

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

Before Commissioners:

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

Retail Ground and Parcel Select Ground
Service Standard Changes, 2022

Docket No. N2022-1

ADVISORY OPINION ON THE SERVICE STANDARD CHANGES
ASSOCIATED WITH RETAIL GROUND AND PARCEL SELECT GROUND



Washington, DC 20268-0001
June 9, 2022

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I. EXECUTIVE SUMMARY

The Postal Service requests an advisory opinion on its proposal to revise the service standards for Retail Ground (RG) and Parcel Select Ground (PSG).¹ Specifically, the Postal Service proposes to upgrade the service standards for RG and PSG from the current 2- to 8-day standard to a 2- to 5-day standard. Request at 2.

In general, decisions regarding the Postal Service's Competitive products—products that have private competitors in the marketplace—are left to the reasonable business judgment of the Governors of the Postal Service. RG and PSG are Competitive products, and the Postal Accountability and Enhancement Act (PAEA)²

¹ United States Postal Service's Request for an Advisory Opinion on Changes in the Nature of Postal Services, March 21, 2022 (Request).

² Pub. L. 109-435, 120 Stat. 3198 (2006).

limited the Commission's oversight role for these types of products.³ Unlike Market Dominant products, the Postal Service's Competitive product prices are not subject to the Consumer Price Index-based price cap and market competition is expected to serve as the primary guarantor of discipline with respect to price and service quality. However, 39 U.S.C. § 3661(b) requires the Postal Service to request an Advisory Opinion from the Commission prior to implementing a change in the nature of postal services that will generally affect service on a nationwide or substantially nationwide basis.⁴ The Commission's Advisory Opinion is nonbinding, and the Commission does not have the authority to enforce its advice regarding the Postal Service's proposed changes to service standards.

The Commission has analyzed the estimated impact of the current proposal on the Postal Service's operational flow, transportation network, financial condition, and the market for competitive parcels. The Commission took into account filings by the Postal Service and the Public Representative, the only parties to participate in this docket.⁵ The Commission's advisory opinion is guided by and comports with the policies of Title 39. This Advisory Opinion includes several key findings.

First, the Commission finds that there are immediate benefits from reducing the number of times RG and PSG pieces are handled during processing. However, the Commission is concerned that this proposal may result in an increased need for manual processing and staff availability for facilities already failing to meet operating plans. This could lead to disruptions in processing and transportation operations and cost increases.

³ This is discussed in more detail below in Section VI.A.

⁴ 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).

⁵ The Commission invited interested persons to formally participate in the proceeding via intervention and informally participate via filing a statement of position. The Postal Service and the Public Representative were the only parties that participated in this proceeding.

Second, the Commission finds that the projected transportation efficiencies—reduced reliance on air transportation and a more efficient surface transportation network—are not evident in the near term. The Postal Service expects them to materialize over time, provided the proposed changes capture some of the demand for shipping of medium-speed, low-price, large packages via ground transportation.⁶ The Postal Service is unable to predict when these efficiencies might materialize. The Commission notes that the calculated transportation cost changes are based on numerous assumptions, several of which might be unrealistic.

Third, the Commission finds that the planned changes have the potential for meeting market demand and enhancing service to customers sending larger packages. However, the Commission identifies several areas of concern relating to the market research conducted by the Postal Service and used to support its assertions. Specifically, the Commission notes the lack of research targeted to current customers of the products at issue.

Based on these findings, the Commission provides the following recommendations to the Postal Service for consideration before implementing its plan. The Postal Service should:

- Design a timeline, which includes all intended incremental changes to the processing network operations and how each would contribute to the eventual, more efficient, shape-based processing network envisioned in its 10-year plan
- Design a plan to monitor all implications of each such incremental network change, in order to learn from previous changes and fine-tune subsequent changes
- Conduct more robust research into the market segment that the upgraded RG and PSG service standards would attract, to gain a better idea of this unknown profile in order to ensure that continued provision of low prices for potentially high-cost shipping of new volumes does not negatively impact contribution for RG and PSG products

⁶ RG and PSG provide delivery services for parcels up to 130 inches in combined length and girth, weighing up to 70 pounds. See Mail Classification Schedule (MCS) §§ 2135.2 and 2115.2.

- Design and implement a plan to monitor the impact on shipping options in the competitive parcels market, especially the impact on mailers who actually use RG and PSG, mailers who are particularly price-sensitive, and large-sized business mailers
- Design and implement a plan to monitor any volume diversion from Priority Mail and the impact on other Postal Service products

II. PROCEDURAL HISTORY

A. Pre-Filing Issues

On March 23, 2021, the Postal Service published a 10-year strategic plan announcing potential changes intended to achieve financial stability and service excellence.⁷ In furtherance of this plan, on March 4, 2022, the Postal Service filed a notice of its intent to conduct a pre-filing conference regarding its proposed changes to the service standards for RG and PSG.⁸

On March 8, 2022, the Commission issued Order No. 6115, which established Docket No. N2022-1 to consider the Postal Service's proposed changes, notified the public concerning the Postal Service's pre-filing conference, and appointed a Public Representative.⁹ Due to the COVID-19 pandemic, the Postal Service held its pre-filing conference virtually on March 15, 2022.¹⁰

⁷ See United States Postal Service, *Delivering for America: Our Vision and Ten-Year Plan to Achieve Financial Sustainability and Service Excellence*, March 23, 2021, at 3, available at https://about.usps.com/what/strategic-plans/delivering-for-america/assets/USPS_Delivering-For-America.pdf (Postal Service Strategic Plan). Further information related to the Postal Service's Strategic Plan is available at <https://about.usps.com/what/strategic-plans/delivering-for-america/>.

⁸ Notice of Pre-Filing Conference, March 4, 2022, at 1.

⁹ Notice and Order Concerning the Postal Service's Pre-Filing Conference, March 8, 2022 (Order No. 6115).

¹⁰ See Request at 8; Notice and Order on the Postal Service's Request for an Advisory Opinion on Changes in the Nature of Postal Services, March 23, 2022, at 2 (Order No. 6124).

B. The Postal Service Request

On March 21, 2022, the Postal Service filed its request for an advisory opinion from the Commission regarding planned changes to the service standards for RG and PSG. See Request. The intended effective date of the planned changes is no earlier than 90 days after the filing of the Request. *Id.* at 5. The Postal Service certifies that it has made a good faith effort to address the concerns of interested persons about the Postal Service's proposal raised at the pre-filing conference. *Id.* at 8.

In support of its Request, the Postal Service provided the direct testimony of three witnesses: Steven E. Jarboe (USPS-T-1), Kevin P. Bray (USPS-T-2), and A. Thomas Bozzo (USPS-T-3).¹¹ The Postal Service identified a fourth individual, Sharon Owens, to serve as its institutional witness and provide information relevant to the Postal Service's proposal that is not provided by other Postal Service witnesses. Request at 10. Additionally, the Postal Service filed five library references, one of which is available to the public and four of which are designated as non-public material.¹²

Witness Jarboe discusses the current trends in the subject market for RG and PSG, the customer base, and how the proposed service standard changes may impact the market and customers. See USPS-T-1.

Witness Bray discusses the overall impact of the proposed changes on the Postal Service's operational flow and transportation methods. See USPS-T-2.

Witness Bozzo discusses the estimated change in cost due to the proposed changes and the methodology used to estimate the cost impact. See USPS-T-3.

¹¹ Direct Testimony of Steven E. Jarboe on Behalf of the United States Postal Service, March 21, 2022 (USPS-T-1); Direct Testimony of Kevin P. Bray on Behalf of the United States Postal Service, March 21, 2022 (USPS-T-2); Direct Testimony of A. Thomas Bozzo on Behalf of the United States Postal Service, March 21, 2022 (USPS-T-3).

¹² Library Reference USPS-LR-N2022-1/1, March 21, 2022 (revised April 15, 2022); Library Reference USPS-LR-N2022-1/NP1, March 21, 2022; Library Reference USPS-LR-N2022-1/NP2, March 21, 2022; Library Reference USPS-LR-N2022-1/NP3, March 21, 2022; Library Reference USPS-LR-N2022-1/NP4, March 21, 2022.

C. Commission Action and Evidentiary Record

On March 23, 2022, the Commission issued Order No. 6124, which set forth a procedural schedule and designated Chairman Michael Kubayanda as Presiding Officer.¹³ Due to lack of questions from the public and a later stipulation between the Postal Service and the Public Representative, there were several revisions to the schedule, including cancelling the technical conference, removing the dates for the hearing, modifying the deadline to file designated materials, and shortening the time to file reply briefs.¹⁴

On April 15, 2022, the Postal Service filed a notice of revisions to certain pages of the supporting testimony filed on behalf of two of its witnesses.¹⁵ The Postal Service states that these revisions involve replacing a figure to more accurately conform with the text in the testimony and updating the overall net cost impact of the planned changes due to a revision to an input cost number relating to air transportation. See Notice of Revisions to Testimony at 1-2. The Postal Service also filed a notice revising supporting Library References USPS-LR-N2022-1/1 and USPS-LR-N2022-1/NP3.¹⁶

No party intervened in this proceeding. Five Presiding Officer's Information Requests (POIRs), containing more than 40 questions, many of which included multiple subparts, were issued to further develop the record.¹⁷ The Postal Service provided

¹³ Order No. 6124; see Notice of Errata, March 23, 2022 (correcting the Technical Conference date listed in the procedural schedule in Order No. 6124, Attachment at 1, from March 30, 2022 to March 31, 2022).

¹⁴ Order Cancelling Technical Conference, March 29, 2022 (Order No. 6129); Presiding Officer's Ruling on Motion and Adjusting Procedural Schedule, April 19, 2022; see Consent Motion of the United States Postal Service to Accelerate the Procedural Schedule, April 19, 2022.

¹⁵ Notice of Revisions, April 15, 2022, PDF file "Notice of Revisions.pdf" (Notice of Revisions to Testimony).

¹⁶ Notice of Revisions, PDF file "Notice of Filing Revised LRs.pdf" (Notice of Revised Library References).

¹⁷ Presiding Officer's Information Request No. 1 and Notice of Filing Under Seal, April 1, 2022; Presiding Officer's Information Request No. 2, April 6, 2022; Presiding Officer's Information Request No. 3 and Notice of Filing Under Seal, April 8, 2022; Presiding Officer's Information Request No. 4 and Notice of Filing Under Seal, April 15, 2022 (POIR No. 4); Presiding Officer's Information Request No. 5 and Notice of Filing Under Seal, April 19, 2022.

responses to each POIR.¹⁸ In accordance with Order No. 6124, the Postal Service filed a consent motion to admit into evidence the direct testimonies and related library references of Postal Service witnesses Jarboe, Bray, and Bozzo.¹⁹ In addition, the Public Representative filed notices designating certain POIRs as the written cross-examination of the Public Representative to be included in the evidentiary record.²⁰ The Presiding Officer granted the Consent Motion and designated additional materials and material officially noticed in this proceeding.²¹

The Public Representative filed a statement of position, and the Postal Service filed initial and reply briefs.²²

The evidentiary record in this docket closed on April 26, 2022. See POR No. N2022-1/2.

¹⁸ Responses of the United States Postal Service to Questions 1-10 of Presiding Officer's Information Request No. 1, April 8, 2022 (Response to POIR No. 1); Responses of the United States Postal Service to Questions 1-7 of Presiding Officer's Information Request No. 2, April 13, 2022 (Response to POIR No. 2); Responses of the United States Postal Service to Questions 1-18 of Presiding Officer's Information Request No. 3, April 15, 2022 (April 15 Response to POIR No. 3); Response of the United States Postal Service to Question 19 of Presiding Officer's Information Request No. 3, April 20, 2022 (April 20 Response to POIR No. 3); Responses of the United States Postal Service to Questions 1-6 of Presiding Officer's Information Request No. 4, April 22, 2022 (Response to POIR No. 4); Responses of the United States Postal Service to Questions 1-6 of Presiding Officer's Information Request No. 5, April 25, 2022 (Response to POIR No. 5). On April 21, 2022, the Postal Service filed a notice of revisions to certain responses to POIR No. 4 in non-public Library Reference USPS-LR-N2022-1/NP10. See Notice of the United States Postal Service of Filing of Revised Library Reference USPS-LR-N2022-1/NP10 -- Errata, April 21, 2022 (Revised Library Reference USPS-LR-N2022-1/NP10).

¹⁹ Consent Motion of the United States Postal Service to Admit into Evidence the Direct Testimonies and Related Library References of Postal Service Witnesses Jarboe, Bray, and Bozzo, April 19, 2022 (Consent Motion).

²⁰ Public Representative Notice of Designations, April 26, 2022; Public Representative Notice of Supplemental Designations, April 26, 2022.

²¹ Presiding Officer's Ruling Granting Motion to Admit Evidence, Designating Additional Materials in the Evidentiary Record, and Closing the Record, April 26, 2022 (POR No. N2022-1/2).

²² Statement of Position of the Public Representative, May 11, 2022 (PR Statement of Position); Initial Brief of the United States Postal Service, May 11, 2022 (Postal Service Brief); Reply Brief of the United States Postal Service, May 13, 2022 (Postal Service Reply Brief).

III. COMMISSION LEGAL AUTHORITY

The Postal Service is required to request an advisory opinion from the Commission for proposed changes in the nature of postal services on a nationwide or substantially nationwide basis. See 39 U.S.C. § 3661(b). The Commission's rules require the Postal Service to file its request "not less than 90 days before the proposed effective date of the change in the nature of postal services involved." 39 C.F.R. § 3020.112.

Users of the mail are afforded a hearing on the record before the Commission's review is complete. 39 U.S.C. § 3661(c). The Commission's advisory opinion, based on evidence developed during hearings in accordance with 5 U.S.C. §§ 556 and 557, considers whether the Postal Service's planned changes conform, in terms of its objectives and effects, to the policies of section 3661 and the remainder of Title 39. "The opinion shall be in writing and shall include a certification by each Commissioner agreeing with the opinion that in [their] judgment the opinion conforms to the policies established under [Title 39]." *Id.* The advisory opinion process is intended to better inform the Postal Service in its decision-making process, provide an opportunity for the public to question and challenge Postal Service assumptions, provide transparency into the decision-making and policy-development process the Postal Service undertook, and provide a different perspective for the Postal Service's consideration.²³

²³ See Docket No. N2014-1, Advisory Opinion on Service Changes Associated with Standard Mail Load Leveling, March 26, 2014, at 7.

IV. SUMMARY OF POSTAL SERVICE PROPOSAL

A. Postal Service Request

“RG is an economical ground shipping solution for retail (single-piece) customers for packages, thick envelopes, and tubes weighing less than 70 pounds and up to 130 inches combined length and girth that are not required to be sent as [First-Class Mail (FCM)].” Request at 2. “RG service is available at Post Offices and other postal retail facilities,” and “[p]ricing depends on package weight, size, and the distance to be shipped.” *Id.* PSG is similar to RG in that it is limited by weight and overall size and priced by weight, size, and the distance to be shipped, but it is targeted at commercial shippers. *Id.* In addition, unlike RG, it allows for initial entry into the mail flow both at Post Offices and at originating downstream processing and distribution centers (P&DCs). *Id.*

Currently, for end-to-end package service within the contiguous United States, RG and PSG have a service standard ranging from 2 to 8 days. *Id.* at 3. The Postal Service plans to upgrade that service standard to correspond with the 2- to 5-day service standard for First-Class Package Service (FCPS) considered by the Commission in Docket No. N2021-2. *Id.* at 2, 3. The Postal Service asserts that the proposed change would simplify the operational scheme for processing and transporting RG and PSG package volume within the contiguous United States by combining it with FCPS volume. *Id.* at 3. Table IV-1 below compares the current to the new service standards.

**Table IV-1
Comparison of Current Standards with Proposed Standards**

Service Standard	Current Rules (Contiguous U.S.)	Planned Rules (Contiguous U.S.)
2-day	If Origin and Destination processing and distribution center (PDC) are the same facility, then Service Standard is 2 days	Intra-sectional center facility (SCF) and Origin to Destination pairs where total transit time is up to 8 hrs* (~372 miles) from Origin to Destination area distribution center (ADC) to Destination SCF
3-day	If Origin and Destination PDC are not the same facility, then the package is routed through a network distribution center (NDC) and an auxiliary service facility (ASF), if needed If Origin and Destination NDC are the same, and there is no ASF required, then Service Standard is 3 days	Where the total transit time is greater than 8 hrs and up to 32 hrs* (~1,488 miles) from Origin PDC to Destination ADC to Destination SCF
4-day	If Origin and Destination NDC are the same, and there is an ASF required, then Service Standard is 4 days	Where the total transit time is greater than 32 hrs and up to 50 hrs* (~2,325 miles) from Origin PDC to Destination ADC to Destination SCF
5-day	If Origin and Destination NDC are not the same, determine the travel days between NDC facilities If an ASF is not required, and the travel time between NDC facilities is 1 day or less, then the Service Standard is 5 days	Where the total transit time is greater than 50-hrs from Origin PDC to Destination ADC to Destination SCF
6-8-day	If Origin and Destination NDC are not the same, determine the travel days between NDC facilities within Service Standard Directory If ASF is not required, then the Service Standard = travel time of 2 or more days + 4 If ASF is required, then the Service Standard = travel time of 2 or more days + 5	N/A

Source: Request at 3-4.

The Postal Service asserts that the proposed service standards “are predicated on the planned change to the FCPS service standards and the concomitant improvement and optimization of the Postal Service’s package processing and surface transportation network and depends on consolidation with FCPS domestic surface volumes.” *Id.* at 4.

However, the Postal Service notes that certain packages are not included in the planned service standards, including RG and PSG packages sent to or from domestic locations outside the contiguous United States, packages containing hazardous materials, and live animals shipped by RG. *Id.* at 4-5. For RG and PSG packages outside the contiguous United States, the Postal Service asserts that volume “would have to be carried by air to meet the planned service standard, which cannot be done cost effectively.” *Id.* at 4. It states that it is considering whether this proposal would enable it to “adjust the service standards for any piece originating or destinating outside the contiguous United States that traverses the contiguous United States during some portion of the piece’s journey.” *Id.* at 5. For RG and PSG packages containing hazardous materials or live animals, it asserts that some RG and PSG packages may be routed by air transport where it is more cost-effective to do so and certain hazardous materials (HAZMAT) or live animals may not be suitable for this mode of transport. *Id.*

The Postal Service states that its fundamental rationale for the proposed changes is to enhance service to customers sending larger packages. *Id.* at 6. It asserts that by consolidating RG and PSG volume with FCPS volume, it can offer faster service for packages that exceed the weight and size limitations of FCPS. *Id.* The Postal Service submits that the proposed changes will result in further improvement and rationalization of its portfolio of package products. *Id.* It submits that customers will benefit from the provision of a low-cost, medium-speed shipping service for packages in excess of one pound. *Id.* at 6-7. It also notes that the market for faster, economical ground shipping products has seen significant growth recently and is expected to continue to grow. *Id.* at 8.

Additionally, the Postal Service contends that shifting RG and PSG volume to follow FCPS volume would enable the further optimization of its package processing

and surface transportation networks in three ways. *Id.* at 11-12. First, it asserts that the added volume would fill existing unused capacity, maximizing surface transportation utility and value. *Id.* at 12. Second, the Postal Service states that, by eliminating the current interim processing stops, it can reduce the overall processing burden while improving speed and reliability by reducing touch points. *Id.* Third, it asserts that by combining multiple sorts, the proposed change would improve volume and capacity in surface lanes. *Id.*

The Postal Service asserts that the proposed changes will continue to achieve the broader policies of Title 39, United States Code. *See id.* at 7-8. The Postal Service discusses how the proposed changes would continue to satisfy the universal service provisions appearing in 39 U.S.C. §§ 101, 403, and 3661(a) under the proposed service standards. *See id.* The Postal Service also asserts that the proposed changes would not impair compliance with the policies of 39 U.S.C. § 3633, which govern the financial performance of Competitive products. *See id.* at 8. The Postal Service further asserts that the proposed changes will not cause any undue or unreasonable discrimination against any users of the mail. *See id.*

The Postal Service states that the proposed service standard changes would not be implemented any sooner than 90 days after the filing of its Request. *Id.* at 5.

B. Witness Steven E. Jarboe Testimony

Witness Steven E. Jarboe serves as the Director of Shipping and Commerce Strategy at the Postal Service, where his office develops, implements, and deploys new shipping strategies and solutions. USPS-T-1 at i. His testimony discusses the current trends in the subject market, the customer base, and how the proposed service standard changes may impact the market and customers. *Id.* at 1.

Witness Jarboe states that the planned service standard change for FCPS that was the subject of Docket No. N2021-2 provided the Postal Service with an opportunity to address the unmet market demand for a medium-speed, low-cost shipping alternative. *Id.* at 2. He states that the Postal Service engaged the Boston Consulting Group (BCG) and the Colography Group (CG) to evaluate the market for shipping

packages. *Id.* at 6. He testifies that CG concluded that the market for ground shipping service was large and growing. *Id.* Specifically, he asserts that the analysis disclosed an unmet market need for an economically priced, medium-speed ground shipping product. *Id.* at 5-6. Furthermore, he explains that the demand for ground shipping service is likely to increase because more commercial shippers are relocating inventories closer to urban centers. *Id.* at 6-7. He states that it is the Postal Service's experience that ground shipping customers tend to be more price conscious. *Id.* at 7.

Witness Jarboe states that BCG conducted interviews with shipping industry leaders, logistic experts, and mid-market shippers. *Id.* BCG also conducted an online survey of commercial e-commerce business shipping decision-makers to understand how they prioritize shipping services and features and assess their price sensitivity to changes in time in transit. Witness Jarboe testifies that the interviews and survey generated responses that demonstrated existing demand for increased package delivery speed. *Id.*

He states that historically, Priority Mail (PM) has been the Postal Service's only product option for price/time in transit for weight-rated products, and it is considered a medium-speed, medium-price product. *Id.* at 8. He further states that FCPS provides a medium-speed, low-price shipping option for lightweight packages. *Id.* However, he asserts that the Postal Service does not have a similar product for large packages in the medium-speed, low-price market sector. *Id.*

He explains that prior to January 2022, RG and PSG were priced similarly to PM, despite offering lower speeds. *Id.* He testifies that in January 2022, the Postal Service reduced prices for RG and PSG to improve the desirability of these products within the low-speed, low-priced market sector for large packages. *Id.* at 9. However, he states that the current service standard for RG and PSG (at 2- to 8-days) does not align with and is considerably slower than the service expectation for comparable products of private-sector competitors. *Id.*

By aligning RG and PSG processing and transportation with FCPS, witness Jarboe states that the Postal Service believes it can serve this market demand without

appreciably increasing costs. *Id.* at 9-10. He asserts that “having a 2- to 5-day product for both light and heavier packages will better align the Postal Service’s product portfolio to the package shipping market and enable the Postal Service to better compete with its private-sector competitors.” *Id.* at 10.

In describing the impact on other products, witness Jarboe states that combining the processing and transportation of RG and PSG with FCPS may lead to some changes in the carriers that the Postal Service uses, but the impact on FCPS costs is minimal. *Id.* He also states that because the enhanced RG-PSG product is priced below PM, which presently serves the medium-speed, medium-price market segment, an enhanced RG-PSG product may result in some diversion of PM volumes. *Id.* at 10-11. However, he explains that PM remains a faster shipping option in some lanes and has other benefits (such as flat rate pricing, included insurance, and container options) that will differentiate it from RG and PSG. *Id.* at 11.

Finally, witness Jarboe concludes his testimony with a discussion of how the planned changes are consistent with the policies and requirements of Title 39. *Id.* at 11-12.

C. Witness Kevin P. Bray Testimony

Witness Kevin P. Bray serves as the Executive Manager of the Mail Processing Infrastructure and Optimization group at the Postal Service, which develops and supports mail processing systems and applications that enable effective and efficient processing of mail through the postal network. USPS-T-2 at i. He also manages the Area Mail Processing team that provides implementation for all facility consolidations. *Id.* His testimony discusses the nature of the changes in service standards for RG and PSG, the new operational methodology that makes the service standard changes possible, and the impact on the number of 3-digit Origin to Destination processing facility pairs (OD pairs) that would be subject to a change in service standards. *Id.* at 1.

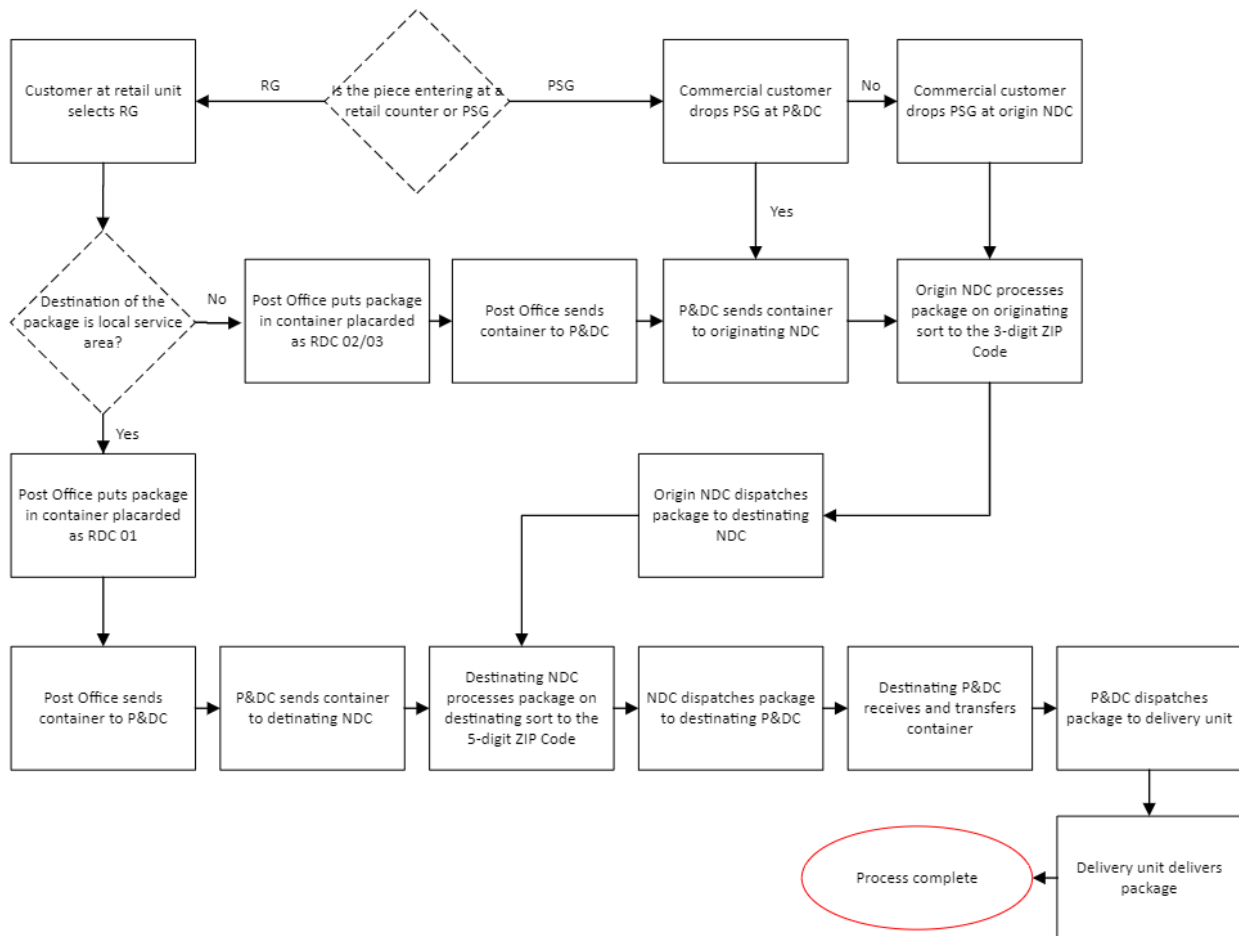
Witness Bray begins by providing an overview of the current-state trajectory of RG parcels within the contiguous United States between origin and destination points, listing six processing nodes through which RG parcels travel.²⁴ He explains that in the current state, RG parcels enter the postal network at Post Offices, where they are placed in bins according to their destination points. *Id.* at 2. RG parcels travelling to local area destination points are placed in bins that are routed to tier 1 network distribution centers (NDCs), while parcels travelling to destinations outside that of the local NDC are placed in bins that are routed to tier 2 NDCs. *Id.* From Post Offices, RG bins travel to P&DCs, where they are grouped and then conveyed to geographically appropriate NDCs. *Id.* at 2-3.

At NDCs, RG parcels are sorted based on their destination ZIP Codes—parcels destined to local destination points are sorted based on their 5-digit destination ZIP Codes, while parcels destined to points outside the local area are sorted based on their 3-digit destination ZIP Codes. *Id.* at 3. Next, NDCs convey sorted RG parcels to appropriate processing facilities—parcels with destination points within the local area, and sorted to 5-digit destination ZIP Codes, are routed to geographically appropriate P&DCs, while parcels with destination points outside the local area, and sorted to 3-digit destination ZIP Codes, are routed to geographically appropriate destination NDCs for further processing. *Id.* Destination NDCs sort RG parcels received from origin NDCs based on their 5-digit destination ZIP Codes, and route them to geographically appropriate P&DCs. *Id.* Destination P&DCs combine RG parcels with other mail destined for the same 5-digit ZIP Codes and route these shipments to appropriate destination delivery units (DDUs), from where all mail is delivered to destination addresses. *Id.* at 4.

²⁴ *Id.* at 2-4. Throughout his testimony, witness Bray refers to the individual processing nodes as “touches.”

Witness Bray explains that the current-state trajectory for PSG is identical to that of RG with the exception that PSG, a commercial product utilized by medium- and large-sized shippers, can enter the Postal Service’s mailstream at P&DCs or NDCs, in addition to Post Offices. *Id.* at 4-5. From their points of entry, PSG parcels follow the same paths as those described for RG. *Id.* at 5. A graphic representation of the current-state operational flow for RG and PSG is depicted in Figure IV-1 below.

**Figure IV-1
Current-State Operational Flow for RG and PSG**



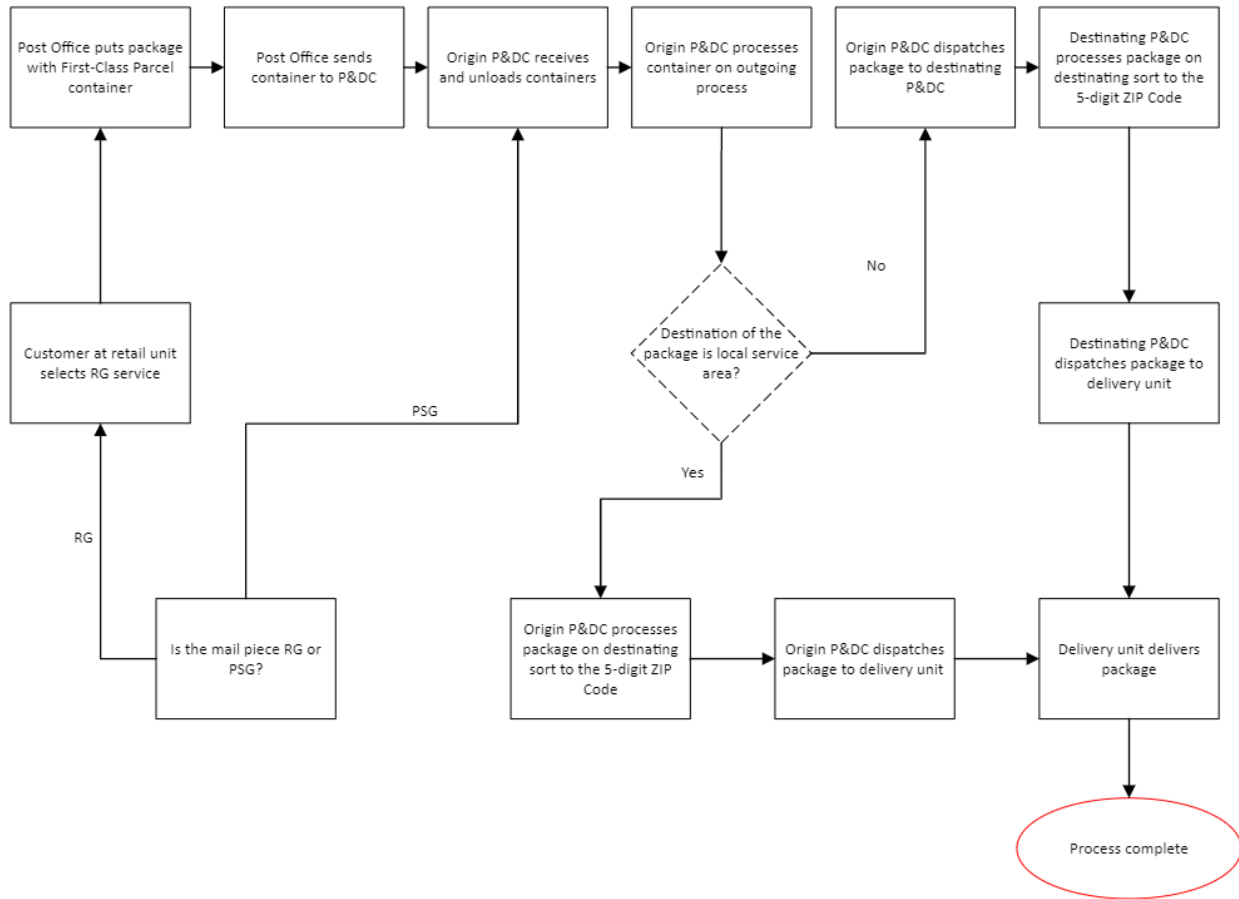
Source: USPS-T-2 at 5.

Witness Bray continues with the description of the future-state operational flow for RG and PSG within the contiguous United States, under which RG and PSG parcels would be consolidated with FCPS items for processing and transportation. *Id.* at 5-9. He describes this consolidation as boasting the advantage of requiring fewer touch points. *Id.* at 6.

Witness Bray explains that RG parcels would continue to enter the Postal Service's mailstream at Post Offices in the future-state operational flow, where they would be merged with FCPS shipments. *Id.* The combined shipments would travel to P&DCs for sortation based on their destination ZIP Codes. *Id.* Shipments with local destination points would be sorted based on their 5-digit destination ZIP Codes, combined with other mail destined for the same 5-digit ZIP Codes, and routed to DDUs for final delivery. *Id.* Shipments to destination points outside the local area would be sorted based on their 3-digit destination ZIP Codes and routed to destination P&DCs for further processing. *Id.* Destination P&DCs would sort these shipments based on their 5-digit destination ZIP Codes, combine them with other mail destined for the same 5-digit ZIP Codes, and route them to DDUs for final delivery. *Id.*

As with the current-state trajectory, PSG shipments would follow the same trajectory as the combined RG and FCPS shipments in the future state, with the future-state trajectory possibly starting at a Post Office, P&DC, or NDC for PSG parcels. *Id.* at 9. Witness Bray explains that PSG shipments deposited at NDCs would be routed to P&DCs where they would be combined with FCPS shipments. *Id.* A graphic representation of the future-state operational flow for RG and PSG is depicted in Figure IV-2 below.

**Figure IV-2
Future-State Operational Flow for RG and PSG**



Source: USPS-T-2 at 10.

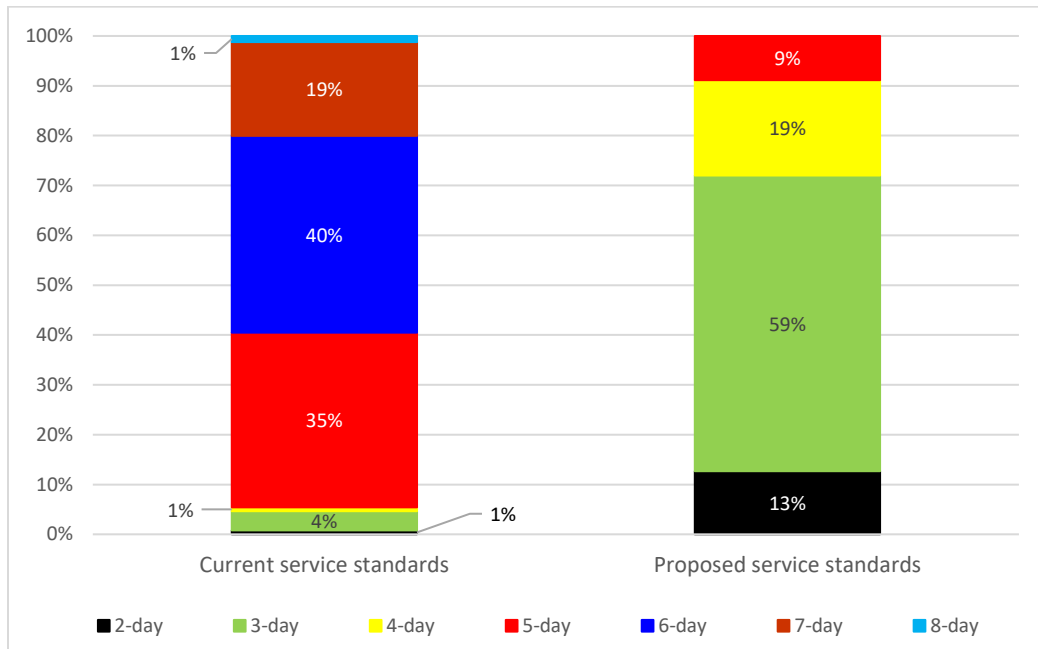
Witness Bray states that the business rules, which correspond to the currently applicable 2- to 8-day service standards for RG and PSG within the United States, are identical for the two products. *Id.* at 5. He provides that the streamlined operational flow described above would allow certain RG and PSG parcels to reach their destinations sooner and, as a result, the Postal Service plans to align service standards for RG and PSG with those for FCPS.²⁵ He confirms that such change would result in continued application of identical business rules for two parcel products when subject to the 2- to 5-day service standards. USPS-T-2 at 10.

Witness Bray states that the fundamental benefit of the upgraded service standards for certain RG and PSG parcels is the enhanced service to customers sending large parcels.²⁶ He includes a table with OD pairs within the contiguous United States that would be subject to the planned service standard changes, indicating shifts in the number of 3-digit ZIP Code pairs from the current 2- to 8-day service standards to the planned 2- to 5-day service standards, as well as a chart to illustrate the shifts in proportions of contiguous 3-digit ZIP Code pairs between the current and future state. USPS-T-2 at 11-12. The chart, replicated in Figure IV-3 below, illustrates that while in the current state, RG and PSG volumes corresponding to 40 percent of 3-digit ZIP Code pairs in the contiguous United States are subject to the 2- to 5-day service standards, in the future state, all contiguous 3-digit ZIP Code pairs with RG and PSG volumes would be subject to the enhanced 2- to 5-day service standards.

²⁵ *Id.* at 7, 10. Witness Bray refers to aligning service standards for RG and PSG with the 2- to 5-day service standards for FCPS, which were the subject of the Docket N2021-2 proceeding, and which the Postal Service implemented during the course of this proceeding on May 1, 2022. See generally Docket No. N2021-2, Advisory Opinion on the Service Standard Changes Associated with First-Class Package Service, September 29, 2021 (Docket No. N2021-2, Advisory Opinion); see also United States Postal Service *National news*, U.S. Postal Service Implements New First-Class Package Service Standards and Updates Priority Mail Service Standards, April 18, 2022, available at <https://about.usps.com/newsroom/national-releases/2022/0418-usps-implements-new-first-class-package-service-standards.htm>.

²⁶ *Id.* The Commission notes that RG and PSG include parcels of up to 70 pounds, with a maximum of 130 inches in combined length and girth. See MCS § 2135.2 for RG size and weight limitations and MCS § 2115.2 for PSG size and weight limitations.

Figure IV-3
Percent of 3-digit ZIP Code Pairs within the Contiguous United States Subject to the Currently Applicable 2- to 8-Day Service Standards and to the Planned 2- to 5-Day Service Standards



Source: USPS-T-2 at 11-12; Library Reference N2022-1/NP4, Excel file “RG-PSG Service Standards Change to FCP - Contiguous Only.xlsx.”

Witness Bray proceeds to describe the anticipated impact of the proposed changes on the transportation network. USPS-T-2 at 12-13. He anticipates that sufficient capacity is available in the surface transportation network in place for FCPS to absorb future RG and PSG shipments. *Id.* at 12. He provides that floor utilization in surface transportation for FCPS typically ranges from 42 to 48 percent. *Id.* For more recent utilization rates,²⁷ available from the “SVweb, Transportation Summary Dashboard,” witness Bray reports approximately 46 percent average floor utilization for plant-to-plant Highway Contract Route (HCR) transportation excluding surface transfer centers (STCs) and a 62 percent average utilization for STC transportation. *Id.* at 12-13. He concludes that the small volumes attributable to RG and PSG, bundled with

²⁷ These utilization rates are for the December 11, 2021 through March 7, 2022 period. *Id.*

FCPS volumes, would confer gains in efficiency by occupying underutilized space. *Id.* at 13.

Witness Bray continues with a description of certain exceptions to the planned changes and divides them into two categories: exceptions to the planned service standards changes and exceptions to the planned operational flow. *Id.* at 13-17. Regarding the first category of exceptions, witness Bray explains that current service standards would continue to apply to HAZMAT shipments, certain live animal shipments, and offshore shipments, and that these shipments would, for the time being, remain within their current transportation networks. *Id.* at 1, 13.

Witness Bray clarifies that offshore RG and PSG shipments would be excepted from the service standard upgrade at least initially since bundling RG and PSG with FCPS in these lanes would require air transportation, which could not be done cost-effectively. *Id.* at 15-16. However, he adds that the Postal Service is exploring adjusting service standards for pieces originating or destinating outside the contiguous United States for the portion of their journey traversing the contiguous United States, while continuing to utilize cargo ships to transport RG and PSG parcels between the points of departure from the contiguous United States and offshore processing facilities. *Id.* at 15.

With respect to the second category of exceptions, witness Bray explains that RG and PSG shipments that would be excepted from the planned operation flow would include parcels subject to the upgraded service standards but deviating from the operational flow due to surface transportation not being feasible within the 5-day window, or due to insufficient density to justify the cost of ground transportation. *Id.* at 1, 16.

He states that RG volume transported by air would increase from the current 14.0 percent to an estimated 28.9 percent following the service standard upgrade. *Id.* at 17. For PSG, he projects an increase in the percentage of volume transported by air from the current 15.6 percent to an estimated 15.9 percent. *Id.* However, he anticipates that the surface transportation network will grow and lead to a less frequent

recourse to air transportation, with the air transportation option eventually becoming almost entirely eclipsed by surface transportation, and a vast preponderance of RG and PSG parcels transported in the surface network. *Id.*

Witness Bray concludes that the proposed change “would improve processing times by reducing the number of touches” through which RG and PSG parcels travel during processing. *Id.* He points out that the consolidation of RG and PSG with FCPS “would also enable the further optimization of the Postal Service’s package processing and surface transportation networks and would maximize surface transportation utility and value.” *Id.* He adds that “[t]he elimination of interim processing stops would reduce the overall processing burden, and the combination of multiple sorts would improve volume and capacity in surface lanes.” *Id.* at 17-18.

D. Witness A. Thomas Bozzo Testimony

Witness A. Thomas Bozzo is Vice President with Laurits R. Christensen Associates (LRCA), an economic research and consulting firm located in Madison, Wisconsin. USPS-T-3 at i. At LRCA, his work involves theoretical, statistical, and measurement issues related to Postal Service costing, particularly for mail processing. *Id.* His testimony describes the methodology used by the Postal Service to estimate the expected mail processing and transportation cost changes resulting from the planned changes. He also presents the overall estimated change in cost. *Id.* at ii.

Witness Bozzo states that moving PSG and RG pieces to the FCPS mailstream as described in witness Bray’s testimony may reduce mail processing costs on net by reducing “touches” of PSG and RG at NDCs. *Id.* at 1. He asserts that “[s]ome high-zone PSG and RG pieces currently transported by surface modes will require FedEx Day Turn air transportation to meet the planned service standards,” and “some FCPS will shift from commercial flights to FedEx Day Turn transportation since mixed FCPS,

PSG, and RG pieces will include parcels exceeding weight limits for commercial air transportation.”²⁸

To estimate the cost impacts from the operational changes, witness Bozzo “compare[s] mail processing and transportation costs for PSG and RG based on current mailflows to estimated costs for mailflows under the planned service standards.” *Id.* at 2. He states that “[c]osts representing the current PSG mailflows are available using Commission-accepted methodology from models provided in the Postal Service’s Annual Compliance Report (ACR), folders USPS-FY21-NP15 (mail processing) and USPS-FY21-NP16 (transportation).” *Id.*

Witness Bozzo testifies that mail processing costs for the future state can be estimated by modifying the PSG models from Library Reference USPS-FY21-NP15 to reflect FCPS mailflows. *Id.* The modified models are provided in Library Reference USPS-N2022-1-NP3. *Id.* He states that “the PSG mail processing and transportation models may be adapted to estimate the change in RG mail processing costs.” *Id.* He assumes that effects on FCPS mail processing costs from adding PSG and RG to the FCPS mailflows are negligible because the combined PSG and RG volume is small relative to FCPS. *Id.* He states that “[m]ultiplying the unit cost differences by PSG and RG volumes provides the volume variable cost (VVC) impact, excluding any effects of volume changes induced by the service standard changes.” *Id.*

²⁸ *Id.* at 1-2. The Postal Service explains that surface transportation is typically less expensive than air transportation. For air transportation modes, the Postal Service describes that air cargo transportation (such as FedEx Day Turn) is more expensive than commercial air carriers. See Docket No. N2021-1, Direct Testimony of Stephen B. Hagenstein on Behalf of the United States Postal Service, April 21, 2021, at 3 (Docket No. N2021-1, USPS-T-3). See also Docket No. N2021-1, Direct Testimony of Robert Cintron on Behalf of the United States Postal Service, April 21, 2021, at 11-12, 25. In the case of the instant proposal, the Postal Service explains that the calculated savings for RG and PSG shifting from the surface network to the air cargo transportation reflect the “relatively high costs for longer-distance (high zone) surface transportation.” USPS-T-3 at 6.

For transportation cost impacts, witness Bozzo explains that these “impacts are obtained by computing transportation costs per cubic foot in the current state for FCPS, PSG, and RG pieces that would change modes under the planned standards.” *Id.* He states that “[c]urrent-state costs are commercial air costs for FCPS and surface transportation costs from [Library Reference] USPS-FY21-NP16 for PSG and RG.” *Id.* at 2-3. He states that “the future state cost per cubic foot is for FedEx Day Turn transportation.” *Id.* at 3. Like the mail processing calculations, he states that “the transportation cost impacts are derived by multiplying the cost differentials by the cubic feet of FCPS, PSG, and RG that would change transportation modes.” *Id.*

He states that, based on FY 2021 PSG volume, the estimated change in PSG mail processing cost is a reduction of \$14.9 million. *Id.* at 5. Using FY 2021 RG volume, he states that mail processing cost for RG is estimated to decline by \$17.1 million. *Id.* Thus, he estimates that the total mail processing cost impact is a reduction of \$31.9 million for both PSG and RG. *Id.*

Witness Bozzo states that transportation cost impacts arise from transportation mode shifts for portions of FCPS, PSG, and RG volumes. *Id.* He asserts that the mode shift is estimated to increase FCPS cost by \$40.4 million.²⁹ For PSG and RG, he explains that the mode shift to air transportation is expected to reduce transportation costs for high-zone PSG and RG by \$0.1 million and \$4.6 million, respectively, and the total cost change for both PSG and RG is a reduction of \$4.7 million. USPS-T-3 at 6. Thus, he states the projected net transportation cost change is an increase of \$35.7 million. *Id.*; Notice of Revisions to Testimony at 1-2, 6.

²⁹ *Id.* at 6. The transportation cost figures provided by witness Bozzo were revised by the Postal Service on April 15, 2022. See Notice of Revisions to Testimony at 1-2, 6.

V. BRIEFS

The Public Representative filed a statement of position, and the Postal Service filed initial and reply briefs.³⁰ The statement of position and briefs are summarized below.³¹

A. Public Representative

The Public Representative states that he generally supports the Postal Service's proposed changes. PR Statement of Position at 1. He explains that the proposed changes may benefit customers by providing a medium-speed, low-price ground shipping option for larger products, while also allowing the Postal Service to further optimize its processing and transportation networks. *Id.* at 14. However, he notes several areas of the plan where the impacts of the changes may not have been fully examined. *Id.* at 1, 14-20.

He first contends that the effect the operational changes necessary to increase RG and PSG speed will have on the on-time service performance of RG and PSG cannot be predicted with any certainty. *Id.* at 14. He notes that the service standard changes to FCPS, FCM, and end-to-end Periodicals have no proven record of success, and no operation or pilot testing has occurred for those products or for RG and PSG. *Id.* He states that the implementation of service standard changes without adequate testing opens the Postal Service up to potential risks. *Id.* at 15. However, even though the Public Representative states he cannot accurately predict whether the on-time service performance for RG, PSG, or FCPS will improve if this plan is implemented, he asserts that it is fair to assume that on-time service performance could improve if this plan is successfully implemented, considering that the plan intends to reduce touches of the mail and many of the current problems regarding service performance can be attributed to these multiple touches. *Id.*

³⁰ See *generally* PR Statement of Position; Postal Service Brief; Postal Service Reply Brief.

³¹ The Commission did not receive any additional statements of positions from the public.

Regarding transportation issues, the Public Representative explains that the Commission previously noted in Docket No. N2021-2 that the Postal Service's transportation network is experiencing numerous issues, such as routine delays caused by loading problems, disruptive weather events, underperforming contract trucker suppliers, and pandemic-related issues. *Id.* He asserts that the proposed changes do not solve these problems and may well exacerbate them, specifically noting that inter-sectional center facility (SCF) network costs increased 32 percent between FY 2020 and FY 2021. *Id.* at 15-16. He explains that shifting RG and PSG to the FCPS operation may help optimize productivities and combat increasing surface transportation costs and suggests that the Postal Service continue to monitor these inter-SCF network costs going forward. *Id.* at 16.

The Public Representative also notes that the Commission and Public Representatives in Docket Nos. N2021-1 and N2021-2 identified issues regarding the use of modeling and market research instead of testing and explained that the modeling and research conducted by the Postal Service have limited predictive value. *Id.* at 16-17. Although he acknowledges the difficulties and costs associated with operational and pilot testing, the Public Representative reiterates that, given the dynamic nature of mail processing and delivery, such testing can be beneficial. *Id.* at 17.

In addition, the Public Representative takes issue with the Postal Service's assertions regarding the impact on customer satisfaction. *Id.* First, he states that the Postal Service's assertion that ground shippers are price conscious may not be properly supported by quantitative or qualitative evidence. *Id.* He notes that the Postal Service relied on its Commercial Shipper Survey, which appears to be directed at all shippers and may not be representative of the actual group it purports to measure. *Id.* at 17-18. He states that although it is logical to assume that ground shippers are more concerned with price than speed because they are choosing to send items by ground rather than air, there may be other reasons customers may choose to ship via ground including reliability. *Id.* at 18. Second, the Public Representative notes that the survey conducted by BCG was limited in terms of the number and type of participants and is concerned that the survey does not sufficiently support the Postal Service's expectation regarding

RG mailers. *Id.* He states that “[n]othing in the Postal Service’s Request permits an accurate assessment as to whether RG mailers are likely to be satisfied with the service standard changes.” *Id.*

Finally, the Public Representative states that he finds no issue with the Postal Service’s financial estimates. *Id.* at 19. He notes that the methodology used to calculate the projected cost savings is sound and finds it reasonable that moving a relatively small amount of volume to the FCPS mailflow would have negligible effects on the existing processing of FCPS and other parcel products. *Id.* He also acknowledges that the proposed changes have a “relatively small impact on total mail processing and transportation costs.” *Id.* However, the Public Representative states that he cannot conclusively find that the projected cost estimate is accurate, given the Postal Service’s track record in this docket and in other similar cases involving projected finances. *Id.* He also notes that the current projected cost estimate does not appear to consider any volume diversion from PM to RG and PSG, and the Postal Service should be mindful of this possibility when projecting the cost implications of the proposed changes. *Id.* at 20.

The Public Representative concludes that he supports the Postal Service’s proposed service standard changes but suggests that the Postal Service be mindful of the limitations of its projections and conclusions. *Id.* at 21.

B. Postal Service

The Postal Service reiterates the assertions presented in the Request and revised testimonies. *See generally* Postal Service Brief; Postal Service Reply Brief. It maintains that the proposed changes are part of the evolution of the Postal Service’s Strategic Plan and further the plan’s goals of service excellence and financial sustainability. Postal Service Brief at 1.

The Postal Service contends that while the planned changes to the RG and PSG service standards build on the transportation and operation improvements described in Docket Nos. N2021-1 and N2021-2, the changes at issue in this docket involve discrete innovations. *Id.* at 2. Specifically, the proposed changes seek to enhance delivery speed, while the other changes sought to enhance reliability. *Id.* The Postal Service

again states that by consolidating RG and PSG volume with FCPS volume, it can offer faster service for packages that exceed the weight and size limitations of FCPS and address the market need for a low-price, medium-speed shipping service for packages in excess of one pound. *Id.* at 2-3. It further asserts that by making the product more attractive to potential users, the proposed changes will improve product revenue and service in furtherance of the Postal Service's financial sustainability and service excellence goals. *Id.* at 8.

The Postal Service acknowledges that an enhanced RG-PSG product may result in some diversion of PM volumes. *Id.* at 16. However, it states that the critical question is not whether volume diversion will occur but to where (and to whom) foreseeably diverted volumes will migrate. *Id.* at 17. The Postal Service explains that diversion from one Postal Service product to another, resulting in short-term loss, is a more desirable outcome than diversion to competitors, resulting in long-term loss. *Id.* The Postal Service further states that revenue diversion from PM to RG-PSG would be offset by: "(1) cost savings resulting from reduced PM air transportation cost relative to lower RG-PSG ground transportation; (2) cost savings from efficiencies and densities that will be gained by processing and transporting FCPS, RG and PSG volumes together; and (3) enhanced efficiencies and unit cost reductions that will be enjoyed from newly acquired RG-PSG volume joining the ground transportation and processing stream." *Id.* The Postal Service also asserts that the planned changes accord and conform with relevant statutory policies. *Id.* at 18-25.

In response to the Public Representative, the Postal Service states that it appreciates the Public Representative's support and his suggestions. However, it contends that its underlying investigation and decision-making process was "sufficient, robust and proportionate to the risks and rewards embodied by the planned RG-PSG service standard changes." Postal Service Reply Brief at 3.

First, the Postal Service argues that the planned changes will not exacerbate transportation issues nor degrade on-time service performance. *Id.* It states that the planned changes instead will likely result in increased reliance on air transportation, at least initially, and will not require more extensive use of surface transportation than

previously required. *Id.* at 4. It explains that the proposed changes “aim to achieve a more efficient deployment of underutilized capacity within the already-existing FCPS transportation network.” *Id.* The Postal Service also argues that the reduced touches should decrease the occasions for human and/or mechanical failure and that it is unclear what in its proposal supports the notion that service performance might worsen. *Id.*

Second, the Postal Service asserts that pilot testing would not have added value to the modeling and research already conducted in support of its proposal. *Id.* at 5. The Postal Service states that it assessed its capacity to implement the planned changes and that an analysis of operation plans strongly supports the feasibility of the proposed changes. *Id.* The Postal Service contends the cases in Docket Nos. N2021-1 and N2021-2 are not analogous to this case because these proposed changes, unlike those proposed in Docket Nos. N2021-1 and N2021-2, involve the opportunity to use a transportation network already in place. *Id.* at 5-6. The Postal Service further argues that isolating the planned changes from the broader context to conduct a pilot test would raise significant challenges while providing limited insight. *Id.* at 6. The Postal Service explains that it could have lost the opportunity to better and more quickly serve its customers if the proposal had been delayed by “tests of dubious utility.” *Id.*

Third, the Postal Service asserts that its customer survey is adequate and appropriate. *Id.* Responding to the Public Representative’s discussion on how conclusions regarding customer behavior were reached, the Postal Service states that its conclusions are correct and undisputed regarding how they were obtained. *Id.* at 6-7. It argues that the Public Representative provides no reasoning that suggests why a survey of all shippers would not also represent the views of customers who use only ground shipping products. *Id.* at 7. Furthermore, the Postal Service explains that the target population of the survey was not “all shippers.” *Id.* The Postal Service reiterates that it is speed, and not price, which is the driving issue behind the proposed changes and its analysis reflects that goal. *Id.* at 7-8. The Postal Service notes that the Public Representative acknowledges that he has no ability to predict how the proposed changes will affect on-time service performance and even accepts that on-time service

performance could improve if the plan is successfully implemented. *Id.* at 8. The Postal Service further notes that given customer responses regarding the speed and small volume of RG, the added cost and effort to conduct an additional survey directed exclusively toward retail customers cannot be justified. *Id.* at 8-9.

Finally, the Postal Service contends that its cost projections are accurate, sound, and thorough and that it has addressed the impact of volume diversion in its initial brief and its POIR responses. *Id.* at 9-10.

Based on the record, the Postal Service provides its proposed findings and conclusions. Postal Service Brief at 25-29; Postal Service Reply Brief at 10-11.

VI. COMMISSION ANALYSIS

A. Introduction

RG and PSG are Competitive products. Generally, decisions regarding the Postal Service's Competitive products are left to the reasonable business judgment of the Governors of the Postal Service. Consequently, the Commission's oversight role is far more limited. For example, the Governors of the Postal Service may establish rates and classes for all Competitive products, subject to certain price floor regulations promulgated by the Commission pursuant to 39 U.S.C. § 3633, as well as notice requirements. See 39 U.S.C. § 3632. With respect to service standards, the PAEA and federal regulations require the Postal Service to give advance notice of plans to change its service standards and to submit proposed changes for the Commission to issue an advisory opinion;³² however, the Commission lacks the authority to enforce its advice regarding the Postal Service's proposed changes to service standards. Further, certain statutory provisions related to service standards that apply to the Postal Service's Market Dominant products do not apply to Competitive products such as: the objectives

³² 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).

and factors governing the Postal Service's revisions of its service standards for Market Dominant products (39 U.S.C. § 3691(b)-(c)), the requirement that the Postal Service publish its service standards for Market Dominant products in the Code of Federal Regulations (39 U.S.C. § 3691(a)), and the requirement that the Postal Service measure and report quality of service for each Market Dominant product (39 U.S.C. § 3652(a)). The Postal Service does submit highly aggregated, non-public information about the service performance of some Competitive products to the Commission as a part of its statutorily required annual performance plan (39 U.S.C. § 2803).

B. Roadmap of Analysis

The following sections of this Advisory Opinion discuss the estimated impact of the proposal on the Postal Service's package processing, transportation network, and market demand. Based on the Commission's analysis, the Commission provides recommendations for the Postal Service to consider if it chooses to implement its proposal.

1. Overarching Conclusion

The Postal Service's proposal represents an improvement of service and thus, generally, benefits mailers and is in the public interest. Additionally, the goals of the proposal intuitively makes sense: improving service standards to make RG and PSG a more desirable ground shipping option for packages greater than one pound, relieving downward pricing pressure on PM, and streamlining the operational flow of RG and PSG by combining it with FCPS to minimize touchpoints and processing at NDCs.

However, the Commission is concerned that the improvement in service may be at the expense of profitability, or may result in cannibalization of PM or other products. Moreover, the Postal Service assumes the proposed changes will lead to an increase in volume with a positive contribution, but the anticipated improvement in contribution depends on whether the Postal Service's analysis is based on realistic assumptions, including assumptions about the profile of any future RG and PSG volumes. Furthermore, the Postal Service provides no indication about when it expects the anticipated future benefits of the proposed changes to materialize. The success of the

Postal Service's proposal is dependent on results that the Postal Service has not demonstrated in its proposal, namely: operational implementation; achievement of consistency/reliability over time, reasoned assumptions with regard to demand changes, modeled efficiencies matching efficiencies that can be achieved in reality, and potential diversion of volume from PM and FCPS.

2. Package Processing Findings

The Commission finds that there are immediate benefits from reducing the number of times RG and PSG pieces are handled during processing. However, it is uncertain how efficiently P&DCs can handle additional volume of large parcels, which might require more manual processing than FCPS volume requires. Processing delays have implications on timely dispatch operations and can lead to inefficiencies in transportation. Furthermore, the calculated financial impact includes only cost changes associated with eliminated or transferred operations for current (FY 2021) RG and PSG. The estimated effect on FCPS mail processing cost is assumed negligible (\$0). The calculated financial impact does not consider mail processing cost changes associated with future RG and PSG parcels that the proposed changes might attract.

In addition, the Postal Service has indicated transitioning to shape-based mail processing facilities in its 10-year plan, but it is left unexplained whether the proposed change is an intermediate step. The Commission recommends that the Postal Service design a timeline, which includes all intended incremental changes to the processing network operations as part of this plan, and how each would contribute to the eventual, more efficient, shape-based processing network. It also recommends that the Postal Service design a plan to monitor all implications of each such incremental network change, in order to learn from previous changes and fine-tune subsequent changes. Achieving processing operations that support the goals of service excellence and financial sustainability depends on post-implementation monitoring, since projecting impacts of changes to the complex postal network of inter-twined operations is often based on assumptions that may prove to be unreliable.

3. Transportation Findings

The Commission finds that the projected transportation efficiencies—reduced reliance on air transportation and a more efficient surface transportation network—are expected to materialize over time, provided the proposed changes capture some of the demand for low-price, medium-speed ground transportation large packages. In the meantime, there is no evidence that the proposed change would reduce reliance on air transportation and is expected, in fact, to increase transportation costs. Improved surface capacity utilization is largely dependent on timely processing and dispatch of the combined RG/PSG/FCPS volumes and adherence to operating plans. To achieve a more optimized transportation network, the proposed changes should try to capture the optimal mix of parcels. While the planned service standards would allow the extension of transit windows in order to support coast-to-coast surface transportation, low volume density in long-distance lanes prevents a shift to surface transportation on the basis of cost-effectiveness. Additionally, obstacles such as the persistently increasing HCR cost per mile, particularly in long-distance surface trucking (associated with national truck driver shortage), might raise the volume density threshold that would be sufficient to justify the increasing costs of long-distance surface transportation.

New RG and PSG volumes assigned to surface lanes should have size and weight characteristics similar to FCPS to enable dispatching all RG, PSG, and FCPS pieces at the same time, as bundles, so as to enable placing those bundles on shared surface transportation without adding trips to the already underutilized surface network. Heavy, oversized, non-machinable PSG/RG items that are more difficult to process are at risk of slowing down joint flows or being delayed.

The Postal Service calculated the financial impact of the planned changes on the transportation network based on cubic foot and distance profiles of current RG and PSG. As such, the true financial impact on the transportation network in future years will depend on the cubic foot and distance profiles of new RG and PSG parcels that the upgraded service standards and unchanged prices would attract, which are still unknown.

The Commission recommends that the Postal Service conduct more robust research into the market segment that the upgraded RG and PSG service standards would attract to gain a better idea of this unknown profile. This would help ensure that provision of low prices for potentially high-cost shipping of new volumes does not negatively impact contribution for RG and PSG products.

4. Market Demand/Research Findings

The Commission finds that the planned changes have the potential for meeting market demand, filling an identified gap in the market, and enhancing service to customers sending larger packages. However, the impact on mailers who currently use RG and PSG is unclear. Furthermore, there is a risk that the proposed changes will divert package volume from PM. Should the planned changes attract a higher concentration of high-cost volume to low-density areas, this would negatively impact the expectation of the increase in positive-contribution volume. The Commission recommends that the Postal Service monitor the impact of the planned service standard change on shipping options in the competitive parcels market, as well as the impact on mailers who actually use RG and PSG, mailers who care only or mainly about price, and large-sized business mailers. The Postal Service should also monitor the volume diversion from PM and impact on other Postal Service products.

C. Mail Processing Analysis

1. Overview

The Postal Service states that combining RG and PSG with FCPS flows would improve processing times by reducing the number of processing nodes that RG and PSG would traverse, enable further optimization of the Postal Service's package processing network, and reduce the overall processing burden. USPS-T-2 at 17-18. The Postal Service estimates mail processing costs savings of \$17.1 million for RG and

\$14.9 million for PSG, associated with modified mail processing flows following the implementation of the proposed service standard changes.³³

For FCPS and other parcel products processed at P&DCs, the Postal Service expects the “relatively small addition of workload” from RG and PSG volumes to have “negligible effects” on their existing processing operations.³⁴

2. Commission Analysis

The Postal Service’s projections for mail processing costs savings referenced above reflect estimated changes in unit mail processing costs between the current and future mail processing flows, which were combined with the current (FY 2021) RG and PSG volumes. USPS-T-3 at 2. The Postal Service notes that the projected mail processing cost changes do not include “effects of volume changes induced by the service standard changes.” *Id.*

In the sections that follow, the Commission analyzes the assumptions that the Postal Service used to estimate the \$31.9 million in savings associated with simplified mail processing flows for RG and PSG parcels. The Commission then discusses the uncertainties associated with future RG, PSG, and other parcel volumes, and their potential impacts on the efficiency of mail processing operations and costs in a more distant future. Lastly, the Commission provides a recommendation that additional analysis is conducted prior to the implementation of the proposed service standard changes, recognizing that such analysis could better inform the Postal Service on the attributes of future large parcel volumes that the service standard changes for RG and PSG might attract. More granular data on future large parcel volumes are relevant to ensure the efficiency of processing operations and could prevent implementation of changes that have the potential to undermine the Postal Service’s goal of service excellence. The Commission also recommends that the Postal Service design a

³³ USPS-T-3 at 5; see Library Reference USPS-N2022-1/1 (as revised on April 15, 2022), Excel file “RG.PSG.FCPS.Cost.Impact.Public.Revised.04.15.2022.xlsx,” tab “Summary_MP_Trans.”

³⁴ USPS-T-3 at 1. For FCPS, the Postal Service estimates \$0 change in the product’s mail processing costs. See Library Reference USPS-N2022-1/1 (as revised on April 15, 2022), Excel file “RG.PSG.FCPS.Cost.Impact.Public.Revised.04.15.2022.xlsx,” tab “Summary_MP_Trans.”

timeline of all intended incremental changes it plans to implement to accomplish the goals laid out in its 10-year plan and specify how actions, such as this service standard change, fit into that timeline. See *generally* Postal Service Strategic Plan.

a. Impact on Mail Processing Operations

The Postal Service conducts separate mail processing impact analyses for machinable and non-machinable parcels, for each of RG and PSG. The Postal Service explains that due to the “very small share” of oversized volumes for each product, it did not perform similar analyses for oversize RG and PSG flows.³⁵ In its estimation process, the Postal Service relies on certain assumptions, which are discussed in more detail by product, below.

(1) Retail Ground

As described in witness Bray’s testimony, the current-state operational flow for PSG volume that enters the Postal Service’s network at Post Offices is identical to that for RG. USPS-T-2 at 5. The Postal Service confirms that this would continue to be the case under the simplified operational flow. *Id.* at 10. Consequently, the Postal Service explains that its mail processing impact analysis for RG is based on the Current PSG Mail Processing Cost Model, “adapted to estimate the change in RG mail processing costs.”³⁶

³⁵ USPS-T-3 at 3 n.1. The Postal Service defines oversized PSG as “any piece that measures more than 108 inches (but not more than 130 inches) in length plus girth,” regardless of weight. Pieces weighing more than 70 pounds are considered “nonmailable” although evidence suggests the Postal Service may still accept such items. See MCS § 2115.6; OIG Report “Package Delivery in Rural and Dense Urban Areas,” at 14.

³⁶ USPS-T-3 at 2; see Docket No. ACR2021, Library Reference USPS-FY21-NP15, January 13, 2022, Excel file “USPS-FY21-NP15.Rev.1.13.22.xlsx” (Parcel Select/Parcel Return Service Mail Processing Cost Model). For the remainder of the discussion, the Commission will refer to all calculations included in the Parcel Select/Parcel Return Service Mail Processing Cost Model that are associated with PSG as “Current PSG Mail Processing Cost Model.” See Library Reference N2022-1/NP3, April 15, 2022, Excel file “USPS-FY21-NP15.RG.MOD.Current.Revised.04.15.2022.xlsx” (Current RG Mail Processing Cost Model).

To modify the Current PSG Mail Processing Cost Model for the purpose of RG mail processing impact estimation, the Postal Service relies on the following assumptions:

- Mail processing activities performed at each processing node for RG pieces are identical to those performed for PSG pieces that enter the postal network at Post Offices.³⁷
- Mail processing activities performed for RG pieces have the same productivities as those for PSG pieces that enter the postal network at Post Offices.³⁸
- One hundred percent of RG volume is deposited at origin delivery units (DUs). This assumption replaces volume distribution between three entry points included in the Current PSG Mail Processing Cost Model.³⁹

The combined effect of these assumptions is that the current-state unit mail processing costs for RG differ from the current-state unit mail processing costs for PSG almost entirely due to the difference in the distribution of these products' volumes between entry points to the postal network.⁴⁰

Origin processing operations and unit costs. To estimate the impact of reduced touch points for RG parcels, the Postal Service's analysis indicates no change in

³⁷ Compare Current RG Mail Processing Cost Model, with Current PSG Mail Processing Cost Model.

³⁸ Compare Current RG Mail Processing Cost Model, with Current PSG Mail Processing Cost Model.

³⁹ While PSG parcels are assumed to enter the postal network at each of origin DUs, origin P&DCs, or origin NDCs, all RG parcels are assumed to originate at Post Offices. See USPS-T-2 at 5, 9. Compare Current RG Mail Processing Cost Model, with Current PSG Mail Processing Cost Model.

⁴⁰ More specifically, the Current RG Mail Processing Cost Model assumes handling of all RG shipments at both origin DUs and origin P&DCs, due to all of RG volume traversing through both processing facilities before being routed to origin NDCs for outgoing processing. By contrast, it is only at origin NDCs that the Postal Service handles all PSG pieces, since only a portion of PSG volumes enter the network at origin DUs and at origin P&DCs. This is accounted for in the Current PSG Mail Processing Cost Model accordingly. Compare Current RG Mail Processing Cost Model, with Current PSG Mail Processing Cost Model. The only other differences stem from the slightly higher hourly wage rate assumed for RG processing activities than for PSG activities, and from lower proportion of RG pieces destinating in the local area of origin NDCs, which require additional sortation, based on 5-digit destination ZIP Codes. Compare Current RG Mail Processing Cost Model, with Current PSG Mail Processing Cost Model.

activities performed at origin DUs or their associated costs, between current and future-state trajectory.⁴¹

The Postal Service assumes that of the total RG volume, which currently traverses through each of origin DUs, origin P&DCs, and origin NDCs for outgoing mail processing and dispatch to destination NDCs, a certain portion would continue being routed to origin NDCs for outgoing processing and dispatch in the future state.⁴² For the remaining portion, subject to simplified processing flow and fewer processing touches, the Postal Service adds two kinds of activities to origin P&DCs' operations: outgoing sortation activities and activities associated with loading of postal containers for dispatch to destination P&DCs.⁴³

The Postal Service's analysis indicates reduced costs for origin NDCs, associated with reduced sortation and dispatch requirements due to the assumption that only a portion of RG parcels will follow the current processing trajectory in the future state. The Postal Service's analysis also indicates increased costs for origin P&DCs in the future state, associated with added sortation- and dispatch-related requirements for the portion of RG parcels assumed to benefit from a more simplified processing flow. Overall, the Postal Service's analysis indicates reduced costs on origin processing operations in the future state, with the estimated cost reduction being substantially more significant for non-machinable parcels than for machinable parcels.⁴⁴

Destination processing operations and unit costs. The Future RG Mail Processing Cost Model assumes that all RG volumes, whether dispatched from origin NDCs or from origin P&DCs, would be routed to destination P&DCs for destination

⁴¹ Compare Current RG Mail Processing Cost Model, with Future RG Mail Processing Cost Model.

⁴² See Future RG Mail Processing Cost Model, tab "Other Inputs," cell B56 for the portion of RG volume assumed to stay in the NDC network for outgoing processing.

⁴³ Compare Current RG Mail Processing Cost Model, with Future RG Mail Processing Cost Model.

⁴⁴ Compare Current RG Mail Processing Cost Model, with Future RG Mail Processing Cost Model.

processing under the future trajectory.⁴⁵ The Future RG Mail Processing Cost Model also includes newly added sortation activities at destination P&DCs.

The Postal Service's analysis indicates that costs incurred at destination NDCs and auxiliary service facilities (ASFs) in the current state would be eliminated entirely in the future state, due to all volumes being dispatched to destination P&DCs. The Postal Service's analysis also indicates cost increases for destination P&DCs associated with the newly added incoming RG parcel sortation activities. However, the overall impact on destination processing operations is a cost reduction, with the estimated reduction in costs for non-machinable volume processing being significantly more substantial than the estimated cost reduction for machinable RG parcels' processing.⁴⁶

(2) Parcel Select Ground

The estimated impact on PSG processing operations and costs is based on the Current PSG Mail Processing Cost Model from the FY 2021 Annual Compliance Review docket.

The mail processing activities that would be added or eliminated in the future processing state are identical for PSG as those assumed for RG, described in more detail above. Additional unit cost impacts estimated for PSG and not for RG stem from the following assumptions included in the Future PSG Mail Processing Cost Model:

- Increase in the proportion of PSG parcels that would be deposited at origin P&DCs and a reduction in the proportion of PSG parcels that would be deposited at origin NDCs in the future-state operational flow⁴⁷

The Postal Service's analysis indicates unit mail processing cost increases for origin P&DCs associated with the newly added processing activities and with the higher

⁴⁵ Compare Current RG Mail Processing Cost Model, with Future RG Mail Processing Cost Model.

⁴⁶ Compare Current RG Mail Processing Cost Model, with Future RG Mail Processing Cost Model, tabs "GROUND MACH" and "GROUND NMO" in each file.

⁴⁷ Library Reference USPS-LR-N2022-1/NP3, Excel file "USPS-FY21-NP15.Rev.PSG.Future.xlsx."

proportion of PSG volumes entering the postal network at these facilities in the future state processing flow. The Postal Service's analysis also indicates unit mail processing cost reductions associated with fewer PSG parcels assumed to enter the postal network at origin NDCs in the future state, as compared to the current state, as well as with a smaller proportion of PSG parcels traversing NDCs for origin processing and dispatch than in current state. Since the PSG (and RG) Mail Processing Cost Models assume higher productivity of P&DCs' mail processing operations than those of NDCs' operations, the overall impact is a reduction in unit costs incurred on origin processing operations, with the estimated reduction in costs for non-machinable volume processing being significantly more substantial than the estimated cost reduction for machinable PSG parcels' processing.⁴⁸

Similar to the impact on RG destination processing, destination NDCs and ASFs are bypassed in the future state processing flow, resulting in elimination of costs associated with processing activities performed at these facilities currently. As is the case for RG processing, the increase in unit mail processing costs associated with the additional activities and processing requirements for destination P&DCs are low enough to lead to an overall decrease in processing costs associated with destination processing activities for PSG parcels in the future state processing trajectory. The estimated decrease in unit mail processing costs associated with destination processing activities for non-machinable volume is again more substantial than the estimated cost reduction for destination processing of machinable PSG parcels.⁴⁹

(3) First-Class Package Service

The Commission compares the volume and mail processing cost of FCPS and RG-PSG to evaluate the Postal Service's assertion that given the relatively small volume of RG-PSG requiring a "relatively small addition of workload" from RG and PSG

⁴⁸ April 15 Response to POIR No. 3, question 10.d. *Compare* Current PSG Mail Processing Cost Model, *with* Future PSG Mail Processing Cost Model.

⁴⁹ *Compare* Current PSG Mail Processing Cost Model, *with* Future PSG Mail Processing Cost Model.

volumes, there should be “negligible effects” on their existing processing operations.⁵⁰ Based on volume and mail processing cost data from FY 2017 to FY 2021, the combined RG-PSG volume and mail processing cost represent a relatively small percentage of FCPS volume and mail processing cost.⁵¹

The Commission concludes that it is reasonable to assume FCPS mail processing cost may not be impacted materially given the relatively small volume of RG and PSG currently. However, it is difficult to predict the magnitude of mail processing cost impact should the enhanced-service RG-PSG volume grow. The Commission is concerned that FCPS's service performance may be negatively impacted if mail processing of larger and heavier RG-PSG packages takes longer, potentially delaying processed FCPS packages that would share its transportation.

b. Mail Processing Cost Impact

The Postal Service multiplies the changes in unit mail processing costs associated with added or eliminated processing activities, as well as the changes associated with reduced or increased volumes handled in existing processing operations, with FY 2021 RG and PSG volumes, to calculate mail processing cost impacts for each product. This is done separately for machinable and non-machinable parcels.

Of the estimated overall mail processing cost savings for RG and for PSG, the largest portion is attributable to non-machinable parcels.⁵² However, only a small portion of RG and PSG parcels are assumed to be non-machinable in the Postal Service’s mail processing cost impact calculations. *Id.*

⁵⁰ USPS-T-3 at 1. For FCPS, the Postal Service estimates a \$0 change in the product’s mail processing costs. See Library Reference USPS-N2022-1/1 (as revised on April 15, 2022), Excel file “RG.PSG.FCPS.Cost.Impact.Public.Revised.04.15.2022.xlsx,” tab “Summary_MP_Trans.”

⁵¹ Non-Public Technical Appendix. Percentage calculated using FY 2017 through FY 2021 FCPS and RG-PSG volume and mail processing cost data from Docket Nos. ACR2017 through ACR2021, Library References NP15 and NP19.

⁵² Library Reference USPS-N2022-1/NP3, Excel file “RG.PSG.FCPS.Cost.Impact.nonpublic.revised.04.15.2022.xlsx.”

The Postal Service acknowledges that machinable and non-machinable data are not available for RG parcels and assumes nearly identical distributions of machinable, non-machinable, and oversized parcels for RG and as is reported for PSG parcels in the FY 2021 Annual Compliance Review docket.⁵³ However, the data for FY 2021 suggest otherwise.⁵⁴ Comparing the percentage of volume reported as Balloon, Oversized, or DIM-Weighted, RG has significantly greater volume in all three categories compared to PSG.⁵⁵ While not all non-machinable items may be “Balloon,” “Oversized,” or “DIM-Weighted,” it is suggestive that packages mailed under the two products do have very different characteristics. This could indicate a greater proportion of non-machinable volume for RG than for PSG parcels, including greater requirements for manual processing, and more likely disruptions to FCPS flows from RG flows than assumed in the RG mail processing cost models.

The Postal Service indicates that potentially underestimating non-machinable RG volumes represents a conservative approach, in the sense that it could only lead to increased savings for NDCs’ processing operations. April 15 Response to POIR No. 3, question 6. However, such underestimations could also indicate that the expected impacts on FCPS flows might be less negligible than the Postal Service anticipates, due to more likely disruptions to FCPS flow processing, and the resulting delays in the combined RG, PSG, FCPS dispatches.⁵⁶

⁵³ Library Reference USPS-N2022-1/NP3, Excel file “RG.PSG.FCPS.Cost.Impact.nonpublic.revised.04.15.2022.xlsx.” Response to POIR No. 2, question 7.c.

⁵⁴ Docket No. ACR2021, Library Reference USPS-FY21-NP1, Excel file “FY2021 RG BD.xlsx.”

⁵⁵ Docket No. ACR2021, Library Reference USPS-FY21-NP1, Excel file “FY2021 Parcel Select BD.xlsx.”

⁵⁶ The Commission notes that the Postal Service’s transportation mode impact analysis is based on an assumed transportation of FCM/FCPS/RG/PSG bundles, which would be possible if these four products’ volumes were also processed and dispatched from P&DCs as bundles. However, witness testimonies filed in the instant proceeding do not reference FCM and only describe RG and PSG as being added to FCPS flows, following the implementation of the proposed changes. The impact that the added volumes of large parcels could have on mail processing operations for FCM is not accounted for in the Postal Service’s mail processing impact analysis. See Section VI.E.2.a., *infra*.

c. Anticipated Impact of Future Volumes on the Mail Processing Network Efficiencies and Costs

In past proceedings, the Postal Service described challenges P&DCs face, related to the need for manual processing of some parcels, staff shortages, constraints associated with volume arrival profile, dock congestion, etc. See Docket No. N2021-1, Advisory Opinion at 140. The Postal Service also indicated that its past attempts for improved transportation operations were unsuccessful and that this was, in part, due to site-specific constraints, forcing adjustments to departure times of scheduled transportation, and thus negatively impacting pairings of volumes at origin P&DCs. See *id.* at 122.

The Postal Service does not provide any data or any alternative evidence that would support its expectation of negligible impact from added large parcels (*i.e.*, parcels weighing between 1 and 70 pounds) to FCPS processing flows (*i.e.*, flows of packages weighing up to 1 pound). The Commission is concerned that an increase in processing requirements, including an increased need for manual processing and staff availability, for facilities already failing to meet operating plans⁵⁷ could lead to disruptions in processing and transportation operations and cost increases.

A Postal Service Office of Inspector General (OIG) study indicates FedEx Corporation and United Parcel Service, Inc. lowered the weight threshold for their parcel products from 70 pounds to 50 pounds.⁵⁸ The same OIG study suggests that while the Postal Service might be a more attractive option for price-conscious shippers due to no surcharges for heavy parcels,⁵⁹ “it also makes it a potential dumping ground for bulky, hard-to-deliver packages.”⁶⁰ The impact on FCPS processing efficiency of such a

⁵⁷ Postal Service Strategic Plan at 11.

⁵⁸ See United States Postal Service, Office of Inspector General, Report No. RISC-WP-20-008, Package Delivery in Rural and Dense Urban Areas, September 16, 2020, at 14, available at <https://www.uspsoig.gov/sites/default/files/document-library-files/2020/RISC-WP-20-008.pdf> (OIG Report No. RISC-WP-20-008).

⁵⁹ See Mail Classification Schedule § 2135.4 for surcharges the Postal Service currently applies to RG parcels, and MCS § 2115.4 for PSG parcels.

⁶⁰ OIG Report No. RISC-WP-20-008 at 14.

possible development is not accounted for in the provided analysis, which is based on the known profile for current (FY 2021) PSG parcels and on a profile for current RG parcels that is assumed to be identical to PSG. However, even if future parcel volumes are not known, the Commission notes that the market research analysis the Postal Service presents in the instant proceeding does not include expected demand from retail customers, the primary consumer of the RG product. Response to POIR No. 5, question 4.a.

3. Conclusion

Based on these findings, the Commission recommends that the Postal Service conduct additional analysis prior to the implementation of the proposed service standard changes. The purpose of such analysis would be to inform the Postal Service on the attributes of future large parcel volumes that the enhanced service standard changes for RG and PSG might attract. The Commission recognizes that the importance of such additional analysis lies not only in gathering information on factors that are relevant to the efficiency of processing operations, but also in the effect that efficient mail processing operations, or their lack, might have on the efficiency of the Postal Service's downstream operations: transportation and delivery networks.

The Commission agrees with the Postal Service OIG that inefficient operations lead to cost increases,⁶¹ thus potentially undermining not only the Postal Service's goal of service excellence but also its goal of financial sustainability. Efficient operations are acutely important in the parcel market, where the Postal Service faces competition and is under pressure to keep prices low. *Id.*

Additionally, the Commission perceives the incremental implementation of the numerous planned changes indicated in the Postal Service's 10-year plan to provide the opportunity to evaluate the impacts of changes already implemented. Such an exercise would enable the Postal Service to evaluate the robustness of the assumptions used to project impacts of past proposals, for which outcomes can already be observed,

⁶¹ See OIG Report No. RISC-WP-20-008 at 3, 8.

measured, evaluated against projections, and used to fine-tune any remaining future planned changes to the postal network. The Commission also notes that any changes to services offered to postal products are likely to have impacts that extend beyond the operations and costs attributed to the respective products. As such, the Commission recommends that the Postal Service design a timeline of all intended incremental changes it plans to implement to accomplish the goals laid out in its 10-year plan. The Commission recommends further that such timeline includes plans for monitoring the impacts of different strategic changes on relevant aspects of its operations, whether they are isolated to respective products or extend to operations at a facility or a network level.

D. Transportation Impact Analysis

1. Overview

The Postal Service states that combining RG and PSG with FCPS flows would not require adding trips to the surface transportation network, since the network “in place for FCPS contains sufficient capacity to absorb future volumes of RG and PSG shipments.” USPS-T-2 at 12. As such, the Postal Service claims that the proposal would increase volume and improve capacity utilization in surface lanes and enable further optimization of the Postal Service’s surface transportation network. *Id.* at 12-13, 17-18. However, the Postal Service’s transportation impact analysis does not include an estimate for the anticipated increase in surface network capacity utilization.⁶²

In addition, the Postal Service estimates that enhancing service standards for RG and PSG, and combining their flows with FCPS, will result in an increase in the proportions of RG and PSG volumes transported by air. For RG, the Postal Service estimates that air volume would increase from the current 14.0 percent to 28.9 percent;

⁶² The Postal Service includes various estimates of the current surface network’s capacity utilization, ranging from 42 percent to 62 percent. See USPS-T-2 at 12-13; see also Response to POIR No. 2, question 2.a.i.

for PSG, the estimated increase is from the current 15.6 percent to 15.9 percent.⁶³ For FCPS, the Postal Service projects volumes shifting from commercial air carriers to FedEx Day Turn transportation. USPS-T-3 at 1-2.

The Postal Service projects a \$40.4 million transportation cost increase for FCPS, a \$4.6 million reduction in transportation costs for RG, and a \$0.1 million reduction in transportation costs for PSG, resulting from transportation mode and air carrier shifts described above.⁶⁴

2. Commission Analysis

The projections referenced above are based on the following assumptions: implementation of the 2- to 5-day service standards for RG and PSG, as well as for FCPS; the “concomitant improvement and optimization” of the surface transportation network; and consolidation of RG and PSG volumes with “other [contiguous] First-Class volume.” USPS-T-2 at 15; Response to POIR No. 2, question 6.a., 6.d. The Postal Service clarifies that no transportation modeling was required in the instant proceeding and that the transportation impact analysis of the proposed changes consists of analyzing the impact on transportation mode assignments for contiguous lanes.⁶⁵

The Postal Service expects that over time, as volume and the surface transportation network grow, the Postal Service’s ability to shift more volume from air to surface would improve.⁶⁶ As a result, its surface transportation capacity utilization

⁶³ The Commission notes that 14.0 percent of RG and 15.6 percent of PSG represent percentages of these products’ volumes estimated to have been transported by air in FY 2021, when the products were transported in the NDC network. USPS-T-2 at 17. Library Reference USPS-N2022-1/NP3, Excel file “RG.PSG.FCPS.Cost.Impact.nonpublic.revised.04.15.2022.xlsx,” tabs “Summary_Trans” and “Current State.”

⁶⁴ USPS-T-3 at 6; Notice of Revisions to Testimony at 1-2, 6; Library Reference USPS-N2022-1/1 (as revised on April 15, 2022), Excel file “RG.PSG.FCPS.Cost.Impact.Public.Revised.04.15.2022.xlsx,” tab “Summary_MP_Trans.”

⁶⁵ This corresponds to offshore RG and PSG shipments, *i.e.*, shipments with either origin or destination outside the contiguous United States, being excluded from the service standard upgrade for the time being. Response to POIR No. 1, question 1.a., 1.b.; Library Reference USPS-N2022-1/NP4, PDF file “N2022-1-NP4.Bray.Preface.pdf” (Library Reference USPS-N2022-1/NP4 Preface); USPS-T-2 at 15-16.

⁶⁶ USPS-T-2 at 17; April 15 Response to POIR No. 3, question 8.a., 8.c.; Response to POIR No. 5, questions 2, 5.

would also improve. *Id.* This expectation is based on an assumption that the enhanced service standards for RG and PSG will “allow [the Postal Service] to be better positioned to meet growing consumer and business needs for a medium-speed, low-price ground transportation solution for shipping large packages within the contiguous United States,” thereby growing volume. April 15 Response to POIR No. 3, question 8.a., 8.c. The Postal Service is unable to predict when these more distant efficiency improvements will materialize. Response to POIR No. 5, question 2.

In the sections that follow, the Commission analyzes the projected \$35.7 million cost increase. The Commission then discusses the anticipated future improvements in transportation efficiencies. Lastly, the Commission recommends that the Postal Service conduct additional analysis prior to the implementation of the proposed service standard changes.

a. Transportation Mode Impact Analysis

The Postal Service explains that the surface transportation network used in its transportation impact analysis is the same as the final network which resulted from its transportation model in Docket No. N2021-2.⁶⁷ This surface transportation network included efficient trip structure and was projected to enable transporting the FCM/FCPS Model’s existing surface volumes as well as volumes diverted from the air network with about half as many trips as the Postal Service reported in the comparable actual surface transportation network. Docket No. N2021-2, Advisory Opinion at 114-20.

The Postal Service states that its instant proposal is based on an assumption that adding RG and PSG to FCPS lanes would “build density and potentially justify shifting additional volume from air transportation to surface transportation.” Response to POIR No. 1, question 1.b. Consequently, the Postal Service included 3-digit ZIP Code pairs with daily volumes for each of RG, PSG, FCM, and FCPS in its analysis conducted in the instant proceeding. Response to POIR No. 2, question 6.a., 6.d.; April

⁶⁷ Response to POIR No. 1, question 1.a. See Docket No. N2021-2, Advisory Opinion at 114-20 for the discussion of the final network from the Postal Service’s transportation model, in which FCM and FCPS were subject to the more relaxed, 2- to 5-day service standards (FCM/FCPS Model).

15 Response to POIR No. 3, question 18.a. To evaluate potential air-to-surface volume shifts from the added RG and PSG volumes, the Postal Service conducted a transportation mode impact analysis, described below.

*FCM/FCPS/RG/PSG Model's baseline network.*⁶⁸ For its transportation mode impact analysis, the Postal Service started with a baseline network, in which individual OD pairs were assigned transportation modes for FCPS lanes as of February 2022.⁶⁹ The Commission notes that while all modeled products in this network were subject to the 2- to 5-day service standards, its surface transportation reach corresponds to the 1- to 4-day service standard window for FCPS.⁷⁰ The Postal Service refers to the FCM/FCPS/RG/PSG Model's baseline network as "the current state of the FCPS surface transportation network." USPS-T-2 at 16.

As part of its transportation mode impact analysis, the Postal Service evaluated the baseline network's capability to transport modeled products by surface transportation within transit windows available under the 2- to 5-day service standards.⁷¹

⁶⁸ As described below, the transportation mode impact analysis was based on adding RG and PSG to the optimized surface transportation network from the Docket No. N2021-2 proceeding (FCM/FCPS Model's final network) and the implementation of the 2- to 5-day FCPS service standards. Accordingly, the Commission will refer to the transportation mode assignments generated by network scenarios from the instant proceeding as pertaining to the FCM/FCPS/RG/PSG Model for the remainder of the discussion.

⁶⁹ The Commission notes that in the documentation provided in the instant docket, the Postal Service refers interchangeably to lanes and OD pairs. The Commission also notes that each lane or OD pair is assigned a transportation mode in the Postal Service's analyzed transportation network scenarios, discussed in this section. Response to POIR No. 1, question 1.b.; Library Reference USPS-N2022-1/NP4 Preface.

⁷⁰ The Postal Service explains that while FCPS was subject to the 1- to 3-day service standards during February 2022, the transportation mode assignments in the baseline network include more volume transported by surface than the 3-day surface reach would allow due to 1 transit day temporarily added for FCPS during the COVID-19 pandemic. Response to POIR No. 2, question 6.a.

⁷¹ This corresponds to the Postal Service's statement that the proposed RG and PSG service standards are predicated on the implementation of the planned change to the FCPS service standards. USPS-T-2 at 15, 16-17; Library Reference USPS-N2022-1/NP4 Preface.

The mileages used in the baseline network's surface lanes are from the Postal Service's FCM/FCPS Model's final surface network.⁷²

To determine surface viability, the Postal Service calculated transit times for individual OD pairs, assuming an average driving speed of 46.5 miles per hour, similar dispatch times from origin P&DCs for all modeled products' volumes, and critical entry times (CETs) at destination P&DCs that were product specific.⁷³

Only contiguous air lanes for which surface transportation represented a service-responsive alternative for FCM and for FCPS, RG, and PSG volumes were considered in the subsequent evaluation of cost-effectiveness of surface transportation versus air transportation.⁷⁴ This means that offshore volumes are excluded from the service standard upgrade at this time. USPS-T-2 at 13, 15-16. The Postal Service indicates that delivery by surface transportation was deemed logistically viable in most cases. *Id.* at 16.

Evaluation of cost-effectiveness for surface vs. air transportation and FCM/FCPS/RG/PSG Model's final network. To evaluate the cost-effectiveness of surface transportation for surface-viable lanes, the Postal Service compares the cost of surface transportation "over a given distance" to the cost of air transportation.⁷⁵

The estimated air transportation costs are calculated based on the cubic foot capacity needing air transportation for FCM, FCPS, RG, and PSG volumes in the evaluated lanes and an assumed air transportation cost per cubic foot. The calculated surface transportation costs are based on the number of surface trips that the modeled

⁷² This corresponds to the Postal Service's statement that the planned changes are "predicated on the concomitant improvement and optimization" of the Postal Service's surface transportation network. USPS-T-2 at 15; April 15 Response to POIR No. 3, question 18.a.

⁷³ The Postal Service indicates that all modeled products' volumes were assumed to depart origin P&DCs at about 4 a.m. The documentation filed in the instant proceeding indicates CETs specific to modeled products were used in the transit time analysis and determination of surface-viability for OD pairs. USPS-T-2 at 16; Library Reference USPS-N2022-1/NP4, Excel file "Model_3.17.2022.xlsx."

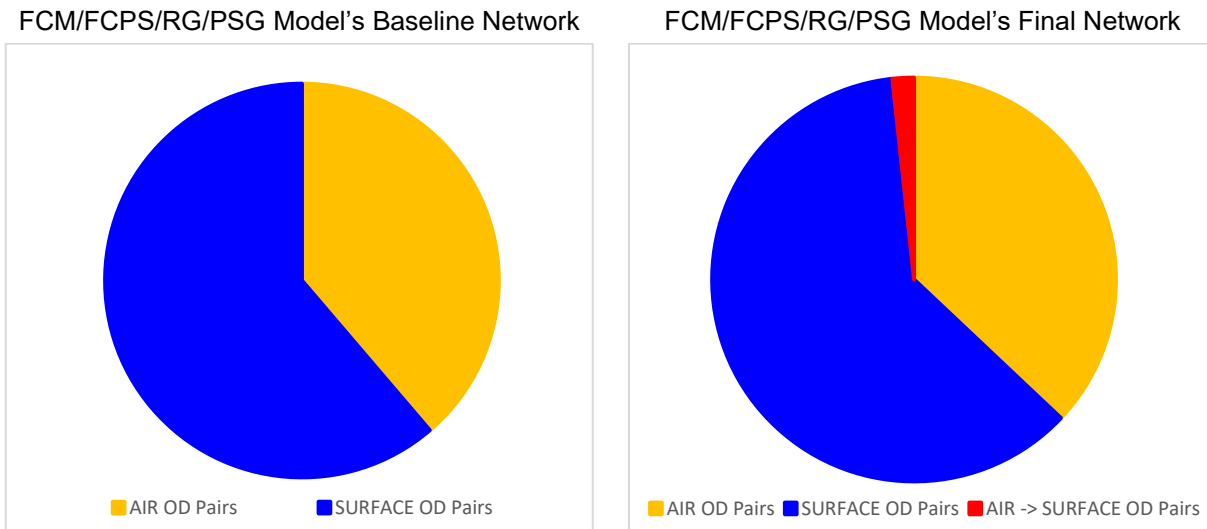
⁷⁴ Library Reference USPS-N2022-1/NP4, Excel file "Model_3.17.2022.xlsx."

⁷⁵ USPS-T-2 at 16-17; Library Reference USPS-N2022-1/NP4, Excel file "Cost Analysis.xlsx."

volumes' cubic foot capacity would necessitate, as well as the corresponding trips' mileages and an assumed surface transportation cost per mile.⁷⁶

Figure VI-1 below illustrates transportation mode assignments for OD pairs in the FCM/FCPS/RG/PSG Model's baseline network and in the final network, which resulted from the Postal Service's surface-viability and cost-effectiveness analyses.

Figure VI-1
Transportation Mode Assignments for OD Pairs in the FCM/FCPS/RG/PSG Model's Baseline and Final Networks



Source: Library Reference USPS-N2022-1/NP4, Excel files "Model_3.17.2022.xlsx" and "Cost Analysis.xlsx."

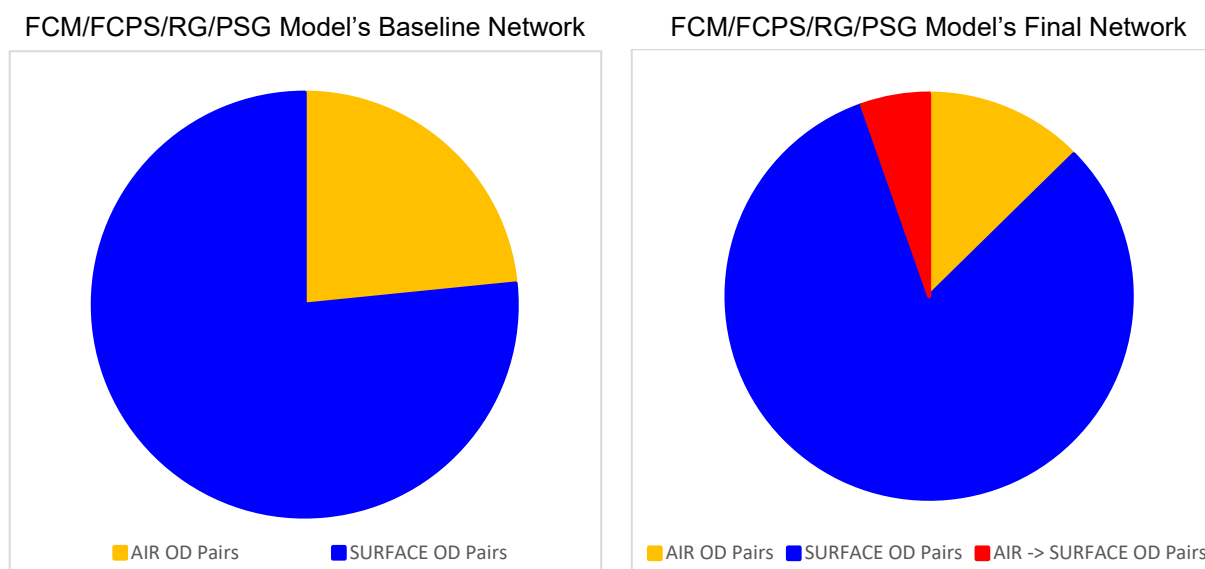
Note: OD pairs included in Figure VI-1 represent data for contiguous United States.

⁷⁶ Library Reference USPS-N2022-1/NP4, Excel file "Cost Analysis.xlsx."

The Commission’s analysis of the Postal Service’s data suggests that of the contiguous air lanes included in the FCM/FCPS/RG/PSG Model’s baseline network, for which a service-responsive surface alternative lane exists in the efficiently routed surface network, surface transportation was determined more cost-effective than air transportation for only a small fraction of lanes.⁷⁷

Figure VI-2 depicts combined cubic foot capacities for the modeled products’ volumes that correspond to air, surface, and air-to-surface OD pairs shown in Figure VI-1 above.

**Figure VI-2
Transportation Mode Assignments for Modeled Products’ Combined Cubic Foot Capacities in the FCM/FCPS/RG/PSG Model’s Baseline and Final Networks**



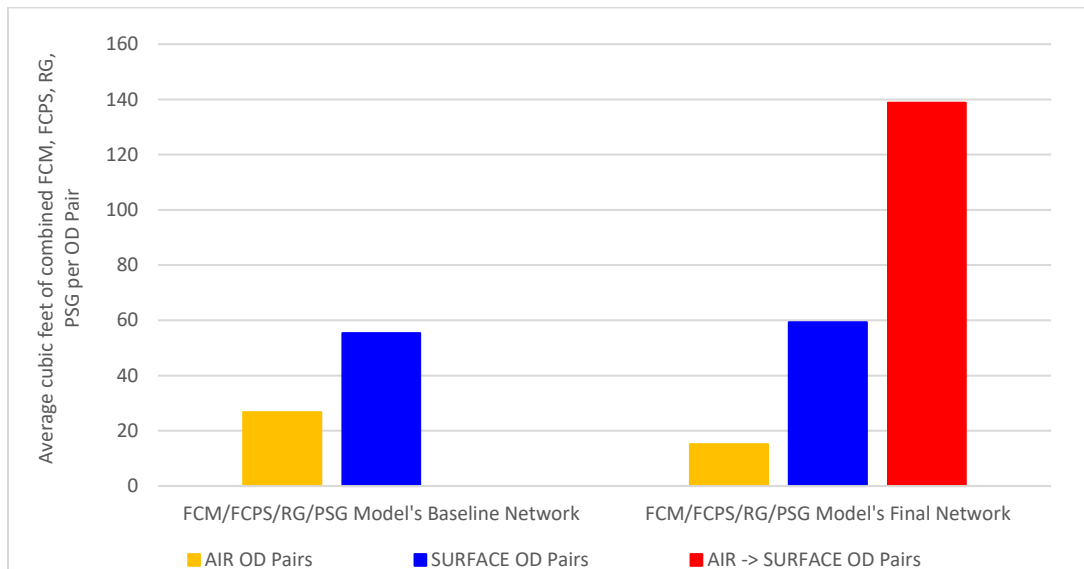
Source: Library Reference USPS-N2022-1/NP4, Excel files “Model_3.17.2022.xlsx” and “Cost Analysis.xlsx.”

Note: The cubic foot capacity data illustrated in Figure VI-2 represent data for contiguous United States.

⁷⁷ Library Reference USPS-N2022-1/NP4, Excel files “Model_3.17.2022.xlsx” and “Cost Analysis.xlsx.” For a more detailed discussion on the transportation mode impact analysis’ results, see the Non-Public Technical Appendix to this Advisory Opinion.

Combining cubic foot capacities from Figure VI-2 with number of OD pairs from Figure VI-1 provide average cubic foot density per lane. The combined data, illustrated in Figure VI-3, indicate that lane density⁷⁸ in the FCM/FCPS/RG/PSG Model’s baseline and final networks is much higher for surface lanes than it is for air lanes. The data in Figure VI-3 also suggest that the density in long-distance lanes that were determined to divert from air to surface (*i.e.*, in lanes labeled as “AIR -> SURFACE OD Pairs” in Figure VI-3) significantly surpasses both air and surface lanes’ average densities.⁷⁹

**Figure VI-3
Average Density per OD Pair in the FCM/FCPS/RG/PSG Model’s Baseline and Final Networks, by Transportation Mode Assignment**



Source: Library Reference USPS-N2022-1/NP4, Excel files “Model_3.17.2022.xlsx” and “Cost Analysis.xlsx.”

⁷⁸ Lane density referenced here is expressed as cubic feet of transported mail volume per lane.

⁷⁹ The Commission notes that it is typically the longest lanes that are assigned to air transportation to ensure mail delivery within applicable service standards and the corresponding transit windows. Docket No. N2021-1, USPS-T-3 at 5; Library Reference USPS-N2022-1/NP4, Excel files “Model_3.17.2022.xlsx” and “Cost Analysis.xlsx.”

The Postal Service's data indicate that the FCM/FCPS/RG/PSG Model's final surface transportation network, with an extended 5-day surface reach and with efficiently routed, multi-stop trips, is capable of transporting more volumes in a cost-effective manner than are transported in the current FCPS surface transportation network.

The Commission notes that the Postal Service's cost-effectiveness analysis started with a consolidation of analyzed volumes from individual surface-viable lanes into significantly fewer surface trips.⁸⁰

This consolidation of volumes from multiple lanes onto shared surface transportation increased density for the evaluated long-distance surface trips.⁸¹ However, the Commission notes that FCM business rules and CETs are not identical to the business rules for FCPS (and to proposed business rules for RG and PSG), despite all products being subject to the 2- to 5-day service standards.⁸² This could present an obstacle to the volume consolidations assumed in the Postal Service's cost-effectiveness analysis.

In addition, the volume and surface trip consolidation discussed above is based on an assumption that volumes for all four products are processed and dispatched at the same time as bundles.⁸³ However, witness testimonies do not reference FCM, and only describe RG and PSG as being added to FCPS flows, following the implementation of the proposed changes. See USPS-T-2 at 1, 5-10; see *also* USPS-T-3 at 1, 3-5. As discussed in Section VI.C.2. above, the Commission is concerned that the Postal Service's mail processing impact analysis does not estimate the impacts that additional large parcels (with RG and PSG weighing up to 70 pounds) might have on the efficiency

⁸⁰ Library Reference USPS-N2022-1/NP4, Excel files "Model_3.17.2022.xlsx" and "Cost Analysis.xlsx."

⁸¹ For a more detailed discussion on volume consolidation assumed in the Postal Service's cost-effectiveness analysis, see the Non-Public Technical Appendix to this Advisory Opinion.

⁸² USPS-T-2 at 8-9; Docket No. N2021-1, Advisory Opinion on Service Changes Associated with First-Class Mail and Periodicals, July 20, 2021, at 124-25 (Docket No. N2021-1, Advisory Opinion).

⁸³ Library Reference USPS-N2022-1/NP4, Excel file "Cost Analysis.xlsx."

of mail processing operations for small packages (with FCPS weighing up to 1 pound). The impact on FCM mail processing is also not accounted for in the Postal Service's mail processing analysis.

Moreover, to calculate surface transportation costs, the Postal Service includes trips mileage between origin P&DCs and destination STCs, rather than between origin and destination P&DCs.⁸⁴ This assumption results in the calculated costs for surface trips underestimating the costs that the Postal Service would incur transporting modeled volumes between origin and destination processing facilities.

Considering that the projected transportation mode impact analysis is based on assumptions that the Postal Service has not demonstrated it is operationally capable of achieving, the Commission is concerned that its projected transportation mode and transportation cost impacts may not materialize. Specifically, if the volume and surface trip consolidations do not materialize in the actual network, fewer potential long-distance trips would have densities that would enable cost-effective diversions from the air to the surface network. Consequently, adding RG and PSG to FCPS flows could lead to adding expensive long-distance surface trips with low-capacity utilization to the network, or it could lead to more RG and PSG volumes transported by air than anticipated.

Exceptions to the planned service standards. The data filed in the instant proceeding indicate that the Postal Service excluded certain OD pairs associated with offshore shipments from the transportation mode impact analysis.⁸⁵ The provided data do not indicate that any other shipments excepted from the service standard changes (HAZMAT and live animal shipments) were treated differently (e.g., placed on separate trips) in the Postal Service's transportation mode impact analysis. *Id.*

⁸⁴ Library Reference USPS-N2022-1/NP4, Excel file "Cost Analysis.xlsx."

⁸⁵ The Postal Service's data indicate that OD pairs, which were excluded from the transportation impact analysis, included those with either origin or destination processing facility codes from a list of offshore codes. This corresponds to offshore RG and PSG volumes being excluded from the service standard upgrade for now. USPS-T-2 at 13, 15-16; Library Reference USPS-N2022-1/NP4, Excel files "Model_3.17.2022.xlsx" and "Cost Analysis.xlsx."

The Postal Service's failure to adequately account for such shipments contributes to the Commission's concern that the assumed consolidations of all modeled volumes discussed above overly simplifies the relevant operations, which in turn renders the projected proportions of RG and PSG that will require air transportation in the future network less reliable.

Exceptions to the planned operational flow. For RG and PSG parcels that would be subject to the planned service standard changes but would deviate from the planned operational flow, the Postal Service points to "the current state of the FCPS surface transportation network," in which surface transportation may not be a cost-effective alternative to air transportation for long-distance volumes, due to low volume density in long-distance surface transportation. USPS-T-2 at 16-17.

As shown in Figure VI-2 above, the transportation mode impact analysis conducted in the instant proceeding suggests an increase in the combined capacity of FCM/FCPS/RG/PSG bundles transported in the surface network in the future state than the current FCPS surface transportation network would be capable of transporting cost-effectively. The Commission notes that the Postal Service's analysis suggests that such increases are evident for all products' volumes, including those for FCM and FCPS, that would divert to the surface network in the future state.⁸⁶

However, the Postal Service does not include the projected diversions for FCM and FCPS among the reported transportation mode impacts or calculate the associated changes in transportation costs. This is especially surprising considering the Postal Service presents the service standards upgrade proposed in the instant proceeding as based on an expected increase in long-distance lane density, potentially justifying shifting additional FCM and FCPS volumes from the air to the surface transportation network. Response to POIR No. 1, question 1.b.

⁸⁶ Library Reference USPS-N2022-1/NP4, Excel files "Model_3.17.2022.xlsx" and "Cost Analysis.xlsx."

The current state of the FCPS network and alternative interpretation of the transportation impact analysis results. The Postal Service explains that it did not calculate savings associated with the potential FCPS diversions because “some FCPS lanes are expected to remain transported by air in the near-term, due to lack of density to justify adding surface transportation at this time.” Response to POIR No. 2, question 6.d. The Postal Service states that its reported shift from commercial air to cargo (*i.e.*, FedEx Day Turn) air carrier for FCPS represents a “conservative estimate.” *Id.* question 2.a.

The Commission notes that the Postal Service’s anticipation of no change in transportation mode assignments for FCPS (and FCM) corresponds to transportation mode assignments from the FCM/FCPS/RG/PSG Model’s baseline network. The Commission reiterates that in the baseline network, all modeled products, including RG and PSG, are subject to the 2- to 5-day service standards. However, the baseline network’s surface reach corresponds to the 1- to 4-day service standards that applied to FCPS during the FY 2021.

The Commission further emphasizes that while coast-to-coast surface transportation is logistically possible within the 5-day window that would apply to all modeled products’ volumes following the implementation of the proposed service standards upgrade, the Postal Service does not currently operate such long-distance trips to transport existing long-distance First-Class volumes.

In order to add newly purchased long-distance transportation to the existing surface transportation network in a cost-effective manner (*i.e.*, in order to operate trips that enabled the air-to-surface diversions for OD pairs and the corresponding cubic foot capacities for modeled FCM, FCPS, RG, and PSG in the FCM/FCPS/RG/PSG Model’s final network), transported volumes would need to be sufficient to justify the cost of such long-haul transportation.

As illustrated in Figure VI-3 above, it is only the existing air OD pairs with high average volume densities that were determined to divert to the surface network following the addition of RG and PSG to the First-Class flows. However, it was not the

density of individual lanes that led to the determination of cost-effectiveness of surface transportation for their respective volumes, but rather the volumes consolidated from multiple long-distance lanes onto substantially fewer surface trips that constituted justifiable volume levels.

The Postal Service's conservative approach to projecting no transportation mode shifts for FCPS (and FCM) and referring to such developments as representing a near-term scenario indicates that the Postal Service anticipates the current FCPS surface transportation network, with surface trips and volume pairings responsive to the 4-day service standard, will be able to accommodate the addition of RG and PSG into FCPS flows. However, this suggests a greater need for air transportation for RG and PSG than projected. Being able to meet 5-day service standards for all products using surface transportation would therefore be a more long-term goal requiring sufficiently high volume in long-distance lanes.

The Postal Service's conservative approach to reporting modeled transportation impacts on FCM and FCPS (*i.e.*, reporting of impacts that pertain to the baseline network) additionally indicates that the percentages of RG and PSG estimated to be transported by air (28.9 percent and 15.9 percent, respectively), which result from the implementation of the optimized surface transportation network (*i.e.*, which were enabled by the FCM/FCPS/RG/PSG Model's final network), represent a more distant scenario in comparison with the near-term impacts anticipated for FCM and FCPS before such efficient network is operational.

The Commission notes that the optimized surface transportation network, first generated by the FCM Model,⁸⁷ then further enhanced by the FCM/FCPS Model,⁸⁸ was based on a transportation model using oversimplified assumptions, with reduced complexity of postal business rules, and an efficient trip structure projected to enable

⁸⁷ See generally Docket No. N2021-1, Advisory Opinion. The transportation modeling in the Docket No. N2021-1 proceeding assumed implementation of more relaxed service standards for FCM, with the service standards extended from 1 to 3 days to 2 to 5 days (FCM Model).

⁸⁸ The additional efficiency gains realized in the FCM/FCPS Model were associated with increased volume densities in long-distance lanes, enabled by a concurrent implementation of the more relaxed (2- to 5-day) service standards for both FCM and FCPS.

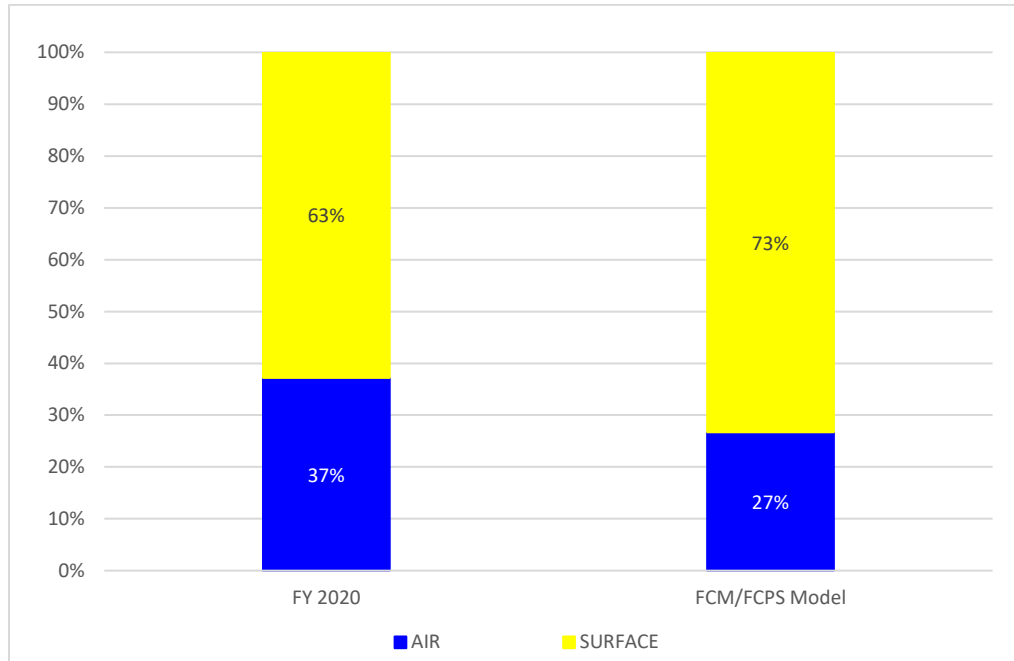
transporting the then-current surface volumes as well as volumes diverted from the air network with about half as many trips as were reported in the comparable actual surface transportation network. Docket No. N2021-2, Advisory Opinion at 4-5, 103-38; Docket No. N2021-1, Advisory Opinion at 24, 133. In the respective proceedings, the Commission opined that for this network's efficient routing and trip consolidation to materialize, its complex operations would need to be timely all along its multi-stop trips. Docket No. N2021-2, Advisory Opinion at 4-5, 103-38; Docket No. N2021-1, Advisory Opinion at 137, 143-146. However, the Postal Service had not tested whether it could achieve such operations. *Id.* The Postal Service referred to its FCM Model and its FCM/FCPS Model as directional, a "decision-supporting" rather than a "decision-making" tool," noting that the model's final network was subject to significant post-processing and refinements into routes "that can be implemented."⁸⁹

The Postal Service does not provide information on the outcome of the transportation planners' final determination on the extent of the refinements needed for modeled routes before they can be implemented into actual routes. Nevertheless, the Postal Service's transportation mode impact analysis is entirely based on volumes moving in this optimized surface transportation network. And it is this optimized network that led to the projected 28.9 percent of RG and 15.9 percent of PSG to be routed via the air network.

Figure VI-4 below shows the percentages of FCPS volumes transported by air and surface in FY 2020 next to the projected percentages of FCPS volumes in the FCM/FCPS Model.

⁸⁹ Docket No. N2021-1, Advisory Opinion at 24, 133 (internal citations omitted); Docket No. N2021-2, Advisory Opinion at 3, 23, 53, 128 (internal citations omitted).

**Figure VI-4
Percent of FCPS Volume by Transportation Mode in FY 2020 and in the
FCM/FCPS Model**



Source: Docket No. N2021-2, Library Reference USPS-LR-N2021-2/NP10, July 23, 2021, Excel file “POIR No.4 Q18 Final.xlsx.”

Note: The volume data illustrated in Figure VI-4 represent data for contiguous and non-contiguous United States.

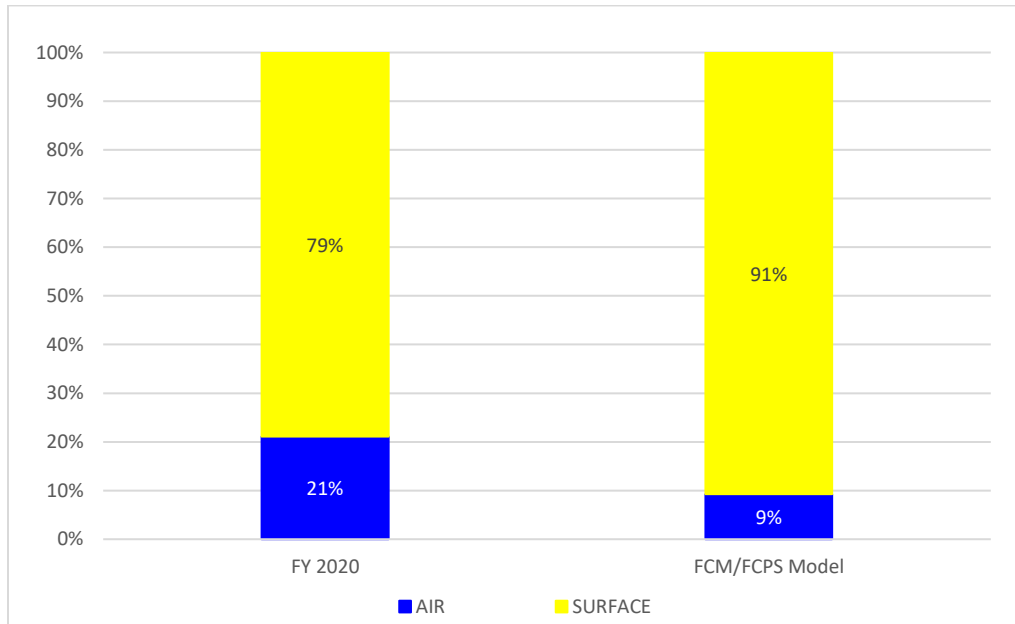
The Postal Service’s analysis suggests that substantial air-to-surface volume shifts have taken place during FY 2021, with the actual FY 2021 FCPS volumes transported in the surface network being very similar to those projected from the concurrent implementation of the FCM and FCPS service standards, and a concomitant implementation of the optimized surface transportation network.

Further, the FCM/FCPS/RG/PSG Model indicates additional potential for air-to-surface volume shifts for FCPS which, as discussed earlier, the Postal Service does not anticipate to materialize in the near term.⁹⁰

⁹⁰ For a more detailed discussion on the transportation mode impact analysis’ suggested results for FCPS, see the Non-Public Technical Appendix to this Advisory Opinion.

Figure VI-5 below shows the percentages of FCM volumes transported by air and surface in FY 2020 next to such volume projections from the FCM/FCPS Model.

Figure VI-5
Percent of FCM Volume by Transportation Mode in FY 2020 and in the FCM/FCPS Model



Source: Docket No. N2021-1, Library Reference USPS-LR-N2021-1/3, April 21, 2021, Excel file “3_SSD_5D_Vol_Impacts_CONUS.xlsx;” Docket No. N2021-2, Library Reference USPS-LR-N2021-2/NP10, Excel file “POIR No.4 Q18 Final.xlsx.”

Note: The volume data illustrated in Figure VI-5 represent data for contiguous and non-contiguous United States.

As shown in Figure VI-5 above, significant volume shifts to the surface network were anticipated from the concurrent implementation of the more relaxed service standards for FCM and FCPS, from the product's FY 2020 levels.

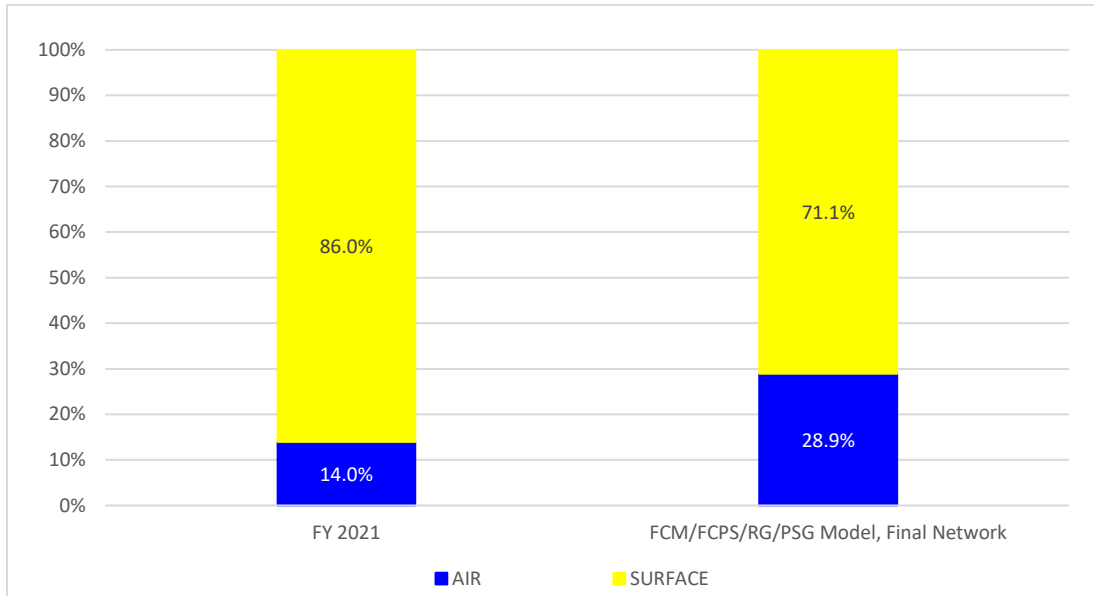
The transportation mode impact analysis conducted in the instant proceeding suggests sizeable air-to-surface volume shift potential for FCM between the current state FCPS network and the proposed new operational flow, which the Postal Service does not include among the projected transportation efficiencies enabled by the instant proposal. However, the Commission notes that the transportation mode assignments generated from the FCM/FCPS/RG/PSG Model do not represent improvements compared to the 9 percent of FCM volume that the FCM/FCPS Model enabled.⁹¹

Considering the Postal Service's conservative approach to the reporting of the transportation mode impacts suggested by its analysis for FCM and FCPS, the Commission examines the similarly near-term impacts of the instant proposal, resulting from the FCM/FCPS/RG/PSG Model's baseline network, for RG and PSG.

Figure VI-6 below illustrates transportation mode assignment for RG for FY 2021 (when the product was transported in the NDC network), and those determined in the final network of the FCM/FCPS/RG/PSG Model.

⁹¹ For a more detailed discussion on the transportation mode impact analysis' suggested results for FCM, see the Non-Public Technical Appendix to this Advisory Opinion.

**Figure VI-6
Percent of RG Volume by Transportation Mode in FY 2021 and in the
FCM/FCPS/RG/PSG Model’s Final Network**



Source: Library Reference USPS-N2022-1/NP3, Excel file “RG.PSG.FCPS.Cost.Impact.nonpublic.revised.04.15.2022.xlsx;” Library Reference USPS-N2022-1/NP4, Excel file “Model NASS Pairs with Final Mode Assignment.xlsx.”

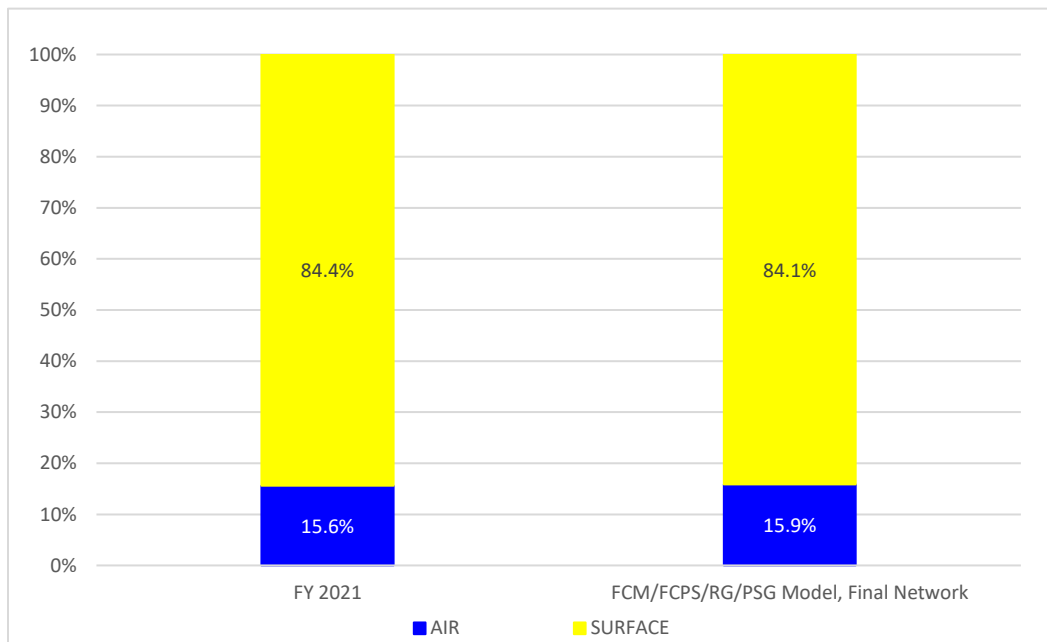
Note: The volume data illustrated in Figure VI-6 represent data for contiguous and non-contiguous United States.

The data underlying Figure VI-6 suggest that the implementation of the enhanced service standards for RG, and a concurrent implementation of the efficiently routed surface transportation network, is estimated to double RG volumes transported by air from their current (FY 2021) levels. The Commission notes that the transportation mode impact analysis suggests that prior to the full implementation of the optimized surface network and continued operation of the current FCPS transportation network (*i.e.*, the same network in which the Postal Service anticipates no additional FCPS volume diversions in the near term), the anticipated percentage of RG volume that

would require air transportation to meet the upgraded service standards would be higher than 28.9 percent.⁹²

Similar presentation for PSG volume is included in Figure VI-7 below.

Figure VI-7
Percent of PSG Volume by Transportation Mode in FY 2021 and in the FCM/FCPS/RG/PSG Model’s Final Network



Source: Library Reference USPS-N2022-1/NP3, Excel file “RG.PSG.FCPS.Cost.Impact.nonpublic.revised.04.15.2022.xlsx;” Library Reference USPS-N2022-1/NP4, Excel file “Model NASS Pairs with Final Mode Assignment.xlsx.”

Note: The volume data illustrated in Figure VI-7 represent data for contiguous and non-contiguous United States.

⁹² For a more detailed discussion on the transportation mode impact analysis’ suggested results for RG, anticipated prior to the full implementation of the FCM/FCPS/RG/PSG Model’s final network, see the Non-Public Technical Appendix to this Advisory Opinion.

Figure VI-7 illustrates that the implementation of the enhanced service standards for PSG, along with a concurrent implementation of the optimized surface transportation network, is estimated to result in less than 1 percentage point increase in PSG volumes routed via the air network, from their current (FY 2021) levels. However, the transportation mode impact analysis also suggests that prior to the full implementation of the optimized surface network and assuming continued operation of the current FCPS transportation network in the near term, the percentage of PSG volumes that would actually require air transportation to meet the upgraded service standards would be a few percentage points higher.⁹³

A more detailed discussion of transportation mode impacts that resulted from the FCM/FCPS/RG/PSG Model's baseline and final networks is included in the Non-Public Technical Appendix to this Advisory Opinion.

b. Transportation Cost Impact Analysis

The Postal Service calculates cost changes associated with transportation impacts for RG, PSG, and FCPS, but not for FCM. The calculated cost impacts for RG and PSG represent transportation cost changes between FY 2021, when RG and PSG moved in the NDC network, and a future time, when the upgraded service standards for RG and PSG are implemented and the Postal Service operates an efficiently routed surface transportation network. The calculated cost impacts for FCPS represent transportation cost changes between FY 2021 and a time period immediately following the implementation of the 2- to 5-day service standards for RG and PSG, prior to the full implementation of the efficiently routed surface transportation network. Response to POIR No. 2, question 6.d.

⁹³ For a more detailed discussion on the transportation mode impact analysis' suggested results for PSG, anticipated prior to the full implementation of the FCM/FCPS/RG/PSG Model's final network, see the Non-Public Technical Appendix to this Advisory Opinion.

The Commission notes that the calculated transportation cost changes are based on numerous assumptions and inputs, several of which might render the calculated cost changes unrealistic.⁹⁴ The Commission examines these assumptions below.

Additional capacity for large parcels added to small package FCPS flows. The Commission's analysis of the data used in the Postal Service's transportation mode impact analysis suggests that while the instant proposal would add only a small number of large parcels to FCPS flows, the corresponding space they would take up would be disproportionately larger, particularly for RG.⁹⁵

The Postal Service incurs costs for purchased FedEx Day Turn air transportation on the basis of cubic foot capacity of transported mail volumes. As discussed earlier, should more of the RG and PSG volumes require air transportation before the eventual implementation of the optimized surface transportation, and before the volume in long-distance lanes grows to sufficient levels to justify additional lanes diverted to the surface network, the Postal Service will incur cost increases for FedEx Day Turn transportation that are not accounted for in the estimated transportation cost changes for RG, PSG, and FCPS.

Air transportation costs change proportionally with changes in mail capacity flown, surface transportation costs do not. The Postal Service presents the estimated reduction in transportation costs for RG and PSG (\$4.6 million and \$0.1 million, respectively) as associated with surface to FedEx Day Turn air transportation shifts for RG and PSG volumes. USPS-T-3 at 6. The Postal Service calculates these cost reductions as the differences in the current (FY 2021) unit transportation costs

⁹⁴ During the course of this proceeding, the Postal Service revised the estimated changes in transportation costs projected from the implementation of the instant proposal. The revision was related to an inadequate current-state unit cost assumption used in the Postal Service's analysis, which led to the originally included \$27 million cost increase being revised to an estimated \$36 million cost increase. This revision in turn resulted in the originally included \$5 million in savings on mail processing and transportation being revised to an estimated \$5 million increase in mail processing and transportation costs. See Notice of Revisions to Testimony; Notice of Revisions to Library References. See also Library Reference USPS-N2022-1/1 (as revised on April 15, 2022).

⁹⁵ Library Reference USPS-N2022-1/NP4, Excel files "Model_3.17.2022.xlsx" and "Mode List and Tables for 1.15.22 to 2.25.22 RG-PSG volumes.xlsx."

multiplied by the 14.9 percent of RG and the 0.3 percent of PSG volumes that will be shifting to FedEx Day Turn air carrier.

Since the Postal Service incurs costs for FedEx Day Turn service on the basis of cubic foot capacity flown, the future-state unit transportation costs for the shifting RG and PSG volumes are based on average FY 2021 cost per cubic foot for this carrier as well as average cubic feet per RG and PSG pieces. As for the current-state, the Postal Service assumes FY 2021 high-zone PSG costs per cubic foot as representative of current-state costs incurred on the shifting RG and PSG volumes.⁹⁶

The Commission notes that while it is reasonable to calculate changes in air transportation costs as proportional to changes in cubic foot capacities flown, assuming a proportional relationship between surface transportation costs and changes in mail volumes transported in the surface network might not be realistic.⁹⁷

The Postal Service confirms that diverting RG and PSG volumes from the NDC network would lead to lower levels of capacity utilization on affected trips and adds that “if capacity utilization levels decline significantly” in trucks transporting volumes excepted from service standard upgrade (HAZMAT, live animal shipments, offshore shipments), “redundant trips could be eliminated.” Response to POIR No. 5, question 1.b. However, the Commission finds that eliminating trips in the complex transportation network in which the Postal Service operates is unlikely. The Postal Service explains that its transportation operations involve multiple parameters and serve multiple products, and transportation mode assignment decisions in lanes are made daily, with products from distinct networks transported jointly, within the same network (such as high-zone PSG and PM sharing air transportation) at times. *Id.* This leads to the Commission’s expectation that while the Postal Service will incur costs for transporting

⁹⁶ Library Reference USPS-N2022-1/NP3, Excel file “RG.PSG.FCPS.Cost.Impact.nonpublic.revised.04.15.2022.xlsx.”

⁹⁷ The relationship between changes in transportation costs and changes in transported volumes is expressed through volume variability factors. More specifically, while volume variability factors for incurred air transportation costs are equal to 1.0, expenses incurred on contracted highway transportation have variability factors lower than 1.0. See, e.g., Docket No. ACR2021, Library Reference USPS-FY21-32, December 29, 2021, Excel file “CS14-Public-FY21.xlsx.”

RG and PSG via FedEx Day Turn that are proportional to the additional RG and PSG cubic foot capacity flown via this cargo air carrier in the future state, the Commission does not anticipate that removing RG and PSG volumes out of the NDC network would lead to savings on surface transportation that correspond to the cubic foot capacity of RG and PSG removed from the network.

The Commission notes the pervasive underutilization of surface transportation capacity in the current operating environment. This is evidenced in annual surface transportation cost increases even as mail volumes decline.⁹⁸ Therefore, the Commission finds that the Postal Service's reasoning of RG and PSG volumes constituting too small of a percentage of the packages shipped in its network to result in significant cost changes is not supported by the record in this proceeding.

As the Postal Service points out, it is the factors beyond mail volumes, associated with operational challenges in the processing, transportation, and delivery networks, including staffing availability issues, that lead to inefficient and costly operations, including transportation operations. See *generally* Postal Service Strategic Plan. Adding some of the RG and PSG parcels to FCPS flows, while keeping others in NDC flows, with a possibility of continued depositing of PSG and FCPS flows at origin NDCs, might not simplify operations to the point of trip reduction, and could increase the complexity of both mail processing and transportation operations enough to add trips to the network, which is not accounted for in the Postal Service's transportation cost change estimate.

Consequently, the Commission finds that the transportation cost savings that the Postal Service expects to realize from RG and PSG volumes moving out of the NDC network represent unrealistic expectations.

Furthermore, it is unclear how the implementation of the optimized surface network, combined with transportation mode assignments for February 2022, and

⁹⁸ For example, total accrued highway transportation costs increased 55 percent between FY 2014 and FY 2021, while overall mail volumes declined. See Docket No. ACR2014, Library Reference USPS-FY14-32, December 29, 2014, Excel file "CS14.xlsx." See also Docket No. ACR2021, Library Reference USPS-FY21-32, Excel file "CS14-Public-FY21.xlsx;" Postal Service Strategic Plan at 9-10.

modeled products' daily volumes pertaining to two distinct time periods, 1 calendar year apart, affected the estimated shifts in transportation modes and the calculated changes in transportation costs.⁹⁹ The Postal Service describes day-to-day volume fluctuations where high-zone deferred service products like RG and PSG are transported jointly with PM via air transportation, and explains that the transportation mode assignment decision-making process is conducted for each individual lane. April 15 Response to POIR No. 3, question 5.a., 5.b.; Response to POIR No. 5, questions 1.b., 2. This indicates that the misaligned time periods to which the modeled products' volumes pertain, and the period to which the FCPS transportation mode matrix used in the transportation mode impact analysis pertains, may have affected the projections in a meaningful way.

The Commission is not able to quantify the magnitude of any such potential impact. This is partly due to the lack of data that the Postal Service relies on as inputs for its analyses. Additionally, any attempt to produce estimates that represent potentially more accurate or more adequate alternatives to the Postal Service's projections would need to follow the exact methodology employed by the Postal Service when producing its projections, which is not detailed in the supporting materials filed in this proceeding.

The transportation mode shifts estimated in the instant proceeding are based on transporting combined RG, PSG, FCPS, and FCM volumes in lanes. See Section VI.C.2.a., *infra*. However, as noted earlier, the Postal Service only refers to combined RG, PSG, and FCPS flows in the provided documentation and POIR responses, and it reports on mode shifts for RG, PSG, and FCPS but not for FCM. It is unclear whether the Postal Service will bundle the parcel products' volumes with FCM on expensive cargo transportation. The cost impact of such possible operations is not included in the transportation cost change estimates.

⁹⁹ The documentation filed in the instant docket indicates that the Postal Service combined average daily RG and PSG volumes for January to February of 2022, with average daily FCM and FCPS volumes used in the transportation mode impact analysis pertaining to March 2021. Library Reference USPS-N2022-1/NP4 Preface; April 15 Response to POIR No. 3, question 18.b.

Lastly, the transportation cost changes associated with the reported shifts in transportation mode assignments assume unit costs in both the current and future operational flow that pertain to FY 2021 and do not account for potential increases in the cost of fuel, purchased air transportation, contracted highway transportation costs, inflationary pressures, or any other market developments.

c. Anticipated Impact of Future Volumes on the Transportation Network Efficiencies and Costs

The Postal Service acknowledges that while the improved service standards for RG and PSG “might be expected to increase costs,” the Postal Service also points to their operational implementation as having “potential sources of cost efficiencies.” USPS-T-3 at 1. When comparing the estimated efficiency gains and cost impacts from the FCM/FCPS Model and from the FCM/FCPS/RG/PSG Model, the Postal Service describes the former as aimed at reducing dependency on air transportation and costs, while it describes the instant proposal as intended to enhance service to customers sending large packages, with some efficiency gains anticipated instantly, and others over time. April 15 Response to POIR No. 3, question 13.b., 13.c. Among those more distant benefits, the Postal Service lists improved ability to move more volume to the surface network, to the point of “vast preponderance” of RG and PSG transported via the surface network, better utilized surface transportation network capacity, and cost reduction. *Id.*

For cost-effective long-distance volume shifts to the surface network to materialize, the growth in overall large parcel volumes¹⁰⁰ that the Postal Service counts on would not be sufficient. Rather, it is the sufficiently large volume density in long-distance lanes that would be required. In the meantime, and particularly due to the planned bundling of RG, PSG, and FCPS parcels, the Commission is concerned that the Postal Service might see increased dependency on expensive air cargo transportation.

¹⁰⁰ Response to POIR No. 1, question 6.c.; Response to POIR No. 2, question 1.a.ii., 1.b.

The Postal Service has faced declines in FCM volumes and increases in the number of delivery points over the past decade or more. See Postal Service Strategic Plan at 8-9. The Postal Service explains that FCM volume has provided “the greatest contribution” for maintaining its universal service network. *Id.* at 9. The Postal Service OIG describes growth in ecommerce packages as being “critical to filling the gap left by the decline in letter mail.” OIG Report No. RISC-WP-20-008 at 3.

However, the Postal Service faces competition in the package delivery market, which constrains its ability to increase prices without losing market share. *Id.* at 1, 8; Postal Service Strategic Plan at 10. In order to offset revenue loss from FCM volume decline, while maintaining low prices for a more expeditious service for parcel products (as the Postal Service proposes in the instant proceeding for RG and PSG), the Postal Service “must also maximize the profitability...or contribution” by improving the efficiency of its operations. OIG Report No. RISC-WP-20-008 at 3, 8.

Profitability, however, is “not uniform across the Postal Service’s delivery network.” *Id.* at 3. The Postal Service’s competitors “use sophisticated routing systems” to capture the most efficient deliveries for themselves, while resorting to the Postal Service for the less efficient deliveries. *Id.* at 3, 8. The Postal Service OIG has reported that the Postal Service “is under threat,” particularly in package delivery to high-density areas, with only package delivery to low-density areas remaining strong in recent years. *Id.* at 1, 8. However, due to operational challenges and lower volume density, package deliveries to low-density areas also have the lowest profit margins. *Id.* at 1.

In addition, the Postal Service OIG has reported an increase in big, heavy, oddly shaped, and hard-to-handle parcels delivered by the Postal Service in recent years, with some portion likely exceeding the respective products’ maximum size and weight limits. *Id.* at 14.

In the instant proceeding, the Postal Service proposes to expedite service for RG and PSG while keeping prices low. See, e.g., Response to POIR No. 2, question 5.

The Postal Service anticipates this proposal to attract new, contribution-positive parcel volumes in the long term.

However, the transportation impact analysis discussed in previous sections suggests that with the current size, weight, and distance profiles for modeled volumes, and with an optimally routed, efficiently operating surface network in place, the current proposal would result in increased transportation expenses.

Should the enhanced service for RG and PSG attract parcels with lower profit margins, such as parcels to low-density areas where the Postal Service faces less competition, or hard-to-handle, heavy, oversized parcels, which the Postal Service delivers at prices that are attractive to price-conscious shippers, providing faster service for RG and PSG at unchanged prices may not result in the growth of contribution-positive volume.

In conclusion, the Commission emphasizes that in order to maintain low prices and assure profitability, the Postal Service's ability to reduce costs, through improvements in the efficiency of its operations, is essential. See April 15 Response to POIR No. 3, question 13.b., 13.c.; OIG Report No. RISC-WP-20-008 at 3.

The Postal Service describes recent trends in the market for commercial packages, with retailers relocating inventories closer to population centers. USPS-T-1 at 8. The Postal Service observes that this leads to an increasing need for short-distance ground transportation, as well as a lesser need for expedited long-haul shipments, and contends that these developments are well-suited for more expedited (*i.e.*, subject to shortened service standards) RG and PSG parcels. *Id.*

The Commission notes that the two parcel products under consideration show different distance profiles, as evidenced by RG volume estimated to travel by air being more than double the volume currently traveling by air, while for PSG, such increase in air volume is estimated to be less than 2 percent.¹⁰¹ This is further evidenced by the 47 percent of PSG volume within the contiguous United States that would be subject to the

¹⁰¹ USPS-T-2 at 17; Library Reference USPS-N2022-1/NP3, Excel file "RG.PSG.FCPS.Cost.Impact.nonpublic.revised.04.15.2022.xlsx."

2-day service standard (*i.e.*, within about 372 miles of origin P&DC), while only 21 percent of RG would be subject to the 2-day service standard.¹⁰²

RG is a retail product, while PSG is a commercial product. The anticipated continued increase in short-distance ground transportation is more likely applicable to PSG. USPS-T-2 at 17. If the recent trend of commercial parcel volumes originating closer to customers continues, it may be difficult to reach the long-distance lane density needed for the expected eclipse of the air transportation to take place over time. *Id.*

One of the Postal Service's expectations is that the demand for the expedited service for long-haul shipments would decrease, which would further improve volume density in long-distance surface lanes. Response to POIR No. 2, question 1.a. Such expectation may not be realistic considering increasing competition for retail purchases, and the associated shifts in customers' expectations of a faster (same day or next day), and not slower, delivery. See OIG Report No. RISC-WP-20-008 at 9.

The Commission notes that the Postal Service proposes to add large parcel RG and PSG volumes to the network that serves priority products, subject to shorter service standards, and shorter operating windows, with more expedited service.

This network (inter-SCF) has experienced significantly higher cost increases over the last several years than the NDC network has. Specifically, accrued inter-NDC highway transportation costs increased about 5 percent between FY 2017 and FY 2021, while for inter-SCF network, the highway transportation costs increased 57 percent over the same time period.¹⁰³ In the last fiscal year alone (*i.e.*, between FY 2020 and FY 2021), inter-SCF highway transportation costs increased 32 percent.¹⁰⁴

¹⁰² Library Reference USPS-N2022-1/NP4, Excel file "RG-PSG Service Standards Change to FCP - Contiguous Only.xlsx."

¹⁰³ Docket No. ACR2017, Library Reference USPS-FY17-32, December 29, 2017, Excel file "CS14-Public-FY17.xlsx;" Docket No. ACR2021, Library Reference USPS-FY21-32, Excel file "CS14-Public-FY21.xlsx."

¹⁰⁴ Docket No. ACR2020, Library Reference USPS-FY20-32, December 29, 2020, Excel file "CS14-Public-FY20.xlsx;" Docket No. ACR2021, Library Reference USPS-FY21-32, Excel file "CS14-Public-FY21.xlsx."

The Postal Service explains these cost increases as resulting from a combination of factors, listing lack of air capacity and market forces that led to surface transportation cost increases. Response to POIR No. 2, question 3.a. The Postal Service describes that the air capacity shortages led to volume shifts to the surface network, or to more expensive charter flights. *Id.* For the volumes shifting to surface, the Postal Service describes increases in miles driven and significant increases in costs per mile for contracted highway transportation due to the national shortage of truck drivers.¹⁰⁵

As noted in Section VI.C.2.a., above, the analysis of the current FCPS transportation network indicates diversions of FCPS volumes from the air to the surface network in FY 2021, with diversions for FCM less notable. These air-to-surface shifts were, however, not accompanied by cost reductions as past proceedings indicated that relaxing of service standards and extending of FCM and FCPS operating windows would enable. See *generally* Docket No. N2021-1, Advisory Opinion; Docket No. N2021-2, Advisory Opinion.

The 32 percent increase in inter-SCF highway transportation costs could indicate that the trips were added to the network, and the available surface capacity was not used to the extent possible.

In addition, the significant cost increases associated with the national truck driver shortages could lead to ever-increasing volume thresholds that would constitute levels sufficient enough to justify adding long-distance trips to the network and reduce reliance on air transportation. The Postal Service describes the importance of the developments in surface transportation costs relative to the developments in air transportation costs and acknowledges that the dynamic effects of the prospective future volumes and market changes were not incorporated in the cost impact estimates presented in the instant docket. Response to POIR No. 5, question 6.b.; Response to POIR No. 5, question 2. The Commission notes that such effects need to be accounted for and

¹⁰⁵ *Id.*; see United States Postal Service, Office of Inspector General, OIG Report No. RISC-WP-22-002, The Truck Driver Shortage: Implications for the Postal Service, March 7, 2022, at 4 (OIG Report No. RISC-WP-22-002).

underscore the need for a thorough market research prior to the implementation of this proposal, to ensure increase of contribution-positive volume.

3. Conclusion

The Commission notes that the Postal Service's POIR responses indicate that the Postal Service monitors surface transportation capacity utilization rates, transportation mode assignments for product volumes, and surface network mileages. Response to POIR No. 2, question 3.c. The Commission recommends that the Postal Service rely on its available data sources and account for the complexity of its operations¹⁰⁶ in all future nature of service proceedings to help ensure that any proposed changes do not have unintended consequences on the efficiency of its operations, accrued costs, and contribution from products.

The Commission finds the incremental implementation of the numerous planned changes indicated in the Postal Service's 10-year plan provides the opportunity to evaluate the impacts of past changes, already implemented. Such an exercise would enable the Postal Service to evaluate the robustness of the assumptions used to project the impacts of past proposals, for which outcomes can already be observed, measured, evaluated against projections. Further, the results of such analysis and review may be used to further refine future planned changes to the postal network. Consequently, the Commission recommends that the Postal Service monitor the impacts of all nationwide changes implemented to date and use these data to refine any planned future proposals so that the data enhance the Postal Service's intended goals of financial sustainability and service excellence.

Finally, the Commission recommends that the Postal Service conduct a more robust market research analysis prior to the implementation of the enhanced service standards for RG and PSG, with the goal of ensuring that the weight, capacity, and distance profiles of future large parcel volumes, which the enhanced service standard

¹⁰⁶ The Postal Service acknowledges the complex nature of its network, listing multiple factors affecting its operations, including changes in volumes, transportation mode shifts, new processing nodes, fluctuations in daily volumes, transportation mode decision-making at the individual lane level, to name a few. Response to POIR No. 2, question 3.c.; Response to POIR No. 5, question 2.

upgrade for RG and PSG might attract, do not lead to increases in high-cost and low-contribution volumes, and potentially undermine the Postal Service's goal of financial sustainability.

E. Market Demand/Research Analysis

1. Overview

The Postal Service claims that the fundamental rationale for the proposed service standard changes for RG and PSG is to enhance service to customers sending packages weighing more than 1 pound and up to 70 pounds without increasing prices. USPS-T-1 at 1-2, 13. The Postal Service asserts that the improvement in service standards for RG and PSG will enable the Postal Service to meet market demand for a "low-price, medium-speed"¹⁰⁷ ground transportation product for shipping packages with competitive pricing and improved reliability in meeting service expectations. *Id.* at 2. Additionally, witness Jarboe suggests that by improving service speed through the proposed service standard changes for RG and PSG, the Postal Service may gain market share in this consistently growing business segment. *Id.* at 13. Witness Jarboe considers the potential impact on other Postal Service products, specifically volume diversion from the "medium-speed, medium-price" PM but maintains that other service enhancements would differentiate PM from the enhanced RG-PSG. *Id.* at 11. The question remains open as to whether the proposed service standard change will help the Postal Service increase its market share by diverting package volume from its competitors or cannibalizing its own "medium-speed" and higher priced product, PM.

¹⁰⁷ In its Response to POIR No. 1, question 5.b., the Postal Service defines the term, "low-price" as a price less than published parcels destined to zone 2, 1LB (net minimum) charge for pound-rated competitive parcels. The Postal Service defines the term, "medium-price" as prices that are associated with more expedited products and the term, "high-price" as prices that are associated with express products.

2. Commission Analysis

Using witness testimony, library references, and OIG reports, the Commission considers the competitive marketplace in which the RG-PSG products are offered and contemplates whether enhancing the service of RG-PSG will help the Postal Service meet market demand. The Commission evaluates whether the market research provided by the Postal Service demonstrates that the proposed service standard changes will attract more potential RG-PSG customers and whether this research sheds light upon the impact on shipping options in the competitive parcels market. Finally, the Commission evaluates the Postal Service's potential impact on other Postal Service products.

a. Enhancing Service and Meeting Market Demand

The postal products predominantly used for the shipping of greater-than-1-pound parcels are RG, PSG, and PM. USPS-T-1 at 1, 8. RG is a “low-speed, low-price” ground shipping option for retail (single-piece) customers for packages, thick envelopes, and tubes weighing less than 70 pounds and up to 130 inches combined length and girth. *Id.* at 9. PSG is similar to RG but unlike RG, PSG is targeted at commercial shippers and allows for initial entry of packages into the mail flow at downstream P&DCs. *Id.* at 2. PM is a “medium-speed, medium-price” shipping option for retail and commercial customers with a 1- to 3-day service standard and offers enhanced features such as flat-rate pricing and insurance. *Id.* at 11. The Postal Service notes that prior to January 2022, RG-PSG were priced similarly to PM, despite being a slower speed shipping option. *Id.* at 8. The Postal Service also offers the “medium-speed, low-price” FCPS product as a shipping option for retail and commercial customers shipping lightweight (less-than-1-pound) packages. The Postal Service notes that it has no similar shipping option for large packages in the “medium-speed, low-price” market sector. *Id.*

The Postal Service retained CG and BCG for its market research. *Id.* at 6. CG demonstrated that the Postal Service and its competitors saw large volume growth in package demand driven primarily by growth in volume of ground shipments. Comparing

FY 2021 to FY 2017, CG found that the package shipping market experienced a 14 percent compound annual growth rate (CAGR) in total volume. This was driven by a 15 percent CAGR in packages transported by ground during the same time frame, during which there was just a 9 percent CAGR in packages transported by air. *Id.* at 7. The main conclusion from CG's market research is that the market for ground shipping service was large and growing. *Id.*

In addition, BCG conducted a survey of potential RG-PSG customers that include shipping industry leaders, logistics experts, mid-market shippers, and e-commerce shipping decision-makers to evaluate their shipping prioritization of service, features, and price.¹⁰⁸ The BCG Survey results suggest that increased package delivery speed is a top priority for customers considering their shipping options in the package shipping market. USPS-T-1 at 7. The BCG Survey also found that given retailers' expectation of continued growth in e-commerce, retailers will continue to move their inventories closer to population centers, thus shrinking demand for expedited, long-haul shipments and increasing demand for short distance and economical ground shipping options. *Id.* at 8.

The OIG report, "Package Delivery in Rural and Dense Urban Areas," appears to corroborate the Postal Service's claims about the market underlying its planned changes to enhance service for customers sending larger packages. OIG Report RISC-WP-20-008 at 14-15. The OIG report indicates that the Postal Service faces increased competition in medium- and high-density areas and that its package growth remained strong (in FY 2019) only in low-density parts of the country. *Id.* at 14. The proposed service standard changes could increase the unmet (less competitive) market demand for parcel shipping in low-density areas. Whether the Postal Service can meet the increase in demand in low-density areas with faster speeds at low prices without loss of

¹⁰⁸ *Id.* The Postal Service filed an Excel workbook showing a portion of the results of the survey conducted by BCG in Library Reference USPS-LR-N2022-1-NP2, titled, "BCG Survey Output Request.xlsx." In the Preface to Library Reference USPS-LR-N2022-1-NP2, the survey was titled, "Commercial Shipper Survey." In the April 15 Response to POIR No. 3, question 4.e., the Postal Service filed an Excel workbook titled, "SMB Survey Output Request.xlsx" to include all of the responses to the BCG survey questions. The Commission will refer to the survey conducted by BCG as "BCG Survey."

contribution remains unexamined, especially if the postal network becomes the dumping ground of bulky, difficult-to-deliver packages as described above. *Id.*

In conclusion, the Postal Service contends that package volume will continue to grow and the demand for speed at “low price” is the top priority for shipping decision-makers. The Postal Service aims to meet the growing demand for short-distance and economical parcel shipping service by enhancing RG-PSG without increasing price, believing that this will help grow its market share in the large package shipping market. USPS-T-1 at 7. However, the Postal Service’s expectations may be overly optimistic as it did not appear to consider the potential impact of attracting additional, less-compensatory package volume in low-density areas from price-conscious shippers. Moreover, while the Postal Service’s market research findings suggest that the volume of ground shipments is growing, the Postal Service’s proposed changes will shift more RG-PSG to air transportation in the immediate future. Although the Postal Service expects the shift to air transportation to be temporary and plans to revert to ground transportation once they achieve sufficient volume to justify long-distance surface transportation, the Postal Service does not provide a time frame for when their plan will be realized.

b. Projected Market Impact

The BCG Survey results show that there is existing demand for increased package delivery speed. *Id.* The survey also indicates that retailers expect continued growth in e-commerce spurred from the pandemic, thus driving retailers to continue expanding their Business-to-Consumer (B2C) business models and to relocate inventory closer to population centers. *Id.* at 8. The Postal Service suggests that the BCG Survey’s findings demonstrate “less need for expedited, long-haul shipments and an increasing need for short distance, less-expensive ground transportation.” *Id.* The Postal Service asserts that the enhanced RG-PSG will be “well-suited” to meet the shift in demand. *Id.*

The Commission commends the Postal Service for retaining a third-party expert to conduct the BCG Survey and for its efforts to include meaningful portions of its

potential customer base via directly sampling those shippers that may be attracted by the proposed service standard changes. In addition, the Commission acknowledges that the BCG Survey was stratified to encompass small- and medium-sized business commercial shippers of various industries. Small- and medium-sized businesses are among the target customers that may consider RG-PSG as an attractive shipping option once it is enhanced by the proposed service standard changes.

While the Commission recognizes BCG's representation of potential commercial customers, specifically small- and medium-sized businesses, it also identifies several technical areas of concern relating to the survey. First, the Postal Service notes that the survey sample comprised of shipping industry leaders, logistics experts, mid-market shippers, and an online survey of commercial e-commerce business shipping decision-makers; but the Postal Service does not provide information pertaining to why these sources were combined, why large-sized businesses and individuals were excluded, and whether there may have been selection bias in the respondents chosen for the survey. *Id.* at 7.

Second, with respect to the potential representativeness and validity of the BCG Survey, the BCG Survey responses only reflect the views of small- and medium-sized business commercial mailers, not addressing the views of retail (individual) mailers, large-sized business commercial mailers, existing RG-PSG shippers, and other stakeholders such as the recipients of RG-PSG (discussed in more detail below). Third, mailers who are price-insensitive and strictly prioritize speed in their shipping decision-making or, conversely, those who are strictly price-sensitive and do not prioritize speed in their shipping decision-making were not represented in the BCG Survey. See Revised Library Reference USPS-LR-N2022-1/NP10, question 4.b.ii.

The Commission understands that developing a survey that is fully representative is challenging because the user base of PSG-RG is small, and it recognizes that the objective of the BCG Survey is to evaluate the shipping decision-making process of shippers who currently do not view RG-PSG as shipping options that meet their needs.

Another shortcoming of the BCG Survey is that it appears to ignore the recipient side of volume demand. The BCG Survey poses questions to determine how commercial shippers prioritize speed and price.¹⁰⁹ However, an important driver of shippers' decisions is the preference of the recipient. It makes sense that recipients in many cases will drive the choice of shipping because two of the Postal Service's main customer segments for RG-PSG are retailers and online marketplaces. These customer segments have an end-customer (recipient) that in many cases can indicate directly to the business shipper the desired type of shipment; for instance, the business fulfilling the order may present options for speed of delivery (along with the corresponding pricing) to the recipient at the time of making the transaction. See Revised Library Reference USPS-LR-N2022-1/NP10, question 4.c.

Package recipients care about the price and speed of service they receive from the Postal Service. The upgraded service standards proposed by the Postal Service may cause some recipients to value PM less and opt for other shipping services, whether they be RG-PSG or those offered by a competitor. On the other hand, recipients that value speed over price may still not see PSG-RG as fast enough. "Speed" and "price" as referenced by the BCG Survey were asked in the specific context of shipping decision-making, and the survey findings reveal some level of interest in a "low-price, medium-speed" package delivery product among small-business mailers. See Library Reference USPS-LR-N2022-1/NP2.

"Speed" and "price" are observed to be the top drivers of shipper decision-making according to the BCG Survey. See Library Reference USPS-LR-N2022-1-NP2. However, a substantial portion of respondents say their customers expect packages to arrive in 3 days. See Revised Library Reference USPS-LR-N2022-1/NP10, question 4.e. Despite the enhanced service standard change of RG-PSG from 2- to 8-day standard to a 2- to 5-day standard, respondents who filter shipping speed for 3 days or less may still not choose RG-PSG as their preferred shipping option if it falls into the 4-

¹⁰⁹ See Library Reference USPS-LR-N2022-1/NP15, April 25, 2022, question 4.

or 5-day standard.¹¹⁰ The Commission maintains that recipients are a relevant source of information, which the Postal Service should consider when determining the impact of the proposal on market demand.

Relatedly, the Commission believes that the impact of the proposed service standard change has been understudied for large-sized business shippers and existing customers of RG-PSG and PM. The Postal Service projects that the enhanced RG-PSG will see a 15 percent volume growth; however, it is unclear how much of the growth in RG-PSG will stem from volume diverted from Postal Service's competitors or other Postal Service products, such as PM. See *id.* question 6.c. The BCG Survey appears to ignore the potential impact on the shipping decision-making of existing PM customers that are large-sized businesses. Since speed and price both emerged as key factors for choosing a shipping service, with the enhanced service standard of RG-PSG and lower prices, existing PM customers may opt for the enhanced speed and lower-priced RG-PSG, at least in the short term. The Postal Service asserts that the "low-price" will be maintained for RG-PSG but it is not clear for what duration of time. See Response to POIR No. 4, question 1.d. The BCG Survey also ignores the potential impact on existing RG-PSG customers. See Library Reference USPS-LR-N2022-1/NP15, question 4.b.

When asked to compare the BCG Survey's findings with those of the Brand Health Tracker (BHT),¹¹¹ the Postal Service by its own admission recognizes that different conclusions may be reached by surveying different segments of the customer base. See Revised Library Reference USPS-LR-N2022-1/NP10, question 3.a. The BHT includes both consumer and business respondents, whereas the BCG Survey only includes respondents that are small- and medium-sized businesses. The Commission

¹¹⁰ See Library Reference USPS-LR-N2022-1/NP6, April 8, 2022, question 2.

¹¹¹ The Brand Health Tracker is a survey-based report that reflects "consumer perception of both the Postal Service and its competitors, advertising effectiveness, overall satisfaction and satisfaction with individual attributes." United States Postal Service, Office of Inspector General, Report No. 19RG003MS000-R20, U.S. Postal Service Sales and Marketing Key Performance Indicators, October 27, 2019, at 6.

questions the utility of the BCG Survey given its unrepresentative sample of respondents.

c. Potential Impact on Other Postal Service Products

While the Postal Service maintains that PM remains a faster shipping option in some lanes, with a 1- to 3-day service standard that would continue to differentiate PM from RG and PSG, it acknowledges that some diversion from PM could occur. See Library Reference USPS-LR-N2022-1/NP6, question 7.b. The Postal Service did not appear to examine the proposed service standard change of RG-PSG on existing PM customers, nor did it attempt to quantify the potential volume diversion from PM. The Postal Service appears to expect minimal risk of diverting volume from postal products to RG-PSG and that any revenue loss caused by such diversion would be offset by cost reductions generated by the proposal. See Revised Library Reference USPS-LR-N2022-1/NP10, question 12. However, the initial cost impact of these changes is a net cost increase, and the Postal Service does not provide an estimated time frame for when future cost reductions will be realized. Although the Postal Service does not expect the enhanced RG-PSG service to cannibalize PM volume, it posits several scenarios of PM volume that may be at risk of diverting to RG-PSG, specifically pieces that will likely receive the same speed and where RG-PSG is priced lower. *Id.* Based on observations of recent PM volume trends, the Postal Service claims that some PM volume may have diverted to its competitors and the enhanced RG-PSG may help prevent further loss of postal volume. See Library Reference USPS-LR-N2022-1/NP15, question 5. The Commission observes that, although overall PM has experienced annual growth from FY 2017 to FY 2021, Retail PM has experienced a different volume trend from overall PM during this time period.¹¹²

The Commission believes that, although overall PM volumes may not be impacted materially by the proposed changes, shorter distance and hence, lower zone PM pieces may divert to the enhanced RG-PSG given the similar speed and lower price

¹¹² Non-Public Technical Appendix at 23; Priority Mail Billing Determinants for FY 2017 through FY 2021; Docket Nos. ACR2017 through ACR2021, Library Reference NP1.

for RG-PSG. The Postal Service categorizes PM as “medium-speed, medium price” and plans to turn the “low-speed, low-price” RG-PSG into an enhanced “medium-speed, low-price” RG-PSG. The Postal Service provides an estimated percent of the discount from PM prices that would be sufficient to render it “low-price.” See Library Reference USPS-LR-N2022-1/NP6, question 5.e. Given the similar service standard and the existing price gap of PM and the enhanced RG-PSG, the Postal Service may be underestimating the risk of cannibalizing PM.¹¹³ The Postal Service may need to collect information on existing PM customers and quantify the PM volume that is at risk of diverting to the enhanced RG-PSG.

The Postal Service asserts that the “low-price” will be maintained for RG and PSG given the future cost savings it projects from efficiency gains by combining RG and PSG with the mail flow of FCPS. See Response to POIR No. 4, question 1.d. However, the Postal Service does not appear to consider the upward pricing pressure on FCPS resulting from the increase in transportation costs of FCPS. The Commission believes that the upward pricing pressure on FCPS may be potentially driven by the efficiency gains for RG and PSG at the expense of FCPS.

3. Conclusion

The proposed service standard changes for RG and PSG have the potential to enable the Postal Service to grow its market share by meeting an unmet market demand for a “medium-speed, low-price” package shipping service. However, there may be an unanticipated or underestimated impact on existing RG and PSG customers, specifically applying upward pressure on RG and PSG prices in the long-term due to the additional cost of providing enhanced service. Furthermore, the risk of cannibalizing PM, a more compensatory product, was not sufficiently considered by its market research. Contribution is not uniform across the Postal Service’s delivery network. In addition, should the proposed changes attract a higher concentration of higher-cost

¹¹³ In its Response to POIR No. 4, question 4.b., the Postal Service states that it has no plans to maintain a particular price gap between PM and RG-PSG. See Library Reference USPS-LR-N2022-1/NP12, April 22, 2022.

volume to low-density areas, this would negatively impact the expectation of the increase in positive-contribution volume.

The Commission agrees with the Postal Service that the greatest benefits of the proposed service standard changes for RG and PSG are expected to come in the long term, but the Postal Service is unable to estimate the magnitude of such impact without data on projected future RG and PSG and other products' volumes. The Postal Service is also not able to project when the expected benefits might occur. Moving forward, the Commission recommends that the Postal Service monitor the impact on shipping options in the competitive parcels market, especially the impact on mailers who use RG, PSG, and PM, and mailers who are strictly price conscious and larger-business shippers. The Commission also encourages the Postal Service to monitor any volume diversion from PM and impact on other Postal Service products.

VII. CERTIFICATION

It is the opinion of each of the Commissioners listed below, pursuant to 39 U.S.C. § 3661(c), that this Advisory Opinion conforms to the policies established under Title 39, United States Code.

Michael Kubayanda, Chairman

Ann C. Fisher, Vice Chairman

Mark Acton, Commissioner

Ashley E. Poling, Commissioner

Robert G. Taub, Commissioner