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BEFORE THE
POSTAL REGULATORY COMMISSION
WASHINGTON, D.C. 20268–0001

PERIODIC REPORTING (PROPOSAL SEVEN)	Docket No. RM2023-2

PETITION OF THE UNITED STATES POSTAL SERVICE FOR THE INITIATION OF A PROCEEDING TO CONSIDER PROPOSED CHANGES IN ANALYTICAL PRINCIPLES (PROPOSAL SEVEN)
(December 12, 2022)

Pursuant to 39 C.F.R. § 3050.11, the Postal Service requests that the Commission initiate a rulemaking proceeding to consider a proposal to change analytical principles relating to the Postal Service's periodic reports. The proposal, to make a one-time adjustment in the FY 2022 Annual Compliance Report to exclude from institutional costs the extraordinary $57 billion negative expense representing the reversal by the Postal Service Reform Act of all past due retiree health benefit payments that were unpaid between September 2012 and September 2021, is labeled Proposal Seven and is discussed in detail in the attached text.

This pleading is styled as a petition to change an accepted analytical principle because of guidance from the Commission in Order No. 6363 (pages 11-12), which reversed its prior determination that such a petition was unnecessary. While the Postal Service is filing this petition based on the Commission's decision in Order No. 6363, this should not be interpreted as a concession by the Postal Service that Order No. 6363 reached the correct conclusion in this regard. The Postal Service, however, does not view resolution of the question of whether this matter truly involves a change in analytical principles as having any material bearing on the underlying merits of this request.

Respectfully submitted,

UNITED STATES POSTAL SERVICE

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Proposal Seven: Preclude the massive one-time negative accounting entry associated with the statutory reversal of past prefunding requirements from affecting institutional costs in the FY 2022 Cost and Revenue Analysis (CRA)

Objective

The objective of this proposal is to address the appropriate regulatory treatment of unique and non-recurring accounting occurrences that are the result of statutory change, specifically the reversal by the Postal Service Reform Act (PSRA) of all past due retiree health benefit (RHB) prefunding payments that were unpaid between September 2012 and September 2021. The Postal Service proposes to segregate this extraordinary $57 billion reversal from the other FY 2022 accounting costs that flow into the ACR regulatory cost, precluding its effects from overwhelming routine institutional cost expenses actually incurred in FY 2022 and thereby inappropriately disrupting vital regulatory functions.

Background

This proposal follows the withdrawal by the Commission in Order No. 6363 (December 9, 2022) of its previous approval (in a letter dated October 7, 2022) of the general approach outlined above. That approach was first described in a letter dated August 12 from the Postal Service to the Commission that noted the passage of the PSRA and indicated how the retiree health benefit payment effects of that law were being reflected in accounting submissions (e.g., monthly Financial Information filings, the Quarterly Form 10-Q Report, and the Annual Form 10-K Report). The August 12 letter also explained how and why the Postal Service, for purposes of our regulatory cost presentation in the FY 2022 Annual Compliance Report (ACR), intended to deviate from the default accounting treatment, although exclusively with respect to the $57 billion negative expense associated with the cancellation of the unpaid prior year prefunding obligations.

Nearly two months later, having received no feedback from any other stakeholders, the Commission posted its October 7 letter that essentially endorsed the approach the Postal Service had outlined in the August 12 letter, describing the contrary approach as creating “nonsensical” results and acting to “distort” trend analyses and potentially “interfere” with regulatory purposes. On October 13, 2022, a consortium of mailer associations submitted a letter seeking reconsideration of the Commission’s October 7 letter. They argued procedurally that the treatment endorsed by the Commission would constitute a change in analytic principles that could only be adopted following a rulemaking proceeding, and that substantively it would be beneficial to reflect the negative $57 billion expense in the CRA in order to eliminate any positive institutional cost amount that could provide the basis for a FY 2022 density authority calculation. In contrast to their claim that the regulatory treatment of the negative $57 billion expense should follow the accounting treatment, they also sought to require the attribution of some so-called RHB “normal costs,” despite the fact that neither RHB “normal costs” nor any other RHB expenses were accrued in FY 2022. The Commission had not directly addressed that issue in its October 7 letter.

On November 4, 2022, one of the signatories to the October 13 Mailer letter, the Greeting Card Association (GCA), filed a formal petition to initiate a rulemaking (Docket No RM2023-1), in which the positions and arguments presented in the Mailer letter were essentially incorporated by reference. Less than a week after the filing of the GCA petition, the Postal Service on November 10 responded in opposition, contending that the Commission's endorsement of our intended treatment of the PSRA effects on RHB regulatory costs did not require reconsideration, and denying any need for further proceedings on the matter. Eleven days later, without seeking leave, the mailer associations on November 21 replied to the Postal Service's opposition, although as noted by the Commission in Order No. 6363, the reply did not present any new arguments.

Order No. 6363 sought to resolve the various issues raised by these circumstances. Reversing its prior conclusion that there was no accepted analytical principle to apply in the instance of the PSRA statutory change triggering a unique, non-recurring event, the Commission in Order No. 6363 found that an accepted analytical principle could be discerned. Based on the General Ledger account and the Cost Segment 18 component in which the $57 billion multi-year reversal has been recorded, the Commission now decided that conformance with the accepted analytical principle would be to treat the reversal the same for regulatory purposes as the much smaller amounts previously recorded each year in that account and in that component. Order No. 6363 at 9. Accordingly, the Order specified that unless continued application of this analytical principle were revisited in a rulemaking, the $57 billion negative expense should be treated as any other institutional cost in FY 2022, which the Commission acknowledged would likely cause the unusual result of overall FY 2022 institutional costs summing to a negative number. *Id*. The instant Proposal Seven thus constitutes the Postal Service's acceptance of the Commission's belated invitation to revisit the matter and to seek authorization to deviate in the FY 2022 CRA from what has now been identified as the otherwise applicable analytical principle with respect to the $57 billion reversal recorded in account 51265.000 in this year's General Ledger.[1]

Proposal

As explained in the Postal Service's August 12 Letter and the November 10 Opposition to the GCA Petition in Docket No. RM2023-1, in past years following passage of the PAEA, consistent with generally accepted accounting principles (GAAP), the Postal Service accrued expenses in each year for that year's scheduled prefunding payment for retiree health benefits. For regulatory purposes, it was entirely rational during those years to treat those accrued expenses each year like all other expenses for that year. This procedure allowed a fair representation of the totality of costs faced by the Postal Service in that year that needed ether to be attributed to products or classified as institutional. Nonetheless, default treatment of a steady series of *annual* prefunding costs does <u>not</u> automatically constitute the appropriate procedure for the treatment of the sudden and unprecedented occurrence of a one-time reversal of a *decade's* worth of unpaid prefunding expenses from prior years. Thoughtful response to a drastically different new situation requires adoption of an approach specifically targeted to the extraordinary circumstances presented. The Commission recognized as

[1] Order No. 6363 also rejected the mailers' contention that a failure to accrue (and attribute some portion of) normal costs would likewise constitute a deviation from an accepted analytical principle. *Id.* at 10. The Commission instead agreed with the Postal Service that, under the terms of the PSRA, no RHB costs are incurred in FY 2022, and applying the accepted analytical principles therefore yields the conclusion that there are no RHB costs (including any normal costs) for which to account in this year's CRA. *Id*. Since this interpretation of the established methodology aligns with the Postal Service's intended treatment (or, perhaps in this instance, nontreatment) of normal costs, Proposal Seven does not address this aspect of Order No. 6363.

much in the observations on pages 2 and 4 of the Commission Letter regarding "unique and non-recurring accounting occurrences that are the result of statutory change."

Importantly, all sides have already acknowledged the inevitable result under current circumstances in FY 2022 of treating this one-time reversal under GAAP as being relevant to the determination of the Postal Service's regulatory costs – total institutional costs reported for the year would be a very large negative number.[2] Postal Service Letter at 2, Mailer Letter at 6, Order No. 6363 at 9-10. The Postal Service and the Commission, moreover, have recognized the absurd effects of such an occurrence. In its original letter, the Postal Service summarized its concerns as follows:

> 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.

August 12 Letter at 2.

[2] In terms of rough order of magnitude, the FY 2022 total institutional costs calculated under the mandate of Order No.6363 will be approximately as much below zero as total institutional costs have typically been above zero in recent years, although the exact amount will likely be somewhat less negative than recent institutional cost amounts have been positive. The point, though, is that the result will not be minimally negative, but rather negative by a very wide margin.

Correspondingly, in its original October 7 response endorsing the Postal Service's planned treatment, the Commission found:

> Including this unique and non-recurring elimination of past due prior years' RHB payments in the costs reported in the CRA would create nonsensical results and potentially interfere with the regulatory purposes of the CRA. It would also distort trend analysis and comparisons to past or future years' CRA results.

Commission Letter at 3. Order No. 6363 did absolutely nothing to disavow these (correct) conclusions. *See* Order No. 6363 at 9-10 and footnote 15. Given that application of what the Commission has now identified as a controlling analytical principle would "create nonsensical results and potentially interfere with the regulatory purposes of the CRA," it is self-evident that a deviation from those procedures for FY 2022 is fully warranted.

Of course, Order No. 6363 also noted that default adherence to the prior procedure would "nullify the density-based rate authority for a year," precisely the outcome the mailers seek to ensure. *Id.* at 10. As explained in the Postal Service's opposition to the GCA petition, however, this circumstance does not convert "nonsensical" results (i.e., massively negative institutional costs in one fiscal year) to sensible ones. Opposition at 6-7. Density authority was established with a very specific purpose in mind: to offset unavoidable increases in per-unit costs over time caused by the decline in mail density. The Commission explained the rationale for this additional rate authority as follows:

> Put simply, when the Postal Service delivers fewer mailpieces to more delivery points, those costs which are driven by factors other than marginal changes in volume are spread over fewer pieces, necessarily increasing the per-unit cost. The loss of its economies of density means

> that the Postal Service's per-unit costs will be unavoidably higher than they were before the decline in density.

Order No. 5763, Docket No. RM2017-3 (Nov. 30, 2020) at 72. Operation of none of the elements identified by the Commission as the drivers of the need for the density authority were affected by passage of the PSRA. Mail volumes are still declining, delivery points are still increasing, and both of these trends are likely to continue going forward. Under these circumstances, it would be the *preclusion* of density authority (caused by including the $57 billion reversal) rather than the *allowance* of density authority (as a completely rational side effect of removing the $57 billion reversal) that would constitute interference with and disruption of appropriate regulatory functions. Hence, to persist in the application of what the Commission has now determined to be the currently controlling procedures in the face of unique and nonrecurring circumstances for the sole purpose of depriving the Postal Service of density authority in FY 2022 would be irrational both when considering the broader regulatory purposes of the institutional cost calculation, as well as the narrower question as to the calculation of density authority.

Thus, to avoid the "nonsensical" result of massively negative institutional costs, Proposal Seven seeks the allowance of procedures to exclude the negative $57 billion expense associated with the cancellation by the PSRA of all past due RHB prefunding payments that were unpaid between September 2012 and September 2021 from the calculation of FY 2022 total institutional costs. The Postal Service can envision at least two equally valid sets of procedural steps to achieve this objective. The Postal Service would find either of these acceptable, because the conceptual outcomes of both are identical.

The more direct set of steps and the preferable approach would be simply to "zero out" Component 203 in the Cost Segment 18 tab of the Reallocated Trial Balance (USPS-FY22-5), by omitting the reallocation of the negative $56,975,093,943.28 from Trial Balance account 51265.000 into Component 203. See the discussion of these accounts and components on pages 7-9 of Order No. 6363. The result of that would be a Cost Segment 18 total in the Reallocated Trial Balance that would differ by that approximately $57 billion amount from the Cost Segment 18 total displayed on row 2000 of the Statement of Revenue and Expenses (September 2022) posted on November 10, 2022. And that same difference would then flow into the total costs displayed in the Summary tab of the Reallocated Trial Balance, in the CSSummary tab of the Cost Segments and Components Report (USPS-FY22-2), and on page 3 of the CRA (USPS-FY22-1). The end result would be total costs at the bottom of the CRA that differed by that same amount from the sum of the Total Operating Expenses, Impact of Postal Service Reform Legislation, and Interest Expense rows of the Postal Service's Statements of Operations in the 10-K.[3] And since amounts in Component 203 are treated as institutional costs, the total cost difference precipitated by "zeroing out" Component 203 would be matched by an identical difference in institutional costs (i.e., the $57 billion negative expense would have successfully been prevented from inappropriately affecting FY 2022 institutional costs), compared with the institutional costs that would be generated without Proposal Seven. This first set of steps would match the Postal Service's intentions as expressed in the August 12 letter.

[3] *See* page 45 of the 2022 Report on Form 10-K (November 10, 2022).

But Order No. 6363 suggests the possibility of an alternative set of steps to achieve the same objective. On page 9 of the Order, the reporting category of "Miscellaneous Items" is injected into the discussion. As discernible from both page 3 of the CRA and the CRA note cited on page 9 of Order No. 6363, Miscellaneous Items have routinely appeared only in the Revenue column. Yet conceivably the Commission this year could authorize the expansion of that category to encompass Miscellaneous Costs as well. Under this scenario, a new tab in the Reallocated Trial Balance file and the Cost Segment and Component file could be created for Miscellaneous Costs that would, in effect, operate as an undefined additional cost segment. Instead of being reallocated into Component 203 in Cost Segment 18, the $57 billion negative expense amount from Trial Balance account 51265.000 could be reallocated to the Miscellaneous Costs tab. This seemingly has the same effect as the set of procedures described above in the sense that the amount for *Component 203* would still be zero for the year, but instead of being disregarded entirely, the amount from Trial Balance account 51265.000 would be shifted elsewhere. Under this alternative set of procedures, as would be appropriately explained in the CRA Notes, the Miscellaneous Items row in the CRA would now include entries in both the revenue and the cost columns. Since the entire purpose of the exercise is to segregate the extraordinary $57 billion negative expense from routine institutional costs, the bottom line total costs row of the CRA would *include* Miscellaneous Costs, but that amount would be *excluded* from the All Other (i.e., institutional cost) row.

As emphasized above, these two sets of procedures conceptually reach the same result with respect to total institutional costs, which is the primary focus of

Proposal Seven. The essentially cosmetic difference is that with the first set of steps, the total CRA costs would not match the total 10-K costs, while with the second set of steps, the total costs would match. If the alternative second set of procedures were authorized for FY 2022, in future years, Miscellaneous Items would presumably revert to a revenue-only row, and the Miscellaneous Costs tabs would be omitted from the Reallocated Trail Balance and the Cost Segments and Components files. While the Postal Service considers the first set of steps to be the preferable course of action, the alternative second set of steps described herein also seems acceptable.

Impact

As highlighted throughout the above discussion, the intended impact of Proposal Seven is to exclude the one-time massive negative RHB expense accrual triggered by the PSRA from overwhelming routine FY 2022 institutional costs. In so doing, it would avoid the inappropriate detrimental regulatory consequences of the “nonsensical” result of negative institutional costs previously and correctly recognized by the Commission.