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

Statutory Review of the System for Regulating Rates and Classes for Market Dominant Products (Consolidating Docket Nos. RM2024-4, RM2022-5, RM2022-6, and RM2021-2)	Docket Nos. RM2024-4 RM2022-5 RM2022-6 RM2021-2

COMMENTS OF THE NATIONAL POSTAL POLICY COUNCIL

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Table of Contents

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(July 9, 2024)

The National Postal Policy Council ("NPPC") respectfully submits these comments on the Commission's Advance Notice of Proposed Rulemaking.[1] NPPC's members primarily mail Presorted First-Class Mail, but also use Single Piece, Metered Mail, Business Reply Mail in First-Class Mail, and USPS Marketing Mail Carrier Route letters.

NPPC members and the Postal Service – a public service provided by the federal government – both want the Service to provide dependable and high-quality nationwide service at affordable prices in a cost-effective manner. Unfortunately, results on all counts are falling substantially and worrisomely short, including the subject of this rulemaking.

It is clear at this point, more than three years since the current system for regulating Market Dominant rates was established that the new system is not working. Not only have the higher rates proved ineffective at correcting the issues for which it was designed, but they are impeding the very public service mission that they intended to

1 Order No. 7032 (Apr. 5, 2024), 89 *Fed. Reg*. 25554 (Apr. 11, 2024) ("*ANPRM*").

support while not achieving certain other objectives – particularly those relating to rate stability, cost control, and quality service.

If the Postal Service's pricing of its monopoly products, based upon excessive rate authorities, and service performance that consistently falls short of its own standards drive away substantial volumes and discourage public use of the mails, is it really fulfilling its public service mission as charged by 39 U.S.C. §101? NPPC believes the answer is no. Under the current system, the Postal Service today is losing the public's business at an alarming rate. An improved system is urgently needed.

I. INTRODUCTION AND SUMMARY

In Docket No. RM2017-3, the Commission concluded that the system for regulating the rates of Market Dominant postal products was not achieving several Objectives established by the Postal Accountability and Enhancement Act ("PAEA").[2] The unmet Objectives pertained to pricing for allocative efficiency, maintaining high quality service standards, and the financial stability of the Postal Service (particularly its incentives for cost reductions and improved efficiency and a failure of some mail to cover its attributable costs).[3]

On that basis, the Commission modified the rate-setting system established by Congress by creating three new rate authorities to allow the Postal Service to raise rates by more than the statutory price cap set at the consumer price index for urban consumers. That action weakened the incentives to reduce costs under a price cap

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2 Pub. L. 109-435, 120 Stat. 3198 (Dec. 20, 2006).

3 *See* Order No. 5763, Docket No. RM2017-3, at 7-10 (Nov. 30, 2020), summarizing findings in Order No. 4257, Docket No. RM2017-3, at 142, 249 & 250 (Dec. 1, 2017).

system by introducing cost-of-service principles. Although the Commission pledged to review the current (as modified) system in five years, the Commission has now accelerated that review.

The failure of the current system is illustrated by the fact that in what the Postal Service's current strategic plan – the Delivering for America Plan ("DFAP") – promised would be a financially break-even year in FY 2023,[4] the Postal Service fell short of that target by $6.5 billion despite massive financial relief from Congress and had a $2.3 billion net operating loss.[5] Even after adjusting for non-cash workers' compensation, postal operating costs rose by 4.0 percent while volumes fell to the lowest level since 1968.[6] Total operating expenses rose to a record high.[7] That failure manifests itself in excessive costs and an unprecedented decline in productivity. This has occurred during a period in which the Postal Service has reduced its service standards and yet has generally been unable to achieve even the still-lower performance "targets" it sets for itself.

The basic problem with the current ratemaking system is that the Postal Service has not had sufficient incentive to improve its operating costs for Market Dominant mail and the system has led to severe losses of badly needed volume as mailers are increasingly unwilling to pay continually soaring rates for less service.

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4 United States Postal Service, *Delivering for America*, at 51, Figure 35.

5 *See* Postal Regulatory Commission, *United States Postal Service Financial Results and 10-K Statement Fiscal Year 2022*, at 1 (May 17, 2023) ("*FY 2023 Financial Analysis*").

6 *USPS FY 2023 Form 10-K, at* 46 (Nov. 14, 2023) (adjusted for non-cash workers' compensation at 19) ("*USPS FY 2023 Form 10-K*").

7 In nominal (not inflation-adjusted) dollars.

To preserve the Postal Service, the Commission must replace the current system with one that creates stronger incentives to control costs, to encourage greater volume (which will improve productivity) through pricing and fewer rate changes, and to improve operational efficiency and quality service.

NPPC recommends that the system be modified as follows:

- Limit the Postal Service to no more than one Market Dominant rate adjustment per fiscal year;
- Eliminate the density factor;[8]
- Impose an X-Factor to force the Postal Service to control its costs, coupled with a performance incentive mechanism that would allow it additional rate authority if it achieved pre-established metrics pertaining to volume, productivity, and service;
- Let expire (by its own terms) the retirement authority or, if this proceeding is complete before that authority is used for the fifth time, cease it, but going forward condition retention of the compounded total of all amounts collected by that authority on the Postal Service's continued making the required payments to the Treasury; and
- Improve the workshare discount rules to enhance efficiency.

II. BACKGROUND

The Postal Service possesses an unparalleled national network that provides collection, processing, transportation, and delivery services throughout the United States and provides access to foreign posts as well. Its competitive advantages include a nationwide transportation, processing, and delivery network supported by a legal

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[8] These comments do not address the two percent additional authority for non-compensatory classes, which to date has not affected NPPC members.

monopoly over letter mail,[9] exclusive access to mailboxes,[10] a strong brand name, and extensive real estate holdings assembled over more than two centuries.

Unlike 30 years ago, Market Dominant mail alone cannot support the postal system. Today, it is essential that the Postal Service also obtain both significant revenue and contribution to institutional costs from its Competitive offerings, as both the Postal Service and Commission have recognized.[11] Conversely, Competitive packages need letter mail to sustain the Service's viability. For example, if Competitive products were to cover completely the $6.5 billion loss the Postal Service incurred in FY 2023, the Postal Service would need to more than triple its volume of Priority Mail or double its volume of its Ground Advantage and Parcel Select products, a highly unrealistic expectation. For that reason, among others, NPPC supported the provision in the Postal Service Reform Act of 2022 ("PSRA") in which Congress directed that there be an integrated delivery network.

A. The PAEA Applied Price Cap Regulation To Market Dominant Products While Largely Deregulating Competitive Products

From 1970, when the Postal Service was converted from an Executive Branch cabinet agency to its current status, its prices were regulated under a cost-of-service "breakeven" regime created by the Postal Reorganization Act ("PRA"). Under that system, the Governors determined the revenue requirement for a future test year and the

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9 *See* 18 U.S.C. §§ 1693-1699 & 39 U.S.C. §§ 601-606 (Private Express Statutes).

10 18 U.S.C. § 1725 (mailbox rule).

11 The Postal Service's Integrated Financial Plan projects Shipping and Packages will account for 33.7 percent of FY 2024 revenue. United States Postal Service, *Fiscal Year 2024 Integrated Financial Plan*, at 2 (Nov. 20, 2023) ("*FY2024 IFP*").

then-Postal Rate Commission recommended rates for all postal products to achieve that revenue. Over time, that system led to repeated large and often unpredictable rate increases because there was neither a legal requirement that the Postal Service control costs nor consequences if it failed to do so; it simply folded the excessive costs, including an cost called prior year loss recovery, into the revenue requirement.[12] The Postal Service's concerns about the length of the cumbersome process and a desire for more pricing flexibility, and mailers' concerns over the lack of cost control and sharp price increases, led Congress to understand the need to reform the process.

In 2006, Congress repealed the PRA's cost-of-service regime when it enacted the PAEA. However, the PAEA did not change that the Postal Service is, first and foremost, a public service. Among the primary objectives of the PAEA were (1) to protect captive mailers from higher rates; (2) to promote cost control by limiting rate increases for Market Dominant products to the level of Consumer Price inflation; and (3) to create more accountability for service performance; while (4) allowing the Postal Service to offer Competitive Products in a less regulated manner.

For Competitive products, the PAEA granted the Postal Service substantial pricing flexibility to enable it to compete better with the private firms in that market. Congress

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[12] The PRA did contain a provision stating that postal rates and fees shall be "reasonable and equitable and sufficient to enable the Postal Service under honest, efficient, and economical management" to maintain, continue, and develop postal services. *See* former 39 U.S.C. §3621. The PAEA moved that language into the new exigency provision. *See* 39 U.S.C. §3622(d)(1)(E). However, that provision, read literally, applies to postal *management*, not the Postal Service *operations*, and in any event has not been used to reduce a revenue requirement set by the Governors.

relied on market pressure to restrain Competitive prices to competitive levels while prohibiting cross-subsidization by monopoly services.[13]

In contrast, the PAEA recognized that Market Dominant mail both remains subject to the Postal Service's two legal monopolies – which confer the Postal Service with market power to support its public service mission – and that the former cost-of-service regime failed to provide a meaningful incentive for the Service to control costs. Thus, Congress adopted a different approach: imposing a price cap measured by the Consumer Price Index-Urban Consumers and directing this agency to establish a system for regulating the rates of Market Dominant products subject to the price cap to achieve nine specified objectives, taking into account 14 additional factors. The objectives and factors do not establish separate public policies, but rather are guides for the Commission in implementing the Market Dominant rate system that helps support of the Postal Service's public service mission.

The price cap was intended, *inter alia*, to rein in the excessive postal spending that had occurred under the former cost-of-service regime. Under a price cap system, the regulated entity may increase net income from its regulated offerings by increasing volume, reducing cost, or both. The entity's incentive to reduce costs is that it can retain all the cost savings. In the case of the Postal Service specifically, the PAEA gave the Postal Service three ways to increase its net income: (1) increasing mail volume; (2)

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[13] Market pressure works to keep rates at competitive levels only if true competition exists. The Postal Service's recent price increases of 40 percent or more for DDU-entered Parcel Select packages raise a legitimate question whether the Service faces effective competition in last-mile package delivery. It certainly does not for letter delivery.

controlling cost increases below CPI, particularly for Market Dominant products; and (3) earning greater profits from Competitive products.

Unfortunately, in the PAEA, and at the insistence of the then-current Administration, Congress also saddled the Postal Service with a unique obligation to prefund certain retiree benefits on an unprecedented scale.[14] These mandated payments generally were about $5 billion annually, which the Postal Service paid until 2011 and thereafter did not (the non-payments were treated as accrued costs and therefore counted in net income calculations). The Service never suffered any penalty or sanction for failing to make the required payments. However, the Postal Service typically reported annual losses. For most of that era, the losses were approximately the amount of the required, but not paid, prefunding of the retiree health benefits. *See* Order No. 4257 at 168, Table II-10. Ignoring the prefunding obligation, the Postal Service usually showed an operating profit over that period. *Id*. at 164, Table II-8.[15]

B. The Changes To The System Made In Docket No. RM2017-3

In Docket No. RM2017-3, the Commission concluded that the system created by Congress was not achieving several statutory Objectives – those of pricing efficiency, maintaining high quality service standards, financial stability, and reasonable rates. By

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[14] PAEA, §8909a(2)(B) (““[T]he Office shall compute, and by June 30 of each succeeding year shall recompute, a schedule including a series of annual installments which provide for the liquidation of any liability or surplus by September 30, 2056, or within 15 years, whichever is later, or the net present value….”

[15] Current postal management’s eagerness to blame prior leadership and the Commission for past financial difficulties is misplaced. *See Cover Letter from the Postmaster General, Delivering for America Responses of the United States Postal Service to the Reporting Requirements Specified in the Postal Service Reform Act of 2022: FY 2024 1st and 2d Quarter* (May 31, 2024). The Postal Service’s losses were almost entirely on paper, as the non-payment of the retiree health benefit funding obligations generally approximated the amount of the accounting losses.

far the most important factor in that decision was the RHB prefunding obligation, which accounted for $54.8 billion of the accounting losses.[16] In Order No. 5763, while retaining the CPI price cap set by Congress, the Commission crafted three new additional rate authorities which allow the Postal Service to exceed the cap: a density factor, a retirement authority, and a two percent additional rate authority for non-compensatory classes.

The retirement authority was tied to certain retirement funding obligations. As adopted, it is set to expire after five years (although the higher rates it generated – amounting to over $2 billion in additional revenue through the first four years[17] – will remain in the base rates). The density authority is designed to recover network costs and is calculated using a procedure whose inputs include growth in delivery points, volume changes, and the share of postal costs classified as institutional. Because year-over-year volume changes are not consistent, the result is that the size of the density factor fluctuates widely from year-to-year, ranging so far from a low of 0.583 percent to a high of 4.500 percent.[18] Both the retirement and density authorities were designed to allow the Postal Service to recover specific costs, which marked a return to cost-of-

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16 *See* Order No. 4257 at 171. These were accounting losses, not cash losses, because the Postal Service did not make the required prefunding payment in any year after FY 2010. After enactment of the PSRA, the Commission ordered the Postal Service to pay the sums recovered via the retirement authorities towards its remaining unfunded CSRS and FERS liabilities identified in 39 C.F.R. §3030.182. Order No. 6482, Docket No. ACR2022, at 11 (Apr. 3, 2023).

17 Calculated by multiplying the Market Dominant revenue by the additional retirement rate authority and then summing the annual results as found in FY23.Rate.Authorities.Workbook.xlsx, “Retirement Rate Authority” tab.

18 *See ANPRM* at 11, Table II-2.

service concepts and, by enabling direct recovery of those costs,[19] a shift away from the PAEA's emphasis on incentivizing the Postal Service to reduce costs.

The Commission also authorized the Service to raise rates for non-compensatory classes by an additional 2 percent. Finally, it adopted regulations governing the relationship of discounts and avoided costs in pricing of workshare discounts.

The Commission considered adopting a "service performance" mechanism but did not do so.[20] It subsequently commenced a new proceeding to examine performance incentive mechanisms to encourage increased efficiency, reduce costs, and maintain high quality service standards.[21] That proceeding subsequently was held in abeyance until being revived in June 2023,[22] and has now been merged into this docket.

It should be remembered that Order No. 5763 never purported to solve through rates alone what the Commission viewed as the Postal Service's financial instability. Instead, it had the more modest goal of putting the Postal Service on a "path" towards financial stability – a much different thing:

> Taken together, the modifications adopted in these final rules are designed to remedy the deficiencies in the existing ratemaking system….The modified ratemaking system is intended to balance the PAEA's statutory objectives in order to place the Postal Service on a sustainable financial path for the future.[23]

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19 The Commission described the density factor as intended to recover expected network costs in the short and medium term. Order No. 5763 at 93-94. That is a cost-of-service concept that reduces the incentive to lower costs, differing only in that it attempts to project costs forward rather than trying to recover past losses.

20 *See* Order No. 5763 at 258.

21 Order No. 5816, Docket No. RM2021-2 (Jan. 15, 2021), 86 *Fed. Reg*. 8330 (Feb. 5, 2021) ("*Advance Notice of Proposed Rulemaking Regarding Performance Incentive Mechanism").*

22 *See Order Reactivating Docket and Setting Comment Deadline*, Order No. 6537, Docket No. RM2021-2 (June 12, 2023).

23 Order No. 5763 at 24.

But the path was never intended to be solely revenue-funded. The Commission recognized that "Bridging the gap between revenue and expenses must be achieved through a combination of prudent pricing and operational decisions over time. To do otherwise would fail to achieve Objectives 1 and 2." Order No. 5763 at 347. Thus, the Commission warned the Postal Service not "to address its financial challenges solely by raising rates." *Id*. at 186.

By retaining a (modified) price cap, the Commission sought to encourage the Postal Service to increase net revenue by controlling costs. But it remained the task of the Service and its leadership to complete the job. That meant that the Postal Service had its own responsibility to control costs, improve productivity, and operate in the honest, efficient, and best practices manner expected by Congress.

C. The Postal Service's Results Under The Current System

The *ANPRM* asks whether the current system is achieving the statutory objectives, taking into account the factors. The place to start is the Postal Service's performance under the current system, which took effect in January 2021 and was first used in the rates that took effect in August 2021. The system has been in effect throughout Fiscal Years 2022 and 2023 and continues in place today, with preliminary financial results reported for two-thirds of FY 2024.

Results show the current system is not working as intended. Despite billions of dollars in additional revenues from the new rate authorities, the Postal Service's efficiency has not improved, its volume has fallen, it has lowered service standards, and is falling short of its financial promises. Not only has the new system failed to achieve the statutory Objectives 1, 3, 5, and 8, which it was intended to do, but it has led the Postal Service to fail to achieve other Objectives.

1. Revenues have increased by far less than rates

Since August 2021, when the first rates using the new authorities took effect, total Market Dominant revenue has increased, as Order No. 5763 presumably intended. However, the effects of the additional rate authorities – of which the Postal Service has used the maximum amounts at every opportunity[24] – on net incomes have been offset by plummeting volumes and collapsing productivity.

Despite repeated maximum rate increases that the *ANPRM* (at Table II-2) calculates totals more than 25 percent, the Postal Service's net increase in Market Dominant revenues has been only 4.4 percent since the new authorities took effect. That is the net result of unprecedented twice-a-year rate increases that cumulatively have far exceeded inflation or any increases under the previous system, including the exigent increase approved in Docket No. R2013-11.

The primary reason Market Dominant revenues have been so much less than the increases has been a stunning loss of Market Dominant volume, which is summarized below.

2. Net losses are increasing

[24] The Commission disclaimed that it was letting the Postal Service raise rates, stating that whether to use the additional rate authorities was up to the Governors' business judgment. Order No. 5763 at 270. Surprising no mailer, the Postal Service has used every bit of its authority on every occasion while claiming to be "judicious." This has resulted in the Commission recently pleading with the Service not to use the rate authorities that the Commission itself established. *See* Order No. 7155, Docket No. R2024-2, at 3 (May 30, 2024).

In FY 2023, the Postal Service reported a net loss of $6.5 billion in FY 2023. That loss exceeded the Postal Service's losses in most years under the former rate system. Some factors, such as workers compensation, the CSRS supplemental liability, and the FERS supplemental liability – which accounted for $4 billion of the Postal Service's net loss – are outside of the Service's direct control.[25] However, those costs are not part of and so do not explain the continued "controllable" losses that exceeded $2 billion.

In FY 2022, the first full year under the current system, the Postal Service reported a GAAP profit in FY 2022 due to legislative changes regarding retiree health benefit funding, but for that one-time forgiveness would otherwise have shown a loss from operations of about $950 million.[26] Even using the Postal Service's preferred measure of "Controllable (Loss) Income," it lost $0.5 million that year.[27] It also reported a loss of $4.9 billion in FY 2021. The Service's total loss would have been $4.4 billion more in FY 2022, and $1.4 billion more in FY 2023, had the Postal Service but for an interpretation of the PSRA that permitted the Postal Service to forgo accruing retiree health benefit normal costs ("RHBNC") while continuing to adjust its balance sheet to include those costs.[28]

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[25] The Postal Service does have some indirect control of these costs, at least over time, by managing the size of its workforce which gives rise to these obligations. Note that in economic cost terms, the Postal Service's loss was even greater than the accounting loss due to the omission of retiree health benefit normal costs.

[26] Office of Inspector General, *State of U.S. Postal Service Financial Condition*, Audit Report No. 23,-167-R24, at 1 (June 21, 2024) ("*OIG 2024 Report on USPS Financial Condition*") (noting that actual expenses exceeded expenses projections and actual revenue in both FY 2022 and FY 2023).

[27] United States Postal Service, *Form 10-K Fiscal Year 2022*, at 19 ("*USPS FY2022 Form 10-K*").

[28] *See* Order No. 6464, Docket No. RM2023-3 (Mar. 27, 2023). *See also USPS FY 2023 Form 10-K,* at 31. The retiree health benefit normal costs are included in the Postal Service's liabilities even though they do not flow through the income statement to do so.

These losses have occurred despite total revenue of $79.3 billion in FY 2023, $78.8 billion in FY 2022, and $77.1 billion in FY 2021. *USPS FY 2023 Annual Report to Congress* at 52. These were record revenues in their years.

The Postal Service expects a net loss of $6.3 billion in FY 2024 and a controllable loss of $0.8 billion.[29] As of the date of these comments, it appeared well on track to incur the predicted loss, or greater.

3. Volumes have declined

Since August 2021 (less than two months before FY 2022 began), when the first rates under the current system took effect, Market Dominant mail volumes have declined by 10.3 percent.

Looking solely at First-Class Mail Presort Letters, one of the Postal Service's most profitable category and one of principal concern to NPPC members, Figure 1 below shows the volume changes over the past five years:

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[29] *FY2024 IFP* at 1.

Figure 1—First-Class Mail Presort Letter Volume Since FY 2019

Fiscal Year	Volume (millions)	% Change
2019	35,207	
2020	34,167	-3.0%
2021	33,344	-2.4%
2022	32,170	-3.5%
2023	30,811	-4.2%

Source: Public CRA Reports

The volume declines accelerated in FY 2023. NPPC believes that a likely explanation for that is that business mailers by then had had time to adjust their mailing plans to the cumulative effects of price increases, as well as to the increased frequency of rate changes and the reduced service standards.[30] Total Market Dominant volume had fallen from 136,897 million pieces in FY 2019 to 120,372 million in FY 2022, and then more sharply in FY 2023 to 109,450 million.

The inverse relationship between volume and unit cost is illustrated by comparing the data for USPS Marketing Mail volumes reported in Figure 3. In FY 2022, Marketing Mail volume rose by 1.3 percent, while unit cost for the class declined (but note that the exclusion of RHBNC also reduced unit costs for that year). In contrast, in FY 2023, Marketing Mail volume fell by 11.4 percent while its unit cost rose by 12.1 percent, or 6.7 percent when adjusted for inflation.

What is genuinely alarming about these volume losses is that the Postal Service is losing business at a very high rate in the absence of any external shocks to the

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30 The Postal Service's price elasticity estimates are based on inflation-adjusted (or real) price changes. But mailers, particularly business mailers, respond in the short term to nominal increases as well, particularly in a period of relatively high inflation. Economists refer to this as "money illusion."

national economy. There is no Great Recession; there is no pandemic. Volume today is leaving due to the Postal Service's high pricing and poor service quality.

4. Productivity has declined

The Commission used Total Factor Productivity ("TFP") in Docket No. RM2017-3 as a metric to evaluate changes in efficiency. It concluded that as of 2017, "efficiency increased during the PAEA era" but that the pace of improvement had slowed. Order No. 4257 at 211 & 220. Unfortunately, in retrospect it appears that 2017 was the high watermark of postal labor productivity, and that one must go back to 2015 for the peak of TFP.

As discussed further below, the Postal Service's change in TFP in FY 2023 was negative 4.0 percent.[31] That was the worst TFP performance by the Postal Service since data have been reported beginning in 1963.[32]

When volume falls faster than costs decline, productivity suffers. The Postal Service's current inability to reduce labor hours to reflect volume drops as much as its cost analyses say that it should is causing productivity to decline.

D. Summary Of Recommendations

Under the current system, the Postal Service has shown itself unable either to increase or retain volume *or* to improve productivity to any reasonable extent. It has also

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31 Docket No. ACR2023, USPS-FY23-17, TFP Materials, FY2023 TFP Summary Tables (Public), "Workload & Input".

32 Docket No. ACR2023, USPS-FY23-17, TFP Materials, Table Annual 2023 (public).xlsx, "Tfp-52."

raised rates twice a year, reduced service standards,[33] largely failed to meet even those,[34] and suffered chronic unproductivity.[35]

A Market Dominant pricing system that produces an inefficient, high cost, and poorly performing Postal Service while losing large amounts of volume is clearly not achieving the statutory Objectives. As discussed below, the current system has not maximized the incentives to promote efficiency and cost reduction, has not maintained quality service standards, has failed to incentivize the cost savings necessary to sustain the system, and has not resulted in a just rate schedule. On the contrary, it has enabled excessive and multiple rate increases that have driven volume away and resulted in an unprecedented decline in productivity.

Accordingly, NPPC recommends that the system be modified as follows:

- Limit the Postal Service to no more than one Market Dominant rate adjustment per fiscal year;
- Eliminate the density factor;
- Impose an X-Factor to force the Postal Service to control its costs, coupled with a performance incentive mechanism that would allow it additional rate authority if it achieved pre-established metrics pertaining to volume, service performance, and productivity;
- Let expire (by its own terms) the retirement authority or, if this proceeding is complete before that authority is used for the fifth time, cease it, but going forward condition retention of the compounded total of all amounts collected by that authority on the Postal Service's continued making the required payments to the Treasury; and

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33 *See United States Postal Service Request for an Advisory Opinion on Changes in the Nature of Postal Services*, Docket No. N2021-1 (April 21, 2021) (First-Class Mail and Periodicals service standards) & *United States Postal Service Request for an Advisory Opinion on Changes in the Nature of Postal Services*, Docket No. N2022-2 (September 2, 2022) (Critical Entry Times for Periodicals).

34 *See* Service Performance Results - What we do - About.usps.com.

35 *See* Docket No. ACR2023, USPS-FY23-17, Table Annual 2023 (public).xlsx, "Tfp-52" tab.

- Improve the workshare discount rules to enhance efficiency.

These recommendations are discussed in more detail in Section IV below.

III. THE CURRENT SYSTEM FOR REGULATING THE RATES FOR MARKET DOMINANT MAIL IS NOT ACHIEVING THE STATUTORY OBJECTIVES

In Docket No. RM2017-3, the Commission construed each of the nine statutory Objectives, concluding that the system then in effect had failed to achieve Objectives 1 (maximizing incentives for efficiency), 3 (high quality service standards), 5 (financial stability), and 8 (just and reasonable rate schedule). It is evident that the revised system is not achieving these Objectives either, but also has caused other Objectives not to be met as well.

A. The Current System Is Not Maximizing Incentives To Reduce Cost And Increase Efficiency As Required By Objective 1

Objective 1 directs the Commission to design a system to "maximize incentives to reduce costs and increase efficiency," 39 U.S.C. §3622(b)(1). This Objective is to be applied in conjunction with the other Objectives, and indeed when properly applied should enable their achievement as well. There is absolutely no conflict between increasing efficiency and maintaining high quality service standards and sound finances. Efficient operations provide high quality performance.[36]

1. Postal Service productivity has declined and unit costs risen

It is difficult to conclude that the current system is maximizing the Postal Service's incentives to increase efficiency and productivity. Productivity has declined in each year

[36] An efficient business provides good service with sound operating margins. Efficiency in government operations is generally associated with good quality service at appropriate cost.

since the current rate system took effect, reaching the lowest on record only last year. And while the Postal Service frequently states that it has ample incentive to reduce its costs, whatever internally-driven incentive it may have appears inadequate.

In Docket No. RM2017-3, the Commission primarily used the change "in real unit market dominant attributable costs" to measure whether costs had declined. Order No. 4257 at 183-185. It also considered trends in the Postal Service's Total Factor Productivity. At that time, the Commission found that the attributable costs of market-dominant products had declined, along with volume, from FY 2007 to FY 2016. *Id*. at 190. It concluded that the Postal Service had been able to reduce costs and increase operational efficiency during the PAEA, but the results had been insufficient to achieve overall financial stability. *Id*. at 222.

NPPC has updated that analysis by calculating the real unit attributable cost (indexed to FY 2023) to examine trends since the Commission drew its conclusions in Order No. 4257. The table below uses Fiscal Years, not calendar years as did the Commission, so the numbers do not correspond directly. Note that the significant drop in unit cost in FY 2022 is due to the exclusion of retiree health benefit normal costs from being incurred.

Figure 2 presents the Postal Service's total costs, total costs attributed to Market Dominant products, unit costs for Market Dominant products, and Total Factor Productivity change as reported for the years 2019 through 2023.[37]

[37] FY 2019 was the last "normal" year under the former system. FY 2020 is included but that year was greatly affected by the COVID-19 pandemic. Its results, while accurate for that year, may distort the longer-term trends.

Figure 2—Total and Unit Costs and Market-Dominant Volumes (Real – Indexed to FY 2023)

Measure	FY '19	FY '20	FY '21	FY '22	FY '23
Total Costs (millions)	$95,209.8	$96,539.8	$92,969.5	$83,777.4	$85,802.0
Market-Dominant Total Costs (millions)	$34,333.1	$31,541.9	$30,904.8	$27,635.8	$26,441.8
Market-Dominant Volume (millions)	136,897	122,054	121,640	120,372	109,450
Market-Dominant Unit Cost	$0.251	$0.258	$0.254	$0.230	$0.242
Total Factor Productivity Change	-0.4	-1.1	0.6	-0.9	-4.0

Source: Public CRA Reports (indexed to FY 2023 using data from the Bureau of Labor Statistics) & USPS-FY23-17

Total Market Dominant costs have trended downward since FY 2019 in real terms, which one would expect given the loss of some 27.5 billion pieces of annual volume (20 percent) over that time. But the cost declines have not kept pace with the volume losses.

In FY 2023 alone, *despite the loss of nearly 9 percent of Market Dominant volume,*[38] real Market Dominant costs declined by only 4.3 percent (when compared to inflation-adjusted FY 2022 figure. Consequently, real Market Dominant *unit* costs rose by 5.2 percent in FY 2023 as shown in Figure 3, because the Postal Service has not captured the expected workhour and other savings.

[38] When adjusted for inflation, total Market Dominant attributable costs declined in FY 2023 but should have fallen by far more given the size of the volume loss.

Figure 3—Volume & Real Unit Cost for Major Market-Dominant Products FY 2021-FY 2023

Product	Measure	FY '21	FY '22	FY '23
Market-Dominant Mail	Volume (millions)	121,640	120,372	109,450
	YoY % Volume Δ		-1.0%	-9.1%
	Unit Cost	$0.254	$0.230	$0.242
	YoY % Unit Cost Δ		-9.6%	+5.2%
First-Class Mail Presort Letters	Volume (millions)	33,344	32,170	30,811
	YoY % Volume Δ		-3.5%	-4.2%
	Unit Cost	$0.164	$0.150	$0.161
	YoY % Unit Cost Δ		-8.1%	+7.0%
First-Class Mail	Volume (millions)	50,905	49,090	46,178
	YoY % Volume Δ		-3.6%	-5.9%
	Unit Cost	$0.271	$0.246	$0.254
	YoY % Unit Cost Δ		-8.9%	+3.2%
USPS Marketing Mail	Volume (millions)	66,236	67,121	59,449
	YoY % Volume Δ		+1.3%	-11.4%
	Unit Cost	$0.192	$0.175	$0.187
	YoY % Unit Cost Δ		-8.8%	+6.7%

Source: Public CRA Reports (costs indexed to FY 2023 using data from the Bureau of Labor Statistics)

As the Commission noted in Order No. 4257, real Market Dominant unit attributable costs declined from 2007 to 2017 before drifting back up. After 2017, those real costs continued to drift up until they reset in FY 2022 with the exclusion of RHBNC, but they resumed their rise in FY 2023.[39]

Looking at domestic First-Class Mail, the class of most interest to NPPC, real unit costs rose in FY 2023 both for the class and for Presort Letters, while volumes fell by about 6 percent and 4 percent, respectively:

[39] Although mail mix changes likely contributed to the reduction in FY 2022, had RHBNC been included, Market Dominant unit attributable costs very likely would the unit costs would have been about 4 cents higher and higher when compared to FY 2021.

Figure 4—FY 2023 First-Class Mail

	Total Costs	% Change	Unit Cost	% Change	Volume
Total FCM	$11,745	-2.9	$0.254	3.2	-6.1%
Presort Letters	$4,962	+2.5	$0.161	7.0	-4.2%

(Total costs in millions).[40] The attributable costs of First-Class Presort Letters costs increased substantially on both a total and a per-unit basis, while volumes fell by 4.2 percent.

Real Market Dominant unit costs have declined since FY 2019 by about 3.67 percent, a decline for which the exclusion of RHBNC is a major factor.[41] However, volumes fell far faster, by 20 percent over the same period. Looking only at FY 2023, although weighted mail volume fell by 8.1 percent in FY 2023,[42] workhours fell by only about 2.3 percent and unit costs increased.[43]

The Postal Service's inability to reduce workhours sufficiently in response to volume declines is responsible for much of the increase in Market Dominant unit costs in FY 2023. The reduced volume did reduce the total number of workhours, but the Postal Service captured far fewer workhour savings than it should have. In FY 2023, weighted

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40 Cost comparison is between FY 2023 data reported by the Postal Service in its Cost and Revenue Analysis filed with the *ACR* and the determinations as to FY 2022 data reported in the Commission's *Annual Compliance Determination Report FY2022 ("ACD FY2022")*. *Compare* Docket No. ACR2023, USPS-FY23-1, Public FY23CRAReport.xlsx, "Cost1 & Volume1" tabs *with* Docket No. ACR2022, USPS-FY22-1, Public_FY22CRAReport-UpdtedOrder6459.xlsx, "Cost1 & Volume 1 tabs (Mar. 29, 2023). Volume comparison is to Docket No. ACR2023, USPS-FY23-42, FY2023_RPWsummaryreport_public_ACR.xlsx. Total costs and unit cost figures have been adjusted for inflation using data from the Bureau of Labor Statistics.

41 Other factors include a shift in the mail mix from higher cost to lower cost products. For example, the share of the First Class mailstream consisting of the higher cost Single Piece Letters and Cards products has declined from 30 percent in FY2019 to 26 percent in FY2023, which the lower cost Presort Letters and Cards product now comprises 72 percent.

42 *See* Docket No. ACR2023, USPS-FY23-17, FY2023 TFP Summary Tables (Public).xlsx, "Workload & Input" tab.

43 *See USPS FY 2023 Form 10-K*, at 24.

mail volume fell by 8.1 percent,[44] but workhours fell by only about 2.3 percent.[45] Given the well-established volume variabilities, the Postal Service should have captured savings from a nearly 4.8 percent reduction in workhours (or nearly twice the workhour reduction seen).[46]

The OIG recently noted that although the Service's planners assumed that volume decreases "would result in a comparable decrease in work hours" but that "actual results show that work hours were not reduced at the same rate as volume."[47] While NPPC members greatly appreciate the jobs that postal workers, mail handlers and letter carriers do, the fact remains that labor costs account for about 70 percent of postal costs and the Postal Service must do a better job of managing its labor costs to be sustainable.[48] As the OIG notes: "the reduction in work hours did not align with the volume decline as assumed in the DFA plan."[49]

The Postal Service's inability to control workhours was a major factor in its TFP in FY 2023 of negative 4.0 percent.[50] As Figure 5 below shows, both TFP and labor

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[44] *See* Docket No. ACR2023, USPS-FY23-17, FY2023 TFP Summary Tables (Public).xlsx, "Workload & Input".

[45] *See USPS FY 2023 Form 10-K,* at 24.

[46] Calculated by multiplying the weighted mail volume change (decline of 8.1 percent) and the volume variability of personnel costs from the USPS-FY23-2, FY23Public+Cost+Segs+and+Comps.xlsx (53.4 percent).

[47] *OIG 2024 Report on Postal Service Financial Condition,* at 7 & 8.

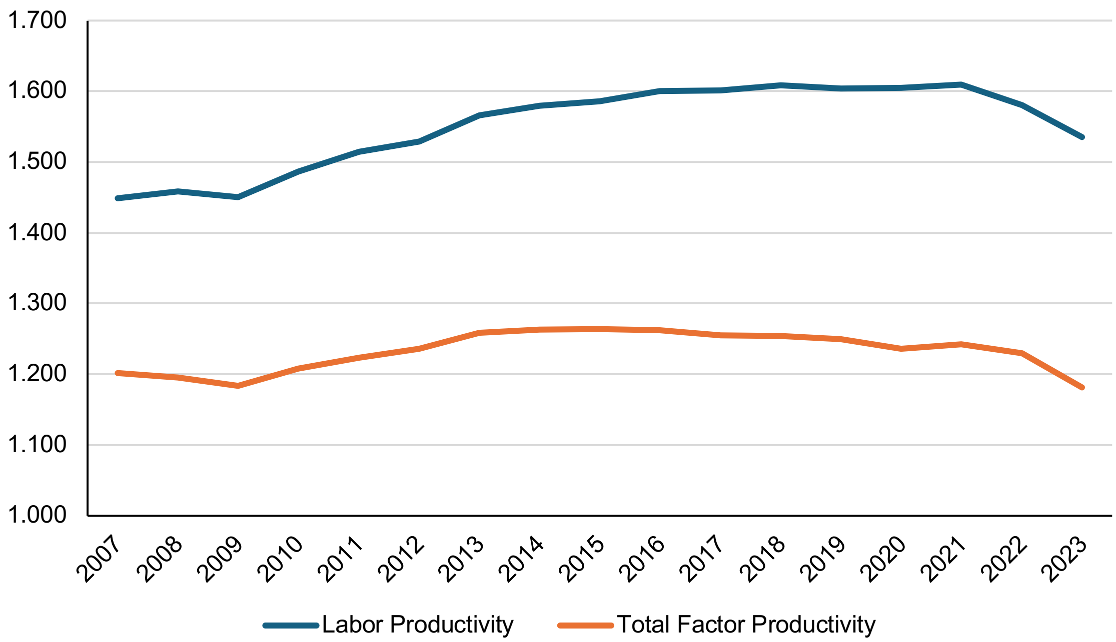
[48] *See USPS FY 2023 Form 10-K*, at 46.

[49] *OIG 2024 Report on USPS Financial Condition*, at 7.

[50] Docket No. ACR2023, USPS-FY23-17, TFP Materials, FY2023 TFP Summary Tables (Public), "Workload & Input" tab.

productivity have fallen sharply since FY 2021, the year when the new rate authorities were first used:

Figure 5—Labor Productivity and Total Factor Productivity (FY 2007 – FY 2023)[51]



Labor contributed a negative 2.1 percent and materials a negative 1.9 percent to TFP. Strikingly, the Postal Service's many capital investments appear to have had *zero* effect on TFP in FY 2023.[52] Although TFP is probably a more useful measure when viewed over time, the past five years show a downward trend. And that poor (un)productivity leads directly to higher unit costs.[53]

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[51] Docket No. ACR2023, USPS-FY23-17, Table Annual 2023 (public).xlsx, "Tfp-52" and "Tfp-53" tabs.

[52] *See* Docket No. ACR2023, USPS-FY23-17, FY2023 TFP Summary Tables (Public).xlsx, "Workload & Input" tab.

[53] *See* Docket No. ACR2023, USPS-FY23-17, Table Annual 2023 (public).xlsx, "Tfp-52" tab.

The declining productivity is an unintended consequence of the current system, under which the Service knows that it has an opportunity to recoup inefficiency through the density authority. With less pressure or incentive to reduce costs and increase efficiency, it is unsurprising that the Postal Service has grown even less efficient and seen costs rise even when adjusted for inflation. Therefore, the current system is not achieving Objective 1's goal of maximizing the incentives for efficiency and cost reduction.

2. Workshare discounts chronically understate most cost avoidances

Workshare discounts, when properly set, can promote postal efficiency and productivity by incentivizing mailers to engage in specified mail preparation or entry activities that they can perform more efficiently than the Postal Service, thus enabling the Service to reduce costs. In setting workshare discounts, the Commission has long adhered to the pricing policy of Efficient Component Pricing ("ECP").[54] Under ECP, the most efficiently priced discount is set at 100 percent of the costs avoided by the Postal Service. That sends the most accurate signal so that a mailer who can perform an activity at lower cost will do so. Conversely, when a mailer is unable to perform a task at a lower cost, it is more efficient for the entire postal system for the Postal Service to do that work. This is well understood and was first mentioned by the Postal Service in Docket No. R97-1: "The principle of Efficient Component Pricing (ECP) is that any

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[54] *See Second Opinion and Recommended Decision on Reconsideration*, Docket No. R2006-1, at 15 (May 26, 2007) ("ECP is a bedrock principle of the Commission's original opinion and recommended Decision.").

activity that can be performed by more than one agent should be performed by the most efficient (least cost agent)."[55]

In Docket No. RM2017-3, the Commission adopted regulations – found at 39 C.F.R. §§3030.280 *et seq.* – intended to establish more efficient passthroughs of avoided costs in workshare discounts. To summarize, and somewhat simplify, the Commission targeted discounts to be set at 100 percent of costs avoided, while accepting discount passthroughs of as low as 85 percent as sufficient. Discounts that passed through more than 100 percent of the avoided costs are considered excessive and must be reduced to closer to 100 percent unless an exception applies. Discounts with passthroughs less than 85 percent must be increased by at least 20 percent until that threshold is achieved, unless a specified exception applies.

For these purposes, the costs avoided are those found in the Commission's annual compliance determination most immediately preceding the filing of notice of the new rates. In practice, in each year since the rule's adoption the Postal Service has filed for a rate increase shortly after the Commission has issued an ACD for the preceding fiscal year. For example, in Docket No. R2024-2, filed on April 9, 2024, the Postal Service used the avoided costs determined in the ACD for FY 2023, issued by the Commission on March 28, 2024.

Unfortunately, despite the Part 284 regulations, workshare discounts today rarely set the efficient pricing signals that the Commission intends. That is because of the inherent – and under current rules unavoidable – mismatch between the time when the

[55] Docket No. R97-1, *United States Postal Service Direct Testimony of Peter Bernstein* (USPS-T-31), at 72 (July 10, 1997).

avoided costs are incurred and the time when actual discounts based on those costs are in effect. The mismatch consists of basing discounts for a future period (*e.g.*, in R2024-2, July 9, 2024, onward) on costs incurred during a 12-month period that ended on the previous September 30. This is shown by Figure 6 below:

Figure 6—Time Lag in Cost Avoidance Data

Docket No.	Filing Date	Cost Avoidance Calculation Period	Rates Effective	Time Lag from Cost Avoidance Period Mid-Point to Price Change Mid-Point
R2021-2	5/28/2021	FY 2020 ACR Oct 2019 – Sep 2020	Aug 2021 – Jul 2022	22 Months
R2022-1	4/6/2022	FY 2021 ACR Oct 2020 – Sep 2021	Jul 2022 – Jan 2023	18 Months
R2023-1	10/7/2022	FY 2021 ACR Oct 2020 – Sep 2021	Jan 2023 – Jul 2023	24 Months
R2023-2	4/10/2023	FY 2022 ACR Oct 2021 – Sep 2022	Jul 2023 – Jan 2024	18 Months
R2024-1	10/6/2023	FY 2022 ACR Oct 2021 – Sep 2022	Jan 2024 – Jul 2024	24 Months
R2024-2	4/9/2024	FY 2023 ACR Oct 2022 – Sep 2023	Jul 2024 – Jan 2025	18 Months
Est. R2025-1	Est. Oct 2024	FY 2023 ACR Oct 2022 – Sep 2023	Jan 2025 – Jul 2025	24 Months

Thus, for example, the discounts as of July 14, 2024, have been set using costs avoided averaged over the period October 1, 2022, through September 30, 2023, a period that ended more than nine months previously. This mismatch is well known. NPPC discussed it in its comments on the annual compliance report for 2021,[56] and the Commission discussed it in its Annual Compliance Determination for FY 2023.[57]

Unfortunately, the consequence of the mismatch between the earlier period over which the avoided costs are measured and the later period in which workshare discounts based on those costs are in effect is that the discounts far too frequently understate

56 *Comments of the National Postal Policy Council*, Docket No. ACR2021, at 2-6 (January 31, 2022).

57 *Annual Compliance Determination FY 2023*, at 16 (Mar. 28, 2024) ("*FY2023 ACD*").

avoided costs. This undermines the accuracy of the price signals and results in suboptimal worksharing that leads directly to excessive postal costs.

The Commission's recent Library Reference ACR2023-9 illustrates the problem. That library reference compared the discounts set in Docket No. R2024-1 (October 2023) to the avoided costs (incurred from October 2022 through September 2023). Those discounts were based on FY 2022 avoided costs – that were already more than a year old. Unsurprisingly, nine of the 16 discounts in First-Class Mail were found out of compliance with Part 284 because they passed through too little of the costs avoided; 23 of 30 in Periodicals; and 19 of 58 in Marketing Mail.[58]

In the *FY 2023 ACD* (at 16), the Commission took pains to explain that this, while regrettable, was consistent with current regulations:

> the Commission reiterates that at the time of approval in rate adjustment proceedings, Docket No. R2023-1 and Docket No. R2023-2, all workshare discounts in effect in FY 2023 complied with all workshare provisions, in accordance with 39 C.F.R. §§ 3030.282, 3030.283, 3030.284. *See* Figure II-2, *supra*. The Postal Service does not have the opportunity to bring workshare discounts that have fallen out of compliance with Commission regulations as a result of updated avoided costs filed in the FY 2023 ACR into compliance until the next rate adjustment proceeding. The Postal Service is required to do so at that time.

However, the Commission did not address the inefficient signals and unnecessary costs caused from using past cost data for future workshare discount prices. This distortion is particularly likely for workshare discounts that are based on avoiding mail processing costs, because those are labor costs that generally rise pursuant to wage agreements.

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[58] *See FY2023 ACD* at 18. A far smaller number of discounts were excessive (exceeded 100 percent of the costs avoided): two in First-Class mail and 15 of the 58 in Marketing Mail.

The magnitude of the inefficient signals due to this mismatch is significant. This is shown in detail in the attached Technical Appendix on which Figure 7 below is based.[59] Figure 6 shows, for First-Class and Marketing Mail Automation 5-Digit Letters, the annual growth rates in the avoided costs measured over the past 17 years (from FY 2007 to FY 2023):

Figure 7—Average Growth In Costs Avoided

Product	Measure	Annual Growth Rate	Mid-Point Lag (ACR Mid-Point to Price Increase Mid-Point)	
			July Rate Increase (18 Months)	January Rate Increase (24 Months)
First-Class Mail Automation 5-Digit Letters	Annual Growth Rate	4.6%	7.5%	9.6%
	Lower 95%	3.9%	6.3%	8.1%
	Upper 95%	5.3%	8.7%	11.1%
Marketing Mail Automation 5-Digit Letters	Annual Growth Rate	5.1%	8.4%	10.7%
	Lower 95%	4.5%	7.4%	9.4%
	Upper 95%	5.7%	9.5%	12.1%

This shows the change in costs avoided from the midpoint of the period over which they were measured to the midpoint of the period in which discounts based upon them took effect.

With these calculations, it is possible to calculate actual passthroughs for First-Class Mail 5-Digit Automation Letters and Marketing Mail 5-Digit Automation Letters, two of the most important workshare rates. Figure 8 shows actual passthroughs assuming a July and January price adjustment filing with reported passthroughs of 85, 90, 95 and 100 percent. (These calculations appear in the Technical Appendix.xlsx file on the “Figures 9 & 10” tab.) Of particular note, every workshare discount filed with a reported passthrough of less than 95 percent at the time of filing has an actual passthrough of

[59] This discussion focuses on presortation discounts. Destination entry discounts do not exist in First-Class Mail, which are the primary interest for NPPC.

less than 85 percent during its implementation period, which is below the permissible floor under current regulation.

Figure 8—Comparison of Reported Passthroughs at Filing & Actual Passthroughs During Implementation Period

Product	Reported Passthrough	Actual Passthrough July Filing	Actual Passthrough January Filing
First-Class Mail 5-Digit Automation Letters	85%	78.6%	76.8%
	90%	83.2%	81.4%
	95%	87.9%	85.9%
	100%	92.5%	90.4%
Marketing Mail 5-Digit Automation Letters	85%	77.9%	75.9%
	90%	82.4%	80.3%
	95%	87.0%	84.8%
	100%	91.6%	89.3%

Source: Appendix Supporting Data.xlsx, "Figures 9 & 10"

Furthermore, for presortation discounts set to pass through lower percentages, such as in the range of 85 to 90 percent, the actual passthrough likely would have been below the 85 percent minimum generally required by the Commission's rules.

This is not inconsequential. An inaccuracy of 8 or 10 percent in a workshare discount can drive substantial workshare activity. Inaccurate pricing of the presortation discounts (particularly when set inefficiently low) will cause more postal costs and harm the efficiency of the system. To the extent the Postal Service may believe that it does not capture the cost savings it expects from worksharing, this mismatch may provide an explanation.

In sum, although the current workshare discount rules are an improvement, insofar as no rules were in place to govern workshare discounts prior to Order No. 5763, they are not maximizing the incentives to increase efficiency and reduce cost through presortation because they set future discounts on costs avoided in the past. The result is that presortation discounts require readjustment in nearly every rate filing after an ACD is issued, and in most cases those adjustments must increase the discount because the passthroughs were too small.

B. The Current System Has Failed To Create Predictability And Stability In Rates As Required By Objective 2

Objective 2 directs the Commission to design a system to "create predictability and stability in rates." 39 U.S.C. §3622(b)(2). In Order No. 4257 (at 103), the Commission evaluated "predictability and stability" by looking at both "the timing and magnitude of rate changes." *Id*. at 143. The Commission concluded that the prior system, established in 2007 to implement the PAEA, had achieved the objective of predictability and stability. *Id.* at 143.[60] That is no longer true under the current system.

Predictability refers both to timing and to magnitude of rate changes. *See* Order No. 4257 at 4. Today, the requirement that the Postal Service file a schedule of anticipated rate changes enables mailers to predict the *timing* of rate changes but not their *magnitude*.[61]

Under the current system, wide fluctuations in magnitude have made rate changes unpredictable. Table II-2 of the *ANPRM* presents the rate authorities available and used by the Postal Service under the current system. For First-Class Mail, that Table reports that the Postal Service has raised rates by:

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[60] The Commission compared class-level rate increases to the annual change in CPI and found that most classes received average total price increases close to CPI. Order No. 4257 at 106. This was unsurprising; by law the prices were capped at CPI, which is publicly known, and therefore were both predictable and, because they were limited by inflation, stable.

[61] Sadly, the Postal Service's relentless quest to use all available rate authority has by now taught mailers that the Postal Service will impose the maximum allowed increase at every opportunity, but that is not what the statute means by predictable rate increases.

Docket	% Increase
R2021-2	6.814
R2022-1	6.500
R2023-1	4.202
R2023-2	5,378
R2024-1	1.961
R2024-2	7.755

Increases for individual rate categories have varied more widely. Increases for non-compensatory classes and products were even larger. And as the *ANPRM*'s Table II-2 shows, most of the fluctuation has been caused by the density authority, which has ranged from a high of 4.500 percent to a low of 0.583 percent.

In Order No. 4257 (at 102), the Commission stated:

> a system must include a limitation that is widely understood due to available information in order for the magnitude of price changes to be considered predictable and stable.

However, under the current system there is not sufficient available information that allows the magnitude of rate changes to be predictable. As the Commission knows, the wild card in rates is the density factor, which experience shows is not predictable, despite the Commission's expectation to the contrary. *See* Order No. 5763 at 311-316.

The details that feed into the density authority calculation – growth in delivery points, institutional costs, the proportion of costs that are institutional – are unknown to the mailing public until quite late in December – long past the time when business mailers have set their budgets. Even the Postal Service's filing of its calculations in late December are tentative until the Commission acts, usually in late March, and the Postal Service consistently has proposed new rates within only a few weeks thereafter.

In sum, under the current system, the magnitude of rate changes has been anything but stable or reasonably predictable. Unlike the former system, the current system does not achieve the Objective of predictable and stable rates.

C. The Current System Has Failed To Maintain High Quality Service Standards As Required By Objective 3

Objective 3 directs that the rate system should maintain high quality service standards. 39 U.S.C. §3622(b)(3). In Order No. 4257 (at 250), the Commission concluded that the system "does not effectively encourage the maintenance of high quality service standards." Unfortunately, the current system has not improved matters. In fact, the Postal Service has not "maintained" high quality service standards at all but has reduced service standards under the new system.[62] What's more, it has largely failed to meet even its watered-down standards.

The new system was adopted on November 30, 2020, and took effect in January 2021. Barely three months later, the Postal Service announced its intention to reduce the published service standards for First-Class Mail and for end-to-end Periodicals.[63] The Postal Service proceeded to implement that proposal despite reservations expressed in the Commission's Advisory Opinion.[64]

Only one year later, the Postal Service announced its plan to change the critical entry times for Periodicals, which effectively slowed delivery for large portions of

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62 This was not part of reducing service across the board. In contrast, the Postal Service upgraded the service standards for two Competitive products: Retail Ground and Parcel Select Ground. *See United States Postal Service's Request for an Advisory Opinion on Changes in the Nature of Postal Services*, Docket No. N2022-1 (March 21, 2022).

63 *United States Postal Service Request for an Advisory Opinion on Changes in the Nature of Postal Services*, Docket No. N2021-1 (April 21, 2021).

64 *Advisory Opinion on Service Changes Associated with First-Class Mail and Periodicals*, Docket No. N2021-1 (July 20, 2021).

Periodicals Mail.[65] Despite concerns expressed by the Commission,[66] the Postal Service implemented that proposal as well.

Not only has the Postal Service reduced service standards for these Market Dominant products, but it is largely failing to meet even the reduced service standards. Reviewing the Service's performance in FY 2023, the Commission concluded "service performance failures are ongoing and systemic problems rather than isolated events [are] causing accumulated failures." *ACD FY2023* at 88. The "value of the mail service actually provided" is a Factor which the Commission must consider. 39 U.S.C. §3622(c)(1). NPPC understands that the Postal Service says that its changes in network configuration, transportation, and delivery operations pursuant to the DFAP will also lead to improved service performance and reduced costs.[67] However, that has yet to occur and current trends are not encouraging.

Instead of maintaining high quality service standards, the Postal Service has lowered them yet has been unable to meet even those reduced hurdles. The current system is not achieving Objective 3.

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65 *United States Postal Service Request for an Advisory Opinion on Changes in the Nature of Postal Services*, Docket No. N2022-2 (September 2, 2022).

66 *Advisory Opinion on Changes to the Critical Entry Times for Certain Categories of Periodicals*, Docket No. N2022-2 (November 30, 2022).

67 *See, e.g., Responses of the United States Postal Service To Questions 1-6 of Chairman's Information Request No. 2*, Q1, Docket No. PI2023-4 (Aug. 22, 2023).

D. The Current System Has Allowed The Postal Service Pricing Flexibility

The Postal Service has enjoyed greater pricing flexibility since enactment of the PAEA. Order No. 5763 constrained that flexibility only slightly by imposing regulations governing workshare discounts, but the Commission correctly found that those were necessary to better achieve Objective 1. That conclusion remains valid today, although as noted above those regulations should be improved.

Since 2020, the Postal Service has exercised its pricing flexibility to introduce new offerings, change pricing design, experiment with and, on occasion, introduce new promotions and incentives. For example, in Docket No. R2023-3, the Postal Service introduced innovative volume incentives in First-Class and USPS Marketing Mail. In Docket No. R2024-2, it introduced both new promotions and a new base/design for promotions.

The one area in which the Postal Service remains excessively constrained is negotiated services agreements for Market Dominant domestic mail. Only one such agreement – that with Publisher's Clearing House – has been filed with the Commission in the 3½ years since the conclusion of Docket No. RM2017-3. Although approved, it was not implemented.[68] From NPPC's perspective, this is due less to a reluctance of the Postal Service to consider NSAs than to the Commission's continued application of an outdated test for NSAs that, whatever its merits in the 2000s, sets an extremely high bar for approval.

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[68] *Order Provisionally Adding Publisher's Clearing House Negotiated Service Agreement to the Market Dominant Product List and Directing the Postal Service To Collect and Report Data on a Monthly Basis*, Order No. 6813, Docket No. MC2023-222 (Nov. 22, 2023) (Order approving NSA) & *USPS Notice Regarding Implementation of Publisher's Clearing House NSA, In Response To Commission Order No. 6813*, Docket No. MC2023-222 (Jan. 17, 2024) (providing notice of non-implementation).

In contrast, one area in which the Postal Service has too much pricing discretion is in workshare discount pricing, which unnecessarily allow exceptions for discounts that passthrough less than 85 percent of the avoided costs

In sum, the current system provides the Postal Service with ample pricing flexibility for most purposes but could be improved.

E. The Market Dominant Rate System Has Had Little Effect On The Postal Service's Financial Stability

Objective 5 calls for the system to be designed to achieve, as one of nine goals to be applied in conjunction with one another, "adequate revenues, including retained earnings, to maintain financial stability." 39 U.S.C. §3622(b)(5). In Docket No. RM2017-3, the Commission concluded that awarding the Postal Service additional rate authorities, enabling it to raise rates above CPI levels, was necessary for the Service's financial stability.

The Postal Service has now applied the new rate authorities to the maximum extent in each of the four opportunities it has had to date. Yet the Postal Service has experienced continued, even accelerating, operating losses, losing greater sums than in previous years (including those under the former system) and falling well short of the goals of its operating plan.

The Commission recently summarized the Postal Service's finances succinctly:

> The Postal Service's financial position worsened in FY 2023. The organization record a net loss from operations of $2.3 billion, compared to a net loss of $473 million in FY 2022. The increase of $1.8 billion in the FY 2023 net operating loss is the result of a $2.1 billion increase in operating expenses. The increase in operating expenses occurred despite total mail volume decreasing by 9.7 percent, including a 2.0 percent decrease in the volume of Competitive products. The disconnect between workload and costs also resulted in a 4.0 percent decrease in Total Factor Productivity

> (TFP), the largest decrease in the measure of the Postal Service's efficiency since it was first calculated in 1965.

FY2023 Financial Analysis at 1. The Commission also noted that total revenue from Market Dominant products has fallen by 14.9 percent over the past ten years, as volume declines have more than offset price increases, but the Postal Service has reduced Market Dominant attributable costs over that time by only 9.7 percent. *Id*. at 45.

In contrast, the Postal Service's balance sheet has greatly improved since Docket No. RM2017-3. However, that was due to legislation, not the regulatory system. The largest single such action was the Postal Service Reform Act in 2022, in which Congress erased more than $56 billion of the Postal Service's accumulated unpaid obligation to prefund retiree health benefits and gave it additional relief from making retiree health benefit normal cost payments ($4 billion in recent years). Congress has also granted the Postal Service $10 billion in relief from the CARES Act and $3.0 billion earmarked for electric vehicles and supporting infrastructure in the Inflation Reduction Act.[69] The total of current and prospective relief is approximately $120 billion.

Financial performance under a price cap system requires cost control, operational efficiency, and enough volume to pay the bills. That is how Objectives 1, 3, 5, and 8 work together, and together enable the predictable price changes of Objective 2. But that is not happening under the current system, whose incentives have proven to be inadequate for encouraging volume or reducing costs aggressively. If anything, it creates disincentives to efficiency and productivity by allowing the Postal Service to raise rates to cover its inefficiency and poor productivity.

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[69] Pub. L. 117-169, §70002 (Aug. 6, 2022).

In effect, the current system has allowed the Postal Service to operate under an after-the-fact cost-of-service regulation. That has restored the worst feature of cost-of-service regulation – the lack of real incentive to reduce costs and improve productivity. It also dampens the incentive to encourage volume – as more pieces would improve productivity and more business – because the Service knows it can simply impose above-inflation rate increases on the pieces that remain in the system.

1. Causes Of The Postal Service's Operating Losses

The Commission's financial analysis provides a more detailed analysis of the Postal Service's operating losses. It notes that in FY 2023, the Postal Service's total operating revenue was $78.4 billion, which was down by $2.2 billion from FY 2022. *FY2023 Financial Analysis* at 3. Revenue from Market Dominant products declined by $0.4 billion despite above-inflation rate increases that were more than 10 percent higher than in the preceding year.

The revenue decline was due primarily to the precipitous loss of volume.[70] But revenue was not the cause of the Postal Service's net operating loss. Instead, the Postal Service has a cost problem.

This is evident from the total operating expenses, which at $81.2 billion were $2.1 billion higher than in FY 2022. *Id*. at 3. And this occurred while total mail and services volume fell by 8.7 percent. *Id*. at 90. The Commission has concluded that the increase in operating expenses "was largely caused by increases in compensation and other expenses, partially offset by the decline in purchased transportation." *Id*. at 8.

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70 Changes in the mail mix and in levels of worksharing can also play a role, but the magnitude of the volume decline overshadows those effects. *See FY2023 Financial Analysis* at 10, Figure II-1.

Looking only at Market Dominant products, attributable costs rose 1.1 percent, despite a reduction in revenues from Market Dominant mail (*id*. at 9, table II-20) and a 9.1 percent decline in volume. *Id*. at 42, Table III-1 & 90. Market-dominant attributable costs rose despite that enormous volume decline. The Office of the Inspector General recently reaffirmed that it is "imperative that the Postal Service reduce its work hours in sync with volume declines, to save labor costs and ensure it is operating efficiently."[71]

Despite, or perhaps because of, the additional rate authorities, the Postal Service has incurred growing operational and total losses because it has been unable either to control its spending or increase its business volume. The negative 4.0 percent change in its Total Factor Productivity shows that, despite paying more in factor inputs and making capital investments, while enjoying substantial relief from Congress on both operational expenses (retiree health benefit normal costs) and the balance sheet, the Service has not demonstrated an ability to operate within its means.

2. The Commission's Docket No. RM2017-3 Approach

Although not necessarily agreeing with the analytic approach used in Order No. 4257, NPPC will apply it here – now more than six and ½ years after the Commission concluded that Objective 5 was not being achieved – for consistency. In that review, the Commission interpreted Objective 5 by applying a framework of what it termed short term, medium term, and long-term stability. The Commission defined these terms as:

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[71] *OIG 2024 Report on Postal Service Financial Condition* at 8.

- Short-term: operating profit[72] plus available borrowing authority and end-of-year cash reserves (Order No. 4257 at 159-160);
- Medium-term: net income = total revenue minus (attributable cost + institutional cost) plus borrowing authority; Order No. 4257 at 165;
- Long-term = sufficient net income to generate retained earnings.

After reviewing postal data from 2007 through 2016, the Commission concluded that the original system had allowed the Postal Service to maintain short-term financial stability. Order No. 4257 at 165. Similarly, the Commission reviewed postal financial data from 2007 through 2016 and concluded that the Postal Service had incurred a net loss in every year, and thus had not maintained medium-term financial stability. *Id*. at 168-169. Finally, the Commission concluded that because the Service had a retained earnings deficit of $59.1 billion, long-term financial stability also was not maintained. *Id*. at 171, Table II-12. That calculation was simply the sum of the Postal Service's capital as of 2006, from which it subtracted each year's cumulative annual net incomes (losses).

Relying on the medium- and long-term findings, the Commission concluded that Objective 5 had not been achieved.[73] However, the Commission acknowledged that $54.8 billion of the accumulated deficit consisted of unpaid retiree health benefit prefunding obligations. *Id*. at 171. That deficit continued to grow until Congress repealed that obligation in 2022, erasing $57 billion from the Postal Service's deficit.

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[72] The Commission defined "operating profit" as operating revenue (from mailing products) minus operating expenses (i.e., total costs minus RHBF accruals, noncash workers' compensation, supplemental contribution to FERS and interest expense). Order No. 4257 at 161, Table II-6.

[73] Although the Commission based its conclusion on the three-part analysis, it also reviewed the Postal Service's working capital, capital expenditures, and debt ratios, which it found supported its conclusions. Order No. 4257 at 172-175.

This proceeding is the first in which the Commission is revisiting its findings since that repeal.

3. The Postal Service's current financial condition

In FY 2023, the Postal Service had $79.324 billion in total revenue, which when combined with its cash on hand and available borrowing authority exceeded its total costs of $86.802 billion. *See* Docket No. ACD FY2023, *PRC-LR-1 Product Finances*, "Total All Mail" & *United States Postal Service Fiscal Year 2023 Annual Report to Congress*, at 29.[74] Applying the Commission's Docket No. RM2017-3 analysis, it is evident that the Postal Service continues to achieve short-term financial stability, as its operating revenues plus available cash and borrowing authority easily exceed its operating expenses. The Postal Service also achieved medium-term financial stability in FY 2023 (and FY 2022) because its total revenue plus borrowing authority exceeded the sum of its attributable cost and institutional costs.

Although the Postal Service has not yet generated retained earnings,[75] Congressional action has greatly improved the balance sheet since 2017, when Order No. 4257 was adopted, and 2020, when Order No. 5763 was adopted. Most importantly, Congress eliminated the retiree obligation that was the principal factor driving the

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[74] In FY 2022, the Postal Service had a positive net income of $56 billion due to the repeal of the retiree health benefit prefunding obligation. *USPS FY2022 Form 10-K* at 45. At year end, it had $23.6 billion in cash or cash equivalents on hand. *See United States Postal Service Fiscal Year 2024 Integrated Financial Plan*, at 5.

[75] The Postal Service has acknowledged that retained earnings are not guaranteed by the law. See Reply Comments of the United States Postal Service, Docket No. RM2021-2, at 9 (Oct. 15, 2023). The Postal Service is also correct that retained earnings should be achievable. NPPC submits that retained earnings are achievable if the rate system gives the Postal Service the proper incentives to control its operating costs and focus on improving service. Cost control – and better service to make its offerings more attractive – are what is needed, not simply raising rates.

Commission's concerns in Docket No. RM2017-3. Going forward, the Service could improve its finances if it renews its focus on volume, service, and productivity. That is the path to retained earnings.

And that is without considering other factors relevant to the Postal Service's long-term financial stability. In particular, the Postal Service's balance sheet would be even stronger if included the market value of its real estate, although GAAP principles do not allow it to do so.[76] However, the Postal Service uses non-GAAP measures (such as "Controllable Income") when it suits its own purposes, and the Commission should not blind itself to that value. Indeed, there is more reason for the Commission to consider real estate values now, because the DFAP may allow the Postal Service to eliminate unneeded real estate holdings throughout the nation. Selling surplus real estate should improve the balance sheet. Congress has already determined that, in the unlikely event the Postal Service were to cease operations, proceeds from selling its real estate would fund employee obligations.[77] The real estate plainly has value that can offset Postal Service obligations.

Another consideration is whether the Postal Service will have sufficient funds with which to make appropriate capital investments going forward. Although the DFAP calls for some $40 billion in capital investment, which in total may or may not be necessary,

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[76] The Commission expressly declined to consider the market value of the Postal Service's real estate holdings, citing GAAP. Order No. 4257 at 155. However, even the real estate carried on the Postal Service's books has a net depreciated value of more than $16 billion. The market value of older properties can reasonably be expected to be several times that amount.

[77] *See* 39 U.S.C. §2903; see also 39 U.S.C. §2992 (regarding prudent property management and the potential sale of unneeded real property).

the investments made or committed to date are being spread over time[78] and well within the Postal Service's ability to manage given its cash position of $8.1 billion,[79] $2 billion in borrowing authority,[80] and the stream of revenue from ongoing operations.

In short, the Postal Service is in a better financial position than in 2017 or 2020. That improvement has come thanks to Congress, which forgave the defaulted RHB prefunding payments, erased the obligation to prefund going forward, and appropriated $10 billion in COIVD funding plus $3 billion for energy-efficient vehicles.[81]

In contrast, the rate system cannot be credited with improving the income statement. The higher rates allowed by the current rate system have been almost entirely offset by volume losses and declining productivity. The system has failed to incentivize sufficiently the Postal Service to get better control of its costs, to increase volume to spread the institutional costs of the system over more pieces, or to improve productivity – necessary steps for financial stability.

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78 *Compare* DFAP at 48 *with* the capital spending cash outlays from the Postal Services Integrated Financial Plans:

Category	Capital Investments – Cash Outlays (billions)			
	FY 21	**FY 22**	**FY 23**	**FY 24 (Proj.)**
Facilities	$0.8	$0.6	$1.0	$1.0
Processing Equipment	$0.5	$0.6	$1.1	$0.2
Vehicles	$0.5	$0.4	$0.7	$1.6
IT, Postal Support Equipment & Other	$0.1	$0.2	$0.3	$0.4
Total	**$1.9**	**$1.8**	**$3.0**	**$3.2**

Sources: Fiscal Year 2022 Integrated Financial Plan, at 7; Fiscal Year 2024 Integrated Financial Plant, at 4.

79 *USPS FY2023 Form 10-K*, at 47.

80 *Id.*, at 57.

81 In Order No. 4257 (at 180), the Commission considered the retiree health benefit prefunding payment "a statutory obligation that must be considered in analyzing the Market Dominant ratemaking system's success and includes RHBF as an additional consideration where relevant." It follows that the repeal of the RHB prefunding obligation similarly must be considered today when assessing the system.

Although important, Objective 5 is only one of nine important objectives with which it is to be applied in conjunction. Experience has shown that raising rates by far more than inflation on a dwindling volume of mail has not achieved, and is not likely to achieve, Objective 5, and a new approach is needed.

F. The Current System Has Had A Neutral Effect On The Administrative Burden But Has Decreased The Transparency Of The Ratemaking Process

In Docket No. RM2017-3, the Commission found that the then-current system had reduced the administrative burden and increased the transparency of the ratesetting system. Order No. 4257 at 143. That was a consequence of the changes wrought by the PAEA.

Today, the Postal Service's rate adjustment filings provide the minimum information required. In that sense, therefore, the current system may be said to reduce administrative burdens compared to the former cost-of-service regime. Instead, much of the burden associated with the former rate cases has merely been shifted to the annual compliance review process.

But the rate system today is less transparent. There is no requirement that the Postal Service provide any explanation of its goals, objectives, or any other information that would allow mailers insight into the Postal Service's pricing strategy.

Nor is there any obligation for the Postal Service to explain how proposed new rates comport with the statutory Objectives and Factors. The Commission eliminated that obligation in Order No. 5763 by deeming any rates that satisfy the system automatically to satisfy all the Objectives and Factors as well on the theory that the system itself satisfies the Objectives. Order No. 5763 at 256 ("review for consistency with the objectives and factors is unnecessary in individual rate adjustments under the Commission's modified system, which already takes account of the objectives and factors"); *see also* 39 C.F.R. §3030.1226(j).[82]

As a result, the rate system today requires the Postal Service to provide minimal information and has eliminated any need for the Postal Service to explain how its rate proposals comply with the statute; it need merely notice rates that comply with the system. There is no discussion of how particular rates advance the Objectives or serve the Factors. Thus, the current system is less transparent than previously.

G. The Current System Has Had No Discernible Effect On Mail Security Or Deterring Terrorism

The Commission concluded in Docket No. RM2017-3 that the rate system had achieved Objective 7 because the Postal Service has had adequate funds to maintain safeguards and provide for specific as well as unforeseen security situations. Order No. 4257 at 238. That conclusion remains valid today, as the Postal Service has ample funds available were a need to arise.

H. The Current System Has Not Established A Just And Reasonable Schedule For Rates And Classifications

Objective 8 calls for a just and reasonable schedule of rates and classifications. In Docket No. RM2017-3, the Commission stated that

> for rates to be "just and reasonable" they must be neither *excessive to the mailer* nor threaten the financial integrity of the Postal Service.

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[82] NPPC respectfully disagrees with this approach, which essentially reduces Market Dominant rate adjustment reviews to a mathematical exercise in which the actual rates are not evaluated under the statutory criteria. The treatment of this issue in Order No. 5763 may in retrospect have been an overreaction to the decision in *Carlson v. Postal Regulatory Commission*, 938 F.3d 337 (D.C. Cir. 2019).

Order No. 4257 at 113, n.213 (emphasis added). The Commission has evaluated the justness of rates by whether they are "excessive to the mailer." *Id*. at 116 & 230.

In that proceeding, the Commission reviewed "price increases during the PAEA era" and found that they were not excessive. Order No. 4257 at 118. This conclusion was effectively compelled by the law because the rates during the PAEA era to that time had been capped at inflation (except for a comparatively brief period when an exigent surcharge was in effect). But an approach that deems rates not excessive because they did not exceed a pre-set legal maximum level tied to a common measure for price increases is simply circular. The Commission assumed that the rates in effect when PAEA was enacted were reasonable, and that if rate increases thereafter remained at inflation, then they too were reasonable.

The Commission has not, until this proceeding, reviewed whether rates have been "just" – that is, not excessive – under the new regime. It may not simply conclude in this proceeding, as it did in Docket No, RM2017-3, that rates that were the maximum allowed are just, because to do so would ignore both whether mailers found them excessive and that the limit on prices today is far higher than inflation.

As the *ANPRM* states (at 18, Figure II-1), the current system has produced large compounded rate increases since August 2021:

Authorities	**Aug 2021**	**Jul 2022**	**Jan 2023**	**Jul 2023**	**Jan 2024**	**Jul 2024**	**Avg. Annual**	**Compounded Increase**
CPI	1.244%	5.135%	4.200%	3.406%	1.959%	1.622%	5.921%	18.835%
Density & Retirement	5.562%	1.368%	N/A	1.972%	N/A	6.132%	5.014%	15.807%
Compensatory Total	6.806%	6.503%	4.200%	5.378%	1.959%	7.755%	11.125 %	37.225%
Non-compensatory Total	8.806%	8.503%	4.200%	7.378%	1.959%	9.755%	13.914 %	47.818%

In short, in less than three years First-Class and USPS Marketing Mail have experienced compounded rate increases of about 37 percent. For Periodicals, catalogs and products deemed non-compensatory, the increase is nearly 50 percent.

The cost coverage of every First-Class Mail product has risen each year under the current system. *ACD FY23* at 49, Table III-8. This suggests that rates are even less connected to costs than before. Cost coverages for other Market Dominant classes have increased as well, despite some misleading dips in FY 2022 due to the exclusion of RHBNC in that year. *See id.*, Table III-7 (Marketing Mail)

But the clearest evidence that mailers have found rates under the current system to be excessive has been their actions – voting with their feet. Since rates under the current system took effect near the end of FY 2021, mail has abandoned the system at an accelerated rate:

Figure 9—Rates of Volume Decline

Product	Measure	FY '21	FY '22	FY '23
First-Class Mail Presort Letters	(millions)	33,344	32,170	30,811
	YoY % Volume Δ		-3.5%	-4.2%
First-Class Mail	Volume (millions)	50,905	49,090	46,178
	YoY % Volume Δ	-	-3.6%	-5.9%
Market Dominant Mail	Volume (millions)	121,640	120,372	109,450
	YoY % Volume Δ		-1.0%	-9.1%

First-Class Single Piece volume has disappeared more rapidly than Presort Mail.

The story is similar in USPS Marketing Mail. In FY 2023, Marketing Mail Letters volume fell 12.72 percent from 43.682 billion in FY 2022 to 38.126 billion.[83] That resulted in a decline in revenue from $10.24 billion in FY 2022 to $9.51 billion in FY

83 *Compare FY2022 Financial Analysis, Appendix A with FY2023 Financial Analysis*, at Table A-1.

2023.[84] Although the loss of volume had the effect of reducing the product's total attributable costs, it did so only by about $75.7 million.[85] That 1.4 percent reduction in total costs pales in comparison to the 12.72 percent volume loss, resulting in a net *increase* in unit attributable costs of 13 percent that simply should not have happened.

By leaving the system, former mailers of billions of pieces of mail have made a statement that current prices are excessive. The effect of rate increases on the public and business mailers is a Factor that the Commission is to consider. *See* 39 U.S.C. §3622(c)(3). That indicates that the current system is not producing "just" rates. In short, many (former) mailers consider the postal product now being offered not to be worth the greatly high price.

As for "reasonable," the Commission stated:

> The Commission finds that rates do not threaten the financial integrity of the Postal Service and are reasonable under Objective 8 if market dominant products as a whole are able to make a positive contribution to institutional costs and if each product and class, at a minimum, covers its attributable costs.

Under both the prior system and the current system, Market Dominant products have made a positive contribution to institutional costs. With a few exceptions, each product and class has covered its institutional costs.[86] That the Postal Service overall may have incurred operating deficits is not the fault of Market Dominant products, nor should Market Dominant products have to pay still more to cover those deficits for which they

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[84] *Id*.

[85] *Id*.

[86] Periodicals class remains non-compensatory. Some individual products remain non-compensatory as well. In each case, the problem is cost (mostly Flats mail).

are not responsible. Instead, the Postal Service should look to increase Market Dominant volume, expand Competitive revenues, and reduce costs more aggressively.

In sum, the current system has not maintained a just rate schedule. Although Market Dominant revenues more than cover Market Dominant costs and make a positive contribution to institutional costs, the continuing departure of mail shows that rates under current system are not just, but that mailers consider them excessive for the value and service provided.

I. The Current System Allocates Institutional Costs Appropriately Between The Market-Dominant And Competitive Categories Of Mail As Required By Objective 9

The current system allocates institutional costs pursuant to 39 U.S.C. § 3633. In recent years, Competitive products have easily covered their minimum contribution. NPPC supports the current allocation method and believes it appropriately allocates institutional costs between the Market Dominant and Competitive categories

IV. THE CURRENT RATEMAKING SYSTEM SHOULD BE MODIFIED

The Commission may not simply assume that its findings and conclusions from Docket No. RM2017-3, which were made in 2017 (Order No. 4257) and 2020 (Order No. 5763), remain valid today, nearly seven years later. A regulatory agency is legally obligated to reconsider its conclusions in light of significantly changed circumstances to determine whether a different conclusion is warranted. *E.g., United States Sugar Corp. v. Environmental Protection Agency*, 830 F.3d 579, 606 (D.C. Cir. 2016). Beyond the obligation to reconsider its prior rulings when circumstances have materially changed, the Commission also has independent authority to modify the ratemaking system under Section 3622(a) and 3622(d)(3).

Here, circumstances have changed significantly, both by legislation and operational realities. Since the Commission reached its conclusions in Order No. 4257, Congress has enacted four laws that have transformed the Postal Service's legal and financial landscape. These include the CARES Act,[87] the Consolidated Appropriations Act of 2021, the Inflation Reduction Act (which gave the Postal Service $3 billion to purchase e-vehicles), and the Postal Service Reform Act.

Operationally, the Postal Service has experienced an unprecedented exodus of mail from the postal system as prices and costs have soared and service has been poor. Today, the current system is failing to achieve many of the statutory Objectives.

In modifying the system, the Commission's responsibility is to apply the law as intended by Congress. As explained in Section B below, the Commission has no obligation to design a rate system, or create additional rate authorities, to fund the Delivering for America Plan or any other Postal Service operating plan.

What the Commission does have an obligation to do is to revise the current system to better achieve the statutory Objectives. Section C below sets forth specific proposals to do so.

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[87] Coronavirus Aid, Relief, and Economic Security Act, Pub. L. 116-136 (Mar. 27, 2020). The Commission stated that the CARES Act did not affect its decisions in Order No. 5763. See Order No. 5763 at 29-30 & 338; *see also* Order No. 5818, at 23 (Jan. 19, 2021) (Order Denying Stay). In that Order, the Commission stated that the $10 billion provided to the Postal Service by the Congress did not affect its analysis because it was limited to short-term operating needs and was irrelevant to its medium- and long-term financial stability. However, Congress removed that limitation in December 2020 by repealing the obligation that the Service repay that sum, converting it into a capital contribution. *See* Consolidated Appropriations Act of 2021, Pub. L. 116-260, §801 (Dec. 27, 2020).

A. The Current System Is Failing To Achieve Many Objectives, Including Those Of Maximizing Incentives For Cost Reductions And Efficiency And For Predictable, Stable, and Just Rates

Section 3622(b) directs the Commission to consider the nine Objectives "in conjunction with the others." 39 U.S.C. §3622(b). From the foregoing, it is evident that the current system for regulating the rates for Market Dominant postal products is failing to achieve a proper balance among the Objectives established by Congress.

As discussed in the preceding section, the Postal Service's performance over the past three years demonstrates that the current system:

- Does not maximize incentives to reduce costs and increase efficiency;
- Does not create predictable and stable rates;
- Has not preserved high quality service standards, not has the Postal Service even met most of its reduced targets;
- Has resulted in rates that have led to volume losses that threaten the financial sustainability of the postal system;
- Has not increased the transparency of the ratemaking process; and
- Has not maintained just Market Dominant rates.

To the extent to which the Postal Service's financial condition is improved, that is largely due to Congress's repeal of the prefunding obligation. Despite higher rates, Market Dominant revenues are stagnating as mail increasingly leaves the system, which threatens its long-term sustainability.

There are several explanations for the failure of the current system. Most importantly, the Postal Service simply is not operating as efficiently as it can or should. That is a management issue. The Postal Service has not adequately managed its costs. Indeed, postal costs have trended in the way that they might have under cost-of-service regulation had the latter been in effect during a period of volume decline.

Nor has the Postal Service taken many steps to retain or increase the volume of Market Dominant mail over which its institutional costs may be spread. It is evident that volume losses of 10 percent or more in a single year will result in great unproductivity, but the Postal Service has not tried to stem those volume declines through lower rates.

Indeed, the current system undermines the goal of improving volume. The problem is that the density authority weakens the incentives built into the price cap structure by assuring the Postal Service that it can raise rates to cover the rise in per-unit network costs as volume falls. And while the density factor has accounted for approximately $4.6 billion in postal revenue over the past few years, it has done nothing to encourage the Postal Service to control the network costs it is intended to recover. Instead, by contributing to soaring rates, it is causing letter, card, and flat mail to leave the system. This is turn contributes to the decline in productivity, because the Postal Service has not offset volume losses of that magnitude with cost reductions. This is, in fact, the death spiral that mailers have warned about.

Nor has the current system led to predictable and stable rates. Indeed, it has lost ground on Objective 2, as the former system had provided predictable and stable rates. Today, rates are “predictable” insofar as they can be expected to rise every six months, but the amount of the first increases after issuance of an Annual Compliance Determination certainly are not predictable to business mailers when setting their budgets, which occurs in the preceding calendar year. And the wide range of large increases experienced in the last three years shows that rates certainly are not stable.

As for service, the Postal Service has twice lowered service standards under the current system. It unilaterally sets even more modest “targets” for itself and in most instances fails to meet even those.

The current system is less transparent than pre-2021. Mailers remain in the dark about the Postal Service’s pricing strategy and never receive a long-range projection of how the Service intends to use prices to attain particular results. Nor is there now ever any discussion about how adjusted rates are supposed to better achieve the Objectives established by the PAEA.

Finally, the exorbitant rate increases have not resulted in just rates. Mailers have left the system at unprecedented rates in recent years in response to the combination of high rates and poor service. The loss of volume in turn threatens the sustainability of the network.

Although the Postal Service’s demand models play little specific role in the current Market Dominant rate system, it is fair to wonder whether the current models should measure the demand responses to nominal price and other factors. Not only do the current models rely heavily on trend and intervention variables that lack economic meaning, but the accuracy of the estimated price elasticities is subject to question. For the years in which CPI was the sole cap, the Service’s use of real inflation rates meant that inflation was, in effect, zero. But business mailer budgets are based on nominal dollars, not inflation-adjusted ones, so it is not clear that the Postal Service’s demand models accurately reflect mailer behavior. Couple that to the reliance on trend and intervention variables and there is serious doubt whether the Service’s current models are based on the correct inputs. After all, if mailers perceive service to be of diminished quality, their demand will decline irrespective of price.

The accuracy of demand models matters because the Postal Service would be much better off if it could retain and increase the value of Market Dominant mail, particularly in First-Class Mail – its most profitable product.[88] Any business knows that it is far easier to retain volume than it is to regain volume. Today, First-Class Mail that leaves the system is lost for good. Thus, the loss of a piece of mail in Year 1 costs the Postal Service revenue not only in Year 1, but in the following years as well.

For these reasons, the current system should be modified as described in section C below.

B. The Commission Has No Obligation To Fund Whatever Strategic Plan The Postal Service Is Following

The Postal Service's decisions since 2021 have been based on a strategic plan it calls the Delivering for America Plan. To date, the financial results are well behind schedule, and it may take years until breakeven – once projected for FY 2023, but wildly missed – will occur. The Postal Service consistently cites the DFAP as the justification for its spending, service reduction, and other actions.

Despite having reservations about aspects of the DFAP and its implementation, NPPC is pleased that the Postal Service has a strategic plan. But it is vital to recognize that the Commission is not obligated to fund the Delivering for America Plan or any other

[88] The extent to which the Postal Service relies on its demand models when setting Market Dominant rates is unknown to mailers. No Commission regulation requires it to explain whether, and if so how, the demand models are used, and the Service does not volunteer that information.

plan, nor does the Commission have any statutory obligation to defer to the Governors on the amount of money to be collected from Market Dominant mail.

More particularly, the amount of revenue needed to achieve "financial stability" as set forth in Section 3622(b) is not a matter vested in the Governors or postal management to decide. The Governors' power to set a revenue requirement that the Commission must satisfy was abolished by the PAEA when it replaced rate of return regulation with a price cap. Section 3622 – in which the objective of financial stability appears – is subject to the authority of the *Commission* to interpret and implement, not the Postal Service or its Governors. The Governors cannot simply spend money and expect the Commission to grant sufficient rate authority to cover the costs. The PAEA repealed that regime.

Section 404(b) of the postal law states:

> Except as otherwise provided, the Governors are authorized to establish reasonable and equitable classes of mail and reasonable and equitable rates of postage and fees for postal services *in accordance with the provisions of chapter 36*. Postal rates and fees shall be reasonable and equitable and sufficient 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. §404(b). For this discussion, the important phrase is "in accordance with the provisions of chapter 36." Chapter 36 contains Section 3622, which the Commission has the authority to interpret.

Chapter 3622 also contained the price cap structure created by Congress. For Market Dominant products, Congress limited rate increases to CPI (measured over a class). The Commission has retained that structure, as rate adjustments for Market Dominant products remain subject to a limitation on how much those rates can rise. This is true even though the rate authorities added in Order No. 5763 weakened that constraint by allowing that the Postal Service to recover certain retirement and density costs without having to improve efficiency, volume or service.

But under the PAEA structure, which Congress left untouched in the PSRA, the Governors cannot simply spend money and expect the Commission to grant sufficient Market Dominant rate increases to cover the costs. That would be a return to cost-of-service regulation. Indeed, such a system would be inferior to that under the former Postal Reorganization Act because the Postal Service would set both the revenue requirement *and* specific rates. Were the Commission to do so it would be unilaterally shedding its responsibilities.

The Commission's responsibility is to apply the law. The DFAP is merely a plan, not a magic wand that wipes away statutory language or a license to milk mailers for every possible penny. Under the PAEA, which remains the law, operating costs are not a given that Market Dominant rates must be raised to cover. Instead, the PAEA capped Market Dominant prices and expected the Postal Service to operate within it that constraint. If postal management desired more revenue due to its inability to control costs, the law gave the Postal Service the opportunity to do so by increasing Market Dominant mail volume, increasing profits from Competitive products, or both.

Objective 5 does not require Market Dominant rates to be raised above CPI to fund the Postal Service's non-statutorily mandated operating expenses, regardless of the cap Congress had imposed to restrict those expenses. While Order No. 5763 and the earlier orders devoted much discussion to statutorily mandated payments, such as the now-forgiven retiree prefunding requirement, it implicitly assumed that Market Dominant products should fund the routine costs of the Postal Service regardless of their level. But that turns the law upside down.

Neither the DFAP nor any alternative postal plan is at issue in this proceeding. The Commission is to apply the law as Congress intended, which is to protect mailers of Market Dominant products from excessive rates regardless of whatever strategic plan the Postal Service may be implementing at any given time.[89] That the Postal Service has costly plans is *its* problem; the system established by Congress and implemented by the Commission is intended to limit the Postal Service's revenues from captive ratepayers and force it either (1) to control its costs, or (2) to increase volume, and/or (3) to earn greater profits from Competitive products. If it cannot do so, and is unwilling or unable to manage its costs, the proper venue for it to seek relief is Congress, not this Commission.

C. The Market-Dominant Ratemaking System Should Be Modified

The Commission should modify the Market Dominant rate system as follows:

- Limit general Market Dominant rate increases to one per 12-month period;
- Repeal the density authority;
- Introduce an X-Factor coupled to a performance incentive mechanism that would allow the Postal Service additional rate authority if it met specific metrics for volume, service, and productivity; and
- Improve the worksharing regulation in 39 C.F.R. §3030.284.

[89] In any case, it is doubtful whether the DFAP's projections are even useful at this point. The Office of the Inspector General recently stated: "The DFA plan and its projections no longer provide a reasonable basis for comparisons to future years' results." *OIG Report on State of the U.S. Postal Service Financial Condition* at 4.

By doing so, the Commission would also address the current system's reduction in rate transparency compared to the previous system,

At a minimum, the Commission should not authorize any additional revenues for the Postal Service without conditioning such authorization on attaining set metrics for better performance or productivity that benefit the mailing community. That approach was tried in the previous review, and the results speak for themselves. There is absolutely no evidence that allowing even more money now, without a negative X-factor and strong conditions aimed at costs, volume, and service, would produce a different outcome.

1. Limit general Market Dominant rate increases to one per 12-month period

The Postal Service's current practice of raising rates twice a year is proving disruptive to mailers and harms the Service by sending a strong signal that it cannot be trusted to be a reliable vendor or partner. Business mailers, who account for most of the volume, must undergo the costly process of updating mailing software and adjusting to any associated changes in mailing regulations twice as often, increasing their costs and busywork.[90]

Moreover, the two-a-year rate increases wreak havoc on mailers' budgets and create a near-constant focus on rates and budgets in the C-suites of major mailers. Unsurprisingly, these make business mailers more interested, if not determined, to leave

90 Only last year the Commission urged the Postal Service to consider "how fixed mailing budgets and twice-per-year price changes may be contributing to volume loss the additional costs incurred by mailers related to software and programming updates each time price change, and the limitations that frequent increases place on the Postal Service's ability to analyze up-to-date data related to the effects of price increases." Order No. 6526, Docket No. R2023-2, at 42 (May 31, 2023). But there is no indication that the Service has done so.

the mailstream. The recent accelerated declines in Market Dominant volumes illustrate that mailers are doing so. This harms the Postal Service not only in the year it is not mailed, but also in the following years because once lost, mail (especially First-Class Mail) rarely returns.

The Commission has the legal authority to limit rate adjustment filings to one per year. This is clear not merely from the current statutory language, but also from the changes made by the PAEA in 2006.

First, the plain language of Section 3622 directs the Commission to devise the Market Dominant rate regulatory system. Nothing in Section 3622 denies the Commission the power to limit general rate increases to one per year. Congress delegated to the Commission authority over the system for regulating Market Dominant rates, and Section 3622 is the Commission's to interpret, not the Postal Service's.

Second, the current postal law subjects the Governors' power to set rates to the Commission's jurisdiction. Section 404(b), enacted as part of the PAEA, authorizes the Governors "*[e]xcept as otherwise provided*, . . . to establish reasonable and equitable classes of mail and reasonable and equitable rates of postage and fees for postal services *in accordance with the provisions of chapter 36*." 39 U.S.C. §404(b) (emphasis added). This provision plainly confers on the Governors the power to set rates and fees, but just as plainly subjects that authority to Section 3622 and the system the Commission creates pursuant thereto. Notably, Section 404(b) says nothing about the timing or frequency in which the Governors can set rates or gives the Governors authority to file Market Dominant rate adjustments more frequently than the Commission allows.

Third, this reading is further supported by the statutory history. The PAEA repealed the prior version of Section 3622 which, unlike current law, had provided that "From time to time" the Postal Service could request the former Postal Rate Commission to issue a recommended decision to change rates. The "from time to time" provision allowed the Governors to approve rate requests at any time; however, Congress deleted that provision and current law contains no similar *carte blanche* to the Postal Service.

Fourth, In contrast, where the PAEA wanted to give the Governors clear authority over rate changes, it did so. For Competitive products, Section 3632(a) provides that a simple majority of the Governors holding office "shall establish rates and classes for products in the competitive category of mail in accordance with the requirements of this subchapter and regulations promulgated under section 3633." 39 U.S.C. §3632a).[91] Section 3633 establishes three substantive requirements for Competitive products: (1) a prohibition on cross-subsidization by Market Dominant products; (2) that each Competitive product covers its attributable costs; and (3) that collectively Competitive products contribute an "appropriate share" to the Postal Service's institutional costs. Unlike Section 3622, Section 3633 does not list Objectives or Factors and does not refer to regulating rates. Nor does it provide the Commission with any additional authority over the levels of Competitive rates.

Fifth, this interpretation of both Section 3622 and Section 3633 is fully consistent with the statutory history. Prior to the PAEA, postal rates were governed by the Postal Reorganization Act, which provided for cost-of-service regulation. Inherent in a cost-of-

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[91] "This subchapter" refers to 39 U.S.C. §3631 through §3634. Subsection 3632(b) specifies certain notification requirements. Subsection 3632(c) provided a transition rule that applied until the Commission adopted regulations under Section 3633.

service regulation, the Governors controlled the timing of a rate filing and set the "revenue requirement" for a "test year." Although Commission regulations set some limits on what the test year would be, both timing and amount were the domain of the Governors.[92] That system was abolished by the PAEA, which replaced it with the price cap and current Sections 3622 and 3632.

Sixth, in Docket No. RM2017-3, the Commission construed Section 3622(d)(3) to give it broad authority "to modify or replace all aspects of the existing ratemaking system, including the CPI-U price cap, if necessary to achieve the statutory objectives." Order No. 5763 at 40-59. The Court of Appeals upheld the Commission's interpretation.[93] In view of the Commission's determination that it has authority even to eliminate the price cap, it is difficult to believe that it would not have the lesser power to limit the frequency of rate adjustments.

Such a limitation is also consistent with the thrust of the PAEA. Although Congress did not specifically limit the Postal Service to one Market Dominant rate adjustment per year, it did so as a practical matter because the limitation of total increases to CPI over 12 months rendered that option of little real financial value. Although perhaps in theory the Postal Service could have sought to raise rates by half of CPI every six months, or even more frequently for lesser fractions of CPI, doing so would have been disruptive for little financial benefit and therefore, wisely, it never did. This did

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92 *See Newsweek, Inc. v. United States Postal Service*, 663 F.2d 1186, 1203 (2d. Cir. 1981) (reversing Commission reduction of revenue requirement). In subsequent years, mailers usually disputed the revenue requirement, but the Commission did not alter the Governors' choice except for minor mathematical adjustments. Nor did the Commission exercise the normal regulatory authority in cost-of-service regimes to second-guess the "prudence" of capital investments made by the Governors.

93 *National Postal Policy Council v. Postal Regulatory Commission*, 17 F.4th 1184, 1187 (D.C. Cir. 2021), *cert. denied*, 142 S. Ct. 2868 (2022).

not leave the Service without options if conditions suddenly deteriorated; Congress in the PAEA provided for expedited rate increases if extraordinary or exceptional circumstances warrant. 39 U.S.C. §3622(d)(1)(E).

Limiting the Postal Service to one Market Dominant rate adjustment per twelve months would not affect its ability to introduce new services, market tests of experimental services, or new rate structures. And the Commission could, if it chose, retain the provision for expedited consideration when warranted by exigent circumstances.

2. Repeal the density authority

To better achieve the Objectives of maximizing the incentives to reduce costs, to improve the predictability and stability of rates, to improve the long-term sustainability of the Postal Service, and to achieve just rates, the density factor must be eliminated. It addresses the problem of reduced density in precisely the wrong manner by discouraging volume retention and growth instead of encouraging it while dampening the incentive to reduce costs.

The stated purpose of the density authority is to allow for recovery of increased per-unit network costs caused by the combination of increased delivery points and lower volume (thus less density per delivery point). The problem with the density authority is that it addresses a loss in volume by giving the Postal Service authority to raise rates by even more amounts. It does not address the primary causes: declining volume or the Postal Service's inability to manage costs.

By allowing higher rate increases than otherwise would be the case, the density factor drives out more volume, even if it results in slightly more revenue. And the cycle repeats, as each rate increase drives away still more volume, generating still more rate authority which, when used, then drives away even more volume. It is difficult to see an end.

The density authority hits Market Dominant mail particularly hard in two ways. First, the current formula does not take the revenue of the lost volumes into account – under the formula, the loss of a First-Class letter and the loss of a Priority Mail package have an equal effect on cost recovery. But the loss of a higher priced piece “hurts” the Postal Service more because it takes away more of the revenue that would cover the per-piece cost of delivering to each postal delivery point. Although the losses of a letter and a package have quite different revenue consequences, the density formula ignores that and treats them as having an equal effect on increasing per-unit costs.

Second, network costs are institutional costs, the residual from total costs after accruals for attributable Market Dominant and Competitive products. As the Delivering for America Plan contemplates fewer, more centralized mail operations, delivery and related network costs may comprise even larger portions of total costs. Because the density formula assigns the great majority of institutional costs to Market Dominant mail, which has vastly larger volume, these costs will largely fall on a declining pool of mailers unless the Postal Service can reduce the trends.

In Order No. 5763, the Commission stated that the density authority is targeted at the “root cause” of costs – the loss of density, which is really a loss of volume combined with the growth in delivery points. But the density authority does not really address either cause. Instead of authorizing higher rates, the rate system should be encouraging greater cost control and volume retention and growth. The Postal Service would be in a much better condition if it had the volume it had even a few years ago.

3. Introduce an X-Factor and condition any increase beyond that on the Postal Service having met specific metrics for volume, service, and productivity

The Commission should Impose an “X-factor” to strengthen the Postal Service’s incentives to maximize efficiency and create genuine cost efficiencies, thus securing its financial stability as intended by Congress. An X-Factor, although one has never been applied to the Postal Service, would create a stronger incentive for the Postal Service to control its costs by forcing it to focus more closely on cost control, rather than simply spending beyond its means. It should be sufficiently large to get the attention of postal management while also compensating mailers for the Postal Service’s failure to control costs sufficiently or to provide the promised service.

The Commission should also consider supplementing an X-Factor with a performance incentive mechanism that could allow the Postal Service to earn additional revenue but should do so only if tied to strong metrics to ensure accountability.[94] The Commission has already developed a substantial record on performance incentive mechanisms (“PIMs”) in Docket No. RM2021-2, which has been consolidated with and forms part of the record of this proceeding. NPPC addressed the merits of a performance incentive mechanism in its comments in that docket,[95] and respectfully refers the Commission to those for a more detailed discussion. The point is that a PIM would supplement the current regulatory system by promoting more accountability (by applying directly to rates) than currently exists. Years of annual compliance

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94 Even if the Commission does not adopt an X-Factor it could, of course, consider a performance incentive mechanism of the type outlined here.

95 *Comments of the National Postal Policy Council and the National Association of Presort Mailers*, Docket No. RM2021-2 (Sept. 15, 2023).

determinations have repeatedly found excessive costs and inadequate service performance and directed the Postal Service to conduct reams of analyses and reports, but costs remain excessive, and service remains subpar. Rate incentives could address these shortcomings.

A performance incentive mechanism might allow the Postal Service to earn additional rate authority if it achieved pre-established metrics in a given fiscal year. It should be simple to administer, with easily understandable metrics that the Postal Service cannot manipulate and that can be verified easily. Elements of this should include conditioning any additional rate authority on the Postal Service's achieving each of these metrics:

- increase Market Dominant volume on a year-over-year basis;
- achieve positive productivity, whether measured by Total Factor Productivity or another metric;
- meet all Market Dominant service performance annual targets without reducing any published service standards, business rules, or service performance targets; and
- increase all Market Dominant service performance annual targets every year until they are at least 95 percent of service standards. Once this is achieved, the targets must continue to meet or exceed service standards to avoid a penalty.

4. Improve the pricing efficiency of presortation discounts

The Commission should modify the presortation discount rules to address the recurring problem of discounts drifting too far away from efficient levels. NPPC recommends that the Commission consider the following change:

> Modify rule 3030.284(e) to require presortation discounts to be set to passthrough at least 95 percent of the costs avoided unless the Postal Service can justify, by substantial evidence, an exception. In particular, the

> Commission should delete Rule 3030.284(c) and modify current Rule 3030.284(e) by replacing “85 percent” with “95 percent.”

This change would improve the system’s ability to maximize the incentives for cost efficiency, as required by Objective 1 and taking into account Factor 5, in two ways.

One, by raising the minimum presumptive satisfactory passthrough to 95 percent, the change would both (1) close the gap between actual prices and those set according to Efficient Component Pricing and (2) by requiring discounts when set to passthrough at least 95 percent of avoided costs, they would at least start at more efficient levels so that the likely increases in avoided costs over time would drift less far away from efficient levels. Also, Subpart (e) does not currently adequately address the situation in which the *avoided costs* increase by 20 percent or more, leaving the discount passthrough no closer to 100 percent, so narrowing the allowable range would help to preserve the accuracy of the pricing signal.

Two, for presortation discounts that are already below the current 85 percent threshold, rule 284(c) today requires merely that the Service adjust the amount of the *discount* by a minimum of 20 percent, but without specifically considering the amount by which *avoided costs themselves* may have changed. 39 C.F.R. §3030.284(c); see Order No. 5763 at 216-218. Changing only the amount of the discount without adjusting for changes in the costs avoided, which have likely changed as well, will not ensure that discounts move towards ECP. As postal costs increase, and as per-unit costs may increase due to declines in density and other factors, costs avoided by presortation may increase but the current rule does not truly force discounts to efficient levels. The proposed change, which eliminates subpart (c) corrects that problem by requiring presortation discounts to be set efficiently.

5. The retirement authority should be conditional

By its own terms, the retirement authority will expire as an additional rate authority next year. However, the sums added over the use due to this factor will remain in the base rates. If the Postal Service continues to remit the required payment to the Treasury, no change is required. 39 C.F.R. §3030.184(a).

However, the regulation should be clarified to ensure that if the Postal Service ever fails to make the required minimum remittance to the Treasury, the retirement authority built into the base rates should be annulled and taken out of the base. That is, rates should be *reduced* by the total compounded percentage by which the retirement authority has allowed the Postal Service to pad the rates. The Postal Service should not be allowed to collect revenue based on the retirement authority if it fails to make the required payments. Current regulation 3030.181 does not expressly provide for this contingency.

Similarly, if Congress amends the law to eliminate or reduce the Postal Service's obligation to fund FERS or CSRS benefits or to allow the Service a greater investment return than is currently available, a corresponding reduction must be made to the rates.

6. The Commission should ease the test for NSAs, niche classifications, and contracts

NPPC encourages the Commission to take a more flexible approach to Market Dominant negotiated services agreement. The Postal Service by now has considerable experience in negotiating contracts for its Competitive products. The Commission should encourage it to explore transferring that experience to Market Dominant products, which Congress has expressly encouraged. *See* 39 U.S.C. §3622(c)(10).

One way this could be done is by discarding the so-called "Panzar test" or at least being more receptive to alternative tests. The Commission has indicated previously that it will explore these issues. *See* Order No. 6813, Docket No. MC2023-222, at 19 & 23 (Nov. 22, 2023) (Publisher's Clearing House NSA). More generally, the Commission should be receptive to agreements designed to retain and increase Market Dominant volume.

D. These Changes Would Better Achieve The Objectives, Taking Into Consideration The Factors

Congress stipulated that the statutory Objectives must be applied in conjunction with one another, considering the factors. The Objectives are to guide the Commission in shaping a system for regulating the rates of Market Dominant products in a way that furthers the Postal Service's public service mission while protecting mailers subject to the Service's legal monopolies.

The proposals outlined above would improve the current system in several ways.

First, they would more effectively achieve Objectives 1, 3, 5, and 8, which the Commission found were not achieved under the former system, than the system adopted in Order No. 5763. They would so by tightening the emphasis on cost control and removing impediments to volume growth and improved productivity under the current system.

Second, these changes would address the reduced predictability and stability of rates under the current system and improve the transparency of the process. By limiting rate changes and making the pricing adjustments more predictable and stable, these changes would also enhance the Postal Service's dependability as a reliable business partner.

V. CONCLUSION

The current system for regulating the rates charged for Market Dominant products was well-intentioned but is not achieving the desired results. Instead of facilitating ever-higher rate increases, it instead should focus on encouraging the necessary efficiency. Stabilizing and improving volume through smaller rate increases, less frequent rate changes, and more efficient worksharing signals should go a long way towards improving efficiency, reducing unit costs, and improving productivity. By improving the Postal Service's efficiency, mailers should also receive a quality of service much more closely approaching what the Service promises today in its service standards.

For the foregoing reasons, the National Postal Policy Council urges the Commission to modify the system for regulating Market Dominant postal rates in a manner consistent with these comments.

Respectfully submitted,

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