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UNITED STATES
POSTAL SERVICE

August 12, 2022

Honorable Erica Barker
Secretary
Postal Regulatory Commission
901 New York Avenue, NW, Suite 200
Washington, DC 20268-0001

Dear Ms. Barker:

As you are no doubt aware, the Postal Service Reform Act (PSRA) was enacted on April 6, 2022, and had certain specific effects on the Postal Service's finances. This letter is to inform the Commission as to how the Postal Service expects to reflect some of these financial effects for regulatory purposes at the end of the year when, pursuant to section 3652 of title 39, it submits to the Commission the Annual Compliance Report (ACR) for FY 2022.

Specifically, section 102 of the PSRA repealed the requirement that the Postal Service annually prepay future retiree health benefits and cancelled all past due prefunding payments. As indicated in the note on page 1 of the United States Postal Service Financial Information (Unaudited) for April 2022 (submitted on May 24, 2022), as well in the Postal Service's Quarterly Report on Form 10-Q (submitted on August 9, 2022), for accounting purposes these changes result in a one-time reversal of $59.6 billion for retiree health benefits that had been accrued but unpaid as of March 2022. Importantly, however, as reflected in notes (d) and (e) on page 3 of the April 2022 Financial Information, and on page 24 of the Form 10-Q, there are two elements of this total amount. The first element is an amount of $2.150 billion representing elimination of the current year retiree health benefit normal cost payment. The second element is an amount of $57.475 billion representing the reversal of the current year retiree health benefit amortization payment ($0.5 billion) and the reversal of all past due retiree health benefit payments that were unpaid between September 2012 and September 2021 ($57.0 billion).

For accounting purposes, when submitting the FY 2022 Financial Statements that are part of the Form 10-K that will be filed in November, the Postal Service will treat the above amounts as described above. Consequently, in the Statements of Operations, there will be significant one-time reductions in FY 2022 Operating Expenses, with very substantial effects on the bottom-line FY 2022 Net Income/Loss.

While this treatment in the financial reports is dictated by accounting standards, the Cost and Revenue Analysis (CRA) Report submitted each year as part of the ACR primarily fulfills regulatory functions, not accounting functions. For example, the CRA does not include a row for Net Income/Loss. Rather, the focus of the CRA is on costs and revenues by products and groups of products. It allows evaluation of compliance with statutory and regulatory policies such as the requirements that each market dominant class be compensatory; that each competitive product be compensatory; and that competitive products as a whole not be cross-subsidized, bear an appropriate share of institutional costs, and allow transfer of an assumed income tax on competitive products income.

Despite these functional differences, the costs in the General Ledger are the foundation for the Reallocated Trial Balance Report that is the starting point of the CRA model. This is manifested most clearly in the equivalence each year between the Total cost row in the CRA and the sum of the Total Operating Expenses and Interest Expense rows of the Postal Service's Statements of Operations.[1] Ordinarily, the totality of costs accrued in the General Ledger for a given year are the exact same costs classified in the CRA as either attributable or institutional for that year.

Under the unique circumstances triggered in FY 2022 by enactment of the PSRA, however, rigid default application of the accounting treatment employed in the Financial Statements would preclude meaningful achievement of various regulatory objectives. Specifically, the Postal Service considers that it is inappropriate to take into account the elimination of prior years' past-due prefunding payments when determining the Postal Service's attributable and institutional costs for purposes of the CRA, as compared to the costs accrued for purposes of the General Ledger. If the CRA were to recognize the PSRA's massive, one-time reversal relating to prior years' retiree health benefit expenses, the result would almost certainly be negative total institutional costs in FY 2022, essentially rendering irrelevant the level of all other institutional costs this year. With negative institutional costs, evaluation of compliance with the appropriate share provision would be impossible, creating a situation which would then also impede calculation of the imputed federal income tax.

To avoid these outcomes, the Postal Service intends to omit from the Reallocated Trial Balance (and hence the CRA and the ACR) the $57.0 billion negative expense representing the reversal of all past due retiree health benefit payments that were unpaid between September 2012 and September 2021. In other words, the Reallocated Trial Balance in FY 2022 will differ from the totality of costs in the General Ledger by $57.0 billion, representing the past-due payments.

This approach appropriately recognizes that the elimination of these prior-year expenses, while a negative expense for accounting purposes, does not reflect a change in annual institutional costs for regulatory purposes. It will allow FY 2022 institutional costs to remain positive and within the same general magnitude as experienced in recent years (although, obviously, fully recognizing all of the other factors still

[1] For example, compare page 3 of the FY 2021 Public CRA in USPS-FY21-1 with page 56 of the 2021 Report on Form 10-K (November 10, 2021).

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specifically influencing institutional costs in FY 2022). Moreover, given the one-time nature of the specific accounting transactions involved, institutional costs in FY 2023 and onward will not be affected by these reversals. Omitting prior years' past-due payments from the FY 2022 Reallocated Trial Balance thus constitutes one of the extremely rare circumstances in which the appropriate accounting treatment of certain expenses does not constitute the appropriate regulatory treatment.

To be clear, though, the Postal Service will maintain the usual consistency between the General Ledger and the CRA with respect to the treatment of the *current-year* retiree health benefit normal cost ($2.150 billion) and amortization payments ($0.5 billion) identified on page 3 of the Unaudited Financial Information for April 2022, and on page 24 of the Form 10-Q. These amounts represent a reversal of amounts accrued earlier in FY 2022. The effect of this will be, at the end of the year, no expenses for current year retiree health benefit normal cost and amortization payments.[2] Since the April reversal will have zeroed out the expenses accrued in previous months, at the end of the year, there will be nothing left to reverse, and the April reversal will thus be "omitted" from both the General Ledger and the Reallocated Trial Balance. In the sense of both showing no expenses in FY 2022 for current year retiree health benefit normal cost and amortization payments, the CRA and the year-end General Ledger will therefore be consistent. As such, while the CRA will indirectly reflect the fact that the PSRA has reduced the Postal Service's costs by eliminating these payments (as compared to what the CRA costs would have been if the PSRA had not been enacted), there is no need for a deviation from the General Ledger in this regard.

[2] Indeed, the absence of these specific expenses for the full year is already reflected on page 3 of the Form 10-Q. The Statement of Operations on that page has a row labelled as "Impact of Postal Service reform legislation," and it shows an amount in the column for the Three Months Ended June 30, 2022, of $59.625 billion (rounds to $59.6 billion), but a corresponding amount of only $56.975 billion (rounds to $57.0 billion) in the year-to-date column for the Nine Months Ended June 30, 2022. The difference between these two figures arises from the inclusion in the Three Months figure of the current-year retiree health benefit normal cost and the current-year amortization payments. As discussed above, with the effects of those entries constrained to April (or, in terms of the quarterly reports, to Quarter Three), the negative $57.0 billion adjustment for the past due RHB payments is the sole amount now anticipated to be omitted from the annual Reallocated Trial Balances and the CRA.

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While it is still several months before the Postal Service will be providing its year-end submissions, it seemed worthwhile to advise the Commission (and other potentially interested stakeholders) of our plans. Please feel free to contact me if you have any questions, or if further information would be helpful.

Best regards,

/s/

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