

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

PERIODIC REPORTING

Docket No. RM2011-11

PETITION OF THE UNITED STATES POSTAL SERVICE REQUESTING  
INITIATION OF A PROCEEDING TO CONSIDER A PROPOSED CHANGE  
IN ANALYTICAL PRINCIPLES (Proposal Three)  
(May 18, 2011)

Pursuant to 39 C.F.R. § 3050.11, the Postal Service requests that the Commission initiate a proceeding to consider a proposal to change analytical principles relating to the Postal Service's periodic reports. The proposal, labeled Proposal Three, is discussed below, and in greater detail in the attached text. (Proposal One for this year was filed on April 6, 2011. Order No. 713 (April 8, 2011), Docket No. RM2011-9. Proposal Two was filed on May 10, 2011. Order No. 727 (May 12, 2011), Docket No. RM2011-10.)

Proposal Three seeks authorization to change the methodology used for allocating stamp and meter Postage-in-the-Hands-of-the-Public (PIHOP) revenue in the RPW Report. The current methodology allocates two Trial Balance PIHOP revenue accounts (stamp and meter) to products using the total ODIS-RPW sampling revenue distribution key. The proposed methodology would allocate stamp PIHOP using the ODIS-RPW sampling revenue stamp indicia distribution key, and would allocate meter PIHOP using the ODIS-RPW sampling revenue meter indicia distribution key. The primary objective of the proposed methodology is to obtain a more appropriate

allocation of the impact of PIHOP adjustments between Priority Mail and First-Class Mail, although other classes would benefit from more accurate reporting as well.

The Postal Service requests that the Commission initiate a rulemaking proceeding pursuant to 39 C.F.R. § 3050.11 to consider this proposal.

Respectfully submitted,

UNITED STATES POSTAL SERVICE

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## Proposal Three

### PROPOSED CHANGE IN RPW METHODOLOGY FOR PIHOP ADJUSTMENTS

#### **OBJECTIVE:**

This request asks for a change in the methodology for allocating the adjustments to stamp and meter revenue to account for the portion of sales that are deferred, known as “Postage-in-the-Hands-of-the-Public (PIHOP)” in the RPW Report. The current methodology allocates two Trial Balance PIHOP revenue adjustment accounts (stamp and meter) to products using the same total ODIS-RPW sampling revenue distribution key. The proposed methodology would allocate stamp PIHOP using the ODIS-RPW sampling revenue stamp indicia distribution key, and would allocate meter PIHOP using the ODIS-RPW sampling revenue meter indicia distribution key. Stamp and meter PIHOP would also be removed from the Book Revenue Adjustment Factor.

#### **BACKGROUND:**

The general concern is that stamp and meter PIHOP adjustments are likely being misallocated in the RPW Report. The current methodology does not take into consideration the relative use of stamps or meters as payment for the various services. For instance, using total ODIS-RPW sampling revenue as the distribution key tends to allocate more of the stamp PIHOP adjustments to Priority Mail than is appropriate, given that relatively little of Priority Mail is paid for through stamps.

#### Postage-in-the-Hands-of-the-Public

The Postal Service establishes Trial Balance revenue accounts for isolating, reporting and accounting for revenue by method of payment and for other reasons.

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Trial balance revenue adjustment accounts exist for PIHOP. PIHOP adjustments are made by the Postal Service's Accounting function to recognize the difference between meter and stamp postage sold, but not used during a specified time period. If, for example, \$100 worth of stamps are sold in a specified time period, but only \$90 worth of stamps are used in this time period, there is a \$10 PIHOP liability, and an adjustment decreases the stamp revenue account in the general ledger by \$10. Stamp and meter *sales* are recorded in Postal Service accounts. Stamp and meter revenue *usage* is estimated by the ODIS-RPW sampling system. The difference between sales and usage is the adjustment for PIHOP. PIHOP adjustments can be negative (sales greater than usage), or positive (usage greater than sales) in any given time period.<sup>1</sup> Since the introduction of Forever Stamps, PIHOP liability for stamps has been generally increasing, as the public appears to be holding stamps for longer periods prior to using them. New stamp consignment arrangements with major companies, as well as the recent introduction of Forever Stamp coils, also tend to create large supplies of stamps that are held longer prior to distribution and/or use. Finally, declines in First-Class single piece mail volume can also contribute to the increase in stamp PIHOP liability, to the extent that the public has not altered its purchase patterns for stamps to match such declines.

Two trial balance revenue adjustment accounts exist for PIHOP. Account 41199.000 is for Stamp PIHOP adjustments, and includes both denominated and

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<sup>1</sup> Thus, changes in PIHOP moving from one period to the next can be positive or negative, but, obviously, the overall amount of postage held by the public must always be a positive number. The amounts which appear in the trial balance adjustment accounts under consideration in this proposal represent *changes* in the respective types of PIHOP for the reporting period in question.

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Forever Stamps. Meter PIHOP adjustment account 41222.000 includes meter, pre-canceled stamp and mail-in-transit PIHOP. The attached Excel file Prop.3.PIHOP.Attach.1.xls shows the monthly accounting adjustments to PIHOP liability (and thus to revenue) for the first six months of FY2011, and for the same period last year.

### RPW Reporting

Regulatory reporting of revenue, pieces and weight is presented in the "Revenue, Pieces and Weight By Class and Special Services" report filed quarterly with the Postal Regulatory Commission, in accordance with Commission Rule 3050.25. This report is usually referred to simply as the RPW Report. The RPW system was discussed in detail in witness Pafford's testimony (USPS-T-3) in Docket No. R2006-1. Revenue, pieces and weight are reported for Postal Service products through various source systems such as the Trial Balance revenues, the Bulk Revenue, Pieces and Weight (BRPW) system (Docket No. R2006-1, Library Reference LR-L-14), and the Origin-Destination Information System and Revenue, Pieces and Weight (ODIS-RPW) probability sampling system (Docket No. R2006-1, Library References USPS-LR-L-16 and USPS-LR-L-17). The Adjustment Revenue, Pieces and Weight (ARPW) system (Docket No. R2006-1, Library Reference USPS-LR-L-18) describes how these source systems are combined and adjusted such that the revenue equals the total USPS Trial Balance.

Ideally, the two sources of ODIS-RPW revenue (Census Revenue and Sampling Revenue) would total to Total Accounting Revenue in the Trial Balance. In reality, though, when the two sources sum to a total which does not match the Trial Balance

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total, the assumption is made that the Census Revenue is correct, and that the Sampling Revenue needs to be adjusted so that the resulting sum of Census Revenue and adjusted Sampling Revenue matches the control (Trial Balance) total. To facilitate that process, a figure known as the Residual USPS Trial Balance total is calculated, which is simply the difference between the control (Trial Balance) total and the Census Revenue. The Sampling Revenue must thus be adjusted to match the Residual USPS Trial Balance Total.

In the ARPW process, ODIS-RPW total sampling revenue (including stamp, meter and window service entry) is ratioed back to Residual USPS Trial Balance revenue such that the sum of ratioed ODIS-RPW total sampling revenue plus total RPW “census” revenue equals the total USPS Trial Balance. The ratioing process is called book revenue adjustment, and the resulting ratio is called the Book Revenue Adjustment Factor (BRAAF). This process was summarized in Library Reference USPS-LR-L-18, Section 2, in Docket No. R2006-1.

The two PIHOP Trial Balance accounts are two of the many accounts that make up the Residual Trial Balance revenue. This revenue is distributed to products without regard to indicia (stamp, meter, or any other indicia that makes up the total ODIS-RPW sampling revenue). That is, stamp and meter PIHOP are distributed to products based on the total sampling revenue distribution, and not by the stamp or meter product revenue distribution.

### Problems with the Current Methodology

As stamp PIHOP has grown with the introduction of Forever Stamps, it has become evident that the product results reported in RPW are being incorrectly

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estimated. For example, too much stamp PIHOP is being distributed to Priority Mail, when very little Priority Mail is mailed using stamps. First-Class single piece mail, conversely, has not been getting enough of the stamp PIHOP revenue. Meter PIHOP has also been allocated incorrectly, as it is distributed using the same distribution key as stamp PIHOP. Since stamp PIHOP has been more negative in FY2011 than in FY2010, the downward effect on Priority Mail revenue reported in the current year is increasing, which creates distortions when comparing this year's Priority Mail revenue to that reported in FY2010. Other products estimated by the ODIS-RPW sampling system are affected as well.

The distribution of PIHOP in RPW and its effect on Priority Mail and First-Class Mail sampling estimates can best be described by deconstructing the Book Revenue Adjustment Factor (BRAAF) as applied in the Adjustment RPW process. For purposes of illustration, we will use the most recent Postal Quarter; Quarter 2, FY2011. The Book Revenue Adjustment Factor (BRAAF) is defined as:

$$\text{BRAAF} = \frac{\text{Total Accounting USPS Revenue} - \text{Total RPW Census Revenue}}{\text{Total ODIS-RPW Single-Piece Sampling Revenue}}, \quad \text{or}$$

$$\text{BRAAF} = \frac{\text{Residual Trial Balance}}{\text{Total ODIS-RPW Single-Piece Sampling Revenue}}$$

The 'RPW and BRAAF' tab in Prop.3.PIHOP.Attach.2.xls shows the construction of the BRAAF and the construction of RPW Priority Mail and First-Class Mail single piece revenue for Q2 FY2011. In Q2 FY2011 the BRAAF = \$5,076,344,388 / \$5,530,345,743 = 0.91791, where the numerator is the Residual trial balance and the denominator is the

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total ODIS-RPW sampling revenue. Priority Mail, which makes up 22.8 percent (\$1.26B) of the total ODIS-RPW sampling revenue in the denominator of the BRAF, is adjusted by multiplying the sampling revenue by 0.91791. The final adjusted Priority Mail sample estimate is approximately \$1.16B ( $\$1.26B * 0.91791$ ). Similarly, the ODIS-RPW sampling First Class Mail revenue (\$3.70B), which makes up 66.9 percent of the total ODIS-RPW sampling revenue in the denominator of the BRAF, is adjusted to approximately \$3.39B. Then, for example, the Priority Mail adjusted sampling revenue of \$1.16B is added to "census" sources for Priority Mail of \$.17B to sum to the \$1.33B shown in the Q2 FY2011 RPW report for Domestic Priority Mail.

The 'Decomposition' tab in Prop.3.PIHOP.Attach.2.xls decomposes PIHOP in the BRAF for the RPW Priority Mail and First-Class Mail single piece revenue for Q2 FY2011. Specifically, deconstructing the Residual trial balance revenue of \$5,076,344,388 into its stamp PIHOP (-\$178,900,000) and meter PIHOP (-\$45,600,000) components results in a BRAF decomposition of:  $(5,300,844,388 + (-\$178,900,000) + (-\$45,600,000)) / \$5,530,345,743 = \$5,300,844,388 / \$5,530,345,743 - \$178,900,000 / \$5,530,345,743 - \$45,600,000 / \$5,530,345,743$ . ODIS-RPW estimated Priority Mail revenue for stamp PIHOP would contribute  $(-\$178,900,000 / \$5,530,345,743) * \$1.26B = -\$40.8M$  to the RPW Report total Priority Mail revenue. Similarly, First-Class Mail revenue in the RPW Report would get a contribution of negative \$119.6M from stamp PIHOP  $(-\$178,900,000 / \$5,530,345,743) * \$3.70B = -\$119.6M$ ). As shown in the Excel spreadsheet, after negative \$40.8M goes to Priority Mail and negative \$119.6M goes to First-Class Mail, the balance (negative \$18.5M) of the negative \$178.9M stamp PIHOP goes to Other Classes and Services. In

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percentage terms, roughly 67 percent of the stamp PIHOP adjustment goes to First-Class Mail, 23 percent goes to Priority Mail, and 10 percent to other products.

Conducting the corresponding exercise for the meter PIHOP, again as shown in the spreadsheet, the total meter PIHOP of negative \$45.6M can be decomposed into negative \$10.4M for Priority Mail, negative \$30.5M for First-Class Mail, and negative \$4.7M for Other Classes and Services, also reflecting the identical percentage splits.

### Allocation of Stamp PIHOP to Priority Mail and First-Class Mail

In the above process, the allocation of stamp PIHOP is too high for Priority Mail and too low for First-Class Mail. There is a very small percentage of stamps applied to Priority Mail packaging. The Quarterly Statistics Report (QSR) Q4 YTD FY2010 table for stamp indicia, for example, shows that approximately \$143.5M of the total \$5.7B Priority Mail revenue, or 2.5 percent, is mailed with stamps. In Q1 FY2011, 1.4 percent of total ODIS-RPW sample stamp indicia revenue is Priority Mail and 98.1 percent is First-Class Mail. This can be seen in the highlighted areas of the 'Revenue Keys' tab in Prop.3.PIHOP.Attach.3.xls. The percentages shown in the tab are the ODIS-RPW sampling revenues subset by indicia. If the shares of ODIS-RPW sampling revenue by indicia were used as the distribution key, instead of the share of total ODIS-RPW sampling revenue distribution being used currently, the stamp PIHOP of negative \$178,900,000 would be allocated in the amount of approximately negative \$2.5M ( $-\$178.9M * 1.4$  percent) to Priority Mail, negative \$175.5M ( $-\$178.9M * 98.1$  percent) to First-Class Mail, and negative \$0.9M ( $-\$178.9 * 0.5$  percent) to other classes and services.

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### PROPOSAL:

The proposed methodology follows from the above discussion. The stamp and meter PIHOP account revenues would be assigned to products based on the ODIS-RPW sampling stamp and meter indicia product distributions. Pieces and weight would be constructed as described below. These data would be brought in as a manual input (as discussed in Library Reference USPS-LR-L-18, Docket R2006-1, Section 3.c). Finally, the residual Trial Balance would exclude the revenues from the two PIHOP accounts, so as not to double count. Specifically, the methodology is:

- Stamp PIHOP Revenue - Stamp PIHOP is allocated to the ODIS-RPW sample estimates of stamp indicia at the RPW mail category code level (RPW Extract). These revenue estimates are added as a manual input in the RPW report. The 'Revenue Keys' tab in Prop.3.PIHOP.Attach.3.xls shows the calculation of stamp PIHOP revenue by mail category for Q2 FY2011.
- Stamp PIHOP Pieces and Weight – Pieces and weight are constructed at the mail category level by dividing the stamp PIHOP revenue by the ODIS-RPW sample revenue per piece and revenue per pound stamp indicia estimates, respectively. These estimates are added as a manual input along with revenue. The 'Pieces & Weight Conversion' tab in Prop.3.PIHOP.Attach.3.xls shows the calculation of stamp PIHOP pieces and weight by mail category for Q2 FY2011.

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- Meter PIHOP Revenue – Meter PIHOP is allocated to the ODIS-RPW sample estimates of meter indicia at the RPW mail category code level (RPW Extract). Meter PIHOP revenue will exclude Mail-in-Transit PIHOP. Mail-in-Transit PIHOP reflects PIHOP for all mail classes (including Bulk Mail) and therefore should be excluded from this reallocation. These meter PIHOP revenue estimates are added as a manual input in the RPW report. The ‘Revenue Keys’ tab in Prop.3.PIHOP.Attach.3.xls shows the calculation of meter PIHOP revenue by mail category for Q2 FY2011.
- Meter PIHOP Pieces and Weight – Pieces and weight are constructed at the mail category level by dividing the meter PIHOP revenue by the ODIS-RPW sample revenue per piece and revenue per pound meter indicia estimates, respectively. These estimates are added as a manual input along with revenue. The ‘Pieces & Weight Conversion’ tab in Prop.3.PIHOP.Attach.3.xls shows the calculation of meter PIHOP pieces and weight by mail category for Q2 FY2011.
- The Book Revenue Adjustment Factor (BRAAF) is constructed without the stamp and meter PIHOP revenues included in numerator (Residual Trial Balance).

The ‘Proposed BRAAF Construction’ tab in Prop.3.PIHOP.Attach.3.xls shows the reconstruction the Book Revenue Adjustment Factor and its approximate change in the Q2 FY2011 RPW Report for Priority Mail and First-Class Mail single piece. Domestic Priority Mail revenue increases from \$1.333B shown in the Q2 FY2011 RPW Report to

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\$1.368B, while First-Class Single letters, for example, decreases from \$2.701B to \$2.638B. (First-Class Single-Piece of all shapes decreases from \$3.638B to \$3.585B.)

### **RATIONALE:**

Current RPW product and mail class reporting is being adversely affected by the current methodology used to spread Postage-in-the-Hands-of-the-Public. Because it much more closely reflects the relative usage of stamps and meters among various types of mail categories included in the sampling portion of RPW, the proposed change to PIHOP allocation would constitute a much improved methodology for revenue, pieces, and weight reporting. If this change in analytical principles were accepted, RPW reporting would immediately begin using the new methodology, and any postal quarters published under the old methodology would be recast in the end-of-year RPW revision process.

### **IMPACT:**

The impact of the proposed change would be as suggested in the above discussion. Using FY2011 Quarter 2 as an illustration, the stamped PIHOP distribution factor for First-Class Mail changes from 66.9 percent to 98.1 percent, for Priority Mail changes from 22.8 percent to 1.4 percent, and for other classes and services from 10.3 percent to 0.5 percent. The effect on meter PIHOP, though, would be far less substantial. Again using FY2011 Quarter 2, the meter PIHOP distribution factor for First-Class Mail changes from 66.9 percent to 62.5 percent, for Priority Mail changes from 22.8 percent to 27.6 percent, and for other classes and services from 10.3 percent to 9.9 percent. Applying these changed distribution factors to the actual amounts

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shown in the various PIHOP accounts, Domestic Priority Mail revenue would increase from \$1.333B shown in the Q2 FY2011 RPW Report to \$1.368B, while First-Class Single letters, for example, would decrease from \$2.701B to \$2.638B. The full impacts of the change in FY2011 Quarter 2 are presented in the Proposed BRAF Construction tab of the Prop.3.PIHOP.Attach.3.xls spreadsheet.

## CERTIFICATE OF SERVICE

I hereby certify that I have this date served the foregoing document in accordance with Section 12 of the Rules of Practice and Procedure.

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