Postal Regulatory Commission
Submitted 12/29/2011 4:13:37 PM
Filing ID: 79166
Accepted 12/29/2011

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

ANNUAL COMPLIANCE REPORT, 2011	Docket No. ACR2011

UNITED STATES POSTAL SERVICE
FY 2011 ANNUAL COMPLIANCE REPORT
(December 29, 2011)

Section 3652 of title 39 requires the Postal Service to file with the Postal Regulatory Commission (Commission), within 90 days after the end of each fiscal year (FY), a variety of data on "costs, revenues, rates, and quality of service," in order to "demonstrate that all products during such [fiscal] year complied with all applicable requirements of [title 39]." The Postal Service hereby provides its Annual Compliance Report (ACR or Report) for FY 2011.

I. OVERVIEW OF REPORT

A. Contents

Much of the information within this Report is included in materials appended as separate folders. A list of those materials is attached at the back of this Report as Attachment One. The appended materials are sequentially numbered and labeled as USPS-FY11-1, USPS-FY11-2, etc. Materials in the nonpublic annex (discussed below in Section V) are labeled as USPS-FY11-NP1, USPS-FY11-NP2, etc.[1] All materials on the list (both public and nonpublic) are submitted in electronic form, although a few are

[1] In those designations, the NP is intended to signify "nonpublic."

submitted in hard copy form as well. Each item includes a preface document explaining the purpose, background, and structure of the underlying material, as well as its relationship with other materials in the Report.

Broadly speaking, there are four sets of items included in the appended material. The first set consists of the product costing material filed on an annual basis in accordance with the Commission's periodic reporting rules. The focus of these materials, in terms of the ultimate output, is the Cost and Revenue Analysis (CRA) report. The second set consists of the comparable costing material with respect to international mail, filed in recent years in response to the Commission's international reporting requirements. The focus of these materials, in terms of output, is the International Cost and Revenue Analysis (ICRA) report.

The third set consists of material relating to intra-product cost analyses, which include those analyses necessary for an examination of workshare discounts pursuant to section 3652(b) (a topic discussed in Section II.G below). This special cost study material generally focuses on categories below the product level. The fourth set is billing determinant information which, for both domestic and international mail, has generally been filed with the Commission on an annual basis, or more frequently, based on the periodic reporting rules.

All four of these major sets of material (CRA, ICRA, cost studies, and billing determinants) are similar to those previously submitted to the Commission in prior ACRs. Moreover, they are presented in formats similar (if not identical) to the formats used in previous ACRs. The Postal Service has sought to maximize the ease with which these materials may be reviewed.

As in previous ACRs, certain materials are presented in two versions, one public and the other nonpublic. The public versions of these materials are limited either to information on market dominant products, or to information on individual market dominant products and comparable aggregate information on competitive products as a whole (or, with respect to the Public CRA, aggregate information on five groups of competitive products). Correspondingly, the nonpublic versions are either limited to information on competitive products, or they contain information on both types of products in contexts in which it is not possible to segregate the two. In the nonpublic versions, however, competitive product information is disaggregated to individual competitive products. This is discussed further in Section V below.

Section 3652(g) requires the Postal Service to submit, together with this Report, a copy of its most recent Comprehensive Statement. A copy of the Postal Service's FY 2011 Comprehensive Statement is filed as USPS-FY11-17. Similarly, a copy of the Postal Service's annual report to the Secretary of the Treasury regarding the Competitive Products Fund, required by section 2011(i) of title 39, is filed as part of USPS-FY11-39, along with the other Competitive Products Fund materials provided in accordance with Commission Rules 3060.20 through 3060.23.

B. Roadmap

A separate roadmap document is included as USPS-FY11-9. The roadmap is a technical document that consolidates brief descriptions of each of the materials provided, as well as the flow of inputs and outputs among them. It also discusses any changes between the methodologies used to prepare this Report and the methodologies applied by the Commission in the FY 2010 Annual Compliance

Determination Report (ACD). The document also includes the listing of special studies and the discussion of obsolescence required by Commission Rule 3050.12.

C. Methodology

The methodologies employed to prepare this ACR are familiar to the Commission from previous ACRs. Because, in general, the methodologies replicate those applied most recently by the Commission, the scope of new methodologies has been minimized. However, because postal operations and postal data collection are not entirely static, some minor changes have been necessary. Methodology changes are identified in a separate section of the roadmap document (USPS-FY11-9). They are also discussed in the preface accompanying each of the appended materials; often, this preface contains a discussion that is more detailed than that contained in the roadmap document. Thus, if a change relates to an area of particular interest to the reader, it may be useful to refer to the particular item in question, rather than relying exclusively on the roadmap document.

The Postal Service has filed a number of proposals to change methodologies in the past year. These proposals are summarized in the table below. The table includes proposals that were still under review by the Commission when the FY 2010 ACD was issued.

PROPOSAL NO.	TOPIC OF PROPOSAL	FILED	DOCKET NO.	NOTICE NO.	NOTICE DATE	DISPOSITION ORDER NO.	DISPOSITION DATE
FY 2010 ACR							
Ten	Change for Clerk and Mailhandler labor costs for inbound international by country group	12/20/2010	RM2011-5	625	12/28/2010	724	05/04/2011
Eleven	Report International Money Transfer Service (IMTS) for Inbound and	12/20/2010	RM2011-5	625	12/28/2010	724	05/04/2011

	Outbound in the ICRA						
Twelve	Alternative inputs for the Media Mail mail processing cost model, Bound Printed Matter transportation cost model, Bulk Parcel Return Service (BPRS) cost model	12/20/2010	RM2011-5	626	12/28/201	724	05/04/2011
Thirteen	Change to Parcel Select/Parcel Return Service mail processing models	12/22/2010	RM2011-6	626	12/28/2010	719	04/28/2011
Fourteen	Change to Parcel Select/Parcel Return Service transportation cost model.	12/22/2010	RM2011-6	626	12/28/2010	719	04/28/2011
FY 2011 ACR							
One	Convert Post Office Box Group E Costs to Institutional	04/08/2011	RM2011-9	713	04/08/2011	744	06/09/2011
Two	NSA Model (NP27) Changes	05/10/2011	RM2011-10	727	05/12/2011	751	06/20/2011
Three	Change PIHOP in ODIS/RPW	05/18/2011	RM2011-11	736	05/23/2011	816	08/19/2011
Four	Change Inbound RPW Reporting	08/08/2011	RM2011-12	810	08/17/2011	920	10/21/2011
Five	New MP Cost Pool for FSS Operations	08/08/2011	RM2011-12	810	08/17/2011	920	10/21/2011
Six	Additional “Non-MODS” MP Cost Pools	08/08/2011	RM2011-12	810	08/17/2011	920	10/21/2011
Seven	Mixed Mail Distribution Keys for Allied Labor	08/08/2011	RM2011-12	810	08/17/2011	920	10/21/2011
Eight	Express Mail Signature Waiver as Non-Accountable Mail	08/08/2011	RM2011-12	810	08/17/2011	920	10/21/2011
Nine	Change in Method for International Cost and Revenue Analysis (ICRA) Report*	11/01/2011	RM2012-1	963	11/10/2011		
Ten	Change in the In-Office Cost System for	11/01/2011	RM2012-1	963	11/10/2011		

	Parcel Select Pieces That Are Undeliverable as Addressed)						
Eleven	Change for Delivery Cost Savings for Negotiated Service Agreement (NSA) Express Mail	11/01/2011	RM2012-1	963	11/10/2011		
Twelve	Modification of the Standard Mail Presort Letters Mail Processing Cost Model	11/01/2011	RM2012-1	963	11/10/2011		
Thirteen	Development of a New Mail Processing Cost Model for Media Mail / Library Mail	11/01/2011	RM2012-1	963	11/10/2011		
Fourteen	Changes in Special Services Cost Models	11/01/2011	RM2012-1	963	11/10/2011		
Fifteen	Changes to Return Receipt Cost Models	11/01/2011	RM2012-1	963	11/10/2011		
Sixteen	Productivity Measurement for Flats Sequencing System	11/30/2011	RM2012-2				
Seventeen	Consolidated MODS Operation Groups for Letter Automation Productivities	11/30/2011	RM2012-2				
Eighteen	Modifications to the Flats Cost Models	11/30/2011	RM2012-2				
Nineteen	Modification of the First-Class Mail Presort Letters Mail Processing Cost Model	11/30/2011	RM2012-2				
Twenty	Modification of the BRM Cost Model	11/30/2011	RM2012-2				

* In its Docket No. RM2012-1 Petition, the Postal Service mistakenly titled Proposal Nine “Change in Method for Inbound RPW Reporting.” The proposal should have been titled “Change in Method for International Cost and Revenue Analysis (ICRA) Report.”

With respect to those proposals that are still pending, where those proposals affect materials filed in this Report, the Postal Service has generally prepared two versions of the materials, one incorporating the proposals and one not incorporating the proposals. There are three exceptions to this practice. First, Proposal Ten, Docket No.

RM2012-1, reflects a change in how the In-Office Cost System (IOCS) attributes the costs of undeliverable as addressed Parcel Select pieces. Because of the wide-ranging downstream implications of data systems such as IOCS, it would not be feasible to account for two versions of such datasets in the ACR. Given this reality, and given that not incorporating the Proposal Ten change would result in inaccurate costs, the Postal Service has incorporated Proposal Ten into the ACR materials. Specifically, USPS-FY11-37 and USPS-FY11-NP21, which are affected by Proposal Ten, do not provide alternate sets of materials.

Second, Proposal Eleven, Docket No. RM2012-1, reflects a change made in Proposal Eight, Docket No. RM2011-12, that has already been approved by the Commission. Therefore, USPS-FY11-NP27, which is affected by Proposal Eleven, assumes the approval of Proposal Eleven. Third, with respect to Proposal Eighteen, Docket No. RM2012-2, the completion of the deployment of the Flats Sequencing System (FSS) in FY 2011 necessitates cost estimations of FSS-processed mail, but the pre-Proposal Eighteen model does not estimate such costs. Therefore, USPS-FY11-11, which is affected by Proposal Eighteen, provides one version of materials that incorporates the Proposal Eighteen modification relating to FSS processing costs but does not incorporate Proposal Eighteen's other three modifications, and an alternate version that incorporates all four Proposal Eighteen modifications. The Postal Service requests that the Commission waive the requirement of 39 C.F.R. § 3050.10 with respect to the Postal Service's incorporation of Proposals Ten, Eleven, and Eighteen into the ACR materials.

To facilitate both the preparation and review of future ACRs, it would be helpful to have more expeditious review of proposals to change analytical principles, particularly for proposals that are filed well in advance of the ACR, such as Proposals Nine through Fifteen from Docket No. RM2012-1, which were filed on November 1, 2011. The Postal Service understands the need for the Commission to do a thorough review, however, and endeavors to propose changes far enough in advance of the ACR for such review. However, it is sometimes not possible to identify the need for a change in analytical principles until the preparation of the ACR is underway.

II. MARKET DOMINANT PRODUCTS

A. Applicable Requirements of Title 39

By FY 2009, prices and fees in effect during the entire fiscal year had been established under Postal Accountability and Enhancement Act (PAEA) procedures, rather than under the previous Postal Reorganization Act (PRA) procedures.[2] Therefore, the price setting standards set forth in the PAEA should be applied in evaluating statutory compliance for FY 2011.

B. Product-by-Product Costs, Revenues, and Volumes

For FY 2011, with the limited exceptions indicated below, cost, revenues, and volumes for all market dominant products of general applicability are shown directly in the FY 2011 CRA (or ICRA). The one exception is International Reply Coupon Service. The ICRA reports only outbound revenue for this product and does not report any FY 2011 inbound and outbound costs or transactions.

[2] The only exceptions were a few carryover international rates.

C. Negotiated Service Agreements (NSAs)

Information for domestic market dominant NSAs is presented in two ways in the ACR. First, on a fiscal year basis, the revenue, costs, and volumes for the NSAs have been extracted from the relevant product CRA lines. This extracted information is then shown in the line “Standard Mail Domestic NSAs.” These data are further disaggregated by individual NSA in USPS-FY11-30. In addition to presenting this fiscal year information, USPS-FY11-30 also presents data for the contract year. Commission Rule 3020.21(1) requires the net benefit calculation for each NSA to be conducted based on contract years, rather than fiscal years, to accommodate NSAs in which discounts are based on volume thresholds reached during a contract year. Those net benefit calculations also appear in USPS-FY11-30.

It is important to note that there is a distinction between the “net benefit calculations” and the data reported in the CRA line item for NSAs. The net benefit calculations are intended to isolate the incremental benefit of the NSA (*i.e.*, the pieces that would not have been mailed if not for the NSA), whereas the CRA reports the entire volume related to the NSA, regardless of whether it is deemed “incremental.”

D. Service Performance

During FY 2010, the Commission issued its final rules on periodic reporting of service performance measurement and customer satisfaction, which are codified at 39 C.F.R. Part 3055.[3] Among other things, Commission Rules 3055.20 through 3055.24 require annual reporting of service performance achievements at the national level for all market dominant products. Reporting, however, is not required where the

[3] Order No. 465, Order Establishing Final Rules Concerning Periodic Reporting of Service Performance Measurements and Customer Satisfaction, Docket No. RM2009-11 (May 25, 2010).

Commission has granted a semi-permanent exception or a temporary waiver.[4] The Postal Service's report, including information responsive to the criteria listed in Rule 3055.2(b)-(k), is included as USPS-FY11-29.

The Postal Service set aggressive on-time targets of 90 percent or above for all market dominant products. Overall, the Postal Service has been successful in continuously improving these scores. For some products and in some districts, these targets have already been met or exceeded. However, there are several instances where the targets have not yet been met at the national level. The Postal Service's targets are intended to guide longer-term improvement and are based on the continued evolution of Intelligent Mail barcode systems and on customers' participation in data collection, which enables performance measurement at the necessary levels. The specific reasons why national scores have not been met are discussed in USPS-FY11-29.

In addition, 39 C.F.R. § 3055.7 requires the Postal Service to evaluate final delivery service performance to the remote locations of Alaska, Honolulu and Caribbean Districts as compared to the service performance to the Gateway cities of Anchorage, Honolulu and San Juan on a biennial basis beginning with the FY 2011 ACR. Accordingly, the Postal Service is submitting its Offshore Special Study Results in USPS-FY11-29.

E. Customer Satisfaction with Market Dominant Products

Section 3652(a)(2)(B)(ii) requires the Postal Service to provide measures of the degree of customer satisfaction with the service provided for its market dominant

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[4] *Id.* at 21-23.

products. In FY 2011, the Postal Service implemented a new approach for measuring customer experience and satisfaction with products.

1. Overview

The Customer Engagement and Strategic Alliance (CE&SA) group in Consumer and Industry Affairs at Postal Service Headquarters was responsible for survey measurement of the level of customer satisfaction with market dominant products during FY 2011. Surveys were administered across each quarter of the year for two customer groupings – Residential and Small/Medium Business customers – and once per quarter for Large Business customers.

2. Background

In FY 2010, the Postal Service transitioned from a longstanding customer satisfaction measurement (CSM) system administered by The Gallup Organization, to a customer experience based measurement (Customer Experience Measurement, or CEM) system, which focuses on sending and receiving mail and on Post Office and contact experiences. Results obtained through the CEM system cannot be compared to previous results because of material differences in survey methodology. The FY 2008 and 2009 CSM surveys were interim methodologies used until the new CEM system was in place for FY 2010.

3. Methodology

For the CEM system in FY 2011, Residential and Small/Medium business customers were randomly selected, contacted by mail, and given the opportunity to complete either an online or a hard copy survey. Large business customers were randomly selected and contacted by mail and asked to complete a survey online.

Residential and Small/Medium businesses were sampled sufficiently to ensure, at the Performance Cluster level, a minimum precision level of +/- 3 percentage points, at the 95 percent level of confidence, per postal quarter. Large business customers were sampled in sufficient quantity to ensure, at the national level, a precision level of +/- 3 percentage points, at the 95 percent level of confidence, per postal quarter.

To measure customer experience with market dominant products, residential and small business survey respondents were asked to rate their product satisfaction using a six-point scale: *Very Satisfied*, *Mostly Satisfied*, *Somewhat Satisfied*, *Somewhat Dissatisfied*, *Mostly Dissatisfied*, and *Very Dissatisfied*. Respondents were also given the option of marking "*Don't Use Product*." Those that responded in this manner were not included in the calculations for satisfaction with market dominant products. Large business customers were asked which market dominant products they used, and then instructed to rate their satisfaction with their experience with those products. Customers who indicated that they did not use a product or were not familiar with a product were excluded from the calculated satisfaction ratings.

In FY 2011, instead of reporting a combined score for the top three box ratings (*Excellent*, *Very Good*, and *Good* in FY 2009), the Postal Service used a more stringent reporting system, combining only the top two box scores of *Very Satisfied* and *Mostly Satisfied*. The scores reported for market dominant products in FY 2011 result from combining only these *Very Satisfied* and *Mostly Satisfied* ratings.

4. Survey Results – Ratings for Market Dominant Products

The table below reflects the CEM survey data responsive to the requirements in Section 3652(a)(2)(B)(ii). The results represent data from residential, small/medium business, and large business customer segments. For each row of data, the table indicates the mail service and the corresponding customer rating (combined top two box scores - Very Satisfied and Mostly Satisfied rating).

Customer Satisfaction with Market Dominant Products (Mailing Services) - FY 2011

Market Dominant Products (Mailing Services)	Residential % Rated Very/Mostly Satisfied	Small/Medium Business % Rated Very/Mostly Satisfied	Large Business % Rated Very/Mostly Satisfied
First-Class Mail	*94.20*	*92.96*	*92.10*
Single-Piece International	*86.63*	*83.86*	*89.15*
Standard Mail	*84.07*	*87.09*	*85.57*
Periodicals	*86.97*	*85.07*	*84.26*
Single-Piece Parcel Post	*89.16*	*87.93*	*87.48*
Media Mail	*88.39*	*87.11*	*86.67*
Bound Printed Matter	*86.22*	*84.90*	*84.09*
Library Mail	*86.99*	*85.90*	*86.79*

5. Comparison of Results from FY 2010 and FY 2011

The CEM system offers the advantage of: (1) random selection of large numbers of respondents; (2) a better-defined six-point rating scale compared to a five-point scale used previously; and (3) the change to reporting a more stringent top two box satisfaction rating score rather than the top-three-box scores from previous years. Product satisfaction showed rating increases in FY 2011 over FY 2010, for all products and among all the customer segments (Residential, Small/Medium Business, and Large Business). The Parcel Post rating increased the most with Residential customers (.96 points), Bound Printed Matter increased 1.50 points with Small/Medium Business customers, and Single-Piece International saw the greatest increase with Large Business Customers (2.89 points).

F. Product Analysis

1. First-Class Mail

First-Class Mail is considered by many as the "flagship" class of the Postal Service. Any matter eligible for mailing (except Standard Mail entered as Customized Market Mail) is eligible for mailing via First-Class Mail. A critical feature of First-Class Mail is that it is sealed against postal inspection, except as authorized by law. First-Class Mail is used by households for personal and business correspondence and transactions such as bill-paying. Business users may choose First-Class Mail because of its reliability and service standards, which are higher than those of Standard Mail and the other market dominant mail classes. Mail containing personal information is required to be sent First-Class Mail, Express Mail, or Priority Mail, unless it meets the Standard Mail, Periodicals, or Package Services preparation requirements for incidental First-Class Mail attachments or enclosures. Express Mail and Priority Mail, designated as competitive products, are more expensive and offer equal or faster service or other features.

Presort prices are available to First-Class Mail customers mailing letters, postcards, flats and parcels with a minimum volume requirement of 500 pieces per mailing. Presort Letters and Cards has more volume than any other product in the class and includes incentives to reduce costs and increase efficiency through worksharing, which is discussed in more detail in Section II.G.

Overall, First-Class Mail volumes continued to decline at a significant pace in FY 2011. After experiencing a 6.6 percent decline from FY 2009 to FY 2010, First-Class Mail volumes declined another 6.4 percent from FY 2010 to FY 2011, or 5.0 billion pieces. First-Class Mail volumes were most significantly impacted by the continuing effects of the recent economic recession, but electronic diversion, which is an ongoing structural problem, continued to erode mail usage.

First-Class Mail Single-Piece Letters and Cards volume declined by 10.5 percent, or 3.0 billion pieces, while Presort Letters and Cards declined by 3.7 percent, or 1.7 billion pieces. First-Class Mail Flats declined by 10.1 percent, or 251 million pieces, while First-Class Mail Parcels increased by 6.5 percent, or 39 million pieces.

The cost coverage for First-Class Mail is generally higher than other market dominant classes and, of all mail classes, First-Class Mail traditionally has made the highest contribution to covering institutional costs, due to the combination of its high volume and high cost coverage. This is a reflection of the high value of service in terms of delivery, privacy, and other features of First-Class Mail. In addition, many ancillary services are available to First-Class Mail customers. By providing a high-value service to both consumer and business customers, First-Class Mail also promotes the public policies of title 39.

The pricing for Single-Piece Letters and Cards is important to ensuring the simplicity of the price structure and maintaining identifiable relationships among the various classes of mail for postal services. Given the value of First-Class Mail, the higher cost coverage was deemed by the Commission to be appropriate in the pre-PAEA pricing regime, and remains appropriate. The continued health of First-Class Mail is of critical importance to the Postal Service, both to assure adequate revenues and, given its large volume and contribution, to help create price predictability and stability by providing a solid and reliable base.

Table 1: First-Class Mail Volume, Revenue, and Cost by Product								
Product	Volume (million)	Revenue ($million)	Attribu-table Costs	Contri-bution	Revenue/ Piece	Cost/ Piece	Unit Contri-bution	Cost Cover-age
Single-Piece Letters/Cards	25,847	$11,581	$7,185	$4,396	$0.448	$0.278	$0.170	161.19%
Presorted Letters/Cards	44,494	$15,488	$5,184	$10,305	$0.348	$0.116	$0.232	298.80%
Flats	2,231	$2,814	$1,946	$868	$1.261	$0.872	$0.389	144.58%
Parcels	638	$1,284	$1,169	$115	$2.013	$1.832	$0.181	109.88%
Domestic NSA First-Class mail	0	$0	$0	$0				
First-Class Mail Fees		$146.1						
Total First-Class Domestic Mail (incl. fees)	73,210	$31,314	$15,484	$15,830	$0.428	$0.211	$0.216	202.2%
Outbound Single-Piece First-Class Mail Int'l	310	$648	$438	$209	$2.087	$1.413	$0.674	147.7%
Inbound Single-Piece First-Class Mail Int'l	238	$136	$172	-$36	$0.573	$0.724	-$0.152	79.0%
Total First-Class Mail	73,759	$32,098	$16,095	$16,003	$0.435	$0.218	$0.217	199.4%

As shown in Table 1, in FY 2011, First-Class Mail covered its attributable costs and made a significant contribution toward the Postal Service's institutional costs.

First-Class Mail has six products: Single-Piece Letters/Postcards; Presorted Letters/Postcards; Flats; Parcels; Outbound First-Class Mail International; and Inbound Single-Piece First-Class Mail. Table 1 shows that (with the exception of Inbound Single-Piece First Class Mail) each of these products covered its attributable costs and made a contribution to institutional costs during FY 2011.

i. Single-Piece Letters and Cards

This product consists of letter-shaped single-piece First-Class Mail and single-piece First-Class Mail cards. The cost coverage for this product in FY 2011 was 161.2 percent, which is reasonable given the value of First-Class Mail service. However, this product has experienced large volume drops, larger than the First-Class Mail class average. As pointed out above, the volume drop for this product between FY 2009 and

FY 2010 was 10.5 percent, whereas the overall volume drop for First-Class Mail was 6.4 percent. As discussed above, the generally poor economic environment and the ready availability of electronic alternatives are the primary reasons for this decline.

ii. Presorted Letters and Cards

This product consists of letter-shaped presorted First-Class Mail, and presorted First-Class Mail cards. As noted above, the minimum volume requirement for eligibility is 500 pieces per mailing.

The cost coverage for First-Class Mail Presorted Letters/Cards was 298.8 percent; as discussed in footnote 21, the increasing differential between the unit contributions of the presorted and single-piece products is becoming a cause for concern. In FY 2011, product volume declined 3.7 percent. While it is the largest product within First-Class Mail, continued presort volume declines create significant financial concerns.

Worksharing in First-Class Mail is discussed further in Section II.G of this Report.

iii. Flats

The First-Class Mail Flats product consists mostly of single-piece mailings, but presort prices are offered for Mixed ADC, ADC, 3-digit, and 5-digit sortation.

iv. Parcels

Effective at the beginning of FY 2012, First-Class Mail Commercial Base Parcels, which includes single-piece (permit and IBI indicia) and presort Parcels, and First-Class Mail Commercial Plus Parcels were transferred to the competitive product list, leaving only Retail Parcels and Keys and Identification Devices in the market dominant First-Class Mail Parcels product. The FY 2011 CRA estimates of revenue, volume and costs provided in Table 1 include all First-Class Mail Parcels, including those that have now moved to the competitive list. The full product's cost coverage was 109.9 percent in FY 2011. The workshare discounts for presort First-Class Mail Parcels are discussed below in Section II.G.

v. Outbound Single-Piece First-Class Mail International

Outbound First-Class Mail International consists of Single-Piece Letters, Postcards, Flats, and Parcels. The product's FY 2011 cost coverage was 147.7 percent.

vi. Inbound Single-Piece First-Class Mail International

Inbound Single-Piece First-Class Mail International consists of single-piece Letters, Postcards, Flats, and Parcels sent from foreign postal administrations for delivery in the U.S. The Postal Service does not independently determine these prices for delivering foreign origin mail. Over a four-year period, prices for this product are set according to a Universal Postal Union (UPU) terminal dues formula established in the Universal Postal Convention. Because the UPU per item and per kilogram terminal dues rates were based on a percentage of the one-ounce retail Single Piece First-Class Mail rate and were not based on USPS costs, the FY 2011 cost coverage for this product was 79.0 percent. The Postal Service continues with its strategy for improving the total inbound cost coverage via bilateral agreements with some of its larger exchange partners in the upcoming calendar year.[5] Moreover, the present terminal dues formula resulted in a positive net contribution of single piece First-Class international mail

[5] Inbound Single-Piece First-Class Mail International at Non-UPU Rates are the result of negotiations with Canada Post Corporation and other foreign postal operators. Under the current bilateral agreement, southbound letter post rates from Canada increased in January 2011 (Docket No. R2010-2) and will increase again in January 2012 (Docket No. R2012-5). From 2012 forward, the Canada Post bilateral agreement will be included in the product grouping for Inbound International Multi-Service Agreements with Foreign Postal Operators.

because the Postal Service is a net exporter and generated significant revenue from the outbound flows.

vii. First-Class Mail Incentive Programs

Mobile Barcode Promotion Program: The 2011 Mobile Barcode Promotion Program started in July 1, 2011 and ended in August 31, 2011. Its primary intent was to generate awareness of how mobile technology can be integrated in mail campaigns. During the established program period, the Mobile Barcode Promotion provided a three percent discount, to mailers that complied with the program's eligibility requirements, on the total postage for commercial First-Class Mail and Standard Mail letters, postcards and flats that included a two-dimensional mobile barcode inside or on the mailpiece and that were sent using a permit imprint payment method. In the two month program period, the Postal Service issued over $5 million in rebates for 480 million First Class Mail pieces.

2. Standard Mail

Standard Mail is primarily used by businesses for advertising purposes. The class is also used by nonprofit customers for fundraising activities. It consists mainly of circulars and catalogs, but also includes some merchandise. Standard Mail is a commercial bulk mail class and requires a permit and a minimum of 200 pieces or 50 pounds of mail per mailing. Standard Mail pieces must weigh less than 16 ounces and must be presorted.

Standard Mail provides a lower level of service, speed and privacy, and requires greater mailer preparation than First-Class Mail; and mail processing and delivery can be deferred to meet the Postal Service's operational needs. Consistent with its lower value of service, mailers pay lower prices than for First-Class Mail. In general, business mailers use Standard Mail to send items of lower intrinsic importance and value as well as items that do not require expeditious delivery, taking advantage of the class's lower prices. And, while Standard Mail has a complex pricing structure, its principal users are sophisticated businesses that are able to handle that complexity. Moreover, the complexity of the pricing structure allows the Postal Service to flexibly tailor pricing to meet the complex needs of its customers—thereby encouraging mail use—and to encourage efficient use of the mail.

Table 2: Standard Mail Volume, Revenue, and Cost by Product

Product	Volume (million)	Revenue ($million)	Attributable Costs	Contribution	Revenue/ Piece	Cost/ Piece	Unit Contribution	Cost Coverage
HD/Sat Letters	5,654	$ 768	$ 349	$ 419	$ 0.136	$ 0.062	$ 0.074	220.0%
HD/Sat Flats & Parcels	11,425	$ 1,881	$ 883	$ 998	$ 0.165	$ 0.077	$ 0.087	213.0%
Carrier Route	9,336	$ 2,230	$ 1,648	$ 582	$ 0.238	$ 0.176	$ 0.062	135.3%
Letters	50,584	$ 9,735	$ 5,289	$ 4,447	$ 0.192	$ 0.104	$ 0.088	184.1%
Flats	6,783	$ 2,494	$ 3,143	$ (649)	$ 0.367	$ 0.463	$ (0.096)	79.4%
Parcels & NFMs	734	$ 651	$ 767	$ (117)	$ 0.887	$ 1.046	$ (0.159)	84.8%
Standard Mail NSAs	176	$ 38	$ 23	$ 15	$ 0.217	$ 0.132	$ 0.085	163.8
Standard Mail Fees	0	$ 68						
Total Standard Mail (incl. fees)	84,691	$ 17,826	$ 12,078	$ 5,748	$ 0.210	$ 0.143	$ 0.068	147.6%
Former Regular & Nonprofit Regular*	58,101	$ 12,849			$ 0.221			
Former ECR & Nonprofit ECR*	26,414	$ 4,871			$ 0.184			

* These are included to allow comparison with former subclass-level data.

As shown in Table 2, in FY 2011, Standard Mail covered its attributable costs and made a significant contribution toward covering the Postal Service's institutional costs. Standard Mail prices changed by 1.739 percent in FY 2011. As noted above, Standard Mail is used by both commercial mailers and by qualified nonprofit mailers who receive preferred pricing. By law, when the Postal Service adjusts Standard Mail prices, the average revenue per piece for Standard Mail sent by nonprofit mailers must be 60 percent of the average revenue per piece for Standard Mail sent by commercial customers. For all of FY 2011, the ratio was 66.5 percent. The recently approved Docket No. R2012-3 price adjustments, to be instituted on January 22, 2012, should help lower this ratio.[6]

In FY 2011, the Standard Mail class had six products: Letters; Flats; NFMs and Parcels; Carrier Route Letters, Flats and Parcels; High Density and Saturation Letters; and High Density and Saturation Flats and Parcels. Each product includes both commercial and nonprofit mail. Table 2 shows that each of these products, except Flats and NFMs/Parcels, covered its attributable costs and made a contribution toward institutional costs. In each of the last four fiscal years, Flats and NFMs/Parcels did not cover costs. As noted below, NFMs/Parcels are being restructured in FY 2012. Issues relating to Flats pricing are subject to a petition for review filed by the Postal Service with the Court of Appeals for the District of Columbia Circuit.

[6] As discussed in Docket No. R2012-3, the transfer of commercial Standard Mail machinable and irregular parcels to the competitive product list, to become effective on January 22, 2012, will also affect this ratio. The Postal Service believes that the Docket No. R2012-3 price adjustments will appropriately adjust for the transfer and its effect on the ratio. However, this cannot be fully evaluated until FY 2012 cost data are available.

The following sections discuss each product in greater detail. Cost coverages by product are noted in each product section below.

i. High Density and Saturation Letters

The Standard Mail High Density and Saturation Letters product is designed for businesses to send geographically targeted messages to potential customers. It is used to communicate messages that do not require the most expeditious, and therefore more expensive, mail processing and delivery. Consistent with this lower level of service, its prices are below the prices for First-Class Mail Letters. High Density and Saturation Letters are designed for advertising markets in which business customers have many alternative options to convey their messages, such as local radio and television, handbills, telephone directories, etc. The Postal Service has long recognized this fact when pricing this product. To retain and grow the volume of geographically targeted High Density and Saturation Letters, the Postal Service has maintained the prices of these categories below the price of regular Standard Mail Letters, despite the fact that all categories of Standard Mail letters are increasingly processed and delivered via the same channels. The prices for this product changed by 0.615 percent in FY 2011.

High Density and Saturation Letters has the lowest overall prices offered by the Postal Service to send advertising mail. Nevertheless, based upon FY 2011 costs, the product covered its attributable costs with a coverage of 220.0 percent, thereby making a contribution toward the Postal Service's institutional costs.

High Density and Saturation Letters are eligible for price discounts for dropshipping. Mailers who do this extra work pay lower prices consistent with the costs their worksharing avoids for the Postal Service. Based on FY 2011 avoided costs, the passthroughs of the dropship avoided costs for High Density and Saturation Letters were all below 100 percent. In Docket No. RM2009-3 the Commission determined that the Saturation letters pricing category was not a workshared category of High Density letters; therefore the pricing restrictions of section 3622(e) do not apply to the price differences between Saturation and High Density letters. A more detailed discussion of worksharing in Standard Mail is contained in Section II.G of this Report.

The Standard Mail High Density and Saturation Letters product meets the public's need for a business-oriented, lower value, lower priced alternative to First-Class Mail letters to reach geographically concentrated customers with advertising messages. The product is reasonably and fairly priced for the value its customers receive, bears a fair share of the institutional cost burden of the Postal Service, and is available to business customers without undue discrimination. Therefore, Standard Mail High Density and Saturation Letters promote the policy goals of title 39.

ii. High Density and Saturation Flats and Parcels

The Standard Mail High Density and Saturation Flats and Parcels product is designed for businesses to send geographically targeted messages to potential customers. It is also used to distribute product samples to geographically concentrated markets. This product is used to communicate messages or deliver samples that do not require the most expeditious, and therefore more expensive, mail processing and delivery. Consistent with this lower level of service, its prices are below the prices for First-Class Mail flats and parcels. The High Density and Saturation Flats and Parcels product is designed for advertising markets in which business customers have many alternative options to convey their messages, such as local radio and television, handbills, telephone directories, etc., or to distribute samples. The Postal Service has long recognized this market characteristic when pricing this product. The prices for this product changed by 0.403 percent in FY 2011.

This product has the lowest overall prices offered by the Postal Service to send advertising flats or product samples. Nevertheless, based upon FY 2011 costs, the High Density and Saturation Flats and Parcels product covered its attributable costs with a coverage of 213.0 percent, thereby making a reasonable contribution toward the Postal Service's institutional costs.

High Density and Saturation Flats and Parcels are eligible for price discounts for dropshipping. Mailers who do this extra work pay lower prices consistent with the costs their worksharing avoids for the Postal Service. Based on FY 2011 avoided costs, the passthroughs of the dropship avoided costs for High Density and Saturation Flats and Parcels were below 100 percent. In Docket No. RM2009-3 the Commission determined that the Saturation flats and parcels pricing categories were not workshared categories of High Density mail; therefore the pricing restrictions of section 3622(e) do not apply to the price differences between Saturation and High Density flats and parcels. A more detailed discussion of worksharing in Standard Mail is contained in Section II.G of this Report.

The Standard Mail High Density and Saturation Flats and Parcels product meets the public's need for a business-oriented, lower value, lower priced alternative to First-Class Mail flats and parcels options to reach geographically concentrated customers with advertising messages and lightweight merchandise samples. High Density and Saturation Flats and Parcels are required to be sequenced in delivery order (or to be addressed using sequenced detached address labels), allowing the Postal Service to deliver them more efficiently. The product is reasonably and fairly priced for the value its customers receive; it bears a fair share of the institutional cost burden of the Postal Service; and is available to business customers without undue discrimination. Therefore, the Standard Mail High Density and Saturation Flats and Parcels product promotes the policy goals of title 39.

iii. Carrier Route (Letters, Flats, and Parcels)

Although it also includes both letter- and parcel-shaped mail, the Standard Mail Carrier Route product consists predominantly of catalogs and other advertising flats sent by businesses and having a minimum address density of ten pieces per carrier route. There are relatively few letters and almost no parcels in this product.

The Carrier Route product allows businesses to send customers promotional material that does not require the most expeditious mail processing and delivery. This allows the Postal Service to reduce its costs compared to products like First-Class Mail letters, flats, and parcels; consistent with these lower costs, Standard Mail Carrier Route prices are lower than the prices for similarly-shaped First-Class Mail. Although mail pieces in this product are required to be presorted by carrier routes, delivery point sequencing has reduced the value of carrier route presorting for letters. The deployment of FSS equipment may have similar consequences for flat-shaped mail.

Carrier Route mail pieces are eligible for dropshipping discounts. Mailers who do this extra work pay lower prices consistent with the costs their worksharing avoids for the Postal Service. Based on FY 2011 avoided cost data, the passthroughs of the dropship avoided costs for Carrier Route mail pieces were all below 100 percent. Prior to Docket No. RM2009-3, the Commission had determined that there was a worksharing relationship between Carrier Route mail and High Density mail and, therefore, the pricing restrictions of section 3622(e) apply to the price differences between these categories. A more detailed discussion of worksharing in Standard Mail is contained in Section II.G of this Report.

In FY 2011, the prices for Standard Mail Carrier Route pieces changed by 1.376 percent. Table 2 shows that, based upon FY 2011 costs, the Carrier Route Letters, Flats, and Parcels product covered its attributable costs with a cost coverage of 135.3 percent. This cost coverage shows that the Carrier Route product made a reasonable contribution toward the Postal Service's institutional costs.

The Standard Mail Carrier Route Letters, Flats and Parcels product helps to meet the need for a business-oriented, lower value, lower priced alternative to First-Class Mail. The Standard Mail Carrier Route product is reasonably and fairly priced for the value its customers receive, bears a fair share of the institutional cost burden of the Postal Service, and is available to business customers without undue discrimination. Therefore, this product promotes the policy goals of title 39.

iv. Letters

The Standard Mail Letters product is used primarily for demographically targeted advertising, including fundraising by nonprofit organizations. It provides a way for businesses to communicate with customers, or potential customers, that does not require the most expeditious, and therefore, more expensive, mail processing and delivery. Consistent with these features, its prices are below the prices for First-Class Mail letters. Prices for Standard Mail Letters were increased by 1.810 percent in FY

2011. Based upon FY 2011 costs, the Letters product covered its attributable costs with a coverage of 184 percent, thereby making a reasonable contribution toward the Postal Service's institutional costs.

Standard Mail Letters are eligible for price discounts for presorting, pre-barcoding and dropshipping. Mailers who do this extra work pay lower prices consistent with the costs their worksharing avoids for the Postal Service. Based on FY 2011 cost data, there are three discounts that exceed avoided costs out of a total of nine worksharing discounts for this product. Worksharing in Standard Mail is discussed further in Section II.G of this Report.

Overall, the Standard Mail Letters product meets the need for a business-oriented, lower value, lower priced alternative to First-Class Mail letters. The product is reasonably and fairly priced for the value its customers receive, bears a fair share of the institutional cost burden of the Postal Service, and is available to business customers without undue discrimination. Therefore, Standard Mail letters promote the policy goals of title 39.

v. Flats

The Standard Mail Flats product consists primarily of advertising flyers and catalogs that are demographically targeted. It is primarily used by businesses selling merchandise and for fundraising by nonprofit organizations. Like Standard Mail Letters, it allows businesses to send existing or potential customers promotional material that does not require the most expeditious, and therefore, more expensive, mail processing and delivery. Consistent with these features, Standard Mail Flats prices are below the prices for First-Class Mail flats. In FY 2011, the prices for Standard Mail Flats increased by 0.835 percent.

Table 2 shows that the Flats product had a cost coverage of 79.4 percent in FY 2011. The Postal Service believes that pricing and efficiency measures need to be taken to move this product toward covering its costs and making an appropriate contribution toward institutional costs.

In the FY 2010 ACD, the Commission found that the prices in effect in FY 2010 for Standard Mail Flats did not comply with 39 U.S.C 101(d). The Commission stated its view that the loss in contribution from Standard Mail Flats over the last three years reflected an unfair and inequitable apportionment of the costs of postal operations to all Standard Mail users, and it directed the Postal Service to increase the product's cost coverage through a combination of above-average price adjustments and cost reductions until such time that the product's revenues exceed its attributable costs.[7]

On April 17, 2011, the Postal Service sought judicial review of this directive as (1) contrary to the express terms of the PAEA, (2) beyond the Commission's authority in the context of its review of an Annual Compliance Report, and (3) arbitrary and capricious in that the Commission failed to address the argument that such a course of action may actually result in less contribution and, therefore, have a negative impact on the Postal Service's financial stability.[8] This appeal is still pending.

In Docket No. R2011-2, the Postal Service increased Standard Mail Flats prices by 0.835 percent. This moderate increase was given in an effort to gradually move

[7] FY 2010 Annual Compliance Determination Report (ACD), Docket No. ACR2010 (Mar. 29, 2011), at 106.
[8] *U.S. Postal Service v. Postal Regulatory Commission*, No. 11-1117 (D.C. Cir.)

Standard Mail Flats towards 100 percent cost coverage without placing an undue burden on the already fragile catalog mailing industry, which depends heavily on Standard Mail Flats. The Postal Service explained that it kept the increase moderate to avoid large volume losses that might have resulted from too large price increases, especially considering that past flats price increases combined with a weak economy had resulted in a severe contraction in the catalog business. The Postal Service sees the catalog industry as a growth segment in its business over the long run and believes that increasing prices too quickly could force catalog mailers to cut their mailing lists and lose their customers, which are very costly to reacquire.

Standard Mail Flats are eligible for price discounts for presorting, prebarcoding and dropshipping. Mailers who do this extra work pay lower prices consistent with the costs their worksharing avoids for the Postal Service. In FY 2011, all discounts but four were less than or equal to their respective avoided costs. Worksharing in Standard Mail is discussed further in Section II.G of this Report.

The Standard Mail Flats product meets the need for a business-oriented, lower value, lower priced alternative to First-Class Mail. The Standard Mail Flats product is available to customers without undue discrimination, and promotes the policy goals of title 39.

vi. Parcels and Not Flat-Machinables (NFMs)

The Standard Mail Parcels and NFMs product consists of parcel-shaped pieces that do not meet the eligibility standards for letters or flats. It is primarily used by businesses fulfilling merchandise orders, for sending marketing materials that do not meet the size restrictions for letter- and flat-shaped, mail, and for fundraising by nonprofit organizations. Like other Standard Mail products, it provides an option for businesses to send customers merchandise and promotional material that do not require the most expeditious, and therefore more expensive, mail processing and delivery. Consistent with these features, Standard Mail Parcels and NFMs prices are below the prices for First-Class Mail and Priority Mail parcels.

As seen in Table 2, the Parcels and NFMs product cost coverage was 84.8 percent in FY 2011. In its FY 2010 ACD, the Commission recognized that although the NFMs/Parcels product did not produce sufficient revenues to cover its attributable cost, the Postal Service was making significant efforts to address the problem. In FY 2011, the Postal Service increased the prices for this product by 11.346 percent.

Like other Standard Mail products, Parcels and NFMs are eligible for price discounts for presorting, prebarcoding, and dropshipping. Mailers who undertake this extra work pay lower prices consistent with the costs their worksharing avoids for the Postal Service. In FY 2010, all discounts but eight were less than or equal to their respective avoided costs. Worksharing in Standard Mail is discussed further in Section II.G.

The Standard Mail Parcels and NFMs product meets the need for a business-oriented, lower value, lower priced alternative to First-Class Mail and Priority Mail parcels. It is available to customers without undue discrimination, and promotes the public policy goals of title 39.

The Standard Mail Parcels and NFMs offerings will change in FY 2012. In Order No. 1062, the Commission approved the transfer of commercial Standard Mail machinable and irregular parcels from the market dominant product list to the competitive product list, where they will become “Lightweight Parcel Select,” effective January 22, 2012.[9] Thus, Standard Mail will retain commercial machinable and irregular parcels for only a portion of FY 2012. Further, in accordance with Order No. 987, NFMs will become “Marketing Parcels” on January 22, 2012. Marketing Parcels will have different mailing standards than NFMs.[10] Some commercial NFMs used for fulfillment purposes will not meet the Marketing Parcels mailing standards and will therefore migrate to Lightweight Parcel Select. Nonprofit Parcels will remain the same, and some Nonprofit NFMs used for fulfillment purposes that do not meet the Marketing Parcels mailing standards will migrate to Nonprofit Parcels.

vii. Standard Mail Incentive Programs

Saturation Mail Incentive Program: The Saturation Mail Incentive Program began on January 1, 2011, and will end on December 31, 2011. From January 1 to September 30 2011, a total of 1,960 customers applied for the program, of which 922 qualified and remained in the program. Since the program will end December 31, no rebates have been paid, but from January 1st to September 30, the Postal Service estimates that $5.89 million would have been paid. During this same time period, the Postal Service estimates that the program generated over 218 million new pieces of Saturation mail, and produced about $29.9 million in new revenue.

Mobile Barcode Promotion Program: The 2011 Mobile Barcode Promotion Program started in July 1, 2011 and ended in August 31, 2011. Its primary intent was to generate awareness of how mobile technology can be integrated in mail campaigns.

[9] Order No. 1062, Docket No. CP2012-2 (Dec. 21, 2011). Upon transfer, the parcels will become a “Lightweight” subcategory of Parcel Select.
[10] Order No. 987, Docket No. R2012-3 (Nov. 22, 2011).

The Mobile Barcode Promotion provided a three percent discount on the total postage for commercial First-Class Mail and Standard Mail letters, postcards and flats sent using a permit imprint payment method, which include a two-dimensional mobile barcode inside or on the mailpiece, during the established program period, to mailers that comply with the eligibility requirements of the program. In the two month period, the Postal Service issued $29 million in rebates for 4.5 billion Standard Mail pieces.[11]

3. Periodicals

The Periodicals class consists of magazines, newspapers, and other periodicals that meet specific criteria for eligibility, including applicable editorial content, circulation, advertising, and other requirements established by law. Eligible publications include general publications, publications requested by the recipient, and publications of institutions and various government agencies, as well as foreign publications. The Periodicals class exists as a preferred class of mail because of periodicals' high intrinsic worth, specifically their educational, cultural, scientific, and informational value, which benefits both individuals and society.

In Docket No. R2012-3, the Postal Service filed for a CPI price increase to be effective in January 2012. The request for Periodicals was set exactly at the cap: 2.133 percent. The overall product percentage changes were 2.136 percent for Outside County and 2.054 percent for Within County. A new price cell of $3.365 was added for Origin Mixed Area Distribution Center (ADC) pallets to encourage palletization rather than sacking where feasible. This option will allow mailers who enter mail at origin to be more efficient by using origin-entered mixed ADC pallets. Because this price will

[11] Order No. 731, Docket No. R2011-5 (May 17, 2011).

encourage more efficient behavior and data are not available to model changes in mailer behavior, a conservative hypothesis that there would be no migration to the new MADC pallet price was used in calculations regarding the price cap, an approach with which the Commission concurred in Order No. 987.[12]

Periodicals has not been covering its attributable costs, and the cost coverage declined again slightly in FY 2011, to 74.9 percent. As discussed above, Periodicals' cost coverage continues to present a challenge to the Postal Service and mailers, since the Periodicals class does not satisfy section 3622(c)(2) of title 39. Further, publishers face increasing competition from electronic media, typically low profit margins, and the generally poor economic climate. Even if it were possible under the statute to increase prices to cover all costs, according to publishers, the resulting prices would drive many out of the print business altogether and speed migration to electronic alternatives. In this event, because of the drop in overall volume, it seems likely that revenues would remain below costs.

The Postal Service and the Commission, as well as Periodicals publishers and mailers, have recognized the special role and longstanding deteriorating financial situation of Periodicals. The Postal Service continues to pursue operational efficiencies as detailed in the *Periodicals Mail Study*,[13] as well as opportunities to fine-tune prices that signal the appropriate level of cost-reducing behavior. In particular, the Postal Service is focusing pricing research on bundle and container "cost passthroughs" (price

[12] Stating that no data was available on this matter, the Order said that "[t]he Commission finds that the addition of this upstream pallet option will not materially impact the price cap calculation." Order No. 987, at 39.
[13] *Periodicals Mail Study: Joint Report of the United States Postal Service and Postal Regulatory Commission* (Sept. 2011), at Chapter 6.

as a percent of cost), which have been low since the new Periodicals pricing structure was recommended by the Commission in Docket No. R2006-1. This inquiry has been encouraged by the Commission's findings in the FY 2010 ACD.[14]

Table 3: Periodicals Volume, Revenue, and Cost by Product								
Product	Volume (Million)	Revenue ($Million)	Attributable Costs ($Million)	Contribution ($Million)	Revenue / Piece ($)	Cost / Piece ($)	Unit Contribution ($)	Cost Coverage (%)
Within County Periodicals	662	69	89	(20)	0.105	0.135	(0.030)	77.5
Outside County Periodicals	6,415	1,744	2,341	(597)	0.272	0.365	(0.093)	74.5
Fees		8	-	-	-	-	-	-
Total Periodicals Mail (incl.fees)	7,077	1,821	2,430	(609)	0.257	0.343	(0.086)	74.9

The Periodicals class has two products: Within County Periodicals and Outside County Periodicals. Table 3 shows that neither product covered its attributable costs in FY 2010. The total Periodicals' coverage was 74.9 percent. As discussed above, efforts are underway to determine what steps can be taken to improve Periodicals' contribution. Although Periodicals is challenged in terms of cost coverage, its important role in allowing for dissemination of educational, cultural, scientific, and information value to the recipient of mail matter is vital, and promotes the public policies of title 39.

i. Within County Periodicals

Within County prices are available for Periodicals that are entered in the county where they are published for delivery within that county. Other detailed requirements apply. Within County Periodicals prices are lower than Outside County prices, and in FY 2011 the Within County cost coverage was slightly higher than that of Outside

[14] FY 2010 ACD, at 90.

County. As shown in Table 3, Within County Periodicals' cost coverage was 77.5 percent in FY 2011, and the revenue per piece is the same as in FY 2010.

ii. Outside County Periodicals

Periodicals mail that is not eligible for Within County Periodicals prices must pay Outside County prices. Certain categories, such as Nonprofit, Classroom, or Science of Agriculture publications, are separately authorized to qualify for Periodicals prices. There are other special provisions, including a discount for certain Outside County periodicals of limited circulation, which reflect the societal benefit of information dissemination.

As shown in Table 3, Outside County Periodicals' cost coverage was 74.9 percent in FY 2011.

4. Package Services

The Package Services class is comprised primarily of parcels and mainly used to ship merchandise, but it also includes some catalogs and other bound printed items that are too heavy to be sent as Standard Mail. Any item that is not required to be sent as First-Class Mail can be sent using one or more of the Package Services products. Package Services is used by both commercial mailers and by households, and has products and mail categories designed to meet the needs of each group of mailers. Package Services mail may weigh up to 70 pounds, except for mail entered as Bound Printed Matter Parcels or Bound Printed Matter Flats, which have lower, 15-pound, weight limits.

Package Services products provide a lower level of service and speed, and in some cases require greater mailer preparation than First-Class Mail; and mail processing and delivery can be deferred to meet the Postal Service's operational needs. Package Services mail can also be opened for postal inspection. Consistent with this lower value of service, mailers receive prices that are lower than those of First-Class Mail and Priority Mail. In general, mailers often use Package Services products to send items of lower intrinsic value and importance as well as items that do not require expeditious delivery, taking advantage of the class's lower prices.

Package Services prices increased by 1.741 percent on April 18, 2011. As shown below in Table 4, the Package Services class failed to cover its attributable costs in FY 2011. The cost coverage for the domestic products in the class as a whole was 94.0 percent.

Table 4: Package Services Volume, Revenue and Cost by Product

Product	Volume (Million)	Revenue ($Million)	Attributable Costs ($Million)	Contribution ($Million)	Revenue / Piece ($)	Cost / Piece ($)	Unit Contribution ($)	Cost Coverage (%)
Parcel Post[15]	70	732	821	(89)	10.431	11.694	(1.263)	89.2
Bound Printed Matter Flats	252	204	125	79	0.811	0.498	0.313	162.8
Bound Printed Matter Parcels	245	310	315	(5)	1.263	1.282	(0.020)	98.4
Media Mail/Library Mail	108	332	431	(99)	3.079	3.998	(0.919)	77.0
Fees		3						
Inbound Surface Parcel Post	1	19	11	8	18.641	10.543	8.098	176.8
Total Package Services Mail (incl. fees)[16]	676	1,600	1,703	(103)	2.367	2.518	(0.152)	94.0

The Package Services mail class has five products: Parcel Post; Bound Printed Matter Flats; Bound Printed Matter Parcels; Media Mail/Library Mail; and Inbound

[15] In previous years, this product has been referred to as "Single-Piece Parcel Post". Going forward, it will be referred to simply as "Parcel Post".
[16] Totals are calculated from unrounded numbers and then rounded. This is why the rounded totals do not always equal the sum of the rounded subtotals in Table 4.

Surface Parcel Post (at UPU rates). Three of the four domestic products (Parcel Post, BPM Parcels and Media Mail) had cost coverages below 100 percent, leading Package Services to fail to cover its attributable costs. Among the domestic products, only BPM Flats covered its costs. The Postal Service is concerned about the financial condition of these products, and is addressing the situation by increasing prices more for the products that are failing to cover costs and less for BPM Flats.

i. Parcel Post

Any mailable matter that is not required to be sent using First-Class Mail, or to be entered as Periodicals, can be sent using Single-Piece Parcel Post. This product meets the needs of businesses and households for a lower cost way to ship parcels that do not require the most expeditious, and therefore more expensive, mail processing, transportation, and delivery. Consistent with this less expedited service, the prices for Single-Piece Parcel Post are below the prices for retail Priority Mail. By offering a lower priced, less expedited alternative to Priority Mail, Single-Piece Parcel Post promotes the policy goals of title 39.

Single-Piece Parcel Post has a price structure that is simple and conceptually easy for retail customers to understand. For its single pricing category, prices vary by weight and distance. Prices are presented in a convenient, easy to read table. Single-Piece Parcel Post has no worksharing pricing categories, and no special mail preparation is required to use this product.

Table 4 shows that Single Piece Parcel Post had a cost coverage of 89.2 percent in FY 2011. The Postal Service believes pricing and product actions need to be taken to improve Single-Piece Parcel Post's cost coverage. In Docket No. R2012-3, the Postal

Service proposed an increase of 2.47 percent to move Single-Piece Parcel Post closer to covering its costs.

ii. Bound Printed Matter Flats

Like Media Mail (discussed below), Bound Printed Matter (BPM) Flats is a content-restricted product. This product is a commercial product that is used by businesses to send large catalogs and similar flat-shaped flexible items that are too heavy to be sent using Standard Mail. Unlike Media Mail, BPM Flats are mainly advertising matter, and are not typically used for personal, literary, or educational correspondence. BPM Flats mail pieces may weigh up to 15 pounds, though most heavier pieces do not meet the physical dimensions to qualify as Flats and must be mailed using the BPM Parcels product.

The BPM Flats product meets the needs of businesses seeking to send customers promotional material that does not require the most expeditious mail processing and delivery. This allows the Postal Service to reduce its costs compared to products like Priority Mail. Consistent with these lower costs, BPM Flats prices are lower than the prices for similarly-shaped Priority Mail. Mailers can lower their cost of mailing even further by dropshipping, presorting, or prebarcoding. Mailers who do this extra work pay lower prices consistent with the costs their worksharing avoids for the Postal Service. In FY 2011, the passthroughs of the worksharing avoided costs for BPM Flats mail pieces are all at or below 100 percent, with one exception (the DNDC discount). Worksharing in BPM Flats is discussed further in Section II.G. The BPM Flats rate design is more complex than that of Media Mail or Parcel Post, but it is a business product, and its users are overwhelmingly sophisticated commercial mailers for whom the complexity of the pricing schedules should pose no problems.

BPM Flats prices increased by 0.7 percent in April, 2011. Table 4 shows BPM Flats covered its attributable costs with a cost coverage of 162.8 percent in FY 2011. This cost coverage shows that BPM Flats made a reasonable contribution toward the Postal Service's institutional costs.

The BPM Flats product helps to meet the need for a business-oriented, lower value, lower priced alternative to Priority Mail to send large catalogs that cannot be sent using Standard Mail. BPM Flats is reasonably and fairly priced for the value its customers receive, bears a fair share of the institutional cost burden of the Postal Service, and is available to business customers without undue discrimination. Therefore, BPM Flats promotes the policy goals of title 39.

iii. Bound Printed Matter Parcels

Bound Printed Matter (BPM) Parcels is a content-restricted product with the same content requirements as BPM Flats. This product is a commercial product that is used by businesses to send books, directories, and large catalogs that are too heavy to be sent using Standard Mail, and too rigid or too thick to qualify as BPM Flats. Unlike Media Mail, BPM Parcels may contain advertising matter. BPM Parcels may weigh up to 15 pounds.

The BPM Parcels product mainly meets the needs of businesses seeking to fulfill customer orders for books and large catalogs that do not require the most expeditious mail processing, transportation, and delivery. This lower level of service allows the Postal Service to reduce its costs compared to products like Priority Mail. Consistent with its lower costs and value, BPM Parcels prices are lower than the prices for similarly-shaped Priority Mail. Mailers can lower their cost of mailing even further by dropshipping, presorting, or pre-barcoding. Mailers who do this extra work pay lower prices consistent with the costs their worksharing avoids for the Postal Service. In FY 2011, the passthroughs of the worksharing avoided costs for BPM Parcels mail pieces are all at or below 100 percent (with the exceptions of the DNDC discount and DDU discount). Worksharing in BPM Parcels is discussed further in Section II.G. The BPM Parcels price design is more complex than that of Media Mail or Parcel Post, but it is a business product and its users are overwhelmingly sophisticated commercial mailers for whom the complexity of the pricing schedules should pose no problems.

The prices for BPM Parcels were increased by 2 percent in April 2011. Table 4 shows that BPM Parcels had a coverage of 98.4 percent in FY 2011. The 98.4 percent cost coverage represents significant improvement over the 92.1 percent cost coverage reported in FY 2010. Additional pricing and product actions can improve BPM Parcels' cost coverage to 100 percent.

The BPM Parcels product helps to meet the need for a business-oriented, lower value, lower priced alternative to Priority Mail to send books and large catalogs that cannot be sent using Standard Mail or BPM Flats products. The BPM Parcels product is reasonably and fairly priced for the value its customers receive, and is available to business customers without undue discrimination. Therefore, BPM Parcels product promotes the policy goals of title 39.

iv. Media Mail / Library Mail

Media Mail / Library Mail is a content-restricted product. By law, its content is restricted to books, noncommercial films, computer-readable media, and similar media items that typically have educational, cultural, scientific or informational value. Media Mail items cannot contain advertising, other than incidental announcements of books. This product is used by businesses and by the general public to send books and eligible media or other permitted items either for business, or for personal, educational, or literary purposes. Library Mail is a preferred-price category in this product. Libraries, educational institutions and certain other nonprofit organizations use Library Mail to send eligible items to their customers.[17] By law, Media Mail / Library Mail prices are unzoned and do not vary by distance.

Media Mail / Library Mail meets the needs of businesses, households, and eligible organizations for a low cost way to ship eligible materials that do not require the most expeditious, and therefore more expensive, mail processing and delivery. Consistent with this lower value of service, the prices for this product are below the prices for retail Priority Mail and Single Piece Parcel Post. The prices for Media Mail / Library Mail were increased by 2 percent in April 2011. Table 4 shows that Media Mail/Library Mail's coverage was 77.0 percent in FY 2011.

Media Mail / Library Mail has a simple price structure. Within each pricing category, the prices vary only by weight. The product has two worksharing pricing categories to meet the needs of business mailers, in addition to its single piece category that is used by both businesses and consumers. Media Mail / Library Mail users are

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[17] Library Mail has similar, though not identical, content restrictions as Media Mail.

eligible for price discounts for presorting and pre-barcoding. Mailers who do this extra work pay lower prices. The discounts for basic presorting and for pre-barcoding are consistent with the costs their worksharing avoid for the Postal Service. In FY 2011, all passthroughs of the worksharing avoided costs were at or below 100 percent for Media Mail/Library Mail. Worksharing in Media Mail / Library Mail is discussed further in Section II.G of this Report.

By law, Library Mail prices are to be set at 95 percent of Media Mail prices. The current prices meet this requirement.

Media Mail / Library Mail meets the public's need for an affordable business- and consumer-oriented, lower value, lower priced alternative to Priority Mail and Single Piece Parcel Post to mail books and other eligible matter. Its pricing meets all the requirements specific to this product described in the law. It is available to customers without undue discrimination, and its pricing reasonably and fairly reflects the value its customers receive and the educational, cultural, scientific and informational value of its content. In general, Media Mail /Library Mail is consistent with the policy goals of title 39.

5. Special Services

Table 5: Special Services Mail Volume, Revenue and Cost by Product

Product	Volume (Million)	Revenue ($Million)	Attributable Costs ($Million)	Contribution ($Million)	Revenue / Piece ($)	Cost / Piece ($)	Unit Contribution ($)	Cost Coverage
Certified Mail	251.2	708.8	599.3	109.4	2.82	2.39	0.44	118.26%
COD	0.8	6.7	4.4	2.3	8.15	5.34	2.81	152.69%
Insurance	34.6	116.7	103.4	13.2	3.37	2.99	0.38	112.80%
Registered Mail	2.7	45.2	42.8	2.4	16.83	15.93	0.90	105.67%
Stamped Envelopes	N/A	10.6	6.9	3.7	N/A	N/A	N/A	154.34%
Stamped Cards	53.7	1.6	0.8	0.8	0.03	0.02	0.01	196.48%

Other Ancillary Services	N/A	771.7	579.5	192.26	N/A	N/A	N/A	133.18%
Total Ancillary Services	N/A	1,661.3	1,337.1	324.2	N/A	N/A	N/A	124.25%
Int'l Ancillary Services	2.4	32.7	38.8	-6.1	13.71	16.286	-2.579	84.16%
Caller Service	N/A	92.2	27.8	63.3	N/A	N/A	N/A	331.69%
Address Management Services	N/A	15.4	9.9	5.5	N/A	N/A	N/A	155.56%
Change of Address Credit Card Authentication*	12.1	12.1	N/A	N/A	N/A	N/A	N/A	N/A
Confirm	N/A	3.0	1.1	1.6	N/A	N/A	N/A	276.42%
Customized Postage	5	1.5	0.1	1.4	N/A	N/A	N/A	3000.00%
Int'l Reply Coupon Service	N/A	0.2	N/A	N/A	N/A	N/A	N/A	N/A
Int'l Business Reply Mail Service	0.2	0.2	N/A	N/A	1.45	N/A	N/A	N/A
Money Orders	115.5	172.7	123.4	49.26	1.50	1.07	0.43	139.90%
Post Office Box Services	N/A	801.9	592.8	209.1	N/A	N/A	N/A	135.28%
Stamp Fulfillment Services	2.7	2.7	5.2	-2.5	1.01	1.93	-0.92	52.1%
Total Special Services Mail**	N/A	2,795.86	2,108.5	687.4	N/A	N/A	N/A	132.6%

* See USPS-FY11-NP26 for cost after revenue-sharing with third-party partners.

Special Services includes a broad spectrum of products. Ancillary Services is a product comprised of the many services that may be obtained in conjunction with other products. The other products within Special Services are generally "stand-alone" in that they can be purchased without necessarily paying postage for any other product. Rather than recite the policy goals for each of the products in the sections below, it is noted that the many services meet the specific needs of customers, are priced in a manner that is fair for the value they provide, and cover their attributable costs. Thus, Special Services generally promote the policy goals of title 39.

i. Ancillary Services

The Ancillary Services are those Special Services that may only be used in conjunction with another product. Some of the services are quite small, whereas others, such as Certified Mail ($708.8 million in revenue), raise substantial revenue. Total revenues for all Ancillary Services in FY 2011 were $1.7 billion.

ii. International Ancillary Services

International Ancillary Services generated $32.7 million in revenue in FY 2011, up from $25.6 million in 2009, with a cost coverage of 84.2 percent. The negative contribution is fully attributable to inbound registered mail, which is priced by the Universal Postal Convention with no direct relationship to the cost of the service. Despite the product-specific negative contribution of inbound registered mail, the UPU Convention still offers the opportunity for favorable destination delivery costs for outbound mail, thereby enhancing contribution on outbound flows.

iii. Address Management Services

The Postal Service provides address management services to decrease the amount of undeliverable mail and to help mailers enter mail that has better address hygiene. Total revenue for Address Management Services in FY 2011 was $15.4 million.

iv. Caller Service

Caller Service includes revenues from both Caller Service and Reserve Number products. Caller Service allows business customers to pick up their box mail at a Post

Office call window or loading dock when the office is open. Caller Service customers may choose when to pick up their mail and, accordingly, can have increased access to their mail, even if the box section is not open.

Reserve Numbers allow a company to reserve a box number for future Caller Service use. Caller Service and Reserve Number revenues were $92.2 million in FY 2011.

v. Change-of-Address Credit Card Authentication

To ensure that Change of Address Requests made either over the phone or via the Internet are valid, the Postal Service charges a fee of $1 to a credit card to ensure that the address for which the change is requested matches the address on the credit card used to pay the $1 fee. In FY 2011, customers paid $12.1 million, but the Postal Service accrued only a portion of that revenue, since some of it is retained by a third party for administering this service. Postal Service revenue and cost coverage information are provided in USPS-FY11-NP26.

vi. Confirm

Confirm allows business subscribers to monitor specifically barcoded letters and flats as they are processed. Confirm service generated $3.0 million in revenue in FY 2011.

vii. International Reply Coupon Service

International Reply Coupon Service generated $0.2 million in revenue in FY 2011. The ICRA does not report costs for this service.

viii. International Business Reply Mail Service

International Business Reply Mail Service generated $0.2 million in revenue in FY 2011. The ICRA does not report costs for this service.

ix. Money Orders

The three types of Postal Service Money Orders (APO/FPO, up to $500 and over $500) generated a combined $172.7 million in revenue in FY 2011.

x. Post Office Box Service

Post Office Box Service includes revenues from Post Office Box fees. Post Office Boxes are available in 5 different sizes and have seven different fee groups. The service accounted for $801.9 million in revenues in FY 2011.

During FY 2011, the Commission approved the Postal Service's proposal to shift the cost of providing fee group E PO Box Service from PO Box Service attributable costs to Postal Service institutional costs.[18] The institutionalization of fee group E costs plus a drop in facility related expenses, mainly due to building depreciation, caused market dominant PO Box Service costs to decline from $675 million in FY 2010 to $593 million in FY 2011. As a result, the cost coverage of market dominant PO Box Service increased to 135 percent.

xi. Customized Postage

Customized Postage is the fee charged for the authority to produce stamps that bear customer-selected images or logos aligned with Postal Service-approved indicia of postage. In FY 2011 $1.5 million dollars in revenue were collected for these fees, although $300,000 of this revenue is the result of a late payment by one of the four customers in FY 2010. In any case, revenue is well above costs for this product.

[18] Order No. 774, Docket No. RM2011-9 (June 9, 2011).

xii. Stamp Fulfillment Services (SFS)

There was $2.7 million of revenue resulting from the fees charged for the fulfillment of stamp orders via Stamp Fulfillment Services in FY 2011. Stamp Fulfillment Services had attributable costs of $5.2 million, resulting in a cost coverage of 52.1 percent. The Postal Service is instituting a particularly large price increase for Stamp Fulfillment Services on January 22, 2012; this should significantly improve the product's cost coverage.

6. Negotiated Service Agreements (NSAs)

The Postal Service had three domestic market dominant Negotiated Service Agreements (NSAs) in effect during FY 2011, with Bradford Group, Lifeline Screening, and Discover Financial Services. Only Bradford Group qualified for discounts.[19] Details are provided in USPS-FY11-30.

The domestic NSAs in effect in FY 2011 were intended to improve the net financial position of the Postal Service by driving the growth of profitable volume (and thus increasing overall contribution to institutional costs). By providing discounts on incremental pieces above a threshold, these NSAs encouraged customers to mail more pieces than they otherwise would have. Because those pieces still provided additional contribution to institutional costs, even after discounts were included, the NSAs contributed to the improvement of the net financial position of the Postal Service. The data in USPS-FY11-30 show that the amount of rebates paid pursuant to the NSAs in the contract years ending in FY 2011 was $114,000.

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[19] The first contract year for the Discover NSA has not been completed. Therefore, under the terms of the agreement, postage rebates have not yet been earned and the contract cannot yet be evaluated using the methodology discussed here.

Using the valuation method traditionally employed by the Postal Service, the calculations in USPS-FY11-30 show a cumulative net benefit (after rebates are deducted) of negative $114,000. Using the Panzar/Wolak approach employed by the Commission, however, the cumulative net effect was $55,038. Under either method, the cumulative net effect of the NSAs was not sufficient to materially alter the reported overall contribution or cost coverage for Standard Mail. The Postal Service has no reason to believe that any of these NSAs caused unreasonable harm in the marketplace. The scale of the domestic agreements was sufficiently small to make market effects unlikely, and similar functionally-equivalent NSAs were, or could have been, made available to similarly-situated mailers.

G. Workshare Discounts

With respect to each market dominant product for which a workshare discount was in effect during the reporting year, section 3652(b) of the PAEA requires that the Postal Service provide:

> (1) The per-item cost avoided by the Postal Service by virtue of such discount.
>
> (2) The percentage of such per-item cost avoided that the per-item workshare discount represents.
>
> (3) The per-item contribution made to institutional costs.

The data for workshare discounts can be found in USPS-FY11-3.[20] In that item, the workshare discounts are shown as the difference between the current prices of the workshared piece and a benchmark piece. Passthroughs are calculated for each

[20] USPS-FY11-3 cites to the applicable cost studies that have also been filed. Also, an alternate version of USPS-FY11-3 is filed reflecting the cost avoidance resulting from proposed methodological changes filed in various carwash proposals.

discount as the ratio of the discount to the avoided cost. Per-item unit contribution is addressed at the product level in the CRA, reflecting data availability at this time. USPS-FY11-3 does not analyze non-workshare price differences.

1. Order No. 536

On September 14, 2010, the Commission issued Order No. 536 containing its decision in rulemaking Docket No. RM2009-3. The Order attempted to resolve some disputed interpretations of the worksharing provisions of the PAEA, provided direction for the implementation of those provisions, and gave notice of a follow-on rulemaking to establish an appropriate benchmark for Presort First-Class Mail workshare discounts. The Order would significantly impact the way prices are set for First-Class Mail presorted letters and for Carrier Route, High Density and Saturation Standard Mail. The Postal Service petitioned the United States Court of Appeals for the District of Columbia Circuit to review aspects of Order No. 536.

The Court's dismissal of the Postal Service's petition for review on the ground that the petition was premature indicates that the Commission must complete its work and establish a new benchmark for Presort First-Class Mail workshare discounts in Docket No. R2010-13 before the analytical framework adopted in Order No. 536 can govern any workshare discounts. Until that time, the Postal Service will continue to price its products accordingly. Once the Commission adopts a benchmark at the conclusion of the current rulemaking proceeding, the Postal Service intends to petition for review again, raising the same issues it raised in the earlier petition along with any other issue that may develop in the current rulemaking proceeding.[21] Nothing in this Report is intended to waive any of the Postal Service's arguments to the Court.

2. Application of Section 3622(e) to Passthroughs

In evaluating passthroughs for the 2011 ACR, the Postal Service notes that changes in costs between FY 2010 and FY 2011 result in some passthroughs increasing and some decreasing. In fact, some discounts now have passthroughs below 100 percent whereas the passthroughs for the same discounts estimated in the 2010 ACR were at or above 100 percent, and some discounts now have passthroughs greater than 100 percent, when they formerly were below.

Overall, any evaluation of the statutory appropriateness of passthroughs needs to be made in the context not only of the calculated cost avoidance, but also considering all of the statutory criteria, such as the objective that prices be predictable and stable. An increase or decrease in a passthrough based on the cost avoidance calculated for a given fiscal year does not in itself trigger the requirement for an immediate price change. Rather, it is an indication that a specific discount / cost avoidance relationship needs to be fully re-evaluated in the context of all of the statutory criteria, as well as pending price adjustments.

[21] In the FY 2010 ACD, the Commission noted presort customers' concern that the presort cost coverages were too high and could soon be not "just and reasonable." FY 2010 ACD, at 85. In response, the Commission stated that it would continue to monitor these cost coverages to ensure compliance with the law. *Id.* Unfortunately, in FY 2011, the difference between the unit contributions of presorted First-Class Mail letters and single-piece First-Class Mail Letters increased (from 5.2 cents in FY 2010 to 6.1 cents in FY 2011). Under the Commission's workshare rules, this difference in unit contribution is almost certain to grow. Thus, the Commission's current interpretation and application of the workshare provision appears to be on a collision course with the clear statutory objective of a just and reasonable rate schedule. The Commission should restart its workshare rulemaking, stayed during the pendency of the Postal Service's petition for review to the United States Court of Appeals for the District of Columbia Circuit, and address this looming conflict.

As the Postal Service has noted below for each of the passthroughs exceeding 100 percent in FY 2011, this re-evaluation will be undertaken by the Postal Service when it prepares its next price adjustment, and will then be reviewed by the Commission. This approach is consistent with subsections (B) and (D) of section 3622(e)(2) – the efficient operation of the Postal Service and the need to mitigate rate shock necessitate a measured approach to adjusting passthroughs. It would be inefficient and unduly disruptive to the Postal Service and to its customers to immediately adjust prices to adjust passthroughs that exceed 100 percent. The inability of customers to rely on stability of prices between regularly scheduled price adjustments would significantly undermine the ability of the Postal Service to use prices to signal efficient behavior.

As the Postal Service has stated in the past, section 3622(e) must be applied over the long term, as a principle that should guide pricing over a series of price adjustments.[22] This comprehensive, long-term approach is especially critical given the fragility of the current business environment and the desirability of maintaining and encouraging mail usage.

3. First-Class Mail

i. Single-Piece Letters and Cards

The First-Class Mail Single-Piece Letters and Cards product has just one worksharing discount, which is applicable to both Qualified Business Reply Mail (QBRM) Letters and QBRM Cards. The calculated passthrough for this discount has increased from 164.3 percent in FY 2010 to 287.5 percent in FY 2011. The increase

[22] *See* Response of the United States Postal Service to Commission Information Request No. 1, Docket No. R2008-1 (Mar. 4, 2008).

stems from a significant reduction in avoided cost, from 1.3 cents to 0.8 cents. In future price adjustments, the Postal Service will be mindful of this passthrough. In Docket No. R2012-3, the Postal Service reduced the QBRM discount from 2.3 cents to 2.2 cents, which should help in gradually moving the passthrough towards 100 percent.

ii. Presorted Letters and Cards

Given the Commission's position in Order No. 536 that there is a worksharing relationship between single-piece letters and presort letters but that the Bulk Meter Mail (BMM) benchmark is no longer valid, the calculations of the Automation Mixed AADC Letters and Nonautomation Presort Letters passthroughs are no longer meaningful. Nonetheless, in the absence of a new benchmark from Docket No. RM2010-13 and a resolution from the Court of Appeals as to whether a worksharing relationship exists between single-piece mail and presorted mail, the Postal Service is continuing to provide passthrough calculations for Automation Mixed AADC Letters and Nonautomation Presort Letters using BMM Letters as a benchmark.

Out of the seven other First-Class Mail presorted letters and cards workshare discounts, the passthroughs for five exceed 100 percent. The passthrough for Automation AADC Letters is 104.8 percent in FY 2011, no change from FY 2010 ACD. The cost avoidance for this particular presort level was 2.1 cents in the last ACR. Proposal Nine methodological changes increased it to 2.2 cents. The current estimate is once again at 2.1 cents. The current discount is 2.2 cents. Also, in Docket No. R2012-3 the Postal Service proposed and the Commission approved a uniform price for both AADC and 3-Digit Automation Letters. Once the network rationalization initiative presented in Docket No. N2012-1 is implemented, the Postal Service expects to propose a combined, possibly plant level, sort for this mail. The Postal Service would estimate cost avoidances based on the redesigned network and offer discounts based on its new operational environment and market needs.

The passthrough for 5-Digit Automation Letters is 104.2 percent in FY 2011, compared to 84.6 percent in FY 2010. This cost avoidance has shrunk from 2.6 cents in FY 2010 to 2.4 cents in FY 2011. Docket No. R2012-3 prices to be implemented in January 2012 should return this passthrough to 100 percent.

The passthrough for Mixed AADC Automation Cards is 131.6 percent in FY 2011, compared to 55.6 percent in FY 2010. The shift is due in large part to the cost avoidance declining from 2.7 cents in FY 2010 to 1.9 cents in FY 2011. The Postal Service will take into account this new smaller cost avoidance in future price changes.

The passthrough for Automation AADC Cards is 120 percent in FY 2011, compared to 90.9 percent in FY 2010. The FY 2011 cost avoidance is 1.0 cents, down from 1.2 cents in FY 2010, while the current discount is 1.2 cents. Upon the implementation of the Docket No. R2012-3 prices in January 2012, the discount will be reduced to 1.1 cents, lowering the passthrough to 109 percent. Postal Service will be mindful of this passthrough in future price changes.

The passthrough for 5-Digit Automation Cards is 116.7 percent in FY 2011, compared to 92.9 percent in FY 2010. The cost avoidance has changed from 1.4 cents in FY 2010 to 1.2 cents in FY 2011, while the discount remains at 1.4 cents. The Postal Service will be mindful of the new cost avoidance in future price changes.

iii. Flats

Two of the First-Class Mail Flats passthroughs exceed 100 percent. The Automation ADC Flats passthrough has been reduced to 226.4 percent in FY 2011, from 277.3 percent in FY 2010, as a result of an increase in the cost avoidance and a slight reduction in the discount. The 3-Digit Automation Flats passthrough is 134.9 percent in FY 2011, compared to 108.9 percent in FY 2010. The increase occurred despite a reduction in the discount from 6.1 cents to 5.8 cents. The current cost avoidance is 4.3 cents compared to 5.6 cents in FY 2010. The Postal Service will be mindful of these passthroughs in future price changes.

iv. Parcels

The resulting passthroughs within this product are 12.1 percent and 30.1 percent for 3-Digit and 5-Digit Presort Parcels, respectively, compared to 15.4 and 36.7 percent in FY 2010. They are both lower than 100 percent, as they were in the FY 2010 ACD. Given that First-Class Mail Parcels' cost coverage is only 109 percent, higher passthroughs for this product were not necessary or desirable in FY 2011. In FY 2012, the Presort Parcels will be on the competitive product list, so the workshare rules will not apply.

4. Standard Mail

i. Letters

Three workshare passthroughs for Standard Mail Letters exceed 100 percent. The passthrough for nonautomation 3-digit nonmachinable letters is 152.0 percent in FY 2011, down from 258.8 percent in FY 2010. The passthrough for nonautomation ADC nonmachinable letters is 117.5 percent in FY 2011, compared to 78.4 percent in FY

2010. The passthrough for nonautomation 5-digit nonmachinable letters is 125.7 percent, compared to 111.4 percent in FY 2010.

The latter two passthroughs increased because of changes in cost estimates between FY 2010 and FY 2011. In Docket No. R2011-2 the Postal Service aligned all three of these discounts with avoided costs. The Postal Service intends to adjust prices toward setting discounts at or below avoided costs in the next general price change.

ii. Flats

Three workshare passthroughs for presorted Standard Mail Flats exceed 100 percent: The passthrough for automation 3-digit flats is 121.7 percent in FY 2011, compared to 121.4 percent in FY 2011. The passthrough for nonautomation 3-digit flats is 106.1 percent in FY 2011, compared to 73.8 percent in FY 2010. The passthrough for nonautomation 5-digit flats is 118.8 percent in FY 2011, compared to 118.3 percent in FY 2010.

In Docket No. R2011-2, the Postal Service aligned the nonautomation 3-digit flats and nonautomation 5-digit flats presort discounts with avoided costs. In that same price adjustment, the nonautomation 3-digit flats presort discount was set at 85.2 percent of avoided costs. These three passthroughs are above 100 percent in FY 2011 because of changes in cost estimates between FY 2010 and FY 2011. The Postal Service intends to adjust prices to move toward setting discounts at or below avoided costs in the next general price change.

In addition, the passthrough for pre-barcoded automation mixed ADC flats exceeds 100 percent. The passthrough is 271.4 percent in FY 2011, compared to 248.0 percent. In the FY 2010 ACR, the Postal Service noted that this large discount was necessary to encourage pre-barcoding of flats as a way to support the implementation of the Flats Sequencing System program. In Docket No. R2011-2, the Postal Service began the process or moving this discount closer to avoided costs, lowering the discount from 6.2 cents to 5.7 cents. A decrease in the avoided costs between FY 2010 and FY 2011, from 2.5 cents to 2.1 cents, however, has caused the passthrough to increase. The Postal Service intends to gradually eliminate the excess incentive over a series of general price adjustments, to avoid rate shock.

iii. Parcels and NFMs

Five passthroughs for presorted Standard Mail Parcels and NFMs exceed 100 percent. The passthrough for NDC machinable parcels is 114.6 percent in FY 2011, compared to 99.6 percent in FY 2010. The passthrough for NDC irregular parcels is 300.8 percent in FY 2011, down from 330.9 percent in FY 2010. The passthrough for SCF irregular parcels is 146.2 percent in FY 2011, compared to 115.8 percent in FY 2010. The passthrough for NDC NFMs is 180.4 percent in FY 2011, down from 219.2 percent in FY 2010. And the passthrough for SCF NFMs is 139.3 percent in FY 2011, compared to 127.7 percent in FY 2010.

In FY 2011, the Commission approved the use of a new cost model for Standard Mail NFMs and Parcels. This new model has resulted in significant changes in the avoided cost estimates for NFMs and Parcels worksharing and is the primary reason why the above five passthroughs exceed 100 percent. The Postal Service does not intend to maintain these presort discounts permanently above avoided costs, although the large changes required to adjust some of the current discounts down to the new avoided costs may require a transition period to avoid rate shock and to avoid unduly disrupting the Postal Service's operations. Nevertheless, the Postal Service will attempt to reduce or eliminate these excess presort discounts in the next general price change where it can do so without running the risk of rate shock.[23]

Three passthroughs for pre-barcoded Standard Mail Parcels and NFMs exceed 100 percent. The passthroughs for pre-barcoded mixed NDC machinable parcels, mixed NDC irregular parcels, and mixed NDC NFMs are all 156.1 percent in FY 2011, down from 184.2 percent in FY 2010.

In the FY 2010 ACR, the Postal Service noted that these discounts were necessary to promote a totally pre-barcoded incoming parcel mailstream, which would allow elimination of keying stations at sorting facilities and facilitate implementation of electronic manifesting (a cost savings not incorporated in the barcoding savings estimate). In the FY 2010 ACD, the Commission found the non-barcoded surcharge to be justified at 7.0 cents. In Docket No. R2011-2, the Postal Service reduced the surcharge to 6.4 cents, believing that the surcharge's purposes could still be met at the lower level.

The previous Standard Mail NFMs and Parcels cost model used for the FY 2010 ACR did not estimate costs separately for pre-barcoded and non-barcoded Standard

[23] In Order No. 1062, Docket No. CP2012-2 (Dec. 21, 2011), the Commission approved the transfer of commercial machinable and irregular parcels (which comprised the great majority of parcels volumes) to the competitive products list. Earlier, in Order No. 987, Docket No. R2012-3 (Nov. 22, 2011), the Commission approved the classification changes that terminated the NFMs classification and developed the Marketing Parcels classification in its place. The foregoing statements about the Postal Service's intentions to adjust discounts toward avoided costs assume that the avoided costs for the FY 2011 full (pre-transfer) parcels category and for the NFMs category will be appropriate proxies for the costs of the remaining (nonprofit fulfillment) parcels, and for the costs of Marketing Parcels, respectively. The Postal Service will evaluate cost information on these significantly altered classifications as it becomes available to determine the appropriateness of these assumptions. Furthermore, the substantial changes in the definition of Standard Mail parcels, with the reclassification of the majority of these pieces to the competitive side, will introduce significant uncertainty as to whether the cost avoidances will be similar next year.

Mail NFMs and Parcels. The new cost model approved in FY 2011 provides separate cost estimates for pre-barcoded and non-barcoded pieces. The new model has estimated the avoided costs for prebarcoding Standard Mail parcels and NFMs to be 4.1 cents. In light of this information, the Postal Service will re-examine the non-barcoded surcharge in its next general price adjustment to determine how the surcharge should be modified in light of the purposes of the surcharge as well as the results of the new cost model.

5. Periodicals

Section 3622(e)(2)(C) exempts passthroughs for discounts "provided in connection with subclasses of mail consisting exclusively of mail matter of educational, cultural, scientific and informational value" from the 100 percent passthrough standard of section 3622(e), a provision which covers the entire Periodicals class. Nonetheless, the Postal Service recognizes the importance of detailed cost data with regard to Periodicals, and in the interest of openness and transparency, describes the Periodicals passthroughs below.

i. Outside County

Using the FY 2011 costs presented in this ACR, ten passthroughs exceed 100 percent.

In the Presorting category, three passthroughs of these fell between 102 percent and 116 percent. They were Machinable Nonautomation 5-digit flats compared to the benchmark Machinable Nonautomation 3-digit/SCF flats at 102.1 percent; Nonmachinable Nonautomation ADC flats compared to the benchmark Nonmachinable Nonautomation MADC flats at 110.5 percent; and High Density flats compared to the benchmark Carrier Route flats at 116.0 percent. Two of the Presorting passthroughs were high: the passthrough for Nonmachinable Automation 3-digit/SCF flats compared to the benchmark of Nonmachinable Automation ADC flats was 677.8 percent, and the passthrough for Nonmachinable Nonautomation 3-digit/SCF flats compared to the benchmark Nonmachinable Nonautomation flats was 937.5 percent.

The two Pre-Barcoding passthroughs were above 100 percent: Machinable Automation MADC flats compared to the benchmark Machinable Nonautomation MADC flats was 123.1 percent and Nonmachinable Automation MADC flats compared to the benchmark Nonmachinable Nonautomation MADC flats was 750 percent.

The passthrough between Machinable Automation 5-digit flats and Machinable Automation 3-digit/SCF was exactly 100 percent. Outside County passthroughs not discussed above were less than 100 percent.

Passthroughs for Automation letters are significantly above 100 percent; but the impact is negligible, given that the volume is very low.

ii. Within County

All Within County passthroughs were below 100 percent.

6. Package Services

i. Media Mail / Library Mail

All passthroughs for both Media Mail and Library Mail were at or below 100 percent in FY 2011.

ii. BPM Flats and BPM Parcels

Three passthroughs for BPM Flats and BPM Parcels exceed 100 percent. The passthroughs for the BPM Flats and BPM Parcels DNDC drop ship discounts are both

102.4 percent, down from 126.2 percent for Flats and 125.1 for Parcels in FY 2010. The passthrough for the BPM Parcels DDU drop ship discount is 100.8 percent, down from 104.3 percent in FY 2010. The Postal Service intends to further reduce these passthroughs through its next price adjustment, provided that these adjustments can be made without undue risk of rate shock to the affected mail categories.

III. COMPETITIVE PRODUCTS

A. Applicable Requirements of Title 39

By FY 2009, prices and fees in effect during the entire fiscal year had been established under PAEA procedures, rather than under the previous PRA procedures.[24] Therefore, the price setting standards set forth in the PAEA should be applied in evaluating statutory compliance for FY 2011.

B. Product-by-Product Costs, Revenues, and Volumes

For FY 2011, cost, revenues, and volumes for competitive products of general applicability are shown directly in the FY 2011 CRA (or ICRA). In the Public CRA, competitive products are disaggregated into five groups – Total Express Mail, Total Priority Mail, Total Ground, Total International Competitive, and Competitive Services. The constituent products for each of those groups are listed in a table in the attached Application for Non-Public Treatment of the Non-Public Annex (Attachment Two). Those groups are further disaggregated in the Nonpublic CRA (USPS-FY11-NP11). For competitive products not of general applicability, available data on international customized mailing agreements (ICMs) for FY 2011 are presented in the ICRA

[24] The only exceptions were a few carryover international rates.

materials within USPS-FY11-NP2. For domestic competitive products not of general applicability, information is provided in USPS-FY11-NP27.

C. Section 3633 Standards

The competitive product pricing standards of section 3633 have been implemented by the Commission at 39 C.F.R. § 3015.7. This section discusses the available FY 2011 data with reference to those standards.

First, subsection 3633(a)(1) states that competitive products should not be cross-subsidized by market dominant products. The Commission's regulations define the most appropriate test for this standard as the incremental cost test for the aggregation of competitive products.[25] Simply stated, if the aggregate revenues from competitive products equal or exceed the aggregate incremental costs of competitive products, then competitive products overall are not being cross-subsidized by market dominant products.

As in the FY 2009 and FY 2010 ACRs, the Postal Service is presenting what can be termed a "hybrid" estimate of incremental costs, in which an estimate of the aggregate incremental costs of domestic competitive products (including group specific costs) is added to an estimate of the attributable costs of international competitive products. The "hybrid" characterization reflects the blending of an actual estimate of domestic incremental costs with an attributable cost proxy for international incremental costs. The need for the hybrid approach is caused by the structure of the ICRA, which precludes direct application of the incremental cost model to international products. As demonstrated in Proposal 22, Docket No. RM2010-4, the hybrid estimate is an

[25] *See* 39 C.F.R. § 3015.7(a).

improvement over the full proxy of attributable costs for both domestic and international competitive products, plus group specific costs, used before FY 2009.[26] The hybrid approach provides stronger protection against cross-subsidy than the previous full proxy approach.

The incremental cost for domestic competitive products, and the hybrid incremental cost for the group of all competitive products, are presented below:

INCREMENTAL COST CALCULATION FOR TOTAL COMPETITIVE PRODUCTS

	Attributable Cost (000s)	Group Specific (000s)	Incremental Cost (000s)	Hybrid Incremental Cost (000s)
Domestic Competitive	$ 5,567,563	$ 32,797	$ 5,694,176	$ 5,694,176
International Competitive	$ 1,112,441	$ -	N/A	$ 1,112,441
Total Competitive	$ 6,680,004	$ 32,797	N/A	$ 6,806,617

Source: USPS-FY11-NP10

The total competitive hybrid incremental cost is $6,806,617 thousand, which is the sum of the hybrid incremental costs for domestic competitive mail and the hybrid incremental costs for international competitive. In the past, the Commission used attributable cost plus group specific cost for the cross-subsidy test. That proxy would provide a cost floor of $6,712,801 thousand ($6,680,004 + $32,797). The hybrid provides a preferred cost floor because it includes at least some properly calculated incremental costs, and is a better approximation of the true incremental costs required for the test.[27]

[26] Proposal 22 was approved by the Commission in Order No. 399, Docket No. RM2010-4 (Jan. 27, 2010).

[27] As demonstrated in Proposal 22, the resulting hybrid will be greater than the group's overall attributable cost (while not overstating the incremental costs for competitive products). This means that the hybrid is a preferred cost floor for performing a cross subsidy test.

The hybrid incremental costs of $6.807 billion are well below total competitive products revenue of $8.997 billion (shown on page 3 of USPS-FY11-1). Therefore, based on these estimates, it is clear that competitive products in FY 2011 were not cross-subsidized by market dominant products, and thus were in compliance with subsection 3633(a)(1).

Second, subsection 3633(a)(2) requires that each competitive product cover its attributable costs. Comparing the revenue of each competitive product shown in the Nonpublic CRA (USPS-FY11-NP11) with its attributable costs indicates that all of the competitive products are covering their attributable costs, with the exception of: (1) International Money Transfer Service – Inbound; and (2) Inbound International Expedited Services. The Postal Service furnishes the following comments on each such product:

Product	Comment
International Money Transfer Service – Inbound	International Inbound Money Transfer Service represents the commissions and per item payments the Postal Service receives from foreign postal operators for the delivery of paper money orders to customers in the United States. These fees and commissions were negotiated, in most cases, prior to the establishment of the Postal Service under the PRA and in all cases prior to the amendments to that Act brought about by the PAEA. The reciprocal fees and commissions were negotiated based on the balance of expected costs and revenues, with the Postal Service almost always being the net exporter. Thus the lower the amount of the reciprocal fee or commission, the lower the cost to the Postal Service. The agreements have been deemed to be international law agreements by the Department of State and cannot be terminated or renegotiated without delegated authority. The Postal Service continues to pursue the authority to terminate and renegotiate these agreements, but until such time as it obtains the necessary authority, it must continue to honor the agreements. The net contribution of International Money

	Transfer Service, taking both inbound and outbound elements into account, provided a positive net contribution to the Postal Service in FY 2010.
Inbound International Expedited Services	All Inbound International Expedited Services (inbound EMS) are reported in aggregate. As per Docket No. CP2010-90, inbound EMS charges were raised in January 2011, and hence the price increase for CY 2011 would not be reflected in the first quarter of the postal 2011 fiscal year. Moreover, the Postal Service is again raising Inbound International Expedited Services 2 rates this coming January as per Docket No. CP2011-66. The statutory pricing criteria for competitive products was satisfied by the estimates presented in that docket.

Third, subsection 3633(a)(3) states that competitive products must collectively cover what the Commission determines to be an appropriate share of the Postal Service's institutional costs. In its regulations, the Commission has determined that an appropriate minimum share is 5.5 percent of total institutional costs.[28] Page 3 of USPS-FY11-1 shows total institutional costs of $29.554 billion. Applying the 5.5 percent to that figure yields a target contribution of $1.625 billion. To evaluate achievement relative to that target, we once again refer to page 3 of USPS-FY11-1, and subtract total competitive attributable costs of $6.680 billion from total competitive product revenue of $8.997 billion, leaving an aggregate competitive product contribution of $2.317 billion. The target is exceeded, and the requirement of subsection 3633(a)(3) has been met.

IV. MARKET TESTS

A. Market Dominant Market Tests

Three market dominant market tests of experimental products were offered under the provisions of section 3641 in FY 2011: Alternate Payment Method for Greeting

[28] *See* 39 C.F.R. § 3015.7(c).

Cards, Every Door Direct Mail (EDDM), and Mail Works Guarantee. Information for these market tests is provided below:

Market Test	Revenue	Cost	Volume
Alternate Payment Method for Greeting Cards	$ 1,420,358	$ 773,297	2,978,783
Every Door Direct Mail	$ 5,014,098	$ 2,330,496	35,310,548
Mail Works Guarantee	0	0	0
Total Market Dominant	$ 6,434,456	$ 3,103,793	

Given the dissimilarity of the three market dominant experimental products, the Postal Service has not calculated an aggregate volume. The Postal Service does not possess comprehensive cost information for the market tests. The cost listed above for Alternate Payment Method for Greeting Cards represents the information technology costs associated with the product, and the cost listed above for EDDM represents processing and delivery costs. The Postal Service has not yet received any volume for Mail Works Guarantee.

The Postal Service does not have a method for estimating the quality of service of its market dominant experimental products. Nonetheless, for Alternate Payment Method for Greeting Cards, the quality of service associated with First-Class Mail would apply, and for EDDM, the quality of service associated with Standard Mail would apply. The Postal Service does not believe that the offering of any of the three market dominant experimental products created an inappropriate competitive advantage for the Postal Service or any mailer.

B. Competitive Market Tests

Two competitive market tests of experimental products were offered under the provisions of section 3641 in FY 2011: Collaborative Logistics and Gift Cards.[29] Information for these two market tests is provided below:

Market Test	Revenue	Cost	Volume
Collaborative Logistics	$ 2,278,674	USPS-FY10-NP27	35,742
Gift Cards	$ 96,012	$ 20,489	18,034
Total Competitive	$ 2,374,686	USPS-FY10-NP27	

While the information listed above would ordinarily be filed in the nonpublic annex, the Postal Service has provided it here publicly because it already exists in public form in the Postal Service's data collection reports filed with the Commission. The cost for Collaborative Logistics has not been made public in the data collection reports; it is provided in USPS-FY11-NP27. However, the revenue from Collaborative Logistics exceeded the product's costs. Given the dissimilarity of the two competitive experimental products, the Postal Service has not calculated an aggregate volume.

The Postal Service does not have a method for estimating the quality of service of its competitive experimental products. The Postal Service does not believe that the offering of any of the two competitive experimental products created an inappropriate competitive advantage for the Postal Service or any mailer.

V. <u>NONPOSTAL SERVICES</u>

Commission Rule 3050.21(i) requires the ACR to include estimates of the costs, volumes, and revenues for nonpostal services. In the FY 2010 ACD, page 152, the

[29] Samples Co-Op Box, which was offered in FY 2010, was no longer in effect in FY 2011.

Commission linked further reporting on nonpostal services to approval of classification language in Docket No. MC2010-24. That docket was still pending at the end of FY 2011. In this ACR, the Postal Service has attempted to improve its reporting, but the information provided below is generally comparable to what has been provided previously. Provided below is information regarding the two market dominant nonpostal services in effect, MoverSource and Philatelic Sales.

Market Dominant

MoverSource (IMAGITAS)		
Revenue	$53,664,715	
Expense	$1,790,445	
Net Income (Loss)	$51,874,270	
Volume	NA	
Philatelic Sales		
Revenue	$171,954	*
Expense	$838,164	*
Net Income (Loss)	($666,210)	
Volume	173,144	

*Revenue and expense are for stamp fulfillment only

Comparable data for the ten competitive nonpostal services in effect is provided in USPS-FY11-NP27. Those nonpostal services are: Affiliates for Website, Affiliates – Other, FedEx Dropboxes, Officially Licensed Retail Products (OLRP), Licensing Programs Other than OLRP, Electronic Postmark, Non-Sale Lease Agreements, Passport Photo Service, Photocopying Service, and Training Facilities. The revenues for each of these products exceed the associated costs, except for Electronic Postmark.

Electronic Postmark did not receive any business in FY 2011, but there were some minor costs associated with maintaining the product.

VI. <u>NONPUBLIC ANNEX</u>

Section 3652(f)(1) contemplates the use of a nonpublic annex for documents or other materials that the Postal Service considers exempt from public disclosure, pursuant to 39 U.S.C. § 410(c) and 5 U.S.C. § 552(b). In particular, section 410(c)(2) exempts from mandatory disclosure "information of a commercial nature…which under good business practice would not be publicly disclosed." In previous years, the ACR had a nonpublic annex containing, generally speaking, the following: (1) the billing determinants for domestic and international competitive products, (2) the ICRA, and all supporting documentation underlying the ICRA, and (3) data for international customized agreements with customers. Starting in FY 2008, the nonpublic annex also included *nonpublic* versions of the CRA and Cost Segments and Components reports that provided disaggregated as well as aggregated information for competitive products, plus versions of the CRA "B" workpapers, the CRA model, the files relating to the costing data systems (IOCS, CCCS, RCCS, and TRACS), and special cost study workpapers or other similar background materials which contained sensitive disaggregated information on competitive products. Additionally, though, the FY 2008, FY 2009, and FY 2010 ACRs also included *public* versions of those materials, which provided detailed information on market dominant products, but in which information on competitive products (if any) had been aggregated.

For this year, in accordance with section 3652(f)(1) of title 39, a complete listing of what is within the FY 2011 nonpublic annex is provided in the attached list of documents. *See* Attachment One. In general, the FY 2011 nonpublic annex contains the same type of materials that were provided in the FY 2010 nonpublic annex. Moreover, regarding the split of materials between public and nonpublic documents and files, the FY 2011 materials continue important differences introduced in FY 2009. First, in the Public CRA, rather than aggregating all competitive product information into one row, that row has been disaggregated into five rows, each presenting information for a group of competitive products. The five groups are Total Express Mail, Total Priority Mail, Total Ground, Total International Competitive, and Competitive Services. The rows in the Nonpublic CRA which have been rolled up into each of those five rows in the Public CRA are listed in a table in the attached Application for Non-Public Treatment of the Nonpublic Annex. *See* Attachment Two, page 12. Second, as it did last year, the nonpublic annex this year includes information on individual domestic competitive product Negotiated Service Agreements (NSAs), provided in USPS-FY11-NP27. Third, because they were prepared on very short notice, FY 2008's public versions of certain supporting documentation (*e.g.*, CRA model, B workpapers, etc.) did not necessarily flow smoothly. Starting in FY 2009, great effort was devoted to preserving linkages in the public versions, and the situation in that regard thus improved substantially. Over the course of Docket Nos. ACR2009 and ACR2010, no issues arose regarding this matter, and the successful practices of those years have been continued this year. Once again, however, to preserve a unified set of source documents, the data reported in the ACR come from the non-public versions. Should any discrepancies arise between public and nonpublic versions because of issues such as rounding, the nonpublic versions would take precedence.[30]

Of course, another major difference between FY 2009 and FY 2008 with respect to the nonpublic annex was the promulgation of the Commission's final rules on treatment of confidential material. Docket No. RM2008-1, Order No. 225 (June 19, 2009). As a consequence of those rules, as it did the last two years, the Postal Service is once again providing the attached Application for Nonpublic Treatment of Materials regarding the nonpublic annex. Perhaps more importantly, however, eligible individuals who seek to examine what has been filed in the nonpublic annex may expect to receive a prompt response to a request to view such materials under standard protective conditions. See Commission Rule 3007.40.

While the new rules establish the process by which issues of confidentiality are addressed, they should not alter the importance of the statutorily-recognized need to protect sensitive commercial information. The continued confidentiality of these types of data, for example, remains essential to the Postal Service's ability to negotiate international customized mailing agreements (ICMs), other bilateral and multilateral agreements with foreign postal administrations, and vendor arrangements that support international services. For ICMs and foreign post arrangements, revenue, piece, and weight data have also historically been treated as commercially sensitive and confidential. This treatment reflects the Postal Service's assessment that public

[30] As it does every year, the Postal Service encourages any participant having difficulties working with any of its documentation, public or nonpublic, to contact Postal Service counsel to initiate informal dialogue to resolve any problems as quickly as possible. Given short timeframes, joint efforts at direct cooperation would seem to have the highest probability of promptly resolving technical difficulties, to the mutual benefit of all concerned.

disclosure of actual data concerning agreements, as well as retail services that compete with offerings by freight forwarders and other private international delivery companies, would interfere with the Postal Service's ability to compete for customers. This practice was consistently followed by the Postal Service in the numerous ICMs and other international agreements filed with the Commission during the course of this fiscal year.

Of course, while ICMs have been common in the past for international competitive products, the Postal Service has only rather recently under the PAEA begun to negotiate similar contract pricing arrangements with respect to domestic competitive products. Domestic customers for competitive products who under the PRA could influence the postal prices they paid only by participation in postal rate proceedings can now directly negotiate with the Postal Service for what they view as more favorable prices for their particular circumstances. Access to virtually any cost information on competitive products may give them an advantage in the negotiation process which, by definition, could act to the detriment of the Postal Service during that same negotiation process. These developments require reassessment to achieve an equilibrium that respects the Postal Service's enhanced competitive role, and the Commission's new responsibilities. Indeed, the language of the PAEA calls for such an equilibrium.[31]

Costing information for products as a whole, or for specific product features, tends to be highly confidential in the business world, and the Postal Service should be able to protect such information in accordance with industry standards. The ability of the Postal Service to negotiate favorable contracts could be severely compromised if costing information were to become available either to the customers with whom the

[31] *See, e.g.,* 39 U.S.C. § 3652(e)(1).

Postal Service is negotiating, or to competitors who might be seeking to negotiate contracts with the same customers. The Postal Service's competitors, for example, could use such information to target their efforts and undercut the Postal Service's prices. The Postal Service is aware of no competitor or private shipping company of comparable size and scope that releases cost information regarding specific products to the public.

Respectfully submitted,

UNITED STATES POSTAL SERVICE

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December 29, 2011

LIST OF MATERIALS PROVIDED BY THE UNITED STATES POSTAL SERVICE FOR PURPOSES OF THE FISCAL YEAR 2011 ANNUAL COMPLIANCE REPORT

Number	
USPS-FY11-1	FY 2011 Public Cost and Revenue Analysis (PCRA) Report
USPS-FY11-2	FY 2011 Public Cost Segments and Components Report
USPS-FY11-3	FY 2011 Discounts and Passthroughs of Workshare Items
USPS-FY11-4	FY 2011 Market Dominant Billing Determinants
USPS-FY11-5	Cost Segment and Components Reconciliation to Financial Statements and Account Reallocations (Reallocated Trial Balances)
USPS-FY11-6	General Classification of Accounts (Formerly Handbook F-8)
USPS-FY11-7	Cost Segment 3 Cost Pools & Other Related Information (Public Portion)
USPS-FY11-8	Equipment and Facility Related Costs
USPS-FY11-9	FY 2011 ACR Roadmap Document
USPS-FY11-10	FY 2011 Special Cost Studies Workpapers - Letter Cost Models (First-Class Mail and Standard Mail)
USPS-FY11-11	FY 2011 Special Cost Studies Workpapers - Flat Cost Models (First-Class Mail and Standard Mail) & Periodicals Cost Model
USPS-FY11-12	Standard Mail Hybrid/Parcel Cost Study

USPS-FY11-13	FY 2011 Special Cost Studies Workpapers - Drop Ship Cost Avoidances for Periodicals and Standard Mail
USPS-FY11-14	Mail Characteristics Study (Public Portion)
USPS-FY11-15	FY 2011 Special Cost Studies Workpapers – Bound Printed Matter Mail Processing Cost Model / Media Mail – Library Mail Mail Processing Cost Model
USPS-FY11-16	FY 2011 Special Cost Studies Workpapers - Bound Printed Matter Transportation Costs / Bulk Parcel Return Service Cost Model
USPS-FY11-17	2011 Comprehensive Statement of Postal Operations
USPS-FY11-18	FY 2011 ECR Mail Processing Unit Costs
USPS-FY11-19	FY 2011 Delivery Costs By Shape
USPS-FY11-20	FY 2011 Window Service Cost by Shape
USPS-FY11-21	FY 2011 QBRM and BRM Costs
USPS-FY11-22	FY 2011 Bound Printed Matter Mail Processing Costs
USPS-FY11-23	MODS Productivity Data
USPS-FY11-24	FY 2011 Non-Operation Specific Piggyback Factors (Public Portion)
USPS-FY11-25	FY 2011 Mail Processing Piggyback Factors (Operation Specific)
USPS-FY11-26	FY 2011 Mail Processing Costs by Shape (Public Portion)

USPS-FY11-27	FY 2011 Nonprofit Mail Cost Approximations
USPS-FY11-28	FY 2011 Special Cost Studies Workpapers – Special Services (Public Portion)
USPS-FY11-29	Annual Report on Service Performance for Market Dominant Products
USPS-FY11-30	FY 2011 Market Dominant NSA Materials
USPS-FY11-31	FY 2011 CRA Model (Model Files, Cost Matrices, and Reports) (Public Version)
USPS-FY11-32	FY 2011 CRA “B” Workpapers (Public Version)
USPS-FY11-33	Rule 3050.14 Alternative Format Report (Public Version)
USPS-FY11-34	City Carrier Cost System (CCCS) Statistical and Computer Documentation (Public Version)
USPS-FY11-35	Rural Carrier Cost System (RCCS) Statistical and Computer Documentation (Public Version)
USPS-FY11-36	Transportation Cost Systems (TRACS) Statistical and Computer Documentation (Public Version)
USPS-FY11-37	In-Office Cost System (IOCS) Statistical and Computer Documentation (Public Version)
USPS-FY11-38	USPS Market Dominant Product Customer Satisfaction Measurement Survey Instruments
USPS-FY11-39	FY 2011 Competitive Products Fund Reporting Materials
USPS-FY11-40	2011 Rural Mail Count

USPS-FY11-41	International Market Dominant Billing Determinants
USPS-FY11-42	FY 2011 Revenue, Pieces, and Weight Report (Public Version)

THE BELOW ITEMS WILL BE DESIGNATED AS PART OF THE NONPUBLIC ANNEX:

USPS-FY11-NP1	FY 2011 Domestic Competitive Product Billing Determinants
USPS-FY11-NP2	FY 2011 International Cost and Revenue Analysis (ICRA) Report
USPS-FY11-NP3	FY 2011 International Cost Segments and Components Report
USPS-FY11-NP4	FY 2011 ICRA Domestic Processing Model (Cost Matrices, Reports, Control File, & Changes)
USPS-FY11-NP5	FY 2011 ICRA Overview/Technical Description
USPS-FY11-NP6	FY 2011 International Cost Segment Spreadsheets
USPS-FY11-NP7	Cost Segment 3 International Subclass Costs by Cost Pools (Volume Variable Cost Pools)
USPS-FY11-NP8	FY 2011 International Competitive Products Billing Determinants
USPS-FY11-NP9	FY 2011 Miscellaneous International Data
USPS-FY11-NP10	FY 2011 Competitive Product Incremental and Group Specific Costs
USPS-FY11-NP11	FY 2011 Nonpublic Cost and Revenue Analysis (NPCRA) Report

USPS-FY11-NP12	FY 2011 Nonpublic Cost Segments and Components Report)
USPS-FY11-NP13	FY 2011 CRA Model (Model Files, Cost Matrices, and Reports)
USPS-FY11-NP14	FY 2011 CRA “B” Workpapers (Nonpublic Version)
USPS-FY11-NP15	FY 2011 Special Cost Studies Workpapers – Parcel Select / Parcel Return Service (PRS) Mail Processing Cost Model (Nonpublic Portion)
USPS-FY11-NP16	FY 2011 Special Cost Studies Workpapers - Parcel Select/ Parcel Return Service (PRS) Transportation Cost Model (Nonpublic Portion)
USPS-FY11-NP17	FY 2011 Special Cost Studies Workpapers Parcel Select / Parcel Return Service (PRS) Cube-Weight Relationship Estimation (Nonpublic Portion)
USPS-FY11-NP18	Cost Segment 3 Cost Pools & Other Related Information (Nonpublic Portion)
USPS-FY11-NP19	FY 2011 Non-Operation Specific Piggyback Factors (Nonpublic Portion)
USPS-FY11-NP20	FY 2011 Mail Processing Costs by Shape (Nonpublic Portion)
USPS-FY11-NP21	In-Office Cost System (IOCS) Statistical and Computer Documentation (Nonpublic Version)
USPS-FY11-NP22	City Carrier Cost System (CCCS) Statistical and Computer Documentation (Nonpublic Version)
USPS-FY11-NP23	Rural Carrier Cost System (RCCS) Statistical and Computer Documentation (Nonpublic Version)

USPS-FY11-NP24	Transportation Cost Systems (TRACS) Statistical and Computer Documentation (Nonpublic Version)
USPS-FY11-NP25	Mail Characteristics Study (Nonpublic Portion)
USPS-FY11-NP26	FY 2011 Special Cost Studies Workpapers – Special Services (Nonpublic Portion)
USPS-FY11-NP27	2011 Competitive NSA & Nonpostals Materials
USPS-FY11-NP28	Rule 3050.14 Alternative Format Report (Non-Public Version)
USPS-FY11-NP29	Cost Segment and Components Reconciliation to Financial Statements and Account Reallocations (Reallocated Trial Balances) (Nonpublic Version)
USPS-FY11-NP30	FY 2011 Revenue, Pieces, and Weight Report (Nonpublic Version)

APPLICATION OF THE UNITED STATES POSTAL SERVICE FOR NONPUBLIC TREATMENT OF MATERIALS

In accordance with 39 C.F.R. § 3007.21 and Order No. 225,[1] the United States Postal Service (Postal Service) hereby applies for nonpublic treatment of certain materials filed under seal with the Commission. The materials covered by this application consist of the entire Nonpublic Annex of the FY 2011 Annual Compliance Report (ACR). The Nonpublic Annex includes 30 separate folders, as shown on the List of Materials provided as Attachment One to the ACR. As is apparent from that List, the majority of these folders have a corresponding public folder. In many instances, a set of material has been divided into a portion that relates to Market Dominant products, and a portion that relates to Competitive products. In those instances, the public folder includes the portion of material relating to Market Dominant products, and the nonpublic folder includes the portion of materials relating to Competitive products. In many other instances, two versions of materials are prepared. The nonpublic versions present summary information, or contain the background material from which summary information has been developed, in which Competitive product data have been disaggregated to the product level. The corresponding public versions present summary information, or contain the background material from which summary information has been developed, in which Competitive product data have been aggregated above the product level. In still other instances, a nonpublic folder contains information about Competitive products, and there is no corresponding public folder, because there is no corresponding need for similar information relating to Market Dominant products. As an example, Commission Rule 3015.7(a) calls only for the

[1] PRC Order No. 225, Final Rules Establishing Appropriate Confidentiality Procedures, Docket No. RM2008-1 (June 19, 2009).

incremental costs of Competitive products, so there is a nonpublic folder on the incremental costs of Competitive products, but there is no need for a corresponding public folder on the incremental costs of Market Dominant products. In general, except for the five groups of Competitive products for which cost data are shown in the Public Cost and Revenue Analysis (CRA), all disaggregated cost information relating to Competitive products, and all background data used to develop disaggregated cost information on Competitive products, are filed under seal in the Nonpublic Annex.

(1) The rationale for claiming that the materials are nonpublic, including the specific statutory basis for the claim, and a statement justifying application of the provision(s);

The materials designated as nonpublic consist of commercial information concerning postal operations and finances that under good business practice would not be disclosed publicly. Based on its longstanding and deep familiarity with postal and communications business and markets generally, and its knowledge of many firms, including competitors, mailers, and suppliers, the Postal Service does not believe that any commercial enterprise would voluntarily publish information pertaining to the costs, volumes, revenues, and markets for its competitive products, as well as inbound market dominant products for which rates are negotiated with other postal operators. In the Postal Service's view, this information would be exempt from mandatory disclosure pursuant to 39 U.S.C. § 410(c)(2) and 5 U.S.C. § 552(b)(3) and (4).[2]

[2] In appropriate circumstances, the Commission may determine the appropriate level of confidentiality to be afforded to such information after weighing the nature and extent of the likely commercial injury to the Postal Service against the public interest in maintaining the financial transparency of a government establishment competing in commercial markets. 39 U.S.C. § 504(g)(3)(A). The Commission has indicated that "likely commercial injury" should be construed broadly to encompass other types of injury, such as harms to privacy, deliberative process, or law enforcement interests. Commission Order No. 194, Second Notice of Proposed Rulemaking to Establish a Procedure for According Appropriate Confidentiality, Docket No. RM2008-1 (Mar. 20, 2009), at 11.

(2) Identification, including name, phone number, and email address for any third-party who is known to have a proprietary interest in the materials, or if such an identification is sensitive, contact information for a Postal Service employee who shall provide notice to that third party;

The Postal Service believes that the only third parties that have a proprietary interest in the materials submitted in connection with the FY 2011 Annual Compliance Report are (1) entities, including foreign postal operators, holding competitive negotiated service agreements (NSAs) in FY 2011 for which data are reported on a contract-specific basis, (2) Federal Express Corporation (FedEx Express) with respect to data concerning Global Express Guaranteed (GXG), (3) the Canada Post Corporation (CPC), (4) Correos de México, and (5) other foreign postal operators who tendered postal items to the Postal Service, or to whom the Postal Service tendered items, in FY 2011 at rates not of general applicability. Except with respect to the fourth category as described below, the Postal Service gives notice that it has already informed each third party, in compliance with 39 C.F.R. § 3007.20(b), of the nature and scope of this filing and its ability to address its confidentiality concerns directly with the Commission.

Various materials contain data specific to customers holding competitive NSAs, such as Priority Mail and/or Express Mail contracts, Parcel Select contracts, Parcel Return Service contracts, Global Expedited Package Services contracts, Global Reseller Expedited Package Services contracts, Global Plus 1 and 2 Contracts, Global Direct Contracts, Inbound Direct Entry agreements, Inbound International Expedited Services 1, the Royal Mail Inbound Air Parcel Post Agreement, Direct Entry Parcels contracts, and International Business Reply Service competitive contracts. For certain of the NSA customers for which the Postal Service has already disclosed the counter-party's identity, the Postal Service identifies the following contacts:

- For the Inbound Direct Entry Contract with New Zealand Post Limited: Mr. Lindsay Welsh, Regional Business Director - Europe/North America, +64 4 496 4574, lindsay.welsh@nzpost.co.nz;
- For the Inbound Direct Entry Contract with China Post Group: Mr. Zhu Lei, Deputy Manager, International Operations, China Post EMS and Logistics Corporation (China Post Group), +86 10 67 077 331, zhulei@ems.com.cn;
- For the Inbound Direct Entry Contract with Hongkong Post: Jeremy Wan, Senior Manager, International Letters, +852 2921 6026, jeremy_wan@hkpo.gov.hk, and Penny Hung, Manager, International Letters, +852 2921 2115, penny_hung@hkpo.gov.hk;
- For the Inbound Direct Entry Contract with P&T Express Service Joint Stock Company: Ms. Dang Thi Bich Hoa, General Director, +84 43 757 5588, hoadb@ems.com.vn;
- For the Royal Mail Inbound Air Parcel Post Agreement: David Breeze, Parcelforce Worldwide (Royal Mail Group Limited), +44 784 149 9741, david.breeze@parcelforce.co.uk;
- For the China Post Group Inbound International Expedited Services 1 agreement and the China Post Inbound Market-Dominant Multi-Service Agreement, Mr. Zhu Lei, Deputy Manager, International Operations, China Post EMS and Logistics Corporation (China Post Group), +86 10 67 077 331, zhulei@ems.com.cn, and

- For the Hongkong Post Inbound Market-Dominant Multi-Service Agreement, Mr. Jeremy Wan, Senior Manager, International Letters, Hongkong Post, +852 2921 6026, jeremy_wan@hkpo.gov.hk.
- For the Strategic Bilateral Agreement Between United States Postal Service and Koninklijke TNT Post BV and TNT Post Pakketservice Benelux BV, Mr. Ben Pilgram, Consultant, International Distribution Agreements, PostNL, +31 (0)6 83 64 57 90, ben.pilgram@postnl.nl

Because the Postal Service maintains that the remaining competitive NSA customers' identities are commercially sensitive and should not be publicly disclosed, the Postal Service employees responsible for providing notice to these third parties are:

- Elizabeth A. Reed, Attorney, Pricing and Product Support, whose telephone number is (202) 268-3179 and whose email address is elizabeth.a.reed@usps.gov; and
- Mr. James J. Crawford, Business Development Specialist, Global Business, whose telephone number is 202-268-7714 and whose email address is james.j.crawford@usps.gov.

The International Cost and Revenue Analysis (ICRA) report and supporting documentation contain data specific to GXG service, which the Postal Service offers in partnership with FedEx Express.[3] The Postal Service identifies James H. Ferguson, Corporate Vice President, Customer and Business Transactions, FedEx Corp. & General Counsel, FedEx Corporate Services, Inc., as the appropriate contact on behalf

[3] Although FedEx Express might have a proprietary interest in data reflecting charges between the Postal Service and FedEx Express and possibly data showing volume or weights for GXG, the Postal Service maintains that the Postal Service is the only party with a proprietary interest in revenue data reflecting GXG transactions between the Postal Service and its customers.

of FedEx Express. Mr. Ferguson's telephone number is (901) 434-8600, and his email address is jferguson1@fedex.com.

The International Cost and Revenue Analysis (ICRA) report contains data for various products that is specific to CPC. These data pertain to various categories of inbound mail that CPC tenders in a "customer" capacity and to categories of outbound mail that CPC delivers for the Postal Service in a "supplier" role, in both cases pursuant to CPC's negotiated bilateral agreement with the Postal Service. The Postal Service identifies Terry Dunn, General Manager, International Relations, Canada Post Corporation, as the appropriate contact on behalf of Canada Post. Mr. Dunn's telephone number is (613) 734-8894, and his email address is terry.dunn@canadapost.ca. Canada Post has requested that any communications regarding confidential treatment of these data be sent with a courtesy copy to Ewa Kowalski, Manager, International Mail Settlement, Canada Post Corporation. Ms. Kowalski's telephone number is (613) 734-6201, and her email address is ewa.kowalski@canadapost.ca.[4]

The ICRA report also contains inbound and outbound international mail data specific to Correos de México, the public postal operator for Mexico, and in which Correos de México might be deemed to have a proprietary interest. Due to language and cultural differences as well as the sensitive nature of the Postal Service's

[4] In the event of a request for early termination of non-public treatment under 39 C.F.R. § 3007.31, a preliminary determination of non-public status under 39 C.F.R. § 3007.32, or a request for access to non-public materials under 39 C.F.R. § 3007.40, the Postal Service notes, on Canada Post's behalf, that differences in the official observation of national holidays might adversely and unduly affect Canada Post's ability to avail itself of the times allowed for response under the Commission's rules. In such cases, Canada Post has requested that the Postal Service convey its preemptive request that the Commission account for such holidays when accepting submissions on matters that affect Canada Post's interests. A listing of Canada's official holidays can be found at http://www.pch.gc.ca/pgm/ceem-cced/jfa-ha/index-eng.cfm.

relationship with Correos de México, the Postal Service proposes that a designated Postal Service employee serve as the point of contact for any notices to Correos de México.[5] The Postal Service identifies as an appropriate contact person Guadalupe Contreras, Business Systems Manager, International Postal Affairs. Ms. Contreras's phone number is (202) 268-4598, and her email address is guadalupe.n.contreras@usps.gov.

The ICRA report contains rate information and other information that might be deemed proprietary to postal operators who are partners in the E Parcels Group arrangement. For the same reasons as for Correos de México, the Postal Service proposes that a designated Postal Service employee serve as the point of contact for any notices to the relevant postal operators. The Postal Service identifies as an appropriate contact person Franca Davis, Executive Director, International Strategy and Business Development Support. Ms. Davis's phone number is (202) 268-5459, and her email address is franca.s.davis@usps.gov.

Finally, the ICRA report contains rate information and other information that might be deemed proprietary to postal operators whose governments are members of the UPU. For the same reasons as for Correos de México, the Postal Service proposes that a designated Postal Service employee serve as the point of contact for any notices to the relevant postal operators. The Postal Service identifies as an appropriate contact person Flori McClung, Manager, UPU Relations. Ms. McClung's phone number is (202)

[5] The Postal Service acknowledges that 39 C.F.R. § 3007.21(c)(2) appears to contemplate only situations where a third party's identification is "sensitive" as permitting the designation of a Postal Service employee who shall act as an intermediary for notice purposes. To the extent that the Postal Service's proposal might be construed as beyond the scope of this exception, the Postal Service respectfully requests a waiver that would allow it to designate a Postal Service employee as the contact person under these circumstances, in light of the practical considerations outlined herein.

268-2603, and her email address is flori.mcclung@usps.gov. In view of the practical difficulties, the Postal Service has not undertaken to inform all affected postal operators about the nature and scope of this filing and about the ability to address any confidentiality concerns directly with the Commission as provided in 39 C.F.R. § 3007.20(b). To the extent that the Postal Service's filing in the absence of actual notice might be construed as beyond the scope of the Commission's rules, the Postal Service respectfully requests a waiver that would allow it to forgo providing a notice to each postal operator. It is impractical to communicate with dozens of operators in multiple languages about this matter.

(3) A description of the materials claimed to be nonpublic in a manner that, without revealing the materials at issue, would allow a person to thoroughly evaluate the basis for the claim that they are nonpublic;

The materials in the Nonpublic Annex fall into several categories. The first category is the Nonpublic CRA, and all of the background materials feeding into the Nonpublic CRA. These materials, in general, show cost information at the product level, including disaggregated information for Competitive products. These materials are found in folders USPS-FY11-NP11, USPS-FY11-NP12, USPS-FY11-NP13, USPS-FY11-NP14, USPS-FY11-NP18, USPS-FY11-NP19, USPS-FY11-NP20, USPS-FY11-NP21, USPS-FY11-NP22, USPS-FY11-NP23, USPS-FY11-NP24, USPS-FY11-NP25, USPS-FY11-NP27, and USPS-FY11-NP28. Descriptions of the contents of these folders can be found in the roadmap document, filed as USPS-FY11-9. The roadmap indicates the corresponding public folder which contains information similar to that in each nonpublic folder, except that, in the public folder, the cost information for Competitive products is generally aggregated into one Competitive products row.

Therefore, examination of the corresponding public folder should allow a person to understand the nature of the contents of the nonpublic folder, and evaluate accordingly.

A second category consists of Special Cost Studies materials that provide cost information below the product level for Competitive products. These materials are found in folders USPS-FY11-NP15, USPS-FY11-NP16, USPS-FY11-NP17, and USPS-FY11-NP26. Again, descriptions of the contents of these folders can be found in the roadmap document, filed as USPS-FY11-9. The roadmap indicates the corresponding public folder which contains information similar to that in the nonpublic folder, except that, in the public folder, the cost information below the product level relates to Market Dominant, rather than Competitive products. Therefore, examination of the corresponding public folder should allow a person to understand the nature of the contents of the nonpublic folder, and evaluate accordingly.

A third category consists of the International CRA (ICRA) and the supporting documentation. These materials are found in folders USPS-FY11-NP2 through USPS-FY11-NP7 and USPS-FY11-NP9. Collectively, they present the inputs and the analyses used to attribute and distribute costs to International products. In general, the ICRA follows the same basic methodologies used in the CRA – dividing accounting data into cost segments and components, distributing the attributable costs within segments to products, and summing the total attributable costs of a product across segments. Descriptions of the contents of the individual ICRA-related folders can be found in the roadmap document, USPS-FY11-9. There are no corresponding public folders.

A fourth category is the Competitive product billing determinants. These are found in USPS-FY11-NP1 for domestic Competitive products, and USPS-FY11-NP8 for

International products. They are comparable in format to the Market Dominant billing determinants presented in USPS-FY11-4, but include the corresponding information for Competitive products. Again, examination of the corresponding public folder should allow a person to understand the nature of the contents of the nonpublic folder, and evaluate them accordingly.

Another folder in the Nonpublic Annex is USPS-FY11-NP10, which presents the application of the incremental cost methodology set forth in the Petition for Proposal Twenty-two (filed on Oct. 23, 2009, and considered as part of Docket No. RM2010-4) to Competitive products. The outputs of that application are shown in the text of the FY 2011 ACR itself, and USPS-FY11-NP10 merely provides the background materials supporting those outputs. The incremental cost model used in USPS-FY11-NP10 is comparable to the model employed in USPS-T-18 in Docket No. R2006-1, and the group specific costs are based on the same type of analysis considered by the Commission as Proposal One in Docket No. RM2008-2, and applied (to Market Dominant products) in USPS-FY08-33. The contents of USPS-FY11-NP10 are described in the roadmap document, USPS-FY11-9.

In general, the premise of this application is that, for Competitive products and certain market dominant international products, disaggregated cost data (and detailed volume and revenue data, such as that provided in billing determinants) constitute commercially-sensitive information and should not be publicly disclosed. The Postal Service is therefore placing all such information in the Nonpublic Annex, and filing it under seal. One exception to this approach appears in the Public CRA. The Public CRA (USPS-FY11-1) presents some disaggregated data for Competitive products, but those data are not disaggregated down to the product level, as they are in the Nonpublic CRA (USPS-FY11-NP11). Instead, in the Public CRA, the Postal Service is breaking out data for Competitive products into five Competitive product groups. Those groups are Total Express, Total Priority, Total Ground, Total International Competitive, and Total Competitive Services. (The product rows in the Nonpublic CRA that are rolled up into each of the five Competitive product group rows in the Public CRA are shown in the table below.) At this level of disaggregation, the Postal Service has been unable to identify any of its major competitors that are publicly disclosing a potentially greater amount of disaggregated competitive cost data. The Postal Service maintains that the further disaggregation shown in the Nonpublic CRA should thus appropriately remain confidential. The Postal Service believes that the approach jointly embodied in its Public CRA and Nonpublic CRA prudently maximizes the amount of information available to the public, keeping such information as detailed as possible without prompting the competitive concerns outlined in the following section below.

Category in Public Version CRA	**Categories Rolled in from Nonpublic Version CRA**
Total Express Mail	Domestic Express Mail Domestic Express Mail NSAs
Total Priority Mail	Domestic Priority Mail Domestic Priority Mail NSAs Priority Mail Fees
Total Ground	Parcel Select Mail Parcel Select NSAs Parcel Return Service Mail Parcel Return Service NSAs
Total Competitive International	Outbound International Expedited Services Inbound International Expedited Services Outbound Priority Mail International Inbound Air Parcel Post International Priority Mail (IPA)

	International Surface Airlift (ISAL) International Direct Sacks M-Bags Inbound Surf. Parcel Post (at Non-UPU Rates) Outbound Intl Negotiated Serv. Agreement Mail Inbound Intl Negotiated Serv. Agreement Mail International Money Transfer Service International Ancillary Services
Total Domestic Competitive Services	Premium Forwarding Service Address Enhancement Services Greeting Cards Shipping and Mailing Supplies Post Office Box Service

(4) Particular identification of the nature and extent of commercial harm alleged and the likelihood of such harm;

If the information that the Postal Service determined to be protected from disclosure due to its commercially sensitive nature were to be disclosed publicly, the Postal Service considers it quite likely that it would suffer commercial harm. This information is commercially sensitive, and the Postal Service does not believe that it would be disclosed under good business practices. In this regard, the Postal Service is not aware of any business with which it competes (or in any other commercial enterprise), either within industries engaged in the carriage and delivery of materials and hard copy messages, or those engaged in communications generally, that would disclose publicly information and data of comparable nature and detail.

The protected materials consist of comprehensive analytical tools and reports employed by the Postal Service for several purposes in its operations and finances. Most prominently, in the context of the ACR, they enable the Postal Service to address the issues mandated in 39 U.S.C. § 3652(a) having to do with the costs, revenues, rates, and quality of service of competitive postal products. Furthermore, many of the materials outlined in section (3) above consist of sub-reports, workpapers, and other documentation used to create the basic reports in the CRA and ICRA. These materials share the protected status and confidential nature of the basic reports, since they provide the building blocks that permit compilation of the data and statistics and would permit competitors to gain the same types of knowledge, understanding, and insights at finer levels of detail. The Postal Service believes that this information would lead to competitive harm, if publicly disclosed.

As explained below, the data and information considered to be non-publc can be classified in several general groupings: product cost information; general product volume and revenue information; product billing determinants; and information pertaining to service and pricing agreements with particular mailers or suppliers (NSAs). The following describes generally the expected harms from each of these classes of information. The explanations also include a separate discussion of international mail products, and their relatively distinct characteristics that arise from the structure of international business, including the involvement of foreign postal operators and international organizations.

Cost Information

Information relating to the costs of producing products is generally considered to be among the most sensitive commercial information. The CRA and ICRA present data and statistics for products that would provide competitors with valuable information, enabling them to better understand the Postal Service's cost structures, operational capabilities, and pricing and marketing strategies. This confidential information includes per-piece costs in several analytical categories (attributable costs, volume variable costs, and product-specific costs), as well as cost contribution and cost coverage (margin) by product. Such information would be extremely valuable to competitors in assessing the strengths and weaknesses of various postal products. Armed with detailed product cost information, competitors would be able to better identify and understand areas where they could adapt their own operations to be more competitive with postal products and better assess how to price and market their own products in such a way as to target the Postal Service's weaknesses and compensate for its strengths in producing and marketing various products. Furthermore, information contained in the various sub-reports, workpapers, and other documentation that feed the reports would provide an even more refined knowledge of the Postal Service's costs, cost structures, and capabilities. In this regard, the structure of the Postal Service's analytical tools and reports is well known among the postal community from years of exposure in general rate cases under the former regulatory regime. Postal costs are recorded in elaborate systems of general ledger accounts. These are grouped into various functional and other categories (cost segments and components) for further analysis and ultimate allocation and distribution to individual products. The level of detail contained in the sub-reports and workpapers is highly refined and would enable competitors, and existing and potential customers with whom the Postal Service might negotiate particular contract rates, to gain competitive or negotiating advantages that could lead to suppressing potential financial gains from the sale of postal products or the diversion of business away from the Postal Service to competitors. Either of these results would constitute serious commercial harm.

<u>Volume and Revenue Information</u>

Competitors could use the product-specific revenue, pieces, and weight information to analyze the Postal Service's possible market strengths and weaknesses and to focus sales and marketing efforts on those areas, to the detriment of the Postal Service. Disclosure of this information would also undermine the Postal Service's position in negotiating favorable terms with potential customers, who would be able to ascertain critical information about relevant product trends (*e.g.*, average revenue per piece, average weight per piece). Finally, as explained in greater detail below, disclosure would expose certain foreign postal operators and other customers to the same competitive harms, to the extent that a category is associated with a single customer or a small group of customers. The Postal Service considers these to be highly probable outcomes that would result from public disclosure of the material filed nonpublicly.

<u>Billing Determinants</u>

Billing determinants present a special category of volume and revenue information that would enable highly refined understanding of individual products aligned specifically to their specific price structures. In this regard, billing determinants present a picture of each product's experience, analyzed according to the different mail characteristics that comprise the elements of the product's price structure. Detailed billing determinants, especially combined with specific product cost information, would enable competitors to better analyze the strengths and weaknesses of individual products, including specific elements of the markets for them, such as advantages in certain weight categories and distance zones. This information would provide insights into how competitors might adapt their operations and product offerings, alter their pricing, and target their marketing to take business away from the Postal Service.

Armed with this type of information, competitors would likely focus their marketing and price cutting efforts on the Postal Service's most profitable products. This would lead to erosion of contribution for these products through lost sales and/or the need to lower prices to remain competitive. Postal product cost and contribution information would provide suppliers of postal transportation and other services with information they could use to seek higher rates for services they provide. This would lead to higher postal costs and loss of contribution. Although the extent of the commercial harm is difficult to quantify, even small changes in market share, prices, or costs could lead to millions of dollars in lost revenue, higher costs, and lower margins. It is highly likely that if this information were made public, the Postal Service's competitors and suppliers would take advantage of it almost immediately.

Negotiated Service Agreements

The utility of the sensitive information in billing determinants and other materials would be particularly enhanced with regard to NSA product information relating to particular customers. First, revealing any customer identifying information would enable competitors to focus marketing efforts on current postal customers which have been cultivated through the Postal Service's efforts and resources. The Postal Service considers it highly probable that, if this information were made public, the Postal Service's competitors would take immediate advantage of it. Many NSAs include a provision allowing the mailer to terminate the contract without cause by providing at least 30 days' notice. Therefore, there is a substantial likelihood of losing the customers to a competitor that targets them with lower pricing.

Other NSA-related information consists of mailing profiles. This information, if disclosed from any source within the CRA or ICRA, would offer competitors invaluable insight into the types of customers to whom the Postal Service is offering each type of competitive NSA. Even without identifying individual mailers, competitors would be able to direct their sales and marketing efforts at the customer segment that the Postal Service has had the most success at attracting. This would undermine both existing customer relationships and the potential for other new NSA customers.

A similar rationale applies to information showing product revenue, volume according to weight, pricing, and insured value levels, as well as adjustment factor calculations based on product revenues. This information is commercially sensitive, and the Postal Service does not believe that it would be disclosed under good business practices. Competitors could use the information to analyze the Postal Service's possible market strengths and weaknesses and to focus sales and marketing efforts on those areas, to the detriment of the Postal Service. The Postal Service considers these to be highly probable outcomes that would result from public disclosure of the material filed nonpublicly.

Commercially sensitive information related to NSAs is included in the agreements and their annexes, and in related financial work papers. Typically, these materials are filed under seal or redacted when the agreements are established as products. Since the Commission's rules governing confidentiality have taken effect, the Postal Service has filed applications for nonpublic status with each agreement. The reasoning expressed in those applications supports and is consistent with the discussion here.

Information derived from these documents is included in some of the materials filed in the Nonpublic Annex here. This information may include prices, product cost, contribution, or cost coverage. It also may concern customer mailing profiles, product volume, weight and revenue distribution, and product insured-value distribution. Competitors for the services covered by these agreements consist of domestic and international transportation and delivery firms and even foreign postal operators, which could use the information to their advantage in negotiating the terms of their own agreements with the Postal Service. Competitors could also use the information to assess offers made by the Postal Service to customers for any possible comparative vulnerabilities and to focus sales and marketing efforts on those areas, to the detriment of the Postal Service. Customers could use the information to their advantage in negotiating the terms of their own agreements with the Postal Service. The Postal Service considers these to be highly probable outcomes that would result from public disclosure of the redacted material.

Potential customers, including foreign postal operators, could deduce from the rates provided in individual pricing agreements, in work papers, or in a Governors' Decision, whether additional margin for net profit exists. From this information, each customer or foreign postal operator could attempt to negotiate ever-decreasing prices or incentives, such that the Postal Service's ability to negotiate competitive yet financially sound rates would be compromised.

Information derived from financial work papers supporting NSAs can include costs, assumptions used in pricing formulas and decisions, formulas and negotiated prices, mailer profile information, projections of variables, and cost coverage and contingency rates that have been included to account for market fluctuations and exchange risks. All of this information is highly confidential in the business world. If this information were made public, the Postal Service's competitors would have the advantage of being able to assess the Postal Service's costs and pricing and determine the absolute floor for Postal Service pricing, in light of statutory, regulatory, or policy constraints. Competitors would be able to take advantage of the information to offer lower pricing to postal customers, while subsidizing any losses with profits from other customers. Such competitors could include foreign posts, which in some instances are not required to use the Postal Service for delivery of parcels destined to the United States. Additionally, foreign postal operators or other potential customers could use costing information to their advantage in negotiating the terms of their own agreements with the Postal Service. Eventually, this could freeze the Postal Service out of the relevant markets.

International Product Information

The Postal Service believes that the same vulnerabilities and harms discussed above that would result from the disclosure of the cost, volume, and billing determinant information would also generally apply to international product information designated as nonpublic. In particular, the harms resulting from disclosure of competitive information in the CRA would also result from disclosure of similar information, workpapers, and supporting documentation related to the ICRA. International mail products and business, however, exhibit operational and pricing distinctions not always shared by the domestic counterparts. In particular, international products may be either inbound or outbound and, in some instances, are affected by bilateral and multilateral agreements among foreign postal operators. In some cases, particular lines within the ICRA reflect agreements with a single foreign postal operator. The public disclosure of this information would likely lead to limitations on the negotiating positions of both the Postal Service and the other foreign postal operator in similar agreements they might wish to negotiate with other foreign postal operators. The same is true where the partner is a private entity rather than a foreign postal operator: for example, disclosure of statistical, billing, and cost information about GXG could limit the ability of FedEx Express, a supplier to the Postal Service, to negotiate effectively and could allow competitors to analyze the traffic for competitive advantage against FedEx Express. Further, the outbound letter monopoly has been largely suspended by virtue of 39 C.F.R. § 320.8, thereby contributing to the intensity of competition in this market. The more disaggregated nature of the product information in the international context and the relatively smaller numbers associated with them makes the international data particularly vulnerable to analysis and use by competitors.

(5) At least one specific hypothetical, illustrative example of each alleged harm;

The following restates the harms discussed above and presents at least one hypothetical situation illustrating the consequences of disclosure.

Harm: Competitors, mailers, and suppliers could use cost, revenue, and volume summary data and statistics in the CRA and the ICRA, disaggregated by individual product and by NSA category, to gain knowledge and insights about the relative strengths and weaknesses of the Postal Service's competitive product lines. That refined understanding would, in turn, give competitors advantages in seeking to divert business from the Postal Service and to gain new

business for which the Postal Service might compete. Mailers and suppliers would be able to negotiate favorable deals with the Postal Service more effectively. As a result, the Postal Service would experience losses of existing and new business, or erosion of contributions and margins.

Hypothetical: The CRA and ICRA provide data by product that indicate total revenues, attributable costs, volume variable costs, product specific costs, and per-piece attributable costs, contribution, and cost coverage (margin). These data are broken out by individual product and separated between products purchased through public schedules and those purchased through contract rates (NSAs). Hypothetically, this information is made public. Competitors use it to gain a refined understanding of the relative strengths and weaknesses of the Postal Service's product lines (domestic and international), the individual strengths and weaknesses of particular products, and the degree to which products are sold through public schedules, compared to contract pricing arrangements. Financial analysts for the competitors relay their assessments to colleagues in the competitors' marketing and investment divisions. This information provides a better foundation to enable competing firms to make decisions regarding investments and product design in their own product lines. Based on such assessments, for example, firms that have individual products for domestic express service (overnight), international express service, or package service comparable to Priority Mail determine that they have potential for competitive gain against the Postal Service in these areas and, accordingly, decide to allocate investments in improved operations, supplier arrangements, and technologies to improve their competitive positions. To the extent that these decisions actually make the firms more competitive, the Postal Service loses existing or new business.

Hypothetical: Cost, contribution, and/or cost coverage information is released to the public and becomes available to a competitor. The competitor, which could be a foreign postal operator operating in the United States, assesses the profitability of certain services based on the data released. The competitor then targets its advertising and sales efforts at actual or potential customers in market segments where the Postal Service has substantial contribution, thereby hindering the Postal Service's ability to keep these customers' business.

Hypothetical: Cost, contribution, and/or cost coverage information is released to the public and becomes available to a supplier of materials, transportation, or other services. Suppliers are made aware of expected contribution margins by product and are better able to assess the relative strengths and weaknesses of the Postal Service's product lines. With this information, suppliers, including foreign postal operators in the case of international products, decide to increase the rates they charge the Postal Service to provide transportation and/or other services or become more resistant to negotiating favorable prices for their goods and services.

Hypothetical: Cost information is disclosed to the public. Mailers who seek to negotiate individual contract rates with the Postal Service gain a better understanding of the average or unit costs of particular products, as well as the relative and absolute strengths and weaknesses of particular product lines. This information enables the mailers to negotiate contract rates with the Postal Service more effectively than in the absence of such information. Similar disclosures result in advantages for foreign postal operators or other competitive entities in international mail.

Harm: The various companion reports, sub-reports, workpapers, special cost and other studies, and documentation contained in the Nonpublic Annex would

provide detailed and refined knowledge and understanding of the individual costs, cost structures, contributions, and cost coverages (margins) of individual postal products and contract pricing agreements. These materials, which produce and support the summary data and statistics contained in the CRA and ICRA, would provide highly detailed information regarding operational procedures used to produce the products, the costs and relative efficiencies of operations and sub-operations, and the amount and character of overhead, including the relative proportions of volume variable and overhead costs. Companion reports and sub-reports provide detailed functional analyses of Postal Service costs within a framework that is well-understood, or easily learned, from information in the Public Annex, or from familiarity with or research into past postal rate cases. Public disclosure would therefore be tantamount to publishing virtually every detail regarding the relative costs and efficiencies of providing postal competitive products. This information would provide blueprints for competitors, suppliers, and mailers who might seek to negotiate favorable contract rates. The information would better enable them to make favorable operational, investment, pricing, and marketing decisions in relationships with the Postal Service. The results would be loss of existing or future business for the Postal Service, or the erosion of total revenues, contributions, margins, and overall financial stability.

Hypothetical: The Cost Segments and Components reports of the CRA and ICRA are disclosed to the public. These reports group costs recorded in postal accounts according to various functional categories. The costs are distributed by postal product. The hypothetical disclosure provides competitors with a detailed understanding of the cost structures of each competitive postal product, the relative strengths and weaknesses of each product from cost perspectives, and the flexibilities available to the Postal Service within the legal framework applicable to postal prices. The refined understanding resulting from disclosure enables competitors to make decisions that would compensate for Postal Service strengths and capitalize on its weaknesses. These decisions might involve design of competing firms' own products, alternative price structures, operational procedures, and marketing strategies. They could also involve formulation of negotiating approaches and strategies by existing and potential suppliers of goods and services used in producing postal products, and the formulation of more informed negotiating positions by mailers seeking to enter into favorable contract rate arrangements with the Postal Service. Such competitive advantages lead to diversion of business away from the Postal Service or reduction of potential contribution from individual contracts.

Hypothetical: Cost distribution models, cost estimation models, and several sub-reports feeding into the CRA and ICRA are disclosed to the public. These materials provide highly refined information that would improve understanding of product cost structures and the behavior of postal costs. Certain cost reports, such as those outlining in detail the application of specific cost pools by mail processing operation in estimating product costs, provide detailed knowledge of operational procedures employed by the Postal Service in offering products and services. This information enhances competitors' abilities to make informed decisions about investment in capital and technologies used to produce their own competing products. For example, knowledge of inflexibilities in processing Priority Mail, or in transportation used to convey Parcel Return Service, leads competitors to explore more efficient processing of competing products or to negotiate more competitive transportation contracts used for competing products. Over time, annual disclosures of such information enable competitors (or suppliers and mailers) to identify and understand trends in cost behavior that better inform their decision-making. Such developments lead to an erosion of the Postal Service's competitive position and a loss of business or contribution.

Hypothetical: Information in certain reports and documentation of special cost and other studies (*e.g.*, Parcel Return Service cost models) is disclosed publicly. Such information provides a better understanding of the Postal Service's customer base for particular products. For instance, data from mail characteristics studies enables competitors to formulate a profile of the Postal Service's customer base for certain products. This information better enables competitors to devise marketing and sales strategies that target the most vulnerable markets for particular postal products. More effective marketing by competitors leads to reduced sales by the Postal Service and an erosion of contributions and margins.

Hypothetical: Cost models and sub-reports feeding the CRA and ICRA reports are disclosed to the public. Detailed knowledge of the Postal Service's cost estimation, cost distribution, and special study models and procedures provides competitors, as well as mailers who seek favorable contract rates, with tools that enhance their abilities to analyze postal costs and operations. Large, sophisticated firms who have competed with the Postal Service for long periods of time have been exposed to them before and likely have developed their own sophisticated analytical tools and therefore might not benefit as much from these models; however, the hypothetical availability of this information decreases barriers to entry in certain competitive markets and creates new competitors that erode the Postal Service's customer base.

Harm: Competitors could use disaggregated product volume, weight, and revenue distribution information to assess vulnerabilities and focus sales and marketing efforts to the Postal Service's detriment.

Hypothetical: Disaggregated revenue, volume, and weights contained in the Nonpublic Annex are disclosed to the public. Another delivery service's employee monitors the filing of this information and passes it along to the firm's sales and marketing functions. The competitor assesses the profitability of certain services on a per-piece or per-pound basis or the Postal Service's relative concentration in certain service offerings. The competitor then targets its advertising and sales efforts at actual or potential customers in market segments where the Postal Service appears to have made headway, hindering the Postal Service's ability to reach out effectively to these customers.

This example applies even more strongly for information split between NSA mail and other mail in the same category, because the competitor can assess the profitability and market strengths of the Postal Service's offerings to a small subset of NSA customers, thereby gaining somewhat more particularized insight into the characteristics of customers that the Postal Service specifically targets with its own contractual sales efforts.

A more pointed variant on this hypothetical pertains to Inbound Surface Parcel Post (at Non-UPU Rates). Because this category is associated with a single foreign postal operator (Canada Post Corporation or CPC), a competing delivery service provider with access to this information can use it to determine the average per-item and per-pound price offered by the Postal Service to CPC, as well as the average weight of Surface Parcel Post items from Canada. The competitor can use that information as a baseline to negotiate with freight companies to develop lower-cost alternatives and entice CPC's volume away from the Postal Service's domestic delivery network.

Harm: Customers, including foreign postal operators, and suppliers could use disaggregated product volume, weight, and revenue distribution information to undermine the Postal Service's leverage in negotiations.

Hypothetical: Disaggregated revenue, volume, and weight information in the Nonpublic Annex would be released to the public. A foreign postal operator's employee monitors the filing of this information and passes the information along to its international postal relations functions. The foreign postal operator assesses the Postal Service's average per-item or per-pound revenue for categories about which it is negotiating with the Postal Service, with particular focus on categories known to be included in NSAs with other foreign postal operators (*e.g.*, Inbound International Letter-Post NSA Mail, Inbound International Priority Mail NSAs, Inbound Surface Parcel Post (at Non-UPU Rates), Inbound Air Parcel Post, and Inbound EMS). Accurately or not, the foreign postal operator uses the average revenue information as a justification for pricing demands in negotiations, refusing to accept a higher price without steeper concessions than the Postal Service might otherwise have been able to foreclose. The Postal Service's ability to negotiate the best value from the bargain suffers as a result. This hypothetical applies with equal force for customers other than foreign postal operators, for NSA mail and non-NSA mail that can be made subject to an NSA (*e.g.*, International Priority Airmail, which can be included in Global Plus 1 NSAs), and for partnerships with suppliers such as FedEx Express with respect to GXG.

Harm: Public disclosure of information in the report would be used by competitors of the NSA customers to their detriment.

Hypothetical: A competitor of a Postal Service NSA customer obtains unredacted versions of the billing determinants for domestic and international products, including NSAs and ICMs. It analyzes the work papers to assess the customer's underlying costs and uses that information to identify lower cost alternatives to compete against the Postal Service customer. Likewise, suppliers of goods and services to the NSA customer can use the detailed information to their advantage in negotiations with the NSA customer.

Harm: Public disclosure of information contained in the Nonpublic Annex associated with international delivery services provided in partnership with specific third parties would be used by those parties' competitors to their detriment.

Hypothetical: A competitor of Canada Post Corporation, such as a competing international delivery service, obtains information contained in the Nonpublic Annex. The competitor analyzes the information to assess the average per-piece and per-pound revenue for Inbound International Letter-Post NSA Mail, Inbound Xpresspost, and/or Inbound Surface Parcels (at Non-UPU Rates), which correspond to Canada Post's average per-piece and per-pound cost for U.S. delivery of its pertinent products. The competitor uses that information to assess the market potential and, as a baseline, to negotiate with U.S. customs brokers and freight companies to develop lower-cost alternatives and undermine Canada Post's market offerings. The same scenario could apply with respect to comparable information, such as settlement charges due or payable, for other foreign postal operators or for FedEx Express concerning GXG.

Harm: Competitors could use customer mailing profiles, product volume, weight, and revenue distributions, and product insured-value distribution information to assess vulnerabilities and focus sales and marketing efforts to the Postal Service's detriment.

Hypothetical: Customer mailing profile information in the Nonpublic Annex is released to the public. Another delivery service's employee monitors the filing of this information and passes the information along to its sales and marketing functions. The competitor assesses the typical size, mailing volume, and content characteristics of Postal Service NSA customers. The competitor then targets its advertising and sales efforts at actual or potential customers with similar profiles, hindering the Postal Service's ability to reach out effectively to these customers.

This hypothetical would apply even for more generic product-level data, from which one could calculate the distribution of the Postal Service's overall customer base in terms of item weight, revenue, or value (in the case of international insurance). For these reasons, release of any of the nonpublic information would pose actual commercial harm to the Postal Service, regardless of the information's present favorability.

Harm: Revealing customer identifying information associated with competitive domestic and international NSAs would enable competitors to target the customers for sales and marketing purposes.

Hypothetical: The identities of customers with which prices are established in NSAs are revealed to the public. Another expedited delivery service passes along the information to its sales function. The competitor's sales representatives quickly contact the Postal Service's customers and offer them lower rates or other incentives to terminate their contracts with the Postal Service in favor of using the competitor's services. Lost sales undermine the Postal Service's revenues.

Harm: In billing determinants and supporting documentation pertaining to domestic and international competitive NSAs, disclosure of information that would reveal prices associated with particular pricing agreements would provide competing domestic and foreign postal operators, or other potential customers, extraordinary negotiating power to extract lower rates from the Postal Service.

Hypothetical: Customer A's negotiated rates are disclosed publicly. Customer B sees the rates and determines that there may be some additional profit margin between the rates provided to Customer A and the statutory cost coverage that the Postal Service must produce in order for the agreement to be added to the competitive products list. Customer B, which was offered rates identical to those published in Customer A's agreement, then uses the publicly available rate information to insist that it must receive lower rates than those the Postal Service has offered it, or it will not use the Postal Service for its expedited package service delivery needs.

Alternatively, Customer B attempts to extract lower rates only for those destinations for which it believes the Postal Service is the low-cost provider among all service providers. The Postal Service may agree to this demand in order to keep the customer's business overall, which it believes will still satisfy total cost coverage for the agreement. Then, the Customer would use other providers for destinations other than those for which it extracted lower rates. This would affect the Postal Service's overall projected cost coverage for the agreement, so that it no longer would meet its cost coverage requirement. Although the Postal Service could terminate the contract when it first recognized that the mailer's practice and projected profile were at variance, the costs associated with establishing the contract, including filing it with the Postal Regulatory Commission, would be sunk costs that would have a negative impact on the product overall.

Harm: In billing determinants and supporting documentation pertaining to domestic and international competitive NSAs, public disclosure of information contained in underlying financial analyses would be used by competitors and customers to the detriment of the Postal Service.

Hypothetical: A competing package delivery service obtains a copy of information contained in unredacted versions of financial work papers associated with particular agreements. It analyzes information contained in the work papers to determine what the Postal Service would have to charge its customers in order to comply with business or legal considerations, including meeting its minimum statutory obligations regarding cost coverage and contribution to institutional costs. It then sets its own rates for products similar to those that the Postal Service offers its customers below that threshold and markets its purported ability to beat the Postal Service on price for domestic or international delivery services. By sustaining this below-market strategy for a relatively short period of time, the competitor, or a group of the Postal Service's competitors acting in a similar fashion, freeze the Postal Service out of one or more relevant delivery markets. Even if the competing providers do not manage wholly to freeze out the Postal Service, they significantly cut into the revenue streams upon which the Postal Service relies to finance provision of universal service.

Harm: In billing determinants and supporting documentation pertaining to domestic and international competitive NSAs, public disclosure of product volume, weight, revenue distribution, and product insured-value distribution would enable competitors to assess vulnerabilities and focus sales and marketing efforts to the Postal Service's detriment.

Hypothetical: For Inbound Air Parcel Post, a competing package delivery service determines what the Postal Service would need to charge its customers (which may include foreign postal operators) to meet its minimum statutory obligations for cost coverage and contribution to institutional costs. The competing package delivery service then sets its own rates for products similar to those the Postal Service offers other postal operators under that threshold and markets its ability to beat the Postal Service's price for inbound air parcels. By sustaining this below-market strategy for a relatively short period of time, the competitor, or a group of the Postal Service's competitors acting in a likewise fashion, freezes the Postal Service out of the inbound air parcel delivery market.

Hypothetical: For Inbound Surface Parcel Post (at Non-UPU rates) and Canada Post Bilateral for Inbound Competitive Services, another postal operator sees the price and concludes that there may be some additional profit margin between the rates provided to Canada Post and the statutory cost coverage that the Postal Service must produce in order for the agreement to be added to the competitive products list. That postal operator then negotiates lower prices with the Postal Service on its own behalf or uses its knowledge to offer postal customers lower prices than they currently receive. Either or both ways, the Postal Service loses market share and contribution.

(6) The extent of protection from public disclosure deemed to be necessary;

The Postal Service maintains that the portions of the materials filed nonpublicly and relating to competitive products should be withheld from persons involved in competitive decision-making in the relevant markets for competitive delivery products (including private sector integrators and foreign postal operators), as well as their consultants and attorneys. Additionally, the Postal Service believes that actual or potential customers of the Postal Service for these or similar products should not be provided access to the nonpublic materials.

(7) The length of time deemed necessary for the nonpublic materials to be protected from public disclosure with justification thereof; and

The Commission's regulations provide that nonpublic materials shall lose nonpublic status ten years after the date of filing with the Commission, unless the Commission or its authorized representative enters an order extending the duration of that status. 39 C.F.R. § 3007.30.

(8) Any other factors or reasons relevant to support the application.

None.

Conclusion

For the reasons discussed, the Postal Service asks that the Commission grant its application for nonpublic treatment of the Nonpublic Annex of the FY 2011 ACR.

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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December 29, 2011