

10-YEAR SYSTEM OF RATEMAKING REVIEW AND POSTAL REFORM

NATIONAL POSTAL POLICY COUNCIL: QUARTERLY MEETING

December 5, 2013

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Introduction

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- Recently at the Commission
- On the horizon

Recently at the Commission...

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- Terms Expired for Commsrs. Hammond and Langley
- General Counsel
- Government Shutdown effects
- CPI Rate Adjustment Case (R2013-10) Final Order
- Exigent Rate Adjustment Request Ongoing
- Proposed Cap Rule Changes for Promotions
- Discover NSA
- USPS Financials

Recently at the Commission...

Commissioners Hammond and Langley

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- Commissioners Hammond and Langley are currently absent from the Commission as of Oct. and Nov.
 - ▣ Both have been re-nominated by the President
 - ▣ Both have had a hearing on the nomination by the Committee of jurisdiction
 - ▣ Both have had a mark-up of their nominations by the Committee of jurisdiction
- Nominations must next be considered by the Senate

Recently at the Commission...

General Counsel

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- Earlier this autumn, the Commission's General Counsel, Steve Sharfman, announced his pending retirement.
 - ▣ Steve will depart in the early part of 2014
 - ▣ Commission actively engaged in seeking a replacement
 - Presently interviewing prospective executive search firms

Recently at the Commission...

Government Shutdown

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- October 1 through 16, 2013 appropriations lapse
 - ▣ Required the Commission to cease operations
 - ▣ Commission funds “appropriated” by Congress from the Postal Service’s general fund 39 U.S.C. § 504(d)
 - ▣ Adjusted deadlines for CPI Rate Adjustment Case and Post Office Closing Appeal

Recently at the Commission...

Extraordinary and Exceptional Rate Adjustment Request

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- ❑ Technical Conferences held 10/24-11/ 1
- ❑ Hearings held 11/18 and 19, recordings and transcripts available at www.prc.gov
- ❑ Initial Comments were due 11/26
- ❑ Reply Comments due 12/6
- ❑ To date more than 10 written information requests, with over 100 questions asked by the Commission
- ❑ 90 day mark from filing: 12/25
- ❑ Thank you for your participation – your comments and thoughts are appreciated

Recently at the Commission...

Inflation (CPI) Rate Adjustment Order

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- On November 21, 2013, Commission issued an order on the Postal Service's request for an Annual Inflation (CPI)-based rate adjustment (Order 1890)
 - ▣ Found that the prices proposed by the Postal Service were in line with the CPI-based cap
 - ▣ Found that the proposal to eliminate automation rates for non-Full Service IMb users constituted a “deletion” or “redefinition” of rate cells that had a price-cap impact in Periodicals, Standard, and First-Class Mail

Recently at the Commission...

Inflation (CPI) Rate Adjustment Order

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- Order 1890
 - ▣ Required the Postal Service to:
 - Delay the implementation of the Full Service IMb rate penalty;
 - Adjust rates to account for the IMb rate change; or
 - Propose an alternative
 - ▣ There was a non-profit workshare discount that did not align with its commercial counterpart that was not justified, and the Commission ordered the Postal Service to address it
 - ▣ USPS intends to comply, delaying IMb and equalizing workshare discount by lowering commercial discount

Recently at the Commission...

Rulemakings

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- Price Cap Calculation
 - ▣ In Order No. 1879, issued November 18, 2013, the Commission announced a proposed rulemaking for the treatment of pricing incentives and de-minimis rate increases
- Pitney Bowes Benchmark
 - ▣ In Order No. 1753 issued June 18, 2013 the Commission revised the benchmark for the 5-digit letters worksharing discount
 - ▣ In Order No. 1793 issued July 29, 2013 the Commission extended the revision to Standard Regular 5-digit mail

Recently at the Commission...

Discover NSA

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- Commission approved amendment to Discover NSA in Order No. 1720, issued May 17, 2013
 - ▣ Amendment allows some priority mail volume to be counted in the calculation of its adjusted revenue threshold under the agreement
 - ▣ Decision keeps Discover from being “penalized” under the agreement for upgrading some First-Class Mail to Priority Mail

Recently at the Commission...

USPS Financial Performance

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□ Financial Performance

▣ September net loss of \$114 million

- \$213 million better than SPLY
- However, loss is affected by a non-cash adjustment to revenues regarding accounting of Forever Stamp revenue
- Removing this \$1.3 billion one-time adjustment yields a positive \$128 million net revenue for September

▣ October net operating income of \$274 million

- About the same as SPLY (\$3 million higher)
- Volume dropped 9%, lowering revenue by \$144 million, offset by \$147 million expense cuts
- However, net loss of \$410 million after accounting for the retiree health benefits expense and adjustment to workers' compensation

Recently at the Commission...

USPS Financial Performance

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- Financial Performance (continued)
 - Year-end financials will be available in February, prelim:
 - FY 2013 ended with a \$982 million net operating loss, \$1.4 billion better than last year
 - Revenues increased by \$800 million despite loss of volume of 1.4 billion pieces
 - Compared to the plan, \$1 billion better than expected, due in large part to less losses in market dominant products than forecast

On the Horizon...

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- 10-Year Review of System of Ratemaking
- Procedures for Nature of Service Cases
- Annual Compliance Determination and Annual Report Restructuring
- Elasticity Estimates
- Postal Reform: One Commissioner's Perspective
- Changes in Service Proposed Since PAEA

On the Horizon...

10-year Review of the System of Ratemaking

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- Starting 10-years after the enactment of the PAEA, the Commission shall review the system for regulating rates for market-dominant products

39 USC § 3622(d)(3)

- ▣ Review to determine if the system is achieving the objectives listed in 3622(b) while taking into account the factors of 3622(c)
- ▣ If the Commission determines, after notice and comment, that the system is not meeting the objectives, by regulation it may modify or replace it as necessary to meet the objectives

On the Horizon...

10-year Review of the System of Ratemaking

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- Review of statutory criteria
 - ▣ Objectives - 39 U.S.C. 3622(b)
 - ▣ Factors – 39 U.S.C. 3622(c)

On the Horizon...

10-year Review of the System of Ratemaking

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□ Objectives:

- To maximize incentives to reduce costs and increase efficiency
- To create predictability and stability in rates
- To allow the Postal Service Pricing flexibility
- To assure adequate revenues, including retained earnings, to maintain financial stability

On the Horizon...

10-year Review of the System of Ratemaking

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- Objectives (continued):
 - To reduce the administrative burden and increase the transparency of the ratemaking process
 - To enhance the security of the mail and deter terrorism
 - To establish and maintain a just and reasonable schedule for rates and classifications (but still allow USPS to make reasonable unequal changes within, between, or among classes)
 - To allocate the total institutional costs of the USPS appropriately between market-dominant and competitive products

On the Horizon...

10-year Review of the System of Ratemaking

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- Factors the Commission shall take into account:
 - The value of the mail service actually provided each class or type of mail to the sender and recipient, including the collection, mode of transport, and priority of delivery
 - The requirement that each class of mail or type of mail service bear the direct and indirect postal costs attributable to it, through reliably identified causal relationships plus that portion of other costs reasonably assignable
 - The effect of rate increases on the public, business mail users, and enterprises in the private sector engaged in delivery
 - The available alternate means of sending and receiving letters and other mail matter at reasonable costs
 - The degree of preparation of mail for delivery performed by the mailer and its effect on USPS cost reductions

On the Horizon...

10-year Review of the System of Ratemaking

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- Factors the Commission shall take into account (continued):
 - ▣ Simplicity of structure for the entire schedule and simple, identifiable relationships between the rates or fees charged the various classes of mail
 - ▣ The importance of pricing flexibility to encourage increased mail volume and operational efficiency
 - ▣ The relative value to the people of the kinds of mail matter entered into the system, and the desirability and justification for special classifications and services of mail
 - ▣ The importance of providing classifications with extremely high degrees of reliability and speed of delivery and of providing those that do not require high degrees of reliability and speed of delivery

On the Horizon...

10-year Review of the System of Ratemaking

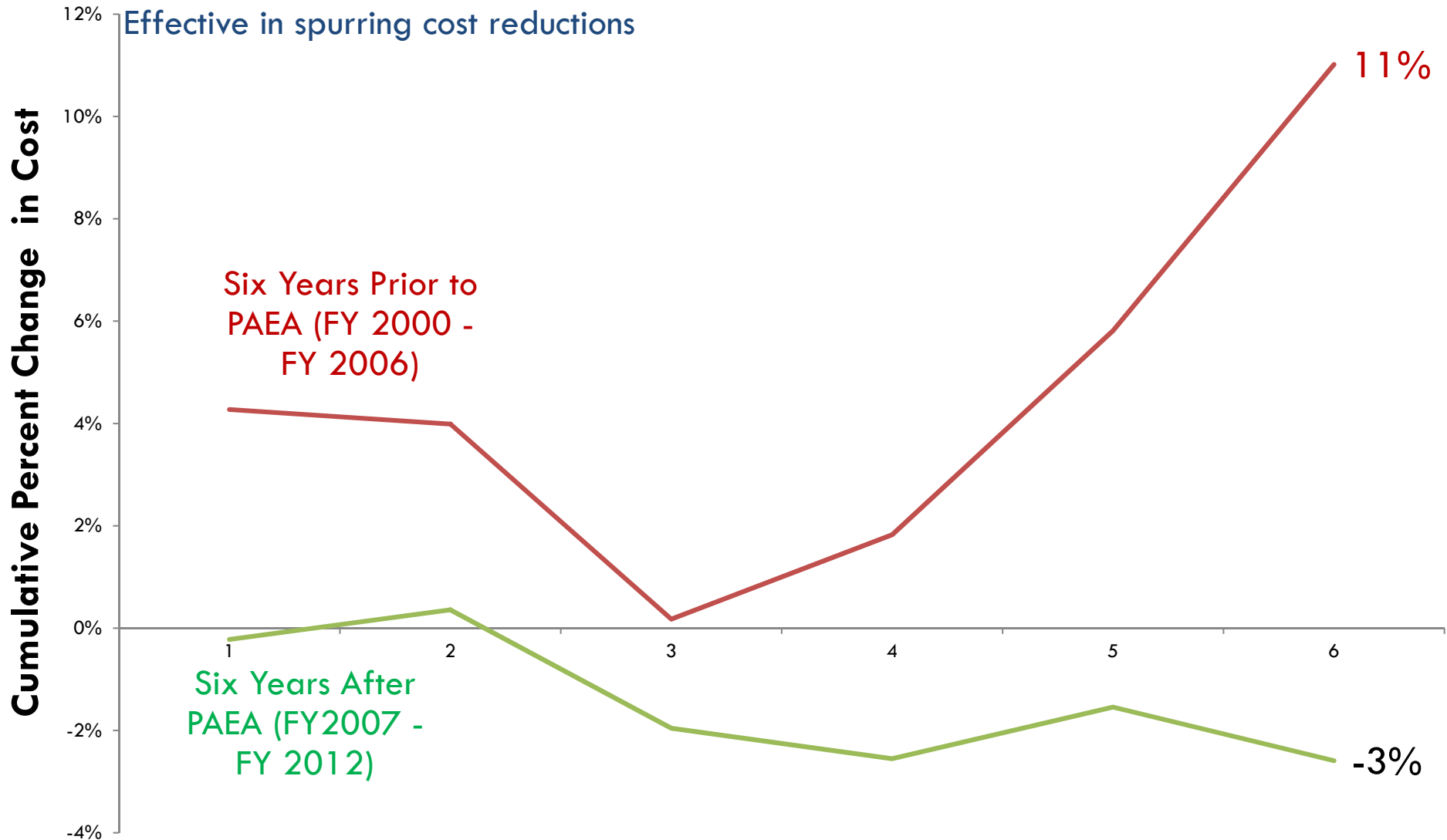
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- Factors the Commission shall take into account (continued):
 - ▣ The educational, cultural, scientific, and informational value to the recipient of mail matter
 - ▣ The need for the USPS to increase efficiencies and reduce costs, including infrastructure costs, to help maintain high quality and affordable services
 - ▣ The value to the Postal Service and postal users of promoting intelligent mail and of secure, sender-identified mail
 - ▣ The policies of title 39 and other factors the Commission deems appropriate.

On the Horizon...

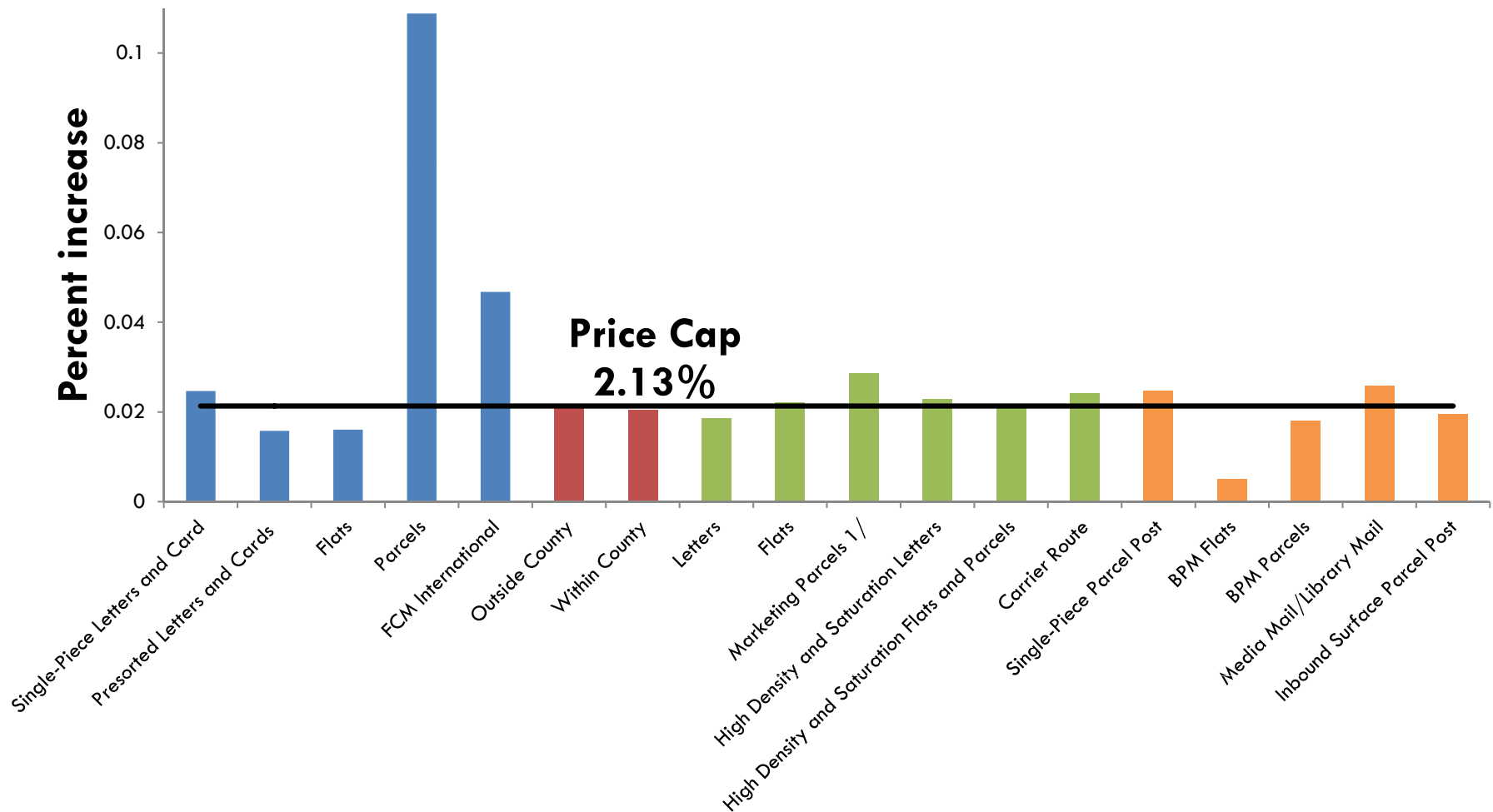
10-year Review of the System of Ratemaking

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On the Horizon...

10-year Review of the System of Ratemaking



On the Horizon...

10-year Review of the System of Ratemaking

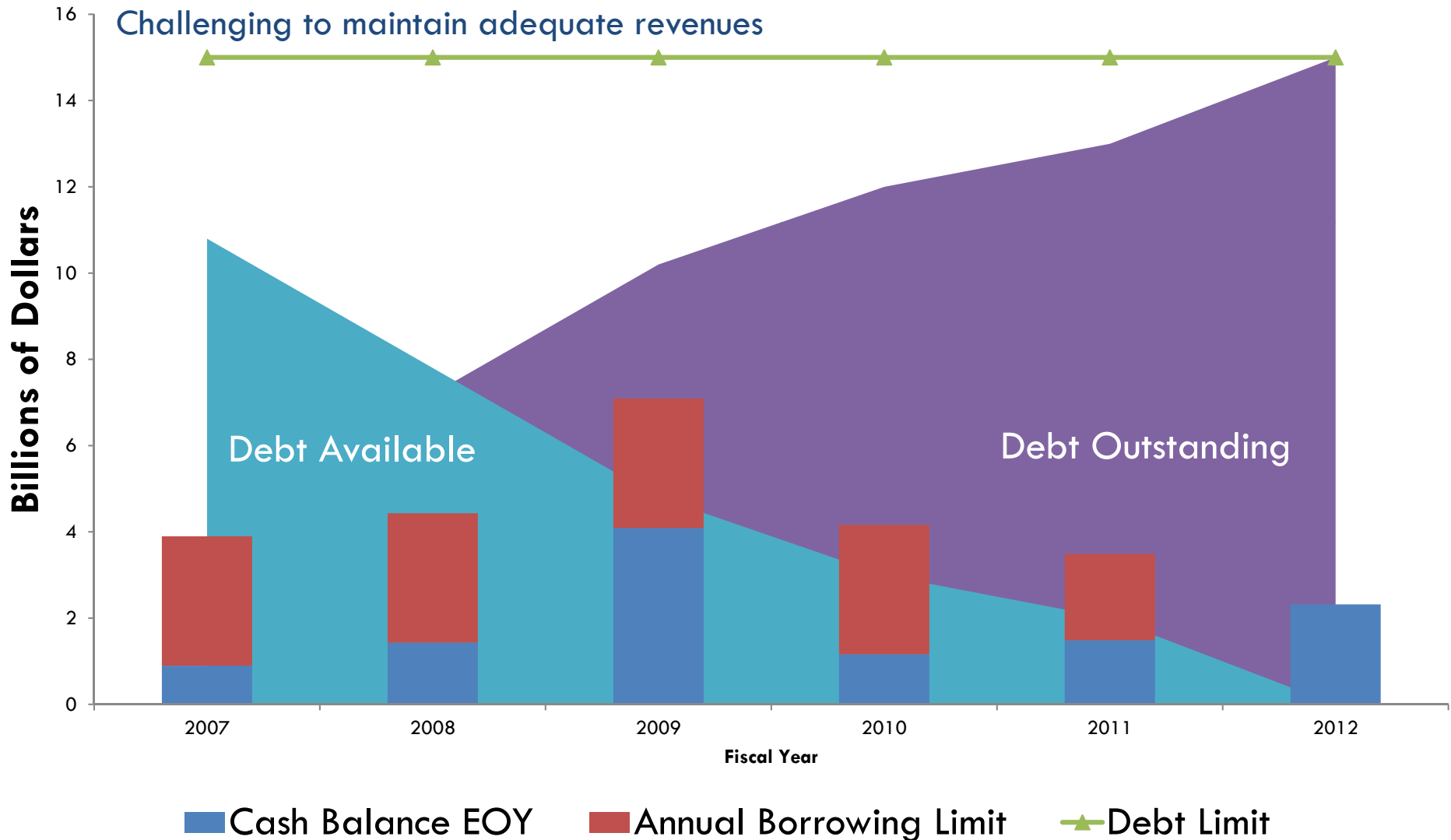
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- Other relevant data:
 - Over 375 competitive NSAs and 20 market-dominant NSAs reviewed since PAEA (desirability of special classifications, pricing flexibility)
 - Rulemaking evaluating the appropriate share for competitive products (allocation of institutional costs)
 - Market dominant annual CPI adjustment cases reviewed in 45 days instead of 10 months (reduce administrative burden, increase transparency)
 - Postal Service discretion to allocate non-discriminatory and reasonable prices under the cap (pricing flexibility)

On the Horizon...

10-year Review of the System of Ratemaking

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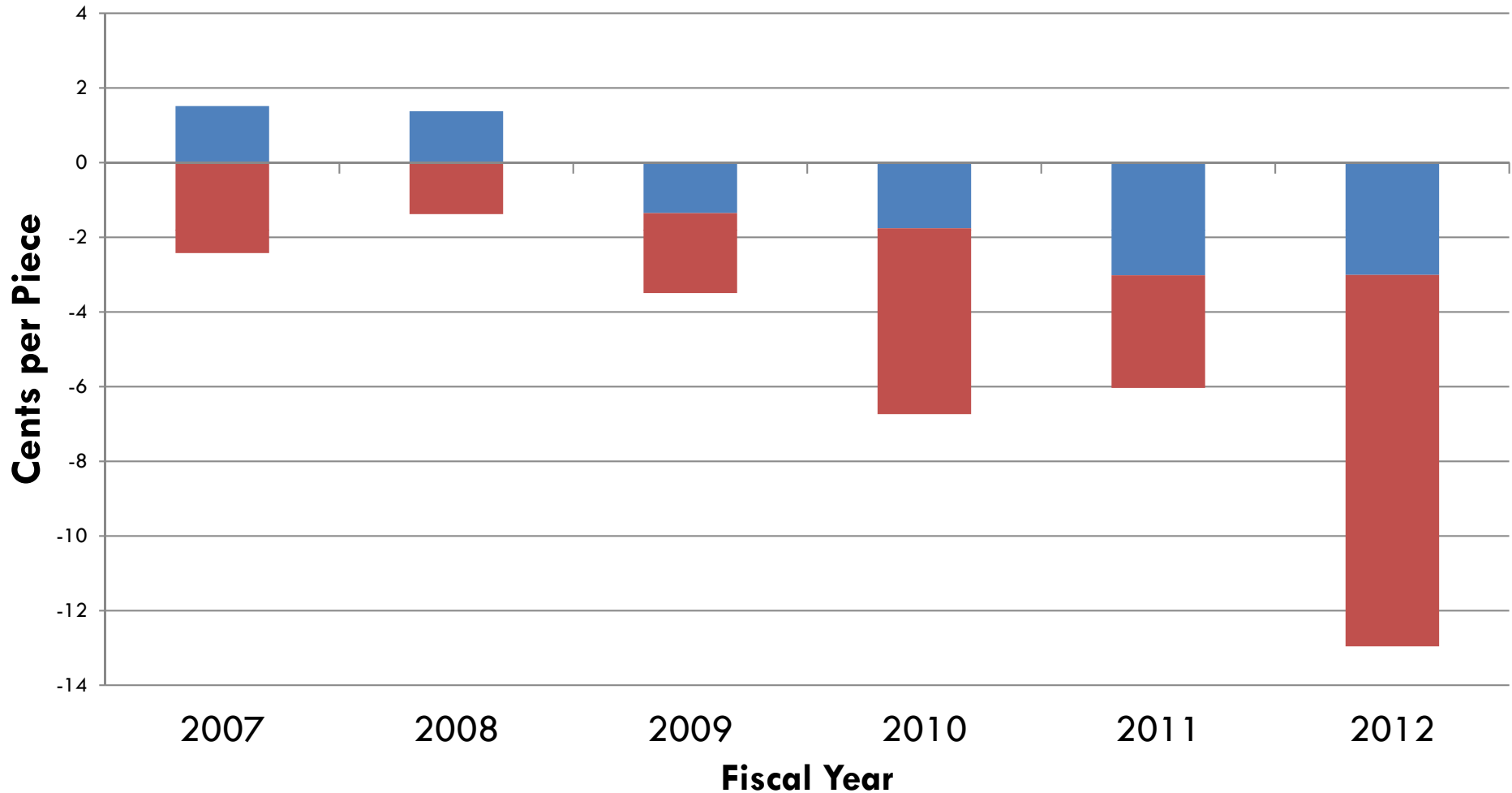


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On the Horizon...

10-year Review of the System of Ratemaking

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■ Net Revenue per Piece w/o RHBF

■ Net Revenue Per Piece with RHBF

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On the Horizon...

Procedures for Nature of Service Cases Docket RM2012-4

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- Commission proposed rules for Nature of Service (Advisory Opinion) cases
 - ▣ Requiring pre-filing consultations with affected groups
 - ▣ Limiting discovery and motions practice
 - ▣ Limiting the focus of hearings
 - ▣ Limiting the length of briefs
 - ▣ Considering possible alternatives after the case in a special study
- Comments and reply comments received in August
- Commission will be working on next steps

On the Horizon...

Changes in Service Proposed since PAEA

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□ Post-PAEA Nature of Service Review

Proposed Change	Approx. Annual Savings (\$Billions)
Saturday Delivery	\$1.744 (PRC Estimate: N2010-1)
Proposed Changes Dollars at Stake	Loss Under Management Control
<u>\$2.84-4.40 billion</u>	<u>\$2.4 billion</u>
<u>Total</u>	<u>\$2.84 – 4.40</u>

- While less than the net revenue loss of over \$12 billion, note the total figure is still greater than those operating losses under management control

On the Horizon...

Annual Compliance Determination and Annual Report Restructuring

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- The Commission is reviewing the format of its most common reports, including the ACD and the Annual Report to determine if change would benefit the users of those reports
 - ▣ Streamlining to avoid duplication?
 - ▣ Smaller, more focused reports on individual topics?
 - ▣ Thoughts and suggestions welcome!

On the Horizon...

Elasticity Estimates

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- How the Commission/USPS uses or calculates elasticities
 - ▣ Commission use:
 - Calculate Market Dominant NSA “Net Financial Benefit”
 - Evaluation of Exigent Rate Request Roll-Forward
 - Calculate Volume Generated by Pricing Incentive Programs
 - ▣ USPS use:
 - Exigent Rate Request Roll-Forward
 - Demand Forecasting/Internal Analyses

On the Horizon...

Postal Reform: One Commissioner's Perspective

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- ❑ Remove 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)
- ❑ Allow the Postal Service greater ability to change its structure, in both product offerings and labor utilization

Closing

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- Thank you!
- Comments, thoughts, and suggestions welcome

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