Mailers Hub News

May Summary *From the May 9 and 23 issues*

Associations Respond to USPS Opposition to Ratesetting Changes

In separate filings on April 11, two groups of industry associations had petitioned the Postal Regulatory Commission to reconsider the additional rate authorities it granted the Postal Service in a final rule issued November 30, 2020. Their request followed by less than a week the enactment of the *Postal Reform Act of 2022* which significantly reduced the debt and future costs of the Postal Service that had driven the PRC's rulemaking and its conclusion. Both petitions predicated their request on the provision of the legislation that eliminated the prefunding obligation and its associated financial burden, estimated to reduce USPS red ink by as much as $108 billion over ten years. As was probably expected, the Postal Service moved on April 20 that both petitions be rejected:

> "In every respect, these filings are deficient, and the Commission should decline to open a rulemaking. ... As petitions for rulemaking, they fail to comply with the Commission's applicable rules. More fundamentally, the petitions fail to provide any substantive basis for the Commission to institute a review of the market-dominant regulatory system ... now, or at any time before the scheduled five-year review. ..."

In their April 27 responses, the industry groups disputed the bases for the Postal Service's opposition:

> "... The Postal Service misstates the relief requested by the Petitioners, mischaracterizes the arguments made by Petitioners, and ignores the obvious fact that its financial condition has significantly changed after the passage of the Postal Service Reform Act. As described in the Petition for Rulemaking, the fundamental premises underlying the Commission's rules granting the Postal Service authority to increase rates by more than the annual change in the Consumer Price Index have changed. While one can argue over *how much* impact these changes have on the Postal Service's financial condition, one cannot reasonably argue – as the Postal Service does – that no fundamental change has occurred. Thus, despite the Postal Service's protestations, a new notice-and-comment review of the market dominant ratemaking system is appropriate now. ..."

There is no timeline for the PRC to rule on the petitions or motions. If the commission rejects the petitions, the current ratesetting process remains unchanged. However, if it accepts the petitions and opens a new rulemaking, the most likely result would be the elimination of the added "prefunding" rate authority granted by the PRC in 2020. The "density" adder could be amended, but it's a virtual certainty that the non-compensatory provision (affecting "underwater" products) would be retained.

USPS Releases Second Quarter Results

On May 5, the Postal Service released its *Form 10-Q* for the second quarter of fiscal 2022 (January 1 – March 31). The period covers the post-holiday mailing season and usually has lower volume and revenue than the preceding quarter. Despite weak volume compared to the same period last year, total revenue in PQ II of FY 2022 was higher thanks to a price increase implemented in August 2021. However, while the overall increase in August was about 6.8%, revenue for the quarter was up less than 4.75% because of lower volume, particularly of higher-contribution products like First-Class Mail, Priority Mail, and ground parcels.

(in millions)	Three Months Ended March 31, 2022	Three Months Ended March 31, 2021[1]
Operating Revenue:		
First-Class Mail[2]	$ 6,270	$ 5,974
Marketing Mail[3]	3,740	3,228
Shipping and Packages[4]	7,873	7,775
International	417	558
Periodicals	224	235
Other[5]	1,262	1,120
Total operating revenue	**$ 19,786**	**$ 18,890**
Volume:		
First-Class Mail[2]	12,979	13,061
Marketing Mail[3]	15,842	14,616
Shipping and Packages[4]	1,772	1,866
International	90	109
Periodicals	804	936
Other[6]	61	74
Total volume	**31,548**	**30,662**

[1] Prior period amounts for certain service categories include reclassifications of amounts amongst ser current period presentation. These reclassifications are immaterial for each affected category and hav

Total market-dominant mail volume was higher over the period than a year ago, driven by increased post-pandemic Marketing Mail activity, but – continuing historic trends – all classes were still lower than pre-pandemic PQ II of FY 2019. Meanwhile, competitive product revenue was up only 1.3% as volume decreased by more than 5%. For the first half of FY 2022, competitive products' revenue and volume are both lower than for the first half of the previous year, continuing their retreat from mid-pandemic highs.

Despite lower volume and decreased service standards (implemented at the start of the fiscal year on October 1), expenses continued to grow, driven primarily by employee compensation and benefits and an increased workers compensation liability. In all, total quarterly expenses outran revenue by $639 million (and $2.186 billion for the first half year), considerably worse than SPLY, regardless of the impact of the workers' comp liability. Higher compensation costs can be attributed to increased workhours, a larger complement of career employees, and the impact of generous wage increases agreed to by the USPS in contracts with its craft labor unions. Overall transportation costs were basically flat, though highway costs grew and air costs decreased as lowered service performance goals enabled a shift to slower ground transportation.

PRC Issues Financial Analysis of the USPS

On May 18, the Postal Regulatory Commission released its *Financial Analysis of United States Postal Service Financial Results and 10-K Statement* for fiscal 2021 (October 2020 through September 2021). The document was formerly part of the *Annual Compliance Determination*, issued no later than March 31, but in recent years has been released later as a separate report. The 113-page analysis is comprehensive and detailed, with dozens of charts illustrating a variety of financial conditions, including USPS revenue and costs. The PRC summarized the agency's financial position at the end of FY 2021:

- The Postal Service's total net loss was $4.9 billion.
  - The net deficit was $75.7 billion, consisting of an accumulated deficit of $88.8 billion offset by capital contributions of $13.1 billion. The net deficiency is $5 billion less than in FY 2020, primarily as the result of the $10 billion capital contribution in the Coronavirus Aid, Relief, and Economic Security (CARES) Act.
- The Postal Service's cash and cash equivalents total, excluding restricted cash, was $23.9 billion, an increase of $9.6 billion.
  - Remaining available borrowing authority from the PAEA-mandated debt ceiling of $15 billion was $4 billion, an increase of $3 billion.
  - The cash ratio, which measures the amount of cash, cash equivalents, or short-term investments available to cover current liabilities, was 0.28, an increase of 0.09 compared to the prior year. The FY 2021 cash ratio was also higher than the 10-year average of 0.15.
- The Postal Service's operating revenue was $77 billion, which was $3.9 billion higher than the previous year.
  - Pandemic-induced e-commerce led to $3.6 billion or 11.8% more Competitive product revenue, but the growth slowed during the second half of the year.
  - In FY 2021, revenue from Competitive products exceeded First-Class Mail revenue.
  - Market Dominant revenue decreased by $97 million in FY 2021, a substantially smaller decrease than FY 2020, as the economy recovered and USPS Marketing Mail volume increased during the second half of the year.
- Net operating expenses stood at $79.6 billion, which were $3 billion greater in FY 2021 than the prior year, and $3.2 billion more than the Integrated Financial Plan.
  - Increased expenses for compensation (3.6%) and transportation (9.5%) were driven by pandemic-related increases in more labor-intensive package shipping, disruptions in air and highway transportation, and enhanced safety measures.
- Personnel-related expenses made up 75.7% of total expenses.
  - Overtime hours increased by 23 million compared to FY 2020, and total workhours increased by 1.4%, the highest rate in the past five years.
  - Total postal employees increased by a net of 9,000. Over the past decade (FY 2012-FY 2021), the Postal Service has reduced its full-time and part-time workforce by approximately 12,000 employees and added approximately 36,000 non-career employees.

Excluded Mail Continues to Reduce Volume "In Measurement"

Despite its generalized service performance claims, the volume of market-dominant mail that is excluded from the Postal Service's measurement process continues to justify questions about whether those claims are representative. Because the USPS measurement process relies on pieces bearing an intelligent mail barcode, documentation from mail preparers, and processing over automated equipment, any mail not meeting one of those basic requirements reduces the volume of mail potentially eligible for measurement, even before other reasons for exclusion apply.

The latest data filed with the Postal Regulatory Commission by the USPS are for its second fiscal quarter (January 1 – March 31, 2022). According to the PQ II *Revenue, Pieces, and Weight* report, the total mailpiece volume of Presorted First-Class Mail was 9,552,094,920; the total volume of Marketing Mail letters was 12,843,624,237; and the total volume of Periodicals was 803,828,462.

According to the PQ II *Quarterly Result Aggregation for Presort First-Class Letters/Postcards*, 5,535,528,933 pieces – about 58% of total volume – were "in measurement." The remaining 42% – over four billion pieces – were excluded from measurement because they fell into one of the fifteen categories of exclusion used by the USPS; see the chart below. About three-fourths of total excluded volume – roughly 2.7 billion pieces – were not counted because of the "long haul" and "no start-the-clock" exclusions. (The USPS has recently announced changes to reduce the volume of "long haul" exclusions.)

By definition, therefore, pieces lacking an IMB, either one applied by the mailer or by the USPS, or that are not automation compatible, or that bypass automated processing, are not "seen" and, consequently, the duration of their movement through the mailstream is not measured. Aside from such pieces, yet more are excluded for one of several reasons detailed in the business rules associated with the service measurement system.

For Marketing Mail, according to the PQ II *Quarterly Result Aggregation for USPS Marketing Mail* reports for destination entry and origin entry letters, 8,253,743,888 letters – about 64.3% of total volume – were "in measurement." The remaining 33.7%, about 4.33 billion pieces, were excluded from measurement for one of the fifteen reasons, over 70% of which, about 3.01 billion pieces, because of "no piece scan" or "no start-the-clock."

For Periodicals, according to the PQ II *Quarterly Result Aggregation reports for Within- and Outside-County Periodicals*, 58.1% of the mail (467 million pieces) was "in measurement." Of the remaining 41.9%, about 394.7 million pieces, exclusion for "no piece scan" or "no start-the-clock" was the reason 67.7% (267.2 million pieces) were disqualified.

As noted, the USPS continues to issue weekly press releases presenting homogenized class averages, but the underlying data paints a less deceptive picture. By excluding significant volumes of mail for a long list of reasons – of which some, like "no piece scan" or "no start-the-clock" are the fault of the USPS, not the mail preparer – the agency can limit the mail on which its scores are based to only the "best."

PQ II/FY 2022 USPS Service Performance: Little Improvement

As commercial mail producers and their clients are aware, the Postal Service lowered service standards for First-Class Mail and some Periodicals effective last October 1, and set new performance targets for all mail for FY 2022. The performance reports it filed May 10 with the Postal Regulatory Commission are based on these revised targets. The latest scores show little improvement compared to PQ I, despite lower volume, better weather, and more workers. All service level scores for First-Class Mail were below the previous quarter – and mostly below the scores in late FY 2021 under the previous service standards. The aggregate scores for Marketing Mail letters and flats also were lower than the PQ IV, FY 2021, as were Periodicals.

Area and districts in the west again generally performed better while those in the east generally did worse. The Pacific Area led with the most top quarterly scores for First-Class Mail and Marketing Mail, while the Cap Metro Area had more of the worst quarterly scores.

Meeting or exceeding targets for First-Class Mail were 33 districts for overnight, 29 for two-day, 12 for 3-day, 8 for 4-day, and 59 for 5-day service; fewer met or exceeded targets in PQ II than in PQ I. Conversely, 12 districts reported quarterly First-Class Mail scores that were ten points or more below target – more than for the previous quarter.

For Marketing Mail, 10 districts fell short of the service target for letters, and 20 districts missed the mark for carrier route mail, and 57 districts fell short of the service target for flats, fewer in each category than for PQ I.

Scores for Periodicals are not reported below the area level but were again well below service targets.