DISSENTING OPINION OF VICE CHAIRMAN TAUB

A. Overview.

The Commission's calculation of the contribution loss "due to" the Great Recession is contrary to Commission Order No. 864[1] (interpreting on Remand the relevant law (39 U.S.C. § 3622(d)(1)(E)) and regulations (39 C.F.R. § 3010.60-65)), and therefore, I must dissent. In brief, the Commission fails to reasonably measure both the volume loss due to the Great Recession and the continuing financial harm to the Postal Service caused by that volume loss. In addition, the Commission's methodology for rescinding the exigency increase has not been vetted with the public, and I am concerned about potential unintended consequences as a result.

B. The Commission fails to appropriately calculate the financial harm to the Postal Service "due to" the Great Recession.

In crafting the price cap regime, Congress built in a safety valve – the exigent provision – to address circumstances causing such substantial and unforeseen harm that the Postal Service could not adjust in the ordinary course of business. As acknowledged in the Commission's decision, the Postal Service suffered a catastrophic financial blow from the Great Recession (*i.e.*, the "extraordinary or exceptional circumstances"). Therefore, the task for the Postal Service is to quantify the net contribution loss due to the Great Recession.

In Order No. 864, the Commission explained that a precise revenue loss number was not required. While the Commission would not expect absolute precision, any number must be quantified with supportable methods and factor out the "non-exigent" circumstances. The Commission recognized that some exigent circumstances, such as a natural disaster that destroyed facilities, lend themselves to more accurate quantification than the very different evidentiary challenges presented by calculating the

[1] Docket No. R2010-4R, Order Resolving Issues on Remand, September 20, 2011 (Order No. 864).

net adverse financial impact of the Great Recession and its impact on postal volumes. For a large exigent amount, as we have here, the Commission expected to see sophisticated data collection and estimation methodologies, as well as expert opinions and statistical analyses. The Commission assured the Postal Service that its concern that the causal nexus of "due to" would require a "strict level of precision," "absolute precision," or "perfect proportionality" was misplaced. "The Postal Service is not expected to engage in 'a quixotic search for perfect proportionality .' It is simply expected to support its exigent request with credible proof of the type described above." Order No. 864 at 52.

The Postal Service complied with Order No. 864 by quantifying the net adverse financial impact of the Great Recession with a combination of econometric models and expert opinion. Based primarily on the work of its witness Thomas Thress, the Postal Service calculates those impacts in terms of estimated annual effects in a given year. Thress estimated, within each market dominant mail class, the volume loss by year attributable to the Great Recession.

Those losses do not include his separate estimates of mail volume by year and by class that was lost due to the continuing and on-going effects of pre-existing trends in electronic diversion. The Postal Service's analysis calculates a material amount of additional electronic diversion. The Postal Service estimated that by Fiscal Year 2012, in addition to the billions of pieces of mail that were diverted to electronic media in 2007, an additional 12 billion pieces per year were being diverted, independent of the Great Recession.[2]

The Commission uses Thress' model to estimate volume losses, but the Commission chooses to omit certain variables relied upon by Thress in this proceeding. The Commission also treats the Great Recession as a normal business cycle. It

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[2] The Postal Service in its witness testimony and answers to numerous Presiding Officer Information Requests (POIRs) (*see*, for example, POIR No. 3, question 1 and POIR No. 9, question 9), shows that 12 billion pieces is lost to diversion independent of the Great Recession and incorporates this into its net calculation of impact.

assumes that once the rate of volume decline for a class of mail is no longer increasing (or the rate of volume growth is no longer falling) on account of factors reflecting the Great Recession, the impact of the exigent circumstance – *i.e.*, the impact of the Great Recession – has ended. It considers any subsequent period as the "new normal" and that the Postal Service must simply adapt. Critically, the Commission fails to recognize the continuing financial harm associated with the volume loss.

Yet the objective established by Order No. 864 is that the Postal Service must estimate what mail volume would have been if the Great Recession had not occurred – in other words, *the volume lost due to the Great Recession*. Counter to what is required of the Postal Service, the Commission instead presumes that the effects of the Great Recession suddenly ended 3 years ago for most classes of mail.

1. Moving the goal posts: The Commission creates new standards and burdens of proof.

Order No. 864 outlined the nature and amount of proof as well as the supportable quantification methods required of the Postal Service. The Commission recognized that when faced with the unique circumstance of the Great Recession, statistical information and expert analysis would be part of the proof needed. In contrast, a straightforward exigency – for instance, destruction of facilities – would lend itself to more accurate calculations of equipment expenses and construction costs.

The Commission acknowledges in Order No. 864 that there would always be some degree of imprecision in the quantification of harm, particularly with regard to the difficulties inherent in untangling the interaction of multiple factors. It established a standard that the Postal Service must support its exigent request with credible proof based on a combination of econometric models and expert opinion. The Postal Service, through Thress and its entire postal demand analysis group, provides both, not only in Thress' original Statement, but also in his responses to an extensive number of POIRs and his Reply.

However, the Commission now dismisses critical aspects of the Postal Service's data that are based on expert analysis and estimation methodologies. The Commission claims that Thress' conclusions regarding the relative roles of the Great Recession versus ongoing electronic diversion, and his choice of macroeconomic variables are "not justified." The Commission criticizes Thress for not including certain variables in his model, yet acknowledges that no commenter offered a model that included these variables and that the record is void of a model that is available to do so. The Commission appears to believe Thress should have developed one nonetheless. Separating volume lost due to the Great Recession from loss due to other factors, primarily electronic diversion, is, to say the least, challenging. While not without flaws, Thress' model and analysis represent a credible attempt to distinguish the causes of the volumes lost.

Moreover, as required by the U.S. Court of Appeals for the District of Columbia Circuit in remanding the original exigency case to the Commission, Order No. 864 specified the proof required for the Postal Service to demonstrate the causal nexus of "due to" – including guidance on quantification requirements, nature and amount of proof, supportable quantification methods, not exceeding the net adverse financial impact, and administrative feasibility. However, in Chapter IV, the Commission **now** introduces *four new standards* to determine the end of what can be calculated "due to" the exigent event, centered on a view of what is a purported "new normal."

Much should be expected of the Postal Service when requesting a rate change "due to" extraordinary or exceptional circumstances, but with no opportunity for input or comment, and contrary to Order No. 864, the Commission now requires a strict level of precision and imposes new additional standards.

2. The Postal Service is not a private company.

The Commission's adoption of a "new normal" is also problematic. The Commission assumes that there is no longer an exigent effect when certain macroeconomic factors indicate that volume decline has stabilized over a limited period of time. In doing so, the Commission implies that the Postal Service can simply adjust to both volume level shifts and the change in the long-term trends as if it is a typical business cycle upturn.

But as the Postal Service has demonstrated, the Great Recession had a starkly atypical effect on mail volume.[3] The Great Recession appears to be much more similar in scope to the Great Depression. The Great Recession is neither "short term" nor a "cycle." As demonstrated in POIR No. 1, question 9, among others, one impact of the Great Recession was to change long-run trends in mail volumes. This type of analysis is what is required by Order No. 864. The record before the Commission demonstrates that the Great Recession, and its impact on mail volumes, continues to have a negative impact on the Postal Service.

How is this "new normal" **not** "due to" to the exigent circumstance – the Great Recession? Under the Commission's decision, the "new normal" suddenly ends the impact of the extraordinary and exceptional circumstance. 39 C.F.R. 3010.61(a)(7) requires an assessment of whether the exigent circumstances were foreseeable and could have been avoided by reasonable prior action. How could the continuing effects of the Great Recession on postal volumes been avoided by reasonable prior action? How is it that the Postal Service suddenly experiences no further impact from the Great Recession (*i.e.*, the extraordinary and exceptional circumstance) and that the continuing financial harm attributable to volumes lost due to the Great Recession has ended?

The Postal Service outlines in this case, and the Commission acknowledges, that the Postal Service has undertaken many efforts to adjust to the "new normal." However, unlike entities in the private sector, the Postal Service cannot suddenly eliminate institutional costs in response to volume declines by shrinking the size and scale of its networks. As the Commission observes in Chapter V, the Postal Service is unlike a private company.

[3] *See, e.g.*, Thress Reply at 9-11; Thress Statement at 7.

The Postal Service explains that its networks are much more a function of its universal service obligations and service standards rather than mail volume. It lacks the ability to react as quickly as private companies might in response to adverse circumstances. The "new normal" appears to assume the Postal Service could shed its fixed (institutional) cost obligations instantaneously with exogenous events. This view is unsupported on the record in this proceeding, yet the Commission uses it to truncate the financial harm caused by the Great Recession. Generally, the Postal Service must deliver mail to every address, and the size of the delivery network keeps growing every year despite the fact that mail volumes are declining. Universal service standards and obligations, rather than mail volume, are in many respects the more critical drivers of the scope of the required facility network.

By definition, the same is true of institutional costs. If specific cost components varied automatically in response to changes in mail volume, they would not be institutional costs, but rather volume-variable costs. With respect to volume-variable costs, the Postal Service has generally been able to adjust to the new lower overall levels of mail volume.[4]

However, the continued loss of contribution is due to the extraordinary and exceptional event of the Great Recession. Mail volume in 2011 and 2012 is substantially below what it would have been in the absence of the Great Recession, and therefore any evaluation of impact "due to" the effects of the Great Recession cannot ignore these "effects." The continuing effect in these years is certainly not zero. In sum, the principal flaw in the Commission's Order is the failure to recognize that, regardless of the volume loss found due to the Great Recession, the financial harm of that loss does not end immediately. While there may be disagreement over how long the recovery period should be, there can be no reasonable disagreement that it persists for some time.

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[4] Indeed, positive productivity is the *only* evidence that the Commission cites in the fourth prong of its newly created "due to" analysis in Chapter IV for the Postal Service purportedly adjusting to the "new normal."

C. The formula to rescind the increase risks creating unintended consequences.

The Commission calculates the impact of the exigent event as a one-time loss of contribution. The Commission creates an approach that will measure the exigent recovery by revenue, not contribution. In doing so, it establishes a formula to rescind the exigent increase based on the level of "additional" revenue that will be estimated to result from the adjustment, calculated quarterly.

I am concerned that this formula is being imposed without the full benefit of broad public input and an opportunity to fully assess potential unintended consequences on both the Postal Service and mailers.

D. Concluding observations.

The Postal Service presents an extensive array of information demonstrating the effects of many shifts in consumer and business behavior triggered by the Great Recession. For example, as explained in POIR No. 1, question 9, the Great Recession continues to display more tenacity than almost anyone expected. Changes of this nature have a significant effect on underlying mail volume trends and continue to adversely impact the Postal Service.

Unlike every other recession since World War II, the Great Recession was accompanied by a financial crisis and a sustained drop in household net worth. The unemployment rate has exceeded seven percent for almost five years, despite the withdrawal of millions of discouraged workers from the labor force. Indeed, the unemployment rate would currently be 10.9 percent if the workforce participation rate were as high as it was in January 2009. Public attitudes have become deeply pessimistic in ways apparently unprecedented since World War II.[5] The economist and

[5] In past recessions, more than half of Americans believed their incomes would grow in the next year; not this time. The share expecting gains collapsed to less than 45 percent after 2008 and is still below half, finds a study by Federal Reserve economist Claudia Sahm. *See* Federal Reserve "FEDS Notes" Sept. 26, 2013, *Why Have Americans' Income Expectations Declined So Sharply?* The despondency, she writes, may signal a permanent shift in consumer psychology that undermines recovery.

New York Times columnist Paul Krugman recently suggested that “depression-like conditions” might persist “for decades.”[6]

We are in unfamiliar economic territory and as demonstrated in this proceeding, effects “due to” the Great Recession persist. By law, regulation, and Order No. 864, the Postal Service must include in the “due to” calculation the *total* impact on mail volume from the exigent event (*i.e.*, the Great Recession). The Commission fails to account for the entire, ongoing impact of the exigent event on the Postal Service’s ability to recover lost contribution.

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Robert G. Taub, Vice Chairman

[6] November 17, 2013, New York Times, Paul Krugman Op-Ed, *A Permanent Slump?*