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Introduction

- Role of the Commission
- Recent Regulatory Activity
- Regulatory Issues Ahead
- Challenges in Current Environment, Reform
- Closing

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Role of the Commission

The Commission fulfills three key roles

- Ensure the Postal Service complies with the law
- Provides transparency and accountability of the Postal Service
- Advise the Service on changes in service that are at least substantially nationwide in effect

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On March 28 the Commission issued its Annual Compliance Determination (ACD) discussing:

- Overall financial condition of the Postal Service
- Standard flats cost coverage/pricing
- Non-profit worksharing discounts
- Periodicals costing and service issues
- First-Class Mail elasticity and pricing

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Recent Regulatory Activity - ACD

Financial Performance

- $15.9 billion loss in FY 2012
  - $11.1 billion Retiree Health Benefit Fund expense
  - $2.4 billion Workers’ Compensation Liability expense
  - $2.4 billion Loss Under Management Control

- Sixteen workshare discounts exceeded costs
  - Directed to improve or explain in next rate adjustment

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Recent Regulatory Activity – ACD

Findings - Standard Flats

- In 2010 the Commission found that the prices in effect for Standard Mail Flats in FY 2010 did not comply with 39 U.S.C. 101(d)
  - Finding predicated on a series of previous regulatory concerns expressed in ACDs and annual rate adjustments
  - There was a significant (and growing) cost coverage shortfall that persisted over a significant period, there was evidence that the shortfall was likely to increase further, and the Postal Service had failed to address the shortfall or take remedial steps
- Culminated in a direction to the Postal Service to increase Standard Mail Flats cost coverage through a combination of above-average price adjustments and cost reductions

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Recent Regulatory Activity – ACD

Findings - Standard Flats

- Standard Mail Flats Cost Coverage and Losses

<table>
<thead>
<tr>
<th>FY</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
<th>2012</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cost Coverage</td>
<td>94.4%</td>
<td>82.4%</td>
<td>81.8%</td>
<td>79.5%</td>
<td>80.7%</td>
</tr>
</tbody>
</table>

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Recent Regulatory Activity – ACD

Findings - Standard Flats

- FY 2012 Std Mail Volume & Contribution ($5.341b)

- Total Contribution = $5,341m

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Recent Regulatory Activity – ACD

Findings - Standard Flats

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Recent Regulatory Activity – ACD

Findings - Standard Flats

- Postal Service began making progress on Standard Mail Flats’ cost coverage
- No changes to the directive in the FY 2010 ACD are necessary
- Postal Service should continue with its three-year plan of cost reductions and rate increases

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Recent Regulatory Activity - ACD

Findings - Non-profit

- Non-profit workshare discounts in the FY 2012 ACD
  - Comments received from the Alliance of Nonprofit Mailers concerning differential between regular worksharing and nonprofit worksharing discounts
  - The Commission found that the discounts varied (in FY 2012) without explanation or justification from the Postal Service
  - Settlement between ANM and the USPS

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Recent Regulatory Activity - ACD

Findings - Periodicals

- Volume, Revenue, Cost, and Coverage

<table>
<thead>
<tr>
<th></th>
<th>Periodicals FY 2012 Financial Results</th>
<th>Periodicals FY 2011 Financial Results</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Volume</td>
<td>Revenue</td>
</tr>
<tr>
<td>Within County</td>
<td>631,286,455</td>
<td>$ 66,495,595</td>
</tr>
<tr>
<td>Outside County</td>
<td>6,110,064,496</td>
<td>$ 1,656,732,110</td>
</tr>
<tr>
<td>Total</td>
<td>6,741,350,951</td>
<td>$ 1,731,485,915</td>
</tr>
</tbody>
</table>

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### Service Performance (% on time)

**On-Time Service Performance (%) FY 2012**

<table>
<thead>
<tr>
<th></th>
<th>Quarter 1</th>
<th>Quarter 2</th>
<th>Quarter 3</th>
<th>Quarter 4</th>
<th>Annual</th>
<th>Target</th>
</tr>
</thead>
<tbody>
<tr>
<td>Destination Entry Outside County</td>
<td>46.3</td>
<td>66.9</td>
<td>83.1</td>
<td>84.6</td>
<td>69.8</td>
<td>91</td>
</tr>
<tr>
<td>End-to-End Outside County</td>
<td>43.3</td>
<td>57.9</td>
<td>74.3</td>
<td>66.6</td>
<td>59.9</td>
<td>91</td>
</tr>
<tr>
<td>Within County</td>
<td>45.9</td>
<td>65.8</td>
<td>82.1</td>
<td>82.6</td>
<td>68.7</td>
<td>91</td>
</tr>
<tr>
<td>Overall</td>
<td>45.9</td>
<td>65.8</td>
<td>82.1</td>
<td>82.6</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**On-Time Service Performance (%) FY 2011**

<table>
<thead>
<tr>
<th></th>
<th>Quarter 1</th>
<th>Quarter 2</th>
<th>Quarter 3</th>
<th>Quarter 4</th>
<th>Annual</th>
<th>Target</th>
</tr>
</thead>
<tbody>
<tr>
<td>Destination Entry Outside County</td>
<td>78.7</td>
<td>77.8</td>
<td>74.3</td>
<td>77</td>
<td>77</td>
<td>91</td>
</tr>
<tr>
<td>End-to-End Outside County</td>
<td>69.2</td>
<td>70.1</td>
<td>65.4</td>
<td>69.9</td>
<td>69.9</td>
<td>91</td>
</tr>
<tr>
<td>Within County</td>
<td>77.9</td>
<td>76.2</td>
<td>72.4</td>
<td>75.5</td>
<td>75.5</td>
<td>91</td>
</tr>
<tr>
<td>Overall</td>
<td>76.7</td>
<td>77.9</td>
<td>76.2</td>
<td>72.4</td>
<td>75.5</td>
<td>91</td>
</tr>
</tbody>
</table>

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## Historical financial results (millions)

<table>
<thead>
<tr>
<th>Year</th>
<th>Volume</th>
<th>Revenue</th>
<th>Cost</th>
<th>Cost Coverage</th>
<th>Contribution</th>
</tr>
</thead>
<tbody>
<tr>
<td>2007</td>
<td>8,795</td>
<td>$2,188</td>
<td>$2,636</td>
<td>83.01%</td>
<td>$ (448)</td>
</tr>
<tr>
<td>2008</td>
<td>8,605</td>
<td>$2,295</td>
<td>$2,732</td>
<td>84.00%</td>
<td>$ (437)</td>
</tr>
<tr>
<td>2009</td>
<td>7,953</td>
<td>$2,038</td>
<td>$2,680</td>
<td>76.04%</td>
<td>$ (642)</td>
</tr>
<tr>
<td>2010</td>
<td>7,269</td>
<td>$1,879</td>
<td>$2,490</td>
<td>75.46%</td>
<td>$ (611)</td>
</tr>
<tr>
<td>2011</td>
<td>7,077</td>
<td>$1,821</td>
<td>$2,430</td>
<td>74.94%</td>
<td>$ (609)</td>
</tr>
<tr>
<td>2012</td>
<td>6,741</td>
<td>$1,732</td>
<td>$2,402</td>
<td>72.10%</td>
<td>$ (670)</td>
</tr>
</tbody>
</table>

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Recent Regulatory Activity - ACD

Findings - Periodicals

- **Historical Financial Results (unit basis)**

<table>
<thead>
<tr>
<th></th>
<th>Cost/Pc</th>
<th>Revenue/Pc</th>
<th>Contribution/Piece</th>
</tr>
</thead>
<tbody>
<tr>
<td>2007</td>
<td>$0.300</td>
<td>$0.249</td>
<td>$(0.051)</td>
</tr>
<tr>
<td>2008</td>
<td>$0.318</td>
<td>$0.267</td>
<td>$(0.051)</td>
</tr>
<tr>
<td>2009</td>
<td>$0.337</td>
<td>$0.256</td>
<td>$(0.081)</td>
</tr>
<tr>
<td>2010</td>
<td>$0.343</td>
<td>$0.258</td>
<td>$(0.084)</td>
</tr>
<tr>
<td>2011</td>
<td>$0.343</td>
<td>$0.257</td>
<td>$(0.086)</td>
</tr>
<tr>
<td>2012</td>
<td>$0.356</td>
<td>$0.257</td>
<td>$(0.099)</td>
</tr>
</tbody>
</table>

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Recent Regulatory Activity - ACD

Findings - Periodicals

**Historical Financial Results (unit basis)**

<table>
<thead>
<tr>
<th>Plant Man</th>
<th>NONMods</th>
<th>Plant Mech</th>
<th>Bundle</th>
<th>Plant Allied</th>
<th>Other Allied</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.47</td>
<td>3.36</td>
<td>1.94</td>
<td>3.00</td>
<td>2.70</td>
<td>0.58</td>
<td>13.05</td>
</tr>
<tr>
<td>0.92</td>
<td>4.42</td>
<td>3.33</td>
<td>2.68</td>
<td>4.15</td>
<td>1.03</td>
<td>16.52</td>
</tr>
<tr>
<td>1.10</td>
<td>4.73</td>
<td>3.55</td>
<td>2.74</td>
<td>4.62</td>
<td>1.11</td>
<td>17.83</td>
</tr>
<tr>
<td>1.02</td>
<td>5.19</td>
<td>3.34</td>
<td>2.76</td>
<td>4.54</td>
<td>1.63</td>
<td>18.48</td>
</tr>
<tr>
<td>1.26</td>
<td>5.74</td>
<td>3.67</td>
<td>2.71</td>
<td>4.54</td>
<td>1.68</td>
<td>19.60</td>
</tr>
<tr>
<td>1.19</td>
<td>5.10</td>
<td>3.48</td>
<td>2.60</td>
<td>4.34</td>
<td>1.91</td>
<td>18.62</td>
</tr>
<tr>
<td>1.20</td>
<td>4.71</td>
<td>4.80</td>
<td>2.51</td>
<td>4.10</td>
<td>1.81</td>
<td>19.12</td>
</tr>
<tr>
<td>1.21</td>
<td>4.89</td>
<td>5.22</td>
<td>2.45</td>
<td>4.30</td>
<td>1.83</td>
<td>19.92</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>FY10</th>
<th>FY11</th>
<th>FY12</th>
</tr>
</thead>
<tbody>
<tr>
<td>Periodicals CRA Unit Cost</td>
<td>Mail Processing</td>
<td>Delivery</td>
</tr>
<tr>
<td>34.25</td>
<td>18.62</td>
<td>12.24</td>
</tr>
<tr>
<td>34.34</td>
<td>19.12</td>
<td>11.97</td>
</tr>
<tr>
<td>35.62</td>
<td>19.92</td>
<td>12.06</td>
</tr>
</tbody>
</table>

Cumulative Change

<table>
<thead>
<tr>
<th>FY10</th>
<th>FY11</th>
<th>FY12</th>
</tr>
</thead>
<tbody>
<tr>
<td>Periodicals CRA Unit Cost</td>
<td>Mail Processing</td>
<td>Delivery</td>
</tr>
<tr>
<td>1.37</td>
<td>1.29</td>
<td>0.18</td>
</tr>
<tr>
<td>4.0%</td>
<td>6.9%</td>
<td>1.5%</td>
</tr>
</tbody>
</table>

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Recent Regulatory Activity - ACD

Findings - Periodicals

- Directed the Postal Service to review its operational strategy to assess what cost savings measures are working, and how they could be improved
- Encouraged the Postal Service to evaluate whether it can change workshare discounts and pricing structure to reverse the negative trend

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Recent Regulatory Activity – ACD

Findings - First-Class Mail

First-Class Mail Presort Coverage and Passthrough

- FCM Presort Cost Coverage is 292 percent
- The 5-digit Workshare discount passthrough was 77.4 percent

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Recent Regulatory Activity – ACD

Negotiated Service Agreements

- Competitive NSAs continue to show significant growth for postal revenues
- Market dominant NSAs are more challenging, to review and to evaluate

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Recent Regulatory Activity – ACD

Competitive Negotiated Service Agreements

- 355 Competitive NSAs approved since the PAEA
  - Competitive NSAs required to cover attributable cost
  - Collectively, competitive products must contribute to institutional costs of the Postal Service (currently 5.5%)

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17 Market Dominant NSAs reviewed since 2009

- Each Market Dominant NSA must be available on public and reasonably terms to similarly situated mailers and either
  - improve the net financial position of the Postal Service
    - Reduce costs; or
    - Increasing overall contribution
  - or Enhance the performance of mail preparation, processing, transportation, or other functions

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Regulatory Issues Ahead

*Delivery Frequency*

- The Postmaster General announced the Postal Service’s intention to move to 5-day mail delivery and 6-day package delivery
  - Revised proposal is to address concerns:
    - Growth in parcel market
    - Reliance on parcels for prescription drug delivery
  - Claims authority to move forward under a Continuing Resolution
- In light of Appropriations bill language, the Board of Governors issued an April 10th Press release to postpone implementation
- 2010 Advisory Opinion methodology with updated costs: $1.744 billion in annual savings
- Annual Report “cost of the USO” for 6-day delivery estimated at $2.480 billion for FY 2011 (no revenue loss)

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Regulatory Issues Ahead

Procedures for Nature of Service Cases Docket RM2012-4

- Commission instituted a rulemaking to revise procedures for Nature of Service (Advisory Opinion) cases
  - Law requires a “hearing on the record”
  - Streamlining process to the extent due process allows

- Next Steps: Proposed Rules
The 2006 law tasked the Commission with reviewing the Postal Accountability and Enhancement Act, including its modern system of ratemaking, 10 years after implementation.

39 U.S.C. 3622(d)(3) provides that the Commission must evaluate if the system is achieving the objectives of the section, while taking into account the factors.

If the Commission determines the system is not achieving the objectives while taking into account the factors, it may, after a notice and comment procedure and by regulation, establish a new system as necessary.

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Regulatory Issues Ahead

Review of the PAEA and Ratemaking

- **Price cap**
  - Effective in spurring cost reductions
  - Effective at constraining price increases
  - Challenge to maintain adequate revenues

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Regulatory Issues Ahead
Review of the PAEA and Ratemaking

Cumulative Percent Change in Cost

Effective in spurring cost reductions

Six Years Prior to PAEA (FY 2000 - FY 2006)

Six Years After PAEA (FY 2007 - FY 2012)

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Effective at constraining price increases

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Regulatory Issues Ahead
Review of the PAEA and Ratemaking

Challenging to maintain adequate revenues

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Challenges and Reform

Commission Action Items

- Consider the “on the record” requirement for hearings in Nature of Service (Advisory Opinion) cases
- Maintain prospective review for changes in the nature of postal services and competitive NSAs
- Raise the market test revenue cap for Market Dominant products to allow for meaningful market tests
- Re-amortize the current mandated payments into the Postal Service Retiree Health Benefit Fund (PSRHBF)

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Challenges and Reform

Options on the Table

- Post-PAEA Nature of Service Review

<table>
<thead>
<tr>
<th>Proposed Change</th>
<th>Approx. Annual Savings ($Billions)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Saturday Delivery</td>
<td>$1.744 (PRC Estimate: N2010-1)</td>
</tr>
<tr>
<td>Mail Processing Realignment</td>
<td>$.45 - 1.96 (PRC Estimate N2012-1)</td>
</tr>
<tr>
<td>POSTPlan</td>
<td>$.39 - .70 (PRC Estimate N2012-2)</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>$2.84 – 4.40</td>
</tr>
</tbody>
</table>

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Closing

- Role of Commission moving forward
- The Universal Service Obligation

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