

BEFORE THE
POSTAL REGULATORY COMMISSION
WASHINGTON, DC 20268-0001

PHI ACQUISITIONS NSA

Docket No. MC2014-21

PHI ACQUISITIONS NSA

Docket No. R2014-6

**RESPONSE OF PHI ACQUISITIONS, INC. TO
CHAIRMAN'S INFORMATION REQUEST NO. 4**
(May 2, 2014)

PHI Acquisitions, Inc. ("PHI") hereby provides its response to Chairman's Information Request (CHIR) No. 4, Question 1.f., issued April 30, 2014 and referred to PHI by the United States Postal Service on May 2, 2014. The question is reprinted verbatim and is followed by PHI's response.

Respectfully submitted,
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1. Please refer to ExigencyAdj_CHIR3Q3.xls. Workbook tab “Exigent Impact Calculation” Cell B53 contains PHI eligible volume for the period FY 2013 Quarter 2 to FY 2014 Quarter 1. The PHI eligible volume for FY 2014 Quarter 1 can be calculated by subtracting the PHI eligible volume for FY 2013 Quarter 2, Quarter 3, and Quarter 4, located in workbook tab “Summary of Steps” Cells C19 through C21, from the total PHI eligible volume located in workbook tab “Exigent Impact Calculation” Cell B53.
 - a. Please confirm that the PHI eligible volume for FY 2014 Quarter 1 is 71 million. If not confirmed, please explain.
 - b. Please confirm that the PHI eligible volume for FY 2014 Quarter 1 represents a 33 percent increase compared with FY 2013 Quarter 1. If not confirmed, please explain.
 - c. Please confirm that a similar increase in PHI eligible volume for the remaining three quarters of FY 2014 would result in a volume that far exceeds both the before rates and the after rates volume projections for Year 1 of the NSA. If not confirmed, please explain.
 - d. Please refer to PHI_NSA_Financials_FINAL_Exigent.xls, workbook tab “1_Inputs” Cell G174. Please confirm that the Postal Service projected volume for FY 2014 represents a volume decrease from FY 2013. If not confirmed, please explain.
 - e. Please confirm that PHI would have to significantly reduce its volume in the last three quarters of FY 2014 in order for FY 2014 PHI eligible volume to match the Postal Service’s volume projection for PHI eligible volume in FY 2014. If not confirmed, please explain.
 - f. Please explain the cause or causes of the 33 percent increase in FY 2014 Quarter 1 volume over FY 2013 Quarter 1, and discuss whether this deviation from previous quarterly volume trends necessitates a revision of

the Postal Service's volume forecast. Please provide a revised volume forecast if necessary.

RESPONSE:

a-e. See Responses of the United States Postal Service filed May 2, 2014.

f. No revisions to the Postal Service's volume forecast are necessary.

The questions above seek to compare the volumes of Eligible Mail entered by PHI in Quarter 1 of FY 2013 (the first quarter of the Year One Baseline volume set forth at Section III.B.1 of the NSA) with the volumes of Eligible Mail entered by PHI in Quarter 1 of FY 2014 (October-December 2013) and to extrapolate volume projections for the remainder of FY 2014 based on this comparison. Although as a numerical matter, the computations set forth in parts (a) through (e) of the question are correct, the comparison oversimplifies and misapprehends PHI's actual mailing practices and the resultant attempt to extrapolate from the comparison produces results that are nonsensical and incorrect.

First, the questions fail to recognize that, as a part of its normal business practices, the dates on which PHI enters mail volume periodically change to account for calendar date drift. That is, at the outset of each year, PHI establishes a "nominal" regular mailing schedule on Monday of each campaign which allows planned direct entry to the Postal Service over several days beginning before and ending after the nominal mail date. Because of calendar date drift, the "nominal" Monday mailing dates get 1 day earlier every year (2 days in leap years), and PHI periodically resets its mailing plan by shifting all nominal mailing dates later by one week to account for this date drift to maintain targeted mail delivery before Christmas. This change then impacts

the entire year to maintain optimal cadence between mail events. The decision to do this mail schedule reset in 2013 was made during the annual planning process in early December 2012, and mail dates started to shift later by a week in early January 2013 and continued to do so throughout calendar 2013. PHI's largest mailing events are "holiday" mailings which occur in September and October; shifts of mailing dates in these months toward the end of September can result in mail being moved from one quarter to another. This is exactly what happened in FY 2014—mailings which were entered in Q4 of FY 2012 (*i.e.*, September 2012), instead of being entered in Q4 of FY 2013, were entered in Q1 of FY 2014 (*i.e.*, in October 2013 instead of September 2013). PHI has calculated that 12.1 million pieces of the 17.8 million piece "increase" purportedly identified in parts (a) and (b) of the question shifted from Q4 of FY 2013 to Q1 of FY 2014. Further, an additional 1.9 million pieces were shifted from January 2014 to December 2013 (*i.e.* from Q2 of FY 2014 to Q1 of FY 2014) in order to obtain an earlier in home date for delivery of these January sales catalogs. Because the questions ignore these operational changes, the purported comparison is invalid; the attempt to extrapolate from an invalid comparison produces results that are equally invalid.

Other shifts occurred which further distort the quarter-to-quarter comparison. Late in 2012, PHI conducted a review of its Add-A-Name ("AAN") processing, which is an analysis by which PHI evaluates the potential return on a mailing to determine how many "holes" in a High Density or Carrier Route mailing can be filled with incremental names. PHI found that it was able to increase the number of High Density "holes" that could be filled to complete a High Density Bundle due to an improvement in the

available AAN Pool performance. The “before AAN” pieces would otherwise have been mailed at the Carrier Route Rate; the AAN process allowed these pieces to move to High Density with the addition of incremental names to complete each High Density Bundle. The resulting complete High Density bundles result in existing eligible Carrier Route mail that is now High Density and additional incremental High Density volume added to complete the High Density bundle. PHI has computed that the Add-A-Name refinements resulted in an increase of 3.5 million pieces of Eligible Mail volume in Q1 FY 2014 over Q1 FY2013. While this unquestionably increased the amount of Eligible Mail, the addition of this volume also increased the contribution earned by the Postal Service because the unit per piece contribution of High Density mail is greater than the per-piece contribution of Basic Carrier Route, and the added 3.5 million names were all High Density.

In addition, completion of the integration into the PHI mail streams of PHI’s most recently acquired title further increased the quantity of Eligible Mail in Q1 of FY 2014 by 0.3 million pieces.

Failure to take account of these and similar shifts as well as seasonal and other volume fluctuations makes the comparisons embodied in parts (a) through (e) of this question inaccurate and the resultant extrapolations set forth in the remaining parts of the questions meaningless.

The following table shows the effects of these business related decisions on the volume of eligible mail actually entered:

Cause:	Eligible Mail Quantity:
Mail Entry dates shift from September 2013 into October 2014	12.1 million moved out of September into October
Increased AAN in Q1 FY 2014	3.5 million incremental pieces
Mail Entry dates shift from January 2014 into December 2013	1.9 million pieces moved out of January into December
Integration of latest acquisition with improved sort	0.3 million incremental pieces in Q1 FY 2014
Total:	17.8 million

Second, the questions fail to account for regulatory lag in the NSA approval process. Under the PRC's customary practice, the Baseline Quarters are to be the most recent four complete quarters before approval of the filing by the Postal Service Board of Governors. The Postal Service approval process does not occur overnight: the NSA in *final form* must first be submitted to the Postal Service's Executive Committee and thereafter must be placed on the Board's docket for consideration. Completion of the final Agreement (including imperatively the determination of the volumes for the most recent four fiscal quarters) occurred in November 2013. Thus the four quarters selected for the computation of the Year One Baseline were the most recent complete four quarters available at the time the NSA was finalized. Board authorization to file the NSA and execution of the Agreement did not occur until January 7. Given this time table, it was not possible to use a different set of quarters to compute the Year One Baseline.

Third, PHI has made a comparison of Eligible Mail volume actually presented to the Postal Service in Q2 of FY 2013 and Q2 of FY 2014. This comparison is set forth in

the table below. It shows an increase in Eligible Mail volume of 6.6% and an increase of only 1.8% in total volume, significantly less than the 33% increase between Q1 of FY 2013 and Q1 of FY 2014.

PHI Total and Eligible Mail Quantity in USPS Q2 2013 vs 2014						
	2013		2014		Y-Y Increase	
	Total Mail Qty	Eligible Mail Qty	Total Mail Qty	Eligible Qty	Total Mail Qty	Eligible Qty
USPS FYQ2	42,298,208	39,458,351	43,058,014	42,057,699	1.8%	6.6%

The table also demonstrates that the use of quarter-to-quarter comparisons is an unsound and inappropriate means of assessing the reliability of the discount structure of this NSA. On its face, 6.6% is within the acceptable range of forecast error but in fact overstates the volume increase: PHI shifted volume originally intended to be mailed in early April 2014 to late March; but for this shift, the Quarterly comparison would have shown an increase in Eligible Mail of 3.8%, well below normal forecast error expectations.

Fourth, all the volumes mailed in Q1 of FY 2014 are pre-exigent rate increase volumes. The exigent rate increase was not approved until December 24, 2013, meaning these volumes were determined before an exigent increase became certain. Moreover, as PHI explained in its Reply Comments, PHI has limited ability to immediately cut circulation in response to the exigent price increase. It is therefore meaningless to extrapolate volumes for the life of the NSA from one quarter of pre-

exigency prices when subsequent quarters will be planned and mailed with exigent rates in effect.

In sum, absolute precision in forecasting is impossible; some forecast error is unavoidable. The attempt to use a limited and unusual quarter-to-quarter comparison to test the reliability of the longer-range forecasts is unsound. Therefore, PHI concurs with the Postal Service's conclusion that there is no need to revise the Postal Service's volume forecasts, which were made with the best information available at the time the NSA was negotiated and provide a reasonable estimate of PHI's future behavior. So long as the NSA has in place a mechanism to adjust Threshold levels based on actual year over year results, as this NSA plainly does, and the baseline volumes are based on the most recent available actual results at the time of the agreement, as they are here, there is every reason to conclude that this NSA will increase Postal Service revenues and contributions.