

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

ANNUAL COMPLIANCE REVIEW, 2012

Docket No. ACR2012

RESPONSES OF THE UNITED STATES POSTAL SERVICE TO
QUESTIONS 1-5 AND 7-9 OF CHAIRMAN'S INFORMATION REQUEST NO. 7

The United States Postal Service hereby provides its responses to the above-listed questions of Chairman's Information Request No. 7, issued on February 1, 2013. Each question is stated verbatim and followed by the response. The responses to Questions 2 and 5 contains redactions. Unredacted copies of the responses are provided under seal in USPS-FY12-NP37.

In addition, some responses make reference to a revised version of USPS-FY12-NP2. The Postal Service expects to file the revised USPS-FY12-NP2 with the Commission on February 11, 2013.

Respectfully submitted,

UNITED STATES POSTAL SERVICE

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Question 1

Please refer to the response to CHIR No. 4, question 12, subpart (b). Also, please refer to the series of periodic reports captioned "United States Postal Service Quarterly Update in Response to Order No. 162" (Quarterly Update), applicable to inbound EMS during FY 2012.¹ Each Quarterly Update groups countries entering inbound EMS under two service tiers: Tier 1, consisting of the postal operators of countries with a performance-level agreement, such as EMS Pay-for-Performance Plan participants and Kalaha Posts Group members; and, Tier 2, all other postal operators.

- a. In the response to subpart (b), the Postal Service states that the "EMS Cooperative Pay-for-Performance Plan was not applicable to the following KPG members: Australia, China, France and Spain."
 - i. For FY 2012, please confirm that Australia and China should have been assigned to Tier 2 in the FY 2012 Quarterly Updates. If not confirmed, please explain why Australia and China were not assigned to either Tier 1 or Tier 2 in the FY 2012 Quarterly Updates.
 - ii. For FY 2012, please confirm that Spain and France should have been assigned to Tier 2, rather than Tier 1, in the FY 2012 Quarterly Updates. If not confirmed, please explain.
 - iii. Other than Australia and China, please confirm that the FY 2012 Quarterly Updates include all countries or territories that enter EMS in the U.S. If not confirmed, please assign any other countries or territories to either Tier 1 or Tier 2 and, for such countries and territories assigned to Tier 1, please indicate whether they are subject to the EMS Cooperative pay-for-performance plan or any other pay-for-performance plan.
- b. In the response to subpart (b), the Postal Service states that pursuant to the KPG Strategic Services Agreement 2012, KPG members are subject to date-certain delivery performance requirements in which "[l]ate deliveries will result in incurring penalties in the form of a postage refund."
 - i. Pursuant to Article 10, section A. of the public version of that Agreement, please confirm that a KPG member that submits inbound EMS for entry into the U.S. must, in the event of late delivery by the Postal Service, refund the mailer-paid postage on application by the mailer. If not confirmed, please explain.
 - ii. In the event of late delivery by the Postal Service, please confirm that the Postal Service does not reimburse the KPG member, or is not otherwise

¹ Quarterly Updates were filed on January 17, 2012; April 2, 2012; July 20, 2012, and October 12, 2012.

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ultimately responsible, for the refund of postage to the mailer. If not confirmed, please explain.

- c. In the public version of the KPG Strategic Services Agreement 2012, referenced in the response to subpart (b), Articles 21, 22, 24, 26, 28, 30, 31, 33 and 36 identify certain expenses allocated to KPG members. For the above referenced Articles, please identify where the FY 2012 expenses allocated to the Postal Service are reported in USPS-FY12-NP2 (Revised), Excel files Reports (Booked).xls (Revised 1-14-13) and Reports.xls (Revised 1-14-13).

RESPONSE:

- a. i. Concerning Australia, for the first quarter of FY2012, prior to the effective date of the bilateral agreement with Australia filed in Docket No. CP2012-1, Australia was assigned to Tier 1 (which includes Pay-for-performance & Kahala Posts Group Members) in the Postal Service's Quarterly Update in Response to Order No. 162 in Docket Nos. MC2009-10 and CP2009-12 for October 1, 2011 to December 31, 2011.² After that, for the second, third, and fourth quarters, Australia entered inbound EMS under the bilateral agreement filed in Docket No. CP2012-1. As a result, when the bilateral was in effect, Australia was not assigned to either Tier 1 or Tier 2 in the Quarterly Updates that the Postal Service filed concerning January 1, 2012 to March 31, 2012,³ April 1, 2012 to June 30, 2012,⁴ and July 1, 2012 to September 30, 2012, because Australia-origin inbound EMS was grouped outside the EMS rates set in connection with

² United States Postal Service Quarterly Update in Response to Order No. 162, Docket No. MC2009-10 and CP2009-12, January 17, 2012.

³ United States Postal Service Quarterly Update in Response to Order No. 162, Docket No. MC2009-10 and CP2009-12, April 2, 2012.

⁴ United States Postal Service Quarterly Update in Response to Order No. 162, Docket No. MC2009-10 and CP2009-12, July 20, 2012.

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the EMS grouping associated with Order No. 162.⁵

China entered inbound EMS for the first quarter of FY2012 under the bilateral agreement that the Postal Service filed in Docket No. CP2010-12, whose effective dates were January 1, 2010 until December 31, 2011.⁶ For the second, third and fourth quarters of FY2012, China entered inbound EMS under the bilateral agreement filed in Docket No. CP2011-68, whose effective dates were January 1, 2012, to December 31, 2012.⁷ As a result, China was not assigned to either Tier 1 or Tier 2 in the Quarterly Updates that the Postal Service filed concerning October 1, 2011 to December 31, 2011,⁸ January 1, 2012 to March 31, 2012,⁹ April 1, 2012 to June 30, 2012,¹⁰ and July 1, 2012 to September 30, 2012, because China-origin inbound EMS was grouped outside the EMS rates set in connection with the EMS grouping associated with Order No. 162.¹¹

ii. For FY 2012, France and Spain were KPG members, and the EMS Cooperative Pay-for-Performance Plan was not applicable to them. Therefore, France and Spain were assigned to Tier 1, rather than Tier 2 in the Quarterly

⁵ United States Postal Service Quarterly Update in Response to Order No. 162, Docket No. MC2009-10 and CP2009-12, October 12, 2012.

⁶ United States Postal Service Response to Order No. 365 concerning the Effective Dates of International Expedited Services 3 Negotiated Services Agreement, Docket Nos. MC2010-13 and CP2010-12, December 30, 2009.

⁷ United States Postal Service Response to Order No. 859 concerning Effective Dates of an Inbound Competitive Multi-Service Agreement with Foreign Postal Operators 1 Negotiated Service Agreement, Docket No. CP2011-68, December 30, 2011.

⁸ United States Postal Service Quarterly Update in Response to Order No. 162, Docket No. MC2009-10 and CP2009-12, January 17, 2012.

⁹ United States Postal Service Quarterly Update in Response to Order No. 162, Docket No. MC2009-10 and CP2009-12, April 2, 2012.

¹⁰ United States Postal Service Quarterly Update in Response to Order No. 162, Docket No. MC2009-10 and CP2009-12, July 20, 2012.

¹¹ United States Postal Service Quarterly Update in Response to Order No. 162, Docket No. MC2009-10 and CP2009-12, October 12, 2012.

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Updates that the Postal Service filed concerning October 1, 2011 to December 31, 2011,¹² January 1, 2012 to March 31, 2012,¹³ April 1, 2012 to June 30, 2012,¹⁴ and July 1, 2012 to September 30, 2012.¹⁵

iii. The U.S. Postal Service hereby confirms that the FY 2012 Quarterly Updates include all countries or territories that enter EMS in the U.S.

b. i. Confirmed

ii. Not confirmed. In the event of late delivery by the Postal Service, the Postal Service reimburses the KPG member for the refund of postage to the mailer. The expenses are included in Postal Service Settlement expenses in the USPS-FY12-NP2 (Revised), Excel files Reports (Booked).xls (Revised 1-14-13) and Reports.xls (Revised 1-14-13).

c. The KPG Strategic Services Agreement 2012 expenses are included in the "Other Costs" line of the A Pages Summary tab of USPS-FY12-NP2 (Revised), Excel files Reports (Booked).xls (Revised 1-14-13) and Reports.xls (Revised 1-14-13).

¹² United States Postal Service Quarterly Update in Response to Order No. 162, Docket No. MC2009-10 and CP2009-12, January 17, 2012.

¹³ United States Postal Service Quarterly Update in Response to Order No. 162, Docket No. MC2009-10 and CP2009-12, April 2, 2012.

¹⁴ United States Postal Service Quarterly Update in Response to Order No. 162, Docket No. MC2009-10 and CP2009-12, July 20, 2012.

¹⁵ United States Postal Service Quarterly Update in Response to Order No. 162, Docket No. MC2009-10 and CP2009-12, October 12, 2012.

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Question 2

The following questions concern Inbound International Expedited Services.

- a. Refer to USPS-FY12-NP2 (Revised), Excel files NSA Summary (Booked).xls (Revised 1-14-13) and NSA Summary (Imputed).xls (Revised 1-14-13), and the worksheet tabs Summary in each file. Under both the booked and imputed methods, please explain why costs for the Inbound International Expedited Services 3 product exceed revenues. Also, please describe what steps the Postal Service will take in the future to ensure that revenues exceed attributable costs.
- b. In Docket Nos. MC2010-13 and CP2010-12, the Postal Service presented a financial model showing that the proposed rates for the Inbound International Expedited Services 3 product, effective in CY 2011 and CY 2012, would cover cost. Please confirm that the financial model is based upon imputed revenues and expenses. If not confirmed, please explain. If confirmed, please explain the causes of the difference between the cost coverage reported for the Inbound International Expedited Services 3 product in FY 2012 under the imputed method and the cost coverage estimated in the Postal Service's financial model.
- c. Please reconcile the sum of pounds for International Expedited Services 3, International Expedited Services 4, and Residual International Expedited Services shown in the Excel files NSA Summary (Booked).xls (Revised 1-14-13) and NSA Summary (Imputed).xls (Revised 1-14-13), worksheet tabs Summary with the pounds for Inbound International Expedited Services shown in USPS-FY12-NP2 (Revised), Excel files Reports (Booked).xls (Revised 1-14-13) and Reports.xls (Revised 1-14-13), worksheet tabs A Pages (c), Table A-2 in each file.

RESPONSE:

a - b. The Inbound International Expedited Services 3 agreement filed in Docket No. CP2010-12 was only in effect for Quarter 1 of FY 2012. Subsequently, inbound EMS was included in the agreement filed in Docket No. CP2011-68, which was in effect for Quarters 2 – 4 of FY 2012.¹⁶ As such, a discussion that includes reference to not only the agreement filed in Docket No. CP2010-12, but also the agreement filed in Docket

¹⁶ See United States Postal Service Response to Order No. 859 concerning Effective Dates of an Inbound Competitive Multi-Service Agreement with Foreign Postal Operators 1 Negotiated Service Agreement, Docket No. CP2011-68, December 30, 2011.

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No. CP2011-68 is more complete and more up-to-date, because it is an apples-to-apples comparison.

The amounts discussed in this response are based on the Imputed version of the Reports files, because the financial models filed to support rates (CP2010-12 and CP2011-68) are based on the Imputed version of the Reports files. The discussion also applies to the results shown in the Reports (Booked) files.

Despite a decrease in revenue between FY 2011 and FY 2012, cost coverage improved as cost decreased more than revenue. The FY 2012 cost coverage was only [REDACTED] lower than that projected in the financial model filed as part of CP2011-68.

A [REDACTED] was the primary contributor to the decrease in revenue between FY 2011 and FY 2012. Although [REDACTED] increased about [REDACTED], [REDACTED] decreased about [REDACTED] between fiscal years. The [REDACTED] from FY 2011 to FY 2012 and the [REDACTED] FY 2011 and FY 2012, but the [REDACTED] mitigated the beneficial impact of the [REDACTED].

c. Concerning International Expedited Services 3, when data were transferred from Reports (Booked).xls (Revised 1-14-13) to the NSA Summary (Booked).xls (Revised 1-14-13), cells q123 and q159 were not converted to pounds (they remained kilograms), resulting in incorrect China Competitive EMS amounts. Converting these kilograms to pounds corrects the problem. This also affects the NSA Summary (Imputed).xls (Revised 1-14-13) reporting of China's weight as well as the Residual International Expedited Services (see cell g127 of the NSA Summary workbooks). Total weight (cell g164 of the NSA Summary workbooks) is unaffected because the China conversion

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errors were offset in the calculation of the Residual International Expedited Services amounts. No such problem existed concerning International Expedited Services 4.

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Question 3

The following questions concern international negotiated service agreements (NSAs) for Global Plus Contracts.

- a. Please reconcile the sum of volumes for Global Plus 1B, Global Plus 1C, Global Plus 2B, and Global Plus 2C contracts presented in USPS-FY12-NP2 (Revised), Excel file NSA Summary (Booked).xls (Revised 1-14-13), worksheet Summary, with the total volume for Global Plus Contracts reported in USPS-FY12-NP2 (Revised), Excel file Reports (Booked).xls (Revised 1-14-13), worksheet tab A Pages (c), Table A-2. Also, please show the distribution of the reconciled total among the Global Plus 1B, Global Plus 1C, Global Plus 2B, and Global Plus 2C contracts.
- b. Please respond to subpart (a), above, with reference to the Excel file NSA Summary (Imputed).xls (Revised 1-14-13), worksheet tab Summary and the Excel file Reports.xls (Revised 1-14-13), worksheet tab A Pages (c), Table A-2.

RESPONSE:

Please see USPS-FY12-NP35, filed concurrently with the response to Chairman's Information Request No. 5, Question 5, and the Reports, Reports (Booked), NSA Summary (Imputed) and NSA Summary (Booked) files of USPS-FY12-NP2 (Revised 2-8-13).

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Question 4

The following questions concern inbound competitive international NSAs for Inbound Competitive Multi-Service Agreements with Foreign Postal Operators.

- a. In USPS-FY12-NP2, the Excel file NSA Summary (Booked).xls (Revised 1-14-13), worksheet tab Summary, combines the financial results for Inbound Competitive Multi-Service Agreements with Foreign Postal Operators 1 with the Canada Post—USPS Contractual Bilateral Agreement for Inbound Competitive Services (CP2012-4). The Excel file Reports (Booked).xls (Revised 1-14-13), worksheet tab A Pages (c), Table A-2, reports these financial results separately. Excluding the financial results for Canada Post—USPS Contractual Bilateral Agreement for Inbound Competitive Services, please reconcile the total revenue, pieces, pounds, volume variable cost, product specific costs (if any), and contribution for Inbound Competitive Multi-Service Agreements with Foreign Postal Operators 1 shown in USPS-FY12-NP2 (Revised), Excel file NSA Summary (Booked).xls (Revised 1-14-13), worksheet tab Summary with the total revenue, pieces, pounds, volume variable cost, product specific costs (if any), and contribution for Inbound Competitive Multi-Service Agreements with Foreign Postal Operators 1 shown in Table A-2. Also, please show the distribution of the reconciled totals among the postal operators listed for Inbound Competitive Multi-Service Agreements with Foreign Postal Operators 1 in the worksheet tab Summary.
- b. Please respond to subpart (a), above, with reference to the Excel file NSA Summary (Imputed).xls (Revised 1-14-13), worksheet tab Summary and the Excel file Reports.xls (Revised 1-14-13), worksheet tab A Pages (c), Table A-2.

RESPONSE:

- a. The inconsistency was the result of missing CPC Expedited Parcel data for part of the year in staging the NSA Summary (Booked).xls (Revised 1-14-13). Total Expedited Parcel revenue for FY 2012 was properly staged in cell v122 of the Summary sheet, but the adjacent cells for pieces, weight and volume variable costs (columns w, x and y of the same row) only picked up data for part of the year. As a result, the CPC Competitive NSA was misreported and did not match the amounts reported on Reports (Booked).xls (Revised 1-14-13).

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Once the CPC changes are implemented on the NSA Summary Reports, the amounts agree with Reports (Booked).xls (Revised 1-14-13). Complete reconciliations between the NSA Summary reports and the Reports files are provided beginning at row 200 of the NSA Summary (Imputed) ChiR7.xls and NSA Summary (Booked) ChIR7.xls included in the revisions to USPS-FY12-NP2 (Revised 2-8-13). These are not highlighted with the other changes because they are not part of the formal report, rather, they are provided to aid understanding the reconciliation.

b. The above reconciliation is not necessary for the NSA Summary (Imputed).xls (Revised 1-14-13) because the CPC Expedited Parcel data were staged correctly in the Imputed version.

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Question 5

The following question concerns International Ancillary Services. In USPS-FY12-1, and the Excel file "Fy2012_RPWsummaryreport_public.xls," the Revenue, Pieces and Weight (RPW) report presents International Ancillary Services revenues of \$29,332. The RPW report also presents Other International Special Services revenue of \$103. In USPS-FY12-42, and the Excel file "FY12PublicCRA.xls," worksheet tab Cost2, the Public Cost and Revenue Analysis (PCRA) report presents Total International Ancillary Services revenue of \$30,012. Please explain where the difference in revenue of \$577 ($\$30,012 - (\$29,332 + \$103)$) is reported in the RPW. Also, please explain the rationale for the difference in the reporting of International Ancillary Services revenue between the RPW report and the PCRA report.

RESPONSE:

The \$577 difference consists of the following fees: [REDACTED] for Certificate of Mailing, [REDACTED] for Undelivered International Mail and [REDACTED] for Postage Due International Mail and they are reported as First-Class Mail Fees in RPW. These fees are separately reported as International fees in the PCRA and they are reported with Domestic fees in RPW.

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Question 7

The reported costs for Customized Postage in FY 2012 are \$77,252, which is 54.5 percent greater than reported costs for Customized Postage in FY 2011. Please explain the reason for the large increase.

RESPONSE:

In FY 2012, an additional Postal EAS employee joined the team, and about a quarter of the employee's time was devoted to licensing and fee activity associated with Customized Postage. As a result, a quarter of the employee's compensation (\$22K) was included in the costs for Customized Postage for FY 2012.

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Question 8

The following table contains the calculation of the Net Value for Contract Year 1 of the MC2011-19 Discover NSA using the Commission's MC2004-3 approved methodology for measuring the Net Value to the Postal Service for Market Dominant NSAs.

[Table Omitted]

- a. Please confirm the Net Value to the Postal Service was $-\$4,337,569$ in Contract Year 1 using the Commission's approved methodology. If not confirmed, please explain.
- b. Please confirm the Postal Service's estimate of the Net Value to the Postal Service of the Discover NSA in Contract year 1 in USPS-FY12-30 is $\$23,567,688$ to $\$25,513,070$. If not confirmed, please explain.
- c. Please discuss the differences in methodology between the Commission's approved method and the Postal Service method.
- d. Please explain which method should be used to measure the Net Value of the Discover NSA.

RESPONSE:

- a. Confirmed.
- b. Confirmed.
- c. The Commission's approved methodology applies a mail class elasticity, which is representative of all mailers, to that of one single mailer, Discover. The Postal Service's methodology differs from the Commission's methodology because it examines the specific trends and characteristics of the customer that is subject to the NSA, which in this case is Discover, and forecasts the volumes based on historic trends as well as prevailing market conditions. This results in a baseline threshold volume that differs from that computed using the Commission's methodology.

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- d. The Postal Service believes that the Commission should use the Postal Service's method to measure the Net Value of the Discover NSA. The Postal Service's method is customer-specific and provides a more accurate look at the expected volumes absent the effect of the NSA, which, in turn, will provide a Net Value which fairly represents the results achieved in the Contract Year 1.

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Question 9

Please provide the FY 2012 Total Factor Productivity figures and the supporting workpapers.

RESPONSE:

The figures appear in USPS-FY12-17, at page 37 of the Comprehensive Statement on Postal Operations. See ChIR7.Q9.xls, attached to this response, for the supporting workpapers.