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Before the
POSTAL REGULATORY COMMISSION
WASHINGTON, DC 20268-0001

Rate Adjustment Due to Extraordinary or Exceptional Circumstances

Docket No. R2013-11

PUBLIC REPRESENTATIVE COMMENTS IN RESPONSE TO THE EXIGENT REQUEST OF THE UNITED STATES POSTAL SERVICE

(November 26, 2013)

Respectfully submitted,

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I. INTRODUCTION AND SUMMARY

A. Introduction

On September 26, 2013, the United States Postal Service (Postal Service) filed a request with the Postal Regulatory Commission (Commission) for authorization to increase rates for market dominant products, which exceed the otherwise applicable limitations allowed by 39 U.S.C. § 3622(d)(1)(A) and 39 CFR § 3010.11.[1] The Postal Service filed this Request pursuant to 39 U.S.C. § 3622(d)(1)(E) and 39 CFR § 3010.60 *et seq.,* the provisions of the United States Code and the Commission's rules applicable to rate adjustments in "exigent" circumstances. The Public Representative respectfully submits the following comments addressing the issues raised by the Postal Service's Request as permitted by Order No. 1847.[2]

[1] Renewed Exigent Request of the United States Postal Service in Response to Commission Order No. 1059, September 26, 2013 (Request).

[2] Notice and Order Concerning Exigent Request, September 30, 2013 (Order No. 1847). *See also,* Ruling Adjusting Procedural Schedule, October 17, 2013 (P.O. Ruling R2013-11/1).

B. Summary

The Public Representative's comments address the sufficiency of the justification for an exigent rate increase (Section III), the volume estimates presented by Postal Service representative Thress (Section IV), proper application of "banked" price authority (Section V), and whether the specific rate adjustments are reasonable and equitable (Section VI).

Section III, Exigency Analysis. The Public Representative believes that the Postal Service has not adequately justified its exigent Request, but leaves open the possibility that in the future the Postal Service may be able to provide adequate justification based upon the effects of the current economic downturn. This is the same conclusion presented in the Docket No. R2010-4 exigent request. The most significant issues are the precedent that will be established by justifying an exigent request based on only one year of the recession, instead of the total recession. This will allow the Postal Service to again file exigent requests based on other years of the recession, and effectively nullify price cap regulation. The Postal Service has also requested annual funding of $1.78 billion in contribution that for all effective purposes will be permanently added to the rate base. With no end date for the exigency, the cumulative funding request is unknown, and not justified.

Section IV, Thress Analysis. Mr. Thress does not establish a satisfactory link between his estimate of volume declines during the most recent recession, and exigent financial outcomes due to the recession. He states that a lower level of equilibrium volume has been in effect since 2010, yet attributes the gap in volume between this new equilibrium and the path of a previously higher equilibrium to be volume lost due to exigent circumstances. He overestimates volumes lost due to exigent circumstances by counting volume changes that occurred during times over which the Postal Service was making operational changes to reduce the impact of unexpected volume losses. He overestimates volumes lost due to exigent circumstances by omitting variables that could directly measure mail lost due to Internet diversion.

Section V, Treatment of Unused Rate Adjustment Authority. The Public Representative applies the treatment of unused rate adjustment authority rules, 39 CFR § 3013.63, and concludes that approval of the exigent request requires the zeroing out of banked authority for all market dominant classes.

Section VI, Rate Analysis. The Public Representative concludes that the Postal Service has proposed prices that are reasonable and equitable for the most part. However, the Public Representative opposes prices for any products that do not cover attributable costs at a time when the Postal Service is experiencing financial difficulties. The Public Representative also opposes setting worksharing prices that deviate significantly from 100 percent passthroughs. Such prices are inefficient and send incorrect pricing signals. The Postal Service again fails to take advantage of the pricing flexibility provided by the PAEA to rectify these persistent pricing problems.

II. THE RECORD AND STATUTORY CONSIDERATIONS

A. Record Overview

On September 26, 2013, the Postal Service filed Renewed Exigent Request of the United States Postal Service in Response to Order No. 1059 (Request). The Postal Service filed three statements and thirteen library references in support of its Request. The following statements were filed:

- Statement of Stephen J. Nickerson on Behalf of the United States Postal Service, September 26, 2013 (Nickerson Statement);
- Statement of Altaf Taufique on Behalf of the United States Postal Service, September 26, 2013 (Taufique Statement); and
- Further Statement of Thomas E. Thress on Behalf of the United States Postal Service, September 26, 2013 (Thress Statement).

The following library references were filed:

- USPS-R2010-4R/2 - First-Class Mail Worksheets;
- USPS-R2010-4R/3 - Standard Mail Worksheets;
- USPS-R2010-4R/4 - Periodicals Worksheets;
- USPS-R2010-4R/5 - Package Services Worksheets;
- USPS-R2010-4R/6 - Special Services Worksheets;
- USPS-R2010-4R/7 - Product Cost & Contribution Estimation Model (Public Version), USPS-R2010-4R/NP1 - Product Cost & Contribution Estimation Model (Non-Public Version);
- USPS-R2010-4R/8 - Cost Factor Development (Public Version), USPS-R2010-4R/NP2 - Cost Factor Development (Non-Public Version);
- USPS-R2010-4R/9 - Revenue and Volume Forecast Materials (Public Version), USPS-R2010-4R/NP3 - Revenue and Volume Forecast Materials (Non-Public Version);
- USPS-R2010-4R/10 - Decomposition of Mail Volume into Sources of Change; and

- USPS-R2010-4R/11 - Calculation of Contribution Lost from Recession-Related Volume Losses.

The above materials were updated as necessary throughout the course of the proceeding.

The Presiding Officer posed Presiding Officer Information Requests to the Postal Service dated: October 23, 2013 (POIR No. 1); October 23, 2013 (POIR No. 2); October 25, 2013 (POIR No. 3); October 29, 2013 (POIR No. 4); October 29, 2013 (POIR No. 5); November 6, 2013 (POIR No. 6) November 8, 2013 (POIR No. 7); November 15, 2013 (POIR No. 8); November 21, 2013 (POIR No. 9); November 21, 2013 (POIR No. 10); and November 21, 2013 (POIR No. 11). The Postal Service provided responses to these requests in the form of written responses and additional Library References.[3]

Finally, public hearings convened in the Commission's hearing room on November 19 – 20, 2013. Messrs. Nickerson, Taufique, and Thress on behalf of the Postal Service answered questions posed by the Commissioners of the Postal Regulatory Commission.

Although not part of the record of this proceeding, the Commission also sponsored three technical conferences. The topics of the technical conferences were as follows:

- Material related to the statements of Mr. Taufique, October 24, 2013;
- Material related to the statements of Mr. Thress, October 31, 2013; and
- Material related to the statements of Mr. Nickerson November 1, 2013.

[3] Several responses were pending at the time these comments were filed.

B. Statutory Considerations

1. United States Code Provisions

Title 39, section 3622, enables the development of modern rate regulation applicable to all Postal Service market dominant products. This section authorizes the Commission to establish “a modern system for regulating rates and classes for market-dominant products.” 39 U.S.C. § 3622(a). It specifies “objectives” (39 U.S.C. § 3622(b)) and “factors” (39 U.S.C. § 3622(c)) that must be considered as part of the regulatory system. Finally, it specifies “requirements” that must be incorporated into the regulatory system. 39 U.S.C. § 3622(d).[4]

Two requirements are directly applicable to the Postal Service’s exigent Request. The first requirement establishes an annual limitation on rate adjustments equal to the Consumer Price Index for All Urban Consumers (CPI-U).

> (1) In general. - The system for regulating rates and classes for market-dominant products shall - (A) include an annual limitation on the percentage changes in rates to be set by the Postal Regulatory Commission that will be equal to the change in the Consumer Price Index for All Urban Consumers unadjusted for seasonal variation over the most recent available 12-month period preceding the date the Postal Service files notice of its intention to increase rates;

39 U.S.C. § 3622(d)(1)(A). This requirement establishes limitations for rate-setting under typical business conditions.

The second requirement establishes an exception to the above limitation. Its purpose is to allow rate adjustments in excess of CPI-U under limited, atypical circumstances.

> (E) notwithstanding any limitation set under subparagraphs (A) and (C), and provided there is not sufficient unused rate authority under paragraph (2)(C), establish procedures whereby rates may be adjusted on an

[4] Additional provisions are included concerning “workshare discounts” (39 U.S.C. § 3622(e)) and transitioning from the previous regulatory system to the new system (39 U.S.C. § 3622(f)).

> expedited basis due to either extraordinary or exceptional circumstances, provided that the Commission determines, after notice and opportunity for a public hearing and comment, and within 90 days after any request by the Postal Service, that such adjustment is reasonable and equitable and necessary to enable the Postal Service, under best practices of honest, efficient, and economical management, to maintain and continue the development of postal services of the kind and quality adapted to the needs of the United States.

39 U.S.C. § 3622(d)(1)(E).

2. Code of Federal Regulations Provisions

The Commission developed implementation rules encompassing 39 U.S.C. § 3622(d)(1)(E). These rules appear at 39 CFR § part 3010, subpart A, General Provisions, and subpart E, Rules for Rate Adjustments in Exigent Circumstances (Type 3 Rate Adjustments). Specific rules applicable to exigent requests address: Applicability (3010.60); Contents of exigent requests (3010.61); Supplemental information (3010.62); Treatment of unused rate adjustment authority (3010.63); Expeditious treatment of exigent requests (3010.64); Special procedures applicable to exigent requests (3010.65); and Deadline for Commission decision (3010.66).

The Public Representative files its comments pursuant to Order No. 1847 and 39 CFR § 3010.65(f).

> (f) Following the conclusion of the public hearings and submission of any supplementary materials interested persons will be given the opportunity to submit written comments on:
>
> > (1) The sufficiency of the justification for an exigent rate increase;
> >
> > (2) The adequacy of the justification for increases in the amounts requested by the Postal Service; and
> >
> > (3) Whether the specific rate adjustments requested are reasonable and equitable.

The Public Representative is permitted to file reply comments pursuant to Order No. 1847 and 39 CFR § 3010.65(g).

> (g) An opportunity to submit written reply comments will be given to the Postal Service and other interested persons.

III. EXIGENCY ANALYSIS

A. Introduction

Postal Service representative Nickerson states the Postal Service "needs this money because it has an ongoing liquidity challenge."[5] He confirms that the liquidity challenge is to some extent the most critical financial issue faced by the Postal Service. Tr. 2/192. His opinion is that the exigency case might not have been filed if not for the liquidity problem. *Id.* at 193. He acknowledges that an exigent increase "does not fix the Postal Service's liquidity problem, but it gives us breathing room." *Id.* at 177, 193. He explains that "what we're doing asking for the extra price increase is we're trying to increase our financial flexibility." *Id.* at 178. He does not envision the anticipated financial need going away. *Id.* at 200. When asked, he could not guarantee that the Postal Service would not seek additional exigent funds based on the same exigent recession. *Id.* at 193, 209-10. Finally, he does not know how exigent price increases could be rolled back. *Id.* at 184.

The Public Representative suggests that the Postal Service has outlined the basis for a "cost of service" price increase, not an exigent increase.[6] The ability to seek a cost of service increase expired approximately one year after enactment of the PAEA.[7]

Under the PAEA, the Postal Service may seek price increases based on a CPI-U price cap system. A major attribute of the price cap system is the incentive it provides to reduce costs. By comparison, the cost of service increase sought by the Postal

[5] Tr. 2/201; "The Postal Service's problem is a lack of adequate liquidity." Nickerson Statement at 5 (footnote omitted).

[6] *See* Tr. 2/206. The Request goes beyond seeking compensation for unexpected and exigent circumstances. The Postal Service has no plans to remove the price increase at any time after the exigent crisis has passed. This would permanently add the price increase to the price base. In this sense, the Postal Service is actually seeking a cost of service increase.

[7] *See* 39 U.S.C. § 3622(f).

Service provides no incentive to reduce costs, provides no incentive to adjust the postal system to a new normal, and is not consistent with the PAEA.

The Postal Service also may seek price increases to address exigent circumstances. The recent recession may have contributed to the liquidity problem, but is dwarfed by other factors such as the Postal Service Retiree Health Benefits Fund (PSRHBF) prefunding issue, and the ongoing electronic diversion of mail out of the postal system. The Postal Service states it requests an exigent price increase due to the recession, but all its argument clearly indicates the need for an exigent price increase is “due to” a perceived cost of service liquidity problem.

Regardless, the Postal Service has not quantified the effects of the recession on the Postal Service in a manor upon which an exigent request can be approved. It has no estimate for when it will recover from the recession, *i.e.,* adjust to a new normal. It has no plans to ever roll back exigent prices, effectively adding the exigent price increase to the rate base forever. It has no explanation of what incentive new exigent prices provide to ever adjust the postal system to new mailing volumes. In conclusion, the Postal Service has not justified its exigent Request.[8]

B. Postal Service Financial Issues

The Public Representative looks to the Postal Service’s recent Form 10-Q, signed August 9, 2013, and its past two 5-year plans to gain a better understanding of its financial problems. From this review, the Public Representative concludes the Postal Service presents evidence of a liquidity problem due to a decline in mail volume

[8] For background, the Public Representative encourages everyone to read Docket No. R2010-4, Public Representative Comments in Response to the Exigent Request of the United States Postal Service, August, 17, 2010 (Background). Most of the argument made therein is applicable to the instant docket. The Public Representative’s conclusions in Docket No. R2010-4 are the same as his conclusions in the instant Docket. “The Public Representative believes that the Postal Service has not adequately justified its exigent Request, but leaves open the possibility that in the future the Postal Service may be able to provide adequate justification based upon the effects of the current economic downturn.” Background at 2.

primarily caused by electronic diversion. The Postal Service nowhere highlights ongoing recessionary problems in these documents.

Notable out-takes from the Postal Service's recent Form 10-Q, signed August 9, 2013, follow:

> The Postal Service continues to suffer from a severe lack of liquidity.

Form 10-Q, August 9, 2013, at 7.

> The requirement of the Postal Accountability and Enhancement Act, Public Law 109-435 (P.L. 109-435) to prefund its retiree health benefit obligations, a requirement not imposed upon other federal agencies or private sector businesses, plus the drop in mail volume and changes in the mail mix caused by changes in consumers' use of mail, have been the major factors contributing to Postal Service losses since the recession ended in 2009. Without structural change to the business model, the Postal Service will continue to be negatively impacted by these factors and, absent legislative change, it anticipates continuing quarterly losses into the foreseeable future.
>
> * * *
>
> This low level of liquidity will continue to exist, absent legislative actions by Congress that have been requested to assist the Postal Service in returning to a financially stable position[.]

Id. at 8.

> The Postal Service continues to introduce new service offerings to generate new revenue and to slow the migration of existing revenue streams to electronic alternatives.

Id. at 9.

> Although significant efforts continue to be made to increase revenues and contain costs under management's control, the Postal Service has not been able to completely offset the impacts of our declining mail volumes. In addition, the accrual of the large PSRHBF prefunding requirement and continuation of six-days-per-week delivery adversely affect our financial results.

Id. at 24.

> Businesses and consumers have embraced greater use of the internet, mobile communications and other technological platforms to communicate and facilitate business transactions. This behavioral shift has had a significant negative impact on our traditional sources of revenue. Although some trends, such as an increase in the shipment of goods purchased online, were positive for our business, the shift to electronic communication alternatives continues to present significant business challenges for the Postal Service.
>
> The impact of technological change has been especially pronounced on our First-Class Mail revenues which continue to decline even as new services, the growth of e-commerce, and successful marketing campaigns have helped us grow our Shipping and Packages revenues.
>
> * * *
>
> We anticipate that the volume of First-Class Mail will never return to former levels experienced in the mid-2000s; in fact, we predict that it will continue to decrease well into the foreseeable future.

Id. at 27.

> First-Class Mail and Standard Mail accounted for approximately 68% of total revenues for the nine month periods ended June 30, 2013, and 2012.
>
> * * *
>
> The most significant factor contributing to this decline continues to be the migration toward electronic communication and transactional alternatives.

Id. at 29.

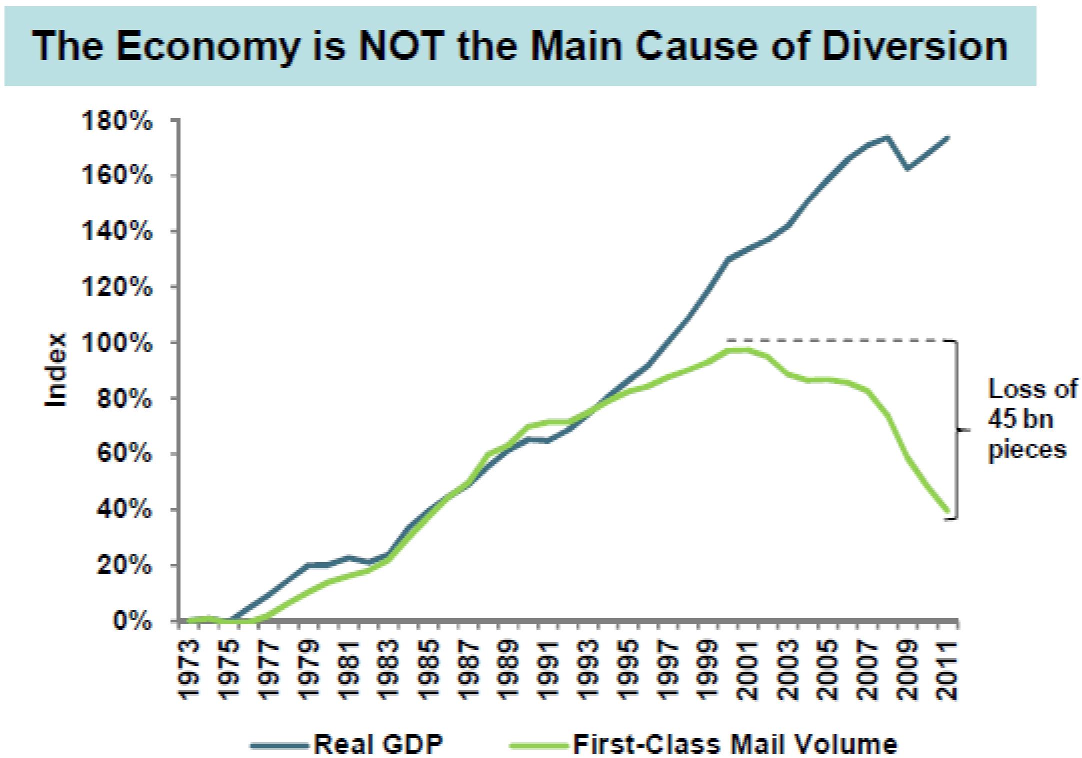
> We continue to see the impact that electronic devices have on written media and expect that the popularity of these devices will continue to have a detrimental impact on our results from Periodicals into the foreseeable future.

Id. at 30.

There is ample discussion concerning the liquidity problem, electronic diversion, and the associated loss of mail volume. If the recession was an important, continuing (exigent) event, the Public Representative would have thought it might have figured prominently in the Postal Service's FORM 10-Q.

The following graph was included in a Postal Service presentation on a slide titled “Electronic Diversion is the Primary Driver of First-Class Mail Volume Decline.”

Figure III-1
Electronic Diversion



United States Postal Service, Plan to Profitability, 5 Year Business Plan, February 16, 2012, at 5. This same slide explains that “Diversion of communication and commerce to electronic channels is a principal contributor to declining First-Class Mail volumes.” It also states “Diversion reflects a permanent secular shift in customer behavior and is more pronounced during periods of economic weakness.”

Compare this to Mr. Thress’s presentation in “TABLE ONE: Exigent FY 2008 – 2012 Losses Attributable to the Great Recession.” He indicates that over 48 billion First-Class Mail pieces were lost (3,926.9 + 10,037.0 + 15,031.7 + 19,044.0 in millions) from 2008 through 2011 attributable to the recession. Thress Statement at 4, Table 1. It would have been interesting to see a reconciliation of the information presented in the 5-year plan, and the Thress statement. As it stands, there appears to be a question of whether volume loss is the result of electronic diversion, or the recession.

It is important for the Commission to understand the causes of mail volume decline since the beginning of the recession. If the economy is "not the main cause" of mail diversion (for at least First-Class Mail), an exigent request should only be granted to the extent it is attributable to an exigent event in the economy actually causing mail diversion. The information in FORM 10-Q and in the 2012 5-year plan appear to support reasons other than the recession for a decline in mail volume.

Mr. Nickerson sheds further light on the Postal Service's problems and the need for an exigent increase. Mr. Nickerson testifies about breathing room the exigent increase might provide the Postal Service in case of an emergency. He states that "[i]mplementation of the exigent price increase will give Postal Service greater ability to make necessary capital investments." Nickerson Statement at 11. He states that the exigent increase "will allow the organization to pay down some of its debt in the short term." *Id.* at 11.

The Public Representative contends that exigent price increases should be used to deal with specific exigencies, and not to create a rainy-day fund to address optional expenditures. If an emergency happens in the future, it may be appropriate to seek exigent relief at that time based on the new exigency. That is the purpose of the exigency provisions. An exigent request should not be approved based on the anticipation that there may be a future emergency, or that breathing room is necessary to deal with unrelated matters.

C. When Will the Exigency be Over

The Postal Service states that "the additional $1.78 billion in contribution is 'necessary' for the Postal Service to continue providing effective and adequate postal services, potentially until such time that Congress makes fundamental changes to the postal business model." Request at 2.

The Public Representative thought he understood that the Postal Service seeks an exigent price increase due to the effects of the recession, *i.e.,* the exigency. It is understandable how Congressional action might improve the Postal Service's cash flow issue. However, the Public Representative fails to understand how Congressional action is going to have any effect on ending the recession (exigency), such that exigent funding will be no longer necessary.

The Postal Service's statement concerning when it will no longer need exigent funding is a clear indication that the purpose of the request is not to deal with the effects of the recession (due to requirement), but to address general, business as usual, cash flow concerns.

What is missing is a Postal Service statement such as an additional $1.78 billion in contribution is "necessary" for the Postal Service to continue providing effective and adequate postal services *until the Postal Service has recovered from the effects of the recession*. This statement must be supported by a description of the Postal Service's recovery plan. The plan must outline the actions and costs necessary to adjust the Postal Service's network to the new normal, and provide estimates of the time required to complete such actions.

D. Postal Service Estimate of Recessionary Effect

The Postal Service Request does not present total revenue and contribution losses "due to" the recession. This might be because the Postal Service would like the Commission to believe the effects of the recession are continuing, and may be felt for 20 or more years.[9]

[9] Mr. Nickerson stated "we very well could be talking about the effects of the great recession 20 years from now. Tr. 2/222.

The Postal Service's statements are confusing, and required POIRs and questions posed at the hearing to be made clear. Table 2 from the Nickerson Statement is replicated in Table III-1.

Table III-1
Exigent Revenue and Contribution Losses (in millions), FY 2008 – FY 2012

	Volume	Revenue	Contribution
FY 2008	(11,061)	($3,398)	($1,246)
FY 2008 thru 2009	(34,759)	($9,973)	($3,634)
FY 2008 thru 2010	(42,333)	($12,763)	($4,816)
FY 2008 thru 2011	(47,981)	($14,898)	($5,770)
FY 2008 thru 2012	(53,546)	($16,883)	($6,644)

Clarification was needed that the volume, revenue, and contribution figures presented by the Postal Service were not cumulative, but represented losses in individual fiscal years. *See* POIR No. 6, question 14. What the Postal Service states is that the row labeled "FY 2008" reflect lost contribution from 11,061 million mail pieces in FY 2008 alone. The row labeled "FY 2008 thru 2009" reflect lost contribution from the same 11,061 million mail pieces lost in FY 2008 plus an additional 23,698 million newly lost mail pieces in FY 2009, for a total of 34,759 million mail pieces lost in FY 2009 alone. Each following row counts the mail volume that was lost in previous years, plus additional piece lost in that year.

Thus, the Postal Service estimates it has lost contribution from 189.7 billion mail pieces due to the recession through the close of FY 2012 (11,061 million mail pieces in FY 2008, 34,759 million mail pieces in FY 2009, 42,333 million mail pieces in FY 2010, 47,981 million mail pieces in FY 2011, and 53,546 million mail pieces in FY 2012).

In a similar fashion, the Postal Service estimates a revenue loss of $57.9 billion due to the recession through the close of FY 2012 ($3,398 million + $9,973 million +

$12,763 million + $14,898 million + $16,883 million). It estimates a contribution loss of $22.1 billion due to the recession through the close of FY 2012 ($1,246 million + $3,634 million + $4,816 million + $5,770 million + $6,644 million). *See* Tr. 2/221.

The saga of volume and contribution losses due to the recession only continues. The Postal Service predicts it will lose contribution from an additional 58,790 million mail pieces in FY 2013 alone. Response to POIR No. 6, question 14. It predicts it will lose contribution from yet another additional 63,895 million mail pieces in FY 2014 alone. *Id.* Per Postal Service analysis, losses continue to amass into the unknown future. Thus, the Postal Service does not present an estimate of total losses due to the recession.

E. Problems With the Postal Service's Approach to Estimating Losses

The Postal Service's approach to analyzing the effects of the recession indicates that it could seek rates to generate $22.1 billion in additional contribution at the conclusion of FY 2012 (if this were even possible). With losses continuing to increase, the Postal Service could seek additional increases based on new recessionary losses far into the future.

The Postal Service's approach assumes it could and possibly should be compensated for mail volume lost during the recession, year-after-year-after-year. Yet, the Postal Service readily admits this is Mail volume that is unlikely to return in the foreseeable future.

This is because the estimates assume that the Postal Service does nothing to shed mail volume capacity to adjust to the new normal.[10] Almost six years after the start of the recession, the Public Representative would assume that postal management has reacted, and is somewhere on the path to adjusting to the new normal. These adjustments must be considered (and offset the losses presented in Table 2) when

[10] If this were the case, the estimates might be accurate, but would be a clear deviation from "honest, efficient, and economical management".

estimating the effects of the recession for the purpose of an exigent request.[11] It is not equitable to compensate the Postal Service for FY 2008 network capacity, when this network capacity is no longer required to meet present or future mail demands. Instead, the Postal Service must quantify the additional contribution needed until it can complete its adjustment to the new normal.

F. Problems With Relying on the Postal Service's Estimates

Instead of basing its Request on an estimated total effect of the recession, the Postal Service bases its Request on the estimate of only one year's losses, FY 2012. The Public Representative takes issue with the arbitrary selection of one year over another. It appears that FY 2012 was selected because it demonstrates the largest volume loss for which other supporting data was available. If the point of this request was to recover from the recession, the request should be based on the total effects of the recession.

The Postal Service states that it "calculates that it has lost approximately 53.5 billion mail pieces due to the recession in fiscal Year (FY) 2012, resulting in a contribution loss of approximately $6.65 billion in that year alone." Request at 2. The Postal Service goes on to state "[t]he Request proposes price increases to recover a modest proportion of that lost contribution, approximately $1.78 billion." *Id.*

These statements raise very serious issues for the Commission to consider. The first issue is whether or not the Postal Service will, in the future, seek to recoup the remaining $4.87 billion ($6.65 billion - $1.78 billion). The Postal Service states that it "has no present intention to pursue the balance of the estimated exigent harm." Response to POIR No. 5, question 2(b). The Postal Service adds a caveat requiring

[11] Otherwise, the Postal Service could have done nothing, let losses mount, and instead seek a potentially larger exigent request in the future based on compounding losses.

approval of the separately filed CPI-U market dominant price increases.[12] *Id.* The Public Representative urges the Commission to not allow the Postal Service to use the recession exigency as a line of credit that can be tapped anytime the Postal Service's liquidity/cash flow problems arise. The Request in effect negates the price cap provisions of the statute. Sufficient time has passed since the onset of the recession for the Postal Service to be able to estimate its exigent needs "due to" the recession.

The second issue is whether the Postal will in the future seek to recoup losses from periods other than FY 2012. If the Commission establishes a precedent that an exigency exists based on the recession, and that the Postal Service properly estimated losses due to that recession in FY 2012 alone, there is nothing to prevent the Postal Service from seeking additional exigent increases based on FY 2008, FY 2009, FY 2010, FY 2011, or FY 2013, etc. Once the precedent is established, it will be difficult for the Commission to arbitrarily limit future requests.

The Postal Service states "we hope to be able to maintain sufficient liquidity through 2017 such that the gains from this case would represent the full and final amount of net contribution that the Postal Service expects to request for volume losses from the 2008 – 2012 period." *Id.* This statement leaves open the possibility of a future exigent filing based upon the same recession.

The Public Representative urges the Commission to avoid establishing a precedent that would provide the Postal Service with a permanent line of credit based on the exigency of a single recession. This will lead to future unpredictable postal rates and will eliminate the price cap as a method of regulating postal prices.

The Commission can address the above issues in several ways. First, the Commission can accurately quantify the monetary effects of the recession over the total

[12] The Public Representative views the caveat as another example of the exigent request being due to the Postal Service's liquidity/cash flow problems and not the recession.

span of the recession.[13] This can include an estimate of future effects, if the Commission believes the effects of the recession might continue into the future. The exigency request should then be based on this total amount, and not on just one fiscal year.

Second, the Commission might rely on the passage of time since the onset of the recession, and the negative implications on price cap regulation, to prevent the Postal Service from returning for a second bite at the apple.[14] Otherwise, justifying an exigent request based on one year of a multiyear exigency, and not the full amount associated with that one year, would mark the end of price cap regulation.

Third, the Commission can restate the purpose of exigency funding. For example, the purpose of exigent funding in this case is to sustain the postal network while the Postal Service right-sizes the network to the new normal. The idea is to break the direct link between lost contribution and exigent recovery. Lost contribution becomes only a starting point in determining the amount of recovery. This is discussed in greater detail below.

G. Approaches to Determining Exigent Losses

In principle, an exigency request due to a recession should be analyzed just like an exigency request due to a natural (or manmade) disaster. Two examples will be considered to illustrate this point. For the first example, consider that a major processing facility is destroyed by a tornado. Assume that this causes the Postal Service to reroute mail through adjacent facilities, and that even with rerouting service

[13] Because the Postal Service did not quantify the effect of the recession in this manor, the Public Representative contends the entire Request is deficient.

[14] The Postal Service appears overly concerned with the timing of the filing of its Request. “Considering these facts, there is no basis to find that the passage of time between the onset of the recession or the issuance of Order No. 1059, and the filing of this response, necessitates dismissal of the Postal Service’s Request.” Request at 39. The Public Representative contends the Commission can always consider the passage of time.

standards cannot be met without rebuilding the destroyed facility. The Public Representative would argue that the Postal Service could justify an exigent request based on the "temporary" cost of rerouting the mail around the destroyed facility, plus the "one time" cost of rebuilding the processing facility.

For the second example, consider a bacteriological attack similar to anthrax. The Public Representative would argue that the Postal Service could justify an exigent request based on the "temporary" cost of rerouting the mail around the infected facility, plus the "one time" cost of installing appropriate bacteriological detection and removal equipment.

An exigency due to a recession should be analyzed in the same way. The Public Representative would argue that the Postal Service could justify an exigent request for the "temporary" cost sustaining the postal network because of a decrease in contribution from lost mail volume. The Postal Service could also recover the "one time" cost of right-sizing its network for anticipated future mail volumes.

The "one time" cost of right-sizing the postal network has not been estimated by the Postal Service in this docket, nor has a plan been presented which explains how this would be accomplished. There is no doubt that the costs will be more difficult for the Postal Service to estimate than a comparable private corporation because of its statutory and unionized workforce requirements.

Along with the one-time cost, the Postal Service also would have to estimate how long right-sizing might take. This time is used to determine the duration of the "temporary" component of recovery.

The "temporary" cost of a decrease in contribution from lost mail volume is the other cost that may be recovered. The magnitude of the recovery can be based on an estimate of volume loss over time due to the recession, being careful not to include volume loss from electronic diversion and other unrelated factors. The time limitation to this recovery would be equivalent to the time required to right-size the network.

Assuming that incremental progress is made on right-sizing the network, the total "temporary" cost recovery can be adjusted downward. This is to account for the fact that network capacity will be reduced over time and the Postal Service need not be made whole to pay for network capacity that no longer exists.[15]

During the November 20, 2013 hearing, Mr. Nickerson made obvious that the Postal Service has a different view concerning how it should be made whole. Mr. Nickerson provides an example that if there were a fire in a personal residence that destroyed a house, the owners would feel the effect of the loss long after the house was rebuilt. *See* Tr. 2/223-4. The implication was that the owner would be due further compensation into the future once the house was rebuilt. It was pointed out to Mr. Nickerson that although the owners may feel the effects of the loss (emotionally or otherwise), the owners are typically made whole through the "one time" payment of insurance.[16] Regardless, Mr. Nickerson continues to believe that the Postal Service is always going to be feeling the effects of the recession on volume and revenue, absent something happening to change that. *Id.* at 2/224.

H. Rolling Back Exigent Prices

To solve some of the problems associated with rolling back temporary exigent price increases, the Public Representative proposes that any exigent price increase approved by the Commission be administered as a price surcharge added to the prices approved in Docket No. R2013-10. The approved Docket No. R2013-10 price tables would remain unchanged and not include exigent prices.

A schedule of surcharges would be developed representing any approved exigent price increases (the delta in prices). Most rounding and other price setting

[15] This is the problem with the Postal Service's current estimate of volume loss. The Postal Service would like to continuously be reimbursed to support the size of its network at the beginning of the recession, even though its network currently is much smaller.

[16] The Public Representative through personal experience would note that insurance typically also pays for the "temporary" cost of lodging while the house is being rebuilt.

constraints proposed by the Postal Service in the exigent docket could be observed. The surcharge price table would remain in effect until the Postal Service recoups the fixed contribution the Commission approves due to the exigency.

Any CPI increases approved prior to the expiration of the surcharge would be based on the existing, un-surcharged rates, with surcharges subsequently added. “Banking” authority rules would be applied to un-surcharged rates. Thus, the surcharge schedule could be used in future years to adjust prices to include the exigent surcharge.

IV. THRESS ANALYSIS

A. Introduction

Mr. Thress undertakes an important task in this proceeding. He estimates the mail volume lost due to the Great Recession (excluding the impact mail volume lost due to Internet diversion). The Public Representative concludes that Mr. Thress's econometric assumptions produce volume declines which overstate the impact of exigent circumstances associated with the recession, and do not allow for the separation of volumes losses due to substitution away from Postal Service-delivered mail (*i.e.,* Internet diversion).

Mr. Thress also does not consider the feasibility of including new Internet variable(s) which could be used to measure Internet diversion. This may have produced a better model of the impact of new Internet technologies on mail volume.

B. Assumptions Which Overstate Volume Declines Due to the Recession

1. The Exigent Period of the Most Recent Recession is Over-Stated

The National Bureau of Economic Research (NBER) has determined that the most recent recession began in December 2007 and ended in June 2009. However, Mr. Thress estimates volume losses from calendar year 2008 through calendar year 2013.[17] He admits that the Great Recession was over by the end of 2010, provided one accepts the view that the Great Recession resulted in a reduction in the long run growth rate of mail volume, to what he terms "the new normal."

> There was a major bottoming out in 2008-2009, but that bottom—but we sort of reached the bottom there. And so to some extent I think it's fair to call maybe 2010 through 2013 the new normal for standard mail.

[17] NBER is the entity that provides the official beginning and ending dates of economic recessions.

Tr. 1/199*; see also,* Response to POIR 3, question 6, c.

If it were the case that a new normal was established by calendar year 2010, then exigent volume losses ended six months after the official end of the current recession. This reduces the Postal Service's estimated loss by more than 13 billion pieces.[18]

2. The Hodrick-Prescott Filter Is Not Properly Employed

Mr. Thress applies a Hodrick-Prescott filter (HP filter) to several macroeconomic variables: employment, retail sales, investment, and exports, in order to separate the cyclical from the trend components of these variables. Thress Statement at II-2. The Public Representative maintains that the cyclical component of the HP filter should not be included in the analysis of lost volume. Because the cyclical component of the HP filter represents economic events to which the Postal Service could have responded, its effect should not be considered an exigent event. Thus, volume losses due to the cyclical component should be removed from estimated volume losses.

Mr. Thress is also inconsistent in his choice of macro-economic variables across products. Variables should be consistently measured so that their effect on volume is consistent. For certain products he uses the "raw" or unfiltered macro-economic variable. For other products, he uses both filtered cyclical and trend components. At other times he uses only the filtered trend or the filtered cycle component. He even uses a filtered trend variable along with the raw values of the same trend variable. Finally, similar products are estimated using different measures of a macro-economic

[18] If compensation for volume losses due to exigent circumstances is primarily based on volume losses, then one must limit the recession to an "exigent time period," the period of time before the Postal Service began a concerted operational response to the volume loss. On the other hand, if one adopts the method, outlined earlier, that compensation should be limited to the revenue losses and one-time expenses or investments needed to reorganize operations to fulfill the new level of reduced demand, then the period of exigency would not be limited to losses before the beginning of operational changes.

variable. Table IV-1 illustrates his inconsistent choice of macro-economic variables used to estimate volumes for different products.

Table IV-1
Inconsistent use of Macro-Economic Variables for Different Products

No Variable	Unfiltered Macro Variable	Filtered Trend Variable	Filtered Cyclical Variable
Bound Printed Matter, Media & Library, PO Box, Certified, Return Receipt, Stamped Envelopes Stamped Cards Parcel Return **Delivery Confirmation – Retail** **Signature Confirmation –** Retail Package Services	Standard ECR, **Periodicals,** **Registry,** Standard NonProfit, ECR, Postal Penalty, **Signature Confirmation – Electronic Package Service,** **Signature Confirmation – First Class Electronic First Class,** **Signature Confirmation – Electronic Priority,** **Signature Confirmation,** **International Express,** **Delivery Confirmation,** Insurance International LCF, International Parcel Airlift, ISAL First Class Parcels, Express Parcel Select, MBags	First Class LCF, Money Orders, Priority & Parcel Post, Retail Other	First Class WS_LCF, **Periodicals (-1),** **Registry** Money Orders

* Uses number of Internet servers as a trend variable.
Note: Similar products, whose volume is estimated using different types of macro-economic variables, are grouped by color.

Mr. Thress has not offered a convincing explanation for his inconsistent use of macro variables. He says that “[i]n some cases…demand for some products may react differently to temporary, or cyclical, changes to the economy than it does to more permanent, trend, changes to the economy.” Response to POIR No .1, question 9, a and b. This answer does not respond to the concerns raised by the Public Representative. First, cyclical should be not used. Second, it does not explain why volume equations for some products do not include a macro-economic trend variable (filtered or unfiltered). Last, since only a few products employ macro-economic variables filtered into a trend component, the Public Representative maintains the Hodrick-Prescott procedure has not added value to Mr. Thress's analysis.

It is also possible there is no methodological reason for his choice of macro-economic trend variables. He may have chosen the combination of macro-economic trend variables that produced the best results. If so, this would elevate empirical outcomes over economic or policy reasoning, and would not be appropriate for an exigent proceeding. The Commission must separate which circumstances and which economic methods represent exigent circumstances from those that do not.

3. Intervention Variables are not Properly Employed

Mr. Thress employs intervention variables to model the impact of short term (several years) economic events on volume. He employs intervention variables for several purposes: to measure the change in worksharing relationships, to improve econometric estimates for short-run periods prior to 2008, and to measure loses in mail volume associated with the Great Recession, beginning in calendar year 2008. Mr. Thress explains that his intervention variables are a type of "impulse-response function." Impulse response functions decompose the impact of a shock to the economy into: (1) an initial pulse; (2) a trend, which usually exhibits a wave or cyclical pattern; and (3) a step component which exhibits attenuation and eventual absence of the initial shock.[19, 20]

Impulse response functions are valuable, not simply because they can improve the accuracy of an estimate over time, but also because they break the responses to external shocks, in this case volume losses due to exigent circumstances, into different components. The Public Representative supports separating volume losses into the three components describe above, but maintains that only the initial pulse or shock represents exigent circumstances due to the current recession. During shocks, the Postal Service is feeling the first impact of economic changes, and is not mounting a concerted operationally adaptive response. Volume losses due to shocks should therefore be considered unexpected and due to exigent circumstances.

In contrast, volume losses due to "trend" and "step" parameters, include sustained, operational, changes being made by the Postal Service, such as plant closings and reductions in hours. Because these changes are planned, they are no longer unexpected, and should not be considered losses due to exigent circumstances.

In Table IV-2, the Public Representative removes all values related to the trend, step, and delta in Mr. Thress's intervention analysis for each product between 2008 and 2014. These results capture the volumes lost to circumstances to which to Postal Service did not adjust, and constrains volume losses to exigent circumstances.[21]

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[19] See e.g., The Unit Impulse Response, http://lpsa.swarthmore.edu/Transient/TransInputs/TransImpulseTime.html.

[20] The functional form of Mr. Thress's "trend" component has a quadratic term, as well as cross terms between itself and various lags, and the step term. These features enable this component to flexibly adapt to cyclical-like or wave-like modulations. *See* USPS-R2010-4R/NP3 – Revenue and Volume Forecast Materials (Public Version), Folder Public Econometrics, at the beginning of file "proguts.prg."

[21] This is accomplished by changing these values to zero in USPS-R2010-4R-NP3, File: POIR.6.Q.14.S-O-C.Calcs.xlsx, in worksheet "Elast."

Table IV-2
Volume Losses Estimated by the Public Representative versus Postal Service Estimates Compared to FY 2007 Volume

Public Representative	**FY 2008**	**FY 2009**	**FY 2010**	**FY 2011**	**FY 2012**	**FY 2013**	**FY 2014**
First-Class Mail	(712.9)	(1,472.6)	(2,070.5)	(2,386.0)	(2,454.1)	(2,454.1)	(2,454.1)
Standard Mail	(2,447.0)	(10,905.9)	(10,962.8)	(10,962.8)	(10,962.8)	(10,962.8)	(10,962.8)
Periodicals Mail	(167.2)	(358.1)	(508.9)	(591.9)	(610.7)	(610.7)	(610.7)
Package Services	(0.4)	(3.7)	(3.7)	(3.7)	(3.7)	(3.7)	(3.7)
Total Market Dominant Mail	**(3,327.4)**	**(12,740.4)**	**(13,545.9)**	**(13,944.4)**	**(14,031.4)**	**(14,031.4)**	**(14,031.4)**
Postal Service Revised	**FY 2008**	**FY 2009**	**FY 2010**	**FY 2011**	**FY 2012**	**FY 2013**	**FY 2014**
First-Class Mail	(3,926.9)	(10,037.0)	(15,031.7)	(19,044.0)	(22,590.2)	(25,893.0)	(29,063.9)
Standard Mail	(6,960.2)	(23,928.6)	(25,989.5)	(27,397.0)	(29,121.5)	(30,787.3)	(32,462.2)
Periodicals Mail	(165.3)	(682.4)	(1,161.4)	(1,356.6)	(1,623.0)	(1,876.6)	(2,118.0)
Package Services	(8.7)	(94.3)	(133.3)	(166.3)	(193.9)	(215.8)	(233.6)
Total Market Dominant Mail	**(11,061.1)**	**(34,742.3)**	**(42,315.9)**	**(47,963.9)**	**(53,528.7)**	**(58,772.8)**	**(63,877.6)**

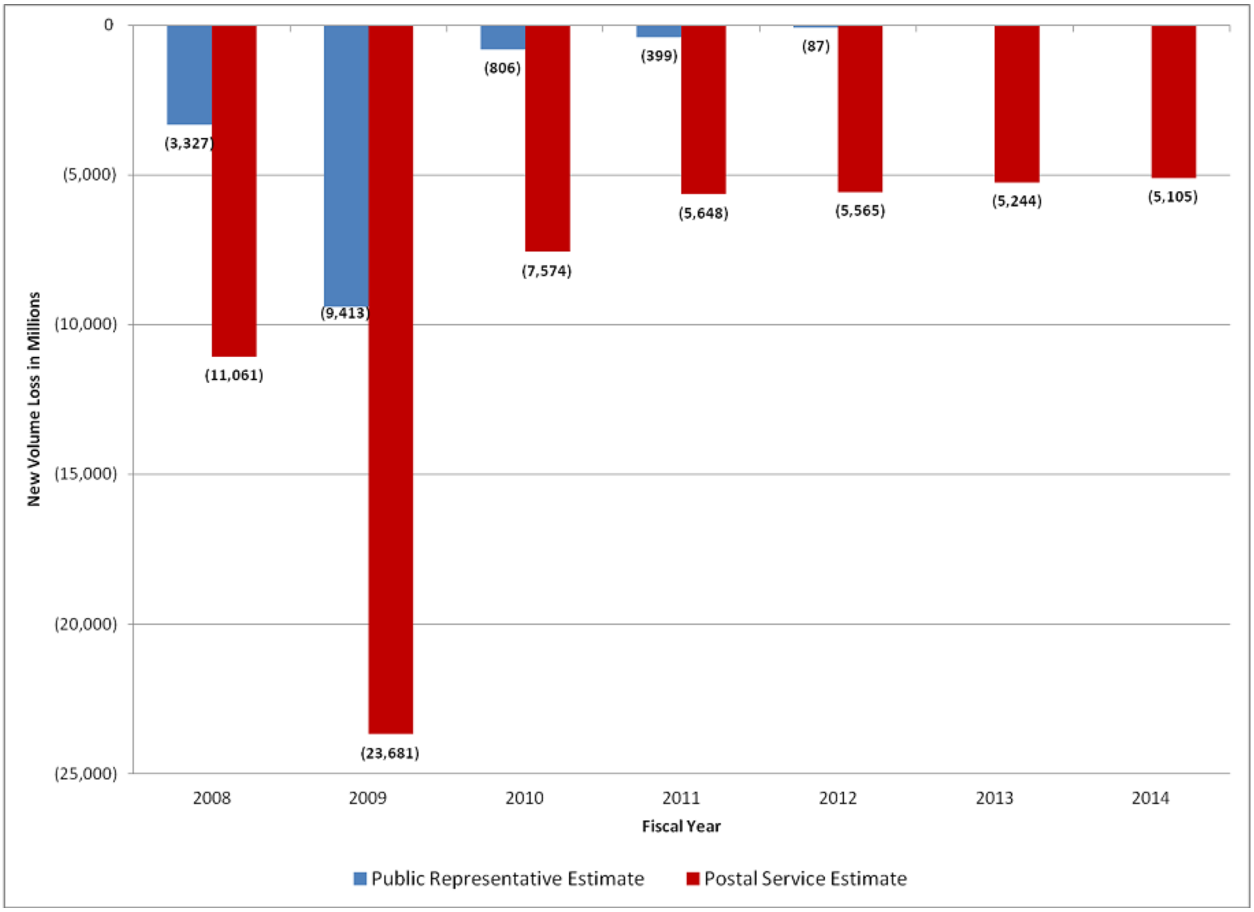
Mr. Thress also combines a variable titled “Qtrs pre-End” with a linear trend variable that begins in the first quarter of 2001.[22] Since the interventions relevant to this case begin in 2008, the Public Representative initialized the trend to the first quarter of 2008, and made all trend values prior to 2008 equal to zero. Otherwise, this linear trend would include volume losses prior to the current recession. Table IV-2 shows the PR’s estimate of exigent volume losses are approximately one-half of those estimated by the Postal Service each year.[23]

[22] *See* Response to POIR No. 6, question 14, spreadsheet entitled “POIR.6.Q.14.S-O-C.Calcs.xlsx,” worksheet “Intervention,”

[23] The Public Representative’s modifications include: removing HP Trend values, removing - step, delta, and trend – values from the intervention variable, and reinitializing the trend pertaining to the variable Qtrs pre-End to begin in 2008. The Public Representative recognizes that the volumes obtained in this manner are approximations. The correct method would rerun Mr. Thress’s programs with the correct values and variables, and methods. The volume losses presented by the Public Representative should be considered lower bound estimates.

The Public Representative estimates that by 2013 no new volume is lost due to the Great Recession. However, the Postal Service estimates that roughly 5 billion new pieces of mail will be lost in FY 2013 and FY 2014 due to the Great Recession. *See* Figure IV-1.

Figure IV-1
Public Representative Versus Postal Service Estimates of New Annual Mail Volume Lost Due to Recession by Fiscal Year



C. A Proper Analysis of Diversion Requires Explicit Measurement of Internet Diversion

Measurement of mobile technology and the rise of Internet-based payment methods are two variables that should have been included in Mr. Thress's analysis. Neither would be measured by the number of households accessing the Internet, which Mr. Thress states has reached the tail of the S-curve. Tr. 1/88.

Mr. Thress subsumes the Internet diversion of mail to any loss of mail during the current recession because he believes Internet-specific variables do not fully measure the loss of mail during the recent recession.

> the broadband variable itself no longer works as an explanatory variable to explain continuing downward trends because the variable's not trending anymore. So we changed our methodology and we went with this same intervention analysis approach. The idea is we introduce trends into our equation when basically the model suggests trends have emerged, and if these trends change over time we introduce new trends to allow them to change over time.

Id. at 89.

> I think, a trend variable is going to pick up anything that trends. It's going to pick up macroeconomic trends, demographic trends, diversion trends. And so it becomes difficult to pull out and say this trend was because of this one specific factor because what it is, it's a combination of all factors, some of which preexisted, and we have the preexisting trends, which we have now taken out.

Id. at 91.

Mr. Thress comes to the conclusion that Internet diversion does not fully capture volume losses during the recession because he limits the measurement of the Internet to the number of households with broadband Internet access.[24] However, he also

[24] "To the extent that—what a smart phone does is it enables us to access the internet in a slightly different way. For 70 percent of mail, of people, they already had that *access* to the internet." Tr. 1/93.

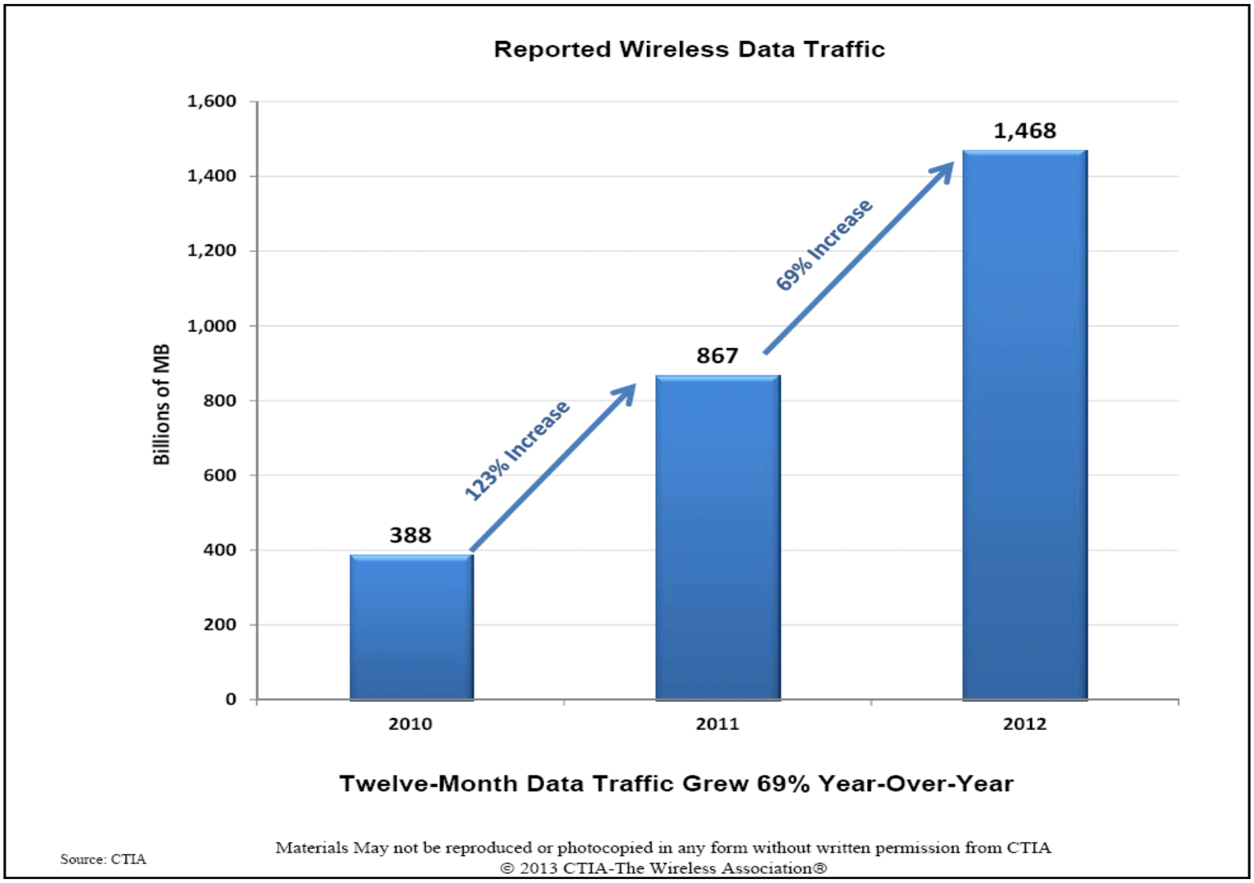
admits that he did not attempt to devise any other measure of Internet diversion. Response to POIR No. 6, question 4, b.

Measures other than the number of households with access to the Internet, such as amount and type of Internet usage should have been explored. For example, the Cellular Telecommunications Industry Association (CTIA) publishes a semi-annual report on various aspects of the cellular telecommunications industry.[25] The Executive Summary offers a glimpse at some of the data that might be used. For example, wireless broadband data traffic grew at impressive rates between 2010 – 2012, as shown in Figure IV-2.[26]

[25] Background on CTIA's Semi-Annual Wireless Industry Survey, http://www.ctia.org/advocacy/research/index.cfm/AID/10316, then click "CTIA Semi-Annual Wireless Industry Survey."

[26] Only the Executive Summary is available, and the entire copy, with all of its data, costs over $1,000, well out of the Public Representative's Budget for this case. It is possible the full report has a longer data series on wireless data traffic. Other data sources might capture Internet usage (rather than access), such as broadband capacity and average throughput per second by year.

Figure IV-2
Annual Percentage Growth in Wireless Data Traffic



In addition, he doesn't discuss data on Internet-based payment methods that do not involve payment by credit card. Such payments might be authorized as electronic transfers from a person's bank account. Paypal is the leading company in this area, and continues to expand its business. Online payments are large, growing, and hold the potential to divert a large volume of mail.[27] Table IV-3 presents relevant data about Paypal.

[27] Mr. Thress criticizes alternate measures of Internet diversion, such as the smartphone, because they are only able to divert a very small amount of mail. Tr. 1/96-97. But Paypal processes a very large number of non-mail transactions.

Table IV-3
Paypal is a Major Player in E-Commerce and On-line Bill Paying

Total amount of PayPal payments made everyday	$315.3 million
Total percentage of Ecommerce that is represented by PayPal	18%
Annual amount of payments made by PayPal mobile phone users	$1 billion
Number of Internet sites that use PayPal	341,497
Total revenue made by PayPal in 2010	$3.4 billion
Total amount of payments processed by PayPal in 2010	$56 billion

Source: http://www.statisticbrain.com/paypal-statistics/

Paypal is but one of a growing number of companies that are developing payment methods using smartphones as an alternative to point of sale charges paid by credit cards.[28] Google wallet, companies using near field communications (NFC), companies that are paid by charging your wireless account, and bill payment by text message authorizing an electronic transfer from one's bank account, are about to challenge the credit card industry.[29]

Measures of Internet usage, such as wireless data traffic and Internet payments, promise to provide data showing substantial annual growth that will allow one to estimate the diversion of mail by the Internet. The Postal Service and the Commission should investigate the feasibility of obtaining Internet data that can be used for econometric estimation. Only by explicitly measuring the rise of mobile technologies and payments made over the Internet is it possible to identify a growing source of Internet diversion.

[28] These types of online payment alternatives, reside solely online and do not involve credit card billing. Therefore they will reduce the mailing of billing statements, although Google wallet offers a credit card option as well as an electronic transfer option.

[29] "Forget Your Wallet," Bloomberg BusinessWeek, By Brad Stone, November 14, 2013; http://www.businessweek.com/articles/2013-11-14/2014-outlook-easy-mobile-payments-in-reach.

V. TREATMENT OF UNUSED RATE ADJUSTMENT AUTHORITY

A. Introduction

The Code of Federal Regulations, 39 CFR § 3010.63, address the treatment of unused rate adjustment authority.

(a) Each exigent request will identify the unused rate adjustment authority available as of the date of the request for each class of mail and the available amount for each of the preceding 5 years.

(b) Pursuant to an exigent request, rate adjustments may use existing unused rate adjustment authority in amounts greater than the limitation described in §3010.28 of this subpart.

(c) Exigent increases will exhaust all unused rate adjustment authority for each class of mail before imposing additional rate adjustments in excess of the maximum rate adjustment for any class of mail.

39 CFR § 3010.63. The comments that follow are intended to guide the Commission in its treatment of unused rate adjustment authority.

B. Postal Service Proposal

39 CFR § 3010.63(a). The Postal Service has identified the unused rate adjustment authority available as of the date of the request for each class of mail and the available amount for each of the preceding 5 years. This is replicated in Table V-1.

Table V-1
Available Unused Rate Adjustment

Class	Unused Authority (%)
First-Class Mail	-0.466
Standard Mail	-0.354
Periodicals	-0.524
Package Services	-0.312
Special Services	+1.814

Request at 37, Table 3.

39 CFR § 3010.63(b). With the unused rate adjustment authority for each class being less than 2 percent, the waiver of the limit specified in 39 CFR § 3010.28, that unused rate adjustment authority used to make a Type 1-B rate adjustment for any class in any 12-month period may not exceed 2 percentage points, is not applicable in this docket.

39 CFR § 3010.63(c). The Postal Service presents two alternatives to address the requirement to exhaust all unused rate adjustment authority for each class of mail. Its preferred approach is for the Commission to only exhaust unused rate adjustment authority that was initially generated prior to June 2010, when it filed its first exigent request (Docket No. R2010-4). Request at 36-37. Alternatively, the Postal Service proposes to exhaust all current unused rate adjustment authority, including any unused rate adjustment authority generated as a result of the recent CPI-U price adjustment (Docket No. R2013-10). *Id.* The Postal Service notes that it would not object to either approach. *Id.* at 38.

C. Application of Unused Rate Adjustment Authority Rules

The second approach offered by the Postal Service, which zeros out all currently unused pricing authority, is the only approach consistent with 39 CFR § 3010.63(c).[30] The intent of 39 CFR § 3010.63(c) is to wipe the slate clean as a result of an exigent request. This promotes predictability and stability in rates following the approval of an exigent request. Mailers should not first be subject to an exigent price increase then be subject to annual price adjustments that are greater than inflation due to the preservation of a certain portion of unused rate adjustment authority.

[30] Also note that the Commission docketed the Postal Service's instant Request as a separate proceeding from Docket No. R2010-4.

The Postal Service's first proposal preserves the amounts of unused rate adjustment authority that was generated after July 2010 for each market dominant class of mail as shown in Table V-2.

Table V-2
Unused Rate Adjustment Authority Generated After July 2010

Class	Docket No. R2011-2 (%)	Docket No. R2012-3 (%)	Docket No. R2013-1 (%)	Docket No. R2013-7 (%)
First-Class Mail	0.003	0.000	0.000	NA
Standard Mail	0.000	0.092	0.021	NA
Periodicals	0.000	0.000	0.001	NA
Package Services	0.001	0.018	0.003	NA
Special Services	0.002	2.114	0.000	1.564

Unused rate adjustment authority for Docket No. R2013-10 has not been finalized.

Allowing the Postal Service to pick and choose what unused rate adjustment authority it wishes to preserve, and what unused rate adjustment authority it wishes to exhaust, is contrary to 39 CFR § 3010.63(c). The Postal Service's preferred approach, to exhaust the negative unused rate adjustment authority generated due to deflation that occurred prior to July 2010, is self-serving. If that rate adjustment authority had been positive, the Postal Service would have likely argued that because the positive authority was calculated after the conclusion of Docket No. R2010-4, it should be preserved.

Assuming that the Commission approves the instant exigent Request, the unused rate adjustment authority for each class of mail will be as shown in Table V-3.

Table V-3
Remaining Unused Rate Adjustment

Class	Unused Authority (%)
First-Class Mail	0.000
Standard Mail	0.000
Periodicals	0.000
Package Services	0.000
Special Services	0.000

VI. RATE ANALYSIS

A. Introduction

The Code of Federal Regulations, 39 CFR § 3010.65(f)(3), permits comments that address "[w]hether the specific rate adjustments requested are reasonable and equitable." The comments that follow are intended to aid the Commission in its statutory task of determining whether a proposed exigent rate adjustment is "reasonable and equitable" such that the adjustment enables "the Postal Service, under best practices of honest, efficient, and economical management, to maintain and continue the development of postal services of the kind and quality adapted to the needs of the United States." *See* 39 U.S.C. § 3622(d)(1)(E).

The comments are provided assuming that the Commission determines that the Postal Service has adequately justified its exigent request based on either extraordinary or exceptional circumstances, and that the magnitude of the proposed adjustment is both adequate and "necessary."

For products that do not cover costs, the Public Representative does not believe it is fair or equitable to subject certain mailers to exigent price increases, while having these same mailers continue to subsidize mailers that utilize products that do not cover costs year-after-year. Furthermore, offering products that do not cover costs does not help the Postal Service's bottom line. It is not indicative of efficient management to fail to take steps to correct such problems when presented with the opportunity to do so, especially in an organization with a history of financial difficulties.

For worksharing discounts that deviate significantly from 100 percent, the Public Representative does not believe it is prudent to offer inefficient worksharing discounts that do not sent appropriate pricing signals. Given the instant opportunity to make corrections, allowing the problem to continue is not indicative of a management concerned with maximizing the Postal Service's financial position.

The Public Representative concludes that except for certain prices that do not cover costs and prices that fail to correct inefficient workshare discounts, the Postal Service proposes prices that are reasonable and equitable.

B. Postal Service Proposed Price Increases

The Postal Service proposes a uniform 4.3 percent price increases across all market dominant products and classes in its exigent request. Taufique Statement at 6. The proposed market dominant price increases are forecasted to provide the Postal Service an additional $1.78 billion in contribution in FY 2014. The additional contribution generated by the exigent request and the distribution across classes is shown in Table VI-1.

Table VI-1
Projected Additional Contribution
Generated From Exigent Rate Adjustment by Class

	Before Rates Contribution ($ millions)	**After (CPI) Rates Contribution ($ millions)**	**After (CPI+Exi) Rates Contribution ($ millions)**	**Difference ($ millions)**	**Additional Exigent Contribution Distribution (%)**
	(1)	(2)	(3)	(4)=(3)-(2)	(5)= (4)/Sum(4)
First-Class Mail	15,464	15,771	16,743	972	54.6
Standard Mail	6,901	7,088	7,712	624	35.0
Periodicals	(454)	(432)	(365)	67	3.8
Package Services	81	92	124	32	1.8
Special Services	462	506	583	77	4.3
International	(162)	(158)	(149)	9	0.5
Total	22,291	22,868	24,649	1,781	100

Source: Nickerson Statement, Attachments 14, 28.

C. First-Class Mail

The Public Representative provides a brief analysis of the proposed prices for First-Class Mail, as they are the prices most applicable to the general public and also generate the majority of new contribution from this Request.

The Postal Service proposes a 2-cent (4.3 percent) increase for single-piece letters. As shown in Table VI-2, the Postal Service estimates that single-piece letters and cards increase will increase contributions by approximately $396 million in FY 2014. The remaining portion of First-Class Mail will provide $581 million in additional contribution.

Table VI-2
Projected Additional Revenue
Generated From Exigent Rate Adjustment
for First-Class Mail by Product

	After Rates (CPI) FY 2014 Contribution ($ millions)	**After Rates (CPI and Exi) FY 2014 Contribution ($ millions)**	**Difference ($ millions)**	**Additional Contribution Distribution (%)**
	(1)	(2)	(3)=(2)-(1)	(4)= (3)/Sum(3)
Single-Piece Letters and Cards	4,545	4,941	396	23.1
Presort Letters and Cards	10,040	10,494	454	23.3
Flats	924	1,027	103	6.0
Parcels	108	132	24	1.4
Total for First-Class Mail	15,617	16,594	977	54.6
Total for all Classes	22,623	24,272	1,718	100

Source: Derived from Nickerson Statement, Attachments 12, 24 and 26.

The Public Representative reviewed the Commission's public commenter file. While most of the comments object to the price increases in favor of the Postal Service cutting costs and right-sizing its business, some commenters suggested that the First-Class single-piece stamp price should be raised further to $0.50.

Other than minor trepidation about any price increase, there is little evidence that the exigent increase will harm retail single-piece mailers and presumably will be absorbed by the general public without much objection. The rate increases that will be experienced by single-piece users are proportional to the rate increases that will be experienced by business mailers. Thus, the rate increases proposed by the Postal Service for First-Class Mail appear reasonable and equitable.

D. Products that do not Cover Costs

There are mailpieces in the system entered at prices that are too low to cover costs. Over the long term, this is not a good business practice. This also is not reasonable or equitable to rate payers who subsidize the underwater products.

The Postal Service's FY 2014 After Rates projections show that five domestic products will continue to fail to recover attributable costs. The Postal Service has proposed price increases that are very close to the average for all five of these products.[31] *See* Table VI-3.

[31] Standard Mail Flats is receiving an above average increase within the Standard Mail class, however, when compared to overall 4.271 percent price increase, Standard Mail Flats is receiving a below average increase (4.259 percent).

Table VI-3
Cost Coverages and Percentage Increases
For Products that are Not Estimated to Cover Costs in FY 2014

	FY 2012 Cost Coverage (%)	FY 2013 Estimated Cost Coverage (%)	FY 2014 AR Estimated Cost Coverage (CPI+Exi) (%)	R2013-11 Proposed Percentage Increase (%)
Standard Mail Flats	80.9	87.0	93.8	4.259
Standard Mail Parcels	85.5	93.1	99.2	4.283
Periodicals In County	70.5	75.7	80.2	4.087
Periodicals Outside County	72.1	76.7	82.1	4.095
Media and Library Mail	85.3	90.9	96.1	4.305

Sources: 2012 ACD, Nickerson Statement Attachments 23 and 26, and Taufique Statement at 9.

The Postal Service is requesting a relatively small exigent increase for these products compared with their annual contribution loss. Only $200 million of additional exigent contribution is expected to come from the seven domestic market dominant products that failed to cover attributable costs in FY 2012.[32] *See* Table VI-4.

[32] The seven domestic products that failed to cover attributable costs in FY 2010 are: Standard Mail Flats, Standard Mail Parcels, Periodicals Within County, Periodicals Outside County, Parcel Post, Media Mail/Library Mail, and Stamp Fulfillment Services. *See* 2012 ACD at 31.

Table VI-4
Projected Additional FY 2014 Contribution
Generated From FY 2012 Underwater Products[33]

	Before Rates Contribution ($ millions)	After (CPI) Rates Contribution ($ millions)	After (CPI+Exi) Rates Contribution ($ millions)	Difference ($ millions)
	(1)	(2)	(3)	(4)=(3)-(2)
First-Class Parcels*	72	108	132	24
Standard Mail Flats	-274	-239	-148	91
Standard Mail Parcels	-5	-3	-1	3
Periodicals In County	-20	-19	-17	2
Periodicals Outside County	-444	-421	-353	68
Parcel Post*	37	38	38	0
Media and Library Mail	-30	-24	-12	12
Total	-663	-561	-361	200
*Portions of First-Class Parcels and Parcel Post were transferred to Competitive in FY 2013.				

Source: Nickerson Statement, Attachments 12, 24 and 26.

Mr. Taufique explains that the Postal Service attempted to address specific cost coverage in the concurrently filed market dominant price adjustment docket, which had an annual limitation of 1.696 percent. *See* Docket No. R2013-10 (market dominant price adjustment docket); Taufique Statement at 4-8. In its exigent request, the Postal Service has proposed to give an across the board price increase for all products regardless of cost coverage. *Id.* at 6.

The Public Representative contends that a uniform price increase is reasonable and equitable in most circumstances. However, where products continuously do not cover costs and the Postal Service is presented with the opportunity to correct the problem, the Postal Service should exercise its pricing flexibility to improve cost

[33] Stamp Fulfillment Services did not cover costs in FY 2012, however Mr. Nickerson does not estimate this product's FY 2014 cost coverage.

coverages. Giving unprofitable products larger than average price increases is reasonable and equitable approach that is necessary at a time when the Postal Service is in financial trouble.

The Public Representative recommends that if the Commission approves the Postal Service's Request, it should adjust the proposed prices to ensure that unprofitable products receive larger price increases than profitable products. This approach will mitigate price increases for profitable products, and help to ensure the Postal Service keep as many profitable mail pieces as possible in the mailstream.

Standard Mail Flats. Under the Commission's direction, the Postal Service has given Standard Mail Flats slightly above average price increases in Docket Nos. R2013-1 and R2013-10.[34] The Postal Service should have taken advantage of the opportunity of the exigent request to give Standard Mail Flats an even greater price increase than other profitable Standard Mail products to accelerate its path toward a greater than 100 percent cost coverage.

The Postal Service only estimates the unit attributable cost of Standard Mail Flats will decrease 0.5 percent from FY 2013 to FY 2014 ($0.441 to $0.439). Nickerson Statement at Attachments 9 and 26. If the Postal Service had a solid strategy to reduce the attributable costs of Standard Mail Flats, it may be reasonable not to give Standard Mail Flats a larger than average price increase. However, as shown in Mr. Nickerson's Attachments, cost savings for Flats are not planned, therefore a larger price increase is warranted. The Public Representative recommends that the price increase for Standard Mail Flats be (at a minimum) 1.05 times the overall proposed price increase of 4.3 percent.

Periodicals. Both products in Periodicals do not cover costs and are not projected to cover costs in FY 2014. In its annual CPI price adjustments, the Postal Service has limited flexibility to fix the cost coverage problems within the class because

[34] The Docket No. R2013-1 Standard Mail Flats price increase was 1.05 x CPI-U, and the proposed price increase for Standard Mail Flats in Docket No. R2013-10 was 1.067 x CPI-U.

both products within the class do not cover costs. An exigent price increase provides an appropriate opportunity to give Periodicals products a price increase that is greater than other market dominant products.

The Postal Service misses this opportunity. Currently, other market dominant classes are subsidizing the Periodicals class. The Postal Service has proposed below average price increases for both In County and Outside County Periodicals (4.095 percent and 4.087 percent) compared to other market dominant products. Taufique Statement at 9. The Postal Service estimates that the unit attributable costs for Periodicals remain constant between FY 2013 and FY 2014 at $0.339. *See* Nickerson Statement, Attachments 9 and 26.

In light of the projected stagnant costs, and limited pricing flexibility in annual CPI price adjustments, the Postal Service should have taken this opportunity to give Periodicals an above average increase in order to improve its cost coverage. If the Commission approves the Request, it should require larger price increases for Periodicals to reduce its subsidization by other market dominant classes.

E. Workshare Discounts

There are 32 workshare discounts that exceed avoided costs. Taufique Statement Attachment A. For many of these discounts, the Postal Service has consistently stated its intention to decrease discounts over time. *See e.g.,* Docket No. R2013-1, Notice of Market Dominant Rate Adjustment at 41-43, 45-49, and 55. The Postal Service has decided to not continue the practice of reducing excessive discounts in its exigent request.

This Request gives the Postal Service the additional pricing flexibility it needs to correct inefficient worksharing discounts. The postal Service must send appropriate pricing signals to further an efficient postal system. If the Commission approves the Request, it should first adjust inefficient worksharing discounts to send appropriate price signals.

VII. CONCLUSION

The Public Representative concludes that the Postal Service has not adequately justified its exigent Request, and until such time that adequate justification can be provided, the Request should be denied. The Postal Service has yet to calculate the total effect of the recession on its finances. It cannot predict an end to the recessionary effects. It has provided no plan for adjusting its network to the new normal.

Similar to pre-PAEA cost-of-service price increases, the proposed exigent prices effectively would become a permanent part of the price base. This is not the intent of the exigency statute.

Approving the Request, as is, would set a precedent allowing the Postal Service to continuously file requests based on the same recession. This will effectively nullify price cap regulation.

If the Request is approved, the prices generally appear reasonable and equitable. However, the Postal Service has not adequately adjusted prices for products that do not cover costs, or adjusted certain worksharing discounts to send appropriate pricing signals.

The Public Representative respectfully submits the foregoing comments for the Commission’s consideration.

Respectfully submitted,

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