

Postal Regulatory Commission Chairman Dan G. Blair

Statement before the Senate Subcommittee on Federal Financial Management, Government Information, Federal Services, and International Security

Wednesday, January 28, 2009

Chairman Carper, Ranking Member Coburn, and members of the Subcommittee, thank you for the opportunity to testify at this timely hearing to discuss the impact of the economic slowdown on the U.S. Postal Service. The mission of the Postal Regulatory Commission is to provide transparency and accountability into the financial operations of the Postal Service. We are the agency's primary regulator and work to provide a window on postal financial operations to Congress, stakeholders and the general public.

Eight years ago, this Committee asked the Government Accountability Office (GAO) to study the precarious financial situation of the Postal Service and its ability to meet its universal service obligation. At that time, the Postal Service revised its financial outlook from an estimated \$480 million deficit in FY 2001 to a \$2 to \$3 billion deficit a few months later. The inability to determine how the Service's financial picture could deteriorate so rapidly prompted the Committee to ask for a comprehensive review by GAO. This joint effort helped put the Service on a path towards financial transparency and transformation, which ultimately led to enactment of the Postal Accountability and Enhancement Act of 2006 (PAEA). The Commission appreciates this Committee's continuing active oversight to safeguard the long-term viability of the U.S. Postal Service and for adding it to the list of urgent issues that merit congressional attention.

Today, the Postal Service is facing troubling financial difficulties that stand to worsen before they improve. The current economic crisis has substantially impacted Postal Service volumes and revenues. For example, the financial sector, which has seen an implosion, accounted for approximately 15 percent of the U.S. Postal Service operating revenues according to the Postal Service's *2008 Annual Report* (p. 23). The economic downturn comes on the heels of continued diversion of single-piece First Class Mail to e-mail and electronic bill payments. The cumulative result of these events has been the most severe volume declines since the Great Depression and significant financial losses for the Postal Service. Postal Service data show

volume declines for every domestic class of mail in FY 2008, with First-Class Mail volume declining almost 5 percent.

To address this crisis in the short-term, the Postal Service has only a limited number of options available for financial relief.

Of the options available, one might include the filing of an “exigent” rate case, which would allow the Postal Service to raise its rates for market dominant products higher than the CPI-based rate cap imposed by the PAEA. To do so, the Service would file an exigency rate case with the Commission and demonstrate “extraordinary or exceptional circumstances” (39 U.S.C.A., §3622). Within 11 months of the enactment of the PAEA, the Commission developed a rate-cap based system for market dominant product rate adjustments. The intent of the new system is to ensure regular, predictable rate adjustments as envisioned by the PAEA. We now expect to receive notification from the Postal Service early each year of a proposed inflation-based rate adjustment for market dominant products. In fact, we anticipate receiving the Service’s next proposed increase in February. To add an exigency filing on top of the anticipated annual rate increase could possibly drive more mailers out of the system, further diminishing future postal volumes and revenues.

Another option would be additional cost reductions. According to the Postal Service, it plans to further reduce costs by \$4 billion in FY 2009. Additional reductions could also be considered. For example, the Service could reduce mail delivery to households from six to five days. In the Commission’s recent *Report on Universal Postal Service and the Postal Monopoly*, we determined that if the Postal Service were to make this service reduction, it could save a potential \$1.9 billion annually. A Postal Service study estimated annual savings of \$3.5 billion. Reductions in service, however, carry potential risks. For instance, the Postal Service estimate did not account for losses in volume as a result of reducing service. The Commission, in its USO Report, recommended that the Postal Service assess how major mailers might react to such a change in service should the Postal Service opt for this type of reduction.

Current annual appropriations language prohibits the Postal Service from reducing mail delivery from six days a week. Therefore, any proposals to change the frequency of mail delivery must be reviewed by Congress. The appropriations language also places restrictions on the closing of small and rural post offices. Congress may want to revisit these legislative limitations if it determines that delivery and service reductions are necessary to ensure future financial viability of the Postal Service.

Congress may also wish to consider raising the Postal Service’s total debt limit as another means of addressing the Service’s financial situation. However, additional debt would have to be paid back with interest. Currently, the Postal Service has a \$15 billion debt ceiling and may increase their debt load no more than \$3 billion in any one year. Over the last three years, the

Postal Service has increased its long term debt outstanding from \$0 in FY 2005 to \$7.2 billion at the end of FY 2008.

Another possible approach would be increasing the direct appropriation from Congress to cover additional operating expenses. The Postal Service generated nearly \$75 billion in ratepayer revenues in FY 2008. The Postal Service is supported almost exclusively by ratepayers and received only \$103 million through direct appropriations. This appropriation covers free mail for the blind, overseas voting, and a reimbursement of prior revenue foregone authorized by the Revenue Foregone Reform Act of 1993.

In considering its options, the Service is seeking legislative relief through an adjustment to its retiree health benefits premium payments. Unlike other federal agencies, the Postal Service is required by law to fund the cost of health benefits premiums for both current and future retirees. Additionally, the Service is required to pay into the Postal Service Retiree Health Benefits Fund regularly scheduled payments as required by law through 2016. As of September 30, 2008, this fund had a positive balance of \$32.6 billion.

This fund is the result of recommendations made in July 2003 by the President's Commission on the United States Postal Service in its report to Congress entitled, "Embracing the Future: Making the Tough Choices to Preserve Universal Mail Service." The report identified the Postal Service's estimated unfunded retiree health benefit of \$48 billion as of FY 2003.

The President's Commission "strongly encouraged" the Postal Board [of Governors] to acknowledge the extent of the obligation in its financial statements, based on the public's "right to know" the fiscal health of its public institutions. The President's Commission also recommended that, "... the Board consider funding a reserve account to begin paying down this obligation, so future ratepayers [would] not be forced to pay for postal services delivered to the nation today."¹

At the time the Report was issued, both the Senate and the House of Representatives postal oversight committees were contemplating postal reform. Ultimately, each body produced reform legislation which required the Service to begin paying down its outstanding unfunded retiree health benefits liabilities.

Ultimately, the Congress enacted the PAEA which required the Postal Service to fund health benefits for current and future Postal retirees according to a mandated payment schedule through 2016. The law requires Postal retiree health benefits be evaluated annually by the Office of Personnel Management with the goal of satisfying any liability funding requirements by 2056.

¹ Report of the President's Commission on the United States Postal Service, p. 124

The Postal Service was also granted a right to request a review of OPM's determinations by the Postal Regulatory Commission (5 U.S.C.A., §8348).²

The total payment for FY 2009 for retiree health benefits is estimated at approximately \$7.4 billion. This includes the scheduled payment of \$5.4 billion, as mandated by the PAEA, and an estimated \$2 billion for current retiree health benefit premiums.

Given its limited choices, a temporary adjustment to the Service's health benefit payment schedule would appear to be the most pragmatic approach for the short term. However, Congress should consider carefully the impact of allowing the Postal Service early access to the Retiree Health Benefits Fund to meet current needs without a plan for ensuring the sustainability of the fund to address the long-term health benefit liabilities.

The Commission recommends that Congress require the Postal Service to provide Congress, the Commission, and the GAO with a comprehensive, forward-looking financial plan. Such a plan should provide more detail than the current strategic plan on how the Service intends to regain long-term financial stability in light of the real possibility of continually declining mail volumes.

As the members of this Subcommittee know, a key goal of the 2006 Act was striking a balance between the Postal Service's need for additional flexibility with the public and mailing community's need for increased financial transparency. The Act granted the Commission new regulatory power to ensure the financial transparency of the Postal Service. The law also requires the Service to comply with Securities and Exchange Commission-like reporting requirements.

As part of the Commission's regulatory responsibilities, my fellow Commissioners and I meet often with Postmaster General John Potter, Deputy Postmaster General Patrick Donahoe, and senior postal executives. We know from these meetings that the Postal Service is focused on addressing this fiscal crisis and is working to make the difficult decisions needed to preserve the Service's financial health and sustainability.

At this time, the Commission is reviewing the Postal Service's Annual Compliance Report (ACR). The Commission's review of this report will address compliance of rates and fees under applicable standards, as well as whether service standards in effect during the period covered by the 2008 ACR were met. This determination, however, focuses on activities of the

² The estimated unfunded liability for the Retiree Health Benefits Fund for FY 2007 and FY 2008 are \$55.0 billion and \$53.5 billion respectively. USPS Form 10-K filing with the Postal Regulatory Commission at pages 18-20.

prior fiscal year. More information about the Postal Service's current financial performance, including access to its integrated financial plans and how well it is performing against that plan, would provide Congress and stakeholders with a clearer picture of postal financial operations.

Mr. Chairman, during this time of financial downturn, timely and sufficient - as well as accessible information on operating results - is crucial. Publicly available monthly reports - to Congress and the Commission - will help keep postal stakeholders abreast of changes in trends and allow prompt reaction to changing circumstances. From 1972 through 2006, the Postal Service submitted monthly accounting period statements to the Commission and Congress. These reports were publicly available and remain posted on the Postal Service's website. However, in 2006, the Service stopped providing this information to the public. Postal management, of course, gets weekly and even daily updates of operations.

Given the tenuousness of the Postal Service's financial situation, more – not less – transparency is called for. The Commission recommends that the Postal Service provide Congress and the Commission with monthly financial reports. These reports are part of the Commission's tools to assess postal finances, operations and service.

Chairman Carper, this concludes my written statement. Again, I thank you for inviting me to testify. I welcome the opportunity to answer any questions members of the Subcommittee may have.