. This contrasts with the density-based rate authority formula, which measures changes in per-unit costs based on the number of mailpieces. However, most cost drivers are correlated with volume, and as described in the next section, for purposes of the density-based rate authority the Commission finds it reasonable to assume that changes in the number of mailpieces results in proportional changes in the number of units of each cost driver. As shown in the following sections, this relationship permits using mailpieces as the measure of volume for purposes of

⁵ The Commission also assumes that the cost functions of each cost segment are differentiable over the same domain.

⁶ It is important to note that assuming constant returns to scale does not prevent the Postal Service from enjoying economies of density.

calculating the amount of the density-based rate authority, while still taking into account the relationship between cost and volume in each cost segment as measured by the cost drivers.

3. Derivation

With the assumption, above, that the generalized cost function for the Postal Service's cost segments is a homogeneous function of degree one, it follows from Euler's homogeneous function theorem that the elasticities of total cost with respect to the cost driver, and with respect to network size, sum to one. Therefore, if the elasticity of total cost, C , with respect to the cost driver, D , is $\varepsilon_C(D)$, then the elasticity of cost with respect to network size, N , is:

$$(1) \quad \varepsilon_C(N) = 1 - \varepsilon_C(D).$$

This identity can be used to express the growth rate of the total cost of the cost segment in terms of the elasticity of total cost with respect to the cost driver, along with the growth rates of the cost driver and the network size, as follows.

First, the percentage growth rate of the total cost of a cost segment over time, $r_C(t)$, equals the partial derivative of cost with respect to time, divided by the total cost:

$$(2) \quad r_C(t) = \frac{\partial C}{\partial t}.$$

By the total derivative rule, equation (2) can be rewritten in terms of the partial derivatives of the cost driver with respect to time, and the network size with respect to time:

$$(3) \quad r_C(t) = \frac{\left(\frac{\partial C}{\partial D}\right)\left(\frac{\partial D}{\partial t}\right) + \left(\frac{\partial C}{\partial N}\right)\left(\frac{\partial N}{\partial t}\right)}{C},$$

which can in turn be rewritten as:

$$(4) \quad r_C(t) = \left(\frac{D}{C}\right)\left(\frac{\partial C}{\partial D}\right)\left(\frac{\partial D}{\partial t}\right) + \left(\frac{N}{C}\right)\left(\frac{\partial C}{\partial N}\right)\left(\frac{\partial N}{\partial t}\right),$$

which becomes:

$$(5) \quad r_C(t) = \left(\frac{\partial C}{\partial D} D \right) \left(\frac{\partial D}{\partial t} \right) + \left(\frac{\partial C}{\partial N} N \right) \left(\frac{\partial N}{\partial t} \right).$$

The first factors of each term of the right side of equation (5) are, by definition, the elasticities of total cost with respect to the cost driver and network size, respectively. Similarly, the second factors of each term are, by definition, the percentage growth rate of the cost driver and network size over time, respectively. Accordingly, equation (5) can be rewritten as:

$$(6) \quad r_C(t) = \varepsilon_C(D) r_D(t) + \varepsilon_C(N) r_N(t).$$

Substitution of equation (1) into equation (6) yields:

$$(7) \quad r_C(t) = \varepsilon_C(D) r_D(t) + (1 - \varepsilon_C(D)) r_N(t),$$

which can be rewritten as:

$$(8) \quad r_C(t) = r_N(t) + \varepsilon_C(D) (r_D(t) - r_N(t)),$$

where the percentage growth rate of total cost is expressed in terms of the elasticity of total cost with respect to the cost driver, along with the percentage growth rates of the cost driver and network size.

The density-based rate authority formula is derived from equation (8) by first noting that, in postal costing methodology, each cost driver is chosen to best reflect the relationship between volume and cost for that cost segment. The cost driver of a cost segment is assumed here to be proportional to volume as measured by the number of mailpieces. Therefore, all else equal, the percentage growth rate of each cost driver can be expected to equal the percentage growth rate of volume. Substitution of the percentage growth rate of volume, $r_V(t)$, into equation (8) yields:

$$(9) \quad r_C(t) = r_N(t) + \varepsilon_C(D) (r_V(t) - r_N(t)).$$

Similarly, in postal costing methodology the elasticity of the total cost of a cost segment with respect to the cost driver equals the ratio of volume-variable cost to total cost.⁷ Thus, using the C_v for volume-variable cost, substitution into equation (9) yields:

$$(10) \quad r_C(t) = r_N(t) + \left(\frac{C_v}{C}\right) (r_V(t) - r_N(t)).$$

The next step to derive the density-based rate authority formula is to convert from total cost to per-unit cost. With the observation that the percentage growth rate of per-unit cost equals the difference between the percentage growth rate of total cost and the percentage growth rate of volume, equation (10) becomes:

$$(11) \quad r_C(t) - r_V(t) = r_N(t) + \left(\frac{C_v}{C}\right) (r_V(t) - r_N(t)) - r_V(t),$$

which can be rewritten as:

$$(12) \quad r_C(t) - r_V(t) = \left(r_N(t) - \left(\frac{C_v}{C}\right) r_N(t)\right) - \left(r_V(t) - \left(\frac{C_v}{C}\right) r_V(t)\right),$$

which simplifies to:

$$(13) \quad r_C(t) - r_V(t) = r_N(t) \left(1 - \frac{C_v}{C}\right) - r_V(t) \left(1 - \frac{C_v}{C}\right),$$

and:

$$(14) \quad r_C(t) - r_V(t) = -\left(1 - \frac{C_v}{C}\right) (r_V(t) - r_N(t)).$$

At the cost segment level, volume-variable costs are attributable. Denoting attributable costs as A , equation (14) becomes:

$$(15) \quad r_C(t) - r_V(t) = -\left(1 - \frac{A}{C}\right) (r_V(t) - r_N(t)).$$

Because $r_C(t) - r_V(t)$ is the percentage growth rate of per-unit costs, and $r_V(t) - r_N(t)$ is the percentage growth rate of density, equation (15) shows how, at the cost segment

⁷ This sets aside product-specific fixed costs, which are small enough not to substantially affect the general system-wide relationship between density and per-unit costs that is the focus of this analysis.

level, the complement of the ratio of attributable costs to total costs, multiplied by negative 1, is the elasticity of per-unit costs with respect to density.

Generalizing from the cost segment level to the Postal Service as a whole, is more difficult, because total institutional costs are not the sum of non-volume-variable costs of each cost segment due to additional complexities of the Postal Service's costing system. In particular, a portion of inframarginal costs are attributed, as are group-specific costs, complicating the analysis. Nevertheless, the Commission finds equation (15) a sufficiently accurate approximation when applied to the Postal Service as a whole to be a useful tool for estimating the expected increase in per-unit costs caused by a particular change in density. When applied to the Postal Service as a whole, the complement of the ratio of attributable costs to total costs is the ratio of institutional costs, I , to total costs, which yields:

$$(16) \quad r_C(t) - r_V(t) = -\left(\frac{I}{C}\right) (r_V(t) - r_N(t)).$$

Substituting the amount of the density-based rate authority for the percentage growth rate in per-unit costs into equation (16), and using delivery points as the measure of network size, as described in the previous section, yields the density-based rate authority formula.

The Commission notes that the formula is built on the same general principles as the rest of the Postal Service's costing system, as generalized to include network size.⁸ The Commission also notes that there is no reason to assume that equation (16) is biased towards producing either an over- or under-estimate of the impact of changes in density on per-unit costs. Additionally, as described in the next section, equation (16)—and thus the density-based rate authority formula—account for much of the nuance of the Postal Service's costing system, including the differences in how volume is

⁸ The Commission reiterates that it is generalizing the cost functions of each cost segment to include as an input the number of delivery points only in the specific context of estimating the density-driven change in per-unit costs, which necessarily involves the consideration of network size.

measured in each cost segment, and the changes in costs between cost segments as the mail mix changes.

4. Properties of the Density-Based Rate Authority Formula

As mentioned in the previous section, the volume-variable costs of each cost segment are determined using the elasticity of total cost with respect to the cost segment's cost driver. Although the total institutional cost of the Postal Service does not equal the sum of the non-volume-variable costs of each cost segment due to the complexities described above, changes in the elasticity of each cost segment still drive changes in the total institutional cost ratio, which will in turn be captured by the use of the institutional cost ratio in the density-based rate authority formula.

If, for example, the mail mix were to change to favor products with lower elasticity of total cost with respect to volume (or analogously, per-unit cost with respect to density), costs will shift from more-elastic cost segments to less-elastic cost segments, which will in turn increase the institutional cost ratio. Similarly, differences in the relationship between volume and cost between mail classes (*e.g.*, the degree weight is a factor in costs) is captured by the fact that each cost segment uses cost drivers tailored to the activity measured by that cost segment. If the mail mix were to shift to classes reliant on air transportation where weight is a larger factor, costs will shift to the relevant cost segments and the elasticity of those segments will have a greater influence on the overall institutional cost ratio. Accordingly, while using the institutional cost ratio as a proxy for the elasticity of per-unit costs with respect to density has the virtue of being a very simple measure, it still accounts for the major sources of nuance in the Postal Service's costing systems. That combination makes the institutional cost ratio a particularly useful proxy for purposes of the density-based rate authority formula.

B. Hypothetical Example

For illustration purposes, the Commission reprints the example presented in Order No. 5337 as Table IV-3. Order No. 5337 at 79-80. This example shows the hypothetical amount of density rate authority that would have been authorized in each of the fiscal years from 2013 through 2019, had the density-based rate authority been in effect those years. Note that for each of these years, using the change in total density produces less density rate authority than the change in Market Dominant density, but that may or may not be true in future years.

Table A-1
Hypothetical Density Rate Authority Using Historical Data

FY Density Rate Authority Authorized	Based on Data from FYs	Institutional Cost Ratio	%Δ Density (MD)	%Δ Density (Total)	Density Rate Authority
2013	2011 & 2012	50.06%	-6.06%	-5.38%	2.69%
2014	2012 & 2013	45.84%	-1.89%	-1.51%	0.69%
2015	2013 & 2014	46.60%	-2.94%	-2.68%	1.25%
2016	2014 & 2015	45.69%	-1.92%	-1.57%	0.72%
2017	2015 & 2016	47.15%	-1.11%	-0.76%	0.36%
2018	2016 & 2017	42.62%	-4.53%	-4.04%	1.72%
2019	2017 & 2018	41.13%	-3.41%	-2.95%	1.21%

Source: See Section I.C., *infra*, for references source data.

C. Data Table Sources

Section IV.C.1. of the Order contains two tables: Table IV-1 and Table IV-2. Each table compiles data from the PAEA period, with each year's data taken from separate sources. These sources are detailed below, along with the sources for Table A-1, *supra*.

Table IV-1. Market Dominant volume data were taken from the Revenue, Piece, and Weight (RPW) reports in the library references filed with the Commission's Annual

Compliance Determinations (ACDs).⁹ Delivery point data were taken from the Postal Service's Total Factor Productivity (TFP) reports.¹⁰

⁹ Docket No. ACR2007, Library Reference PRC-ACR2007-LR1, March 27, 2008, Excel file "07 Summary DM_LR1.xls," tab "PRESS," cell B32 (showing FY 2007 Market Dominant volume); Docket No. ACR2008, Library Reference PRC-ACR2008-LR-1, March 30, 2009, Excel file "08 Public RPW_LR1.xls," tab "RPW Report," cell I105 (showing FY 2008 Market Dominant volume); Docket No. ACR2009, Library Reference PRC-ACR2009-LR-1, March 29, 2010, Excel file "09 Public RPW_LR1.xls," tab "PRC PRW," cell G232 (showing FY 2009 Market Dominant volume); Docket No. ACR2010, Library Reference PRC-ACR2010-LR-1, March 29, 2011, Excel file "10 Public RPW_LR1.xls," tab "PRC RPW," cell G250 (showing FY 2010 Market Dominant volume); Docket No. ACR2011, Library Reference PRC-ACR2011-LR-1, March 28, 2012, Excel file "11 Public RPW_LR1.xls," tab "PRC RPW," cell G250 (showing FY 2011 Market Dominant volume); Docket No. ACR2012, Library Reference PRC-ACR2012-LR-1, March 28, 2013, Excel file "12 Public RPW_LR1.xls," tab "PRC RPW," cell G246 (showing FY 2012 Market Dominant volume); Docket No. ACR2014, Library Reference PRC-LR-ACR2014/1, March 27, 2015, Excel file "14 Public RPW.xls," tab "PRC RPW," cell I248 (FY 2014 RPW) (showing FY 2013 Market Dominant volume); FY 2014 RPW, cell H248 (showing FY 2014 Market Dominant volume); Docket No. ACR2015, Library Reference PRC-LR-ACR2015/1, March 28, 2016, Excel file "15 Public RPW.xls," tab "PRC RPW," cell H252 (showing FY 2015 Market Dominant volume); Docket No. ACR2016, Library Reference PRC-LR-ACR2016/1, March 28, 2017, Excel file "16 Public RPW.xls," tab "FY 2016 Public," cell L78 (showing FY 2016 Market Dominant volume); Docket No. ACR2017, Library Reference PRC-LR-ACR2017-1, March 29, 2018, Excel file "17 Public RPW.xls," tab "FY 2017 Public," cell L78 (showing FY 2017 Market Dominant volume); Docket No. ACR2018, Library Reference PRC-LR-ACR2018-1, April 12, 2019, Excel file "18 Public RPW.xlsx," tab "FY 2018 Public," cell L74 (showing FY 2018 Market Dominant volume); Docket No. ACR2019, Library Reference PRC-LR-ACR2019-1, March 25, 2020, Excel file "19 Public RPW.xls," tab "FY 2019 Public," cell L71 (showing FY 2019 Market Dominant volume).

¹⁰ USPS Annual Tables, FY 2019 TFP (Total Factor Productivity), February 27, 2020, Excel file "Table Annual 2019 Public.xlsx," tab "Out-46," cells K58:K70 (showing delivery points for FY 2007 through FY 2019).

Table IV-2. Total volume data were taken from the RPW reports in the library references filed with the Commission's ACDs.¹¹ Revenue and cost data taken were taken from the financial summary reports from the same library references.¹²

¹¹ Docket No. ACR2007, Library Reference PRC-ACR2007-LR1, March 27, 2008, Excel file "07 Summary DM_LR1.xls," tab "PRESS," cell B33 (showing FY 2007 total volume); Docket No. ACR2008, Library Reference PRC-ACR2008-LR-1, March 30, 2009, Excel file "08 Public RPW_LR1.xls," tab "RPW Report," cell I115 (showing FY 2008 total volume); Docket No. ACR2009, Library Reference PRC-ACR2009-LR-1, March 29, 2010, Excel file "09 Public RPW_LR1.xls," tab "PRC PRW," cell G234 (showing FY 2009 total volume); Docket No. ACR2010, Library Reference PRC-ACR2010-LR-1, March 29, 2011, Excel file "10 Public RPW_LR1.xls," tab "PRC RPW," cell G252 (showing FY 2010 total volume); Docket No. ACR2011, Library Reference PRC-ACR2011-LR-1, March 28, 2012, Excel file "11 Public RPW_LR1.xls," tab "PRC RPW," cell G252 (showing FY 2011 total volume); Docket No. ACR2012, Library Reference PRC-ACR2012-LR-1, March 28, 2013, Excel file "12 Public RPW_LR1.xlsx," tab "PRC RPW," cell G248 (showing FY 2012 total volume); Docket No. ACR2014, Library Reference PRC-LR-ACR2014/1, March 27, 2015, Excel file "14 Public RPW.xlsx," tab "PRC RPW," cell I250 (FY 2014 RPW) (showing FY 2013 total volume); FY 2014 RPW, cell H250 (showing FY 2014 Market Dominant volume); Docket No. ACR2015, Library Reference PRC-LR-ACR2015/1, March 28, 2016, Excel file "15 Public RPW.xlsx," tab "PRC RPW," cell H254 (showing FY 2015 total volume); Docket No. ACR2016, Library Reference PRC-LR-ACR2016/1, March 28, 2017, Excel file "16 Public RPW.xlsx," tab "FY 2016 Public," cell L240 (showing FY 2016 total volume); Docket No. ACR2017, Library Reference PRC-LR-ACR2017-1, March 29, 2018, Excel file "17 Public RPW.xlsx," tab "FY 2017 Public," cell L240 (showing FY 2017 total volume); Docket No. ACR2018, Library Reference PRC-LR-ACR2018-1, April 12, 2019, Excel file "18 Public RPW.xlsx," tab "FY 2018 Public," cell L236 (showing FY 2018 total volume); Docket No. ACR2019, Library Reference PRC-LR-ACR2019-1, March 25, 2020, Excel file "19 Public RPW.xlsx," tab "FY 2019 Public," cell L233 (showing FY 2019 total volume).

¹² Docket No. ACR2007, Library Reference PRC-ACR2007-LR1, March 27, 2008, Excel file "07 Summary DM_LR1.xls," tab "PRESS," cells D70, F75 (showing FY 2007 total revenue and total cost); Docket No. ACR2008, Library Reference PRC-ACR2008-LR-1, March 30, 2009, Excel file "08 Summary_LR1.xls," tab "Financial_Results," cells B14, B16 (showing FY 2008 total revenue and total cost); Docket No. ACR2009, Library Reference PRC-ACR2009-LR-1, March 29, 2010, Excel file "09 Summary_LR1.xls," tab "Financial_Results," cells B14, B16 (showing FY 2009 total revenue and total cost); Docket No. ACR2010, Library Reference PRC-ACR2010-LR-1, March 29, 2011, Excel file "10 Summary_LR1.xls," tab "Financial_Results," cells B14, B16 (showing FY 2010 total revenue and total cost); Docket No. ACR2011, Library Reference PRC-ACR2011-LR-1, March 28, 2012, Excel file "11 Summary_LR1.xls," tab "Financial_Results," cells B14, B16 (showing FY 2011 total revenue and total cost); Docket No. ACR2012, Library Reference PRC-ACR2012-LR-1, March 28, 2013, Excel file "12 Summary_LR1.xlsx," tab "Financial_Results," cells B14, B16 (showing FY 2012 total revenue and total cost); Docket No. ACR2014, Library Reference PRC-LR-ACR2014/1, March 27, 2015, Excel file "14 Summary_LR1.xlsx," tab "Financial_Results," cells C14, C16 (FY 2014 Financial Summary) (showing FY 2012 total revenue and total cost); FY 2014 Financial Summary, cells B14, B16 (showing FY 2014 total revenue and total cost); Docket No. ACR2015, Library Reference PRC-LR-ACR2015/1, March 28, 2016, Excel file "15 Summary_LR1 2.xlsx," tab "PRC RPW," cells B14, B16 (showing FY 2015 total revenue and total cost); Docket No. ACR2016, Library Reference PRC-LR-ACR2016/1, March 28, 2017, Excel file "16 Summary_LR1.xlsx," tab "PRC RPW," cells B14, B16 (showing FY 2016 total revenue and total cost); Docket No. ACR2017, Library Reference PRC-LR-ACR2017-1, March 29, 2018, Excel file "17 Summary_LR1.xlsx," tab "PRC RPW," cells B14, B16 (showing FY 2017 total revenue and total cost);

Table A-1. Volume data were taken from the Postal Service's RPW reports.¹³

Cost data were taken from the Postal Service's Cost and Revenue Analysis reports.¹⁴

Delivery point data were taken from the Postal Service's TFP reports.¹⁵

Docket No. ACR2018, Library Reference PRC-LR-ACR2018-1, April 12, 2019, Excel file "18 Summary_LR1.xlsx," tab "PRC RPW," cells B14, B16 (showing FY 2018 total revenue and total cost); Docket No. ACR2019, Library Reference PRC-LR-ACR2019-1, March 25, 2020, Excel file "FY 19 Summary_LR1.xlsx," tab "Total All Mails (Appendix A)," cells C77, D78 (showing FY 2019 total revenue and total cost).

¹³ See Docket No. ACR2011, Library Reference USPS-FY11-42, December 29, 2011, Excel file "Fy2011_RPWsummaryreport_public.xls," tab "FY 2011 Public," cells L78, L193 (showing Market Dominant and total pieces for FY 2011); Docket No. ACR2012, Library Reference USPS-FY12-42, December 28, 2012, Excel file "Fy2012_RPWsummaryreport_public.xls," tab "Fiscal Year 2012 Public," cells L77, L236 (showing Market Dominant and total pieces for FY 2012); Docket No. ACR2013, Library Reference USPS-FY13-42, December 27, 2013, Excel file "Fy2013_RPWsummaryreport_public.xls," tab "Fiscal Year 2013 Public," cells L78, L238 (showing Market Dominant and total pieces for FY 2013); Docket No. ACR2014, Library Reference USPS-FY14-42, December 29, 2014, Excel file "Fy2014_RPWsummaryreport_public.xls," tab "Fiscal Year 2014 Public," cells L78, L238 (showing Market Dominant and total pieces for FY 2014); Docket No. ACR2015, Library Reference USPS-FY15-42, December 29, 2015, Excel file "Fy2015_RPWsummaryreport_public.xls," tab "FY 2015 Public," cells L78, L238 (showing Market Dominant and total pieces for FY 2015); Docket No. ACR2016, Library Reference USPS-FY16-42, December 29, 2016, Excel file "Fy2016_RPWsummaryreport_public.xls," tab "FY 2016 Public," cells L78, L240 (showing Market Dominant and total pieces for FY 2016); Docket No. ACR2017, Library Reference USPS-FY17-42, December 29, 2017, Excel file "FY2017_RPWsummaryreport_public_eoy.xls," tab "FY 2017 Public," cells L78, L240 (showing Market Dominant and total pieces for FY 2017); Docket No. ACR2018, Library Reference USPS-FY18-42, December 28, 2018, Excel file "FY2018_RPWsummaryreport_public_eoy.xlsx," tab "FY 2018 Public," cells L74, L236 (showing Market Dominant and total pieces for FY 2018).

¹⁴ Docket No. ACR2012, Library Reference USPS-FY12-1, December 28, 2012, Excel file "FY12PublicCRA.xlsx," tab "Cost3," cells F36:F37 (showing institutional and total cost for FY 2012); Docket No. ACR2013, Library Reference USPS-FY13-1, December 27, 2013, Excel file "FY13PublicCRA.xls," tab "Cost3," cells F35:F36 (showing institutional and total cost for FY 2013); Docket No. ACR2014, Library Reference USPS-FY14-1, December 29, 2014, Excel file "Public_FY14CRA.xls," tab "Cost3," cells F34:F35 (showing institutional and total cost for FY 2014); Docket No. ACR2015, Library Reference USPS-FY15-1, December 29, 2015, Excel file "Public-FY15CRA.xls," tab "Cost3," cells F34:F35 (showing institutional and total cost for FY 2015); Docket No. ACR2016, Library Reference USPS-FY16-1, December 29, 2016, Excel file "Public_FY16CRARReport.xls," tab "Cost3," cells F34:F35 (showing institutional and total cost for FY 2016); Docket No. ACR2017, Library Reference USPS-FY17-1, December 29, 2017, Excel file "Public_FY17CRARReport.xlsx," tab "Cost3," cells F34:F35 (showing institutional and total cost for FY 2017); Docket No. ACR2018, Library Reference USPS-FY18-1, December 28, 2018, Excel file "Public_FY18CRARReport.xlsx," tab "Cost3," cells F34:F35 (showing institutional and total cost for FY 2018).

¹⁵ United States Postal Service, USPS Annual Tables, FY 2018 TFP (Total Factor Productivity), July 16, 2019, Excel file "Table Annual 2018 - 2018 CRA Public.xlsx," tab "Out-46," cells K59:69 (showing delivery points for FYs 2013-2018).

II. RETIREMENT-BASED RATE AUTHORITY

The Postal Service is responsible for funding retirement benefits for its employees. OPM computes the annual payment for these obligations (RHB, FEHB, and CSRS). The Commission, through the new rate authority is providing additional price cap authority each year for 5 years (phase-in period). Below is a hypothetical example of how the Commission would calculate the retirement rate authority available during each year during the phase-in period.

A. Hypothetical Example

For illustration purposes, the Commission reprints the example presented in Order No. 5337 as Tables IV-5, IV-6, and IV-7. Order No. 5337 at 99-102. This example shows the amount of retirement-based rate authority that would be available to the Postal Service using the hypothetical data in the tables below. Because the retirement-based rate authority adjusts annually during the phase-in period to changes in both volume and the amount of the amortization payments, the example below is meant to be illustrative, and is not a forecast.

**Table A-2
Hypothetical Input Data**

FY	Statutorily Mandated Amortization Payment (Millions)	Total Revenue (Millions)	Market Dominant Revenue (Millions)	Quarterly MD Volume (Millions)			
				Q1	Q2	Q3	Q4
2020	\$3,100	\$70,800	\$46,000	36,095	31,800	31,000	32,000
2021	\$3,000	\$71,400	\$46,389	31,095	31,800	30,000	30,000
2022	\$3,200	\$72,000	\$46,778	29,800	29,000	29,700	29,000
2023	\$3,500	\$73,000	\$47,427	28,800	29,000	28,700	28,000
2024	\$3,400	\$73,900	\$48,011	28,100	28,000	28,800	28,300
2025	\$3,200	\$74,000	\$48,075	28,300	27,900	28,600	28,300

Table A-3
Hypothetical Retirement Rate Authority Formula Outputs,
Using Data from Table A-2

FY	Compounded Retirement Rate Authority Through Previous FY	Additional Retirement Rate Authority	Date Retirement Rate Authority Authorized	Date of Rate Increase
2021	0.000%	0.861%	January 31, 2021	September 2, 2021
2022	0.853%	0.827%	January 31, 2022	September 15, 2022
2023	1.666%	0.918%	January 31, 2023	September 5, 2023
2024	2.560%	1.111%	January 31, 2024	September 3, 2024
2025	3.631%	0.970%	January 31, 2025	September 6, 2025

Table A-4
Hypothetical Required Minimum Remittances,
Using Data from Tables IV-5 and IV-6

FY	% of MD Revenue in Previous FY Resulting from Retirement Rate Authority	Required Minimum Remittance (Millions)	To Be Remitted By
2022	0.066%	\$31	September 30, 2022
2023	0.889%	\$416	September 30, 2023
2024	1.729%	\$820	September 30, 2024
2025	2.643%	\$1,269	September 30, 2025
2026	3.695%	\$1,776	September 30, 2026

Table A-2 shows the full range of input data required by the proposed formula. Table A-3 shows for each year of the phase-in period, the compounded amount of prior retirement rate authority, the amount of rate authority newly authorized, and the dates that authority was authorized¹⁶ and implemented in a rate increase. Table A-4 shows the percentage of Market Dominant revenue resulting from the retirement rate authority,

¹⁶ The date that the authority was authorized is provided for illustration purposes only, and is not used as an input to or output from the retirement formula.

the required minimum remittance for each fiscal year, and the date by which it is required to be remitted towards the amortization payment.¹⁷ Note that the required minimum remittance for each fiscal year is equal to the amount of additional revenue collected during the previous fiscal year as a result of the prorated, compounded rate increase resulting from the use of retirement rate authority.

The example shows how the proposed formulas use each year's volume and required payment throughout the phase-in period to get closer to the target of generating sufficient additional revenue (if accompanied by an equal rate increase on competitive products) to make the full amortization payment. In the example, the phase-in period lasts from FY 2021 to FY 2025. For illustration purposes, consider the final calculation of retirement rate authority in FY 2025. Under Formula V-1, the first step is to divide the total amortization payment for FY 2024 by the total revenue for that year (FY 2024 data will be the most recent available at the time of the FY 2025 calculation). From Table A-2, those values are \$3.4 billion and \$73.9 billion, respectively. Dividing these two figures shows that, had no previous retirement rate authority been authorized, total revenue would need to increase by 4.600 percent to be able to make the full amortization payment. Because retirement rate authority was granted in 4 previous years, the second step is to subtract the compounded amount of that increase, calculated with Formula V-2, and shown in Table A-3. For FY 2025, that amount is 3.631 percent. Because FY 2025 is the last year of the phase-in period, the 0.970-percentage point difference between 4.600 percent and 3.631 percent does not need to be further amortized, and thus 0.970 percent is the amount of retirement rate authority for FY 2025, as shown in Table A-3.

To calculate the required minimum remittance for FY 2025, Formulas V-3 and V-4 calculate the percentage of Market Dominant revenue collected in FY 2024 as a result

¹⁷ The amount of the required minimum remittance and the due date are requirements that the Postal Service must meet to continue to receive retirement rate adjustment authority. These required minimum remittances and due dates do not affect the Postal Service's statutory obligations to make the full amortization payment as determined by the Office of Personnel Management.

of previously authorized retirement rate authority. As shown in Table A-4 (on the line corresponding the year of calculation, FY 2025), that amount is 2.643 percent. This is lower than the 3.631 percent compounded rate authority figure used in the previous paragraph because the 1.111-percent retirement rate authority authorized in FY 2024 was not used until the last month of FY 2024 (as shown in Table A-3), and thus generated very little additional revenue in FY 2024. Multiplying 2.643 percent by the FY 2024 Market Dominant revenue of \$48.011 billion (shown in Table A-2) produces a minimum required remittance for FY 2025 of \$1.269 billion, as shown in Table A-4.

B. Data Table Sources

Section V.C.1. of the Order contains one table: Table V-1. This table compiles data from the PAEA period, with each year's data taken from separate sources. These sources are detailed below. Tables A-2, A-3, and A-4 show hypothetical figures created for illustrative purposes.

Table V-1. Data for FY 2006 and 2007 was taken from the Postal Service's Annual Reports.¹⁸ Data for FY 2008 and beyond was taken from the Postal Service's 10-K reports.¹⁹

¹⁸ United States Postal Service, 2006 Annual Report, March 23, 2007, at 43; United States Postal Service, 2007 Annual Report, February 11, 2008, at 39, 46.

¹⁹ United States Postal Service, 2008 Report on Form 10-K [Erratum], December 10, 2008, at 19, 47; United States Postal Service, 2009 Report on Form 10-K, November 16, 2009, at 20, 49; United States Postal Service, 2010 Report on Form 10-K, November 15, 2010, at 22, 55; United States Postal Service, 2011 Report on Form 10-K [Erratum], November 16, 2011, at 21, 63; United States Postal Service, 2012 Report on Form 10-K, November 15, 2012, at 41, 78; United States Postal Service, 2013 Report on Form 10-K, January 31, 2014, at 37, 75; United States Postal Service, 2014 Report on Form 10-K, December 5, 2014, at 26, 42; United States Postal Service, 2015 Report on Form 10-K, November 13, 2015, at 37, 55; United States Postal Service, 2016 Report on Form 10-K, November 15, 2016, at 37, 58; United States Postal Service, 2017 Report on Form 10-K, November 14, 2017, at 45, 55; United States Postal Service, 2018 Report on Form 10-K, November 14, 2018, at 53, 64; FY 2019 Form 10-K at 51, 63.

APPENDIX B
LIST OF COMMENTERS AND COMMENTS

Commenter	Citation	Citation Short Form
A.B. Data, Ltd. (A.B. Data)	Comments of A.B. Data, Ltd., January 31, 2020	A.B. Data Comments
Air Force Association (AFA), AMVETS (American Veterans), Association of the Military Surgeons of the United States (AMSUS), Association of the United States Navy (AUSN), Chief Warrant Officers Association of the U.S. Coast Guard (CWOA), Commissioned Officers Association of the U.S. Public Health Service (COA), Enlisted Association of the National Guard of the United States (EANGUS), Fleet Reserve Association (FRA), Jewish War Veterans of the United States of America (JWV), Marine Corps League (MCL), Marine Corps Reserve Association (MCRA), Military Officers Association of America (MOAA), National Military Family Association (NMFA), Non-Commissioned Officers Association (NCOA), Service Women's Action Network (SWAN), The Enlisted Association (TREA), U.S. Coast Guard Chief Petty Officers Association (USCGPOA), Veterans of Foreign Wars (VFW), VetsFirst, United Spinal Association (VetsFirst), Vietnam Veterans of America (VVA), and Wounded Warrior Project (WWP) (collectively, AFA <i>et al.</i>)	Comments of Military and Veteran Service Organizations, February 5, 2020	AFA <i>et al.</i> Comments

Commenter	Citation	Citation Short Form
Alliance of Nonprofit Mailers, Association for Postal Commerce, MPA—the Association of Magazine Media, American Catalog Mailers Association, Direct Marketing Association of Washington, Nonprofit Alliance, Envelope Manufacturers Association, Saturation Mailers Coalition, and Continuity Shippers Association (collectively, ANM <i>et al.</i>)	Comments of the Alliance of Nonprofit Mailers, the Association for Postal Commerce, MPA - the Association of Magazine Media, the American Catalog Mailers Association, the Direct Marketing Association of Washington, the Nonprofit Alliance, the Envelope Manufacturers Association, the Saturation Mailers Coalition, and the Continuity Shippers Association, February 3, 2020	ANM <i>et al.</i> Comments
	Reply Comments of the Alliance of Nonprofit Mailers, the Association for Postal Commerce, MPA - the Association of Magazine Media, the American Catalog Mailers Association, the Direct Marketing Association of Washington, the Nonprofit Alliance, the Envelope Manufacturers Association, the Saturation Mailers Coalition, and the Continuity Shippers Association, March 4, 2020	ANM <i>et al.</i> Reply Comments
Alzheimer's Association	Comments of Alzheimer's Association, February 3, 2020	Alzheimer's Association Comments
American Bankers Association (ABA)	Comments of American Bankers Association, February 3, 2020	ABA Comments
	Reply Comments of American Bankers Association, March 4, 2020	ABA Reply Comments
American Catalog Mailers Association (ACMA)	Initial Comments of the American Catalog Mailers Association (ACMA), February 3, 2020	ACMA Comments
	Reply Comments of the American Catalog Mailers Association (ACMA), March 4, 2020	ACMA Reply Comments
American Consumer Institute Center for Citizen Research (ACI)	Comments of American Consumer Institute Center for Citizen Research Regarding Docket No. RM2017-3 Submitted to the United States Postal Regulatory Commission, January 31, 2020	ACI Comments
American Farmland Trust (AFT)	Comments of American Farmland Trust, February 5, 2020	AFT Comments

Commenter	Citation	Citation Short Form
American Forest & Paper Association (AF&PA)	Comments of the American Forest & Paper Association, January 31, 2020	AF&PA Comments
American Jewish Joint Distribution Committee, Inc. (JDC)	Comments of the American Jewish Joint Distribution Committee, Inc., February 4, 2020	JDC Comments
American Kidney Fund (AKF)	Comments of the American Kidney Fund, February 5, 2020	AKF Comments
American Leprosy Missions (ALM)	Comments of American Leprosy Missions, January 31, 2020	ALM Comments
American Lung Association (ALA)	Comments of the American Lung Association, February 5, 2020	ALA Comments
American Postal Workers Union, AFL-CIO (APWU)	Comments of the American Postal Workers Union, AFL-CIO on the Revised Notice of Proposed Rulemaking for the System for Regulating Rates and Classes for Market Dominant Products, February 4, 2020 ¹	APWU Comments
American Red Cross (Red Cross)	Comments of the American Red Cross, February 3, 2020	Red Cross Comments
American Rivers	Comments of American Rivers, February 10, 2020	American Rivers Comments
Americans United for Separation of Church and State (AU)	Comments of Americans United for Separation of Church and State, February 5, 2020	AU Comments
ANA Nonprofit Federation (ANA)	Comments of ANA Nonprofit Federation, February 3, 2020	ANA Comments
Appalachian Mountain Club (AMC)	Comments of Appalachian Mountain Club, February 3, 2020	AMC Comments

¹ On February 4, 2020, APWU filed a motion for late acceptance of its comments. Motion for Late Acceptance of Comments of the American Postal Workers Union, AFL-CIO on the Revised Notice of Proposed Rulemaking for the System for Regulating Rates and Classes for Market Dominant Products, February 4, 2020. The motion is granted.

Commenter	Citation	Citation Short Form
Arizona Food Bank Network (AZ Food Bank)	Comments of Arizona Food Bank Network, February 5, 2020	AZ Food Bank Comments
Arkansas Electric Cooperatives Inc. (AECI)	Comments of Arkansas Electric Cooperatives Inc., February 4, 2020	AECI Comments
Arthritis Foundation	Comments of Arthritis Foundation, January 28, 2020	Arthritis Foundation Comments
Association of Fundraising Professionals (AFP)	Comments of Association of Fundraising Professionals, February 3, 2020	AFP Comments
Association of Our Lady of Mount Carmel (Our Lady of Mount Carmel)	Comments of the Association of Our Lady of Mount Carmel, February 3, 2020	Our Lady of Mount Carmel Comments
Atlanta Humane Society (AHS)	Comments of Atlanta Humane Society, February 3, 2020	AHS Comments
Baylor College of Medicine (Baylor)	Comments of Baylor College of Medicine, February 13, 2020	Baylor Comments
Berkshire Company (Berkshire Co.)	Comments of the Berkshire Company in Response to Order No. 5337, February 3, 2020	Berkshire Co. Comments
Boys & Girls Club of Greater Nashua (Boys & Girls Club)	Comments of the Boys & Girls Club of Greater Nashua, January 27, 2020	Boys & Girls Club Comments
CARE USA (CARE)	Reply Comments of CARE USA, March 10, 2020	CARE Reply Comments
Catholic Charities of St. Paul and Minneapolis (Catholic Charities)	Comments of Catholic Charities of St. Paul and Minneapolis, February 3, 2020	Catholic Charities Comments
Catholic Relief Services (CRS)	Comments of Catholic Relief Services, February 5, 2020	CRS Comments
Chesapeake Bay Foundation (CBF)	Comments of the Chesapeake Bay Foundation, January 28, 2020	CBF Comments

Commenter	Citation	Citation Short Form
Child Bridge	Comments of Child Bridge, February 4, 2020	Child Bridge Comments
Chimp Haven	Comments of Chimp Haven, February 4, 2020	Chimp Haven Comments
Christian Appalachian Project (CAP)	Comments of Christian Appalachian Project, February 5, 2020	CAP Comments
Coalition for a 21 st Century Postal Service (C21)	Reply Comments of the Coalition for a 21 st Century Postal Service, March 4, 2020	C21 Reply Comments
Commemorative Air Force (CAF)	Comments of the Commemorative Air Force, February 5, 2020	CAF Comments
Compassion International	Comments of Compassion International, February 5, 2020	Compassion International Comments
Council for Advancement and Support of Education (CASE)	Comments of Council for Advancement and Support of Education, February 3, 2020	CASE Comments
Crossroads Rhode Island (Crossroads)	Comments of Crossroads Rhode Island, February 5, 2020	Crossroads Comments
Defenders of Wildlife (DOW)	Comments of Defenders of Wildlife, February 4, 2020	DOW Comments
Disabled American Veterans (DAV)	Comments of Disabled American Veterans, February 13, 2020	DAV Comments
Discover Financial Services (Discover)	Comments of Discover Financial Services on Revised Notice of Proposed Rulemaking, February 3, 2020	Discover Comments
DM Pros, Inc. (DM Pros)	Comments of DM Pros, Inc., February 4, 2020	DM Pros Comments
DOROT	Comments of DOROT, February 4, 2020	DOROT Comments
eBay, Inc. (eBay)	Comments of eBay, Inc., February 3, 2020	eBay Comments

Commenter	Citation	Citation Short Form
Electric Cooperatives of South Carolina (ECSC)	Comments of Electric Cooperatives of South Carolina, January 29, 2020	ECSC Comments
Epsilon	Comments of Epsilon, February 3, 2020	Epsilon Comments
Feed the Children	Comments of Feed the Children, January 22, 2020	Feed the Children Comments
Feeding America	Comments of Feeding America, January 29, 2020	Feeding America Comments
Feeding South Dakota	Comments of Feeding South Dakota, January 31, 2020	Feeding South Dakota Comments
Feeding Wisconsin	Comments of Feeding Wisconsin, February 3, 2020	Feeding Wisconsin Comments
FeedMore WNY (FeedMore)	Comments of FeedMore WNY, February 4, 2020	FeedMore Comments
FINCA International, Inc. (FINCA)	Comments of FINCA International, Inc., February 5, 2020	FINCA Comments
Food & Friends	Comments of Food & Friends, February 3, 2020	Food & Friends Comments
Food Bank for Larimer County, CO (Larimer County Food Bank)	Comments of the Food Bank for Larimer County, CO, January 31, 2020	Larimer County Food Bank Comments
Food Bank of Northeast Arkansas (NE Arkansas Food Bank)	Comments of the Food Bank of Northeast Arkansas, January 31, 2020	NE Arkansas Food Bank Comments
Food Finders Food Bank, Inc. (Food Finders)	Comments of Food Finders Food Bank, Inc., January 28, 2020	Food Finders Comments
Foodbank of Santa Barbara County, CA (Santa Barbara County Foodbank)	Comments of the Foodbank of Santa Barbara County, CA, February 4, 2020	Santa Barbara County Foodbank Comments

Commenter	Citation	Citation Short Form
Foodbank of Southeastern Virginia and the Eastern Shore (SE Virginia Foodbank)	Comments of the Foodbank of Southeastern Virginia and the Eastern Shore, February 3, 2020	SE Virginia Foodbank Comments
Franciscan Friars of the Atonement (Franciscan Friars)	Comments of Franciscan Friars of the Atonement, February 3, 2020	Franciscan Friars Comments
Franciscan Mission Associates (Franciscan Mission)	Comments of Franciscan Mission Associates, January 29, 2020	Franciscan Mission Comments
Gleaners Community Food Bank (Gleaners)	Comments of Gleaners Community Food Bank, February 5, 2020	Gleaners Comments
Golden State Power Cooperative (GSPC)	Comments of Golden State Power Cooperative, January 31, 2020	GSPC Comments
Greeting Card Association (GCA)	Initial Comments of the Greeting Card Association in Response to Order No. 5337, February 3, 2020	GCA Comments
	Reply Comments of the Greeting Card Association, March 4, 2020	GCA Reply Comments
Harvest Hope Food Bank (Harvest Hope)	Comments of Harvest Hope Food Bank (Wendy Broderick, CEO), February 3, 2020	February 3 Harvest Hope Comments
	Comments of Harvest Hope Food Bank (Lenore K. Zedosky, BOD), February 5, 2020	February 5 Harvest Hope Comments
Hawkeye Area Community Action Program, Inc. (HACAP)	Comments of the Hawkeye Area Community Action Program, Inc., February 3, 2020	HACAP Comments
House of Ruth	Comments of the House of Ruth, January 27, 2020	House of Ruth Comments
Human Rights Campaign (HRC)	Comments of the Human Rights Campaign, January 28, 2020	HRC Comments
Idaho Foodbank	Comments of the Idaho Foodbank, January 29, 2020	Idaho Foodbank Comments
Independent Sector	Comments of Independent Sector, February 3, 2020	Independent Sector

Commenter	Citation	Citation Short Form
InnerWorkings	Comments of InnerWorkings, January 30, 2020	InnerWorkings Comments
League of the Miraculous Infant Jesus of Prague (LMIJP)	Comments of the League of the Miraculous Infant Jesus of Prague, February 7, 2020	LMIJP Comments
Logan Eddy	Comments of Logan Eddy, January 29, 2020	Eddy Comments
Lubbock Meals on Wheels, Inc. (Lubbock Meals on Wheels)	Comments of Lubbock Meals on Wheels, Inc., January 23, 2020	Lubbock Meals on Wheels Comments
Mailers Hub LLC (Mailers Hub)	Comments of Mailers Hub LLC, February 3, 2020	Mailers Hub Comments
MANNA FoodBank (MANNA)	Comments of MANNA FoodBank, February 4, 2020	MANNA Comments
March of Dimes	Comments of March of Dimes, February 4, 2020	March of Dimes Comments
Marine Corps Heritage Foundation (MCHF)	Comments of the Marine Corps Heritage Foundation, January 27, 2020	MCHF Comments
Marist Brothers	Comments of the Marist Brothers, January 27, 2020	Marist Brothers Comments
Maryland Food Bank	Comments of the Maryland Food Bank, February 3, 2020	Maryland Food Bank Comments
Meals on Wheels of Mercer County (MOWMC)	Comments of Meals on Wheels of Mercer County, NJ, January 30, 2020	MOWMC Comments
Meals on Wheels of Metro Tulsa, Inc. (MOWMT)	Comments on Meals on Wheels of Metro Tulsa, OK, Inc., January 27, 2020	MOWMT Comments
Mercy Home for Boys & Girls (Mercy Home)	Comments of Mercy Home for Boys & Girls, January 28, 2020	Mercy Home Comments

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Meredith Corporation	Comments of Meredith Corporation, February 3, 2020	Meredith Corporation Comments
Michigan Electric Cooperative Association (MECA)	Comments of the Michigan Electric Cooperative Association, January 31, 2020	MECA Comments
MINDset Direct	Comments of MINDset Direct, January 22, 2020	MINDset Direct Comments
Miriam Magnuson	Comments of Miriam Magnuson, January 30, 2020	Magnuson Comments
Missionary Oblates of Mary Immaculate (MOMI)	Comments of Missionary Oblates of Mary Immaculate (Bill Undertajlo, DOF), January 31, 2020	Undertajlo MOMI Comments
	Comments of Missionary Oblates of Mary Immaculate (Patty Herges Schanz, Group Leader), January 31, 2020	Schanz MOMI Comments
Mono Lake Committee (MLC)	Comments of the Mono Lake Committee, February 3, 2020	MLC Comments
Mount Pisgah Academy	Comments of Mount Pisgah Academy, January 27, 2020	Mount Pisgah Academy Comments
National Association of Letter Carriers, AFL-CIO (NALC)	Comment of the National Association of Letter Carriers, AFL-CIO, January 30, 2020	NALC Comments
National Association of Postal Supervisors (NAPS)	Comments of the National Association of Postal Supervisors (NAPS), January 31, 2020	NAPS Comments
National Committee to Preserve Social Security & Medicare (NCPSSM)	Comments of the National Committee to Preserve Social Security and Medicare, February 3, 2020	NCPSSM Comments
National Museum of Women in the Arts (NMWA)	Comments of the National Museum of Women in the Arts, February 3, 2020	NMWA Comments

Commenter	Citation	Citation Short Form
National Newspaper Association (NNA)	Comments of the National Newspaper Association, January 31, 2020	NNA Comments
National Newspaper Association, Continuity Mailers Association, American Catalog Mailers Association, Envelope Manufacturers Association, Greeting Card Association, Mailers Hub LLC, Saturation Mailers Coalition, Small Business Legislative Council, Inc., Pacific Northwest Association of Want Ad Papers, Mid-Atlantic Free Papers Association, Independent Free Papers of America, Community Papers of Michigan, Community Papers of New England, New York Press Association, Free Community Papers of New York, Midwest Free Community Paper Association, Association of Free Community Papers, Florida Media Association, Southwestern Advertising Publishers Association, and Wisconsin Community Papers (collectively, NNA <i>et al.</i>)	Explanation of Options for a Financially Stable Postal System, February 3, 2020	NNA <i>et al.</i> Comments
National Parks Conservation Association (NPCA)	Comments of National Parks Conservation Association, February 3, 2020	NPCA Comments
National Postal Mail Handlers Union (NPMHU)	Comments of the National Postal Mail Handlers Union on Revised Notice of Proposed Rulemaking, February 4, 2020	NPMHU Comments
National Postal Policy Council, Major Mailers Association, National Association of Presort Mailers, and Association for	Comments of the National Postal Policy Council, the Major Mailers Association, the National Association of Presort Mailers, and the Association for Mail Electronic Enhancement, February 3, 2020	NPPC <i>et al.</i> Comments

Commenter	Citation	Citation Short Form
Mail Electronic Enhancement (collectively, NPPC <i>et al.</i>)	Reply Comments of the National Postal Policy Council, the Major Mailers Association, the National Association of Presort Mailers, and the Association for Mail Electronic Enhancement, March 4, 2020	NPPC <i>et al.</i> Reply Comments
National Rural Electric Cooperative Association (NRECA)	Comments of the National Rural Electric Cooperative Association, February 3, 2020	NRECA Comments
National Taxpayers Union (NTU)	Comments of National Taxpayers Union, February 3, 2020	NTU Comments
National Trust for Historic Preservation (NTHP)	Comments of the National Trust for Historic Preservation, February 3, 2020	NTHP Comments
New England Journal of Medicine (NEJM)	Comments of the New England Journal of Medicine, February 6, 2020	NEJM Comments
New Israel Fund (NIF)	Comments of the New Israel Fund, February 10, 2020	NIF Comments
News Media Alliance (NMA)	Comments of the News Media Alliance, January 31, 2020	NMA Comments
No Kid Hungry (NKH)	Comments of No Kid Hungry, February 10, 2020	NKH Comments
North Carolina Association of Electric Cooperatives (NCAEC)	Comments of the North Carolina Association of Electric Cooperatives, February 3, 2020	NCAEC Comments
North Shore Animal League America (NSALA)	Comments of North Shore Animal League America, February 3, 2020	NSALA Comments
Northern Westchester Hospital (NWH)	Comments of Northern Westchester Hospital, January 28, 2020	NWH Comments
Northwest Arkansas Food Bank	Comments of the Northwest Arkansas Food Bank, February 5, 2020	Northwest Arkansas Food Bank Comments

Commenter	Citation	Citation Short Form
Nutrition & Services for Seniors (NSFS)	Comments of Nutrition & Services for Seniors, January 27, 2020	NSFS Comments
Oblate Missionary Society, Inc. (OMSI)	Comments of Oblate Missionary Society, Inc. (David Uribe, Executive Director), February 3, 2020	Uribe OMSI Comments
	Comments of Oblate Missionary Society, Inc. (Ken Amerson, Associate Executive Director), February 3, 2020	Amerson OMSI Comments
Oblate Missions	Comments of Oblate Missions, February 3, 2020	Oblate Missions Comments
Ohio's Electric Cooperatives (OEC)	Comments of Ohio's Electric Cooperatives, January 27, 2020	OEC Comments
Operation Smile	Comments of Operation Smile (Dr. Bill Magee, Jr., DDS, MD, Co-Founder and CEO), January 28, 2020	Dr. Magee Operation Smile Comments
	Comments of Operation Smile (Katie Downtain Ward, Director, Direct Marketing and Fundraising), January 27, 2020	Ward Operation Smile Comments
	Comments of Operation Smile (Kendra Davenport, CDO), January 28, 2020	Davenport Operation Smile Comments
	Comments of Operation Smile (Libby Czerlinsky, Director, Donor Services), January 28, 2020	Czerlinsky Operation Smile Comments
Osborne Coinage Co. (Osborne Coinage)	Reply Comments of the Osborne Coinage Co., March 4, 2020	Osborne Coinage Reply Comments
Parcel Shippers Association (PSA)	Comments of the Parcel Shippers Association Pursuant to Commission Order No. 5337, February 3, 2020	PSA Comments

Commenter	Citation	Citation Short Form
	Corrected Comments of the Parcel Shippers Association Pursuant to Commission Order No. 5337, February 5, 2020 ²	PSA Revised Comments
Parkinson's Foundation	Comments of the Parkinson's Foundation, February 10, 2020	Parkinson's Foundation Comments
Passionist Missionaries	Comments of the Passionist Missionaries, February 3, 2020	Passionist Missionaries Comments
Peter Roehrich	Comments of Peter Roehrich, January 6, 2020	Roehrich Comments
Physicians Committee for Responsible Medicine (PCRM)	Comments of Physicians Committee for Responsible Medicine, January 31, 2020	PCRM Comments
Pitney Bowes Inc. (Pitney Bowes)	Comments of Pitney Bowes Inc., February 3, 2020	Pitney Bowes Comments
	Reply Comments of Pitney Bowes Inc., March 4, 2020	Pitney Bowes Reply Comments
Port Discovery Children's Museum (PDCM)	Comments of Port Discovery Children's Museum, February 4, 2020	PDCM Comments
Presbyterian Church (U.S.A.), A Corporation (Presbyterian Church)	Comments of Presbyterian Church (U.S.A.), A Corporation, February 3, 2020	Presbyterian Church Comments
Production Management Group, Ltd. (PMG)	Comments of the Production Management Group, Ltd., February 3, 2020	PMG Comments
Public Representative	Comments of the Public Representative on Revised Notice of Proposed Rulemaking, February 3, 2020	PR Comments

² On February 5, 2020, PSA filed a motion for leave to file revised comments correcting a formatting issue on page 9 of the PSA Comments. Parcel Shippers Association Motion for Leave to File Corrected Comments, February 5, 2020. The motion is granted.

Commenter	Citation	Citation Short Form
	Reply Comments of the Public Representative Regarding Revised Notice of Proposed Rulemaking, March 4, 2020	PR Reply Comments
Pursuant	Comments of Pursuant, February 6, 2020	Pursuant Comments
REACH Institute	Comments of the REACH Institute, February 3, 2020	REACH Institute Comments
Reasons to Believe (RTB)	Comments of Reasons to Believe, February 4, 2020	RTB Comments
Redlands Christian Migrant Association (RCMA)	Comments of Redlands Christian Migrant Association, February 4, 2020	RCMA Comments
Regional Food Bank of Oklahoma (Oklahoma Food Bank)	Comments of the Regional Food Bank of Oklahoma, February 3, 2020	Oklahoma Food Bank Comments
Rhode Island Community Food Bank (Rhode Island Food Bank)	Comments of the Rhode Island Community Food Bank, January 31, 2020	Rhode Island Food Bank Comments
Sacred Heart Southern Missions (Sacred Heart)	Comments of Sacred Heart Southern Missions, January 27, 2020	Sacred Heart Comments
Saint Andrew's Abbey (Saint Andrew's)	Comments of Saint Andrew's Abbey, January 27, 2020	Saint Andrew's Comments
Second Harvest Food Bank of Santa Cruz County, CA (Second Harvest Santa Cruz)	Comments of Second Harvest Food Bank of Santa Cruz County, CA, February 3, 2020	Second Harvest Santa Cruz Comments
Second Harvest Foodbank of Southern Wisconsin (Second Harvest Southern Wisconsin)	Comments of Second Harvest Foodbank of Southern Wisconsin, February 3, 2020	Second Harvest Southern Wisconsin Comments
Second Harvest Northern Lakes Food Bank (Second Harvest Northern Lakes)	Comments of Second Harvest Northern Lakes Food Bank, January 31, 2020	Second Harvest Northern Lakes Comments

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Sierra Club	Comments of Sierra Club, February 3, 2020	Sierra Club Comments
Sisters of St. Francis of Assisi (Sisters of St. Francis)	Comments of Sisters of St. Francis of Assisi, February 3, 2020	Sisters of St. Francis Comments
Small Business & Entrepreneurship Council (SBE Council)	Comments of the Small Business & Entrepreneurship Council, February 3, 2020	SBE Council Comments
Society of the Divine Savior Salvatorians (SDSS)	Comments of the Society of the Divine Savior Salvatorians, February 3, 2020	SDSS Comments
Society of the Little Flower (SLF)	Comments of Society of the Little Flower, February 3, 2020	SLF Comments
Southeast Missouri Food Bank	Comments of Southeast Missouri Food Bank, February 3, 2020	Southeast Missouri Food Bank Comments
Southeast Ohio Foodbank	Comments of Southeast Ohio Foodbank, February 3, 2020	Southeast Ohio Foodbank Comments
Special Olympics	Comments of Special Olympics, February 3, 2020	Special Olympics Comments
St. Francis House	Comments of St. Francis House, February 3, 2020	St. Francis House Comments
TennGreen Land Conservancy (TennGreen)	Comments of TennGreen Land Conservancy, February 3, 2020	TennGreen Comments
TheaterWorks Hartford (TheaterWorks)	Comments of TheaterWorks Hartford, January 28, 2020	TheaterWorks Comments
TREA: The Enlisted Association (TREA)	Comments of TREA: The Enlisted Association, January 31, 2020	TREA Comments
Trinity Missions	Comments of Trinity Missions, January 27, 2020	Trinity Missions Comments

Commenter	Citation	Citation Short Form
Trinity Services, Inc. (Trinity Services)	Comments of Trinity Services, Inc., February 3, 2020	Trinity Services Comments
UNICEF USA (UNICEF)	Comments of UNICEF USA, February 3, 2020	UNICEF Comments
United Spinal Association (United Spinal)	Comments of United Spinal Association, February 3, 2020	United Spinal Comments
United States Postal Service (Postal Service)	Initial Comments of the United States Postal Service in Response to Order No. 5337, February 3, 2020	Postal Service Comments
	Reply Comments of the United States Postal Service in Response to Order No. 5337, March 4, 2020	Postal Service Reply Comments
Virginia, Maryland and Delaware Association of Electric Cooperatives (VMDAEC)	Comments of the Virginia, Maryland and Delaware Association of Electric Cooperatives, January 24, 2020	VMDAEC Comments
Visiting Nurse Service of New York (VNSNY)	Comments of the Visiting Nurse Service of New York, February 3, 2020	VNSNY Comments
Volunteers of America Colorado Branch (VOA)	Comments of Volunteers of America Colorado Branch, January 27, 2020	VOA Comments
Washington National Cathedral (WNC)	Comments of Washington National Cathedral, February 6, 2020	WNC Comments
We Raise Foundation (WRF)	Comments of We Raise Foundation, February 3, 2020	WRF Comments
White Coat Waste Project (WCWP)	Comments of White Coat Waste Project, February 3, 2020	WCWP Comments
Wounded Warrior Project (WWP)	Comments of Wounded Warrior Project, January 31, 2020	WWP Comments