AUTHENTICATED
U.S. GOVERNMENT
INFORMATION
GPO

CONTINUING TO DELIVER: AN EXAMINATION OF THE POSTAL SERVICE'S CURRENT FINANCIAL CRISIS AND ITS FUTURE VIABILITY

JOINT HEARING

BEFORE THE

SUBCOMMITTEE ON FEDERAL WORKFORCE, POSTAL SERVICE, AND THE DISTRICT OF COLUMBIA

AND THE

COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM

HOUSE OF REPRESENTATIVES

ONE HUNDRED ELEVENTH CONGRESS

SECOND SESSION

APRIL 15, 2010

Serial No. 111–74

Printed for the use of the Committee on Oversight and Government Reform

Available via the World Wide Web: http://www.gpoaccess.gov/congress/index.html
http://www.house.gov/reform

U.S. GOVERNMENT PRINTING OFFICE

58–338 PDF WASHINGTON : 2010

For sale by the Superintendent of Documents, U.S. Government Printing Office
Internet: bookstore.gpo.gov Phone: toll free (866) 512–1800; DC area (202) 512–1800
Fax: (202) 512–2104 Mail: Stop IDCC, Washington, DC 20402–0001

COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM

EDOLPHUS TOWNS, New York, *Chairman*

PAUL E. KANJORSKI, Pennsylvania
CAROLYN B. MALONEY, New York
ELIJAH E. CUMMINGS, Maryland
DENNIS J. KUCINICH, Ohio
JOHN F. TIERNEY, Massachusetts
WM. LACY CLAY, Missouri
DIANE E. WATSON, California
STEPHEN F. LYNCH, Massachusetts
JIM COOPER, Tennessee
GERALD E. CONNOLLY, Virginia
MIKE QUIGLEY, Illinois
MARCY KAPTUR, Ohio
ELEANOR HOLMES NORTON, District of Columbia
PATRICK J. KENNEDY, Rhode Island
DANNY K. DAVIS, Illinois
CHRIS VAN HOLLEN, Maryland
HENRY CUELLAR, Texas
PAUL W. HODES, New Hampshire
CHRISTOPHER S. MURPHY, Connecticut
PETER WELCH, Vermont
BILL FOSTER, Illinois
JACKIE SPEIER, California
STEVE DRIEHAUS, Ohio
JUDY CHU, California

DARRELL E. ISSA, California
DAN BURTON, Indiana
JOHN L. MICA, Florida
MARK E. SOUDER, Indiana
JOHN J. DUNCAN, JR., Tennessee
MICHAEL R. TURNER, Ohio
LYNN A. WESTMORELAND, Georgia
PATRICK T. MCHENRY, North Carolina
BRIAN P. BILBRAY, California
JIM JORDAN, Ohio
JEFF FLAKE, Arizona
JEFF FORTENBERRY, Nebraska
JASON CHAFFETZ, Utah
AARON SCHOCK, Illinois
BLAINE LUETKEMEYER, Missouri
ANH "JOSEPH" CAO, Louisiana

RON STROMAN, *Staff Director*
MICHAEL MCCARTHY, *Deputy Staff Director*
CARLA HULTBERG, *Chief Clerk*
LARRY BRADY, *Minority Staff Director*

SUBCOMMITTEE ON FEDERAL WORKFORCE, POSTAL SERVICE, AND THE DISTRICT OF COLUMBIA

STEPHEN F. LYNCH, Massachusetts, *Chairman*

ELEANOR HOLMES NORTON, District of Columbia
DANNY K. DAVIS, Illinois
ELIJAH E. CUMMINGS, Maryland
DENNIS J. KUCINICH, Ohio
WM. LACY CLAY, Missouri
GERALD E. CONNOLLY, Virginia

JASON CHAFFETZ, Utah
MARK E. SOUDER, Indiana
BRIAN P. BILBRAY, California
ANH "JOSEPH" CAO, Louisiana

WILLIAM MILES, *Staff Director*

CONTENTS

CONTINUING TO DELIVER: AN EXAMINATION OF THE POSTAL SERVICE'S CURRENT FINANCIAL CRISIS AND ITS FUTURE VIABILITY

THURSDAY, APRIL 15, 2010

HOUSE OF REPRESENTATIVES, COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM, JOINT WITH THE SUBCOMMITTEE ON FEDERAL WORKFORCE, POSTAL SERVICE, AND THE DISTRICT OF COLUMBIA,

Washington, DC.

The committee and subcommittee met, pursuant to notice, at 10 a.m., in room 2154, Rayburn House Office Building, Hon. Stephen F. Lynch (chairman of the subcommittee) presiding.

Present: Representatives Lynch, Maloney, Cummings, Kucinich, Tierney, Clay, Watson, Connolly, Quigley, Davis, Foster, Speier, Driehaus, Chu, Issa, Burton, Duncan, Jordan, and Luetkemeyer.

Staff present: Peter Fise, staff assistant; Adam Hodge, deputy press secretary; Carla Hultberg, chief clerk; Marc Johnson and Ophelia Rivas, assistant clerks; Michael Kubayabda, counsel; Mark Stephenson, senior policy advisor; Ron Stroman, staff director; William S. Miles, staff director, Subcommittee on Federal Workforce, Postal Service, and the District of Columbia; Larry Brady, minority staff director; John Cuaderes, minority deputy staff director; Rob Borden, minority general counsel; Adam Fromm, minority chief clerk and Member liaison; Stephanie Genco, minority deputy press secretary; Howie Denis, minority senior counsel; and Alex Cooper, minority professional staff member.

Mr. LYNCH. Good morning and welcome.

What is encouraging about today's hearing is that it is being convened to specifically discuss suggested solutions for addressing what many have called an unsustainable business model in need of urgent attention and reform. I have had a chance to review both the Postal Service's action plan for the future as well as the recently released GAO report on strategies and options to facilitate progress toward financial viability, and I commend both of those entities for your thorough analysis.

And, given the Postal Service's currently dire situation, both of these reports rightfully touch on some critical and highly controversial issues such as calling for major changes in the frequency of mail delivery, statutory pricing, facility and network optimization and employee compensation and benefits.

I think we all get the fact that the difficult times will require some difficult decisions to be made, and the impact of some of these decisions will more than likely fall heavily across the board, affecting the Postal Service, its customers, employees, stakeholders, and others.

While at the moment there may not be exactly a consensus on what needs to be done to bring about the financial recovery of the Postal Service. The one thing we believe we are all in agreement on is that doing nothing is no longer a viable option.

The keystone of a $1.2 trillion mailing industry and the employer of nearly 700,000 Americans, the solvency and long-term operation of the U.S. Postal Service is essential to our national economy and to our way of life, which is why I am glad that today's hearing gives us an opportunity to lay everything from the value of mail nowadays to the debate over the Postal Service's civil service retirement system out on the table for deliberation and consideration.

I appreciate today's witnesses for being here with us this morning to offer their suggested strategies on how best to increase revenue, reduce cost, and improve efficiency going forward in order to help ensure the future financial viability of the Postal Service.

Again, I would like to thank the chairman, Mr. Towns, for agreeing to hold this joint hearing, and I look forward to an informative discussion this morning.

On our first panel we will hear from the Postal Service and GAO on their reports, while our second panel will discuss the impact of these recommendations and the CSRS pension issues.

Again, I thank all of our witnesses for appearing today, and I look forward to their testimony.

[The prepared statement of Hon. Stephen F. Lynch follows:]

STATEMENT OF CHAIRMAN STEPHEN F. LYNCH

The Committee on Oversight and Government Reform and the Subcommittee on Federal Workforce, Postal Service, and the District of Columbia

Joint Hearing

"Continuing to Deliver: An Examination of the Postal Service's Current Financial Crisis and its Future Viability."

Thursday, March 25, 2010 at 2:00 p.m.
2247 of the Rayburn House Office Building

I thank the Chair for yielding time and for also agreeing to hold today's hearing, which goes to show that you also recognize the critical state of affairs currently confronting the United States Postal Service. As Chair of the Subcommittee with oversight jurisdiction over the Postal Service, I continue to be quite concerned about the recent financial and operational challenges that have caused one of our nation's most robust and fully solvent public entities to end the past three consecutive fiscal years in the red – cumulatively, to the tune of nearly $12 billion dollars. It's no secret that much of the Postal Service's recent financial woes stem from dramatic declines in mail volume and corresponding revenue losses, which are attributable to increased diversion to new modes communication, the nationwide economic downturn and, in some ways, statutorily imposed benefit obligations, such as the prefunding of future retiree health costs. And if projections for this year's end holds true, the Postal Service could stand to lose an additional $7 plus billion dollars.

While we have all known for quite sometime the sources of many of the Postal Service's problems, what's encouraging about today's hearing, Sir, is that it's being convened to specifically discuss suggested solutions for addressing what many have called an "unsustainable business model" in need of urgent attention and reform. I've had a chance to review both the Postal Service's "Action Plan for the Future" as well as the recently released GAO report on "Strategies and Options to Facilitate Progress towards Financial Viability" and commend you both for performing such thorough analysis. Given the Postal Service's current dire situation, both of these reports rightfully touch on some critical and highly controversial issues, such as calling for major changes in the frequency of mail delivery, statutory pricing, facility and network optimization and employee compensation and benefits.

I think we all get the fact that difficult times will require some difficult decisions to be made and the impact of some of these decisions will more than likely fall heavy, across the board – affecting the Postal Service, its customers, employees and stakeholders alike. While at the moment there may not be exact consensus on what needs to be done to bring about the financial recovery of the Postal Service, the one thing I believe we are all in agreement on is that 'doing nothing' is no longer a viable option. The keystone of a $1.2 trillion dollar mailing industry and the employer of nearly 700,000 Americans, the solvency and long term operation of the United States Postal Service is essential to our nation's economy and to our way of life, which is why I am glad that today's hearing gives us an opportunity today to lay everything - from the value of the mail nowadays to the debate over the Postal Service's Civil Service Retirement System responsibility - out on the table for deliberation and consideration.

I appreciate today's witnesses for being here with us this morning to offer their suggested strategies on how best to increase revenue, reduce costs and improve efficiency going forward in order to help ensure the future financial viability of the Postal Service. Again, I'd like to thank the Chairman for agreeing to hold this joint hearing, and I look forward to an informative discussion this morning.

###

Mr. LYNCH. I now yield 5 minutes to our ranking member, Mr. Darrell Issa from California, for his opening statement.

Mr. ISSA. Thank you, Mr. Chairman.

Mr. Chairman, last year we worked together on a bipartisan basis to provide a temporary fix. This committee had hoped that fix would be slightly longer; however, at the end of the day it was a 1-year kick the can down the road fix. Today, it is clear that before any fix of any sort is considered by this committee, we must have a plan that will bring right-sizing, solvency, and a continued level of high service by the Post Office.

Without that level of high service, we do not meet our Constitutional responsibility, which this committee has direct oversight on. Without right-sizing, the services versus the people versus the equipment versus—and I am going to cross the line that we never want to cross—versus the number of physical locations around the country manned by postal personnel, we cannot get even.

For more than 30 years I have been either an executive or member of the board of a company. I still sit on a public company. We are the fiduciaries of your enterprise. As fiduciaries of your enterprise, we must tell you, you have at the current time more or less a third more people than you are properly using. If you were to use the minimum amount of people, highly motivated, properly compensated, you would clearly have a dramatic amount of less people.

Having said that, we have been remiss from the dais in meeting our responsibility. During the last year since we began dealing specifically under this chairmanship with this problem, the Federal work force has grown by nearly as many, if not more, than the amount of people at your surplus. Postal workers are Federal workers. Postal workers are vested in an equivalent system and a transferrable system to that which we here on the dias and all Federal workers are in.

Although there are some slight differences, it is very clear that we have not recognized that if the postal system has more workers than it needs, the Federal work force in general has less than it needs, postal workers represent what is or has been a highly motivated, fairly compensated group of individuals at all levels, entry, managerial, supervisal, and executive.

I hope today, in addition to prepared statements that we have read and we will hear capsulated, that we will hear about the kind of synergies the Federal Government needs to achieve in duties, and from the dias many have suggested that the census should have been done all or in part by those Federal workers presently working for the post office, and other innovative ideas that could be done to make better use of postal facilities.

But more importantly, you must leave here today understanding that Congress needs a plan, like any other Board of Directors, that passes the sniff test, that will, in fact, be reasonable for us to say to the American people the post office will be self-sufficient and solvent, which is a requirement of Congress, but, more importantly, that we are not wasting the time and energies of so many people who have in the past been well-motivated, loyal workers to the postal system by simply saying, sit in the green room, blue room, any color room you have, but today many of them sit in waiting rooms. Nothing is more demoralizing to a worker than to be excess with no plan to deal with that in the future. No postal worker should be given a route that is less than a full day's work. No postal worker should be on the ready if, in fact, that ready bell is not likely to ring.

So, Mr. Chairman, I have been supportive of the postal workers. I intend to continue to be, but I want to make sure that we are doing the best thing we can for those people, and if the American people are watching us hire throughout the Federal work force people who, with transition funds that we could authorize and appropriate, could find themselves in permanent positions, I do not want to wait until it is time to put people on the street who otherwise would be gainfully employed in the Federal service that they signed up for 1, 2, 5, 20, or 30 years ago.

Mr. Chairman, I look forward to the comments and I look forward to working together on a bipartisan basis to fix this troubling problem.

I yield back.

[The prepared statement of Hon. Darrell E. Issa follows:]

EDOLPHUS TOWNS, NEW YORK
CHAIRMAN

DARRELL E. ISSA, CALIFORNIA
RANKING MINORITY MEMBER

ONE HUNDRED ELEVENTH CONGRESS

Congress of the United States

House of Representatives

COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM

2157 RAYBURN HOUSE OFFICE BUILDING
WASHINGTON, DC 20515–6143

Majority (202) 225–5051
Minority (202) 225–5074

Statement of Rep. Darrell Issa, Ranking Member

"Continuing to Deliver: An Examination of the Postal Service's Current Financial Crisis and its Future Viability."

April 15, 2010

Thank you, Mr. Chairman, for holding today's hearing about the ongoing struggles facing the Postal Service and their plans for the future.

Within the broad jurisdiction assigned to this Committee, the responsibility to oversee the United States Postal Service is one of the most critical. Article I, Section 8, of the U.S. Constitution provides that Congress has the power to "establish post offices and post roads." This power, from the earliest days of our Republic, was thought to be relatively benign. But soon after ratification, controversy set in over the extent of Congressional authority.

Nearly one hundred years after Congress established the Office of Postmaster General, the Supreme Court handed down a landmark decision that affirmed the far-reaching power of Congress over the mail. In fact, Congressional control over the Postal Service has been characterized as a constitutionally-mandated monopoly. There is no other authority, and no other institution of oversight, with the ultimate responsibility to address the many problems facing the Postal Service.

And that is why, Mr. Chairman, it falls to us today to examine the causes of the current financial crisis and challenges to the Postal Service's future viability. Those challenges, Mr. Chairman, are many.

First, USPS is rapidly losing revenue. Even before the effects of the current recession were being felt, the price of postage was gradually rising and the volume was steadily dropping. Congress requires the Postal Service to operate like a business, and to be self-supporting, yet the relative inflexibility in pricing hinders USPS's ability to compete with their private sector counterparts.

Second, USPS is struggling with the fiscal strain brought on by an oversized organization. It is clearly time to right-size its workforce to meet current demand. Existing contracts severely limit USPS from adjusting its workforce to bring cost in line with revenue. In spite of efforts to cut labor costs, they continue to consume roughly 80% of total Postal revenue each year. Studies have indicated that a significant reduction in the Postal workforce is in the best interest of the Postal Service and its customers.

Statement of Rep. Darrell Issa, Ranking Member
April 15, 2010
Page 2

We are aware that this year the Postal Service is negotiating two major union contracts and two more next year. These negotiations cannot be business-as-usual. If USPS expects congressional cooperation, then it is going to have to present a strategic plan that brings postal services – including its labor problems – in line for long-term viability.

Third, USPS is struggling to keep pace with technology. Electronic mail and other recent advances in technology offer the kind of convenience and timely delivery that neither the Postal Service nor its private sector counterparts can provide. Facing this reality, USPS must reinvent itself to survive and thus perform its core function of providing mail delivery to every American address.

Last year, Mr. Chairman, we worked on a bipartisan basis to enact H.R. 22 and provide a quick fix for USPS's financial problems. As we approach the fall, we are aware that those problems have not been resolved in any fundamental way, and that a major funding issue is still upon us. Indeed, if we fail to enact serious postal reforms this year, we will have no choice but to come head-to-head with the possibility of another taxpayer bailout. This we will not allow.

To ensure the future success of USPS, every option must be on the table. I trust, Mr. Chairman, that we will be able to build upon our past collaboration to find a permanent bipartisan solution, and I look forward to hearing from today's witnesses.

###

Mr. LYNCH. I thank the gentleman. By prior agreement, the Chair recognizes Mr. Kucinich for 5 minutes.

Mr. KUCINICH. I thank the chairman for holding the hearing on this matter of great significance to the American people.

I want to begin by thanking the men and women who have dedicated their lives to making sure that the commerce of this Nation moves through the mail. Many of you made a life commitment to that work, and it ought to be received with great appreciation by this Congress and by the American people.

The financial issues that are facing the Postal Service will be dealt with, and I am hopeful that this committee will have the opportunity to deal with it in a way that preserves the good faith which the people who serve the U.S. Postal Service have a right to expect from this Congress, and will preserve the appreciation which the American people have for those who are involved in the delivery of the mail.

I understand the importance to local communities of the Postal Service, and I am committed to working with all stakeholders to ensure its financial viability.

In November of last year, this subcommittee held a hearing to examine possible methods of revenue generation, and we know that since then we have seen a great amount of money continue to be lost and the postal consolidation campaigns persist. I am concerned that some of the proposals being considered could lead to the privatization of essential services.

As someone who has had to deal with privatization issues many years ago as a mayor of a city, I can promise you that this is one Member who is not going to sit by and let you use the excuse of financial difficulties as a path to privatize a service that first and foremost ought to be a commitment to the American people of regular delivery of the mail at a fair and reasonable price.

I strongly believe there are ways to generate revenue without cutting jobs and essential services. The GAO report makes the observation that 300,000 postal employees are expected to retire through 2020. It points out that in a 3-year period over 84,000 employees were reduced from the career work force. So it is not as though people aren't looking for ways to operate more efficiently with less people. We have to be careful that we don't, through the desire to try to make this system work more efficiently, harm its ability to deliver the mail.

My constituents continue to express their concern over post office closing, especially in low-income communities with little or no access to transportation or technology. Ultimately, it is going to be up to the Congress to give the Postal Service the flexibility it needs to implement vital revenue generation methods. At the same time, it is our responsibility to ensure that methods of revenue generation do not come at the cost of universal access and the jobs that have been vital to the communities we represent, because universal access is something that is important to the people of this country and it is a major economic issue in communities across America, and it should not be denied to people because they happen to be on a lower end of the economic ladder.

The Postal Service has a very powerful infrastructure already in place, and that should be utilized in any future plan. Instead of consolidating branches and its work force, the Postal Service should examine ways it can provide services and training for its employees that will allow it to complete with some of the other entities that are already out there.

Chairwoman Goldway and National Postal Worker Unions have provided excellent ideas that warrant further examination, such as providing Government services at local post offices and providing retailers a space to sell their services or products.

As the economy moves toward recovery, we must ensure that local post offices are there to serve the local community.

I thank the chairman.

Mr. LYNCH. I thank the gentleman.

The Chair now recognizes the ranking member of the Postal Subcommittee for 5 minutes.

Mr. CHAFFETZ. Thank you, Mr. Chairman. I do appreciate the bipartisan approach in working on these issues, and I do appreciate the efforts that the Postal Service has made.

I am new to this as a freshman here, and I have actually got to tell you that I was pleasantly surprised and appreciative of the fact of how the Postal Service has been addressing the financial needs in a very proactive way and a very difficult way, but being financially responsible and having that at the top of their agenda.

There are difficult decisions to be made. They are going to be painful any way you slice it. But I only wish every other agency within the Federal Government would be as responsive to the financial needs within their agency and their department as the Postal Service has been.

Again, they are upside down financially and struggling, but, again, I wish other departments and agencies would have the same type of approach in being responsible, making difficult decisions, and making the cuts that need to be there.

I also do believe that we need to continue the discussion on the relevancy of the Postal Service and making it more relevant in the business community, making it more relevant in people's lives, and how to drive revenue. We have had good discussions and will continue to have good, hard discussions about where to cut costs, but we also need to continue that discussion about how to become more innovative and how do we service the American people in a better way that will actually drive revenue forward.

Personally, I have deep concerns about the move from a 6-day delivery down to a 5-day delivery. I think there should be a blend. My personal approach to this is that we should give you some flexibility to find "postal holidays" so that you can have the flexibility to take the least, the days that we know that there is less demand and less need in the marketplace to actually deliver, but to say that we are going to eliminate 52 days of service is not going to necessarily drive volume forward.

I don't think eliminating Saturday delivery before the Christmas holiday is necessarily wise. When you look at the fact that we have Mother's Day on a Sunday, I don't think the marketplace is going to be very happy about not being able to deliver mail on Saturday.

Also, if you look at it in a given year, we will have eight or nine holidays where you will not have service on a Monday or a Friday because there is a national holiday, so there are 8 or 9 weeks out of the year where we would go for 3 days with no postal delivery services, and there are many unintended consequences where credit card bills and medicine that may be delivered through the mail and those types of things that I think they need to be more thoroughly explained.

Again, I would hope that we would explore a blend where we give you some flexibility to find that Saturday in August nobody is going to miss it so you can trim costs.

The other thing, Mr. Chairman, that I hope we look at is I still believe that this country lacks in energy policy. If you look at the fuel prices, in January 2009 they were less than $2 a gallon. Now, at least in Utah, I am paying more than $3 a gallon. This country does not have an energy policy, and when we have rising energy costs one of the consequences is a tremendous expense to the Postal Service in the delivery of its goods and services.

Obviously, the biggest thing out there that we have to talk about that is difficult is labor. When you have 80 percent of your expenses tied up in the labor pool, there are going to have to be some very difficult decisions and discussions. I know we have some tough labor negotiations that are coming up. We need to talk about rightsizing the Postal Service and dealing with that. As Congressman Issa talked about, it would be better, best if we could make some of the transition in the astronomical growth we have in the other departments and agencies and being able to transition some of the good Federal workers there at the Postal Service into other applicable jobs. I would hope that we would do a better job of making those transitions.

And then certainly one of the big things that I want to more thoroughly understand, Mr. Chairman, is the CSRS pension issues that we have out there because that over-funding issue is something that we can't just deal with on a Band-aid on a year-by-year basis. But, as Ranking Member Issa said, we have to deal with it in a long-term fashion.

So those are some of my thoughts and perspectives. I look forward to this discussion and ongoing discussion and appreciate the bipartisan way in which we are doing this.

With that I yield back, Mr. Chairman.

Mr. LYNCH. I thank the gentleman.

We will now turn to our first panel of witnesses. It is the committee's policy that all witnesses to offer testimony have to be sworn. Will the witnesses please stand and raise your right hands as I administer the oath?

[Witnesses sworn.]

Mr. LYNCH. Thank you. Let the record show that the witnesses have each answered in the affirmative.

I am going to ask you to bear with me while I do two brief introductions.

Mr. John E. Potter serves as the Postmaster General and CEO of the U.S. Postal Service. Mr. Potter was named the 72nd Postmaster General of the United States of America on June 1, 2001. He currently sits on the Postal Service Board of Governors and is vice chairman of the International Postal Corp., an association of 23 national posts in Europe, North America, and the Asia Pacific.

Mr. Phillip Herr is currently the Director of Physical Infrastructure Issues at the U.S. Government Accountability Office. Since joining GAO in 1989, he has managed reviews of a broad range of domestic and international programs. His current portfolio focuses on programs at the Department of Transportation and the U.S. Postal Service.

Mr. Potter, you are now welcome to offer a 5-minute statement. Thank you.

STATEMENTS OF JOHN E. POTTER, POSTMASTER GENERAL AND CEO, U.S. POSTAL SERVICE; AND PHILLIP HERR, DIRECTOR, PHYSICAL INFRASTRUCTURE ISSUES, U.S. GOVERNMENT ACCOUNTABILITY OFFICE

STATEMENT OF JOHN E. POTTER

Mr. POTTER. Good morning, Mr. Chairman and members of the committee.

For the past 2 years I have testified about the dire financial situation facing the U.S. Postal Service. Today we stand on the brink of financial insolvency, and our cumulative losses could exceed $238 billion by 2020.

I am pleased to report that the Postal Service does have a plan for action to close the growing gap between revenues and expenses; however, before discussing our plan, I would like to comment on a recent audit by our Inspector General concerning the Postal Service over-payments to the Civil Service Retirement System pension fund.

The IG's report is of such significance that it could have an enormous bearing on the speed with which we need to make changes outlined in our plan. The IG found that an inequitable and unreasonable cost sharing methodology was used when the former Post Office Department was reorganized into the Postal Service. That methodology caused the Postal Service to contribute a disproportionate share of CSRS pension costs, resulting in a $75 billion overpayment. We support the IG's recommendation for dividing the responsibility of funding CSRS retirements for our employees by splitting the total pension obligation between pre- and post-1971 employment.

Refunding the $75 billion to the Postal Service would not eliminate the need for us to take additional actions, but it would lessen the immediate financial crisis we are facing. I urge you to take a close look at this critical issue as the first step in resolving the Postal Service financial challenge.

The way Americans communicate has changed dramatically, and the Postal Service has to change. Our management team, with the support and approval of our Board of Governors, has developed a responsive, ambitious, and balanced plan that offers a way forward for a fiscally sound Postal Service. To help close the forecasted $238 billion gap by 2020, our action plan has identified $123 billion of cost savings that are within postal control, and we are implementing those actions today.

We are also focused on growth and we are introducing new products and pricing incentives consistent with our mission, and we are expanding and modernizing our retail access. I am confident that these strategies and other steps from our action plan will allow the Postal Service to remain a viable and valuable entity into the future, allowing us to continue to maintain and finance universal service nationwide; however, we do need congressional help in some key areas to provide management with the flexibility to deal with our financial situation.

Specifically, we request your assistance in restructuring the prefunding of retiree health benefits, adjusting the frequency of mail delivery, providing the freedom to offer access to postal services in places other than traditional post offices, requiring arbitrators to consider the financial condition of the Postal Service, applying the Consumer Price Index price cap to all market-dominant products as opposed to on a class-by-class application, introducing new products consistent with our mission, and, finally, helping us to acquire more streamlined oversight.

The first two of these proposed changes will generate the largest and most immediate financial benefits and move us toward narrowing our financial gap. If Congress is unable to act this fiscal year on broader legislation, our projections show that we will risk running out of cash early in fiscal year 2011; therefore, should there be insufficient time this year to pass comprehensive legislation, the Postal Service will require a reduction in our retiree health benefit trust fund payment this year similar to 2009.

We recognize that our agenda is ambitious and that the challenge will be finding the right balance between taking actions necessary to mitigate our financial crisis, while at the same time implementing a smooth transition for our customers and our employees.

The GAO recognizes the challenge facing us, too. In their recently released report on the Postal Service, they do a thorough job of reviewing a series of complex issues and strategies for long-term structural and operational reform. I am pleased that many of the GAO's findings are consistent with the analysis and the Postal Service action plan, and that the GAO agrees with us that we need congressional action on removing some of our current legal and regulatory constraints.

One area where we disagree with the GAO is their recommendation that additional panels of experts or commissions be established to develop legislative options or proposals for change. Due to the urgency of our finances, we cannot support this. We believe that a sufficient body of evidence exists to help guide the Congress on the changes needed for the future. Our action plan provides us a solid path to ensure that the Postal Service remains strong, healthy, and viable into the future.

Our challenges are urgent, and I look forward to working with the Congress, the GAO, the PRC, and the entire postal community in implementing the best choices for success.

Thank you for your support of our ongoing efforts to ensure a sound Postal Service, and I will be happy to answer any questions you may have.

[The prepared statement of Mr. Potter follows:]

UNITED STATES
POSTAL SERVICE

STATEMENT OF
POSTMASTER GENERAL/CEO JOHN E. POTTER
BEFORE THE
COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM
UNITED STATES HOUSE OF REPRESENTATIVES
AND
SUBCOMMITTEE ON FEDERAL WORKFORCE, POSTAL SERVICE,
AND THE DISTRICT OF COLUMBIA

APRIL 15, 2010

Good morning, Mr. Chairman and members of the Committee. For the past two years, I have testified about the dire financial circumstances facing the United States Postal Service. Once again, I am here to report that our financial situation is precarious, mail volumes continue to decline, and the cost of delivering mail to each address continues to increase. While all postal stakeholders are aware of these circumstances, I am concerned that there is insufficient appreciation for the long-term financial peril that the Postal Service faces. Expert, independent analysis clearly shows an open-ended decline in mail volume and the revenues associated with it. The foundation of our self-sufficient business model has been swept aside by a digital communications revolution and a severe economic crisis. While our Nation will continue to rely on a dedicated delivery network offering universal service, it cannot be supported now and in the future by a business model based on increasing volumes and revenue. Today, the Postal Service stands on the brink of financial insolvency. Without significant and immediate changes, this pattern of constant financial distress will continue unabated for years to come.

Over the past several months, I have had many discussions with members of Congress, Administration officials, business mailers, chief executive officers, and consumers about our financial plight and the action needed to address it. Too much attention has been focused on short-term financial fixes, such as an adjustment to our retiree health benefits fund, or a single, significant service change, such as five-day delivery. Too little attention has been paid to the need for other, significant, across-the-board changes to our regulatory and legal framework. An independent examination of the postal marketplace projects an annual Postal Service loss of $33 billion in 2020 and cumulative losses of $238 billion over the next ten years, if we make little or no changes. A piecemeal approach with short-term financial relief only delays the inevitable, and impedes our ability to maintain productive and efficient operations. Without bold, decisive, and comprehensive action by this Committee and Congress, the Postal Service will face continual financial peril.

Before I discuss the Postal Service's action plan for the future, I would like to call your attention to a study conducted by our Office of Inspector General (OIG) regarding overpayments by the Postal Service to the Civil Service Retirement System (CSRS) pension fund. Given the significance of the OIG's findings, it is imperative that this matter be given prompt consideration by Congress and the Administration. Failure to resolve this matter quickly will have an adverse effect on Congress' ability to consider other legislative proposals beneficial to the Postal Service. It should also be noted that any financial adjustment to the Postal Service's CSRS fund would not eliminate the need for the changes proposed in our action plan, but it could influence the timing of their implementation.

The OIG looked at employees who worked for both the pre-1971 Post Office Department and the U.S. Postal Service. The report reviewed how the retirement obligation for those employees was divided. The CSRS provides annuities based on the employees' highest three-year average base wage and an increasing percentage credit for years of service. When calculating the Postal Service's portion of the obligation, the Office of Personnel Management (OPM) apportioned the obligation based only on the service and base salaries at the time of postal reorganization in 1971. OPM determined that the effects of future salary increases on the amount of the total pension obligation were not the responsibility of the federal government. The OIG maintains that the responsibility for pre- and post-1971 pension costs should be divided between the federal government and the Postal Service in a more reasonable manner. Such a calculation would recognize the future earning potential of postal employees at the time of the 1971 reorganization. The OIG study concluded that the Postal Service was overcharged $75 billion. We have asked the Postal Regulatory Commission (PRC) to retain an actuary in reviewing this matter, and to submit their findings to Congress.

The Postal Service supports the OIG recommendation that the Postal Service and the federal government split the total pension obligation for an employee's civilian service based on years of employment completed pre- and post-1971. This "years of service" method would divide pension liabilities in a far more equitable manner than the current system. OPM currently uses the "years of service" method in allocating health care premiums for retirees. Moreover, the CSRS overpayment could be transferred to finance the Postal Service's Retiree Health Benefits Trust Fund. We are asking Congress to amend the *Postal Act of 2006* to do the following:

- Require OPM to use of the methodology recommended by the OIG;
- Allow the transfer of the funds from the CSRS Trust Fund to the Retiree Health Benefits Trust Fund;
- Eliminate the annual average retiree health benefits pre-payment of $5.5 billion;
- Allow the annual premiums for existing retirees to be paid from the Retiree Health Benefits Trust Fund before 2017; and
- Allow the Postal Service to begin to pay the "normal" cost for its current employees.

This would mean that the Postal Service would be fully funded for both its retirement systems, as well as its health benefit obligation. And, since the Postal Service would be paying the normal cost for current employees, the Postal Service would continue to be fully funded for its retiree health benefits obligation. This change would save the Postal Service roughly $4.6 billion annually.

The OIG report states that "freeing the Postal Service from unjustified legacy costs is critical if the Postal Service is to have the agility it needs to face an uncertain future." It is the right thing to do, and I urge you to take a close look at this critical issue. To be clear, I believe the changes proposed in our plan are inevitable. Adoption of the OIG's recommendation would, however, affect the timing of when these options would need to be implemented.

In regard to our action plan for the future, the Postal Service Board of Governors and postal management have acted vigorously in responding to the ongoing nationwide economic crisis and electronic diversion that has so dramatically eroded mail volume in recent years. We have devoted this same effort in crafting a way forward in light of these circumstances. We used all the resources at our disposal to study current and future economic trends. We asked for an independent examination of the postal marketplace, projections for the future, and recommendations to address the financial and service problems we face. We sought the advice and counsel of the entire postal community in designing a path for the future that preserves affordable, universal mail service.

The results are both encouraging and sobering. While mail volume will continue to drop and postal revenues will remain stagnant over the next ten years, we can still maintain a viable and healthy Postal Service. With increased operational flexibility and reasonable adjustments to our legal and regulatory framework, the Postal Service can continue to provide quality mail services for years to come. On the other hand, this comprehensive analysis revealed that "doing nothing" or "doing little" are not options. Failure to act will only worsen our financial crisis. Applying short-term fixes will intensify the budgetary difficulties the Postal Service will face in succeeding years. Our proposals for changes must be considered in their entirety, as it will take many years for us to reap the cost reduction and revenue generation benefits of these actions.

I am confident that the Congress, the PRC, the Government Accountability Office (GAO), the mailing community, and consumers are committed to the long-term sustainability of the Postal Service. Together, we can make the difficult, yet necessary, decisions to maintain an effective, universal mail network.

Mr. Chairman, we have compiled the results of these studies and our recommendations for change in a document entitled "*Ensuring a Viable Postal Service for America: An Action Plan for the Future.*" I ask that our action plan be included in the hearing record.

To help develop this plan we engaged three of the world's most experienced and respected management consulting firms: McKinsey & Company, The Boston Consulting Group, and Accenture, LLC. We asked each of these firms to act independently and to conduct studies and have conversations with postal customers, mailers, labor associations, regulators, and mailing industry stakeholders. We wanted them to gather information to help us determine the likely state of the mailing industry and the Postal Service over the next decade. Our expectation was for the consultants to produce ideas that would allow the Postal Service to close the growing gap between revenues and expenses without undue impact on stakeholders.

The consultant's key findings included:

- Without fundamental changes, the Postal Service's losses will continue. By 2020, cumulative losses could exceed $238 billion.
- Mail volume will decline by roughly 15 percent to about 150 billion pieces in 2020, from 177 billion pieces in FY 2009.
- The mix of mail will change; First-Class Mail will fall sharply and Standard Mail will stay fairly flat. First-Class Mail contributes more toward covering institutional costs, which support retail, processing, and delivery networks.
- The Postal Service could close the gap by as much as $123 billion, without statutory or regulatory changes, by taking product and service actions, continuing to improve processes and productivity, adopting workforce flexibility improvements, and pursuing purchasing savings. Achieving this will be extremely challenging.
- There are no multi-billion dollar, revenue initiatives that the Postal Service could pursue, inside or outside of our core competencies. Nor do the business models of foreign posts offer any short-term, practical applications for generating revenue here in the U.S.
- Key areas within our core functions have been identified and options provided to close the remaining $115 billion gap. However, legislative and regulatory changes are needed to achieve them.
- The best way to address the financial challenges and preserve the strength of the Postal Service and the entire mailing industry is through a comprehensive approach that balances the needs of all key stakeholders.

The Postal Service created its action plan based on a thorough review and consideration of the consultants' recommendations. Management and the Board of Governors can take actions that will close $123 billion of the $238 billion projected gap. We intend to do everything in our authority to achieve those savings, but they are not without risk. Our plan also provides proposals to address the remaining $115 billion gap and is a balanced and reasonable approach to creating a financially sound future. To implement the plan, a number of fundamental changes are necessary, some of which would require legislative changes. The necessary solutions are:

- Restructure the Prefunding of Retiree Health Benefits – If no adjustments are made to the CSRS fund, we request that Congress permit these payments to be deferred and shifted to a "pay-as-you-go" system comparable to what is used by the rest of the federal government and the private sector. This would provide the Postal Service with an average of $5.6 billion in cash flow per year through 2016. As noted previously, correcting the Postal Service's overpayment to the CSRS pension fund and transferring that amount to the Retiree Health Benefits Fund would eliminate any need for these payments.
- Delivery Frequency – We request the ability to adjust permanently the number of mail delivery days to better reflect current mail volumes and match customer usage.
- Expand Access – We will continue to modernize our channels for alternate access by providing services where our customers are already transacting business. We also will continue to increase and enhance customer access through private sector retail partnerships, kiosks, and improved online offerings. However, the Postal Service needs to be relieved of the statutory prohibition against closing a Post Office for solely economic reasons.
- Workforce – We will work during our upcoming collective bargaining negotiations to establish a more flexible workforce that is better positioned to respond to the changing needs of customers and take advantage of the over 300,000 voluntary separations projected to occur over the next decade, as employees become eligible to retire. We would also ask that Congress pass legislation that requires an arbitrator to take the financial health of the Postal Service into consideration.
- Pricing – We request that Congress apply the Consumer Price Index price cap to the entire basket of Market Dominant products, rather than the current restriction which caps prices for every class at the rate of inflation. This will allow pricing to respond to the demand for each individual product and its costs. In addition, we will use existing flexibility to pursue an exigent price increase. Assuming other parts of our plan can be implemented, the exigent price increase will be moderate and not occur before 2011.
- Expand Products and Services – We ask that Congress permit us to evaluate and introduce more new products and services consistent with our mission. This will allow us to better respond to changing customer needs.
- Oversight – We ask that Congress provide a more streamlined and efficient process that provides appropriate oversight while promoting effective business practices. This will help to achieve the solutions in our action plan.

Some of these solutions could be implemented relatively quickly, while others would require much more time to achieve. Adjusting retiree health benefit payments and implementing five-day delivery will generate the largest and most immediate financial benefits for the Postal Service. Nonetheless, each part of the plan is critical to restoring the Postal Service's financial health. No one solution is the answer to reversing our financial condition. We believe a balanced approach that provides the Postal Service with the flexibility to respond to market dynamics and the speed to bring products to the market quickly, and that incorporates initiatives focused on cost, service, price, new products, and changes in the law would be the best approach. It is also the one that is most likely to perpetuate a financially sound Postal Service, able to meet the needs of the American people. We are ready to proceed with the plan. But we need Congress to provide the legislative reform necessary to move forward.

I would like to provide greater detail regarding our legislative proposals. The *Postal Act of 2006* included ambitious requirements for the Postal Service to prefund its legacy costs. While this appeared to be good public policy at the time, these measures did not anticipate, and were inconsistent with, the economic realities the country would soon face. I refer specifically to the provision that requires the Postal Service to prefund 73 percent of all future retiree health benefits—a 75-year liability—in just a ten-year period ending in 2016. This prefunding mandate is not shared by other federal agencies or private sector companies. The aggressive schedule, a product of budget scoring rules, requires annual prefunding payments averaging $5.6 billion. Moreover, the Postal Service's prefunding account had a balance of more than $35 billion at the end of FY 2009.

Between 2006 and 2009, mail volume fell by 17 percent and revenue fell by 6 percent. Consequently, we do not have the ability to meet this unique statutory requirement to prefund retiree health benefits at the accelerated pace. This enormous obligation costs Postal Service customers—not taxpayers—approximately $50 billion in prefunding over the ten-year period. Eliminating this requirement is one of the major components of our action plan.

The Postal Service greatly appreciates the action taken by Congress last year to enact legislation that restructured the payment for 2009. However, for 2010 and beyond, there is no assurance that similar adjustments will be granted. A restructuring of the payment obligation is urgently needed to allow the Postal Service to continue to fulfill its mission now and in the future. Legislative change would also reduce the need for the Postal Service to borrow funds from the U.S. Treasury for the sole purpose of depositing the money back into a fund at the U.S. Treasury. The Postal Service needs a quick decision by Congress on how this issue will be addressed to provide clarity regarding the amount and timing of other actions that are necessary to close the gap. Our preference is a comprehensive solution, but we need similar relief this year to ensure liquidity in Fiscal Year 2011.

Regarding our request to change the frequency of the number of mail delivery days each week, the statutory requirement for six-day mail delivery has been in existence since 1983. It imposes a very large financial burden, and is inconsistent with the overall mandate of the law requiring the Postal Service to operate like a business. Due to the unprecedented decline in mail volume, there no longer is sufficient volume to sustain the cost of the current six-day delivery network. The number of pieces of mail per delivery has declined from an average of five pieces in 2000 to four pieces in 2009, a 20 percent reduction. Without any changes in the business model, we can expect an average of three pieces per delivery by 2020. However, assuming a scenario of five-day delivery and FY 2009 mail volume, the amount of mail per delivery would increase to more than five pieces. Revenue per delivery point dropped by more than 20 percent between 2000 and 2009, because our largest volume declines occurred in profitable First-Class Mail.

Moving to five-day delivery is necessary to ensure financial viability, both now and into the future. Reducing the frequency of delivery is the single most effective way for the Postal Service to substantially reduce operational costs—allowing us to reduce annual net costs by more than $3 billion. It would greatly assist us with regaining a portion of our financial footing and help to ensure that affordable universal service is maintained nationwide. It is a prudent step a business would take given the financial projections for the future.

Market surveys conducted independently and on behalf of the Postal Service show that customers want to see the Postal Service survive and flourish. Most are willing to accept the elimination of Saturday delivery to reduce the Postal Service's losses. And, most would rather have Saturday delivery eliminated than have stamp prices increased significantly, as would be needed to ensure the Postal Service's financial stability. I would also like to cite the results of a Gallup survey conducted in March 2010. The survey showed that 68 percent of those polled favored a change to five-day delivery "as a way to help the Postal Service solve its financial problems" over other alternatives such as increasing postage prices or closing local Post Offices. This result was echoed by recent *USA Today* and *Washington Post* polls reporting that the majority of those surveyed support five-day delivery as a means of addressing our financial problems. In the *USA Today* survey, 87 percent of Americans rated the Postal Service's performance as "excellent" or "good."

In anticipation of a possible change, we have conducted extensive stakeholder outreach through dozens of meetings with customers. We identified mailer issues and ensured their consideration in developing the proposed five-day plan. These exchanges helped us to understand and address the needs of the mailing industry and the public concerning a potential change in the frequency of mail delivery. The Postal Service has developed a comprehensive operations plan for five-day delivery that addresses most, if not all, possible impacts from required software programming modifications to workforce adjustments. Two major assumptions guided the development of the concept: existing service standards would be maintained and any changes would comply with existing collective bargaining agreements.

Our plan for five-day delivery, which was filed with the PRC last month, includes:

- Residential and business delivery and collections would be discontinued on Saturday.
- Post Offices will be open on Saturdays.
- Post Office Boxes would receive mail delivery on Saturday.
- Express Mail would continue to be delivered seven days a week, including Saturday and Sunday.
- Remittance mail (bill payments) addressed to Post Office Box and Caller Service customers would still be made available to recipients seven days per week.
- Firm hold outs (mail that a business picks up at the Post Office) would continue to be available for Post Office Box addressed mail Monday through Saturday, nationwide.
- No mail pick-up from collection boxes on Saturdays except for dedicated Express Mail collection boxes.
- Acceptance and drop-shipping of destinating bulk mail would continue on Saturday and Sunday.
- Alternate contract locations would remain open on their normal schedules.
- Access to online services via *usps.com* would continue to be available 24/7.

Any change in the number of delivery days will require Congress to eliminate the appropriations language that mandates six-day-a-week delivery. Should Congress approve such a change, we are committed to implementing an in-depth communications plan for our customers and employees to make the transition as smooth as possible. In fact, we have established a dedicated website that describes in detail our plan for implementation. Upon approval, we intend to provide customers with six months notice prior to implementing a change which we estimate would be no earlier than mid-2011. If five-day delivery is enacted, we expect to handle adjustments to our career workforce through attrition, not layoffs, consistent with existing collective bargaining agreements. However, five-day delivery will substantially reduce the need for part-time, noncareer employees, most of whom work one day per week for the Postal Service.

Legislative action is also needed to provide the flexibility to realign our retail network in order to improve service while lowering costs. The Postal Service's primary goal in adjusting its retail network is to find the right balance between cost, efficiency, and providing universal service. In order to do this, we need the flexibility to close Post Offices. This will require the elimination of the statutory prohibition against closing Post Offices solely for economic reasons. The law concerning how we manage Post Offices needs to be modernized to allow our customers to be served where they shop. With more options for consumers, including *www.usps.com*, self-service kiosks, big-box outlets, banks, and the ability to buy stamps in grocery stores and at ATM machines, any law governing Postal Service business practices needs to reflect what consumers want—convenient access to services. Expanding access is part of the action plan. Saving costs on "brick and mortar" expenses will help us remain viable. Continuing to partner with the private-sector to expand nationwide access will help in meeting customer demand for increased access and greater convenience.

Customer research indicates that the American public is not concerned about Post Offices closing if postal services were moved to other retail locations. Many actually preferred to have postal services provided in nearby retail locations. In considering whether to consolidate or close a Post Office, the Postal Service operations plan would take into account convenient alternative places where customers can access postal services. As this realignment takes place, it would be a long-term process of adjusting the number of brick-and-mortar Post Offices while expanding access points for postal services.

The Postal Service must become a leaner organization. The large number of expected employee retirements creates an important opportunity to achieve this through what can be an orderly process of attrition, and by establishing more flexible work rules through the collective bargaining process. Through 2020, approximately 300,000 current employees will be eligible to retire. It would not make sense to replace them with full-time employees if demand is moving in a direction better suited to a part-time workforce.

The Postal Service is fully committed to negotiating collective bargaining agreements that are fair to our employees and our customers. National economic conditions, the current and future viability of the Postal Service, and the need to bargain in good faith for wages and benefits must all be a part of contract negotiations. Under existing law, arbitration is always a possibility. The financial health of the Postal Service and the affordability of postal products should be key considerations in any arbitration ruling. While some arbitrators have considered the fiscal health of the Postal Service, they are not required to take it into account. Our legislative proposal calls for a change to our collective bargaining process that was initially proposed in legislation introduced in the Senate last year. We ask that legislation be adopted to require arbitrators to take into account the Postal Service's financial condition before making any decision.

In order to react to market forces and offset potential declines in revenue and volume, we are also seeking legislative adjustments to the pricing mechanism found in the *Postal Act of 2006*. That law divided postal products into two broad categories: Market Dominant and Competitive, with different rules for each. Market Dominant, or mailing services, refers primarily to First-Class Mail, Periodicals, and Standard Mail. Rate increases for mailing services products are tied to a price cap applied to each mail class based on the Consumer Price Index – All Urban Consumers.

Competitive, or shipping services, refers to products such as Priority Mail and Express Mail that compete with private carriers. Shipping services products do not have a price cap, but have a price floor. Market Dominant products account for about 90 percent of revenue. The Postal Service wants to ensure that prices of Market Dominant products can be based on the demand for each individual product and its costs, rather than capping prices for each class at the rate of inflation. We ask that the inflation price cap be applied to Market Dominant products as a whole, rather than to each class of mail under this category. In asking that the price cap be applied by category, rather than individual products, the Postal Service is seeking the flexibility to price according to market conditions and to maximize revenue. This action would help us ensure that products cover their costs.

As technology and customer needs change, so will the definition of mail. The Postal Service seeks additional flexibility to innovate its products and better meet changing customer demands, while tapping into new sources of revenue. Currently, every potential new product, including individual customer contracts, requires before-the-fact review by both the Postal Service Governors and the PRC. This can delay the implementation of customer contracts, leading to mailer frustration and providing an advantage for competitors. In some other instances, such as the addition, deletion, or transfer of a product from the market dominant to the competitive product lists, there are no time limits on the review. The current regulatory framework should be changed to broaden the definition of postal products, enable streamlined, after-the-fact product and pricing reviews, and place time limits on all areas of review.

We are also seeking adjustments in the oversight of the Postal Service. Our current oversight model includes Presidentially-appointed Governors (USPS) and Commissioners (PRC), Congress, portions of the Executive Branch, GAO, the Postal Service Inspector General, and other federal agencies. In many situations, roles and responsibilities overlap and are not sufficiently clear. Changes in law are necessary to make oversight processes more responsive to market needs. They should include looking at issues such as time limits on reviews, and moving from before-the-fact to after-the-fact reviews. Collectively, these changes would ensure continued protection of customer interests while providing flexibility to manage in the changing postal environment.

I would like to comment on the recently released report by the GAO regarding the Postal Service business model. I appreciate all their efforts and contributions to this critical issue. Their report was mandated by the *Postal Act of 2006* for completion in 2011. However, GAO was asked by this Committee to accelerate its completion given the national, economic conditions of the past two years and our tenuous financial circumstances. For these same reasons, GAO added the Postal Service to the High Risk list in 2009.

Many of GAO's findings are consistent with the analysis and action plan we have submitted for your consideration. GAO's findings include:

- The Postal Service's financial condition is dire, and its outlook is poor. Immediate Congressional action is needed for the Postal Service to attain financial viability. If no action is taken, risks of larger Postal Service losses, rate increases, and taxpayer subsidies will increase.
- The Postal Service must apply the management flexibility called for in the *Postal Act of 2006*, by continuing to restructure its operations, networks, and workforce.
- Congress should consider revising Postal Service retiree health benefits funding and requiring any binding arbitration to take the Postal Service's financial condition into account.
- The Postal Service should pursue the development of new enhanced products to increase revenue.

The GAO report describes a number of strategies and options available to Congress and the Postal Service for long-term structural and operational reform. The Postal Service can improve its financial viability by working with Congress and taking aggressive actions to reduce costs. However, as GAO notes, the Postal Service is unlikely to succeed without Congressional action to remove the legal and regulatory constraints that impede our ability to increase revenue and decrease costs. I look forward to working with Congress, the GAO, PRC, and the entire postal community in implementing the best choices for our continued success.

We do have a concern about one of the options listed in the GAO report. They note that Congress may want to establish a commission of independent experts to assist in making changes to the Postal Service's network, business model, and operations. We believe that such a commission would only add a layer of bureaucracy and delay to problems that require immediate attention. Our challenges are urgent and well documented. Congress should be seeking the most expeditious and effective resolutions to the Postal Service's financial difficulties. Commissions and additional studies will not contribute to that process.

GAO also suggests that the Postal Service be required to provide Congress with regular reports to ensure that our financial condition is improving. We agree, and plan to ensure transparency and accountability through a number of regular reports we currently are required to file. One of the central components of the *Postal Act of 2006* was to provide greater transparency in Postal Service operations. That objective has been met, and existing procedures for documenting our financial and operational condition are sufficient.

Our findings, recommendations, and legislative proposal come as no surprise to postal stakeholders. In our effort to develop a long-term action plan for success, we have made a concerted effort to consider proposals and feedback offered by the entire postal community. Our plan of action has been shared with Congress, the PRC, GAO, mailers, employee groups, and consumers. While no one is to blame for our current financial condition, we must all work together to overcome it. Efforts to fine tune this organization can only occur in a transparent environment with full participation by all stakeholders. We are committed to continuing this process of an open dialogue to ensure the future success of the Postal Service.

Mr. Chairman, our founding fathers recognized the need for a basic and fundamental service to "bind our Nation together." For over 230 years, the Post Office has served that indispensible purpose helping our country grow and prosper. In 1970, Congress passed legislation creating an independent establishment to be operated in a business-like manner. This hallmark legislation was based on the necessity that a national, government–sponsored, postal network required sound business practices and the freedom from political manipulation. Given the communications and technological advancements between 1970 and 2006, it is not surprising that further changes to our legislative mandate were needed to keep up with the times. More fine-tuning is needed to preserve self-sustaining, universal mail services for all Americans.

The Postal Service must be leaner and have the ability to quickly respond to customer needs. Our action plan is a path to a future in which the Postal Service will remain a vital driver of the American economy and an integral part of every American community. We will continue to deliver the greatest value of any comparable post in the world. If given the flexibility to respond to an evolving marketplace, the Postal Service will be an integral part of the fabric of American life for a long time to come.

Thank you for your support of our ongoing efforts to ensure a sound Postal Service. I look forward to working with you and other members of Congress to achieve the passage of legislation that will address our near-term and future challenges. I will be happy to answer any questions that you may have.

###

Mr. LYNCH. Thank you, Mr. Potter.

Mr. Herr, you are now recognized for 5 minutes.

STATEMENT OF PHILLIP HERR

Mr. HERR. Thank you. Chairman Lynch, Ranking Members Issa and Chaffetz, and members of the committee, I am pleased to participate in this hearing and discuss GAO's report that was released this week. Today I will focus my remarks on the Postal Service's financial condition and forecast and strategies and options to facilitate progress toward its financial viability.

Turning first to the Postal Service's financial condition, as mail volume declined by 36 billion pieces in fiscal years 2007 through 2009, the Postal Service's financial viability has deteriorated, leading to $12 billion in losses. Current forecasts for the mail volume will decline to 167 billion pieces this fiscal year, the lowest level since 1992.

The Postal Service projects a record loss of over $7 billion this fiscal year, while adding $3 billion in debt. Its outstanding debt will increase to $13.2 billion, close to its $15 billion statutory limit.

The Postal Service does not expect mail volume to return to its former levels when the economy recovers. The continuing shift to electronic communications and payments has fundamentally changed how mail is used. By fiscal year 2020 the Postal Service projects further volume declines to 150 billion pieces, the lowest level since 1986. First class mail volume is projected to decline by another 37 percent over the next decade, and less profitable standard mail, primarily advertising that is subject to economic fluctuations, is projected to remain roughly flat over the next decade.

Turning to actions needed to facilitate the Postal Service's financial viability, in July 2009 GAO added the Postal Service's financial condition to our high-risk list and reported that action is needed in multiple areas for the Postal Service to make progress toward financial viability. We identified strategies and options that fall into three major categories.

First, compensation and benefits currently represent 80 percent of Postal Service cost, presenting cost savings opportunities. In terms of retirements, about 162,000 postal employees are eligible to retire this fiscal year, and about 300,000 are expected to retire over the next decade. In terms of benefit costs, postal employees have about 80 percent of their health benefit premiums paid, 8 percent more than most Federal employees.

Second, cost savings can be achieved by consolidating processing and retail networks, given mail volume declines. Removing excess capacity is necessary in the 600 processing facilities where first-class mail processing capacity exceeds needs by 50 percent. The network of 36,500 retail facilities can also be reduced. Maintenance has been under-funded for years, resulting in deteriorating facilities and a maintenance backlog. Approximately 30 percent of postal revenue currently comes from stamps purchased at non-postal locations such as grocery stores, indicating the customer has begun shifting to alternatives.

Another opportunity is consolidating the field administrative structure by reviewing the need for 74 district offices and an additional 8 area offices. And, because cost-cutting alone will not ensure a viable Postal Service, generating revenue through pricing and product flexibility is needed. The new flat rate priority mail boxes are an example of how the Postal Service has successfully generated new revenues.

Turning to our report's matters for congressional consideration, to facilitate progress in difficult areas such as realigning postal operations and its work force, Congress may wish to consider an approach similar to a BRAC-like commission used by the Department of Defense. Congress has previously turned to panels of independent experts to restructure organizations and establish consensus. We believe the commission could also help to ensure that Congress and stakeholders have confidence in resulting actions.

We also suggested Congress consider change in two other areas. One would be to revise the statutory framework for collected bargaining to ensure that binding arbitration takes the Postal Service's financial condition into account. Another change to consider is modifying the Postal Service's retiree health benefit cost structure. We believe it is important that the Postal Service fund its retiree health benefit obligations to the maximum extent its finances permit.

Currently, about 460,000 retirees and their survivors receive this benefit and another 300,000 postal employees are expected to use it by 2020. In considering revisions, it will be important to assess what the Postal Service can afford, strike a fair balance of payments between current and future rate payers, and determine how changes would affect the Federal budget.

Mr. Chairman, in conclusion, no single change will be sufficient to address the Postal Service's pressing challenges. The longer it takes to realign the Postal Service to the changing use of the mail, the more difficult change will be.

This concludes my prepared statement, and I am pleased to answer any questions that you or members of the committee have.

Thank you.

[The prepared statement of Mr. Herr follows:]

United States Government Accountability Office

GAO

Testimony

Before the Committee on Oversight and Government Reform and Its Subcommittee on Federal Workforce, Postal Service, and the District of Columbia, House of Representatives

For Release on Delivery
Expected at 10:00 a.m. EDT
Thursday, April 15, 2010

U.S. POSTAL SERVICE

Action Needed to Facilitate Financial Viability

Statement of Phillip Herr, Director
Physical Infrastructure Issues

GAO
Accountability * Integrity * Reliability

GAO-10-624T

April 15, 2010

GAO
Accountability·Integrity·Reliability

Highlights

Highlights of GAO-10-624T, a testimony to the Committee on Oversight and Government Reform and Its Subcommittee on Federal Workforce, Postal Service, and the District of Columbia, House of Representatives

Why GAO Did This Study

The U.S. Postal Service's (USPS) financial condition and outlook deteriorated significantly during fiscal years 2007 through 2009. USPS was not able to cut costs fast enough to offset declines in mail volumes and revenues resulting from the economic recession and changes in the use of mail, such as electronic bill payment. In July 2009, GAO added USPS's financial condition to its high-risk list and reported that USPS urgently needed to restructure to improve its financial viability.

The Postal Accountability and Enhancement Act (PAEA) of 2006 required GAO to evaluate strategies and options for USPS's long-term structural and operational reform and report by December 2011. Because of USPS's financial crisis and the need for urgent action, GAO accelerated its work and issued a report (GAO-10-455) on April 12, 2010.

This testimony provides (1) information on USPS's financial condition and outlook and (2) GAO's perspective on the actions that are needed to facilitate progress toward USPS's financial viability. This testimony is based on GAO's recently issued report and recent testimonies on USPS's financial condition and outlook.

View GAO-10-624T or key components. For more information, contact Phillip Herr at (202) 512-2834 or herrp@gao.gov.

U.S. POSTAL SERVICE

Actions Needed to Facilitate Financial Viability

What GAO Found

USPS is facing a major financial crisis. Mail volume, the primary source of USPS revenues, declined by 36 billion pieces (about 17 percent) over the last three fiscal years (2007 through 2009). Mail volume declines were largely due to the economic downturn and changing use of the mail linked to the continuing shift to electronic communications and payments. USPS's financial outlook is poor as it projects future declines in mail volumes, stagnating revenues, large financial losses, increasing debt, and significant financial obligations, including for retiree health benefits. USPS projects a record loss of over $7 billion in fiscal year 2010. Furthermore, USPS expects to borrow $3 billion, bringing its total outstanding debt to $13.2 billion, close to its $15 billion statutory borrowing limit with the U.S. Treasury. Looking forward, USPS projects that by fiscal year 2020, total mail volume will further decline by 15 percent, to the lowest level since 1986. Absent additional actions to cut costs and increase revenues, USPS expects financial losses will escalate over the next decade.

GAO recently reported that making progress toward USPS's financial viability would primarily involve taking action to rightsize operations, cut costs, and increase revenues. Making the necessary progress would require USPS and Congress to pursue strategies and options that would

- reduce compensation, benefits, and other operations and network costs using the collective bargaining process to address wages, benefits, and workforce flexibility, as well as generating revenues through pricing and product flexibility; and
- address legal restrictions and resistance to realigning USPS operations, networks, and workforce.

USPS included many of these strategies and options in the action plan it issued in March 2010, but these planned actions under its existing authority will not be enough to make it financially viable. Therefore, action by Congress and USPS is urgently needed to

- reach agreement on actions to achieve USPS's financial viability;
- provide financial relief through deferral of costs by revising USPS retiree health benefit funding while continuing to fund these benefits over time to the extent that USPS's finances permit; and
- require that any binding arbitration resulting from collective bargaining would take USPS's financial condition into account.

To facilitate reaching agreement about the difficult constraints and legal restrictions that hamper progress, Congress could consider establishing a panel of independent experts, similar to the approach used by the Department of Defense's Base Realignment and Closure Commission (BRAC), to coordinate with USPS and stakeholders to recommend a package of proposed legislative and operational changes needed to reduce costs and address challenges to USPS's business model.

Chairman Towns, Chairman Lynch, and Members of the Committee and Subcommittee:

I am pleased to participate in this hearing on the U.S. Postal Service's (USPS) financial condition, a topic we have addressed in recent reports and testimonies. My statement will provide (1) information on USPS's financial condition and outlook and (2) our perspective on the actions that are needed to facilitate progress toward its financial viability.

My statement is primarily based upon our report released this week on USPS's business model.[1] The report responded to a provision in the Postal Accountability and Enhancement Act of 2006 (PAEA) that required GAO to evaluate strategies and options for the long-term structural and operational reform of USPS.[2] We also drew on our recent testimonies on USPS's financial condition and outlook and our July 2009 report in which we added USPS's financial condition to our high-risk list.[3] For our recent report, we primarily drew on this past work; other studies; USPS data; interviews with USPS, unions, management associations, Postal Regulatory Commission (PRC), and mailing industry officials; and stakeholder input. We conducted our work in accordance with generally accepted government auditing standards. Additional information on scope and methodology is available in each full product. Related GAO reports and testimonies are listed in the attachment to this statement.

USPS's Financial Condition Has Deteriorated and Its Financial Outlook Is Poor

USPS is facing a major financial crisis. Mail volumes, the primary source of USPS revenues, declined by 36 billion pieces (about 17 percent) over the last 3 fiscal years (2007 through 2009). In particular, First-Class Mail and Standard Mail—which together accounted for 94 percent of volume and about 78 percent of revenue in fiscal year 2009—experienced major declines. These declines were largely due to the economic downturn and the continuing shift to electronic communications and payments.

[1] GAO, *U.S. Postal Service: Strategies and Options to Facilitate Progress toward Financial Viability*, GAO-10-455 (Washington, D.C.: Apr. 12, 2010).

[2] Pub. L. No 109-435, §710, 120 Stat. 3198 (Dec. 20, 2006).

[3] GAO, *High-Risk Series: Restructuring the U.S. Postal Service to Achieve Sustainable Financial Viability*, GAO-09-937SP (Washington, D.C.: July 28, 2009). USPS's transformation efforts and long-term outlook were on our high-risk list from 2001 to 2007.

Both USPS and Congress took actions in fiscal years 2007 through 2009 to help offset these declines by reducing billions in USPS costs. For example,

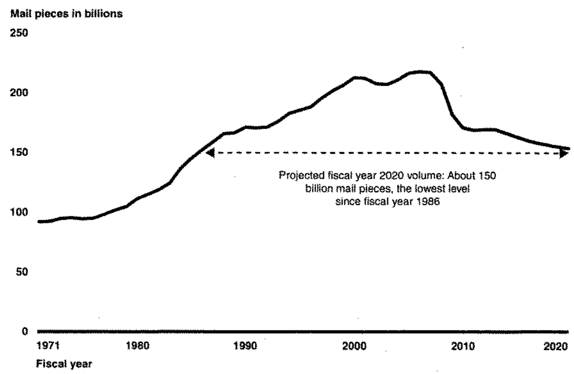
- USPS achieved nearly $10 billion in cost savings during this time, primarily by cutting nearly 201 million work hours. Work-hour savings were achieved by workforce reductions of over 84,000 full- and part-time employees, primarily through retirements; reduced overtime; and changes to postal operations.
- Congressional action late in fiscal year 2009 deferred $4 billion in payments USPS was mandated to make to prefund postal retiree health benefits.[4]

These actions, along with others to generate additional revenues, however, were insufficient to fully offset the impact of mail volume declines and rising personnel-related costs. As a result, over this 3-year period, USPS borrowed the maximum $3 billion each year from the U.S. Treasury and still incurred record net losses, cumulatively losing nearly $12 billion.

USPS's financial problems are likely to continue unless fundamental changes are made to address challenges in its current business model by better aligning costs with revenues. USPS projects future declines in mail volumes, stagnating revenues, large financial losses, increasing debt, and significant financial obligations. For example, total mail volume for the first quarter of fiscal year 2010 was down almost 4.4 billion pieces, a decrease of almost 9 percent over last year. For fiscal years 2010 and 2011, USPS is already projecting annual deficits exceeding $7 billion, creating additional pressures to generate sufficient cash to meet its obligations. USPS expects to borrow $3 billion in fiscal year 2010, which would bring its total outstanding debt to $13.2 billion, close to its $15 billion statutory limit, which it could reach as early as fiscal year 2011. Moreover, USPS projections through fiscal year 2020 indicate that total mail volume is not expected to return to its former levels (see fig. 1).

[4]Pub. L. No. 111-68, § 164, 123 Stat. 2023 (Oct. 1, 2009).

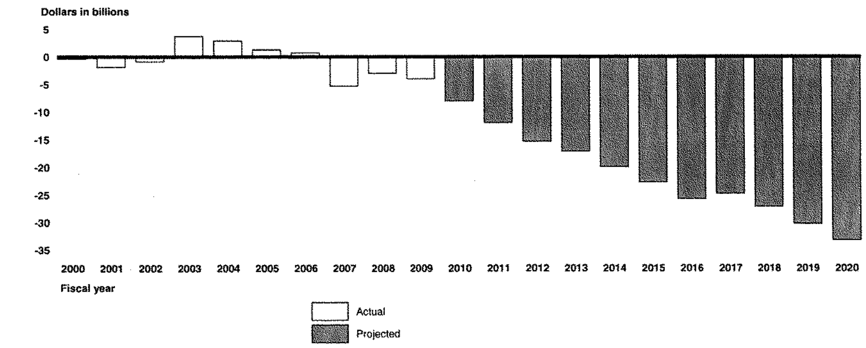
Figure 1: Actual and Projected Total Mail Volume, Fiscal Years 1971 through 2020



Source: USPS.

USPS projects that financial losses will escalate over the next decade, with cumulative losses of over $238 billion by fiscal year 2020 if its planned cost reduction and revenue generation initiatives are not implemented (see fig. 2.).

Figure 2: USPS Actual and Projected Net Income (Loss), Fiscal Years 2000 through 2020



Source: USPS.

Note: The projection for fiscal year 2010 is from USPS's Fiscal Year 2010 Integrated Financial Plan. USPS projections for fiscal years 2011 through 2020 are from its Action Plan and assume that (1) USPS takes no management actions beyond those in its fiscal year 2009 budget and (2) USPS's total statutory borrowing limit of $15 billion would be increased to accommodate these losses. USPS's $8.4 billion in cumulative net income for fiscal years 2003 through 2005 largely resulted from a 2003 law (Pub. L. No. 108-18) that reduced USPS pension benefit payments by about $9 billion over this period.

These financial challenges highlight deficiencies in USPS's business model, which is predicated on fulfilling its mission through self-supporting, businesslike operations. The financial and operational challenges facing USPS have been exacerbated by the recent economic downturn. Because of these challenges, in July 2009, we placed USPS's financial condition on our high-risk list and testified that restructuring is needed to enhance USPS's current and long-term financial viability.[5] We concluded in our most recent report that its business model is not viable because it is unable to reduce costs sufficiently in response to continuing mail volume and revenue declines. We continue to believe that major restructuring is necessary and not doing so will increase the risk that taxpayers and the U.S. Treasury will have to provide financial relief.

[5]GAO-09-937SP and GAO, *U.S. Postal Service: Broad Restructuring Needed to Address Deteriorating Finances*, GAO-09-790T (Washington, D.C.: July 30, 2009).

Actions Congress and USPS Can Take to Facilitate Progress toward Financial Viability

Action by Congress and USPS is urgently needed in a variety of areas to facilitate progress toward USPS's financial viability. We have identified a variety of strategies and options that can be taken to address these challenges. Some of these strategies can be completed within USPS's current authority, while others would need congressional involvement or require collaboration with unions through collective bargaining. The strategies fall into three major categories:

- reducing compensation and benefits costs,
- reducing other operations and network costs and improving efficiency, and
- generating revenues through product and pricing flexibility.

Other options that Congress may want to consider would more comprehensively restructure USPS's statutory and regulatory framework to reflect business and consumers' changing use of the mail. Although our report did not focus on whether USPS's ownership structure should be changed, we identified the following questions that could be helpful when considering this framework:

- *Mission:* What universal postal service, including mail delivery and postal retail service, is appropriate in light of fundamental changes in the use of mail?
- *Role:* Should USPS be solely responsible for providing universal delivery and postal retail service, or should that responsibility be shared with the private sector?
- *Monopoly:* Does USPS need a monopoly over delivery of certain types of letter mail and access to mail boxes to finance—in part or wholly—universal postal service?
- *Governance and regulation:* What is an appropriate balance between USPS's managerial flexibility and the oversight and accountability provided by the current governance and regulatory structure?

To facilitate progress going forward, it will be critical for USPS and Congress to reach agreement with other stakeholders on major issues that impede USPS's ability to implement actions to reduce financial losses, such as the following:

- *Funding postal retiree health benefits:* USPS has said that it cannot afford its required prefunding payments, and several proposals have been made to defer costs by revising the statutory requirements. It is important that USPS fund its retiree health benefit obligations—including prefunding these obligations—to the maximum extent that its finances permit. In revising the requirements, it will be important to consider what is affordable to USPS; what is a fair balance of payments between current and future ratepayers; and what impact such changes could have on the federal budget.[6]

- *Binding arbitration:* One of the most difficult challenges is making changes to USPS's compensation systems, which will be critical to its financial condition since wages and benefits represent 80 percent of its costs. USPS and its employee unions will begin negotiations for new agreements in 2010 and 2011. In this regard, the time has come to reexamine the structure for collective bargaining that was developed 40 years ago. Since that time, USPS's competitive environment has changed dramatically, and rising personnel costs are contributing to escalating financial losses. Thus, Congress should consider modifying the collective bargaining process to ensure that any binding arbitration takes USPS's financial condition into account.

- *Realigning postal services with changing use of the mail:* As mail use by businesses and consumers continues to change, USPS has stated that it cannot afford to provide the same level of services. For example, it has estimated that costs could be reduced by about $3 billion annually if delivery frequency is reduced from 6 days to 5 days per week, but congressional action would be needed to remove statutory requirements for 6-day mail delivery. USPS filed its proposal to eliminate Saturday delivery with the PRC on March 30, 2010. This action will allow public input on this issue and lead to a PRC advisory opinion.

- *Generating revenue through new or enhanced product and services:* A key issue is whether USPS can make sufficient progress using the pricing and product flexibility provided in PAEA or if changes are needed. In 2009, USPS asked Congress to change the law so that it could diversify into nonpostal areas to find new opportunities for revenue growth. USPS and stakeholders we collected information from offered many options for diversification into nonpostal areas, including banking, financial, insurance, and government services, either on its own or in partnership

[6]See GAO-10-455 for a discussion of different approaches for funding USPS's retiree health benefit obligations.

with other private firms or government agencies. USPS also asked for additional pricing flexibility in a recently issued Action Plan.[7] However, it is unclear what the potential impacts of such changes would be and what statutory or regulatory changes would be needed.

- *Realigning operations, networks, and workforce:* Once Congress and USPS have determined what, if any, changes should be made in the products and services that it provides, postal operations, networks, and workforce would need to be realigned. Decisions in this area will involve difficult tradeoffs related to reducing USPS's size so as to remain self-financing and keep prices affordable, versus concerns about how such realignments would affect its workforce, the value of USPS's brand, and its network of physical assets.

When we placed USPS on our high-risk list, we suggested that USPS develop and implement a broad restructuring plan that would identify specific actions planned, key issues to address, and steps Congress and other stakeholders needed to take. On March 2, 2010, USPS issued an *Action Plan* that identified seven key areas in which it would need legislative changes or congressional support. Many of the options discussed are similar to those we have analyzed and included in our recent report. USPS's plan indicates that actions within its control can close $123 billion of this financial gap, but that actions outside its existing authority—including some involving statutory changes—will be needed to eliminate the remaining financial gap. Progress on these issues will likely take several years to fully implement once a decision is made on the scope of needed changes.

Congress, USPS, and other stakeholders need to reach agreement on the actions that should be taken, the desired operational and financial results, and the time frames for implementation. Key questions that need to be addressed include the following:

[7]United States Postal Service, *Ensuring a Viable Postal Service for America: An Action Plan for the Future* (Washington, D.C.: March 2010). USPS's plan and related material are available at the following Web address: http://www.usps.com/strategicplanning/futurepostalservice.htm (accessed on Apr. 9, 2010).

- *Universal service:* What, if any, changes are needed—that is, should delivery services be changed (e.g., frequency or standards), and should retail services be moved out of post offices to alternative locations?

- *Realigning operations, networks, and workforce:* How should USPS optimize its operations, networks, and workforce to support changes in services? How quickly can this happen? How can USPS best work with its employees and customers to minimize potential disruption?

- *New products and services:* What opportunities are there to introduce profitable new postal products and enhancements to existing ones? Should USPS engage in nonpostal areas where there are private-sector providers? If so, under what terms?

In our recent report, we stated that to facilitate progress in difficult areas, such as realigning operations, networks, and workforce, Congress may want to consider an approach similar to that used by the Department of Defense's Base Realignment and Closure Commission (BRAC). USPS agreed with the report's key findings but raised concerns about using a BRAC-type panel and its timing. Congress has previously turned to panels of independent experts to assist in restructuring organizations that are facing key financial challenges. These panels have helped establish consensus and developed proposed legislative or other changes to address difficult public policy issues. Establishing a similar commission or control board of independent experts could provide a mechanism to assist Congress in making timely decisions and comprehensive changes to USPS's business model and operations.

In addition to establishing a panel, our report included two other matters for Congress to consider to address USPS's financial viability in the short term:

- Modify USPS's retiree health benefit cost structure in a fiscally responsible manner.

- Revise the statutory framework for collective bargaining to ensure that binding arbitration takes USPS's financial condition into account.

The current crisis presents an opportunity to act and position this important American institution for the future. The longer it takes for USPS and Congress to address USPS's challenges, the more difficult they will be to overcome.

Messrs. Chairmen, this concludes my prepared statement. I would be pleased to answer any questions that you or other Members of the Committee may have.

Contact and Staff Acknowledgments

For further information regarding this statement, please contact Phillip Herr at (202) 512-2834 or herrp@gao.gov. Individuals who made key contributions to this statement include: Teresa Anderson, Joshua Bartzen, Brandon Haller, Kenneth John, Anar Ladhani, Hannah Laufe, Daniel Paepke, Susan Ragland, Amy Rosewarne, Travis Thomson, and Crystal Wesco.

Individuals who made key contributions to GAO-10-455, the report on which this testimony is based, include: Shirley Abel, Amy Abramowitz, Teresa Anderson, Joseph Applebaum, Gerald Barnes, Joshua Bartzen, William Dougherty, Patrick Dudley, Brandon Haller, Carol Henn, Paul Hobart, Kenneth John, Anar Ladhani, Hannah Laufe, Scott McNulty, Daniel Paepke, Susan Ragland, Amy Rosewarne, Travis Thomson, Jack Wang, and Crystal Wesco.

Related GAO Products

U.S. Postal Service: Strategies and Options to Facilitate Progress toward Financial Viability. GAO-10-455. Washington, D.C.: April 12, 2009.

U.S. Postal Service: Financial Crisis Demands Aggressive Action. GAO-10-538T. Washington, D.C.: March 18, 2010.

U.S. Postal Service: The Program for Reassessing Work Provided to Injured Employees Is Under Way, but Actions Are Needed to Improve Program Management. GAO-10-78. Washington, D.C.: December 14, 2009.

U.S. Postal Service: Financial Challenges Continue, with Relatively Limited Results from Recent Revenue-Generation Efforts. GAO-10-191T. Washington, D.C.: November 5, 2009.

U.S. Postal Service: Restructuring Urgently Needed to Achieve Financial Viability. GAO-09-958T. Washington, D.C.: August 6, 2009.

U.S. Postal Service: Broad Restructuring Needed to Address Deteriorating Finances. GAO-09-790T. Washington, D.C.: July 30, 2009.

High Risk Series: Restructuring the U.S. Postal Service to Achieve Sustainable Financial Viability. GAO-09-937SP. Washington, D.C.: July 28, 2009.

U.S. Postal Service: Mail Delivery Efficiency Has Improved, but Additional Actions Needed to Achieve Further Gains. GAO-09-696. Washington, D.C.: July 15, 2009.

U.S. Postal Service: Network Rightsizing Needed to Help Keep USPS Financially Viable. GAO-09-674T. Washington, D.C.: May 20, 2009.

U.S. Postal Service: Escalating Financial Problems Require Major Cost Reductions to Limit Losses. GAO-09-475T. Washington, D.C.: March 25, 2009.

U.S. Postal Service: Deteriorating Postal Finances Require Aggressive Actions to Reduce Costs. GAO-09-332T. Washington, D.C.: January 28, 2009.

U.S. Postal Service: USPS Has Taken Steps to Strengthen Network Realignment Planning and Accountability and Improve Communication. GAO-08-1022T. Washington, D.C.: July 24, 2008.

U.S. Postal Service: Data Needed to Assess the Effectiveness of Outsourcing. GAO-08-787. Washington, D.C.: July 24, 2008.

U.S. Postal Service Facilities: Improvements in Data Would Strengthen Maintenance and Alignment of Access to Retail Service. GAO-08-41. Washington, D.C.: December 10, 2007.

U.S. Postal Service: Mail Processing Realignment Efforts Under Way Need Better Integration and Explanation. GAO-07-717. Washington, D.C.: June 21, 2007.

U.S. Postal Service: The Service's Strategy for Realigning Its Mail Processing Infrastructure Lacks Clarity, Criteria, and Accountability. GAO-05-261. Washington, D.C.: April 8, 2005.

GAO's Mission

The Government Accountability Office, the audit, evaluation, and investigative arm of Congress, exists to support Congress in meeting its constitutional responsibilities and to help improve the performance and accountability of the federal government for the American people. GAO examines the use of public funds; evaluates federal programs and policies; and provides analyses, recommendations, and other assistance to help Congress make informed oversight, policy, and funding decisions. GAO's commitment to good government is reflected in its core values of accountability, integrity, and reliability.

Obtaining Copies of GAO Reports and Testimony

The fastest and easiest way to obtain copies of GAO documents at no cost is through GAO's Web site (www.gao.gov). Each weekday afternoon, GAO posts on its Web site newly released reports, testimony, and correspondence. To have GAO e-mail you a list of newly posted products, go to www.gao.gov and select "E-mail Updates."

Order by Phone

The price of each GAO publication reflects GAO's actual cost of production and distribution and depends on the number of pages in the publication and whether the publication is printed in color or black and white. Pricing and ordering information is posted on GAO's Web site, http://www.gao.gov/ordering.htm.

Place orders by calling (202) 512-6000, toll free (866) 801-7077, or TDD (202) 512-2537.

Orders may be paid for using American Express, Discover Card, MasterCard, Visa, check, or money order. Call for additional information.

To Report Fraud, Waste, and Abuse in Federal Programs

Contact:

Web site: www.gao.gov/fraudnet/fraudnet.htm
E-mail: fraudnet@gao.gov
Automated answering system: (800) 424-5454 or (202) 512-7470

Congressional Relations

Ralph Dawn, Managing Director, dawnr@gao.gov, (202) 512-4400
U.S. Government Accountability Office, 441 G Street NW, Room 7125
Washington, DC 20548

Public Affairs

Chuck Young, Managing Director, youngc1@gao.gov, (202) 512-4800
U.S. Government Accountability Office, 441 G Street NW, Room 7149
Washington, DC 20548

Please Print on Recycled Paper

United States Government Accountability Office

GAO

Report to Congressional Committees

April 2010

U.S. POSTAL SERVICE

Strategies and Options to Facilitate Progress toward Financial Viability

GAO

Accountability * Integrity * Reliability

GAO-10-455

GAO Accountability * Integrity * Reliability

Highlights

Highlights of GAO-10-455, a report to congressional committees

April 2010

U.S. POSTAL SERVICE

Strategies and Options to Facilitate Progress toward Financial Viability

Why GAO Did This Study

The Postal Accountability and Enhancement Act of 2006 required GAO to evaluate strategies and options for reforms of the United States Postal Service (USPS). USPS's business model is to fulfill its mission through self-supporting, businesslike operations; however, USPS has experienced increasing difficulties. Due to volume declines, losses, a cash shortage, and rising debt, GAO added USPS's financial condition to its high-risk list in July 2009.

GAO's objectives were to assess (1) the viability of USPS's business model, (2) strategies and options to address challenges to its business model, and (3) actions Congress and USPS need to take to facilitate progress toward financial viability. GAO primarily drew on its past work; other studies; USPS data; interviews with USPS, unions, management associations, Postal Regulatory Commission, and mailing industry officials; and stakeholder input.

What GAO Recommends

Congress should consider providing financial relief, such as revising USPS retiree health benefit funding and requiring any binding arbitration to take USPS's financial condition into account. At the same time, Congress should consider setting up a panel of experts to develop proposals for broader legislative and operational reform. USPS agreed with the report's key findings but raised concerns about a panel and its timing. Such panels have successfully informed prior difficult restructuring decisions.

View GAO-10-455 or key components. For more information, contact Phillip Herr at (202) 512-2834 or herrp@gao.gov.

What GAO Found

USPS's business model is not viable due to USPS's inability to reduce costs sufficiently in response to continuing mail volume and revenue declines. Mail volume declined 36 billion pieces (17 percent) over the last 3 fiscal years (2007 through 2009) with the recession accelerating shifts to electronic communications and payments. USPS lost nearly $12 billion over this period, despite achieving billions in cost savings by reducing its career workforce by over 84,000 employees, reducing capital investments, and raising rates. However, USPS had difficulty in eliminating costly excess capacity, and its revenue initiatives have had limited results. USPS also is nearing its $15 billion borrowing limit with the U.S. Treasury and has unfunded pension and retiree health obligations and other liabilities of about $90 billion. In 2009, Congress reduced USPS's retiree health benefit payment by $4 billion to address a looming cash shortfall, but USPS still recorded a loss of $3.8 billion. Given its financial problems and outlook, USPS cannot support its current level of service and operations. USPS projects that volume will decline by about 27 billion pieces over the next decade, while revenues will stagnate; costs will rise; and, without major changes, cumulative losses could exceed $238 billion.

This report groups strategies and options that can be taken to address challenges in USPS's business model by better aligning costs with revenues (see table on next page). USPS may be able to improve its financial viability if it takes more aggressive action to reduce costs, particularly compensation and benefit costs that comprise 80 percent of its total costs, as well as increasing revenues within its current authority. However, it is unlikely that such changes would fully resolve USPS's financial problems, unless Congress also takes actions to address constraints and legal restrictions.

Action by Congress and USPS is urgently needed to (1) reach agreement on actions to achieve USPS's financial viability, (2) provide financial relief through deferral of costs by revising USPS retiree health benefit funding while continuing to fund these benefits over time to the extent that USPS's finances permit, and (3) require that any binding arbitration resulting from collective bargaining would take USPS's financial condition into account. Congress may also want assurance that any financial relief it provides is met with aggressive actions by USPS to reduce its costs and increase revenues, and that USPS is making progress toward addressing its financial problems. USPS's new business plan recognizes immediate actions are needed, but USPS has made limited progress on some options, such as closing facilities. If no action is taken, risks of larger USPS losses, rate increases, and taxpayer subsidies will increase. To facilitate progress in these difficult areas, Congress could set up a mechanism, such as one similar to the military Base Realignment and Closure Commission, where independent experts could recommend a package of actions with time frames. Key issues also need to be addressed related to what changes, if any, should be made to delivery or retail services; to allow USPS to provide new products or services in nonpostal areas; and to realign USPS operations, networks, and workforce.

Highlights of GAO-10-455 (continued)

The table below summarizes selected strategies and options for action by Congress and USPS to address USPS's financial viability, with some options requiring collaboration with unions through collective bargaining.

Challenges	Options for USPS	Options for Congress
Strategy: Reduce compensation and benefits costs		
Workforce size: • About 300,000 postal employees are expected to retire through 2020. • Collective bargaining agreements include limits on outsourcing. • Postal unions are concerned about the loss of jobs paying a middle-class wage and benefits to private-sector jobs with lower wages and no benefit guarantees.	Reduce the size of the workforce through retirements and outsourcing, where it is cost-effective to do so.	
Wages: USPS is required to maintain compensation and benefits comparable to the private sector, and wages account for about one-half of USPS's costs.	Reduce wage costs, for example, through a two-tiered pay system that would pay new hires lower wages and "grandfather" employees in the current system.	Require arbitrators to consider USPS's financial condition when making binding arbitration decisions.
Benefits: • USPS benefits account for over 23 percent of USPS's costs. USPS is required to make annual multibillion dollar retiree health benefit payments. • Employees eligible for workers' compensation benefits can continue these more generous benefits even when eligible to retire.	Reduce benefit costs by reducing USPS health and life insurance contribution rates for active employees to levels comparable to those paid by other federal agencies.	• Defer costs by revising funding requirements for retiree health benefits. • Revise workers' compensation laws for employees eligible for retirement.
Workforce mix and work rules: USPS has a high ratio of full-time career employees—about 78 percent—and wants flexibility to hire more part-time employees.	Adjust workforce mix, for example, by using more part-time staff.	
Strategy: Reduce other operations and network costs and improve efficiency		
• USPS has costly excess capacity and inadequate flexibility to quickly reduce costs in its retail, processing, and delivery networks. • Closing facilities has been limited by political, employee, union, and community opposition to potential job losses. • *Retail:* Legal restrictions limit its ability to close certain types of post offices. • *Delivery:* Delivery is the largest cost segment, labor-intensive, and required by statute to be provided 6 days a week.	*Mail processing:* • Close unneeded facilities. • Relax delivery standards to facilitate closures and consolidations. *Retail:* • Optimize USPS retail facility network (including hours and locations). • Move more retail services to private stores and self-service and close unneeded retail facilities. *Delivery:* Expand use of more cost-efficient delivery, such as cluster boxes. *Field structure:* Reduce the number of field administrative offices.	*Mail processing:* Support having USPS reduce excess capacity by closing some of its major mail processing facilities. *Retail:* Remove statutory and appropriations language restricting USPS's ability to close some of its 36,500 retail facilities. *Delivery:* Remove appropriations language requiring 6-day delivery.
Strategy: Generate revenues through product and pricing flexibility		
• The changing use of the mail is projected to continue limiting USPS's ability to generate sufficient revenues. • Rate increases for market-dominant products are limited by the inflation-based price cap. • Large rate increases may lower USPS revenues in the long run and add to its excess capacity. • In fiscal year 2009, USPS lost $1.7 billion from products with revenues that did not cover costs, mainly Periodicals and Standard Mail Flats (e.g., catalogs).	• Revise pricing for market-dominant products, such as First-Class Mail and Standard Mail. • Address loss-making products by better aligning prices and costs. • Provide volume incentives for certain types of bulk business mail. • Develop new postal products and product enhancements. • Provide incentives by simplifying complex rules for mail preparation.	Determine whether preferential pricing required by law for loss-making products should continue.

Contents

Figures

Abbreviations

AMP	Area Mail Processing
BRAC	Base Realignment and Closure
CBO	Congressional Budget Office
CSRDF	Civil Service Retirement and Disability Fund
CSRS	Civil Service Retirement System
Dual CSRS	Dual Civil Service Retirement System and Social Security
FEHB Fund	Federal Employees Health Benefits Fund
FERS	Federal Employees Retirement System
FTC	Federal Trade Commission
NSA	negotiated service agreement
OIG	Office of Inspector General
OPM	Office of Personnel Management
PAEA	Postal Accountability and Enhancement Act of 2006
PRA	Postal Reorganization Act of 1970
PRC	Postal Regulatory Commission
RHB Fund	Postal Service Retiree Health Benefits Fund
TSP	Thrift Savings Plan
UPS	United Parcel Service
USPS	United States Postal Service

This is a work of the U.S. government and is not subject to copyright protection in the United States. The published product may be reproduced and distributed in its entirety without further permission from GAO. However, because this work may contain copyrighted images or other material, permission from the copyright holder may be necessary if you wish to reproduce this material separately.

GAO

Accountability * Integrity * Reliability

United States Government Accountability Office
Washington, DC 20548

April 12, 2010

Congressional Committees

The Postal Accountability and Enhancement Act[1] (PAEA) of 2006 required GAO to evaluate strategies and options for the long-term structural and operational reform of the United States Postal Service (USPS). At that time, USPS was given additional pricing flexibility and required to develop service standards, while PAEA reconfigured certain financial obligations. These changes provided additional tools to improve its effectiveness and accountability in an increasingly competitive delivery and communications marketplace. Recent developments have highlighted deficiencies in USPS's business model, which is to fulfill its mission through self-supporting, businesslike operations. As mail volume declined in fiscal years 2007 through 2009, USPS financial viability deteriorated, and it was not able to cut costs fast enough to offset the accelerated decline in mail volume and revenue. These volume declines have been brought on by customers' changing use of the mail and have been accelerated by the recession and continuing difficulties in the economy. In fiscal year 2009, total mail volume declined by a record 26 billion pieces, while revenue dropped nearly $7 billion. USPS has incurred close to $12 billion in losses in fiscal years 2007 through 2009 and is rapidly approaching its statutory debt limit. Furthermore, a looming cash shortfall at the end of fiscal year 2009 necessitated last-minute congressional action that deferred costs by reducing USPS's mandated retiree health benefit payments. On the basis of these challenges, in July 2009, we testified[2] that a restructuring of USPS was needed to enhance its current and long-term financial viability and placed USPS's financial condition on our high-risk list.[3]

USPS's financial outlook is poor. In fiscal year 2010, USPS expects a record loss of over $7 billion, its outstanding debt to increase to $13.2 billion, and limited cash flow that will continue to constrain capital investment. USPS projections show losses growing over the next decade

[1]Pub. L. No. 109-435, 120 Stat. 3198 (Dec. 20, 2006).

[2]GAO, *U.S. Postal Service: Broad Restructuring Needed to Address Deteriorating Finances*, GAO-09-790T (Washington, D.C.: July 30, 2009).

[3]GAO, *High-Risk Series: Restructuring the U.S. Postal Service to Achieve Sustainable Financial Viability*, GAO-09-937SP (Washington, D.C.: July 28, 2009). USPS's transformation efforts and long-term outlook were on our high-risk list from 2001 to 2007.

as mail volume declines further and costs rise. USPS remains the largest civilian federal agency (employing about 712,000 employees at the end of fiscal year 2009), has a nationwide network of about 38,000 facilities, and provides 6-day-per-week mail delivery to most of the nation's 150 million addresses.

PAEA required that GAO complete this report by December 2011. Because of USPS's financial crisis and our assessment that restructuring is urgently needed, our work has been accelerated at the request of Members of Congress and is presented in this report. Our objectives were to assess (1) the viability of USPS's business model, (2) strategies and options to address the challenges to USPS's current business model, and (3) actions Congress and USPS need to take to facilitate progress toward USPS's financial viability.

In conducting our work related to assessing the viability of USPS's business model and strategies and options to solve its challenges, we relied on our past work and USPS financial and operating data. We interviewed various USPS officials, including the Postmaster General, the Deputy Postmaster General, the former and current Chairmen of the Board of Governors, and headquarters and field staff. We reviewed USPS's *Action Plan* released March 2010 and its financial and volume projections.[4] We did not assess the validity of USPS's financial and mail volume projections due to time and resource constraints. We reviewed USPS's current legal and regulatory framework and relevant congressional testimonies and hearings. We also reviewed the results of retiree health valuations provided to us by the Office of Personnel Management (OPM) in March 2010, which were based on USPS employee population projections. We did not assess the reasonableness of these projections or OPM's actuarial assumptions and methodology. We utilized OPM's valuation results to analyze the financial impacts of selected options for funding USPS's retiree health benefit obligations.

We also examined studies performed by other postal stakeholders, including the Postal Regulatory Commission (PRC), USPS Office of Inspector General (OIG), the 2003 President's Commission on the United States Postal Service, and other mailing industry experts. We met with

[4]United States Postal Service, *Ensuring a Viable Postal Service for America: An Action Plan for the Future* (Washington, D.C.: March 2010). USPS's plan and related material are available at the following Web address:
http://www.usps.com/strategicplanning/futurepostalservice.htm (accessed on Apr. 9, 2010).

PRC commissioners and staff, representatives of the four major employee unions and three major management associations, USPS OIG, members of the mailing industry, economists, and other stakeholders. We distributed a list of questions to over 60 organizations to collect additional information on actions that could be taken to improve USPS's business model and the potential impacts of these actions. The organizations represented various sections of the postal community, such as postal unions and management associations; small and large mailers; and mailers across various segments (e.g., First-Class Mail, Standard Mail, Periodicals, parcels, newspapers, and nonprofit mail); and other companies in the mailing industry. They were selected on the basis of several factors, including testifying before Congress on postal issues; submitting comments to the 2003 President's Commission; submitting comments to PRC on universal service, the postal monopoly, and the new regulatory structure for ratemaking; and submitting comments to the Federal Trade Commission (FTC) on differences in the legal status between USPS and its competitors.

We gathered and evaluated relevant strategies and options on the basis of a variety of criteria, including their potential to reduce USPS costs, realign its operations, and increase revenues, in light of USPS's current and projected financial condition. In this report, we present selected options that could be considered to address USPS's financial viability on the basis of these criteria. Some options are consistent with actions we have discussed in our past work, while others have been discussed in congressional hearings, regulatory proceedings, and major studies. We analyzed the options on the basis of the criteria that we have previously listed, including available cost and revenue data. Furthermore, assessing certain options related to a comprehensive restructuring of USPS's legal and regulatory framework was limited because it is still too soon to see the full impact of the changes from PAEA. We also plan to address the experiences of foreign postal administrations in a separate report.

We conducted this performance audit from August 2009 to April 2010 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. Appendix I contains a detailed discussion of our scope and methodology. We requested comments on a draft of this report from USPS, and its comments are discussed later in this report and reproduced in appendix II.

Background

Over the last 40 years, Congress has considered several business models to provide postal services to the nation and moved USPS toward a more businesslike entity but has simultaneously placed constraints on its operations. Until 1970, the federal government provided postal services via the U.S. Post Office Department, a government agency that received annual appropriations from Congress. Congress was involved in many aspects of the department's operations, including the selection of managers (e.g., postmasters), and in setting postal rates and wages. A presidential commission (The Kappel Commission) reported to the President in 1968 on the crisis facing the department, which included financial losses, management problems, service breakdowns, low productivity, and low employee morale. The Kappel Commission's basic finding was that "the procedures for administering the ordinary executive departments of Government are inappropriate for the Post Office."[5] Furthermore, it concluded that

> "a transfer of the postal system to the private sector is not feasible, largely for reasons of financing...but the possibility remains of private ownership at some future time, if such a transfer were then considered to be feasible and in the public interest.... We recommend, therefore, that Congress charter a Government-owned Corporation to operate the postal service. The corporate form would permit much more successful operation of what has become a major business activity than is possible under present circumstances."

The Postal Reorganization Act (PRA) of 1970 replaced the department with the current USPS model—an independent establishment of the executive branch designed to be self-sustaining by covering its operating costs with revenues generated through the sales of postage and postal-related products and services. USPS receives no appropriations for purposes other than revenue forgone on free and reduced rate mail.[6]

In 1996, Congress again began considering the merits of postal reform and ultimately enacted PAEA in 2006. A number of factors encouraged reform, including financial challenges, such as growing cash-flow problems and

[5]President's Commission on Postal Organization, *Towards Postal Excellence* (Washington, D.C.: June 1968).

[6]USPS receives annual appropriations for revenue forgone in providing (1) free and reduced rate mail for the blind and (2) overseas voting materials for U.S. elections. Congress appropriated about $118 million to USPS for these purposes for fiscal year 2010.

debt. A second presidential commission examined USPS's future and issued a report in 2003 that recommended a number of actions to ensure the viability of postal services.[7] Additionally, the Postal Civil Service Retirement System Funding Reform Act of 2003 was enacted after OPM determined that USPS was overfunding its employees' pensions.[8] This law required the amounts achieved by reducing the previous pension contributions to be used toward USPS's debt to the U.S. Treasury and set aside any remaining amounts in an escrow account. Congress addressed how the escrowed funds should be used—along with many of USPS's other financial and operational challenges—in PAEA. Key requirements and flexibilities provided in PAEA are detailed in table 1.

Table 1: Selected Requirements and Flexibilities Provided to USPS in PAEA

Key areas	Description
Flexible pricing mechanisms	• Abolished the former process for setting prices that was often lengthy, costly, and litigious. Under the new structure, USPS has broad latitude to announce price changes that are reviewed by the newly created PRC and implemented in a streamlined process. • Allowed USPS to raise average rates for each class of market-dominant products,[a] such as First-Class Mail, Standard Mail, Periodicals, and Package Services, up to a defined annual price cap; exceed the price cap should extraordinary or exceptional circumstances arise; and use any unused pricing authority within 5 years. • Allowed USPS to raise prices for competitive products, such as Priority Mail or Express Mail, as long as each product's revenue covers the product's costs and the revenue from all competitive products covers what PRC determines to be an appropriate share of USPS's institutional costs (overhead costs).
Modern delivery performance standards	• Required establishing modern delivery performance standards for market-dominant products. These standards for on-time delivery of mail enable mailers to have realistic expectations for the number of days mail takes to be delivered, and to organize their activities accordingly.
Restriction on nonpostal products	• Restricted USPS from introducing new nonpostal products and services. • Required PRC to review each nonpostal service USPS already offered and determine whether it should continue based on (1) the public need for the service and (2) the ability of the private sector to meet the public need for the service.
Retiree health benefit payments	• Required the funds accumulated in escrow and annual payments to be made in fiscal years 2007 through 2016 to prefund retiree health obligations.
Ability to retain earnings	• Allowed USPS to retain any earnings.

[7]President's Commission on the United States Postal Service, *Embracing the Future: Making the Tough Choices to Preserve Universal Mail Service* (Washington, D.C.: July 31, 2003).

[8]Pub. L. No. 108-18, 117 Stat. 624 (Apr. 23, 2003).

Key areas	Description
Plan for improving operational efficiency	• Required USPS to develop a plan that, among other things, included a strategy for rationalizing the postal facilities network and removing excess processing capacity and space from the network, as well as identifying the cost savings and other benefits associated with network rationalization.
Financial reporting	• Established new reporting and accounting requirements to enhance collection and reporting of information on rates and financial performance.

Source: GAO analysis of Pub. L. No. 109-435.

[a]Market-dominant products primarily include First-Class Mail (e.g., correspondence, bills, payments, statements, and advertising); Standard Mail (mainly, bulk advertising and direct mail solicitations); Periodicals (mainly, magazines and local newspapers); and some types of Package Services (primarily, single-piece Parcel Post, Media Mail, library mail, and bound printed matter).

PAEA also made changes to USPS's regulatory and oversight structure. In addition to responsibilities for reviewing pricing and nonpostal services described in table 1, the newly created PRC gained additional oversight responsibilities, including responsibility for making annual determinations of USPS compliance with applicable laws, developing accounting practices and procedures for USPS, reviewing the universal service obligation, and providing transparency through periodic reports. The USPS Board of Governors, which has responsibilities similar to a board of directors of a publicly held corporation, directs the exercise of the powers of USPS, directs and controls its expenditures, reviews its practices, conducts long-range planning, and sets policies on all postal matters.[9] PAEA added new qualifications and lengths of term for new board members.

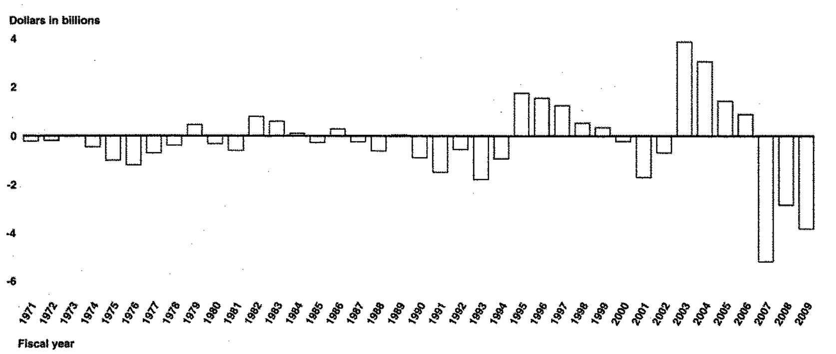
USPS's Business Model Is Not Viable

USPS's business model is not viable due to its inability to reduce costs sufficiently in response to continuing declines in mail volume and revenue. Mail volume declined 36 billion pieces over the last 3 fiscal years, 2007 through 2009, due to the economic downturn and changing use of the mail, with mail continuing to shift to electronic communications and payments. USPS lost nearly $12 billion over this period, despite achieving billions in cost savings, reducing capital investments, and raising rates. However, USPS had difficulty in eliminating costly excess capacity, and its revenue initiatives had limited results. To put these results into context, until recently, USPS's business model benefited from growth in mail volume to

[9]USPS is directed by a Board of Governors consisting of 11 members, including (1) 9 Governors appointed by the President, with the advice and consent of the Senate, to 7-year terms; (2) the Postmaster General, who is appointed by the Governors; and (3) the Deputy Postmaster General, who is appointed by the Governors and the Postmaster General. Not more than 5 of the 9 Governors may belong to the same political party.

help cover costs and enable it to be self-supporting. In each of the last 3 fiscal years, USPS borrowed the maximum $3 billion from the U.S. Treasury and incurred record financial losses (see fig. 1). A looming cash shortfall led to congressional action at the end of fiscal year 2009 that deferred costs by reducing USPS's mandated retiree health benefit payment. Looking forward, USPS projects continued mail volume decline and financial losses over the next decade.

Figure 1: USPS Annual Net Income (Loss), Fiscal Years 1971 through 2009



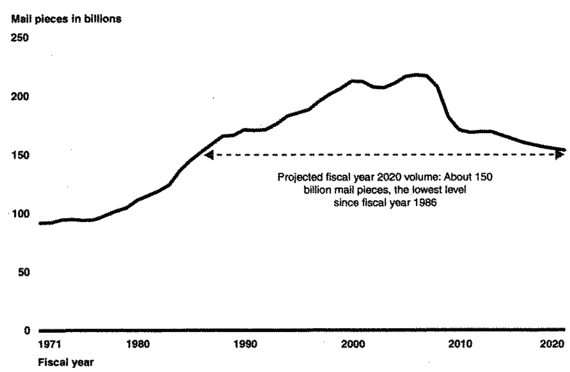
Source: USPS.

Note: A looming cash shortfall in 2009 necessitated last-minute congressional action to defer costs by reducing USPS's mandated payments to prefund retiree health benefits from $5.4 billion to $1.4 billion. While this action provided USPS with $4 billion of financial relief, USPS still reported a loss of $3.8 billion for the year. USPS's $8.4 billion in cumulative net income for fiscal years 2003 through 2005 largely resulted from a 2003 law (Pub. L. No. 108-18) that reduced USPS pension benefit payments by about $9 billion over this period.

USPS Faces Reduced Mail Volume from Changes in Mail Use

In fiscal year 2009, USPS's mail volume declined to 17 percent below its peak of 213 billion pieces in fiscal year 2006. USPS projects that total mail volume will decline to 167 billion pieces in fiscal year 2010—the lowest level since fiscal year 1992 and 22 percent less than its fiscal year 2006 peak. USPS and many mailers who provided information for this study do not expect volume to return to its former levels when the economy recovers. By fiscal year 2020, USPS projects further volume declines of 15 percent to about 150 billion pieces, the lowest level since fiscal year 1986 (see fig. 2).

Figure 2: Actual and Projected Total Mail Volume, Fiscal Years 1971 through 2020

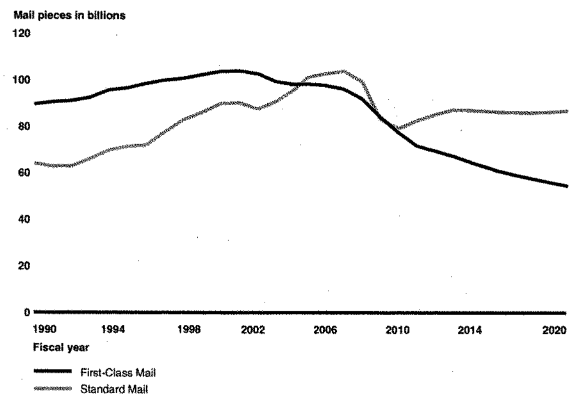


Source: USPS.

- First-Class Mail volume has declined 19 percent since it peaked in fiscal year 2001, and USPS projects that it will decline by another 37 percent over the next decade (see fig. 3). This mail is highly profitable and generates over 70 percent of the revenues used to cover USPS overhead costs.
- Standard Mail (primarily advertising) volume has declined 20 percent since it peaked in fiscal year 2007, and USPS projects that it will remain roughly flat over the next decade. This class of mail is profitable overall but lower priced, therefore, it takes 3.4 pieces of Standard Mail, on average, to equal the profit from the average piece of First-Class Mail.

Standard Mail volume was affected by large rate increases in 2007 for flat-sized mail, such as catalogs, and by the recession that affected advertising, such as mortgage, home equity, and credit card solicitations. These solicitations appear unlikely to return to former levels. Standard Mail also faces growing competition from electronic alternatives, increasing the possibility that its volume may decline in the long term.

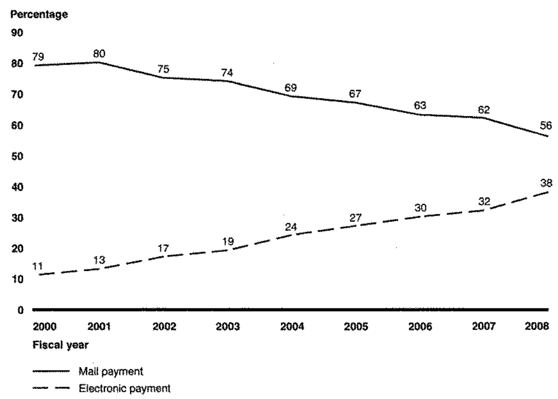
Figure 3: Actual and Projected First-Class Mail and Standard Mail Volume, Fiscal Years 1990 through 2020



Source: USPS.

One reason that mail volumes declined is because businesses and consumers have moved to electronic payment alternatives over the past decade (see fig. 4).

Figure 4: Percentage of Household Bill Payments Made by Mail and Electronically, Fiscal Years 2000 through 2008

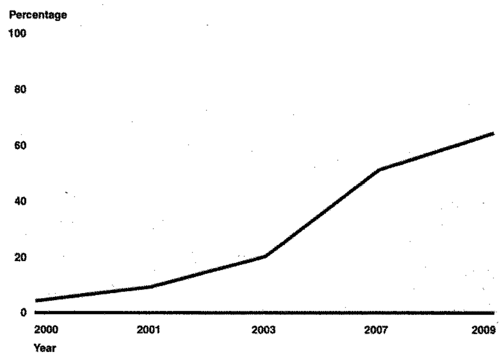


Source: USPS.

Looking forward, the use of electronic alternatives for communications and payments, including broadband and mobile technology, is expected to continue to grow. Nearly two-thirds of American households had broadband service in fiscal year 2008, up from 4.4 percent in less than a decade (see fig. 5). Expanded availability and adoption of broadband technology is being facilitated by federal spending under the American Recovery and Reinvestment Act.[10]

[10]GAO, *Recovery Act: Preliminary Observations on the Implementation of Broadband Programs*, GAO-10-192T (Washington, D.C.: Oct. 27, 2009). Also see GAO, *Recovery Act: Agencies Are Addressing Broadband Program Challenges, but Actions Are Needed to Improve Implementation*, GAO-10-80 (Washington, D.C.: Nov. 16, 2009).

Figure 5: Broadband Use by American Households, 2000 to 2009



Source: U.S. Department of Commerce, National Telecommunications and Information Administration.

USPS Has Made Progress in Reducing Costs but Still Faces Major Cost Pressures

USPS achieved nearly $10 billion in cost savings in the 3 fiscal years 2007 through 2009, primarily by cutting nearly 201 million work hours. Work-hour savings were achieved by workforce reductions of over 84,000 full- and part-time employees, primarily through retirements; reduced overtime; and changes to postal operations. For example, USPS reached agreement with the National Association of Letter Carriers to realign delivery routes, and with the American Postal Workers Union and the National Postal Mail Handlers Union on early retirement incentives. However, USPS's cost savings and added revenue from rate increases and other actions to generate revenues were insufficient to fully offset the impact of declines in mail volume and rising personnel-related costs. Thus, USPS revenues declined by $4.7 billion during this period of time, while its costs declined $7 million.

USPS also has large financial liabilities and obligations that totaled over $88 billion in fiscal year 2009. Over the last 2 fiscal years, total liabilities and obligations have increased by nearly $14 billion (see table 2). USPS debt to the U.S. Treasury, over this same period, increased by $6 billion and pension obligations changed by over $8 billion—from a $5.3 billion surplus to $2.8 billion in unfunded obligations. To put these liabilities and obligations into context, they increased from 100 percent of USPS revenues in fiscal year 2007 to 130 percent of revenues in fiscal year 2009.

Table 2: USPS Financial Liabilities and Unfunded Obligations, Fiscal Years 2007 through 2009

Dollars in billions

	Liabilities				Obligations			
Fiscal year	Outstanding debt	Workers' compensation liabilities	Other liabilities[a]	Total liabilities	Unfunded obligations for retiree health benefits	Unfunded obligations (surplus) for pension benefits[b]	Total unfunded obligations	Total liabilities and obligations
2007	$4.2	$6.8	$13.7	**$24.7**	$55.0	$(5.3)	**$49.7**	**$74.5**
2008	7.2	7.0	13.5	**27.7**	53.5	2.5	**56.0**	**83.6**
2009	10.2	9.1	14.3	**33.5**	52.0	2.8	**54.8**	**88.3**

Source: USPS.

Note: Data may not add exactly to totals due to rounding.

[a]Other liabilities include many items, such as operating expenses that USPS committed to in fiscal year 2009 but has not yet paid and the value of employees' accumulated leave.

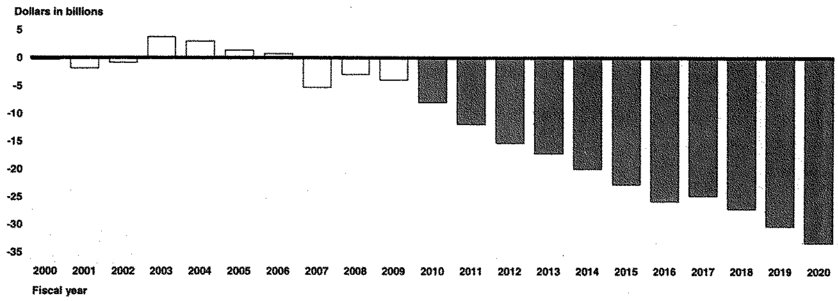
[b]Includes both CSRS and FERS obligations.

USPS's Financial Outlook Is Poor

Declines in mail volume and revenue, large financial losses, increasing debt, and financial obligations will continue to challenge USPS. For fiscal year 2010, USPS is projecting a record loss of over $7 billion and additional pressures to generate sufficient cash to meet its obligations. Furthermore, it has halted construction of most new facilities and has budgeted $1.5 billion in capital cash outlays (mostly for prior commitments), which is down from the average of $2.2 billion in the previous 5 fiscal years. USPS also expects to borrow $3 billion in fiscal year 2010, which would bring its total outstanding debt to $13.2 billion, close to its $15 billion statutory limit.

Looking forward, USPS projects that, absent additional action, annual financial losses will escalate over the next decade to $33 billion in fiscal year 2020 (see fig. 6). According to USPS, its projected losses will result from declining mail volume, stagnant revenue (despite rate increases), large costs to provide universal service, and rising workforce costs. These projections are the most pessimistic in many years. Stakeholder interviews reinforce the conclusion that the recent recession was a "tipping point" that has accelerated the diversion of mail to electronic alternatives, particularly among business mailers who generate the most mail volume and revenues, leading to sobering financial results.

Figure 6: USPS Actual and Projected Net Income (Loss), Fiscal Years 2000 through 2020



Source: USPS.

Note: The projection for fiscal year 2010 is from USPS's Fiscal Year 2010 Integrated Financial Plan. USPS projections for fiscal years 2011 through 2020 are from its *Action Plan* and assume that (1) USPS takes no management actions beyond those in its fiscal year 2009 budget and (2) USPS's total statutory borrowing limit of $15 billion would be increased to accommodate these losses. USPS's $8.4 billion in cumulative net income for fiscal years 2003 through 2005 largely resulted from a 2003 law (Pub. L. No. 108-18) that reduced USPS pension benefit payments by about $9 billion over this period.

Strategies and Options That Address Challenges to USPS's Current Business Model

Making progress toward USPS's financial viability would primarily involve taking action on strategies and options to rightsize operations, cut costs, and increase revenues. USPS does not need—and cannot afford to maintain—its costly excess infrastructure capacity. USPS has achieved noteworthy cost reductions, but much more progress is needed. Making the necessary progress would require (1) taking more aggressive actions to reduce costs and increase revenues within its current authority, using the collective bargaining process to address wages, benefits, and workforce flexibility, and (2) congressional action to address legal restrictions and resistance to realigning USPS operations, networks, and workforce. Key strategies and options, some of which would require statutory changes, fall into the following three major categories:

- reducing compensation and benefits costs,
- reducing other operations and network costs and improving efficiency, and
- generating revenues through product and pricing flexibility.

Ultimately, Congress may want to examine other options that would alter the ownership structure of USPS. For example, USPS might be moved back to being a federal agency funded in part by taxpayer support, or it might be moved to a corporate model. This report does not address the ownership issue because of an array of functional and operational options—discussed throughout this report—that need to be examined immediately. The resolution of some of these more pressing issues might afford a better understanding of whether the ownership structure should be modified.

Options to Reduce Compensation and Benefits Costs

USPS has options to reduce its compensation and benefits costs in the following four key areas: workforce size, to be aligned with reduced workload; wages, which continue to be a key component of costs; benefits, which in some cases are more generous than those provided by other federal agencies; and workforce flexibility, including the mix of full- and part-time employees and work rules that govern what tasks employees can perform. Changes in these areas would need to be negotiated with employee unions and would involve tradeoffs between reducing costs and addressing union concerns that reducing workforce size and compensation and benefits would erode the number of well-paying jobs.

About 85 percent of USPS employees are covered by collective bargaining agreements, which correspond with major crafts (see table 3). USPS and its employee unions will begin negotiations for new agreements in 2010 and 2011. If USPS and its unions are unable to agree, binding arbitration by a third-party panel will ultimately be used to establish agreement. USPS is also required to consult with its management associations that represent postmasters and supervisors. About 78 percent of USPS employees are full time and receive salary increases and cost-of-living adjustments based on predetermined levels. These employees are generally scheduled in 8-hour shifts and can earn overtime pay, except for rural mail carriers, who are generally paid a salary without overtime. Managers are not covered by collective bargaining agreements and are compensated under a pay-for-performance program. About 90 percent of city carriers are full time, while about 55 percent of rural carriers are full time.

Table 3: USPS Employees Covered by Selected Union Contracts as of September 30, 2009

Craft	Number of employees	Name of union	Contract expiration date
Clerks	177,842	American Postal Workers Union	November 20, 2010
Mail Handlers	52,954	National Postal Mail Handlers Union	November 20, 2011
City Carriers	200,658	National Association of Letter Carriers	November 20, 2011
Rural Carriers	122,278[a]	National Rural Letter Carriers' Association	November 20, 2010
Total	**553,732**		

Sources: USPS and employee unions.

[a]Includes 54,529 part-time rural carriers.

USPS has not achieved significant reductions in compensation and benefits, in part due to the following challenges:

- USPS is required by law to maintain compensation and benefits comparable to the private sector. The application of the comparability standard to postal employees—that is, whether a compensation premium exists between postal employees and private-sector employees who do comparable work—has been a source of disagreement between management and postal unions in negotiations and interest arbitration.

- Career USPS employees participate in federal pension and benefits programs, including health care and life insurance. USPS collective bargaining agreements include provisions to reduce USPS's contribution to health care premiums by 1 percent a year from 85 percent in fiscal year 2007 to 81 percent in 2011 or 80 percent in 2012, depending on the agreement. Nevertheless, USPS covers a higher proportion of employee premiums for health care and life insurance than most other federal agencies. The law requires USPS's fringe benefits to be at least as favorable as those in effect when the PRA of 1970 was enacted.[11]

- USPS is also required by law to participate in the federal workers' compensation program[12] and ensure coverage for injured employees. Some benefits provided under the federal program exceed those provided in the private sector. For example, injured USPS employees with dependents receive 75 percent of their salary compared with the 66 percent of pay private employers covered under state workers'

[11]39 U.S.C. § 1005(f).

[12]39 U.S.C. § 1005(c).

compensation laws typically provide. Furthermore, USPS employees receiving this benefit often do not opt to retire when eligible, staying permanently on the more generous workers' compensation rolls.

- Current collective bargaining agreements include provisions related to compensation, leave, workforce composition, and work rules. They also include some provisions that allow USPS to make changes, such as relocating employees, but other provisions limit USPS's flexibility to manage work efficiently and rightsize its workforce. For example, current collective bargaining agreements
  - limit the percentage of part-time and contract workers who help USPS match its workforce to changing workload;
  - limit managers from assigning work to employees outside of their crafts, such as having a retail clerk deliver mail;
  - limit outsourcing for city delivery routes; and
  - contain "no-layoff" provisions for about 500,000 employees and require USPS to release lower-cost part-time and temporary employees before it can layoff any full-time workers without layoff protection.
- Currently, if the collective bargaining process reaches binding arbitration, there is no statutory requirement for USPS's financial condition to be considered. In 2009, proposed Senate legislation[13] included language that would require any binding arbitration in the negotiation of postal contracts to take the financial health of the Postal Service into account.

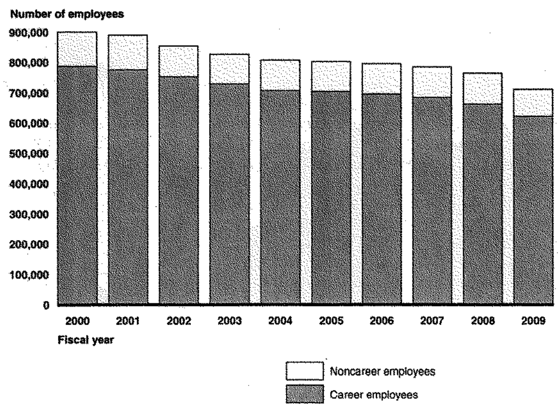
Workforce Size

The 2003 President's Commission reported that "far more than individual benefits, the size of the [postal] workforce determines the cost of the workforce." USPS has worked to reduce the size of its workforce through regular retirements and early retirements in response to recent separation incentives and through a hiring freeze. USPS's workforce of career and noncareer employees declined by nearly 21 percent—from 901,238 at the end of fiscal year 2000 to 712,082 at the end of fiscal year 2009 (see fig. 7). Career employees continued to comprise most of the total workforce throughout this period. USPS has a window of opportunity to reduce the cost and size of its workforce through the large number of upcoming retirements, minimizing any need for layoffs. In this regard, about 5

[13]S. 1507, 111th Cong. (2009).

percent of USPS employees will be eligible and expected to retire each year through 2020—a total of approximately 300,000 employees. Key issues include what size workforce is needed to reflect changes in mail volumes, revenues, and operations; how quickly changes can be made in this area; whether separation incentives should be offered and are affordable; and to what extent and under what terms should outsourcing be considered.

Figure 7: Total Career and Noncareer Postal Employees, Fiscal Years 2000 through 2009



Source: USPS.

Options to reduce the size of USPS's workforce include the following:

- *Retirement and separation incentives:* According to USPS officials, incentives could accelerate the rate of attrition, but it needs to have sufficient cash to fund them.
- *Outsourcing:* Determine which functions would be cost-effective to outsource (using companies or individuals). At the end of fiscal year 2009, USPS had about 36,500 retail facilities, 3,000 of which were contract postal units and 800 of which were community post offices staffed by nonpostal employees. USPS also has long outsourced most of its long-distance air

and ground transportation. In delivery operations, contractors deliver to less than 2 percent of USPS's delivery points. Postal labor unions and some Members of Congress have previously resisted outsourcing. For example, after USPS attempted to contract out some city delivery routes in 2007, legislation was introduced in both Houses of Congress on this matter.[14] USPS and the National Association of Letter Carriers subsequently agreed to a moratorium on outsourcing city carrier delivery through November 2011. Looking forward, the outsourcing issue could involve consideration of the tradeoffs between the loss of government jobs paying middle-class wages and benefits to achieve savings by shifting the work to private-sector jobs that may pay lower wages and not have guaranteed benefits.

- *Layoffs:* USPS could implement layoffs as a last resort if it has too few positions to offer employees affected by restructuring. For example, USPS could implement layoffs as part of shifting from 6-day delivery to 5-day delivery. However, under current collective bargaining agreements, any layoffs of covered employees not protected by no-layoff clauses must first be applied to noncareer employees, such as temporary employees, whose average wages are less than full-time career employees.

Wages

USPS wages were $39 billion in fiscal year 2009—about one-half of its costs. Increasing wages have been a key driver of additional costs, expected to add $1 billion in fiscal year 2010. Wages have traditionally increased on the basis of cost-of-living allowances keyed to the Consumer Price Index. Rising wages also increase benefit costs, such as pensions. Key issues include how USPS can improve its compensation systems to balance the need for fair compensation with reducing costs and increasing incentives to become more competitive. In this regard, a recent legislative proposal would have required that USPS's financial condition be considered if collective bargaining reaches binding arbitration.[15] One option would be a two-tier pay system that would pay new hires lower wages, while "grandfathering" current employees under the current pay structure.

[14]The Mail Delivery Protection Act of 2007, S. 1457, 110th Cong. (2007) would have restricted contracting for mail delivery. The Mail Network Protection Act of 2007, H.R. 4236, 110th Cong. (2007), specified conditions that must be met before USPS entered into some contracts, such as for surface transportation of mail. Additionally, H.Res. 282, 110th Cong. (2007), expressed "the sense of the House of Representatives that the United States Postal Service should discontinue the practice of contracting out mail delivery services."

[15]Postal Service Retiree Health Benefits Funding Reform Act of 2009, S. 1507, 110th Cong. (2009).

Benefits

USPS makes payments to fund its liabilities and obligations for retiree health and pension benefits, health and life insurance premiums, and workers' compensation.[16] Benefits cost USPS almost $17 billion in fiscal year 2009, over 23 percent of its total costs. The cost would have been nearly $21 billion if Congress had not reduced USPS payments for retiree health benefits by $4 billion to address a looming cash shortfall. Key issues are assigning financial responsibility for benefits to USPS, its employees, and current and future ratepayers and balancing USPS's poor financial condition, while keeping rates affordable, meeting legal requirements for employee benefits, and minimizing risk to the taxpayer if USPS would be unable to meet its responsibilities.

Retiree Health Benefits

According to OPM estimates, at the end of fiscal year 2009, the actuarially determined obligation for USPS's future retiree health benefits was about $87.5 billion. At that time, the dedicated Postal Service Retiree Health Benefits Fund (the RHB Fund) had a balance of $35.5 billion, and, therefore, unfunded obligations of $52.0 billion remained. These unfunded obligations developed largely because, prior to the enactment of PAEA in 2006, USPS financed its share of the health insurance premiums for its retirees on a pay-as-you-go basis, rather than on the annual accrued cost of future benefits attributable to the service of current employees. PAEA required USPS to begin prefunding its retiree health benefit obligations with annual payments to the RHB Fund, while continuing to pay its share of the retiree health premiums of current retirees to the Federal Employees Health Benefits Fund (the FEHB Fund).

Since PAEA was enacted, mail volume has declined, USPS's financial condition has deteriorated, and it has had difficulty in making its required payments to prefund its retiree health benefit obligations. In fiscal year 2009, a looming cash shortfall led to last-minute congressional action that deferred costs by reducing USPS's required prefunding payment from $5.4 billion to $1.4 billion. At the end of fiscal year 2009, USPS had about 463,000 annuitants and survivors participating in the Federal Employees Health Benefits Program. Furthermore, 162,000 USPS career employees are eligible for regular retirement this fiscal year, and this number is projected to increase to about 300,000 career employees over the next

[16] USPS accounts for its participation in the federal government's health and pension plans by recognizing these contributions as an expense. This accounting method is based on private-sector standards that employers use to account for multiemployer benefit plans.

decade. For fiscal year 2010, USPS has reported that it is "highly uncertain" whether it will have sufficient cash to cover its required prefunding payment of $5.5 billion that is due by September 30, 2010. According to USPS's fiscal year 2010 budget, by making the required prefunding payment, it will end the fiscal year with a cash balance of only $200 million. However, USPS officials have said that this cash balance would likely be inadequate to finance operations in October 2010, when it must make three payroll payments of close to $2 billion each, as well as a payment for workers' compensation costs expected to exceed $1 billion. In response to these likely conditions, USPS has requested that Congress revise the required schedule for retiree health benefits payments as part of a package to improve its financial viability.

There are multiple options for funding USPS's retiree health benefit obligations. In addition to the current prefunding approach, where the obligations are paid prior to when USPS's share of retiree health premiums are due, there are two broad approaches—(1) a "pay-as-you-go" funding approach, where USPS's share of retiree health premiums are paid as they are billed for current retirees, and (2) an actuarial funding approach, where payments include amounts for "normal costs" to finance the future retiree health benefits attributed to the service of current employees and amortization amounts to liquidate unfunded obligations over a 40-year period. The impact of these various approaches on USPS's payments would depend on whether its share of retiree health premiums would be paid directly by USPS to the FEHB Fund or whether the premiums would be paid from the RHB Fund. Depending on which option is selected, changes could also impact the federal budget deficit. PAEA's approach to funding USPS's retiree health benefit obligations is a combination of the prefunding and pay-as-you-go approaches that we have previously described. Specifically, PAEA requires USPS to make two payments annually over fiscal years 2010 through 2016:

- a payment to the FEHB Fund to cover its share of the premiums for current retirees and
- a statutorily determined payment to the RHB Fund to prefund obligations for future retirees.

Starting in fiscal year 2017—after the last statutorily scheduled prefunding payment—PAEA requires that USPS's share of retiree health premiums be paid from the RHB Fund and requires OPM to determine future payments to the RHB Fund. Each annual payment to the RHB Fund starting in fiscal year 2017 will be the sum of the two amounts that finance the following:

- the annual accrued cost of future benefits attributable to the service of current USPS employees, which OPM refers to as "normal costs," and

- amortization payments over 40 years to liquidate any unfunded obligations.[17]

Table 4 shows USPS payments from fiscal years 2010 through 2020, based on updated estimates that OPM provided to us for this report. Total USPS payments are estimated to increase from $7.8 billion in fiscal year 2010 to $10.3 billion in fiscal year 2016. The payments are estimated to decline to $6.4 billion in fiscal year 2017 and increase to $7.3 billion in fiscal year 2020. Based on GAO analysis, assuming that USPS made these payments through 2020, estimated unfunded obligations of about $33 billion would remain.

Table 4: USPS Retiree Health Benefit Payments under Current Law, Fiscal Years 2010 through 2020, which Include Prefunding through Fiscal Year 2016

Dollars in billions

Fiscal year	USPS payments to RHB Fund	USPS payments to FEHB Fund	Total USPS payments	Payments from RHB Fund to FEHB Fund
2010	$5.5	$2.3	**$7.8**	$0.0
2011	5.5	2.6	**8.1**	0.0
2012	5.6	2.9	**8.5**	0.0
2013	5.6	3.3	**8.9**	0.0
2014	5.7	3.6	**9.3**	0.0
2015	5.7	4.0	**9.7**	0.0
2016	5.8	4.5	**10.3**	0.0
2017	6.4	0.0	**6.4**	4.9
2018	6.7	0.0	**6.7**	5.4
2019	7.0	0.0	**7.0**	5.8
2020	7.3	0.0	**7.3**	6.4
Total	**$66.8**	**$23.2**	**$90.0**	**$22.5**

Source: OPM analysis prepared at GAO's request.

[17]Pub. L. No. 109-435, § 803.

Note: Estimates are based on OPM assumptions that factor in updated USPS workforce size projections, annual inflation in health care costs of 8 percent in fiscal year 2010 that then declines slowly, a general inflation rate of 3.5 percent annually, and RHB Fund interest of 6.25 percent annually. USPS prefunding payments are specified in PAEA and are shown above as USPS Payments to RHB Fund for fiscal years 2010 through 2016. Starting in fiscal year 2017, annual USPS payments will include (1) "normal costs" (i.e., future retiree health benefits costs attributed to the service of current employees) and (2) amortization amounts to liquidate any unfunded obligations over a 40-year period.

In 2009, proposed legislation was introduced in both houses of Congress that would have revised the payment schedule for postal retiree health benefits.[18] The House legislation (H.R. 22) would have shifted responsibility for payments for current retiree health premiums from USPS to the RHB Fund for fiscal years 2009 through 2011. Such action would result in USPS needing to pay additional amounts to the RHB Fund in the future due to the use of those RHB funds for current retiree health premiums. The Congressional Budget Office (CBO) estimated that enacting the House legislation would have a net cost to the federal budget of $2.5 billion over fiscal years 2010 through 2019.[19] The Senate legislation (S. 1507) would have extended and revised prefunding payments to the RHB Fund, with the payment amounts increasing from $1.7 billion in fiscal years 2009 and 2010 to $5.3 billion in fiscal year 2019. CBO estimated that enacting S. 1507 would have a net cost to the federal budget of $2.8 billion over both fiscal years 2010 through 2019 and fiscal years 2009 through 2014.[20] Ultimately, Congress acted at the end of September 2009 to reduce costs by deferring USPS's prefunding payment for retiree health benefits in fiscal year 2009 by $4 billion.[21]

We strongly support the principle that USPS should continue to fund its retiree health benefit obligations to the maximum extent that its finances permit. Deferrals of funding such benefits would serve as financial relief. Such deferrals, however, increase the risk that in the future USPS will not be able to pay these obligations as its core business continues to decline and if sufficient actions are not taken to restructure operations and reduce costs. With these considerations, the current statutory approach for

[18]H.R. 22, 111th Cong. (2009); S. 1507, 111th Cong. (2009).

[19]Congressional Budget Office, *H.R. 22: United States Postal Service Financial Relief Act of 2009* (Washington, D.C.: July 20, 2009).

[20]Congressional Budget Office, *S. 1507: Postal Service Retiree Health Benefits Funding Reform Act of 2009* (Washington, D.C.: Sept. 14, 2009).

[21]H.R. 2918, 111th Cong. (2009), enacted as Pub. L. No. 111-68 (2009).

funding USPS's retiree health benefit obligations can be revised along the lines of the two broad approaches to funding retiree health obligations—pay-as-you-go and actuarial. The approaches vary in the amount of annual payments, which, in turn, impact the unfunded obligation, lower annual payments, and result in higher unfunded obligation balances. For comparison purposes, we present the estimated unfunded balance for USPS's retiree health obligations in fiscal year 2020. These approaches to revising the current statutory approach are presented in the following text to illustrate the wide range of possible options.

Approach #1: Pay-as-you-go approach to funding retiree health benefit obligations

In March 2010, USPS proposed "to shift to a 'pay-as-you-go' system [for its retiree health benefits], paying premiums as they are billed" for current retirees. Estimated annual USPS payments under one possible pay-as-you-go approach are shown in table 5. Under this approach, USPS would make payments to the FEHB Fund for its share of retiree health premiums. The RHB Fund would not make or receive payments, but would continue to earn interest. Based on GAO analysis, USPS's unfunded obligations would be an estimated $99 billion in fiscal year 2020, or about $66 billion more than they would be under current law. This level of unfunded obligations would increase the risk that, absent future events that could reduce USPS's retiree health premiums, USPS's operations in the future may not be able to support the future payments that are expected. However, in such a circumstance, a mechanism could be created to pay a portion of premium payments from the assets that have accumulated in the RHB Fund once a threshold was reached, such as when the pay-as-you-go premium payments reach a particular percentage of postal revenues. Using the RHB Fund to pay a portion of retiree health premiums would reduce USPS's payments to the FEHB Fund and increase USPS's unfunded obligations by a corresponding amount. Such a mechanism could, if implemented carefully, provide some assistance to USPS in meeting its obligation to pay retiree health premiums.

Table 5: A Pay-as-You-Go Approach for Revising USPS Retiree Health Benefit Payments, Fiscal Years 2010 through 2020

Dollars in billions

Fiscal year	USPS payments to RHB Fund	USPS payments to FEHB Fund	Total USPS payments	Payments from RHB Fund to FEHB Fund	Difference between total USPS payments under this option and current law[a]
2010	$0.0	$2.3	**$2.3**	$0.0	$(5.5)
2011	0.0	2.6	**2.6**	0.0	(5.5)
2012	0.0	2.9	**2.9**	0.0	(5.6)
2013	0.0	3.3	**3.3**	0.0	(5.6)
2014	0.0	3.6	**3.6**	0.0	(5.7)
2015	0.0	4.0	**4.0**	0.0	(5.7)
2016	0.0	4.5	**4.5**	0.0	(5.8)
2017	0.0	4.9	**4.9**	0.0	(1.5)
2018	0.0	5.4	**5.4**	0.0	(1.3)
2019	0.0	5.8	**5.8**	0.0	(1.2)
2020	0.0	6.4	**6.4**	0.0	(0.9)
Total	**$0.0**	**$45.7**	**$45.7**	**$0.0**	**$(44.3)**

Source: OPM analysis prepared at GAO's request.

Note: Estimates are based on OPM assumptions that factor in updated USPS workforce size projections, annual inflation in health care costs of 8 percent in fiscal year 2010 that then declines slowly, a general inflation rate of 3.5 percent annually, and RHB Fund interest of 6.25 percent annually.

[a]GAO compiled the data shown in this column. Also, see table 4 for USPS payments under current law.

Different variations on a "pay-as-you-go" approach are also possible, such as using the RHB Fund to pay USPS's share of retiree health premiums for current retirees until the RHB Fund is exhausted and then reverting to USPS funding future premiums from its operations by paying the FEHB Fund directly. Under this alternative, USPS's payments would be suspended until the RHB Fund is exhausted, which would be approximately fiscal year 2025.

Approach #2: Actuarial approach to funding retiree health benefit obligations

An actuarial funding approach for USPS retiree health benefit obligations could provide a financing mechanism that allows the RHB Fund to remain self-sustaining in the long term. Under one such approach, unfunded retiree health benefit obligations would be reamortized starting in fiscal year 2010, instead of fiscal year 2017, as required under current law.

Specifically, starting in fiscal year 2010, USPS would make payments to the RHB Fund that finance the following:

- the annual accrued cost of future benefits attributable to the service of current USPS employees, which OPM refers to as "normal costs," and
- amortization payments over 40 years to liquidate any unfunded obligations.

Under this actuarial funding approach, USPS would make annual estimated payments that total about $80 billion from fiscal years 2010 through 2020 (see table 6). Based on GAO analysis, in fiscal year 2020, the estimated unfunded obligations under this method would be about $48 billion, or about $15 billion more than they would be under current law.

Table 6: Actuarial Funding Alternative for USPS Retiree Health Benefit Payments, Fiscal Years 2010 through 2020

Dollars in billions

Fiscal year	USPS payments to RHB Fund[a]	USPS payments to FEHB Fund	Total USPS payments	Payments from RHB Fund to FEHB Fund	Difference between total USPS payments under this option and current law[b]
2010	$6.3	$0.0	**$6.3**	$2.3	$(1.5)
2011	6.4	0.0	**6.4**	2.6	(1.7)
2012	6.5	0.0	**6.5**	2.9	(2.0)
2013	6.8	0.0	**6.8**	3.3	(2.1)
2014	7.0	0.0	**7.0**	3.6	(2.3)
2015	7.2	0.0	**7.2**	4.0	(2.5)
2016	7.5	0.0	**7.5**	4.5	(2.8)
2017	7.7	0.0	**7.7**	4.9	1.3
2018	8.0	0.0	**8.0**	5.4	1.3
2019	8.3	0.0	**8.3**	5.8	1.3
2020	8.6	0.0	**8.6**	6.4	1.3
Total	**$80.3**	**$0.0**	**$80.3**	**$45.7**	**$(9.7)**

Source: OPM analysis done at GAO's request.

Note: Estimates are based on OPM assumptions that factor in updated USPS workforce size projections, annual inflation in health care costs of 8 percent in fiscal year 2010 that then declines slowly, a general inflation rate of 3.5 percent annually, and RHB Fund interest of 6.25 percent annually.

[a]Starting in fiscal year 2010, USPS payments include (1) amounts for "normal costs" (i.e., future retiree health benefits costs attributed to the service of current USPS employees) and (2) amortization amounts to liquidate any unfunded obligations over a 40-year period.

[b]GAO compiled the data shown in this column. Also, see table 4 for USPS payments under current law.

PAEA's funding requirements represent a significant financial commitment for USPS, especially in light of the current economic environment and the major challenges it faces. As we have testified, we continue to be concerned about those options that would greatly reduce payments in the short term, only to defer payments into the future.[22] Specifically, we are concerned that deferring these payments or some portion into the future increases the risk that USPS may have difficulty in making the future payments, particularly if mail volumes continue to decline. Because its retirees are eligible to receive the same health benefits as other federal retirees, if USPS cannot make its required payments, the U.S. Treasury, and hence the taxpayer, would still have to meet the federal government's obligations.

Pension Benefits

USPS employees participate in the federal government's two civilian pension plans—the Civil Service Retirement System (CSRS) and the Federal Employees' Retirement System (FERS)—that are administered by OPM. As of the end of fiscal year 2009, approximately 80 percent of USPS's employees were enrolled in FERS, while 20 percent were enrolled in CSRS or the Dual Civil Service Retirement System and Social Security (Dual CSRS).[23] As an agency employer, USPS is required by law to make certain payments to the Civil Service Retirement and Disability Fund (CSRDF) to fund its share of CSRS and FERS pension costs. In addition to providing an annuity at retirement based on years of service and "high-3" average pay, FERS also consists of Social Security and the government's Thrift Savings Plan (TSP). As such, USPS contributes the employer's share of Social Security taxes and the required contributions to its employees' TSP accounts.

Because USPS's pension, Social Security, and TSP contributions are in part a function of employee wages as defined for these programs, changes in total employee wages will have a corresponding effect on USPS's costs for these items. USPS's retirement expenses were $5.9 billion in fiscal year 2009. As we have previously mentioned, most USPS employees are full

[22]GAO, *U.S. Postal Service: Deteriorating Postal Finances Require Aggressive Actions to Reduce Costs*, GAO-09-332T (Washington, D.C.: Jan. 28, 2009).

[23]Employees with prior U.S. government service who were hired between January 1, 1984, and January 1, 1987, are covered by Dual CSRS. Less than 1 percent of USPS employees are covered by this plan.

time, can receive overtime pay, and receive pay increases and cost-of-living adjustments as set forth in collective bargaining agreements with various unions. Other USPS employees, typically managers and postmasters, are compensated under pay-for-performance programs. USPS's ability to reduce the size of its workforce and the number of workhours, the strategies and options for which are described elsewhere in this report, will affect the pension, Social Security, and TSP benefit costs it incurs for most of its employees.

Furthermore, the methods and rates at which USPS funds pension benefit costs are set forth in law. In 2002, OPM estimated that, under statutory pension funding requirements applicable to USPS at the time, USPS was on course to overfund its CSRS pension obligations.[24] Congress responded by enacting the Postal Civil Service Retirement System Funding Reform Act of 2003,[25] which changed the prior method of estimating and funding the USPS CSRS pension obligations. The act required USPS to contribute the employer's share of "dynamic normal cost" to the CSRDF, plus an amount to liquidate any underfunding, or "postal supplemental liability," both as determined by OPM.[26] In July 2003, OPM submitted to Congress its plan enumerating the actuarial methods and assumptions by which OPM would make its determinations. In 2004, OPM and the Board of Actuaries for the CSRDF reconsidered OPM's methodology at the request of USPS and concluded that OPM's methodology was in accordance with

[24]USPS contributed 7 percent of its CSRS employees' basic pay to the CSRDF when the Postal Reorganization Act was enacted in 1970. Subsequently, Congress periodically enacted legislation that required USPS to make additional CSRS contributions, primarily for the effect of increases in pension liabilities resulting from increases in employee pay and annuitant cost-of-living adjustments. See GAO, *Review of the Office of Personnel Management's Analysis of the United States Postal Service's Funding of Civil Service Retirement System Costs*, GAO-03-448R (Washington, D.C.: Jan. 31, 2003), appendix II, for a listing and description of key legislation affecting USPS's funding of CSRS costs.

[25]Pub. L. No. 108-18, 117 Stat. 624 (Apr. 23, 2003). See S. Rep. No. 108-35, at 2 (2003).

[26]Postal supplemental liability is the estimated difference of the actuarial present value of retirement obligations for USPS employees less the sum of several items, including the present value of future employer normal cost contributions and employee contributions to the CSRDF; the portion of the CSRDF balance attributable to payments to the CSRDF; and any other appropriate amount determined by OPM under generally accepted actuarial practices and principles. The current requirement is codified, as amended, at 5 U.S.C. § 8348(h). In determining USPS's CSRS contributions, Congress required the use of "dynamic assumptions," which are defined as economic assumptions that are used in determining actuarial costs and liabilities of a retirement system and in anticipating the effects of long-term future investment yields; increases in rates of basic pay; and rates of price inflation.

congressional intent. OPM also rejected an alternative methodology offered by USPS.

In January 2010, the USPS OIG issued a report on funding the USPS's CSRS pension responsibility.[27] This report asserted that, despite the changes brought about in the 2003 Act, the current method of allocating the pension costs for post-1971 pay increases results in the inequitable allocation of pension obligations to USPS. The USPS OIG proposed an alternative allocation methodology that its actuaries estimated would, if implemented, change the funded status of USPS's CSRS pension obligations from a current $10 billion underfunding to a $65 billion overfunding. This alternative allocation methodology is the same methodology that OPM rejected in 2004. Application of the USPS OIG's proposed methodology would result in a shift of pension funding costs from USPS to the U.S. Treasury.

Other Benefits

- *Health and life insurance:* Health insurance premiums for current employees comprise a growing share of USPS expenses, rising from $2.2 billion (3.5 percent of total expenses) in fiscal year 2000 to $5.3 billion (7.4 percent) in fiscal year 2009. Collective bargaining agreements require USPS to pay a more generous share of employees' health and life insurance premiums than most other agencies. For example, USPS paid, on average, 81 percent of health benefit premiums in fiscal year 2009 compared with 72 percent by other federal agencies. It also paid 100 percent of employee life insurance premiums, while other federal agencies pay about 33 percent. One option would be to increase employee premium payments for health and life insurance premiums. USPS's share of the health and life insurance premium payments could be reduced to levels paid by most federal agencies, which would increase the employees' annual premium payments and, according to USPS estimates, would have saved about $615 million in fiscal year 2009.
- *Workers' compensation:* The 2003 President's Commission recommended making USPS's workers' compensation program more comparable to programs in the private sector to control costs, still provide adequate benefits, and address USPS's unfunded liability in this area. The commission recommended that USPS be allowed to (1) transition

[27]United States Postal Service, Office of Inspector General, *The Postal Service's Share of CSRS Pension Responsibility*, RARC-WP-10-001 (Arlington, Va.: Jan. 20, 2010).

employees receiving workers' compensation to its pension plan on the basis of when the employee (if not injured) would be retirement eligible and (2) limit benefits from the current 75 percent for employees with dependents to two-thirds of the maximum weekly rate—the rate that applies to employees without dependents.

Postal Workforce Mix and Work Rules

Limitations on the workforce mix of full-time and part-time postal employees and workforce flexibility rules contained in contracts with USPS's unions are key determinants of how postal work is organized and, thus, of its cost. USPS officials told us that as mail volume declines, it would be more efficient to have a much higher proportion of part-time workers than is currently allowed under the existing agreements. These part-time employees would have flexible schedules and responsibilities and lower pay than full-time career employees. A key issue is how USPS can obtain greater flexibility through the collective bargaining process so that it can adjust its workforce more quickly to adapt to changing volume and revenue. Some options for postal workforce mix and work rules include the following:

- *Part-time workers:* Increase the percentage of part-time employees, who could work more flexible schedules, including less than an 8-hour shift. Such flexibility could help match USPS's workforce to the changing workload, which varies greatly depending on the day of the week and the time of the year.
- *Job Flexibility:* Increase the flexibility to use employees in different assignments. Changes in the skill requirements of some jobs and the needs of operations have made it more feasible and necessary for employees to be trained in different tasks and work in different areas, depending on daily needs. Under current collective bargaining agreements, USPS can assign employees to "cross crafts" and perform different duties, but the agreements require managers to consider wage level, knowledge, and experience before asking employees to perform duties outside of their normal purview.

Options for Reducing Operational and Network Costs and Improving Efficiency

Another area where USPS can reduce operational costs is by optimizing its mail processing, retail, and delivery networks; eliminating growing excess capacity and maintenance backlogs; and improving efficiency. Declines in mail volume and continuing automation have increased costly excess capacity that was a problem even when mail volume peaked in fiscal year 2006. USPS no longer needs—and can no longer afford—to maintain all of its retail and mail processing facilities. For example, USPS has reported that it has 50 percent excess plant capacity in its First-Class Mail processing operations.

Although USPS has begun efforts to realign and consolidate some mail processing, retail, and delivery operations, additional efforts are urgently needed to overcome obstacles. USPS has faced formidable resistance to facility closures and consolidations because of concerns about how these actions might affect jobs, service, employees, and communities, particularly in small towns or rural areas. According to some Members of Congress and postmaster organizations, among others, post offices are fundamental to the identity of small towns, providing them with an economic and social anchor. Another issue is that inadequate USPS financial resources could impede efforts to optimize postal mail processing, retail, and delivery networks by limiting available funding for transition costs.

Reducing operational and network costs would require navigating statutory requirements, regulations, procedures, and service standards, including the following:

- USPS is required by law to provide adequate, prompt, reliable, and efficient services to all communities, including a maximum degree of effective and regular services in rural areas, communities, and small towns where post offices are not self-sustaining.[28] USPS is specifically prohibited from closing small post offices "solely for operating at a deficit."[29] Statutory requirements also specify the process and criteria for post office closings, including appellate review by PRC.[30] Also, USPS regulations prescribe processes for closing, consolidating, and relocating post offices.
- PAEA requires USPS to develop and use procedures for providing public notice and input before closing or consolidating any mail processing or logistics facilities.[31]
- Appropriations provisions restrict post office closures[32] and mandate 6-day delivery.[33]

[28]39 U.S.C. § 101.

[29]39 U.S.C. § 101(b).

[30]39 U.S.C. § 404(d).

[31]Pub. L. No. 109-435, § 302(c)(5).

- Service standards drive operations at mail processing facilities. In this regard, PAEA requires USPS to establish and maintain modern delivery standards.[34] USPS standards currently call for delivery of most local First-Class Mail overnight and most long-distance First-Class Mail in 2 to 3 days.
- A PRC hearing and advisory opinion are required when USPS submits a proposal to make changes that would generally affect service on a nationwide or substantially nationwide basis.[35]

Mail Processing Operations

In 2006, PAEA encouraged USPS to expeditiously move forward in its streamlining efforts, recognizing that USPS has more processing facilities than it needs.[36] USPS has begun efforts to consolidate some mail processing operations, but much more needs to be done. Since 2005, USPS has closed only 2 of its 270 processing and distribution centers. Over this period, it also has closed some facilities, such as 68 Airport Mail Centers and 12 Remote Encoding Centers.[37] Between fiscal years 2005 and 2009, the Area Mail Processing (AMP) process has been used to implement 13 consolidations, saving a projected $31 million, but 39 under consideration were canceled, according to a recent USPS OIG report.[38] This report also noted that another 16 AMP consolidations have been approved, while 30 remained under consideration.

When determining whether to close a particular mail processing facility, key factors include the role of the facility in providing secure and timely delivery in accordance with its service standards as well as the expected cost reductions or productivity gains. Furthermore, we have reported that the process for governing such decisions should be clearly defined and

[32]For example, see Consolidated Appropriations Act, 2010, Pub. L. No. 111-117, div. C, title V, 123 Stat. 3034, 3200 (Dec. 10, 2009), which provides "that none of the funds provided in this Act shall be used to consolidate or close small rural and other small post offices in fiscal year 2010."

[33]For example, see Pub. L. No. 111-117, which provides that "6-day delivery and rural delivery of mail shall continue at not less than the 1983 level."

[34]Pub. L. No. 109-435, § 301.

[35]39 U.S.C. § 3661.

[36]Pub. L. No. 109-435, § 302.

[37]Remote Encoding Centers were established as a temporary solution to automate the processing of mail with handwritten addresses that could not be read by sorting equipment.

[38]United States Postal Service, Office of Inspector General, *Audit Report – Status Report on the Postal Service's Network Rationalization Initiatives*, Report Number EN-AR-10-001 (Arlington, Va.: Jan. 7, 2010).

transparent, and include public notice and meaningful engagement with affected communities, mailers, and employees. In 2005, we recommended that USPS enhance transparency and strengthen accountability of realignment efforts to assure stakeholders that such efforts would be implemented fairly and achieve the desired results.[39] We have since testified that USPS took steps to address these recommendations and should be positioned for action.[40] Individual facility decisions are best made in the context of a comprehensive, integrated approach for optimizing the overall mail processing network. Key process issues in this area include how to better inform Congress and the public about the purpose and scope of USPS's optimization plans, address possible resistance to consolidating operations and closing facilities, and ensure that employees will be treated fairly.

Options in the mail processing area include the following:

- *Close major mail processing facilities:* The Postmaster General and other stakeholders have recently said that USPS could close many major mail processing facilities while maintaining current standards for timely delivery. Some stakeholders have estimated that roughly over one-half of these facilities are not needed.
- *Relax delivery standards to facilitate closures and consolidations:* USPS officials and experts have also noted that additional major processing facilities could be closed if delivery standards were relaxed. For example, one senior USPS official estimated that about 70 processing facilities could be eliminated if local First-Class Mail were to be delivered in 2 days instead of overnight.
- *Introduce a discount for destination-entry of First-Class Mail:*[41] Some mailers favor having USPS introduce a discount for entering First-Class

[39]GAO, *U.S. Postal Service: The Service's Strategy for Realigning Its Mail Processing Infrastructure Lacks Clarity, Criteria, and Accountability*, GAO-05-261 (Washington, D.C.: Apr. 8, 2005).

[40]GAO, *U.S. Postal Service: USPS Has Taken Steps to Strengthen Network Realignment Planning and Accountability and Improve Communication*, GAO-08-1022T (Washington, D.C.: July 24, 2008).

[41]PAEA defined "worksharing discounts" as reductions in postal rates that are provided to mailers for the presorting, prebarcoding, handling, or transportation of mail. Worksharing discounts are generally based on the costs that USPS is estimated to avoid as a result of mailer worksharing activities.

Mail at facilities that are generally closer to the mail's final destination. For mail sent to distant recipients, such destination entry would be expected to bypass some mail processing facilities and some USPS transportation. However, USPS officials told us that they did not believe that USPS could capture the potential cost savings from creating such a discount, because of existing excess capacity. If such a discount were to be applied to mail that is already locally entered—which comprises much First-Class Mail volume—that could reduce revenues with little corresponding cost savings.

Retail Operations

USPS's retail network has remained largely static, despite expanded use of retail alternatives and population shifts. USPS continues to provide service at about 36,500 post offices, branches, and stations and has not significantly downsized its retail operations in recent years. Furthermore, USPS has a maintenance backlog for its retail facilities.[42] USPS officials stated that maintenance has historically been underfunded, causing it to focus on "emergency" repairs at the expense of routine maintenance. USPS has limited its capital expenditures to help conserve cash, an action that may affect its ability to make progress on its maintenance backlog.

USPS recognizes the need to adjust its retail network to provide optimal service at the lowest possible cost and has expanded its use of alternatives to traditional post offices. In 2009, customers could also access postal services at more than 63,000 physical locations, such as purchasing stamps at drug stores and supermarkets. By fiscal year 2009, nearly 30 percent of retail transactions were conducted in locations other than USPS retail facilities. In addition, self-service options, such as Automated Postal Centers, are located in postal retail facilities. Opportunities to consolidate retail facilities are particularly evident in urban and suburban areas, where USPS retail locations are close to one another, customers have more options, and facilities are expensive to operate and maintain.

Some of the key issues in the retail area include whether USPS should retain its current retail network and find sources of revenue to support it other than through the sale of postal products, or whether it should eliminate unnecessary facilities, modernize its retail services, and partner with the private sector to provide services in other locations, such as shopping malls. Another issue is whether USPS should provide other

[42]GAO, *U.S. Postal Service Facilities: Improvements in Data Would Strengthen Maintenance and Alignment of Access to Retail Service*, GAO-08-41 (Washington, D.C.: Dec. 10, 2007).

governmental services in postal facilities and, if so, whether it would receive reimbursement.

Options in the retail area include the following:

- *Optimize USPS's retail facility network by expanding retail access and closing unneeded facilities:* In March 2010, USPS stated that it plans to expand customer access while reducing costs through new partnerships with retailers and other options, such as self-service kiosks. USPS explained that post offices are often less convenient for customers in terms of hours and accessibility, and cost two to three times more than alternatives. USPS also noted that it has more retail locations than McDonalds, Starbucks, Walgreens, and Walmart combined, but the average post office provides service to about 600 customers weekly—or about 1/10th in comparison to Walgreens. Additional postal retail locations could be located within drug stores, grocery stores, and other retail chain stores, such as those in shopping centers and local malls. These retail stores are often open 7 days a week, for longer hours than postal retail facilities. According to USPS officials, stores that could provide access to postal retail services pay their employees less than postal retail clerks who currently earn an average of over $40 per hour in compensation and benefits. USPS stated that it would reduce redundant retail facilities as customers continue to shift to alternatives, but noted that proposals to close facilities have led to protests and resistance. USPS called for Congress to eliminate the statutory prohibition on closing small post offices solely for operating at a loss,[43] and stated that changes would be needed to the regulatory review process for closing post offices. USPS also called for reduced constraints on the decision-making process for providing access to postal services. If USPS is not able to streamline its retail operations, it may need to make major reductions in the hours that post offices and retail facilities are open for window service.

- *Leverage the USPS retail network:* USPS could maintain current retail facilities and leverage this network by providing other nonpostal goods or services. Such activities might be performed by USPS or private-sector partners and other government agencies. For example, these partners and agencies could lease unused space in USPS facilities. Stakeholders suggested many options for diversifying into nonpostal retail areas, which could include selling nonpostal products at postal retail facilities and providing services for other federal, state, or local government agencies.

[43]39 U.S.C. § 101(b).

While this option may increase the use of USPS's retail network, it may raise costs if facility modifications are needed, such as measures to maintain mail security at a facility where other business partners are colocated. Also, some competitors may raise concerns about USPS's legal advantages. For example, according to a 2007 report to Congress by FTC,[44] USPS is exempt from state and local taxes and fees and some other state and local statutes and regulations.

Delivery Operations

USPS has opportunities to reduce delivery costs, which is its most costly operation. More than 320,000 carriers account for close to one-half of USPS salary and benefit expenses. Because USPS delivers 6 days per week to most of its 150 million addresses, regardless of mail volume, it is difficult to reduce delivery costs commensurate with declining mail volume. In fiscal year 2000, carriers delivered an average of about 5 pieces of mail per day to every address, which fell to about 4 pieces in fiscal year 2009—a decline of 22 percent. This trend is continuing as mail volume declines and the delivery network continues to expand. Over 900,000 delivery points were added in fiscal year 2009—increasing costs by over $190 million, according to an USPS estimate.

In addition to the number of delivery points, the efficiency and cost of delivery operations depend on a variety of other factors, including the type of carrier route or the location of the receptacle where mail is delivered. For example, most customers (about 87 percent)[45] receive their mail via one of the three different types of carrier routes identified in table 7. These routes are served by carriers under different compensation systems, which largely account for the differences in their costs.

Table 7: Cost and Percentage of Delivery Routes, by Type, Fiscal Year 2009

Type of carrier route	Average annual national cost per address	Percentage of routes
City delivery	$198	64%
Rural delivery	156	32
Contract delivery	108	3

Source: USPS.

Note: Percentages do not add to 100 percent due to rounding.

[44]Federal Trade Commission, *Accounting for Laws that Apply Differently to the United States Postal Service and its Private Competitors* (Washington, D.C.: December 2007).

[45]The remaining 13 percent of addresses (about 20 million of the total 150 million delivery points) are to Post Office boxes. Most of these deliveries are served by clerks, not carriers.

Cost differences also exist related to the location of the mail receptacle (see table 8).

Table 8: Cost and Percentage of Carrier Deliveries, by Mode, Fiscal Year 2009

Mode of delivery	Average annual national cost per address	Percentage of carrier deliveries
Door[a]	$353	29%
Curbline	224	41
Centralized[b]	161	16
Collection/Cluster box units[c]	158	13

Source: USPS.

Note: Percentages do not add to 100 percent due to rounding.

[a]These deliveries are primarily door deliveries and also include "other" deliveries that are not covered by other categories.

[b]Centralized delivery is defined as delivery and collection services to a number of businesses or residences from a centrally located delivery point or place, such as a group of mailboxes at an apartment building.

[c]This category includes cluster box units (which are centralized units of individually locked compartments for the delivery of mail) and Neighborhood Delivery Collection Box Units (which are centralized units of more than eight individually locked compartments that receive mail).

We have reported on USPS's ongoing efforts to increase the efficiency of mail delivery.[46] USPS has begun to install 100 machines for its $1.5 billion Flats Sequencing System to sort flat-sized mail into delivery order. USPS expects this system to eliminate costly manual sorting, thereby improving delivery efficiency, accuracy, consistency, and timeliness. USPS is also realigning city carrier routes to remove excess capacity, which is expected to generate more than $1 billion in annual savings. This effort is expected to result in reduced facility space needs, increased employee satisfaction, and more consistent delivery service. Route realignment has been made possible by collaboration between USPS and the National Association of Letter Carriers and is continuing this fiscal year. In addition, USPS may have additional opportunities to further increase delivery route efficiency, such as by promoting the use of more efficient delivery modes for new delivery points.

Options in the delivery area include the following:

[46]GAO, *U.S. Postal Service: Mail Delivery Efficiency Has Improved, but Additional Actions Needed to Achieve Further Gains*, GAO-09-696 (Washington, D.C.: July 15, 2009).

- *Decrease delivery frequency from 6 days a week to 5 days a week:* USPS favors eliminating Saturday delivery to provide substantial financial savings.[47] According to USPS studies, its savings would be primarily achieved by eliminating work performed by city and rural letter carriers. Additional savings would be realized from reducing the use of delivery vehicles as well as reducing the scope of mail processing activities that support Saturday delivery. However, concerns have been raised about the impact on customers, who may need to wait longer to receive time-sensitive mail or go to USPS retail facilities to pick up mail; senders, who may have to change when they send mail; and USPS, which may lose the competitive advantage of delivering on Saturdays. According to USPS, eliminating Saturday delivery is estimated to result in annual savings of about $3 billion. PRC reported in 2009 that eliminating Saturday delivery would result in estimated annual savings of about $2.2 billion, on the basis of somewhat different assumptions regarding the likely effects on mail volume and costs. For this option to be implemented, Congress would need to exclude statutory restrictions that mandate 6-day delivery from USPS annual appropriations. USPS filed a request on March 30, 2010, for a PRC advisory opinion on its proposal to eliminate Saturday delivery, which would lead to a public proceeding that would include input by interested parties.
- *Allow USPS to determine delivery frequency on the basis of local mail volume:* A related option would be to change delivery frequency to match mail volumes to demand, which could change by season as well as by local area. For example, USPS could have less frequent delivery in low-volume summer months than the high-volume holiday season. Some residents already do not receive 6-day delivery, particularly those located in remote or seasonal vacation areas. A consequence of this option could be more frequent delivery to areas with higher mail volume, which could be in higher-income areas, which tend to receive much more mail. However, low-income residents and others, such as the elderly and disabled, may rely more on mail delivery. This option may also be criticized as inconsistent with current statutory requirements. USPS is required by law to provide prompt, reliable, and efficient services to patrons in all areas.[48] It is also required by law to provide a maximum degree of effective and

[47] USPS officials indicated that USPS would continue providing window retail service and delivery to Post Office boxes on Saturday as well as remittance mail service for business mailers.

[48] 39 U.S.C. § 101(a).

regular postal services to rural areas, communities, and small towns where post offices are not self-sustaining.[49]

- *Expand the use of more cost-efficient modes of delivery for new addresses, including cluster boxes and curbline delivery:* USPS has recently estimated that this option could annually save around $2.5 billion by moving certain door deliveries to centralized deliveries. However, USPS officials told us that they and some mailers are concerned that this option would lead to residents picking up their mail less frequently, which could delay remittances and lower the value of advertising mail. It also would affect access to mail, particularly for customers who currently have mailboxes attached to their homes.

Streamline Field Structure

Further streamlining of USPS's field structure could help reduce facility and personnel costs. USPS has the authority to review the need for field administrative offices and streamline its field structure. For example, in fiscal year 2009, it closed 1 of its 9 area offices and 6 of its 80 district offices.

Options to Generate Revenues

USPS has many opportunities to generate additional net revenue, particularly from postal products and services; however, as it has noted, results from actions to generate revenue other than rate increases are likely to be limited compared with its expected losses. Aside from rate increases, USPS projects that it can increase profits by $2 billion by fiscal year 2020 through product and service initiatives. For example, according to USPS, it will work to increase direct mail use among small and medium-sized businesses and increase volumes in both First-Class Mail and advertising mail through targeted promotions. USPS also will continue to leverage its "last-mile" network to transport and deliver packages to their final destinations and work to grow other retail services, such as passport services provided by USPS and Post Office box rentals.

Key challenges in the area of revenue generation include the following:

- The short-term results will likely be limited by the economic climate as well as the ongoing diversion to electronic alternatives.

[49] 39 U.S.C. § 101(b).

- The potential for some actions will be limited because they will apply to mail or services that generate only a small fraction of revenues.

- USPS projects that its revenue will stagnate in the next decade despite further rate increases. Its revenue peaked at $75 billion in fiscal year 2007 but is projected to decline to $66 billion in fiscal year 2010, and to reach $69 billion in fiscal year 2020—growth that is below expected inflation.

Rate Increases for Market-Dominant and Competitive Products

Rate increases for market-dominant products, such as First-Class Mail and Standard Mail, would address pressing needs for revenue and could be used to better align rates and discounts with the costs, profitability, and price-sensitivity of mail. In the coming decade, rate increases for market-dominant products up to the price cap could raise significant revenues since these products currently generate 88 percent of revenue, while competitive products comprise nearly all other revenue.

Some key issues include the following:

- At what point are rate increases self-defeating, potentially triggering large, permanent declines in mail volume?

- How does USPS balance increasing rates to generate revenues with the impact on mailers and the long-term effects on volume, revenues, and the broader mailing industry?

- Would an "exigent" increase in postal rates over the price cap be justified, considering that it is limited by law to extraordinary or exceptional circumstances?

Some options include the following:

- *"Exigent" rate increases over the price cap:* USPS projects that its annual losses will increase greatly, even if rates for market-dominant products increase by the maximum allowed under the price cap. To improve its financial viability, USPS announced in March 2010 that it would seek "a moderate exigent price increase" for its market-dominant products that would be effective in 2011. An exigent rate increase over the price cap may produce a large short-term revenue boost. However, a very large rate increase could be self-defeating by increasing incentives for mailers to accelerate diversion to electronic alternatives, thereby lowering revenues in the long run and adding to USPS excess capacity. In 2009, USPS cited the potential impact on mail volume and the mailing industry when it ruled out an exigent rate increase for 2010—a year when the inflation-based price cap was zero—and announced that rates would not change for market-dominant products.

- *Rate increases for competitive products:* USPS annually increased rates in 2008, 2009, and 2010 for competitive products, including Priority Mail and Express Mail. Major USPS competitors, such as United Parcel Service (UPS) and FedEx, also have a history of annual rate increases.

Volume-Based Incentives for Specific Types of Market-Dominant Mail

USPS plans to pursue more volume-based rate incentives to stimulate additional mail use and take advantage of its excess capacity. For example, USPS reported that volume-based incentives can stimulate more advertising mail sent for sales, customer acquisition, and customer retention purposes, which should lead to greater mail use in the future. The additional mail volume can take advantage of USPS's large excess operational capacity. However, results to date suggest that such incentives can increase net income, but they appear to have limited potential compared with USPS losses. For example, a 2009 "summer sale" for Standard Mail that offered lower rates for volumes over mailer-specific thresholds reportedly had little effect on USPS's overall financial results for the fiscal year. USPS has estimated that about 38 percent of the volume qualifying for reduced "summer sale" rates would have been sent in the absence of the incentive, which reduced the profitability of this initiative. USPS plans to implement a similar initiative for summer 2010.

Some mailers have said that USPS should enter into more negotiated service agreements (NSA) with individual business mailers of market-dominant products. NSAs generally specify mutual agreements between USPS and mailers involving the preparation, presentation, acceptance, processing, transportation, and delivery of mailings under particular rate, classification, and service conditions, and restrictions that go beyond those required of other mailers. USPS did not generate net income from its seven NSAs in fiscal years 2007 through 2009 combined. These NSAs generally offered mailers lower rates for volumes that exceeded thresholds and had provisions to reduce some USPS costs, such as not returning undeliverable advertising mail and using electronic communications to provide this information to mailers. In comparison, USPS has negotiated about 100 contracts with business mailers of competitive products. Like NSAs for market-dominant products, contracts for competitive products are generally volume-based. These contracts also have provisions intended to lower USPS's mail-handling costs. PRC has reported that the contracts it approved in fiscal years 2008 and 2009 are expected to improve USPS's net revenue.

In December 2009, USPS officials told us that after PAEA was enacted, USPS preferred to pursue the volume-based incentive programs for market-dominant products that we have previously described, instead of pursuing NSAs. In theory, NSAs can increase net income by incentives tailored to each mailer's business needs, mailing practices, and opportunities to reduce USPS costs. In practice, it may be costly and time-consuming to negotiate NSAs and have them reviewed by PRC. The potential profitability of NSAs has been scrutinized in the past and is listed in PAEA as a factor for PRC to consider, along with (1) issues of fair competition, such as the availability of NSAs to similarly situated mailers, and (2) whether NSAs would cause unreasonable harm to the marketplace. These issues relate to the broader issue of whether USPS should have additional pricing flexibility and less PRC review of rates for its market-dominant products. USPS has suggested that regulatory and legal restrictions in this area need to be removed to provide greater flexibility, explaining that NSAs provide mailers with the opportunity to increase volume at a reasonable price.

Develop New Postal Products and Product Enhancements

During 2009, USPS considered options for developing new postal products and product enhancements, such as (1) "hybrid" mail that could be created online and printed and sent close to its final destination, which might involve USPS partnerships with private companies, and (2) new, low-cost ways for handling consumer electronics and other items that are being returned for recycling or disposal. As an example of recent product enhancements, USPS introduced new flat-rate boxes for Priority Mail, which it reports has met customer needs and generated volume growth. Consistent with USPS's stated strategy of providing greater value to its customers, some stakeholders told us that USPS should better understand and meet the needs and revenue growth opportunities of diverse mailers, in part through greater customer focus and improving the value of mail.

Increase Focus on Volume Growth in the Growing but Competitive Parcel Delivery Market

Competitive products are a promising growth opportunity for USPS, especially packages mailed by businesses to consumers. USPS forecasts that the volume of competitive products will increase 40 percent over the next decade. However, this volume growth is expected to have limited impact on losses, in part because competitive products generate only 12 percent of revenues. USPS is working to increase revenues from competitive products by increasing its market share in the growing package delivery market as well as by delivering more packages of competitors, such as "last-mile" delivery of packages that UPS or FedEx transport close to the destination and provide to USPS for final delivery. A key issue is what the net return would be if USPS pursues a growth strategy requiring costly additional investment to upgrade its automation and tracking capabilities in an area with formidable competitors.

Simplify Complex Rules for Mail Preparation and Entry

USPS may have opportunities to increase volume by reducing mailers' costs to prepare and enter mail as well as allowing more creative mail use for advertising and communications. However, this option could also risk additional costs to handle mail and provide assurance that discounted mail meets the necessary requirements. Some mailer groups and mailers have criticized USPS requirements that they consider to be impediments to volume and revenue growth. These stakeholders said that these requirements are costly for mailers but only yield marginal benefits for USPS, delay delivery, limit the effectiveness of mail, or are enforced in an overly stringent manner. USPS counters that (1) these requirements are needed to limit its handling costs and ensure that discounted mail meets the necessary requirements and (2) there are limited opportunities for it to increase revenues by simplifying its requirements. Some parties have said that USPS should strike a balance between requirements necessary for its operations and the need to provide mailers with flexible, low-cost methods to prepare and submit mail. USPS and mailers have long engaged in collaborative efforts to help define appropriate requirements. Redoubling efforts in this area could produce important benefits for USPS and the mailing industry.

New Nonpostal Products and Services

In 2009, USPS asked Congress to change the law so that it can diversify into nonpostal areas to find new opportunities for revenue growth, and some stakeholders have also supported diversification. USPS and stakeholders we collected information from offered many options for diversification into nonpostal areas, either on its own or in partnership with other private firms or government agencies. New nonpostal products and services that were identified include providing banking, financial, and insurance services; selling nonpostal products at its retail facilities; providing services for other federal, state, or local government agencies; carriers delivering nonpostal items or providing contract services (such as meter reading); advertising at USPS facilities; and providing electronic commerce. Diversification could involve entering new areas or earning revenues from business partners who sell nonpostal products at USPS retail facilities.

Whether USPS should be allowed to engage in nonpostal activities should be carefully considered, including its poor past performance in this area, as should the risks and fair competition issues. We have previously reported the following:

- USPS lost nearly $85 million in fiscal years 1995, 1996, and 1997 on 19 new products, including electronic commerce services, electronic money transfers, and a remittance processing business, among others.[50]

- In 2001, we reported that none of USPS's electronic commerce initiatives were profitable, and that USPS's management of these initiatives—such as an electronic bill payment service that was eventually discontinued—was fragmented, with inconsistent implementation and incomplete financial information.[51]

In enacting PAEA, Congress restricted USPS from engaging in new nonpostal activities. PAEA also required PRC to review USPS's existing nonpostal services to determine whether they should be continued or terminated. PRC recently found the intent of this requirement was to concentrate USPS's focus on its core responsibilities and away from nonpostal services that are not justified by a public need that cannot be met by the private sector. Allowing USPS to diversify into nonpostal activities would raise a number of issues, including whether it should engage in nonpostal areas where there are private-sector providers and, if so, under what terms. Other issues relate to concerns about unfair competition; whether USPS's mission and role as a government entity with a monopoly should be changed; as well as questions regarding how it would finance its nonpostal activities, what transparency and accountability provisions would apply; whether USPS would be subject to the same regulatory entities and regulations as its competitors; and whether any losses might be borne by postal ratepayers or the taxpayer.

USPS reported in March 2010 that even if it could enter nonpostal areas, such as banking or selling consumer goods, its opportunities would be limited by its high operating costs and the relatively light customer traffic of post offices compared with commercial retailers. USPS also stated that the possibility of building a sizable presence in logistics, banking, integrated marketing, and document management is currently not viable because of its net losses, high wage and benefit costs, and limited access to cash to support necessary investment. USPS concluded in its *Action*

[50]GAO, *U.S. Postal Service: Development and Inventory of New Products*, GAO/GGD-99-15 (Washington, D.C.: Nov. 24, 1998).

[51]GAO, *U.S. Postal Service: Update on E-Commerce Activities and Privacy Protections*, GAO-02-79 (Washington, D.C.: Dec. 21, 2001). Also see GAO, *U.S. Postal Service: Postal Activities and Laws Related to Electronic Commerce*, GAO/GGD-00-188 (Washington, D.C.: Sept. 7, 2000).

Plan that building a sizable business in any of these areas would require "time, resources, new capabilities (often with the support of acquisitions or partnerships) and profound alterations to the postal business model."

Options to Reform USPS's Statutory and Regulatory Framework

Addressing challenges to USPS's current business model may require restructuring its statutory and regulatory framework to reflect business and consumers changing use of the mail. While we do not address whether USPS's ownership structure should be modified in this report, many other statutory and regulatory considerations that should help to address the changing use of mail have been discussed and relate to the following elements of USPS's business model:

- *Mission:* What is an appropriate universal service obligation in light of fundamental changes in the use of mail?
- *Role:* Should USPS be solely responsible for providing universal postal service, or should that responsibility be shared with the private sector?
- *Monopoly:* Does USPS need a monopoly over delivery of certain types of letter mail and access to mail boxes to finance—in part or wholly—universal postal service?
- *Governance and regulation:* What is an appropriate balance between managerial flexibility and the oversight and accountability provided by the current governance and the regulatory structure?

USPS's Mission

USPS's statutory mission is to provide postal services to "bind the nation together through the personal, educational, literary, and business correspondence of the people."[52] It is required by law to provide prompt, reliable, and efficient services to patrons in all areas and postal services to all communities. These and related requirements are commonly referred to as the universal service obligation. PRC has reported that universal postal service has seven principal attributes (see table 9).

[52] 39 U.S.C. § 101(a).

Table 9: Attributes of the Universal Postal Service Obligation

Attribute	Description
Geographic scope	USPS is required to provide universal postal service throughout the nation and to and from foreign countries, subject to reasonable economic and efficiency limitations.
Range of products	The range of postal products included in the universal service obligation can change to meet the public's changing needs.
Access to universal services	Access takes into account not only the time and distance needed to get to a location where postal services are available, but also the time spent waiting to obtain services. "Essential postal services" include postal products, mail acceptance points such as collection boxes, access to letter carriers who accept mail for posting, and easily accessible information. Although USPS has discretion to determine the nature and location of postal facilities, these determinations are subject to statutory limitations, such as those related to closing post offices.
Delivery of universal services	Since fiscal year 1984, annual appropriations language has mandated that 6-day delivery continue at not less than the 1983 level.[a] However, USPS has discretion over the method used to deliver mail, such as to mailboxes attached to houses, curbside mailboxes, and cluster boxes.
Prices/Affordability	Requirements include reduced rate or no charge for some mail; uniform rate for at least one class of mail (currently First-Class Mail); and PAEA pricing constraints that include a price cap for market-dominant products.
Quality of service	USPS is required to provide quality postal service, and service changes that are nationwide or substantially nationwide in scope are subject to public comment and a PRC advisory opinion and must meet service quality standards.
Enforcement mechanism	Interested persons may file complaints with PRC for USPS's failure to meet certain statutory provisions, such as ratemaking requirements. If PRC finds a complaint to be justified, PRC is required to order USPS to take the appropriate action to come into compliance.

Source: Postal Regulatory Commission, *Report on Universal Postal Service and the Postal Monopoly* (Washington, D.C.: Dec. 19, 2008).

[a]Consolidated Appropriations Act, 2010, Pub. L. No. 111-117, div. C, tit. V, 123 Stat. 3034, 3200 (Dec. 16, 2009).

Key questions regarding universal postal service include the following:

- How much postal service does the nation need and how should it be funded?
- Should the costs of providing universal service be borne by postal ratepayers, or should taxpayers subsidize some unprofitable aspects of universal service that benefit the nation?
- If USPS cannot be financially viable without reducing universal postal service, what changes would be needed?
- Who should determine whether changes should be made to universal service (e.g., Congress, USPS, or PRC)?

In addition, issues have been raised about whether all postal products should be required to cover their costs, even if they provide social benefits, or receive a subsidy through appropriations. Historically, some types of mail were designed to channel broad public goals, such as furthering the dissemination of information, the distribution of merchandise, and the advancement of nonprofit organizations. For example, Periodicals (mainly, mailed magazines and newspapers) have historically been given favorable rates, consistent with the view that they help bind the nation together, but this class has not covered its costs for the past 13 fiscal years. Losses from Periodicals increased from $74 million in fiscal year 1997 to $438 million in fiscal year 2008 and to $642 million in fiscal year 2009. These escalating losses have provoked growing concern and controversy. Postal stakeholders are currently debating what corrective actions, if any, are warranted, and their possible impact on Periodicals.

Other money-losing types of mail with social benefits include the following:

- Single-piece Parcel Post was introduced in 1913 to provide affordable parcel delivery; this opened up the mail order merchandise market, especially in rural areas.
- Media Mail, or "book rate," as it was formerly known, was initially designed in 1938 to provide lower rates for mailed books and encourage the mailing of educational materials.
- Library Mail was introduced in 1928 as a preferential rate for books sent by or to libraries and was later expanded to schools, colleges, and universities in 1953.

According to a Congressional Research Service report, when Congress put USPS on a self-sustaining basis in 1971, it continued to subsidize the mailing costs of such groups as the blind, nonprofit organizations, local newspapers, and publishers of educational material, by providing an appropriation to cover the revenues that were given up, or "forgone," in charging below-cost rates to these groups.[53] Appropriations for these subsidies mounted as postage rates and the number of nonprofits grew, approaching $1 billion annually in the mid-1980s. Successive

[53]Congressional Research Service, *The Postal Revenue Forgone Appropriation: Overview and Current Issues*, RS21025 (Washington, D.C.: updated Sept. 21, 2006).

administrations sought to cut these costs by reducing eligibility and having other mailers bear more of the burden. Questions continue about how these money-losing types of mail should be funded.

All money-losing market-dominant products lost $1.7 billion collectively in fiscal year 2009, up from $1.1 billion in fiscal year 2008 (see table 10). In addition to the $642 million lost from Periodicals in fiscal year 2009, the largest money-losing product was Standard Mail Flats ($616 million).[54] Losses from Standard Mail Flats have nearly tripled over the past fiscal year. In its Annual Compliance Determination report for fiscal year 2009, PRC discussed actions that could be taken to deal with these and other money-losing products. Some of the losses from Standard Mail are due to unprofitable mail sent by nonprofit organizations. By law, rates for nonprofit Standard Mail are 60 percent of the rates for the most closely corresponding type of for-profit Standard Mail.[55] However, nonprofit rates benefit charitable and religious organizations, and Congress has long required preferential rates for nonprofit mail.

Table 10: USPS Money-Losing Market-Dominant Products, Fiscal Years 2008 and 2009

Dollars in millions

	Net income (loss)		
Market-dominant product	**Fiscal year 2008**	**Fiscal year 2009**	**Change**
Periodicals	$(438)	$(642)	**$(204)**
Standard Mail Flats[a]	(218)	(616)	**(398)**
Standard Mail ("not flat machinables"[b] and parcels)	(165)	(205)	**(39)**
Inbound single-piece First-Class Mail	(102)	(105)	**(3)**
Media and Library Mail	(58)	(74)	**(16)**
Single-piece Parcel Post	(64)	(61)	**3**
Other[c]	(37)	(23)	**14**
Total	**$(1,082)**	**$(1,726)**	**$(644)**

Sources: USPS and PRC.

Note: All data are rounded to the nearest million, including totals and changes between fiscal years.

[54]The Standard Mail Flats product includes some, but not all, flat-sized Standard Mail. This product does not include saturation advertising mail.

[55]39 U.S.C. § 3626(a)(6).

[a]Standard Mail Flats includes some, but not all, flat-sized Standard Mail. For example, saturation advertising mail is not part of the Standard Mail Flats product.

[b]Standard Mail "not flat machinables" include items that cannot be sorted by USPS automation equipment, such as CD jewel cases and other rigid items.

[c]Other includes ancillary services for international mail, Registered Mail, and Stamped Cards (losses in both fiscal years) as well as Bound Printed Matter, inbound surface Parcel Post at Universal Postal Union rates, Confirm Service, and address list services (losses in fiscal year 2009 only).

If Congress were to decide that all market-dominant products should cover their costs, it could also revisit other legal requirements that constrain USPS's pricing flexibility for these products. First, the price cap requirement may need to be revisited to enable some types of mail to be increased over the cap without resorting to the exigent rate increase process. For example, the average rate increase for the Periodicals class is limited to inflation under the price cap. Similarly, single-piece Parcel Post, Media Mail, and Library Mail are a significant part of the Package Services class that is also covered by the price cap. In addition, USPS could continue to gradually implement a rate structure for Periodicals that is based more on costs, which could involve rate increases for mail that is more costly to handle (e.g., mail provided to USPS in sacks, rather than on pallets). However, such a rate structure could disproportionately affect some small-circulation magazines.

Issues regarding which entity should consider and decide on changes to universal service—including Congress, PRC, or USPS—have long been debated. Because many aspects of universal service are required by law, Congress would have to make any changes in these areas. For example, Congress would have to redefine certain aspects of universal postal service that are required under current law, such as 6-day delivery, revised statutory preferences for nonprofit mail, and restrictions on closing small post offices. For some aspects of universal service, such as related pricing issues, PRC has the authority to act by establishing regulations that govern postal pricing and overseeing USPS compliance with legal requirements. USPS has flexibility to act on some other aspects, such as establishing and maintaining service standards for timely mail delivery.

USPS's Role

Another issue is whether postal services are an inherently governmental function, and whether USPS should be the only entity responsible for universal postal service. The federal government's responsibility for postal services is detailed in Title 39 of the *United States Code*. A possible rationale for sharing this responsibility would be to allow private companies to provide postal services, with the idea that competition could give some customers more choices that better meet their needs, through lower cost products and expanded services. A related consideration is that some aspects of postal service, particularly mail delivery, are considered to have economies of scale, meaning that, in theory, one provider might fulfill this function more economically than multiple providers. In practice, multiple providers—including USPS and numerous companies—already deliver mail (e.g., contractors who provide long-distance mail transportation and deliver mail to households located along sparsely populated highway routes).

Another question is whether USPS should continue to fulfill other roles, or whether these roles should be discharged by other agencies. For example whether USPS or some other law enforcement body should enforce postal laws was considered in the postal reform debate—specifically, whether the Postal Inspection Service that enforces mail fraud and other statutes should be transferred to another federal law enforcement agency. Another example is USPS's involvement in responding to national disasters, including hurricanes and terrorist attacks. In this regard, a recent executive order stated that USPS has the capacity for rapid residential delivery of medical countermeasures across all U.S. communities, and that the federal government will use USPS to implement national medical countermeasures in the event of a large-scale biological attack.[56]

USPS Monopoly

USPS has two types of monopolies to (1) deliver certain letter mail and (2) have exclusive access to mailboxes.

The Mail Monopoly

USPS has a monopoly over the delivery of certain letter mail to help ensure that it has sufficient revenues to carry out public service mandates, including universal service.[57] USPS has promulgated regulations to identify exceptions to the postal monopoly.[58] Some key exceptions include "extremely urgent" letters (generally, next-day delivery) and outbound international letters. Most mail volume is covered by this monopoly,

[56]Exec. Order No. 13527, *Establishing Federal Capability for the Timely Provision of Medical Countermeasures Following a Biological Attack*, 75 Fed. Reg. 737 (Dec. 30, 2009).

[57]The basic restrictions on private delivery of letter mail are in seven sections of the federal criminal statutes (18 U.S.C. §§ 1693-1699) as well as additional provisions dealing with private delivery of letters (39 U.S.C. §§ 601-606). These laws generally prohibit anyone from establishing, operating, or using a private company to carry letters for compensation on regular trips or at stated periods over postal routes or between places where U.S. mail regularly is carried. Violators are subject to fines or, in some cases, imprisonment.

[58]See, for example, 39 C.F.R. § 320.6.

regulated as market-dominant mail, and subject to the price cap. Over the years, Congress has reevaluated the need for the mail monopoly, broadening and reducing it at various times, including in PAEA.[59]

For over 200 years, USPS and its predecessor, the former U.S. Post Office Department, operated with a statutory mail monopoly, which restricted the private delivery of most letters. Congress created the mail monopoly as a revenue protection measure to help enable the former Post Office Department to fulfill its mission. A rationale for the mail monopoly is to prevent private competitors from engaging in an activity known as cream-skimming, that is, offering service on low-cost routes at prices below those of USPS, while leaving USPS with high-cost routes. Furthermore, allowing private companies to compete for mail now covered by the monopoly could lead to additional declines in mail volume and revenue, thereby increasing excess capacity and reducing USPS's net income.

According to PRC, the most frequent argument against the mail monopoly is that, assuming a legal framework continues to exist to protect public interest and the provision of universal service, competitive markets might produce more efficient, innovative, flexible, and fairer services to buyers and producers. Narrowing or eliminating the monopoly could increase consumer choice and provide incentives for USPS to become more effective and efficient. Critics of the monopoly also cite the experience of foreign countries that have narrowed, eliminated, or are phasing out their monopolies.

The Mailbox Monopoly

This restriction prohibits anyone from knowingly and willingly placing mailable matter without postage into any mailbox.[60] As we have reported, the purposes of the restriction, which dates back to 1934, were twofold—to stop the loss of postal revenue resulting largely from private messengers delivering customer bills to mailboxes without paying postage and to decrease the quantity of extraneous matter being placed in mailboxes.[61] PAEA did not change the mailbox monopoly.

[59]Pub. L. No. 109-435, § 503.

[60]18 U.S.C. § 1725.

[61]GAO, *Postal Service Reform: Issues Relevant to Changing Restrictions on Private Letter Delivery*, GAO/GGD-96-129B (Washington, D.C.: Sept. 12, 1996).

USPS has stated that continuation of the mailbox monopoly would best preserve customer service, safety, security, and the value of mail. According to USPS, the mailbox monopoly helps deter mail theft and identity theft, facilitates enforcement when violations occur, and is needed for efficient mail collection and delivery. We have previously reported that critics of the mailbox monopoly said it impedes competition and infringes on private property.[62] FTC reported in 2007 that the mailbox monopoly reduces competition and raised competitors' costs of delivering products that otherwise could fit into a mailbox.[63] While FTC recognized mail security and privacy issues, it concluded that Congress and PRC may want to consider whether relaxing the mailbox monopoly to allow consumers to choose to have private carriers deliver competitive products to their mailboxes would create net benefits. In 2008, PRC stated that it "does not recommend any changes to the mailbox rule," citing issues with mail security and USPS efficiency. PRC also noted that its public proceeding evidenced broad support for continuing the mailbox monopoly.

Governance and Regulation

The effectiveness of USPS's governance and regulatory structure is critical to its success and to ensuring that quality affordable postal services are provided to the American people. The 2003 President's Commission noted that managerial accountability must come from the top, with USPS being governed by a strong corporate-style board that holds its officers accountable. The commission concluded that giving USPS greater flexibility would require enhanced oversight by an independent regulatory body endowed with broad authority, adequate resources, and clear direction to protect the public interest and ensure that USPS fulfills its duties. A number of regulatory changes were implemented after PAEA was enacted, and a thorough review of these changes has not been developed. PAEA required PRC to submit a report to Congress by December 2011 concerning "the operation of the amendments made by [PAEA]" and any recommendations for improvements to the U.S. postal laws. Another PRC report is required by December 2016 to determine whether the system for regulating rates and classes for market-dominant products is achieving its objectives.

[62]GAO, *U.S. Postal Service: Information About Restrictions on Mailbox Access*, GAO/GGD-97-85 (Washington, D.C.: May 30, 1997).

[63]*Accounting for Laws that Apply Differently*.

Governance

The Board of Governors directs the exercise of the powers of USPS, directs and controls its expenditures, reviews its practices, and conducts long-range planning. The board sets policy; participates in establishing postage rates; and takes up various matters, such as mail delivery standards and some capital investments and facilities projects. By law, governors are chosen to represent the public interest and cannot be "representatives of specific interests using the Postal Service."[64] Despite the changes made by PAEA, the qualifications of USPS governors continue to be an issue. Members of the Board of Governors told us that the board lacks sufficient business and financial expertise. The members also suggested that some governors should not be politically appointed. In this regard, the 2003 President's Commission recommended that the Board of Governors be comprised of 12 individuals: 3 presidential appointees, 8 independent members selected by the 3 appointees with the concurrence of the Secretary of the Treasury, and the Postmaster General (who would be selected by the other 11 members).[65]

Regulation

Should any of the operational or structural options outlined in this report be implemented, Congress, USPS, the Board of Governors, PRC, and other relevant postal stakeholders could consider whether governance and regulatory structures need to be changed to reflect an appropriate balance in the oversight roles of these entities. PAEA gave USPS more pricing and product flexibility, which was balanced by strengthening PRC's oversight authority. Among other things, PAEA required PRC to develop the regulatory structure for postal rates, consult with USPS on establishing delivery service standards, and annually determine USPS's compliance with applicable laws. Also under PAEA, PRC was granted the authority to issue subpoenas; direct USPS to adjust rates not in compliance with applicable postal laws; or, in cases of deliberate noncompliance with applicable postal laws, levy fines.

[64]39 U.S.C. § 202(a).

[65]Successors to the 8 independent members would be selected by the full board, with the concurrence of the Secretary of the Treasury.

Actions Congress and USPS Can Take to Facilitate Progress toward Financial Viability

Action by Congress and USPS is urgently needed on a number of difficult issues to facilitate progress toward USPS's financial viability by reducing costs, increasing efficiency, and generating revenues. The significant deterioration in USPS's financial condition over the past 2 years, its increasing debt, and the grim forecast for declining volume over the next decade led GAO to add USPS's financial condition to its high-risk list in July 2009. We suggested that USPS develop and implement a broad restructuring plan, with input from PRC and other stakeholders, to identify specific actions planned, key issues, and steps Congress and other stakeholders need to take. On March 2, 2010, USPS issued its *Action Plan*, which identified seven key areas wherein it would need legislative changes or support. Many of the options discussed are also options we have analyzed and included in this report for consideration. USPS forecasts of mail volume, revenue, and net income over the next decade quantify the magnitude of the challenges that it faces from continued volume decline to about 150 billion pieces in fiscal year 2020—about the same as the volume level in fiscal year 1986—and a projected cumulative $238 billion shortfall if no additional efficiency or revenue initiatives are undertaken. USPS's *Action Plan* indicates that actions within its control can close $123 billion of this financial gap, but that actions outside its existing authority—including some involving statutory changes—would be needed to eliminate the remaining financial gap. Action on these issues will likely take several years to fully implement once a decision is made on the scope of needed changes. Therefore, agreement on next steps is urgently needed.

If USPS is to continue being self-financing, Congress, USPS, and other stakeholders will need to reach agreement on major issues that impede its ability to implement actions to reduce losses. These issues include funding postal retiree health benefits; reexamining binding arbitration; realigning services, operations, networks, and workforce to reflect declining volume; and changing use of the mail in a dynamic marketplace as well as generating revenue.

- *Funding postal retiree health benefits:* USPS has said that it cannot afford its required prefunding payments on the basis of its significant volume and revenue declines, incurring large losses, nearing its debt limit, and limited cost-cutting opportunities under its current authority. Several proposals have been made to defer costs by revising the statutory requirements, and it is important that USPS fund its retiree health benefit obligations—including prefunding these obligations—to the maximum extent that its finances permit. In addition to considering what is affordable and a fair balance of payments between current and future ratepayers, Congress would also have to address the impact of these proposals on the federal budget. CBO has raised concerns about how aggressive cost-cutting measures would be if prefunding payments for retiree health care were reduced. This concern further indicates the need for broad agreement on specific realignment actions, the time frame for implementation, and the expected financial impact.

- *Binding arbitration:* One of the most difficult challenges USPS faces is making changes to its compensation systems, which will be critical to its financial condition since wages and benefits comprise 80 percent of its costs. In this regard, the time has come to reexamine the structure for collective bargaining that was developed 40 years ago. Since that time, the competitive environment has changed dramatically and rising personnel costs are contributing to escalating losses. Thus, it is imperative to ensure that USPS's financial condition be considered in upcoming collective bargaining if the process reaches binding arbitration.

- *Realigning postal services with changing use of the mail:* As mail use by businesses and consumers continues to change, USPS has stated that it cannot afford to provide the same level of services and that changes are needed. USPS has estimated that it could reduce costs by about $3 billion annually if it could reduce delivery frequency from 6 days to 5 days, but congressional agreement would be needed to not include a 6-day delivery requirement in USPS annual appropriations. USPS filed a request on March 30, 2010, for a PRC advisory opinion on its proposal to eliminate Saturday delivery.

- *Generating revenue through new or enhanced product and services:* On the revenue side, a key issue is whether USPS can make sufficient progress using the pricing and product flexibility provided in PAEA or whether changes may be needed. The *Action Plan* stated that USPS needs additional authority to adjust its pricing to better reflect market dynamics and proposed some changes. These proposals have not been fully analyzed, nor have PRC and stakeholders had an opportunity to provide input. Thus, it is unclear what statutory or regulatory changes should be made at this time. Another key issue is whether USPS should be allowed to engage in new nonpostal areas that may compete with private firms. Congress considered many of the public policy issues in this area related to fair competition prior to PAEA's enactment in 2006 and decided at that time not to let USPS engage in new nonpostal areas. It is not clear what specific actions USPS would like to take, their expected profitability, or how they might affect other businesses. USPS's current financial condition may limit its expansion into other areas in the short term, but ultimately its plans in this area could affect its operations.

- *Realigning operations, networks, and workforce:* Once Congress and USPS have determined what, if any, changes should be made in the products and services that it provides, corresponding changes will be needed in postal operations, networks, and workforce. This area involves some public policy issues that Congress may want to address. USPS will need to address detailed operational issues related to increasing cost-efficiency. Some of the difficult tradeoffs in this area include USPS's need to significantly reduce its size to remain self-financing and keep prices affordable, versus concerns about whether such reductions could harm the value of its brand, its network of physical assets, and the social benefits that it provides as well as the effects of these actions on its workforce.

USPS has made limited progress in optimizing its networks over the last decade, particularly in facilities that include public access to retail operations. For example, in July 2009, USPS initiated a PRC review of over 3,600 retail stations and branches located primarily in urban and suburban areas for possible consolidation or discontinuance, but fewer than 200 facilities remain under consideration for such actions. PRC issued its advisory opinion on USPS's proposed retail consolidations in early March, which affirmed USPS's authority to adjust its retail network while recommending several process improvements.[66] Considering the numerous statutory and regulatory requirements in this area, it could be difficult to make rapid changes to rightsize its network of 36,500 retail facilities. USPS's *Action Plan* says that it plans to expand access to retail service and, as customers shift to these new services, that it will reduce redundant retail facilities. However, it is unclear what specific changes would be made, how long it would take to make these changes, and how much annual cost savings could be achieved. USPS's *Action Plan* also does not address possible closures of large mail processing facilities to reduce the excess capacity in its mail processing network.

A new approach is urgently needed to make the necessary progress in realigning postal operations and networks as USPS's core business continues to decline. Conducting business as usual is unlikely to produce significant results, particularly in the rapid time frame that would be required to avert massive losses. Thus, it will be important for Congress, USPS, and other stakeholders to reach agreement on the package of

[66]Postal Regulatory Commission, *Advisory Opinion Concerning the Process for Evaluating Closing Stations and Branches*, Docket No. N2009-1 (Washington, D.C.: Mar. 10, 2010).

actions that should be taken, the desired operational and financial results, and the time frames for implementation. Key questions that need to be addressed include the following:

- *Universal service issues:* What, if any, changes are needed—that is, should delivery services be changed (e.g., frequency or standards), and should USPS continue moving retail services out of post offices to alternative locations?

- *New products and services:* What opportunities are there to introduce profitable new postal products and enhancements to existing ones? Should USPS engage in nonpostal areas where there are private-sector providers? If so, under what terms?

- *Realigning operations, networks, and workforce:* How should USPS optimize its operations, networks, and workforce to support changes in services; how quickly can this happen; and how can it work with its employees and customers to minimize potential disruption?

This is an area where Congress may want to consider an approach similar to that used by the Department of Defense's Base Realignment and Closure (BRAC) Commission, which was established to realign military installations within the United States. Under the Defense Base Closure and Realignment Act of 1990, the President can either accept or reject BRAC recommendations in their entirety.[67] If rejected, the BRAC Commission could give the President a revised list of recommendations. If the President accepts the list of recommendations, it is forwarded to Congress and the list becomes final, unless Congress enacts a joint resolution. Our report on the 2005 BRAC round noted that the Department of Defense viewed this BRAC as a unique opportunity to reshape its installations and realign its forces to meet its needs for the next 20 years.[68]

Congress has previously turned to panels of independent experts to assist in restructuring organizations that are facing key financial challenges. These panels have gained consensus and developed proposed legislative or other changes to address difficult public policy issues. For example, the District of Columbia Financial Responsibility and Management Assistance

[67]Pub. L. No. 101-510, § 2901, 104 Stat. 1485, 1808 (Nov. 5, 1990).

[68]GAO, *Military Base Realignments and Closures: Cost Estimates Have Increased and Are Likely to Continue to Evolve*, GAO-08-159 (Washington, D.C.: Dec. 11, 2007).

Authority was established to, among other things, (1) eliminate budget deficits and cash shortages of the District through financial planning, sound budgeting, accurate revenue forecasts, and careful spending; (2) ensure the most efficient and effective delivery of services, including public safety services, by the District during a period of fiscal emergency; and (3) conduct necessary investigations and studies. This organization was suspended in 2001 once relevant legal provisions were met, including achieving a balanced budget for a 4th consecutive year.

Establishing a similar commission or control board of independent experts could provide a mechanism to assist Congress in making timely decisions and comprehensive changes to USPS's business model and operations. A commission of experts may be more appropriate to facilitate the changes needed to achieve financial viability while also considering stakeholder interests. The following questions could assist Congress in developing such a commission:

- What criteria should be used to select commission members, for example, logistics experience, business restructuring, or labor management expertise?
- How could the commission best ensure that diverse stakeholder interests are appropriately considered?
- What would be the time frame of the commission?
- What goals or objectives should guide the commission—for example, ensuring USPS's financial viability, and recommending policy and management changes?

Conclusions

USPS faces daunting financial losses that it projects could total over $238 billion through fiscal year 2020, unless it can substantially reduce its costs, including the size of its operations, networks, and workforce to reflect declining mail volume, and to generate new revenues. USPS's planned actions under its existing authority will not be enough to make it financially viable. Therefore, Congress, USPS, and other stakeholders need to reach agreement on a package of actions to take so that USPS can become financially viable. This agreement will need to address difficult constraints and legal restrictions that continue to hamper progress. Such an agreement is urgently needed so that Congress and stakeholders have confidence that the actions USPS takes will be fair to all stakeholders. Then USPS could begin to plan and make the necessary changes, some of which may require several years to fully implement and realize potential cost savings. For example, restructuring operations and networks would require coordinated actions involving postal employees, mailers, and the public.

To reach agreement on these difficult issues, Congress could engage a panel of independent experts to develop a credible and comprehensive package of specific proposals, including the following:

- Potential changes related to adapting universal postal services to the declining use of mail, such as removing the statutory requirements for 6-day delivery and restrictions on closing post offices.
- Changes needed to realign USPS operations, networks, and workforce with its declining workload, and how to address employee and community concerns and resistance to facility closures.
- Improving opportunities to generate revenues, and whether that should include allowing USPS to engage in new nonpostal areas.

Due to the urgency of USPS's deteriorated financial condition and outlook, and the fact that it is rapidly approaching its statutory debt limit, Congress may need to provide financial relief, for example, by revising the funding schedule for retiree health benefits. Another action that Congress could take in the near term, which would have a longer-term impact, would be to modify the collective bargaining process to ensure that any binding arbitration would take USPS's financial condition into account. Furthermore, Congress may want assurance through regular reports that any financial relief it provides is met with aggressive actions to reduce costs and increase revenues, and that progress is being made toward addressing its financial problems.

Ultimately, Congress may want to consider changing USPS's ownership structure, but the resolution of these more pressing issues might afford a better understanding of whether the ownership structure should be modified. As communications and the use of the mail evolve, Congress will need to revisit policy issues related to USPS, the services it provides, and how to best position the organization for the future. The current crisis presents the opportunity to act and position this important American institution for the future. If no action is taken, the risk of USPS's insolvency and the need for a bailout by taxpayers and the U.S. Treasury increases.

Matters for Congressional Consideration

To address USPS's financial viability in the short term, Congress should consider providing financial relief to USPS, including modifying its retiree health benefit cost structure in a fiscally responsible manner. Congress should also consider any and all options available to reduce USPS costs, including revising the statutory framework for collective bargaining to ensure that binding arbitration takes its financial condition into account. At the same time, to facilitate making progress in difficult areas, Congress should consider establishing (1) a panel of independent experts, similar to a BRAC-like commission, to coordinate with USPS and stakeholders to develop a package of proposed legislative and operational changes needed to reduce costs and address challenges to USPS's business model and (2) procedures for the review and approval of these proposals by the President and Congress. These proposals could focus on adapting delivery and retail services to declining mail volumes; making postal operations, networks, and workforce more cost-efficient; and generating new revenue.

Congress also should consider requiring USPS to provide regular reports to Congress to ensure that USPS is making progress to improve its financial condition. These reports could include the actions taken to reduce costs and increase revenues, the results of these actions, and progress toward addressing financial problems.

Agency Comments and Our Evaluation

USPS provided written comments on a draft of this report by a letter dated April 2, 2010. These comments are summarized below and included in their entirety in appendix II of this report. In separate correspondence, USPS also provided technical comments, which we incorporated as appropriate.

USPS stated that it agreed with many key points in our report and with all but one of our matters for congressional consideration. First, regarding revising USPS retiree health benefit funding, USPS said the prefunding requirement urgently needs to be restructured and agreed that it should continue to fund its retiree health benefits obligation to the maximum extent that its finances permit. Second, USPS agreed that Congress should consider revising the statutory framework for USPS collective bargaining to ensure that binding arbitration takes its financial condition into account. Third, USPS agreed that Congress should consider requiring USPS to provide regular reports to ensure that it is making progress to improve its financial condition. However, USPS raised concerns about using a panel of independent experts to develop a package of proposed legislative and other changes, stating that doing so would add a layer of bureaucracy and delay to problems that require immediate attention. We believe that unless Congress and USPS agree on actions to be taken, USPS will not be able to reduce costs enough to close the revenue gap and achieve financial stability. Congress has used such panels to successfully reach agreement regarding other difficult restructuring issues.

We are sending copies of this report to the appropriate congressional committees, the Postmaster General, the Chairman of the USPS Board of Governors, the Chairman of the Postal Regulatory Commission, and other interested parties. In addition, the report will be available at no charge on GAO's Web site at http://www.gao.gov.

If you or your staffs have any questions regarding this report, please contact me at (202) 512-2834 or herrp@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report. GAO staff who made key contributions to this report are listed in appendix III.

Phillip R Herr

Phillip Herr
Director, Physical Infrastructure Issues

List of Committees

The Honorable Joseph I. Lieberman
Chairman
The Honorable Susan M. Collins
Ranking Member
Committee on Homeland Security and
Governmental Affairs
United States Senate

The Honorable Thomas R. Carper
Chairman
The Honorable John McCain
Ranking Member
Subcommittee on Federal Financial
Management, Government Information,
Federal Services, and International Security
Committee on Homeland Security and
Governmental Affairs
United States Senate

The Honorable Richard J. Durbin
Chairman
The Honorable Susan M. Collins
Ranking Member
Subcommittee on Financial Services and General
Government
Committee on Appropriations
United States Senate

The Honorable Edolphus Towns
Chairman
The Honorable Darrell E. Issa
Ranking Member
Committee on Oversight and Government Reform
House of Representatives

The Honorable Stephen F. Lynch
Chairman
The Honorable Jason Chaffetz
Ranking Member
Subcommittee on Federal Workforce,
Postal Service, and the District of Columbia
Committee on Oversight and Government Reform
House of Representatives

The Honorable José E. Serrano
Chairman
The Honorable Jo Ann Emerson
Ranking Member
Subcommittee on Financial Services and
General Government
Committee on Appropriations
House of Representatives

Appendix I: Objectives, Scope, and Methodology

The Postal Accountability and Enhancement Act (PAEA) of 2006 required us to report on strategies and options for the long-term structural and operational reform of the United States Postal Service (USPS). Because of USPS's financial crisis and our assessment that restructuring is urgently needed, our work has been accelerated at the request of Members of Congress and is presented in this report. The objectives of this report are to assess (1) the viability of USPS's business model, (2) strategies and options to address challenges to USPS's current business model, and (3) actions Congress and USPS need to take to facilitate progress toward USPS's financial viability.

To assess the viability of USPS's business model, we relied on our past work, including putting USPS's financial condition on GAO's high-risk list in July 2009, and on our testimonies regarding its deteriorating financial condition. We interviewed multiple USPS officials, including the Postmaster General, the Deputy Postmaster General, the former and current Chairman of the Board of Governors, and headquarters and field staff during visits to post offices, mail processing facilities, and other facilities that serve urban and rural areas. We reviewed USPS financial and operating information, including its Annual Reports, Integrated Financial Plans, and Comprehensive Statements; other strategic documents, including its transformation plans, *Assessment of U.S. Postal Service Future Business Model*, action plan released March 2010—entitled *Ensuring a Viable Postal Service for America: An Action Plan for the Future* (*Action Plan*)—and the *Action Plan's* financial and volume projections; and collective bargaining agreements. We reviewed USPS's current legal and regulatory framework and relevant congressional testimonies and hearings. We also reviewed the results of retiree health valuations provided to us by the Office of Personnel Management (OPM) in March 2010. OPM's valuations, which include estimates of future obligations, costs, premium payments, and fund balances, were based on USPS employee population projections. We did not assess the reasonableness of USPS's population projections or OPM's actuarial assumptions and methodology. We utilized OPM's valuation results to analyze the financial impacts of selected options for funding USPS's retiree health benefit obligations. We did not assess the validity of USPS's financial and mail volume projections due to time and resource constraints.

Also, we examined reports issued by other postal stakeholders, including the Postal Regulatory Commission (PRC) (particularly its 2008 report on *Universal Postal Service and the Postal Monopoly*), USPS Office of Inspector General, Congressional Research Service, Congressional Budget Office, the 2003 President's Commission on the United States Postal Service, and other mailing industry experts. We also met with PRC commissioners and various staff members; representatives of the four major employee unions and three major management associations (the American Postal Workers Union, National Association of Letter Carriers, National Postal Mail Handlers Union, National Rural Letter Carriers' Association, National Association of Postmasters of the United States, National League of Postmasters, and National Association of Postal Supervisors); USPS Office of Inspector General; Military Postal Service Agency; members of the mailing industry; other postal stakeholders; and economists.

To identify options to address the challenges in the current business model, we reviewed information from many of the sources that we have previously mentioned, including (1) past GAO work, (2) relevant congressional hearings and testimonies, (3) stakeholder studies, and (4) interviews with stakeholders. We then supplemented this information by distributing a list of questions to over 60 organizations to gather their opinions on actions that could be taken to improve USPS's business model and the potential impacts of these actions. Organizations were selected on the basis of a variety of factors, including those who have testified before Congress on postal issues; submitted comments (1) during the public comment solicitations as part of the work of the 2003 President's Commission on the United States Postal Service, (2) to PRC on universal service, the postal monopoly, and the new regulatory structure for ratemaking, and (3) to the Federal Trade Commission on differences in the legal status between USPS and its competitors; and have been active participants in various USPS-related activities, including participation in the Mailers' Technical Advisory Committee (a joint USPS-industry workgroup). We also considered the nature of the organization and selected organizations that represented various sections of the postal community, including unions, management associations, private printing and mailing companies, and mailers across various mail segments (e.g., large and smaller mailers, First-Class Mail, Standard Mail, Periodicals, parcels, newspapers, and nonprofit mail). We received responses from 24 mailing associations, 15 private companies, and 4 postal unions and management associations, which is a response rate of about 70 percent.

We then gathered and evaluated relevant options on the basis of a variety of criteria, including their potential to reduce USPS costs, realign its operations, and increase revenues, in light of its current and projected financial condition. Some options are consistent with actions we have discussed in our past work—such as optimizing USPS's retail, delivery, and mail processing networks—while others have been discussed in congressional hearings, regulatory proceedings, and major studies. Other options, some of which would require significant changes to USPS's legal framework or to current collective bargaining agreements, were selected because they would provide useful context into the key restructuring issues that we have previously described in this report. We did not include every option that we had identified in this report; rather, we present a select listing of options that were based on these criteria. We analyzed each option on the previously mentioned criteria; reviewed available cost and revenue data; and considered potential impacts on various stakeholders, including USPS, employees, mailers, and the public.

For reporting purposes, we grouped options according to these following strategies to align costs with revenues

- reducing compensation and benefits costs;
- reducing other operations and network costs and improving efficiency; and
- generating revenues through product and pricing flexibility.

Our assessment of certain options related to USPS's business model, such as in the governance and regulatory areas, was also limited because it is still too soon to see the full impact of the changes from PAEA. Furthermore, we did not address whether USPS's ownership structure should be altered at this time, but focused instead on the more pressing issues discussed throughout the report. The resolution of these operational issues may afford a clearer understanding of whether USPS's ownership structure should be modified. We also plan to address the experiences of foreign postal administrations in a separate report.

The previously mentioned analysis that we performed was also used as a basis to determine actions that Congress and USPS need to take facilitate progress toward USPS's financial viability. We supplemented this analysis with other GAO work on independent commissions and control boards, including the Department of Defense's Base Realignment and Closure Commission, and the District of Columbia Financial Responsibility and Management Assistance Authority.

We conducted this performance audit from August 2009 to April 2010 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings based on our audit objectives.

Appendix II: Comments from the United States Postal Service

JOHN E. POTTER
POSTMASTER GENERAL, CEO

UNITED STATES
POSTAL SERVICE

April 2, 2010

Mr. Phillip R. Herr
Director, Physical Infrastructure Issues
United States Government Accountability Office
441 G Street, NW
Washington, DC 20548-0002

Dear Mr. Herr:

Thank you for the opportunity to comment on the draft report titled *U.S. Postal Service: Strategies and Options to Facilitate Progress toward Financial Viability* (GAO-10-455). I appreciate the time and effort the Government Accountability Office (GAO) has devoted to these complex issues.

I am pleased that many of the actions set out in the Postal Service's plan also appear in this GAO report, and that we are in agreement on many key points. There is no question that the Postal Service's business model is not viable and that swift action must be taken to avert a financial crisis. Studies have been done, reports generated, polls taken, and projections made and analyzed. The drivers of revenue decline and cost growth are clear. There is no reason to believe that this situation will improve without structural changes.

Eight months have passed since the GAO added the Postal Service to its list of high-risk federal government programs, saying "...the Postal Service needs a restructuring plan to adjust services to meet changes in the way customers use the mail, bring personnel and other costs into better alignment with revenues, and retain earnings to cover capital investments and debt repayment." The current GAO report presents an even-handed, detailed assessment of the Postal Service's continuing challenges.

On March 2, 2010, the Postal Service laid out a practical, actionable, customer-focused plan—one consistent with the GAO's assessment—to close the gap between costs and revenue. The actions and structural changes proposed in the plan seek to make it possible for the Postal Service to continue providing the United States with reliable, affordable, high-quality service, rapidly adjust its business to reflect changing market conditions, and finance the universal service obligation. Some of these actions can be taken under our existing authority. However, the Postal Service cannot achieve solvency using only the authority it has today.

Both the GAO's high-risk assessment and the current report note that the Postal Service must be able to retain earnings to cover capital investments and debt repayment, in addition to funding its existing obligations. The Postal Service completely agrees, and is committed to a solution that provides sufficient liquidity. If a proposed course of action does not provide sufficient liquidity, it is not a viable solution.

The report sets out three matters for Congressional consideration on certain issues and provides a number of related options. We discuss these matters below.

475 L'ENFANT PLAZA SW
WASHINGTON DC 20260-0010
www.usps.com

-2-

1. *Congress should consider providing financial relief, such as revising USPS retiree health benefits funding and requiring any binding arbitration to take USPS' financial condition into account.*

The Postal Service urgently needs a restructuring of the prefunding requirement, which would ease financial pressures while we work to execute additional strategies to reduce costs, grow revenue, and increase efficiencies. Legislative action on the payment schedule would also reduce our need to borrow from the Treasury for the sole purpose of depositing money back into the Treasury for the Retiree Health Benefits Trust Fund.

The report says "USPS should continue to fund its retiree health benefit obligations to the maximum extent that its finances permit." I share that view, and the Postal Service will continue to do everything it can within the current law to regain its financial health. However, the existing business model provides neither the financial resources nor the flexibility to meet the payment schedule in current law. This was amply illustrated in FY 2009, when despite having achieved $6.1 billion in savings and obtaining financial relief from Congress, the Postal Service still ended the year with a $3.8 billion loss.

As important as it is, restructuring of retiree health benefits funding alone is not enough to ensure the Postal Service's short- and long-term financial health. We urge Congress to review potential overpayments to the Postal Service's CSRS pension fund. We support the recommendation of the USPS Office of Inspector General to divide legacy costs in a far more equitable manner than the current system.

In addition, we strongly agree with the GAO report that Congress should consider requiring arbitrators to take the Postal Service's financial condition in making any arbitration award.

2. *Congress should consider setting up a panel of experts to develop proposals for legislative and operational changes*

The GAO report also proposes for consideration the creation of a panel composed of independent experts to work with the Postal Service and stakeholders to provide Congress with a package of proposed legislative and other changes that would focus on allowing the Postal Service to adapt delivery and retail services to declining mail volumes; make its operations, networks and workforce more efficient, and generate new revenue.

We have concerns about this proposal. We believe that it would add a layer of bureaucracy and delay to problems that require immediate attention. Our challenges are urgent and well documented. It is time to act. While a BRAC-type model was effective in managing a limited number of military installations nationwide, it would not be as useful in dealing with postal operations and services found in every community in the country.

3. *Congress should require the Postal Service to provide regular reports on its actions and progress toward financial viability*

The GAO report suggests that Congress consider requiring us to provide regular reports on the actions taken to reduce costs and increase revenues, the results of these actions, and the progress toward addressing its financial problems. We agree, and plan to ensure transparency and accountability through a number of regular reports we currently are required to file. These include quarterly and annual SEC-like reports filed with the Postal Regulatory Commission (PRC) and made available to Congress and stakeholders. We will continue to give extensive information to Congress through the Annual Report, the Comprehensive Statement on Postal Operations, the Annual Network Update to Congress, oversight hearings, and responses to numerous questions submitted in connection with oversight hearings. We also file with the PRC our Annual Compliance Report, which provides detailed information about most aspects of our

-3-

business. Whenever we plan an operational change that would cause a nationwide or substantially nationwide change in service, we provide extensive information in order to secure an advisory opinion from the PRC. In addition, the GAO and the Postal Service Office of Inspector General (OIG) routinely audit numerous aspects of the Postal Service's business and provide their findings to Congress.

Key Strategies and Options

In addition to the matters for Congressional consideration discussed above, the GAO report contains "key strategies and options" in three categories for addressing the Postal Service's situation: (1) reducing compensation and benefits costs; (2) reducing other operations and network costs and improving efficiency, and (3) generating revenues through product and pricing flexibility. Each of these strategies and options is also contained in the Postal Service plan.

Category 1: *Reducing compensation and benefits costs*

We agree with the GAO that we must reduce employee-related costs and increase workforce and work rule flexibility. We note that significant portions of these costs are imposed by statute; namely, the requirements for employee participation in the CSRS or FERS pension plans and retiree health benefits.

Because wages and benefits comprise 80 percent of Postal Service costs, viability is inextricably tied to the level of benefits provided. We must have more control over total compensation. Congressional action should be taken to permit the Postal Service to bargain with postal unions over pension and retiree health programs eligibility and costs, and to reduce pension and retiree health obligations in connection with new employees.

Category 2: *Reducing other operations and network costs and improving efficiency*

We agree that reducing operations and network costs is necessary, and are working hard to accomplish that. While more facilities need to be closed, over the past ten years, the Postal Service has made remarkable reductions in operations and network costs.

Because wages and benefits are such a large proportion of the Postal Service's costs, we have focused first on reducing work hours and personnel as the most important factors in improving the efficiency of our network. Between 2000 and 2010, the Postal Service reduced complement in plant operations by 98,000 employees: from 228,000 in 2000 to 130,000 in 2010.

We concur with the GAO that individual facility decisions are best made in the context of an integrated approach that optimizes the entire mail processing network. To achieve the efficiencies and benefits of a comprehensive network approach driven by good operational and economic intentions, the Postal Service needs the freedom to make independent operational decisions regarding the activities for which it is responsible, with fewer political roadblocks. As the GAO's report notes, the Postal Service faces formidable resistance to facility closures and consolidations. Work we are doing with the OIG to enhance the process for identifying Area Mail Processing consolidation opportunities takes into consideration service standards, customer concerns, and the local business environment and should help reduce such resistance.

Category 3: *Generating revenues through product and pricing flexibility*

We agree that Congress should consider allowing the Postal Service to broaden product and service offerings, consistent with our mission, as a means of financing universal service and continuing to be responsive to the changing needs of our customers. Revenue from additional products and services would help finance universal service and help avoid the need for appropriations.

-4-

In addition to the flexibility to pursue new avenues of revenue generation, we need to modernize the regulatory structure for developing new products and services. A modern structure would allow the speed and flexibility required in today's marketplace. The Postal Accountability and Enhancement Act of 2006 (PAEA) expanded both the scope and degree of oversight imposed on the Postal Service in ways that have proven to be inconsistent with the principle that we operate like a business. For example, all pricing decisions, even on the smallest customer contracts, require the PRC to conduct a before-the-fact review (i.e., before pricing decisions can be implemented). This is not how the marketplace operates and not the way our customers interact with our competitors. A regulatory structure could be designed to allow for an after-the-fact review of pricing and product decisions while still maintaining adequate transparency, customer input, and accountability.

The report also asks whether the Postal Service should be required to sustain loss-making products, or be allowed to pierce the price cap to ensure that such products cover their attributable costs. We believe that all postal customers should not have to bear the losses caused by certain products that do not cover their costs. If Congress wishes to continue preferential pricing for some loss-making classes of products, taxpayers—not ratepayers—should subsidize them. In our plan, we recommend a price cap on market dominant products as a whole rather than by class so that we can price in response to market demand. This approach would also allow us to better adapt prices to the costs of specific products.

Other Issues Raised in the Report

In discussing the Postal Service's role, the GAO report identifies as an issue whether postal services are inherently governmental functions, and whether the Postal Service should be the only entity responsible for universal postal service. The report implies that multiple private sector providers already deliver mail, citing as an example "contractors who provide long-distance mail transportation and deliver mail to households located along sparsely populated highway routes." The Postal Service is the only entity with an obligation to deliver universal service. We do use contractors to perform services for the network, such as transportation and contract delivery. But the Postal Service controls the network and oversees all work performed within it.

Late in its report, the GAO raises the issue of reducing or eliminating the Postal Service's monopoly, and notes that some foreign posts have taken that step. In nearly all such instances, governments have provided their posts with subsidies to cover the universal service obligation, and expanded the posts' abilities to generate additional revenue from new lines of business. In some instances, posts were already earning substantial revenue from their longstanding participation in nonpostal businesses. Today, some earn more from nonpostal than postal sources.

The concept of opening up the Postal Service's business to private sector companies and contractors is often discussed. If given the opportunity to participate in the delivery of mail, private sector companies would avoid hard-to-reach or unprofitable delivery areas. This would increase the cost to the Postal Service of providing universal service because we would lose the revenue from the profitable delivery areas attractive to private sector enterprises, but continue to bear the expense of maintaining a universal network. Other countries where private competitors have taken on delivery services have protected their posts by requiring the competitors to provide or help fund universal service. So far, there is no country in the world where a new player is successfully providing universal service.

The report's discussion of the role of the Postal Service also asks whether it should continue to fulfill all of its current functions, or whether some functions could be discharged by other agencies. One of the functions mentioned is the enforcement of mail fraud and other statutes, which for over two centuries has been fulfilled by the Postal Inspection Service. Annual surveys have found the Postal Service to be the most trusted federal agency, and we believe one of the reasons is the existence of the Postal Inspection Service. Transferring the Inspection Service or

- 5 -

its duties to another agency would diminish that trust and adversely impact our brand and our revenues.

The contents of the GAO's report support many of the actions outlined by the Postal Service's plan. We agree, as the GAO said when adding the Postal Service to the high-risk list last year, that "Action is needed in multiple areas, including possible action and support by Congress; no single change will be sufficient to address USPS' challenges." The plan we outlined on March 2 is consistent with the GAO's call last year to "develop and implement a broad restructuring plan" that would include key milestones and time frames for actions, address key issues, and identify what steps Congress and other stakeholders may need to take.

Again, I appreciate the professional approach and the time the GAO has put into this report in the interest of identifying for Congress strategies to help ensure the Postal Service's financial viability. The Postal Service welcomes further discussion with you and your staff about any of these comments.

Sincerely,

John E. Potter

John E. Potter

Appendix III: GAO Contact and Staff Acknowledgments

GAO Contact

Phillip Herr, (202) 512-2834 or herrp@gao.gov

Staff Acknowledgments

In addition to the individual named above, Shirley Abel, Amy Abramowitz, Teresa Anderson, Joseph Applebaum, Gerald Barnes, Joshua Bartzen, William Dougherty, Patrick Dudley, Brandon Haller, Carol Henn, Paul Hobart, Kenneth John, Anar Ladhani, Hannah Laufe, Scott McNulty, Daniel Paepke, Susan Ragland, Amy Rosewarne, Travis Thomson, Jack Wang, and Crystal Wesco made key contributions to this report.

Related GAO Products

U.S. Postal Service: Financial Crisis Demands Aggressive Action. GAO-10-538T. Washington, D.C.: March 18, 2010.

U.S. Postal Service: The Program for Reassessing Work Provided to Injured Employees Is Under Way, but Actions Are Needed to Improve Program Management. GAO-10-78. Washington, D.C.: December 14, 2009.

U.S. Postal Service: Financial Challenges Continue, with Relatively Limited Results from Recent Revenue-Generation Efforts. GAO-10-191T. Washington, D.C.: November 5, 2009.

U.S. Postal Service: Restructuring Urgently Needed to Achieve Financial Viability. GAO-09-958T. Washington, D.C.: August 6, 2009.

U.S. Postal Service: Broad Restructuring Needed to Address Deteriorating Finances. GAO-09-790T. Washington, D.C.: July 30, 2009.

High-Risk Series: Restructuring the U.S. Postal Service to Achieve Sustainable Financial Viability. GAO-09-937SP. Washington, D.C.: July 28, 2009.

U.S. Postal Service: Mail Delivery Efficiency Has Improved, but Additional Actions Needed to Achieve Further Gains. GAO-09-696. Washington, D.C.: July 15, 2009.

U.S. Postal Service: Network Rightsizing Needed to Help Keep USPS Financially Viable. GAO-09-674T. Washington, D.C.: May 20, 2009.

U.S. Postal Service: Escalating Financial Problems Require Major Cost Reductions to Limit Losses. GAO-09-475T. Washington, D.C.: March 25, 2009.

U.S. Postal Service: Deteriorating Postal Finances Require Aggressive Actions to Reduce Costs. GAO-09-332T. Washington, D.C.: January 28, 2009.

U.S. Postal Service: USPS Has Taken Steps to Strengthen Network Realignment Planning and Accountability and Improve Communication. GAO-08-1022T. Washington, D.C.: July 24, 2008.

U.S. Postal Service: Data Needed to Assess the Effectiveness of Outsourcing. GAO-08-787. Washington, D.C.: July 24, 2008.

U.S. Postal Service Facilities: Improvements in Data Would Strengthen Maintenance and Alignment of Access to Retail Service. GAO-08-41. Washington, D.C.: December 10, 2007.

U.S. Postal Service: Mail Processing Realignment Efforts Under Way Need Better Integration and Explanation. GAO-07-717. Washington, D.C.: June 21, 2007.

U.S. Postal Service: The Service's Strategy for Realigning Its Mail Processing Infrastructure Lacks Clarity, Criteria, and Accountability. GAO-05-261. Washington, D.C.: April 8, 2005.

GAO's Mission

The Government Accountability Office, the audit, evaluation, and investigative arm of Congress, exists to support Congress in meeting its constitutional responsibilities and to help improve the performance and accountability of the federal government for the American people. GAO examines the use of public funds; evaluates federal programs and policies; and provides analyses, recommendations, and other assistance to help Congress make informed oversight, policy, and funding decisions. GAO's commitment to good government is reflected in its core values of accountability, integrity, and reliability.

Obtaining Copies of GAO Reports and Testimony

The fastest and easiest way to obtain copies of GAO documents at no cost is through GAO's Web site (www.gao.gov). Each weekday afternoon, GAO posts on its Web site newly released reports, testimony, and correspondence. To have GAO e-mail you a list of newly posted products, go to www.gao.gov and select "E-mail Updates."

Order by Phone

The price of each GAO publication reflects GAO's actual cost of production and distribution and depends on the number of pages in the publication and whether the publication is printed in color or black and white. Pricing and ordering information is posted on GAO's Web site, http://www.gao.gov/ordering.htm.

Place orders by calling (202) 512-6000, toll free (866) 801-7077, or TDD (202) 512-2537.

Orders may be paid for using American Express, Discover Card, MasterCard, Visa, check, or money order. Call for additional information.

To Report Fraud, Waste, and Abuse in Federal Programs

Contact:

Web site: www.gao.gov/fraudnet/fraudnet.htm
E-mail: fraudnet@gao.gov
Automated answering system: (800) 424-5454 or (202) 512-7470

Congressional Relations

Ralph Dawn, Managing Director, dawnr@gao.gov, (202) 512-4400
U.S. Government Accountability Office, 441 G Street NW, Room 7125
Washington, DC 20548

Public Affairs

Chuck Young, Managing Director, youngc1@gao.gov, (202) 512-4800
U.S. Government Accountability Office, 441 G Street NW, Room 7149
Washington, DC 20548

Please Print on Recycled Paper

Mr. LYNCH. Thank you, Mr. Herr.

I now yield myself 5 minutes for questions.

Mr. Potter, one of the central considerations here is to shift to a 5-day delivery model, and that concerns me greatly, both with respect to the idea of universal service and also the impact on employees within the Postal Service and how we are going to manage this if that is the direction that we go in eventually.

Now, I know that, I think, during your tenure, if I am not mistaken, the post office has already reduced the size of your work force by about 200,000 employees since 2001, which I believe is when you came in. And no one can argue that you haven't done a significant job here in terms of reducing the size of the work force. I think it was 900,000. Now it is about 700,000, maybe a little less, so there has been significant down-sizing already, or right-sizing, as some people have described it. But this shift from 6-day to 5-day, if it were to be embraced, can you lay that out for me?

Look, I come from a postal family, letter carriers, mail handlers, clerks. What is the shake-out on that, and what do you see as the impact of that change?

Mr. POTTER. Well, first of all let me say that I am very sensitive to some of the comments that Congressman Chaffetz said in his opening remarks, but I think the Postal Service is positioned today, best positioned today to make the change in frequency of delivery, and the reason I say that is because I believe that today we could accomplish that without laying off a career employee.

We have flexibility in our system right now. We have a lot of folks who are eligible to retire today. From the National Association of Letter Carrier's side of the aisle, the city carriers, we have some 13,000 non-career employees who were hired knowing that their jobs would be eliminated at some point in time, so that transition for those 13,000 can happen immediately.

We have use of overtime today to the tune of some 9,000 full-time equivalent employees. We can tighten up on that. We have a high number of people who are eligible to retire who could be incented to go.

On the rural carriers' side, the way most rural carrier routes are constructed, the 6th day of delivery is provided by a non-career employee.

So I think that the time for change on frequency of delivery is now, because it can be accomplished without laying people off. If we wait too long in the future, a lot of those non-career employees that I just described on the city side, the flexibility to use them is limited and it will go away, and so we would position ourselves to have to hire career employees in the interim. I think we are about a year away from having to hire to keep our routes staffed. And the time to change is now. And if we did hire within a year, those folks would obviously be people who would have to be laid off later on in the process.

So my opinion, there is a need to address the fact that we are delivering less mail per day. We delivered five pieces on average when I first came into the business; we are down to four pieces of mail per day being delivered, and it is on its way to three, based on a Boston consulting group's forecast.

If you look at using 2009 dollars, we were delivering $1.80 per day per delivery in 2001. That $1.80 per day per delivery is down to $1.40. We have been able to mask that change by the reduction in work force, focused with our unions on productivity. Going forward, it appears that we will have about $1 per day in 2020 being delivered.

That is really the challenge that we all have to face. Granted, there are options here, but one of the solutions has to be to adjust the frequency of delivery. It has to make a contribution to closing the gap that we have now and projected into the future.

Mr. LYNCH. Thank you. My time has just about expired. I will now yield to the ranking member, Mr. Issa, for 5 minutes.

Mr. ISSA. Thank you very much, Mr. Chairman.

I heard something that concerns me. All the reports that I have seen show that you have excess personnel today with 6-day delivery. Is that true?

Mr. POTTER. We have excess—well, let me just describe.

Mr. ISSA. If it isn't Christmas, do you have people sitting in ready rooms and do you believe that you are fully utilizing at the most efficient, effective, and highest utilization based on best practices all of your people at all levels of executive supervisor and all the way down to letter carriers?

Mr. POTTER. The answer is no. Are we operating in an optimum world? The answer is no. You spoke about the fact that we have people who are taken off the workroom floor, and you call it a ready room. It is called whatever it is all over the country.

Mr. ISSA. The articles generally have a term like that.

Mr. POTTER. But the fact of the matter is one of the concerns we have if we leave people on the workroom floor with nothing to do they are going to find something to do and make ourselves less productive.

Mr. ISSA. I am completely supportive that we piddle around, as they used to call WPA. You have to find gainful work.

Mr. POTTER. Right.

Mr. ISSA. No matter how much you are willing to be compassionate, you are not doing anyone a favor.

Mr. POTTER. Right.

Mr. ISSA. Having said that, why is it you are not here today showing us a plan and hopefully, if you have the authority, and if not, ask us for authority, an execution on right-sizing the force? How many billions of dollars would have been saved if you had already aggressively right-sized the force before you came to say I want to go from 6 days to 5? Is it $12 billion? Is it $10 billion? Is it $6 billion? How much of that $12 billion would we have seen if—and I am assuming you have the authority, but if you don't, that is part of what we are here for. How much would have been saved?

Mr. POTTER. Well, I don't have an exact number. It is a couple——

Mr. ISSA. Would it surprise you that the articles indicated it would be about $7 billion that they guess you would have saved had you had an optimized work force with or without the help of Congress? And we are not talking about the one-time cost of transitioning people. We are talking about on a go-forward basis.

Mr. POTTER. I think that is a very high estimate, but let me just talk about the fact that we have down-sized. If you look at how many people we have today versus the same period last year, you are talking about the Federal Government growing, we are down 60,000 employees year over year.

Mr. ISSA. Look, I appreciate that. During the break I went to Kodak. We all know who Kodak is. Kodak had a similar problem a decade ago.

Mr. POTTER. Right.

Mr. ISSA. Film was going away faster than any projected retirement. Now, today there are—they produce state-of-the-art ink-jet printers, they are first in digital. They are making a comeback by reinventing themselves. It is a great thing in America when you are carrying less paper. It is part of America's efficiency. We should not be fighting to try to have people move paper unless it is productive to the American economy. So we have to expect that as e-mail replaces and videoconferencing and all kinds of other techniques replace conventional letters and documents being moved around, that is actually good for the economy.

If the economy is moving away from your essential service in part, at least, is faster than attrition, why haven't you been aggressively here saying you have a growing Federal work force, we have a shrinking need, how do we make this work? Do you need funding to do it? Do you need education? Do you need transition? Do you need an additional preference over and above what you have? Do you need us to absorb the 72 percent versus 80 percent for a period of time on the health care? What is it you need to be able to tell me you do not have one person unnecessarily in a ready room?

Mr. POTTER. What we need is contractual flexibility. If I could just describe, in 2001 we had $11 billion in debt. We went from $11 billion in debt until 2006 we had $2 billion in equity. It was all focused on growing the business, and we reached a peak of volume in 2006 of $213 billion. So when you are managing a business under that environment, we could live with contracts that literally were developed over a 200-year period of time that the Postal Service has been in existence where we had probably too many full-time jobs. But in a world where you could set your watch by how much volume we were getting year to year, in a year where you had 1 percent movement high or low was a lot, that was doable. You could create 8-hour jobs.

What has happened is, as the volume has declined we no longer have 8-hour jobs in all locations, and we have constraints on us that are keeping us from optimizing our work force. Some are built into our union agreements, and we are going to fight vigorously in negotiations this year and, if necessary, arbitration to get those work rules fixed so that we have more flexibility in terms of the work force, more part-time workers.

We are going to go after issues that are constraining us from closing that gap and making the most efficient use of our employees.

I could go on forever, but we do have a very aggressive plan that has been laid out and has been shared. It does talk about eliminating a lot of unnecessary facilities, as referred to by the GAO. It is all part of the plan. That is how we are going to close a gap of $123 billion.

Some cases when we go to do that, although we have the legal authority to do that, we are often constrained by folks betting involved and suggesting to us that we don't do it, including some of the folks in the Congress, and what we need is a clear path to make that happen.

Mr. ISSA. We want to help you with that. I would just close by saying that whether you are on this side of the dias or that side of the dias, taking career jobs that pay real salaries, that allow people to support homes and families, and simply saying you are going to part-time jobs is not really acceptable from the dias. We would like to see a plan that maximizes the amount of people who can afford families to be supported on their salaries, and to the extent that you have alternate plans, part-time and so on, they are certainly going to have to be supported with explaining to us how those people don't need a full-time job, are not looking for a full-time job, or transitioning in your system to a full-time job. That is the reason I opened up with talking about getting people into work force, because I don't think you are going to find on either side of the dias a willingness to simply convert to full-time, home-supporting jobs to part-time jobs.

I yield back.

Mr. POTTER. If I could——

Mr. ISSA. No.

Mr. LYNCH. The Chair now recognizes the gentlelady from New York, Mrs. Maloney, for 5 minutes.

Mrs. MALONEY. Mr. Potter is from New York, I believe, correct?

Mr. POTTER. Excuse me?

Mrs. MALONEY. Aren't you originally from New York?

Mr. POTTER. Yes, I grew up in the Bronx.

Mrs. MALONEY. Yes. So welcome.

First of all, I would like to ask you about this payment that went into the pension fund that was so costly, that if we could address that in some way it would help with the budget concerns that you have. Mr. Potter, on March 18th, just 4 weeks ago, you testified in response to questions from Senator Durbin about the CSRS overpayments, that if the $75 billion were found you would not have to cut the frequency of service, and you testified and I got it out of the testimony, "it would take a lot of pressure off. If that were to happen, we would not have to go to the 5-day delivery." Is that still your testimony, if we could get that situation with the $75 billion taken care of?

Mr. POTTER. If we got $75 billion, we would not have to go from 6-day to 5-day delivery in the short run. Long term, I believe we are going to have to change the frequency of delivery, given the fact that volume has been going away and will continue to decline.

Mrs. MALONEY. And, Mr. Herr, how much should the Postal Service be paying into the retiree health benefits trust fund each year on an actuarial basis, and how does that compare with the current payments? Do you have that, or if you could get it to us in writing later.

Mr. HERR. I would be happy to provide that in writing.

Mrs. MALONEY. OK.

[The information referred to follows:]

action. Under current law, rate increases for market-dominant products, such as First-Class Mail and Standard Mail, could be used to better align rates and discounts with the costs, profitability, and price-sensitivity of mail. In addition, PRC recently identified several instances where USPS rates and discounts do not satisfy the provisions of the law and discussed remedial actions.[2] However, stakeholders have raised questions regarding whether all postal products, including those that receive preferential rates, should be required to cover their costs. The PRC reported that market-dominant products lost $1.7 billion collectively in fiscal year 2009, primarily from Periodicals and Standard Mail Flats such as catalogs. Losses from these products were exacerbated by preferential pricing requirements.

Looking forward, rate increases for market-dominant products up to the price cap could raise significant revenues over the next decade, since these products currently generate 88 percent of revenue, while competitive products generate nearly all other revenue. To improve its financial viability, USPS announced in March 2010 that it would seek "a moderate exigent price increase" for its market-dominant products that would be effective in 2011. An exigent rate increase over the price cap may produce a large short-term revenue boost. However, a very large rate increase could be self-defeating by encouraging mailers to further accelerate diversion to electronic alternatives, thereby lowering revenues in the long run and adding to USPS's excess capacity. Since USPS has never requested an exigent rate increase, it is not clear whether such an increase would be authorized under the provision of the Postal Accountability and Enhancement Act of 2006[3] (PAEA) that limits use of this measure to extraordinary or exceptional circumstances.[4]

Questions from Representative Maloney

1. How much should the Postal Service be paying into the Retiree Benefit Health Benefit Fund each year on an actuarial basis?

Our April 2010 report[5] provides the estimated annual payments that USPS would make into the Postal Service Retiree Health Benefits Fund (PSRHBF) under one actuarial approach for prefunding its retiree health obligations.[6] This approach uses the actuarial methods and assumptions that the Office of Personnel Management (OPM) adopted for reporting retiree health obligations and costs in the 2009 Consolidated Financial Report of the United States and workforce projections supplied by USPS. There are numerous other actuarial approaches for prefunding retiree health obligations that, for example, utilize different methods for allocating future benefit costs and/or a different number of years over which unfunded obligations are to be paid.

---

[2]Postal Regulatory Commission, *Annual Compliance Determination of U.S. Postal Service Performance: Fiscal Year 2009* (Washington, D.C., Mar. 29, 2010).
[3]Pub. L. No. 109-435, 120 Stat. 3198 (Dec. 20, 2006).
[4]39 U.S.C. §3622(d)(1)(E).
[5]GAO-10-455, pages 24-25.
[6]Obligation, in this discussion, refers to the actuarially determined liability.

2. How does that actuarial payment schedule compare to the current payment schedule?

GAO's April 2010 report also discussed how the actuarial payments discussed in Question 1 compare to the schedule provided in current law for fiscal years 2010 through 2020.[7] In brief, over this 11-year period, current law is estimated to require USPS contributions of approximately $90 billion, which amounts to about $9.7 billion more than the actuarial approach we used. USPS has already said that it cannot afford its required prefunding payments under the current schedule. As we stated in our report, any proposals to modify these payments should be structured so that USPS funds its retirement health benefit obligations—including prefunding these obligations—to the maximum extent that its finances permit.

Question from Representative Burton

1. Currently, the USPS is required to prefund their 75 year retiree health benefit obligations over the course of the 10 years. In a given year, if the entirety of the federal government had to do the same, how much would that cost?

Using the same actuarial approach we used in our April 2010 report, we estimated that the annual payment in fiscal year 2010 to prefund the non-postal portion of the federal government's civilian retiree health obligation would be approximately $27 billion. This payment has two components: the cost of currently accruing benefits, or "normal costs," and the amortization of the unfunded obligation in payments over 40 years. Using OPM's health care cost inflation trend rate for fiscal year 2010 of 8 percent, we estimate that the fiscal year 2010 normal cost for non-postal employees would be approximately $10 billion. Further, over 40 years, an annual payment of over $17 billion would be required, using OPM's assumptions of gradually declining health care cost inflation and an interest rate of 6.25 percent compounded annually, to amortize the non-postal, civilian retiree health obligation of nearly $252 billion that GAO derived from OPM's estimates[8] as of the end of fiscal year 2009.

In comparing USPS to the rest of the federal government, it is important to recognize that, unlike most of the federal government which is funded through direct appropriations, USPS operates under a fundamental principle that it should be financially self-supporting. Thus, it strives to generate enough revenues from products and services to cover its costs. Congress, with the enactment of PAEA, required USPS to begin prefunding its retiree health benefit obligations. Requiring USPS to prefund its retiree health obligations to the maximum extent that its finances

---

[7]GAO-10-455, page 25.
[8]The non-postal retiree health obligation was calculated by subtracting USPS's obligations as of September 30, 2009, (as calculated by OPM) from the total obligations that OPM reported in its fiscal year 2009 financial statements for the Federal Employees Health Benefits (FEHB) program.

Mrs. MALONEY. And also, Mr. Herr, companies cut back on pension payments temporarily during the recession and are starting to increase such payments now as the companies start making money. Doesn't that approach make sense for the Postal Service, in addition to the actuarial consideration?

Mr. HERR. I think in this case one of the things that we pointed out in our report for consideration is looking at the health benefits fund, and one of the things we suggest Congress consider there is looking at the law, looking at that payment stream, and opportunities to make that more affordable.

Mrs. MALONEY. And on page 4 of your testimony, you ask Congress to permit funding of retiree health benefits in a manner comparable to what is used by the rest of the Federal Government and the private sector, and is there any agency in the U.S. Government that pre-funds health care, the retiree health benefits obligations? Is there any other one that does that?

Mr. HERR. Not that I am aware of.

Mrs. MALONEY. Are there any States or municipal governments or agencies that pre-fund retiree health benefit obligations?

Mr. HERR. I am not aware of any, ma'am.

Mrs. MALONEY. OK. And what portion of Fortune 100 companies refund [sic] retiree health benefit obligations?

Mr. HERR. I have not done any sort of survey to determine that?

Mrs. MALONEY. Can you find out? I don't think any of them do.

Mr. HERR. I am not aware of any.

Mrs. MALONEY. And what percentage of Fortune 1,000 companies pre-fund retiree health benefit obligations on the accelerated schedule required of the U.S. Postal Service?

Mr. HERR. Again, I would say I am not aware of any.

Mrs. MALONEY. Well, my basic question is: why is the Postal Service treated differently from any other agency and any other company in the private sector? And with respect, Mr. Herr, to funding retiree health benefit obligations, you submit two broad approaches in your report. First, pay-as-you-go approach where the premiums are paid as they are billed, and second an actuarial approach where obligations are starting in 2010 instead of 2017 as current law provides. Is GAO advocating a particular approach as being better than the other?

Mr. HERR. No. In this case, the pay-as-you-go table that we included was illustrative. This is actually a proposal the Postal Service made in its plan.

Mrs. MALONEY. So you prefer the pay as you go?

Mr. HERR. Well, we are not taking the position as to which one. We know that the payments under current law are too steep. We provided the actuarial funding approach so Congress has a sense of what the parameters are to consider, because we realize there are many things that would factor into that kind of decision.

Mrs. MALONEY. And, Mr. Herr, going back to your report, your report discusses the Postal Service's IG's report, which alleges that the Postal Service overpaid $75 billion in CSRS pension obligations. Do you have a position on the merits of the IG's report?

Mr. HERR. We have taken a close look at this, and we believe that OPM acted within its authority and the direction it was given by the law. That law directed OPM to determine, within its discretion, the actuarial funding methods and assumptions by which the Postal Service would make future payments.

The OPM statement today for this hearing has a nice overview of the history of that.

Mrs. MALONEY. And I fail to understand why the Postal Service, which is vital to our economy and in many ways, is treated differently than any other agency and any other private sector. I would venture and like to see a study on cutting the Saturday delivery. I think that would hurt the economy of the postal office. People would go to independent deliveries and their other options, and it could undermine the ability and the finances of the post office which we are trying to protect.

My time is up, but that is a conversation I would like to continue.

I have questions, if you could get them back to the chairman in writing so as we look at this we can look at these other alternatives, too.

And I would like an explanation why is the Postal Service treated differently than any other Federal agency.

Mr. LYNCH. Would the gentleman like to answer that very briefly?

Mr. HERR. I think it goes back to the 2006 legislation. Mr. Potter could certainly amplify these comments, but at that time there was "found money." The Postal Service had an opportunity to repay debt and also to get ahead.

It is important to understand that the obligation for retiree health care as estimated by OPM on this retiree health care issue is $87.5 billion. There is currently $35 billion in the retiree health benefits fund. That leaves a difference of about $50 billion. So part of this is pre-funding benefits that workers and their families will look to draw on.

Mr. LYNCH. We need to move on. I thank the gentlelady.

Mrs. MALONEY. Thank you.

Mr. LYNCH. The Chair now recognizes the gentleman from Utah, Mr. Chaffetz, for 5 minutes.

Mr. CHAFFETZ. Thank you, Mr. Chairman.

In rough numbers, my understanding is you are looking at a $238 billion shortfall that by moving from 6-day to 5-day delivery the estimated savings would be somewhere between $30 and $36 billion; is that correct?

Mr. POTTER. Yes, that is correct.

Mr. CHAFFETZ. We are talking about roughly 15 percent, which is a significant number but it is not the panacea to fix all problems. You said something earlier that I want to make sure I heard correctly. You said that by moving from 6-day to 5-day you would not anticipate laying off anybody who is a career Postal Service worker. Did I hear that right?

Mr. POTTER. Yes, if we did it today. If we wait 5 years, I think it would involve layoffs.

Mr. CHAFFETZ. Where is the savings then? Where are these billions upon billions of dollars that you save by doing that? I mean, if labor cost is 80 percent——

Mr. POTTER. Well, it is the equivalent of 40,000 full-time equivalent employees that we are talking about eliminating the work.

Mr. CHAFFETZ. Right.

Mr. POTTER. And we are talking about saving on fuel——

Mr. CHAFFETZ. But you said you are not going to lay any of those career people off. I understand the part-time folk.

Mr. POTTER. Right. Part time would go, but then, again, it is overtime, which you are not laying anyone off.

Mr. CHAFFETZ. Right.

Mr. POTTER. Eliminating non-career jobs. That is not laying—again, not affecting career employees. And incenting current career employees to retire. A combination of all three I believe would put us in a position where we would not have to lay anybody off to capture the savings.

Mr. CHAFFETZ. As this meeting concludes, if you can help flesh that out so I can understand the math and understand how you get to that number, I would appreciate it, further clarification.

Mr. POTTER. We would be very pleased to bring the report——

Mr. CHAFFETZ. That would be great.

Mr. POTTER [continuing]. To your office and share it with you.

Mr. CHAFFETZ. That would be great.

One of the other things I think has to obviously happen is the closing of physical facilities. One of the challenges you obviously face is that every Member of Congress has postal facilities in their Districts, and I recognize the difficulty you have in trying to close a facility and then having a Member of Congress trying to lobby to keep it open. I, for one, plan to introduce some legislation to give you that ability to create a BRAC-type commission, for lack of a better word, in order to take a third-party, objective point of view so that we can try to get rid of the politics that may occur from the people that serve in these halls here.

Give me a sense, an idea, of how many or how big a scope this is in terms of what you would like to do in terms of closing physical facilities.

Mr. POTTER. Well, in terms of mail processing centers, we believe we can move from the approximate 300 that we have today to somewhere in the order of 150. Now, that is not to say facilities will all close, because they serve different functions.

Mr. CHAFFETZ. Right.

Mr. POTTER. But for outgoing mail or mail that originates in a locale, we believe we can consolidate somewhere on the order of down to about 150 facilities from slightly over 300 today.

Mr. CHAFFETZ. What about good, old-fashioned post offices?

Mr. POTTER. Good, old-fashioned post offices, what we are talking about there is we are not going to eliminate the physical facility where we have delivery. I mean, we have folks who come and deliver the mail.

Mr. CHAFFETZ. Right.

Mr. POTTER. The real challenge there is how do we best provide retail going forward, because if you look at the projections in the future of how many folks are going to buy stamps, it is going to go down as people pay their bills online. We think that the stamp revenue in postal facilities is going to be down 50 percent. So our concern is: how do you maintain those retail assets when literally they are there to sell stamps, and stamp sales are potentially going to go down by 50 percent? So, what we were looking at there is, if the migration continues with folks buying stamps at grocery stores and other locations, or buying online, there will be less demand in the postal lobby.

Today, 30 percent of all retail sales occur outside of a post office, with 50 percent of those sales expected to go away because stamp sales are going away and more people are migrating out of those lobbies. We think thousands of post offices might be candidates to be closed, but maintaining access to people by selling stamps at their door.

Ideally, we would like to think of any computer in America as a post office, and we would like to think of the letter carriers that come to every door every day as servicing those accounts.

Mr. CHAFFETZ. If we could just address in the final seconds that I have here the effect energy prices has on your cost structure——

Mr. POTTER. It is $8 million per penny, so you just described $8 million per penny growth in gasoline prices, so you described that it was $2, it went to $3—$800 million.

Mr. CHAFFETZ. Thank you. Thank you, Mr. Chairman.

Mr. LYNCH. I thank the gentleman.

The Chair now recognizes the gentleman from Ohio, Mr. Kucinich, for 5 minutes.

Mr. KUCINICH. Mr. Chairman, members of the committee, in the analysis that GAO did, they talk about the declines in revenue due to economic downturn, changing use of mail, link to continuing shift to electronic communications, and payments. One of the things that I think the Postal Service has not been mindful of, and certainly GAO doesn't seem to have a fluency with is the problem of people who are on the other side of the digital divide, people who don't have access to the Internet, people who aren't skilled in using electronic payments over the Internet, people who don't do electronic banking, because we have constituencies. I would think that they would tend to be people in lower socio-economic scale, but they also might be people who are elderly, who don't have the fluency with the Internet.

The whole idea of universal service means universal without respect to age, to income, to race, or to any other indices that you might use as a society. Members of this committee, we are actually looking at dismantling universal access.

I want to give you some ideas of how they are doing it. Look in your neighborhoods. Taking mailboxes out of a neighborhood, now for some people that might not seem like a big deal, but suppose you are used to moving the mail from your house to the post office by walking, walking to a mailbox. Mailboxes by the thousands have been removed from communities. Nobody talked to any Members of Congress, I can promise you that. They didn't ask for any of our opinions whether you move a mailbox out.

So then you go to closing post offices. That is the next part of the infrastructure. Then the next step after that is want to talk about doing away with Saturday delivery.

There are FedEx boxes outside of some U.S. Postal Service facilities. The post office, one of their recommendations that I see being made here, is to move to grocery stores and other retail locations, post office operations.

Mr. Potter, have you ever had any discussions, you or members of your staff, or did you have any communications or memoranda or e-mails with respect to talks that you have had with individuals regarding subsequent privatization of post office services, any communication of any kind whatsoever?

Mr. POTTER. As part of our analysis that was done by McKenzie and Co., they did an analysis of whether or not privatization made sense. Their conclusion was that it did not. It is part of the report. Basically, the reason that they said that was that if somebody were to come in and want to take over the Postal Service, that they would want to have a pathway to profit, and the only pathway to profit would be to deal with legacy costs, allow freedom regarding frequency of delivery, and retail outlets. And they concluded that they would even have to go further than what we are proposing in terms of the changes that are out there.

Mr. KUCINICH. That is the McKenzie study.

Mr. POTTER. Yes, sir.

Mr. KUCINICH. But it wouldn't be unusual to have legacy costs dumped on the Government and then have the private sector cherry pick the profits.

Mr. POTTER. Sir, I am not a proponent of that at all. I am saying that we are not proposing privatization. What we are trying to do is preserve——

Mr. KUCINICH. You didn't answer my question. Aside from McKenzie, have you had any meetings with anyone saying, Oh, you are going to let go of Saturday delivery, well, we will fill the gap?

Mr. POTTER. No.

Mr. KUCINICH. Really?

Mr. POTTER. Really.

Mr. KUCINICH. No one on your staff at all?

Mr. POTTER. I don't know. I can only speak for myself. I am not aware of any.

Mr. KUCINICH. And that means that you are really not anticipating then anyone else picking up the slack if you do away with Saturday delivery?

Mr. POTTER. I don't believe the economics are there to do it, and I look at the competition in the package arena and I look at what they charge for Saturday delivery, and they put a premium on Saturday delivery. The lowest price I saw is an additional $12.50 per piece.

Mr. KUCINICH. I will submit some followup questions in writing. I thank you.

Mr. LYNCH. I thank the gentleman.

The Chair now recognizes the gentleman from Missouri, Mr. Luetkemeyer, for 5 minutes.

Mr. LUETKEMEYER. Thank you, Mr. Chairman.

Gentlemen, as we were going through this this morning and we are talking about reducing service, have you had any sort of cost/benefit analysis done, or have you looked into what it is going to cost individuals and businesses if you cut back on your delivery service at all?

Mr. POTTER. We have made inquiries of our customers and we have been talking on a regular basis with our customers. The bulk of our major customers have said that they can make this change and make adjustments to the way their businesses operate and adjust to a 5-day delivery. There are some customers who simply will not be able to make a change, and probably the most obvious example is newspaper delivery, generally in rural areas where they have 6-day newspaper. Obviously, if we are not delivering on Saturday, we don't have a business solution for them. But there have been ongoing dialog with businesses. We probably would have saved well over $3.5 billion had it not been for adjustments that were made in our plan to accommodate businesses in terms of frequency of delivery.

Mr. LUETKEMEYER. OK. I am just curious about that, because I know we may be cutting our nose off to spite our face here if we wind up incurring more costs as a society as a result of what you are proposing here. I mean, there is another cost that is going to be passed along to the consumer if the businesses have to absorb additional costs as a result of the lack of mail service for an additional day.

Mr. POTTER. Well, one of the reasons—I mean, there is a fine balance here between service and cost.

Mr. LUETKEMEYER. Right.

Mr. POTTER. And so the pathway to addressing cost, unfortunately will affect service.

Mr. LUETKEMEYER. Right.

Mr. POTTER. We do want to preserve universal service for all of America, and one way to do it is to reduce the frequency——

Mr. LUETKEMEYER. Right.

Mr. POTTER [continuing]. And keep rates affordable. And so trying to find that balance is very difficult.

Mr. LUETKEMEYER. To followup on a comment of the gentleman, Mr. Kucinich, my concern also is along the lines that if you do away with the 6th day somebody else will step in, provide that service, or cherry pick those areas that they can provide service and make money on that service delivery and then, at the end of the day, by allowing them to sort of get their nose into the business, suddenly whittle away at the rest of the Postal Service business. Is that a possibility?

Mr. POTTER. I don't believe so, sir, but, again, the competition, the main competition, charges a $12.50 premium per piece that is delivered on Saturday. We have a declining business. The fact that we still have a 5-day network, I think makes us extremely strong, and we are very efficient when it comes to the handling of mail.

Mr. LUETKEMEYER. Well, you use the FedEx and UPS folks, and they provide a similar delivery service of packages, so therefore they have already cherry picked out part of your business. It would seem to me that it would make sense that if you gave up part of the business somebody would fill a void there on part of it that can actually make money, and before long they wind up expanding that service to all 5 days rather than just the 6th day.

Mr. POTTER. I am not going to say——

Mr. LUETKEMEYER. I just point that out as a concern.

Mr. POTTER. I am not going to say there is no risk, but I think the risk is minimal.

Mr. LUETKEMEYER. Yes. In your testimony here both of you, Mr. Herr and Mr. Potter, both talked about expanded products and services, and you mentioned one, I think, Mr. Herr, with regards to the new box that whatever fits in, one price and off it goes. That is a neat concept and it works very well, apparently.

What other products and services do you have in the pipeline or considering or things that may be on the horizon for us here?

Mr. POTTER. Well, I will give you one example that we just shared with a convention that we had down in Nashville this week. We are entering into an agreement with Hallmark that they will sell prepaid envelopes for their greeting cards, so it will be one-stop shop. You buy the card, you are buying the prepaid envelope at the same time. We are using an intelligent mail bar code, which is a new code that we have been deploying to help us with the accounting of that process. So that is an example of just trying to bring added convenience to the customer base.

Mr. LUETKEMEYER. That is interesting.

Thank you, Mr. Chairman. I yield back the balance of my time.

Mr. LYNCH. I thank the gentleman.

The Chair now recognizes the gentleman from Virginia, Mr. Connolly, for 5 minutes.

Mr. CONNOLLY. I thank the Chair and I thank both of our panelists for being here this morning.

Mr. Chairman, I will, with your permission, enter my full statement into the record, but I must say, I continue to be bothered by the fact that the approach to trying to deal with the issues of solvency and long-term viability of the Postal Service continue to be ad hoc. I must confess to some disappointment in the GAO report, in particular, that we are not looking at a more comprehensive new business model approach. Ad hoc cuts to delivery service may save money in the short run, at long-term cost in terms of customer base. I think Mr. Chaffetz raised some very legitimate concerns about going from 6 to 5 days a week.

I would note with historical interest that this discussion occurred in 1976, where a similar situation was faced and the Postal Service again said if we don't go from 6 to 5 we will never make it, and subsequently, of course, the Postal Service actually experienced some record profits without cutting service from 6 to 5 days.

I would like to ask the GAO rep, we keep on talking about this $238 billion in cumulative losses, and I bring to your attention the thoughtful testimony of CRS which says you have to look behind that number. First, there are certain assumptions made about what will or will not happen in terms of economic growth and customer base for $238 billion. Second, you would have to ignore the statute that says there is a statutory debt limit actually in USPS, and then you would have to assume Congress does absolutely nothing for 10 years and that you would borrow $231 billion from the U.S. Treasury.

That is a little hard to believe, so I am a little concerned that in bandying about this $238 billion number we are ignoring some obvious things that are going to happen, and it looks, frankly, a little bit like a scare tactic to get us to make some decision that may or may not be popular. And they may, in fact, be viable decisions, but how real really is that $238 billion number? And would you care to respond directly to the Congressional Research Service report, page 11, that lays out the flaws in this $238 billion?

Mr. HERR. I appreciate the question. In looking at that number, we realize that is the number that says if nothing else changes. I agree, things will change. There is attrition that is expected. Given the drop in volume and revenue, the idea that the Postal Service would be self-financing, one would expect that number was probably by far the worst-case scenario.

It is the number that is put out there to provide some context for what happens if nothing were to change, but it is understood that things would have to change in the interim.

Mr. CONNOLLY. And we would do nothing for 10 years.

Mr. HERR. I would assume that would not be the case.

Mr. CONNOLLY. Right. So how real then is the $238 billion number that has been bandied about in testimony here and in the press and—I mean, one begins to conclude it has no basis in fact at all, other than to scare people.

Mr. HERR. Well, I think that it is a starting point. I mean, again, this is a number that the Postal Service came up with, but it is, I think, to provide an illustrative case of not doing anything. And if nothing is done, then you will face those kind of challenges.

Mr. CONNOLLY. Could I ask Postmaster General Potter to respond to that?

Mr. POTTER. Well, I agree with what he just said. It is what happens if nothing is done. We did lay out a way of closing $123 billion of that gap, and, again, through aggressive management, focus on productivity. There is an element of growth that is built into that $123 billion. However, there is a sizable gap beyond that.

Mr. CONNOLLY. Can I interrupt you for just 1 second there, Mr. Postmaster General, because you make a very good point. You would have to assume, for $238 billion to be real, we do nothing, including you. You already said you are going to use the authority you have to make reductions totaling $123 billion; is that correct?

Mr. POTTER. That is correct.

Mr. CONNOLLY. So the $238 billion number is already not real.

Mr. POTTER. It is a theoretical number.

Mr. CONNOLLY. A theoretical number. Except that you have already announced here you are taking steps to make sure that theoretical number is never real.

Mr. POTTER. Exactly.

Mr. CONNOLLY. Thank you.

Mr. LYNCH. I thank the gentleman.

The Chair now recognizes the gentleman from Indiana, Mr. Burton, for 5 minutes.

Mr. BURTON. General Potter, it is good seeing you again.

Mr. POTTER. Good to see you, Mr. Burton.

Mr. BURTON. You have been there for a while and you have done a good job, and I really don't envy the position that you guys are in right now, because with the Internet and everything it has to be a real problem.

Mr. POTTER. Well, I don't envy the Federal Government, either, so you have a tough job, yourself.

Mr. BURTON. Neither do I.

According to Congressional Research Service testimony, the Postal Service has reduced its post office inventory by slightly over 15 percent since 1970, and I assume that these facilities were closed for reasons other than or in addition to profitability. Last year, you began to review stations and branches which the Postal Service maintains that is not subject to the same legal hurdles that post offices. In the absence of these legal hurdles, how many branches have you shuttered, how many will you close, or are you still in study mode? And this is the question: it is my understanding that the Postal Regulatory Commission estimates that closing all small and rural post offices will yield savings of about 7/10 of 1 percent of your operating budget. That doesn't sound like very much. Is that going to make a big impact?

Mr. POTTER. Let me try to answer all those questions.

First, from stations and branches, we did have a national review of stations and branches. Our local offices have made recommendations for changes. Subsequent to that, we received the advisory opinion of the Postal Regulatory Commission and we also completed our analysis on the plan that we submitted to you as part of my testimony. We are in the process of reviewing those recommendations in light of the Postal Regulatory Commission's suggestions, as well as to make sure that we are aligned with our plan to assure that there is access, that we don't close anything without assuring that the community has access. So far we have closed none. OK?

Regarding post offices, I think there is an assumption that if, post offices were under review nationwide, that somehow small post office would be the target of the change, and I will just tell you that Canada embarked on a review of their post offices to determine where they had alternate access in light of some of the challenges that we similarly face. They would close offices where there was no access. Much to their own surprise, what they found out was that many of the rural post offices ended up having to remain open because of the fact that there was no alternative access in many of those communities.

So it is a matter of we don't have a plan to abandon any community. We recognize universal service. The question is: how can that best be provided? And if finding a location that is open 7 days a week and 14 hours a day or more, if that provides better access to a community than a post office that has more restricted hours, then that is the choice that will be made.

So, again, I think that a lot of people rush to judgment about what the outcome of the process will be, and we have not embarked on it. But no, there is no one back in postal headquarters saying this is the community and we are going to wipe these out; it is going to be a matter of a process and it is going to take a lot of time.

Mr. BURTON. So I presume we will see you back here after you go through your study and make your decisions?

Mr. POTTER. Right. And I think it will evolve over time, and it will be on a community-by-community basis.

Mr. BURTON. OK.

Mr. POTTER. It is not going to be made at a national level. We don't know what is going on in the State of Washington or in Florida. Our local managers know best what is down there.

Mr. BURTON. OK. I think Mrs. Maloney asked this question. I don't think she is here now. But I think you said a 1-year fix was supposed to fix the problem that we might be facing as far as going to 5-day delivery service from 6 days. What happened?

Mr. POTTER. Well, just let me see if I can clarify. one of the things that we believe was that we over-funded the Civil Service Retirement System pension fund. We believed that back in 2003 when the law was changed that declared that we were over-funded by $17 billion. At the time, the Postal Service felt that it was over-funded by over $100 billion, and we appealed to the Board of Actuaries at OPM, and they said no, that the way OPM did their analysis was correct.

The 2006 law, Congress added a provision that enabled the Postal Service to appeal to the Postal Regulatory Commission to have an actuary review that decision. We have made that appeal, and I believe the Postal Regulatory Commission is reviewing that.

Should a decision be made that would benefit us in terms of that split that occurred back in 1971 over who paid for what, then we would use some of those funds to delay moving from 6 to 5-day delivery.

Mr. BURTON. Mr. Chairman, could I one more real quick question?

I would like to ask this question of Mr. Herr. I think GAO has recommended that the pre-funding be continued at the Postal Service. I would just like to know, if GAO had to do pre-funding, how much would that cost?

Mr. HERR. What it would cost GAO as an agency?

Mr. BURTON. Yes.

Mr. HERR. I haven't done that analysis.

Mr. BURTON. Well, I am just curious, because you have recommended that the Postal Service be pre-funded, and a lot of people agree with that, but we don't do that with any other agency of Government. I would like to know how much it would cost. If you could give us that for the record, I really would appreciate it.

Mr. HERR. I can ask our financial office to see if they can put that number together.

Mr. BURTON. Thank you, sir.

[The information referred to follows:]

2. How does that actuarial payment schedule compare to the current payment schedule?

GAO's April 2010 report also discussed how the actuarial payments discussed in Question 1 compare to the schedule provided in current law for fiscal years 2010 through 2020.[7] In brief, over this 11-year period, current law is estimated to require USPS contributions of approximately $90 billion, which amounts to about $9.7 billion more than the actuarial approach we used. USPS has already said that it cannot afford its required prefunding payments under the current schedule. As we stated in our report, any proposals to modify these payments should be structured so that USPS funds its retirement health benefit obligations—including prefunding these obligations—to the maximum extent that its finances permit.

Question from Representative Burton

1. Currently, the USPS is required to prefund their 75 year retiree health benefit obligations over the course of the 10 years. In a given year, if the entirety of the federal government had to do the same, how much would that cost?

Using the same actuarial approach we used in our April 2010 report, we estimated that the annual payment in fiscal year 2010 to prefund the non-postal portion of the federal government's civilian retiree health obligation would be approximately $27 billion. This payment has two components: the cost of currently accruing benefits, or "normal costs," and the amortization of the unfunded obligation in payments over 40 years. Using OPM's health care cost inflation trend rate for fiscal year 2010 of 8 percent, we estimate that the fiscal year 2010 normal cost for non-postal employees would be approximately $10 billion. Further, over 40 years, an annual payment of over $17 billion would be required, using OPM's assumptions of gradually declining health care cost inflation and an interest rate of 6.25 percent compounded annually, to amortize the non-postal, civilian retiree health obligation of nearly $252 billion that GAO derived from OPM's estimates[8] as of the end of fiscal year 2009.

In comparing USPS to the rest of the federal government, it is important to recognize that, unlike most of the federal government which is funded through direct appropriations, USPS operates under a fundamental principle that it should be financially self-supporting. Thus, it strives to generate enough revenues from products and services to cover its costs. Congress, with the enactment of PAEA, required USPS to begin prefunding its retiree health benefit obligations. Requiring USPS to prefund its retiree health obligations to the maximum extent that its finances

---

[7]GAO-10-455, page 25.

[8]The non-postal retiree health obligation was calculated by subtracting USPS's obligations as of September 30, 2009, (as calculated by OPM) from the total obligations that OPM reported in its fiscal year 2009 financial statements for the Federal Employees Health Benefits (FEHB) program.

permit will help ensure that funds generated from ratepayers, not taxpayers, will be available to pay for the benefits of USPS retirees.

Lastly, as a matter of clarification, PAEA did not require USPS to fully prefund its retiree health obligation over 10 years, but only to begin prefunding its existing obligations. USPS's reported obligation is the amount of costs that have accrued as of the current date but does not include benefit costs that have yet to accrue for USPS's current or future employees. Assuming that USPS were to make all of its remaining prefunding payments from fiscal years 2010 through 2016 under current law, USPS would still have a remaining unfunded obligation of $27 billion at the end of fiscal year 2016. In comparison, USPS's unfunded obligations for retiree health benefits were $75 billion on September 30, 2006, shortly before PAEA was enacted.

Mr. LYNCH. I thank the gentleman.

The Chair now recognizes the distinguished gentleman from Illinois, Mr. Davis, for 5 minutes.

Mr. DAVIS. Thank you very much, Mr. Chairman. I want to thank you for calling the hearing. I certainly want to thank the witnesses for appearing.

Actually, I want to commend Mr. Potter and his management team, along with the stakeholders and unions, for holding together a system that I think we have sort of been asleep a little bit with. I noticed that Mr. Connolly is not here, the gentleman from Virginia, but I think he makes a very astute observation, and that is that there has been some negligence in terms of planning for this day, and sort of knowing that it was going to come. Someone reminded me when I was in undergraduate school and my advisor had me take 10 hours of German, and I should have been taking 10 hours of Spanish, and I am sure that he meant well. I mean, he had his rationale and he had his motivation for doing it. And I am sure that some of the approaches that we have taken, we have meant well, but I think we had to kind of know that we were moving in the direction just with the change in environment, the change in economies, and the changing of time, that we would be at this juncture.

Mr. Potter, let me ask you, if we were to refund or transfer the overpayment, and I guess the idea is that this would give us some breathing room to try and search for more long-term solutions, how much time, or do you have any projection relative to how much time that might provide us with?

Mr. POTTER. Depending on what was done with the money, we have kind of examined what we would do. I think it gives us a 5-year window, assuming that we could take the moneys, pay down our debt, the debt that we have now, assure that we fully fund CSRS, because there is a potential $10 billion there that there might be a gap, and then use the funds to pre-pay the retiree health benefit trust fund payments that are due in the next 5 years. I think it could cover that gap, but I think at that point in time we would be sitting down again talking about how we effect the changes that we have laid out in our plan.

Mr. DAVIS. Well, let me just say that for this one Member, that sounds like a very rational approach to me, that there are no simple solutions to very complex problems and circumstances, and obviously it is going to take a tremendous amount of understanding, negotiation. I think we have all of the stakeholders that we want to try and keep in business. We certainly want to recognize the problems and workplace concerns of the men and women who actually process and deliver the mail. And so I think that this is an approach that we certainly need to be pursuing.

Mr. Herr, let me ask you: what does high risk mean to the Government Accountability Office?

Mr. HERR. Congressman Davis, GAO has a list of about 30 agencies that are high risk in different areas. In the case of the Postal Service, we refer to the high risk in the sense of the financial condition of the Postal Service, and by that we are referring to the idea that Congress suggested the Postal Service be self-sufficient; that is, to have revenues to cover its cost.

It became clear last summer that was very much at risk, given the decline in mail volume, the decline in revenues, and then what that meant for their business model in terms of their operations.

Mr. DAVIS. And so, if I were to translate that into layman terminology, it would mean that something has to be done.

Mr. HERR. Yes.

Mr. DAVIS. Otherwise, things are going to get worse.

Mr. HERR. Well, yes. You could say that is a good way to put it.

Mr. DAVIS. And, finally, let me just ask you, you did mention that we need to re-examine our structure for collective bargaining——

Mr. HERR. Right.

Mr. DAVIS [continuing]. With the management of the Postal Service and the unions. Could you kind of amplify that a bit?

Mr. HERR. Yes. Part of that is the thinking that—they go into union negotiations this year—if something goes to binding arbitration, simply that the financial condition of the Postal Service is taken into consideration so that there is the possibility that whatever agreement is reached through that process, that it is going to be one that can be sustained going forward.

Mr. DAVIS. Thank you very much, gentlemen.

Mr. Chairman, thank you. I yield back the balance of my time.

Mr. LYNCH. I thank the gentleman.

The Chair now recognizes the gentlelady from California, Ms. Chu, for 5 minutes.

Ms. CHU. Mr. Potter, on the 5-day delivery question, my issue is: once we go down this road where does it all end? It is my understanding that once the language requiring 6-day delivery is repealed, there would be no legal barrier to prevent the Postal Service from reducing delivery days further from 5 days to 4 days or a 3-day delivery. Certainly, we have seen postage stamps increase with alarming frequency, more and more so. For me it is even hard to remember what the last postage stamp rate was.

On delivery issues, Business Week Magazine called on the Postal Service to shift immediately to 3-day delivery within days of the Postal Service's announcement of its action plan. Of course, that would be really alarming. It would destroy half our jobs, but also likely lead to a death spiral for the Postal Service, with less service leading to less mail volume leading to less service and so on.

So, Mr. Potter, what guarantees, if any, would postal workers and the American people receive that there would not be further reductions in delivery days?

Mr. POTTER. Let me just say, Congresswoman, that we did look and try to look out into the future, and what we did do was build a 10-year plan, and so our plan is suggesting that, assuming that there were a broad array of opportunities to close the financial gap, that is all we would have to do in the next 10 years is move from 6 to 5. However, we haven't looked beyond that. In fact, there are many folks who are saying that our estimate of 150 billion pieces of mail in 2020 is optimistic. I hope it is not. We are going to work hard to try and beat that plan, that forecast, but there are no assurances beyond the next decade. I think it is going to be a function of America's use of the mail.

When you think about that, I look at the Postal Service. We are mailing less than we had in the past. The Federal Government is mailing less than they have in the past. Most businesses in America are mailing less mail, and most Americans are mailing less.

Going forward, we think that trend is going to continue, so it does create a very complex situation for us and for everybody. How do you match our use of resources with the revenues that we are going to take in?

Ms. CHU. My other question is whether switching to a 5-day delivery week would actually accelerate the loss of customers, because letters mailed on Friday night would not be picked up until Monday morning or Monday afternoon. Less frequent delivery is going to accelerate the shift to electronic invoicing. Booming businesses like mail order prescriptions would be threatened because they count on Saturday delivery. They might go over to FedEx or UPS. And as they open accounts and become more comfortable with these other services, they would start to use the Postal Services less. So it seems that Saturday delivery is the Postal Service's key strategic advantage over its private competitors over UPS and FedEx and gives away one of the more important comparative advantages in the one area of the postal market that is likely to grow when the economy recovers.

So over time the loss of revenues could outweigh the short-term savings, so how is the Postal Service going to make up for those lost customers?

Mr. POTTER. What is very interesting, I went around the country and talked to a lot of CEOs and others who are in business. When you sit down and you talk to them and you say—for example, you mentioned DVD rentals. You sit down and you talk to those folks, what is your ideal business model for in the next decade? And their business model would be out of the mail. They would do downloads to a box that people have in their home. So their long-term business model is to move away from the mail.

Likewise, when you look at bill presentment and bill payment, the ideal model for these folks is to have 100 percent of bills presented online and 100 percent of bills paid, through online. They recognize that America is in a state of transition, that they are never going to get to 100 percent, and so they need the Postal Service to support their transition into a future state.

The real challenge for all of us is how does the Postal Service change as America changes, and that is what our plan presented, was the fact that we have to be realistic about what is happening going forward, and a lot of folks, Congressman Davis and Congressman Chaffetz, have talked about the fact that we really need to be thinking about the future and designing a plan to move in that direction, and that is what we attempted to do with our plan. It is balanced. Literally everybody is affected by what we did. Nothing in it is easy. It is all hard decisions that had to be made, and so it is best that we could do in terms of trying to come up with something that we think was fair and affects people in a moderate way.

Ms. CHU. Thank you. I yield back.

Mr. LYNCH. I thank the gentlelady.

The Chair now recognizes the gentlelady from California, Ms. Speier, for 5 minutes.

Ms. SPEIER. Thank you, Mr. Chairman.

Thank you, gentlemen, for your participation this morning.

To you, Postmaster General, let me ask you, in your opening comments you referenced that one of the things you could do was create incentives for early retirement. Are you seriously thinking about that? And if so, what would that look like?

Mr. POTTER. We have already done that for the two unions where we had excess employees, and we incented with folks who are eligible to retire, we provided an early out for those who were within 5 years of retirement as part of that effort, and two $7,500 payments, one the day they retired and then one a year later.

For other unions we haven't offered it because we actually are in a position where we need the employees that we currently have, and so down-sizing makes no sense when you need the folks that you have. Why pay people to go just——

Ms. SPEIER. So even with management now you are not looking at any incentives for early retirement?

Mr. POTTER. There is no economic justification to do that right now.

Ms. SPEIER. OK. Let me move on to another line of questioning. Of the 150 billion pieces of mail, how much is direct mail?

Mr. POTTER. How much will be?

Ms. SPEIER. Or how much will be, if that is a future figure.

Mr. POTTER. I believe it is 57 percent.

Ms. SPEIER. So 57 percent is direct mail. Are you losing money on catalog delivery now?

Mr. POTTER. We are not covering our costs on some catalog delivery.

Ms. SPEIER. So wouldn't that suggest that you have to increase the cost?

Mr. POTTER. The price?

Ms. SPEIER. Yes.

Mr. POTTER. Yes.

Ms. SPEIER. The cost to the catalog company?

Mr. POTTER. Well, there is two ways of addressing it. One is to try and take cost out of our system to try and bring our cost in line with what people pay, as well as raise the price to bring it in line.

Ms. SPEIER. So how much are you losing money? Is it $100 million? Is it $10 million?

Mr. POTTER. It depends on what category of mail it is, but there are several types of mail that are not covering their cost.

Ms. SPEIER. I am talking about catalog mail in particular.

Mr. POTTER. I can provide that for the record.

Ms. SPEIER. All right.

Mr. POTTER. I don't know it off the top of my head.

Ms. SPEIER. Would you do that, then?

[The information referred to follows:]

Q7. How much is the Postal Service losing on catalog mail?

Catalog mailers use a variety of Postal Service products to deliver their mail, predominantly Standard Mail Flats and Standard Mail Carrier Route. Although the Standard Mail flats product fails to cover its attributable cost (82.4 percent cost coverage in FY2009), Standard Mail Carrier Route does make a positive contribution (144.6 percent cost coverage in FY2009), and given the distribution of catalogs between the two products, the Postal Service estimates that commercial catalogs as a whole generate enough revenue to cover their attributable cost, although they may not make a large contribution to institutional cost.

###

Ms. SPEIER. Have you looked at other countries and how they are dealing with what have to be similar issues around their Postal Service?

Mr. POTTER. Yes. In Germany they charge 80 cents for a stamp. In Canada they have gone from 6-day delivery to 5-day delivery. The same in Australia. But generally if you look around the world, we have the lowest price stamp, lowest price postage in the world for developed countries.

In addition to that, they are starting to look at things that we have done to grow volume, so they are looking at advertising mail, they are looking at things like opening up their network to allow people to bring mail into their system at different levels. We are the largest post in the world. We deliver over 40 percent of the world's mail. We are the most open post in the world in terms of providing users of the mail access at all levels, not just at origin, but you can bring mail to destination and pay a rate, you can bring mail to the delivery unit and pay an even lower rate.

The key to our business model has been volume. We have a business model that was built on volume. It worked tremendously for——

Ms. SPEIER. But that is not what our business model is going to be moving forward.

Mr. POTTER. It can't be moving forward because volume is going away because of electronic——

Ms. SPEIER. All right. I have one major question. I apologize to Chairwoman Goldway for stealing her thunder a little bit, but in her testimony that she will be making later, she says: in the Postal Service plan, regrettably there is no growth, no rejuvenation, and little innovation. It sounds to me that if we are going to continue to have a Postal Service that is viable, there are lots of changes that have to take place. Probably the most important change is one around innovation, whether it is electrifying your vehicles or looking at derivatives in terms of protecting yourself against the increased cost of gasoline.

Mr. POTTER. [Laughing.]

Ms. SPEIER. No, I am serious. I mean, you are an end user, just like the airlines are an end user for gasoline. They use derivatives to protect themselves against the cost of gasoline or petroleum from going up. I mean, I think we have to look at the entity differently. Whether or not you should be able to actually contract with catalog companies to provide better rates for the volume of shipping that is going on, because if online purchasing is going to be a thing of the future, then your shipping function is going to be far greater than the envelope.

I think the innovation is where we are lacking right now, and I would encourage you in the future to look at that.

My time has expired.

Mr. POTTER. Well, regarding derivatives, we will follow the lead of the Federal Government. You buy a lot of gasoline, as well.

Mr. LYNCH. As I understand, the post office is also paying State gas tax; is that correct?

Mr. POTTER. No.

Mr. LYNCH. You are not?

Mr. POTTER. No.

Mr. LYNCH. OK. The Chair recognizes Mr. Clay from Missouri for 5 minutes.

Mr. CLAY. Thank you, Mr. Chairman. Let me thank you for holding this important hearing to address the essential issue of securing the future of the U.S. Postal Service.

We have all watched the Service suffer under the strain of unprecedented financial loss, and it is clear that a myriad of solutions are necessary.

I want to take this opportunity to urge all of my colleagues to continue to assess this matter and challenge us to move past controversy to find real and helpful solutions.

With that, let me ask Mr. Potter, according to a summary of your report, the Postal Service rejected cost-cutting alternatives like centralized boxes. Can you tell us about the customer polling and other research that was used to reach this conclusion?

Mr. POTTER. Yes. We went out and surveyed customers. McKenzie and Co. surveyed a broad array, a statistically representative sample of America, and asked them a number of questions around alternatives that the Postal Service has to reduce cost. One of them was to take the mailbox from your door and move it to a street corner cluster box which exists in many communities around the country. Newer communities are serviced that way. Over 90 percent of those surveyed said that would be the worst thing that the Postal Service could do in terms of the array of options that was in front of them. They said that would be, in their minds, the biggest degradation to service.

For example, they looked at 6 to 5-day delivery. Every survey I have seen, two-thirds of the respondents say that they would be OK with that. But on the other side, in this case 90 percent said absolutely not. That would be a big diminution of service. That is why we pulled that option off the table. It is worth a couple of billion dollars in savings, but if the American people don't want it, we don't want to go down that path.

Mr. CLAY. OK. Another of these rejected proposals was to offer services besides mail at offices and branch locations. It seems to me that expanding your product and services would make the post office a kind of one-stop shop for customers that would increase revenue. Do you agree with that assessment?

Mr. POTTER. Congressman, we want as much freedom as we possibly can get in the law to look at options to do things outside of what the current law says. In 2006, the PAEA was passed, and it was extremely and is extremely restrictive regarding what the Postal Service can do. Basically, it sells stamps, delivers mail, and engages in the package business. We think there are other opportunities for us to generate revenue, and we would like to have the ability to study that.

Mr. CLAY. And so if you were to change to expand your products and services, what short- and long-term effect would this change have on the Service?

Mr. POTTER. Short term, probably none because one of the things that we did as part of our study was look at whether or not we should be asking to specifically get into other types of businesses that posts around the world are in, like banking, and some folks sell cell phones and other things. What we concluded was that any business you might want to get into has a certain amount of risk and would require capital investment. Given our financial situation, we are not in a position to take risk, nor do we have the capital to invest. But we would like to have the freedom to study these and perhaps, when we are in better shape, to begin to explore these other options.

In the meantime, we certainly would like to consider anything we could do at a post office to serve the Federal Government, because we are—if you think about it, 37,000 outlets for the Federal Government, and we today do passports. If there are other things that we could do, we would certainly want to get engaged to do so.

Mr. CLAY. OK. On the 6-day versus 5-day, can you give me a quick breakdown, basic breakdown on how much this would save?

Mr. POTTER. It will save $3 billion per year, and that will grow, obviously, as inflation in terms of some fuel costs and employee costs go on. So I think if you looked at it 10 years from now, it would be worth over $4 billion.

Mr. CLAY. OK. Final question. Mrs. Maloney noted that you were from the Bronx. Does that make you a Yankee fan or a Mets fan? [Laughter.]

Mr. POTTER. Yankees, of course.

Mr. LYNCH. Very good. The Chair recognizes the gentleman from Massachusetts, Mr. Tierney, for 5 minutes.

Mr. TIERNEY. Thank you, Mr. Chairman.

I thank our witnesses for being here today with us.

Can you tell me how much of the U.S. taxpayers' money now goes in annually to the Postal Service?

Mr. POTTER. We do get about $100 million for services that are provided, but other than that there is no subsidy. Zero.

Mr. TIERNEY. The customer. You get money for them being a customer?

Mr. POTTER. Excuse me?

Mr. TIERNEY. You get the $100 million because they are a customer? You get it for services that you provide to the Government?

Mr. POTTER. Yes. For example, we have to provide free matter for the blind that moves through the mail, and we provide free overseas voting. Those are the two things, the services we provide where we are compensated for them.

Mr. TIERNEY. And other than that, not a dime of taxpayer money?

Mr. POTTER. Exactly.

Mr. TIERNEY. So I don't want to pick a nit with you here or anything like that, but you generally refer to the American people and you survey the American people. You are really surveying your customer base on that?

Mr. POTTER. Exactly.

Mr. TIERNEY. Can you tell me, from your studies, your work on it, do you think there is a social value to what the Postal Service does to the public, in general, in any sense of the way?

Mr. POTTER. Without a doubt. Every week I probably sign five or six letters to employees who do things that we never get any recognition for in terms of being the eyes and ears of a Government entity in local communities, whether that is saving people in a burning building or alerting people, the local police, that there is a crime being committed. It is amazing what we can do there.

Mr. TIERNEY. I agree with you. Even aside from that, just in the every day delivery and performance of your mail, do you think there is a social benefit to the general public to the service that you provide?

Mr. POTTER. Yes.

Mr. TIERNEY. Could you give me a couple examples of what you think those are?

Mr. POTTER. Well, I think just the fact that there are a lot of people who are shut-ins, and the fact that they get mail every day is their connection to the outside world. I also know that we carry a lot of mail for our nonprofit organizations and that we are the main conduit to raise moneys for charitable organizations throughout the country. So if that conduit gets shut off, I think a lot of people are negatively harmed.

Mr. TIERNEY. Mr. Herr, do you agree with that? Do you have any additional thoughts on that?

Mr. HERR. I would agree. I think that your question gets in part to the issue raised by Congressman Kucinich about the social value of the mail and providing services to folks who are on the other side of that digital divide.

Mr. TIERNEY. So let me ask you: if we don't make these changes and things keep going downhill, what we are really looking at at some point is some privatization of this? And if a private company were to take over this responsibility, would it be fair to say that we could expect that you wouldn't get mail, necessarily delivered to your doorstep?

Mr. POTTER. That is an option that they would pursue, yes.

Mr. TIERNEY. You can bet that the prices would go up significantly?

Mr. POTTER. I would think so, other than in some local—in rural areas and suburban areas, without a doubt.

Mr. TIERNEY. And you could bet that some areas wouldn't get served at all, correct?

Mr. POTTER. Yes.

Mr. TIERNEY. As a business decision, you may not bring it out to the person that is living in an area that is difficult.

Mr. POTTER. Certainly that is an option that would exist, so universal service would be threatened.

Mr. TIERNEY. OK. So in all of your business planning and your assessments on that, did anybody take into account some contribution from the taxpayer for the return of all the benefits that they get from having universal service through the Postal Service?

Mr. POTTER. No, we did not. We are not proposing that, but that is certainly an option that you folks, folks in the Congress, could consider.

Mr. TIERNEY. Well, it would have been nice if somebody had studied that. You had all these fancy people, Boston, whatever, I forget the names of the firms, proposing ways to privatize and otherwise do things. It would have been nice if somebody could have taken that aspect and put a value to that and then talk about that. Is that something you might consider doing?

Mr. POTTER. Well, we have put a value on universal service, which is something that was built into the additional law. There was a provision in the original law back in 1971 for the Postal Service to receive compensation because of the fact that we provide universals service at a loss in some cases to different locales in the country. We put a price tag on that of about $4 billion, and it was done recently. We could share that data with you.

Mr. TIERNEY. And do you ever get the $4 billion?

Mr. POTTER. No.

Mr. TIERNEY. And if you updated what the value is in today's present cost——

Mr. POTTER. That is what it is. It had been——

Mr. TIERNEY. A smaller amount?

Mr. POTTER [continuing]. A smaller amount. And now, in today's dollars, it is, like, $4.5 billion, but I will get the exact number for you.

Mr. TIERNEY. Is that an annual value?

Mr. POTTER. Annual. Annual number.

[The information referred to follows:]

Cost of Universal Service Obligation

During the April 15, 2010 Congressional hearing on the Future of the Postal Service, Congressman John Tierney (D-MA) and Postmaster General John Potter discussed the cost of Universal Service. Mr. Potter explained that there was a provision established in 1971 with the creation of the Postal Service for the agency to receive compensation for providing universal service due to the fact that we provide universal service at a loss, in some cases, to different areas of the country. Mr. Potter quoted the value at the hearing at $4 billion, and then expanded the value to $4.5 billion to reflect today's present cost.

The following is some additional information based upon studies conducted by the Postal Service and the Postal Regulatory Commission regarding various aspects of the USO.

USPS Estimate
As background, the USPS estimated the net impact on the Postal Service's financial position from eliminating several aspects of the universal service obligation. Therefore, the USPS's estimates of various aspects of USO cannot necessarily be added up to get to a single cost of the USO.

USPS estimates include some assumptions about the future, and are dependent on both the structure of the USO and the postal and regulatory environment in which the USO is imposed. The USPS estimate of net cost savings from the elimination of Saturday delivery is taken from USPS testimony in Docket No. N2010-1.

PRC estimates
The PRC estimated the profit impact of eliminating various aspects of the USO and their study produced a total cost of the USO. The PRC updated their study to reflect conditions in 2008.

With regard to the impact of 5-day delivery, the primary difference between USPS and the PRC is that the PRC model only estimates the savings from delivery (city and rural carriers), whereas the USPS estimates the savings from delivery, mail processing and transportation.

Estimates of Net Cost Savings of the USO (Billions)

	PRC 2008	USPS	USPS Source
Six Day Delivery	2.16	3.103	2010 Case
NonProfit Discounts	1.223	1.1	FTC Study
Unzoned Media/Library Rates	0.094	-	
Losses on MD products	0.437	0.50	FTC Study
Maintaining Small Post Offices	0.549	1.433	2008 Study
Alaska Air Subsidy	0.124	0.10	2008 Study
Uniform Rates	0.212	0.812	2008 Study
Total	4.799	7.048	

###

Mr. POTTER. If I could just go back a little bit historically, prior to 1970 the Postal Service, 20 percent of the Postal Service was provided for by appropriations, and every year coming up and asking for money became problematic.

Mr. TIERNEY. I know.

Mr. POTTER. And the Postal Service ended up in a very poor condition in the late 1960's because of the difficulty in getting appropriations. That is why we have been reluctant to ask for it.

Mr. TIERNEY. I remember reading it in Washington. And I know sometimes people don't appreciate the value until they lose it, but 80 cents delivery of an envelope might get people's attention.

Mr. POTTER. I think we would lose a lot of mail, though, and a lot of jobs.

Mr. TIERNEY. I think you would.

Thank you, Mr. Chairman. Thank you for your comments.

Mr. LYNCH. I thank the gentleman.

The Chair now recognizes the gentlelady from California, Ms. Watson, for 5 minutes.

Ms. WATSON. I would like to thank the Chair for this hearing and the witnesses for your time and patience. I will direct this to Postmaster Potter.

One of the changes mentioned in the Postal Service's action plan for the future is to create a more flexible work force. While the report states that a leaner organization can be achieved through attrition, as a large number of your employees are expected to retire in the coming years, the report advocates replacing retirees with part-time workers. This concerns me, because part-time work often results in under-employment, where people do not have the opportunity to make a living wage or to receive certain benefits. The Postal Service has a very personal appeal to me because my mother worked there for 34 years, and I worked in the post office in Los Angeles for 7 years, myself, and got through college because of it, and the rest is evident in the successes I have had.

But what percentage of the work force do you envision employing part time, and how will the Postal Service ensure that these workers are fairly compensated for their work? And will part-time workers still be able to participate in collective bargaining processes?

Mr. POTTER. First of all, I share your experience, because I was a clerk and worked my way through the Postal Service, so we share that background.

Regarding part-time, we would want to maximize to the fullest extent possible the number of full-time employees that we have. That is No. 1. We are not talking about abandoning that. We want to maximize full-time employees. However, when you look at our processing centers, we now have machines that process mail at 30,000 pieces an hour. When you look at those jobs, they are not 8-hour jobs. They might be 6-hour jobs. And, by the way, when we say part-time, that is not a euphemism for non-career employees. We are talking about people who might have career jobs but might work 6 days a week, 6 hours a day, as opposed to working 8-hour days, not because we have a preference for 6 over 8, but the work would drive you to have a person working 6.

One of the things that we have done is consolidated tours. I don't know if you worked in the plant, but we have consolidated tours now to try to maximize 8-hour jobs, and will continue to do that. But when you look at the competition that does some similar work to us on the package side and you look at the folks who work in plants, they have a much higher percentage of part-time employees than we do. Ours is less than 10. Theirs is upwards of 40. And we believe that, again, it is a matter of aligning the work and picking and hiring the people to fit the work, again maximizing full-time jobs. We are not abandoning that.

I grew up. I was a member of the union. But we do have a fiscal responsibility here and we have to balance the two and we have to keep rates affordable.

Ms. WATSON. Is the real issue the fact that people are using the Postal Services less and doing more on computers and so on?

Mr. POTTER. Yes.

Ms. WATSON. What is the bottom line, and why are we in this position?

Mr. POTTER. The answer to your question is yes, that is the main cause of the challenge. I think when we hit the recession we kind of hit a tipping point. There were a number of things that happened all at the same time. Businesses went back and had invested in doing business online. They wanted to maximize the benefit from that investment, and the way they did that was to try and drive, as much as possible, transactions online.

By the way, it is not just business. Even the Federal Government—next year there is a law that is going into effect that would have anyone who does tax preparation, if you do more than 20 tax returns you have to file online. It is a good way of doing business. We are not trying to stop progress. But we, in effect, are somewhat the victim of changes that are taking place.

So this is not a matter of our employees not working hard. They are working very hard. They are providing the best service that I have ever seen in the history of the Postal Service to our customers. It is a matter of the American public and the businesses' behavior changing and the tools that they use to conduct business is changing, and we have to change with it.

Ms. WATSON. I am very sympathetic to that issue, having been in that system, as I just described. If you go to part time, will you continue the kinds of benefits that you have now for your workers? Way back in the day, in another era, this was a perfect job for single mothers to take care, because all the benefits were part of the package.

Mr. POTTER. It still is. It still is a great job.

Ms. WATSON. And you could adjust your hours and all.

Mr. POTTER. Right.

Ms. WATSON. So I am very, very concerned if you change that, that we don't put people in a lower category.

Mr. POTTER. Right. If they are career employees, as I described—there will be a mix of some non-career and career, but the career employees would get the full benefits that we provide under our contract. In fact, the non-career employees, based on the health care plan that was just passed, we are going to have to work through the rules around that, and they will be provided health care as required by law.

Ms. WATSON. I see that my time is up, Mr. Chairman, but I just have to make this statement. In some ways I don't see it getting any better, because more and more and more people are online, and it is impacting a lot of different kinds of services and industries, too. You are waiting for recommendations from this commission; is that correct?

Mr. POTTER. No. We have laid out a plan.

Ms. WATSON. You laid out a plan already?

Mr. POTTER. And we are executing what we are in control of under that plan, and we are asking Congress for some flexibilities that don't exist in the current law so that we can embark on different things to bring our costs in line with the revenues we expect.

Ms. WATSON. Well, I think I heard when I came in to the meeting—I have been late—that you are not going to get rid of Saturday deliveries; is that correct?

Mr. POTTER. No, we are proposing that we do. There were a number of panel members who you heard suggesting we not consider it, but I think it is something—what we have put together, Congresswoman, is a series of solutions and ideas on how we can close the gap, and I think what we have to—we suggest to everyone that we have to have very serious dialog about all of those solutions and make tough choices on what we need to do going forward.

Ms. WATSON. Well, I want to go on record as opposing any curtailment of services on Saturday, because many of us who have to travel from here all the way across country, the only day we can get our mail in our hand is Saturday and act on it, because we turn right around and come back here. I live on the West Coast. So please, please, please—I am asking my colleagues, too—I would strongly suggest that you continue Saturday deliveries.

With that, I yield back. Thank you, Mr. Chairman.

Mr. LYNCH. I thank the gentlelady for her thoughtful comments.

I believe this panel has suffered enough, but before proceeding to the second panel I would like to ask unanimous consent from my colleagues that the statement of the full committee chairman, Mr. Towns, and a statement from the National Association of Retired Federal Employees be entered into the record.

Hearing no objection, so ordered.

[The prepared statement of Hon. Edolphus Towns and the statement from the National Association of Retired Federal Employees follow:]

Chairman Edolphus Towns' Opening Statement

April 15, 2010

Good morning and thank you all for being here at this hearing, "Continuing to Deliver: An Examination of the Postal Service's Current Financial Crisis and Its Future Viability."

We are here today to discuss the financial crisis facing the United States Postal Service and the unsustainable business model threatening its viability. For more than 200 years the Postal Service has connected American citizens, facilitated commerce, and provided good paying jobs.

Now, this tradition of service is under more pressure than ever before. Mail volume has dropped precipitously, from 213 billion pieces in 2006 to 177 billion pieces of mail in 2009, causing revenues to fall as well. The Postal Service is losing money at an alarming pace, and its health and pension obligations exceed the Postal Service's ability to pay for them at this time. In response to these problems, the Postal Service has cut jobs through attrition and put many cost saving measures into place over the past decade. Despite these efforts, the Postal Service has not yet implemented a comprehensive strategy to create a business model to put the Postal Service on a sustainable path.

Even in this difficult environment, postal workers continue to deliver a high level of service. The Postal Service remains one of the most trusted organizations in America.

We are not here to blame anybody for these problems. Everyone who has a stake in the success of the Postal Service needs to come together to find solutions that ensure its viability. Today, we will hear about two reports that provide potential solutions to the problems in the postal system.

The 2006 postal reform law required the Government Accountably Office to write a report on the postal business model by 2011. Because of the financial crisis at the Postal Service, GAO moved up the publication of this report by a year. This is a very comprehensive report, and I thank GAO for its timely and thorough work.

The Postal Service also released a report recently, explaining its strategies for the future. The report suggests several measures to help the Postal Service, with a heavy focus on cuts in service.

I recognize that changes are needed, but we need a model for change that carefully balance the economic needs of the Postal Service with its core mission of universal service at affordable prices.

I am also concerned about the impression left by the Postal Service publicity campaign on 5 day delivery. Some newspaper articles have created the impression that 5 day will solve all the Postal Service's problems. We still don't have a firm handle on how much would be saved by eliminating a day of delivery, nor do we have a complete understanding of the impact of this proposal on customers and the postal workforce. We need a through review of all aspects of the postal business model, including 5 day delivery, to make sure that economic and social issues are fully addressed in future business and policy decisions.

Besides long term business strategies for the Postal Service, another key issue is the agency's responsibility for CSRS pension payments for employees. Employees who worked for both the old Post Office Department before 1971, and the independent Postal Service after 1971, receive pension payments that are funded by the federal government and the Postal Service.

The Postal Inspector General says that the Postal Service has overpaid for these pensions by as much as $75 billion dollars. If this is correct, it might put the changes suggested by the Postal Service and GAO in a whole new light.

We will take a closer look at this issue and I hope we can come to some kind of agreement on how to protect retiree pensions and strengthen the Postal Service.

First we will hear from the Postal Service and GAO on their reports, while our second panel will discuss the impact of these recommendations.

Again, I thank all our witnesses for appearing today and I look forward to their testimony.

###

STATEMENT FOR THE RECORD BY
MARGARET L. BAPTISTE, PRESIDENT
NATIONAL ACTIVE AND RETIRED FEDERAL EMPLOYEES ASSOCIATION

THE SUBCOMMITTEE ON THE FEDERAL WORKFORCE, THE POSTAL SERVICE AND THE DISTRICT OF COLUMBIA
COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM
UNITED STATES HOUSE OF REPRESENTATIVES

HEARING ON
"Continuing to Deliver: An Examination of the Postal Service's Current Financial Crisis and its Future Viability."

APRIL 15, 2010

The National Association of Active and Retired Employees (NARFE) represents the retirement interests of currently employed and retired federal workers from the entire federal community, including those now working for and those retired from the U.S. Postal Service. In that role, we guard seriously against any administrative or legislative proposals that could erode or endanger the earned retirement annuities of federal workers.

For that reason, we must voice our concern about the possible and unknown consequences that might arise from either replacing the current formula for determining the Postal Service's payments to the Civil Service Retirement and Disability Fund (CSRDF), or requesting a refund of payments, in the range of $75 billion, from the fund due to what the postal service believes is a calculation error in the payment amount. It has also been suggested that to improve its cash flow, the postal service forgo its $5.6 billion payment to the retiree health benefits fund.

We understand that the Postal Service faces another year of very difficult financial factors, possibly facing even greater losses over the next decade. Clearly, a number of operational and fiscal changes will be made to bring costs and revenues into line again. However, should those changes involve the funding arrangements with the federal annuities and health benefit system, we request that they be done only after a thorough actuarial review by the Office of Personnel Management.

Only after some important questions are answered, should a decision be made. The issues needing more data most important to NARFE are:

- ✓ What is the effect on the CSRDF's liabilities if refunds are made, payments are slowed or a new formula lowers payments from the postal system to the CSRDF?
- ✓ Did OPM calculate the current formula correctly or was there an overpayment by the postal service?
- ✓ If there is a change in funding procedures, is this a more permanent solution that will mean no further potential destabilization to the CSRDF?

In any case, the result will be to remove, slow or lower payments to CSRDF from the postal service.

In the upcoming years there will be enormous efforts by the Administration and Congress to reduce our trillion dollar deficit and US debt burden, while at the same time attempting to deliver financial and health benefits to an aging population. All government programs, particularly retirement and health entitlements will be up for review and consideration. It is important the actuarial and financial status of the civil service retirement fund not be called into question or altered adversely by a new system of payments at this critical time.

Mr. LYNCH. I want to thank both of you for your testimony, your help. As Mr. Issa and Mr. Chaffetz have commented, and Mr. Burton, you don't have an easy job. We have some tough decisions to make. But I appreciate the work that you have put into this. I look forward to working with you on these problems as we move forward.

I bid you both have a good day. Thank you.

I would welcome our second panel to take their places.

Let me welcome our distinguished witnesses for the second panel.

As with the first panel, it is the committee's policy that all witnesses are sworn in. May I please ask you to rise and raise your right hands.

[Witnesses sworn.]

Mr. LYNCH. Let the record show that the witnesses responded in the affirmative.

Please be seated.

I am going to offer a brief introduction of each of our witnesses.

I believe each of you have been here previously. You know the deal with the lights and the testimony. When it turns red, you should probably sum up your testimony.

First of all, the Honorable Ruth Goldway was designated chairman of the U.S. Postal Regulatory Commission by President Barack Obama on August 6, 2009, and she has served with the agency since 1998. She is an experienced regulatory and public affairs professional, with expertise in citizen participation, consumer issues, urban planning issues, as well as the mailing industry.

Mr. David Williams was sworn in as the second independent Inspector General for the U.S. Postal Service in August 2003. Mr. Williams has served as the Inspector General for five Federal agencies. He was first appointed by President George H.W. Bush to serve as the Inspector General for the U.S. Nuclear Regulatory Commission from 1989 to 1996. President William Clinton next appointed him Inspector General for the Social Security Administration from 1996 to 1998 and then as Inspector General for the Department of the Treasury in 1998. In 2001 President George W. Bush named Mr. Williams the acting Inspector General for the Department of Housing and Urban Development, while he was also serving at the Department of the Treasury.

Mr. John O'Brien is Director of Planning and Policy Analysis at the Office of Personnel Management. He joined OPM in April 2009. Prior to that, Mr. O'Brien was the Deputy Director for Research and Methodology at the Maryland Health Services Cost Review Commission. He has a master's degree in public administration from Syracuse University.

Mr. Kevin Kosar has been an analyst at the Congressional Research Service since 2003. He is the author of many CRS reports on the U.S. Postal Service, and he is the contributing editor at Public Administration Review Journal. He received his Ph.D. in politics from New York University.

Welcome all. Chairwoman Goldway, you have the right for a 5-minute opening statement. Welcome.

STATEMENTS OF RUTH GOLDWAY, CHAIRMAN, POSTAL REGULATORY COMMISSION; DAVID WILLIAMS, INSPECTOR GENERAL, OFFICE OF INSPECTOR GENERAL, U.S. POSTAL SERVICE; JOHN O'BRIEN, SENIOR ADVISOR TO THE DIRECTOR, U.S. OFFICE OF PERSONNEL MANAGEMENT; AND KEVIN KOSAR, ANALYST IN AMERICAN NATIONAL GOVERNMENT, CONGRESSIONAL RESEARCH SERVICE

STATEMENT OF RUTH GOLDWAY

Ms. GOLDWAY. Thank you, Chairman Lynch, Ranking Member Chaffetz, Congresswoman Watson, and Congressman Connolly, and other members of the committee and subcommittee. Thank you for the opportunity to testify at this hearing today.

First, I would like to assure the public that changing from 6 to 5 days is not a done deal. It requires the consideration of both my Commission and the Congress, and no decision has yet been made.

The Postal Service presented today its litany of problems and worst-case scenarios, but what do they propose? In two words, reduce service. Fewer employees to serve the public, fewer plans and fewer retail facilities, and fewer collection boxes. The plan also eliminates Saturday mail delivery, always considered a competitive advantage for the Postal Service.

Ultimately, the Postal Service would become a shadow of itself, and those who rely exclusively on the mail, the elderly, the poor, rural America, and those who cannot or will not connect to the Internet, may suffer the most.

Even more troubling, its plan stops at 2020, with nothing to arrest mail declines after that. On the contrary, the plan will spur more declines, a downward trajectory that further shrinks the system, with mail and this fundamental communications infrastructure disappearing in tandem.

This vision of the future is not inevitable. Neither the $238 billion deficit nor the double-digit volume declines seem credible to me. Even in the Internet age, mail has a unique power to touch readers and deliver results for senders. It can drive sales, provide privacy, deliver votes, and shape important personal decisions that affect life and country.

America's mail system can be reinvented and re-energized for a new century of customers; the Postal Service plan, however, has no growth and little innovation, only straight, downward-sloping trend lines.

In my 12 years on the Commission, I can recall times when the Postal Service predicted billion dollar losses and ended the year with billion dollar gains. This year the Postal Service reports through February indicate that it is $1.2 billion ahead of forecast. Mail volume is down by 8 percent, but standard mail and shipping service volumes are up. And both of these products are sensitive to economic conditions and are positive indicators of the economic turn-around.

Given this level of variability in only 6 months, projections that lie 6 years or more ahead are simply unreliable. Rather than beginning with the premise that cuts in size and scope are the only way to solve deficit problems, address these fundamental questions first: what does the law require? What is best for the Nation? How can the Postal Service maintain and improve its universal service obligation? These are the questions that the PAEA requires our Commission to ask. GAO and the Postal Service offer recommendations without this context.

An axiom in the business community is a company can't cut its way to success. You need something new. And the consensus in the mailing community is that there is not much new in these two reports.

The reports should have first looked at how to keep open as many post offices as possible, what new products the public needs that the Postal Service is uniquely positioned to provide, and how to keep delivery at 6 days, and then how to determine the products and service levels that are most advantageous to its future success.

The Postal Service efforts to expand customer access through Internet use and sales of stamps at supermarkets are commendable, but ask the small towns of America if they think Government business should be conducted in Wal-Marts. Envisioning the future calls for a transformative process, not a capitulation to big box retailing.

My written testimony includes many ideas I would have proposed for the Postal Service to accomplish by 2020 and others now being studied by my Commission staff. Among them, develop mail products based on value to the customers, not to rely on volume. This is the fundamental tenet needed to fix the Postal Service's broken business model. Provide a one-stop shop for Government services. Participate as a full partner in the Nation's Census in 2020. Commit to having a network of post offices in key locations open longer hours, even on Sundays. And guarantee at least one 24/7 post office in every big city in America. Convert the vehicle fleet to run on electricity, reducing annual fuel and maintenance expenses by more than $400 million.

Incremental improvements compound and beget real growth.

Nevertheless, I am not a Pollyanna. The Postal Service is facing serious financial difficulties. It may run out of cash at the end of this fiscal year. Over the past 3 years, the Postal Service paid $15 billion or more to the Treasury, while borrowing more than $8 billion from the Treasury. Borrowing these payments does not make sense. Only borrowing for investment in the future does.

The question of whether the Postal Service has been overcharged by $75 billion for its pension liability will be reviewed by the Commission using an independent actuary, and we plan to issue our report about this this summer.

And the Commission is now evaluating the Postal Service's plan for eliminating Saturday mail delivery. In addition to our docketed, on-the-record hearing at the Commission, we will hold a half dozen hearings across the Nation, and have so far received more than 1,500 comments. Our findings and the public record we develop will be available for your consideration within 6 to 9 months.

Before Congress agrees to major service cuts, it should resolve the pension and retiree benefit issues, and the Commission should be allowed to complete its analysis of the 5-day delivery proposal and then present it to you.

As the economy rises, it will carry the mail with it. We must use the up-swing to change the Postal Service into a vibrant communications network, providing universal service and meeting changing customer needs and demands.

That concludes my testimony. Thank you.

[The prepared statement of Ms. Goldway follows:]

Testimony of Chairman Ruth Y. Goldway,
Postal Regulatory Commission
Before the
U.S. House of Representatives Committee on Oversight and Government Reform
and the
Subcommittee on Federal Workforce, Postal Service and the District of Columbia
April 15, 2010

Chairman Towns, Chairman Lynch, Ranking Members Issa and Chaffetz and members of the Committee and Subcommittee, thank you for the opportunity to testify to this joint hearing.

Before addressing the questions you put to the Commission, I must reiterate to the public that no decision has yet been made to reduce service to five days. I am afraid the public has been confused by the Postal Service's recent announcements. We need to reassure them that this important matter requires the consideration of both the Commission and the Congress.

POSTAL SERVICE PLAN FOR THE FUTURE

On March 2 of this year, the Postal Service presented to the Nation its vision for the future of our mail system that I find very troubling. In a litany of problems and worst case scenarios, it estimates that there will be cumulative financial losses of $238 billion by the year 2020 if no changes are made.

What is the Postal Service's response to these potential losses? In two words, it is: reduce service. Its plan promises fewer employees to serve the public, fewer processing plants and postal operated retail facilities, and reduced mail collections and fewer collection boxes – more than 24 thousand collection boxes were removed from American neighborhoods just in the past year. In addition, the Postal Service plan eliminates Saturday mail delivery service, which heretofore has been considered a competitive advantage for the Postal Service.

The basic outcome of all these ideas is that there may well be less mail and less Postal Service and that those who rely exclusively on the mail, the elderly, the poor, rural America and those who cannot or will not connect to the internet may suffer the most.

Even more troubling, its plan stops at the year 2020. There is nothing in the plan to indicate how forecasted mail declines will be arrested in the following decade. On the contrary, the plan's proposals seem likely to spur further declines, a downward trajectory that suggests further shrinkage of the system, with mail and this fundamental communication infrastructure disappearing in tandem.

POWER OF THE MAIL

I do not believe that this vision is the inevitable future of the Postal Service. I believe in the Constitution of the United States and Title 39's mandate to provide a postal system that binds the Nation together. Even in the Internet Age, mail has a unique power to touch readers and deliver results for senders. It can drive sales, touch emotions, deliver votes, and shape important personal decisions that affect life and country.

I also believe that able managers and visionary leaders can navigate the current troubled waters to create growth and find new revenue while also controlling costs. I believe that America's mail system can be reinvented, reengineered and reenergized for a new century of customers. In the Postal Service plan regrettably, there is no growth, no rejuvenation and little innovation.

If the last few years have taught us anything, they have shown how unpredictable the future can be. In my 12 years on the Commission, I can recall times when the Postal Service predicted billion dollar losses and ended the year with billion dollar gains.

Even this year, it looks like the Postal Service might significantly exceed its own expectations. The latest financial report received by the Commission reveals that through the end of February it is nearly $1.2 billion dollars ahead of its forecast. Although mail volume is down by 8 percent, Standard Mail volume grew slightly for the month and Shipping Services are up 1.3 percent for the year. Both of these products are sensitive to changes in economic conditions. It may be that the economy is starting to have a tonic effect on the mail.

Seeing this kind of variability in only six months, suggests that it may be prudent to view projections that lie six years or more down the road with some caution.

A BETTER APPROACH TO THE FUTURE

The Commission commends the Postal Service for its sustained effort over many years to increase productivity, improve processes and lower its costs. We appreciate that this effort must continue and evolve for the future. Today's discussions, however, must not simply focus on costs and deficits. The Postal Service should reposition its goals to meet the needs of an evolving society.

Rather than beginning with the premise that the Postal Service needs to be cut in size and scope to solve the deficit projections, these fundamental questions must first be addressed. What does the Constitution and the law require? What is best for the Nation? How can the Postal Service maintain and improve its universal service obligation and deliver that to citizens and the business community who rely on the mail? These are questions that the Postal Accountability and Enhancement Act requires the Commission to ask.

Both GAO and the Postal Service offer recommendations without this context. An axiom in the business community is that a company cannot cut its way to success. It has to have a real plan. The consensus among the mailers I have spoken with is that there is very little that is new in these two reports.

The consultants hired by the Postal Service, and GAO analysts, should have begun by looking at what it will take to keep open as many post offices, and station and branches as possible; what new products the public needs that the Postal Service is uniquely positioned to provide; how to keep delivery at 6 days, the level required by Congress; and how to determine the service levels that are the most advantageous to its future success.

The consultants and analysts should have reviewed the Postal Service's recent attempts at innovation. In this decade, the Postal Service embarked on two projects that it described as transformative: the Intelligent Mail Barcode (IMb) and the Flat Sequencing System (FSS).

The Postal Service promised that the IMb would revolutionize the transparency and efficiency of letter mail for the Postal Service and its customers, creating new value in the mail and opportunities for growth. The Commission believed the Postal Service and agreed to use the IMb as the basis for a measurement system to track service quality. Yet, we and the mailing community continue to wait for that promise to be realized.

Similarly, FSS promised to transform the processing of flats and catalogs so that they could be sorted automatically into walk sequence, at lower costs and with higher quality. Both the IMb and the FSS are well-behind scheduled implementation. Does the Postal Service think these projects are not as promising as originally envisioned? What can be done to speed up their introduction and acceptance system-wide? Perhaps, the regulator has been too lax. Answers to these questions would better inform future plans.

Why hasn't a detailed, innovative new retail strategy been explored that will, at a minimum, improve the revenues of post offices to the point that their continuance is economically as well as socially justified. I agree that Postal Service efforts to build its website and expand customer access through internet use and sales of stamps at supermarkets are commendable. But ask the small towns of America if they think government business should be conducted in Walmarts. Why would any rational person compare the functions of a Post Office to Walmart as the Postal Service consultants did? Envisioning the future calls for a transformative process not a capitulation to big box retailing.

IDEAS FOR POSITIVE CHANGE

If I had been tasked with developing the 10-year plan, here are some of the ideas I would have proposed for the Postal Service to accomplish by 2020:

1. Develop mail products based on value to the customer not necessarily on volume. This is the fundamental tenet needed to fix the Postal Service's broken business model.
2. Convert the bulk of its vehicle fleet to run on electricity reducing annual fuel and maintenance expenses by more than $400 million per year and increasing America's independence from foreign oil.
3. Have a range of products that are fully trackable and traceable and comparable with those of private package companies.

4. Provide a one-stop shop for government services. Not just passports but national park passes, regional EZ passes, identity cards, etc.
5. Participate as a full partner in the nation's 2020 census, thereby saving the country hundreds of millions.
6. Building on the money order services now offered, introduce and implement a system to provide assistance to the unbanked, replacing usurious "pay day" operations with reliable fair service.
7. Commit to having a network of post offices in key locations that are open more hours than in 2010 and even on Sundays and guarantee at least one 24-7 post office in every big city.
8. Implement a comprehensive Vote-by-Mail system that suits the needs of all the states in the union for federal, state and local elections held at any and all times of the year.
9. Reinvent the letter carrier: Empower him/her to measure real-time service: to be accessible to the community by email; to be the eyes and ears of the community; and to be the sales and service point for small businesses.
10. Reorganize the workforce - not to make them part time employees - but to enhance their skills thereby adding flexibility in the processing centers, new energy conservation technology to logistics and motivated outgoing sales people at retail counters.
11. Commit to having ten other ideas in place and operating within the decade.

Commission staff is also up for the challenge. They are exploring ideas such as auctioning potential discounts for postage rates to get a real measure of market demand; adjusting pricing in First-Class and Standard Mail to improve Postal Service margins and encourage mailer efficiencies; and offering postal vehicles as platforms for sensors that generate revenue from other government agencies or businesses to automatically measure pollution, collect weather data, identify chemical spills, identify cell phone/wireless dead spots, spot natural gas leaks and map potholes.

Just as limiting access and declines in service create a self-fulfilling prophecy, improvements which may seem small can create the incremental reinvigoration that begets real growth.

CURRENT CRISIS

Nevertheless, I am not a Pollyanna. What seems beyond dispute at the moment is that the Postal Service is facing serious financial difficulties this year and next year.

The Postal Service ends its fiscal year on September 30. At that time, they must pay $5.5 billion into a fund for future retiree health benefits. Shortly after that, it will need to make sizeable payments for workers compensation obligations and to meet payroll. These large obligations, falling so close together, could cause the Postal Service to run out of cash. This is similar to the situation it faced last year when Congress provided $4 billion in relief.

My colleagues and I believe that the scheduled payments to fund future retiree health benefits should be readjusted, which would provide the Postal Service with further time to recover from the recession. However I think that the relief should be part of a larger strategy that is both financially and operationally transformative.

RETIREE HEALTH BENEFIT FUNDING

Last May, Chairman Lynch asked the Commission to look at OPM's computation of the Retiree Health Benefits Fund (RHBF) liability. Based on changes in how to calculate long-term medical inflation rates and the declining postal workforce, we found that a recalculation could greatly reduce the Postal Service's liability and lower the required annual payments while meeting the original funding goals of the law.

The current payment schedule has proven to be too ambitious and should be adjusted in some fashion.

Over the past three years, the Postal Service has paid $15.4 billion to Treasury to prefund future retiree health benefits. During that same time, the Postal Service borrowed more than $8 billion from Treasury so that it could make those payments. This arrangement does not protect the Federal government in the event of a Postal Service default. And it burdens the Postal Service with increasing debt service costs, which could exceed $150 million this year. Borrowing by the Postal Service to make the payments does not make sense. On the other hand, borrowing for investment in operational innovations is absolutely necessary.

The RHBF payment schedule must to be revised so the Postal Service can make smaller payments over a longer period of time and/or so that yearly payments are tied to the Postal Service's ability to pay in a given year.

PENSION LIABILITY

Currently, the Civil Service Retirement System pensions are considered fully funded, but a review by the Postal Service Inspector General determined that the Postal Service has been overcharged by $75 billion, related to the service of Post Office Department employees who continued to be employed by the Postal Service after Postal Reorganization in 1971.

Under provisions of the Postal Accountability and Enhancement Act, the Commission is in the process of hiring an actuary, at the Postal Service's request, to review OPM's calculation of the Postal Service pension liability. If any pension surplus is identified through this process, it could be used to lower Postal Service liability and payments for future retiree health benefits. We expect to issue our report this summer.

FIVE-DAY DELIVERY DECISION

Until these overriding retiree funding issues are resolved by Congress, the advisability of enacting major reductions in mail service is questionable. The PAEA requires the Commission to monitor service levels to prevent deterioration in service and assure that the Postal Service meets its Universal Service Obligation (USO). Five-day service may meet the USO. It does in other nations. However, is six-day service a strategic marketing advantage for the Postal Service even if it is not part of the USO? Perhaps a pilot project in a limited geographic area or for one month of the year would be instructive. The implications of reducing service are unknown and must be carefully considered.

Last month, the Commission began a proceeding to evaluate the Postal Service plan for eliminating Saturday mail delivery service. In addition to on-the-record hearings at the Commission, we will hold a half-dozen regional hearings across the Nation and we are soliciting the input of the American people in other ways as well. Already we have received more than 1,500 comments via our web site and through the mail. This is a vital issue for all who depend on the universal mail system.

We will build a comprehensive record on the proposal that fully and accurately reflects the viewpoints of all stakeholders and citizens and carefully evaluates potential cost savings, volume declines and alternatives. We hope to issue our Advisory Opinion in six to nine months.

The Commission's findings and the public record we develop will be readily available to members and your staffs as you consider whether to alter current legislation requiring six day delivery.

TIMING CHANGES

I understand the pressures that the Postal Service is under. And I appreciate the hard work and dedication both management and employees have shown in making changes that reduce costs without too much sacrifice in service - so far. However, I am disappointed that the 10-year plan and the newly issued GAO report are not effective plans for the future. Rather, by concentrating on cuts at the expense of service and innovation, they offer the path to obsolescence.

Now is not the time for sweeping changes to the Postal Service. Before the Congress agrees to major cuts in service, it should resolve the pension and retiree health benefit issues to determine manageable payment schedules for the Postal Service, and the Commission should be allowed to complete its analysis of the five-day delivery proposal and present it to you.

Time will also provide breathing room for hard-pressed Postal customers and the economy. If history is a guide, as the economy rises it will carry the mail with it. I believe it is possible to create a positive plan that really does envision the future, a future with a vibrant communications network providing universal service and meeting changing citizen and customer needs and demands.

Thank you, that concludes my testimony.

# # # #

Mr. LYNCH. Thank you.

Mr. Williams, you are now recognized for 5 minutes.

STATEMENT OF DAVID WILLIAMS

Mr. WILLIAMS. Mr. Chairman and members of the committee, thank you for asking for our testimony today. The Postal Service's financial condition is serious. The situation is a product of the economic downturn and the chaos of the digital age that has sent shock waves through the communications sector of the economy. Further, the Postal Service entered this storm with some chronic problems that had been masked by its success in earlier years.

Two pathways lie before the Postal Service. The most obvious is the serious financial crisis with temporary patches that will consume the energy for change and will leave mounting debts with little chance of repayment. The other pathway is much more hopeful. The current crisis is an opportunity to migrate toward a lean and successful enterprise that is well positioned for a highly adaptive future and that thrives within the model envisioned by the Postal Accountability and Enhancement Act. This pathway will require long-term solutions effectively executed to address a few critically important issues.

First, the optimization of the Postal Service's costly network of plants, post offices, and administrative apparatus must be accomplished as rapidly as possible while balancing commitment to service. Since 2003, the Postal Service has streamlined its network by reducing over 130,000 employees and in 2009 alone cutting $6 billion in costs. These are credible actions, but more is needed to match the declining mail volume projected through 2020.

Next, the rigid work rules do not match the ebb and flow of mail and customer demand in plants and post offices. As the mail continues to decline, the need for more flexible staff to perform a wider range of duties becomes more evident. Also, the greater use of evaluated letter carrier routes would provide better incentives to allow for more effective management.

Third, we in the Postal Service recognize the need for a simplified pricing structure to replace the over 10,000 prices contained in their 1,700-page customer manual. A simpler pricing structure would be easier to use, would encourage new customers, and improve revenue accountability.

Finally, this year Congress directed the Postal Service, OPM, and OMB to develop a fiscally responsible legislative proposal for the Postal Service benefit payments. Our office found three areas where over-payments are occurring: an exaggerated 7 percent health care inflation forecast instead of the 5 percent industry standard, resulting in an overpayment of $13.2 billion by 2016; an excessive 100 percent benefit plan pre-funding requirement compared to OPM's pre-funding level of 41 percent and the S&P 500's 80 percent rate. Even using the higher 80 percent rate funding goal would result in a $52 billion surplus.

Last, the Postal Service fund was over-charged $75 billion so that employees could retire at promised levels. When the Post Office Department became the Postal Service, employees that belonged to the Federal pension fund now contributed to the Postal Service. Retirement costs were divided according to the number of years employees had worked for each fund. However, the Federal pension fund paid for retirements based on 1971 salaries, not final salaries. The Federal pension fund collected full contributions, but paid only partial benefits.

OMB has explained that these mis-charges were in response to what they believed to be the will of Congress expressed in 1974; however, the 1974 language was repealed by Congress in 2003 when large over-payments were discovered. At that time, OPM inexplicably had not detected a 41 percent over-funding error in this $190 billion pension fund. Congress directed OPM to use its authority to oversee the reforms, using accepted dynamic assumptions, to include pay increases and inflation. Fixing the last issue, alone, would fully fund the pension and health care retiree funds. The Postal Service's $7 billion annual payments would no longer be needed since the plans would be fully funded and interest income could pay the annual premiums.

The Postal Service is being bled white with erroneous payments before they open their doors. The $7 billion mis-charge accounts for 66 percent of the Postal Service's projected $11 billion loss this year.

This is also serious because the Postal Service fund is not made up of tax dollars. The two funding streams are employees' own money and money collected from postage sales inflated as a result of the mis-charge.

The mis-charges should be backed out and fund balances reset to proper levels to achieve the retirement reforms Congress enacted in 2003. This would give the Postal Service a good chance of adapting to the efficient market forces envisioned in PAEA.

Thank you.

[The prepared statement of Mr. Williams follows:]

Hearing before the Committee on Oversight and Government Reform and the Subcommittee on the Federal Workforce, Postal Service, and the District of Columbia House of Representatives

Oral Statement
On
Continuing to Deliver: An Examination of the Postal Service's Current Financial Crisis and its Future Viability

April 15, 2010

David C. Williams
Inspector General
United States Postal Service

Mr. Chairman and members of the committee, thank you for asking for our testimony today. The Postal Service's financial condition is serious. The situation is the product of the economic downturn and the chaos of the digital age that has sent shock waves through the communications sector of the economy. Further the Postal Service entered this storm with some chronic problems that had been masked by its success in earlier years.

Two pathways lie before the Postal Service. The most obvious is a serious financial crisis with temporary patches that will consume the energy for change and will leave mounting debts with little chance of repayment.

The other pathway is much more hopeful. The current crisis is an opportunity to migrate toward a lean and successful enterprise that is well positioned for a highly adaptive future and thrives in the model envisioned by the Postal Accountability and Enhancement Act of 2006 (PAEA). This pathway will require long-term solutions, effectively executed, to address a few critically important issues.

- First, the optimization of the Postal Service's costly network of plants, post offices, and administrative apparatus must be accomplished as rapidly as possible, while balancing commitment to service. Since 2003, the Postal Service has streamlined its network by reducing over 130,000 employees and, in 2009 alone, cutting $6 billion in costs. These are credible actions, but more is needed to match the declining mail volume projected through 2020.

- Next, rigid workforce rules do not match the ebb and flow of mail and customer demand in plants and post offices. As the mail continues to decline the need for more flexible staff to perform a wider range of duties becomes more evident. Also the greater use of evaluated letter carrier routes would provide better incentives to allow for more effective management.

- Thirdly, we and the Postal Service, have recognized the need for a simplified, pricing structure, to replace the over 10,000 prices contained in their 1,700 page customer manual. A simpler pricing structure would be easier to use, encourage new customers, and improve revenue accountability.

- Finally, this year Congress directed the Postal Service, OPM, and OMB to develop "a fiscally responsible legislative proposal" for Postal Service benefit payments. Our office found three areas where overpayments are occurring:
    - An exaggerated 7 percent health care inflation forecast instead of the 5 percent industry standard, resulting in an overpayment of $13.2 billion by 2016;
    - An excessive 100 percent benefit plan prefunding requirement compared to OPM's own prefunding level of 41 percent and the S&P

500's, 80 percent rate. Even using the higher 80 percent funding goal would result in a $52 billion surplus.

- Lastly, the Postal Service Pension Fund was overcharged $75 billion, so that employees could retire at promised levels. When the Post Office Department became the Postal Service, employees that belonged to the Federal Pension Fund now contributed to the Postal Service. Retirement costs were divided according to the number of years employees had belonged to each fund. However, the Federal Pension Fund paid for retirements based on 1971 salaries, not final salaries. The Federal Pension Fund collected full contributions, but paid only partial benefits.

  OPM has explained that these mischarges were in response to what they believed to be the will of Congress expressed in 1974 legislation. However, the 1974 language was repealed by Congress in 2003, when large overpayments were discovered. At that time OPM inexplicably had not detected a 41 percent overfunding error in this $190 billion pension fund. Congress directed OPM to use its authority to oversee the reforms using accepted "dynamic assumptions" that include pay increases and inflation.

Fixing the last issue alone would fully fund the pension and health retiree plans. The Postal Service's $7 billion annual payments would no longer be needed, since the plans would be fully funded and interest income could pay annual premiums. The Postal Service is being bled white with erroneous payments before they open their doors. The $7 billion mischarge accounts for 66 percent of the Postal Service's projected $11 billion loss for this year.

This is also serious because the Postal Service Pension Fund is not made up of tax dollars. The two funding streams are employees' own money and money collected from postage sales inflated as a result of this mischarge.

The mischarges should be backed out and fund balances reset to proper levels to achieve the retirement reforms Congress enacted in 2003. This would give the Postal Service a good chance of adapting to efficient market forces envisioned in PAEA.

Mr. LYNCH. Thank you, Mr. Williams.

Mr. O'Brien, you are now recognized for 5 minutes.

STATEMENT OF JOHN O'BRIEN

Mr. O'BRIEN. Thank you, Chairman Lynch, Ranking Member Chaffetz, and members of the committee. I am pleased to be here today on behalf of John Berry of the Office of Personnel Management to discuss the U.S. Postal Service's contribution to the Civil Service Retirement System [CSRS].

OPM commends Chairman Lynch and the committee's efforts to review retirement obligations and other associated matter related to the financial viability of the Postal Service. In particular, we appreciate the opportunity to explain our position on the recent report by the Postal Service's Inspector General, which questioned the calculation of postal contributions to the retirement fund.

The key question that was raised by that report is whether the allocation of costs between the Treasury and the Postal Service to fund postal retirees with service to the Post Office Department prior to the establishment of the Postal Service in 1971 is fair. That is an issue about which is open to debate.

The primary concern of OPM is that the trust funds necessary to provide those benefits are properly funded, and it is important to remember that the level of funding to provide benefits to Postal retirees is not in dispute. The Postal IG's report suggests a new, different way to allocate costs necessary to fund Postal Service retiree benefits. The allocation formula used by OPM is that which is directed under current law and is not, nor should it be, characterized as an overcharge. Furthermore, the allocation methodology is consistent with sound actuarial practice and has been reviewed by outside, independent experts.

A change to current law could reduce the share of retirement costs allocated to the Postal Service and allow the Postal Service to use the resulting funds for other purposes, but it would be a change to current law and a shift from previous legislation and congressional intent.

I would like to give a brief overview of the events that bring us here today.

In 1971, the former Post Office Department was converted to the U.S. Postal Service, an independent entity. Not long after, Congress considered who should be responsible for the increases in retirement obligations for individuals who were employed by the Post Office Department before 1971 that were the results of increases in pay. This resulted in the enactment of Public Law 93–349 in July 1974. The law was clear that the Postal Service assumed the obligation to the retirement fund for increases in pay upon which benefits would be computed. Congress subsequently enacted a number of other laws dealing with other aspects of Postal Service funding, including legislation making the Postal Service responsible for funding the cost of living increases [COLAs] applicable to postal annuities.

More than one of these bills included requirements that the Postal Service make payments to fund under schedules set by Congress. During the period from 1974 to 2002, it was generally assumed that postal payments required by legislation approximately slightly less than the full funding of the Postal CRS obligation; however, this was inaccurate. In 2002, OPM determined that if the Postal Service continued to make payments as it had been, its liability would be significantly over-funded.

To address the issue, OPM sent a legislative proposal to Congress, which was subsequently enacted, to convert the funding mechanism to one applicable to the Federal Employees Retirement System [FERS], which lowered the contributions that were required of the Postal Service. That change did not affect the Postal Service's obligations for cost increases due to increases in pay, because Congress understood that the inclusion of those costs was an inherent aspect of retirement funding, which is evidence from the committee report.

OPM's methodology was considered in a January 2003 GAO report. In that report, the GAO "evaluated the reasonableness of OPM's methodologies for allocating estimated benefit payments and other expenses between service rendered before and after July 1, 1971, the effective date of the Postal Reorganization Act." In that report the GAO suggested no major changes to the methodology used by OPM, although it did recommend a consideration for military years of service, a modification that was made in 2006.

In 2003 the Postal Service sought a new funding policy that would reduce its obligations. Their proposal was that the pre-1971 service be calculated on the basis of a simple years of service approach, essentially the same methodology that has been proposed by the Postal Inspector General in its report this past January.

The matter was carefully considered by OPM and by OPM's Board of Actuaries at that time and declined. The Board of Actuaries concluded that the methodology OPM used was valid and it had followed the intent of the act.

The issue that is before Congress in the past has made changes to postal retiree fundings. We believe it is clear that OPM's actions have been fully consistent with the letter of the law and in accordance with sound actuarial practice.

Finally, funding postal retiree benefits is a separate matter from the issue of retirement funding. The two subjects are intertwined because the Postal Service wishes to use the savings from a recalculation of retirement obligations to satisfy its obligation to fund retiree health benefits. Such a proposal reinforces OPM's testimony. The action suggested by the IG report, transfer funds to the Postal Service for retiree health benefits fund, are impossible without congressional action.

We appreciate the opportunity to appear before you and to explain the basis for calculating postal retirement obligations.

I am pleased to answer any questions you may have.

[The prepared statement of Mr. O'Brien follows:]

STATEMENT

of

JOHN O'BRIEN
DIRECTOR OF PLANNING AND POLICY ANALYSIS
U.S. OFFICE OF PERSONNEL MANAGEMENT

before the

THE COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM
UNITED STATES HOUSE OF REPRESENTATIVES

on

CONTINUING TO DELIVER: AN EXAMINATION OF THE POSTAL SERVICE'S CURRENT FINANCIAL CRISIS AND ITS FUTURE VIABILITY

April 15, 2010

Chairman Towns, Ranking Member Issa, Chairman Lynch, Ranking Member Chaffetz, and Members of the Committee, I am pleased to be here today on behalf of Director John Berry of the Office of Personnel Management (OPM) to discuss "Continuing to Deliver: An Examination of the Postal Service's Current Financial Crisis and Its Future Viability".

OPM commends Chairman Towns and the Committee's efforts to review retirement obligations and other associated matters relating to the financial viability of the United States Postal Service (Postal Service). In particular, OPM appreciates the opportunity to explain the basis for its position in relation to the recent report by the Postal Service's Inspector General.

I would first emphasize that nothing discussed today will affect OPM's ability to deliver annuity payments under the Civil Service Retirement System (CSRS) and retiree health benefits coverage to individuals who have retired from the Postal Service. Postal retirees should have full confidence that they will continue to receive the retirement and health benefits they have earned based upon the valuable services they have performed for our nation.

Before delving into specific details, I would like to note that the issue before us involves questions of public and accounting policy that comes down to the proper allocation of certain pension costs between the Federal Government and the Postal Service, as discussed in more detail below. Notwithstanding the highly technical discussion that we will have today, there is no single "correct answer" in this area. There is more than one reasonable approach that could be used to address this situation. The methodology that OPM has been using since 1974 has been approved by Congress, with the advice of the Government Accountability Office (GAO), conforms with generally accepted actuarial practices and principles, as required by title 5, United States Code, and is a common actuarial practice used in the private sector. OPM also believes that it produces a fair and equitable allocation of the responsibilities regarding the payment of pensions to certain Postal employees.

The core issue is a single question: How do we determine the Federal Government's fair share of the costs under CSRS for service performed for the Post Office Department (POD) prior to the 1971 establishment of the Postal Service? Congress first spoke to this issue in 1974, when it established the policy whereby increases in the retirement value of pre-1971 Postal employment due to increases in Postal salaries (essentially the sole basis for the increases in value) should be paid for by the Postal Service. This is the policy that OPM has followed ever since in making its calculations.

The Postal Service supported enactment of this policy in 1974 and made no objection to it for almost 30 years until 2003, when it sought a new approach that would reduce its obligations. At that time, the Postal Service proposed that the obligations for pre-1971 service be calculated on the basis of a simple years-of-service approach. Other than one technical flaw[1], this is not an inconceivable approach. While it may be worthy of future consideration by the Congress, OPM believes that it is not possible based upon current legislation.

Background

In 1971, the former POD was converted to the Postal Service, an independent entity. Not long thereafter, Congress carefully considered the issue of who should be responsible for the increases in retirement obligations for pre-1971 POD service and attributable to increases in Postal pay, culminating in the enactment of Public Law 93-349 (1974).

The legislative history of P.L. 93-349 explained the public policy adopted by the Congress. The report of the Senate Committee on Post Office and Civil Service discussed both the policy and specifics of the bill:

"STATEMENT"

> "This legislation will resolve the question of who is to be responsible for increases in the unfunded liability of the Civil Service Retirement and Disability Fund which are attributable to new retirement benefits or pay increases granted to Postal employees.
>
> "Under the provisions of H.R. 29, the Postal Service will be required to make payments for that portion of any future increase in the unfunded liability of the Civil Service Retirement Fund which results from an employee-management agreement under title 39, United States Code, or any administrative action taken by the Postal Service pursuant to law, which authorizes (1) new or liberalized

[1] As proposed, this new methodology fails to recognize that annuities accrue more slowly during the first ten years of service.

> benefits payable from the Fund (other than cost-of-living increases), (2) extension of the coverage of retirement law, or (3) increases in pay upon which benefits are computed." [S.Rep. No. 93-947, at 3-4 (1974)]

The Postal Service supported the concept of the bill. Reprinted in the Committee Report is a March 27, 1973, letter from the Postal Service stating its position:

> "This legislation has been proposed on the ground that the Postal Service should operate on a financially self-sufficient basis, meeting its operating costs out of its revenues and not out of hidden subsidies. After careful consideration—and in full awareness of the financial burdens enactment of the bill will impose—the Postal Service has concluded that it is proper, as a matter of principle, for these costs to be imposed on postal ratepayers rather than the taxpayers." [S.Rep. No. 93-947, at 9 (1974)]

Thereafter, Congress enacted a number of laws dealing with other aspects of Postal CSRS funding, including legislation making the Postal Service responsible for funding the cost of cost-of-living-increases (COLAs) applicable to Postal annuities. More than one of these bills included requirements that the Postal Service make payments under schedules set by Congress.

During the period from 1974 through 2002, it was generally assumed that the various Postal payments approximated slightly less than full funding of Postal CSRS obligations. However, this was inaccurate. As noted in the Senate Report on the bill that became P. L. 108-18, *the Postal Civil Service Retirement Systems Funding Reform Act of 2003*:

> "On November 1, 2002, the Office of Personnel Management (OPM) had good news for the Postal Service (USPS). A review of USPS payments to the civil service retirement fund for pension obligations to employees on board before 1984 revealed a far more positive picture than had previously been believed. USPS--unlike any other federal agency--is required to pay into the fund an amount that approximates the full cost of its employees' participation in the Civil Service Retirement System (CSRS). Because pension investments have been earning interest at a higher rate than presumed in the statutory funding formula, OPM reported that the Postal Service's deferred liability for pension obligations was only $5 billion instead of $32 billion. According to OPM, if USPS continues to make payments based on the latter figure, the liability will eventually be over-funded by $78 billion. OPM stated that, `the major reason for the projected over-funding is due to the excess interest earned by the CSRS fund; that is, interest earnings in excess of the 5 percent that was assumed under the statutory funding method.'
>
> "Because of the potential over-funding, and the fact that needed changes in scheduled payments cannot occur without changes to existing laws, OPM sent a legislative proposal to Congress to rectify the situation, while 'protecting

> employee interests and the integrity of the [postal] retirement system.'" [S.Rep No. 108-35, at 2-3 (2003)]

That OPM proposal was enacted, with minor technical changes, as section 2 of the new law. In essence, it converted the funding of Postal benefits under CSRS to the same funding mechanism that is applicable to the Federal Employees' Retirement System. There has been confusion in some quarters as to the intent of Congress with regard to the effect of this change upon the Postal Service's obligations for cost increases due to increases in pay, but that matter is clarified by the Committee Report:

> "Because the dynamic normal cost of CSRS includes the effects of future employee pay raises and retiree COLAs, the separate payments that USPS is required to make under current law to fund the future increases in CSRS annuities that result from pay raises and COLAs would no longer be necessary. Consequently, S. 380 would repeal the provisions of law that require the Postal Service to amortize over 15 years the increases in future CSRS annuities that result from annual employee pay raises and retiree COLAs." [S.Rep No. 108-35, at 2-3 (2003)]

Thus, it is clear that the Congress had no intention to absolve the Postal Service for increases in retirement costs due to pay increases, but rather that Congress understood that the inclusion of such costs was an inherent aspect of the funding mechanism it had established.

OPM's methodology for determining USPS CSRS funding obligations was considered by the GAO in Report Number GAO-03-448R, dated January 31, 2003, which included an examination of the OPM legislative proposal enacted months later as P.L. 108-18. In particular, the GAO report "evaluated the reasonableness of OPM's methodologies for allocating estimated benefit payments and other expenses between service rendered before and after July 1, 1971, the effective date of the Postal Reorganization Act," and suggested no changes to the allocation methodology used for Postal Retirement funding.

In 2003, the Postal Service first suggested that OPM revise the methodology used to establish the appropriate division of responsibility for pre-1971 Postal employment. The matter was carefully considered by both OPM's Board of Actuaries, and by OPM. The Board of Actuaries stated:

> "The Board of Actuaries has reconsidered in detail the methodology used by the U.S. Office of Personnel Management to determine the obligations of the United States Postal Service under the United States Civil Service Retirement System. When private sector plans are transferring participants to a new employer, it is a common practice to allocate liabilities by using a method which reflects the fact that all obligations arising from future salary increases are the responsibility of the new employer. We find this approach to be the most appropriate way to determine the obligations of the Postal Service and further confirm our prior finding that this method clearly follows the intent of Congress in Public Law 93-

349."

The final OPM decision stated:

> "The Board of Actuaries has undertaken such analysis [of the methodology], and their conclusions are set forth in the enclosed letter to the undersigned. As you can see from that correspondence, the Board of Actuaries again considered OPM's methodology and approved that methodology, as well as the computation of the resulting Postal supplemental liability. The Board clearly concluded that the methodology OPM used this year is valid and follows the intent of the Act. We believe the Board of Actuaries' conclusion and OPM's concurrence with that conclusion resolves all substantive issues between our different approaches both for fiscal year 2003 as well as for future years."

Congress next revisited Postal Retirement funding with the enactment of P.L.108-435, the *Postal Accountability and Enhancement Act*, in 2006. That law provided for the Treasury to take responsibility for the cost of military service credit in the computation of CSRS annuities, resulting in a $28 billion dollar savings to the Postal Service, and relieving it from making further CSRS employer contributions based upon a percentage of salary. This change was consistent with the GAO recommendations in the January 2003 report, discussed earlier. OPM did not find any reference in the legislative history of that bill to indicate that Congress took any issue with the methodology by which OPM calculated Postal CSRS obligations. Neither did OPM find any record that the Postal Service raised any concern to Congress about OPM's CSRS allocation method at the time the 2006 legislation was being considered.

Finally, this January, the Postal Inspector General issued the report that led to this hearing.

<u>Discussion</u>

OPM's methodology is based upon long-standing public policy determinations made by prior Congresses. Its actions have been fully consistent with the letter of the law as well as all Congressional expressions of public policy on the subject.

The methodology OPM has applied to determine Postal CSRS funding is generally accepted actuarial practice and is commonly used by pension experts for plan transfers and terminations. Private pension plan transfers are usually made as part of a broader transaction, such as a corporate merger or spin-off, and are part of a negotiation as to the overall allocation of assets and liabilities. Thus the methodology used for allocating pension liabilities for any particular plan must be viewed in the broader scope of the overall asset and liability transaction between the parties. At the time the Postal Service was created in 1971, it assumed certain liabilities, such as those associated with the future retirement benefit accruals for its workforce, but it also received certain considerations, such as the existing assets of the POD.

In sum, OPM believes that the methods currently in use reflect Congressional intent and are consistent with current actuarial practice.

Health Benefits Funding

Funding of Postal Retiree health benefits is an entirely separate matter from the issue of CSRS funding. However, the two subjects are intertwined because the Postal Service wishes to utilize the savings that would result from the Postal IG's recommended approach to CSRS funding in order to satisfy the Postal Service's obligations for retiree health benefits funding.

The Postal Inspector General estimates that adoption of its recommended CSRS methodology would result in approximately $75 billion of CSRS over-funding. Under current law, any Postal surplus would remain in the Retirement Fund until the end of FY2015, when it would be transferred to the Postal Service Retiree Health Benefits Fund. Even if there were authority to transfer the funds immediately, that would not change the fact that statutory provisions require the Postal Service to make payments for current retirees' employer health benefits contributions, as well as scheduled payments of $5.5 to $5.8 billion per year, through FY 2016. Regardless of any decision to change the apportionment of responsibility for pre-1971 service, these other changes sought by the Postal Inspector General would require legislation.

Conclusion

OPM believes that the current methodology is sound public policy, appropriate in the historical context, and consistent with private sector practices. As the Subcommittee examines this situation anew and considers suggestions by the Postal IG for allocating the retirement costs associated with the pre-1971 POD employment of Postal employees, OPM will provide any technical assistance that it can. I appreciate the opportunity to appear before you today and I would be pleased to answer any questions you may have.

Mr. LYNCH. Thank you, Mr. O'Brien.

Mr. Kosar, you are now recognized for 5 minutes.

STATEMENT OF KEVIN KOSAR

Mr. KOSAR. Chairman Lynch, Ranking Member Issa, and members of the committee, the Congressional Research Service thanks you for the opportunity to participate in today's hearing. The committee and subcommittee requested CRS to submit written testimony that discusses a range of postal reform issues relating to the Postal Service's financial condition. CRS has done this.

Here my time will be used to offer some observations on the Postal Service's short-term and long-term financial challenges. These observations are drawn largely from the concluding section of my written testimony.

The short term: in the short term, the Postal Service may face a liquidity problem, possibly as early as this autumn. At the end of the first quarter of fiscal year 2010, the Postal Service had $0.8 billion in cash, which is a low level for an agency with an average weekly operating expense of over $1 billion. Unless the Postal Service runs a profit over the remainder of fiscal year 2010, it will have to borrow money to continue operations. By borrowing from the Federal Financing Bank, the Postal Service can bolster its cash in hand to about $6.5 billion. The $6.5 billion, however, may not be enough to get the Postal Service through the autumn. The agency must pay $5.5 billion into their retiree health benefits fund on September 30th, and it must pay $1.1 billion to the Department of Labor for workers compensation in October. This amounts to $6.6 billion and doesn't exclude any other costs that may come up.

Congress may wish to ask the Postal Service to provide it with a time line that clarifies just how long the agency can continue operations absent legislative action. This would help address any public concerns about the possibility of a Postal Service shut-down occurring in November, when election ballots are being mailed, or in December, when retailers are shipping billions of dollars of goods through the mail.

The long term: while the Postal Service's short-term financial condition is clearly problematic, its long-term financial condition is less obvious. In its report, Ensuring a Viable Postal Service for America, the Postal Service described its plight as a rapidly worsening crisis. The report projects a cumulative debt of $238 billion by fiscal year 2020. It is important to understand the nature of this $238 billion figure. It is not a prediction of what will happen; rather, it is a projection, an estimate of what could happen if certain assumptions hold. These assumptions are not certitude.

First, postal law caps the Postal Service's total debt at $15 billion. In order for the Postal Service to reach $238 billion in debt, Congress would need to abolish this statutory debt limit and then do nothing for 10 years. This seems improbable.

Second, this $238 billion figure assumes the Postal Service will do nothing to reduce its own expenses. This seems unlikely, as the Postal Service and PMG Potter today has stated that it intends to use its existing authorities to reduce costs by $123 billion.

Third, the report's 2020 projection heavily rests on the assumption that mail volume will fall steadily. This assumption appears to be based upon a single study by the Boston Consulting Group, which contends that the rise of the Internet has created a “fundamental and permanent change in mail use by households and businesses.”

This forecast about the future demand for hard copy mail is striking. As the figures on page 12 of my written testimony indicate, since 1930 mail volumes have grown steadily. The consultant’s forecast declares that this long-lasting trend has ended permanently.

Now, this projected 2020 scenario may be questioned on at least two grounds: first, the use of e-mail and the Internet has been growing since the mid-1990’s; yet, between fiscal year 1995 and fiscal year 2006, mail volume went up significantly. So thus far it does not appear that when the demand for electronic communications goes up, the demand for all forms of hard copy mail must go down.

Second, and relatedly, the recent drop in mail volume began about 4 months after the U.S. economy had officially entered a deep recession, so it seems at least plausible that the economic downturn, not the Internet, was the more significant factor in instigating the recent sudden mail volume declines of the past 2 years. And if that is the case, then the Postal Service’s mail volumes and hence its revenues might rise again as the economy improves.

So Congress may wish to study further the recent decline in mail volume to better determine whether this is a temporary change or, as the Postal Service contends, a permanent one.

I thank you, and I would be happy to answer any questions you may have.

[The prepared statement of Mr. Kosar follows:]

Written Statement of Kevin R. Kosar
Analyst in American National Government
Congressional Research Service

Before

The Committee on Oversight and Government Reform and the Subcommittee on Federal Workforce, Postal Service, and the District of Columbia
House of Representatives

April 15, 2010

Continuing to Deliver: An Examination of the Postal Service's Current Financial Crisis and Its Future Viability

Introduction

Chairman Towns and Chairman Lynch, and Members of the Committee and Subcommittee, on behalf of the Congressional Research Service I would like to thank you for this opportunity to appear before you today to discuss the current financial crisis and its future viability of the U.S. Postal Service (USPS).

The Committee and Subcommittee requested that the CRS discuss the USPS's report, *Ensuring a Viable Postal Service for America*, and its proposals to:

(1) cease prefunding its retiree health benefits;
(2) switch to five-day mail delivery;
(3) close post offices; and
(4) have additional flexibility in pricing and introducing products.

The Committee and Subcommittee also asked the CRS to address the recent report by the U.S. Postal Service Inspector General (IG) alleging that the Postal Service has made overpayments related to its Civil Service Retirement System (CSRS) pension responsibility.

Accordingly, my statement presents a summary of the USPS's report, and it addresses the four aforementioned USPS proposals and the recent IG study. My statement concludes with observations on the Postal Service's short-term and long-term financial challenges.

A Summary of the U.S. Postal Service Report, *Ensuring a Viable Postal Service for America*

In March 2010, the USPS released a report titled *Ensuring a Viable Postal Service for America*.[1] The report claims that due to "underlying shifts in the business of mail," the USPS expects to continue losing money—$7 billion in FY2010, and $238 billion in cumulative losses by FY2020.[2] The "underlying cause" for these losses, according to the Postal Service, is a permanent drop in the demand for hard copy mail.[3] In FY2006, the USPS delivered 213.2 billion mail pieces; in FY2010, it delivered 177.1 billion pieces (16.9% fewer).[4] The Postal Service predicts mail volume will fall to 150 billion pieces in FY2020.[5]

To mitigate its financial distress, the USPS will use its own authority to undertake two broad actions: (1) increase its revenues by expanding "products and services across targeted mail and package segments," and (2) cut its costs by reducing its delivery network, shrinking its cohort of full-time employees through attrition, and lowering its transportation and vendor-related

---

[1] U.S. Postal Service, *Ensuring a Viable Postal Service for America* (Washington: USPS, March 2010), at http://www.usps.com/strategicplanning/_pdf/Ensuring_Viable_USPS_paper.pdf.
[2] Ibid., p. 1.
[3] The USPS predicts that the demand for package delivery will be the lone exception to this trend. Demand might grow at a rate of 3% per year between FY2010 and FY2020. In FY2009, package delivery (including Priority Mail and other premium services) provides a small portion ($9.7 billion, or 14.2%) of the USPS's revenues. U.S. Postal Service, *Annual Report 2009* (Washington: USPS, 2009), p. 43, at http://www.usps.com/financials/_pdf/annual_report_2009.pdf.
[4] CRS Report R40626, *The U.S. Postal Service and Six-Day Delivery: Issues for Congress*, by Wendy R. Ginsberg, p. 13.
[5] U.S. Postal Service, *Ensuring a Viable Postal Service for America*, p. 7.

expenditures.[6] Between FY2010 and FY2020, the USPS suggests that these changes could reduce the predicted $238 billion shortfall by $123 billion.

To reduce the remaining $115 billion shortfall, the USPS argues that Congress must enact legislation to alter current postal law.[7] In particular, the USPS requests that postal law to be amended to:

(1) abolish the mandatory USPS annual payment to the Postal Service Retiree Health Benefits Fund (RHBF);
(2) remove the provision in the annual appropriation law that requires the USPS to deliver mail six days per week;
(3) permit the USPS to move more of its retail operations from post offices to private sector retail facilities (e.g., grocery stores);
(4) strengthen the USPS's power to bargain with its unions and increase the usage of part-time employees by requiring an arbitrator between the parties to consider the financial condition of the USPS in rendering decisions;
(5) increase the USPS's flexibility to price its products, especially those mail classes where postage is less than the costs to USPS to deliver them (e.g., periodicals[8] and library mail);
(6) provide the USPS with greater flexibility to offer new products by expanding the legal definition of "postal services;" and
(7) increase the USPS's ability to respond to changes in the market for its products and services by reducing the time the Postal Regulatory Commission (PRC) is permitted to review the USPS's actions and/or making the PRC's reviews post hoc.[9]

Per the Committees' request, the following sections address proposals (1), (2), (3), (5), and (6), as well as the IG's report on CSRS Pensions.

The USPS's Proposal to Cease Prefunding its Retiree Health Benefits

Sections 801 to 803 of the Postal Accountability and Enhancement Act (PAEA; P.L. 109-435; 120 Stat. 3198) changed the USPS from funding its retirees' health care costs from an out-of-pocket or pay-as-you-go basis to prefunding these obligations. To this end, the PAEA requires the USPS to pay more than $5 billion annually from FY2007 through FY2016 to build up a retirement fund from which USPS retirees' benefits will be paid starting FY2017 (**Table 1**).

Table 1. Postal Service Retiree Health Benefits Fund Payments Under PAEA

Fiscal Year	Payment (billions)
2007	$5.4
2008	$5.6
2009	$5.4[a]
2010	$5.5

[6] Ibid., p. 10.
[7] Most postal law may be found in Title 39 of the *U.S. Code*.
[8] On periodicals' failure to cover their mailing costs, see CRS Report R40162, *Postage Subsidies for Periodicals: History and Recent Developments*, by Kevin R. Kosar.
[9] U.S. Postal Service, *Ensuring a Viable Postal Service for America*, pp. 10-15.

Fiscal Year	Payment (billions)
2011	$5.5
2012	$5.6
2013	$5.6
2014	$5.7
2015	$5.7
2016	$5.8

Source: Postal Accountability and Enhancement Act (P.L. 109-435, Sec. 803; 120 Stat. 3251-3252; 5 U.S.C Sec. 8909(d)(3)(A).)

a. FY2009 payment amount of $5.4 billion was reduced to $1.4 billion with enactment of P.L. 111-68.

In FY2017, the USPS will amortize any remaining retiree health benefit obligation over a 40-year period.

On the one hand, prefunding future retirees' health benefits is prudent. Prefunding benefits can help ensure that the USPS does not default and leave its retirees without any health benefits. On the other hand, the USPS is the only federal agency required to do this, and the PAEA's ten-year payment schedule has been questioned.

The U.S. Postal Service Office Inspector General (IG), Office of Personnel Management (OPM), and the Postal Regulatory Commission (PRC) have disagreed on the size of the USPS's future retiree health benefits obligation (**Table 2**). Therefore, they came to different conclusions as to the amount the USPS should pay annually into the RHBF to adequately fund this obligation.

Table 2. Estimates of the USPS's Retiree Health Benefits Obligation and Required Annual Payments (billions)

	OPM	IG	PRC
Estimated obligation as of FY2016	$147.9	$90.5	$113.2
Required annual USPS payment	$5.5	$1.7	$3.4

Source: U.S. Postal Service Office of Inspector General and Postal Regulatory Commission.

These numbers vary greatly because each agency used different assumptions in making their calculations. For example, the IG assumes healthcare costs will rise 5% annually, while the OPM assumes they will rise 7%.[10]

The 111th Congress amended the PAEA's RHBF payment schedule by enacting H.R. 2918, the Legislative Branch Appropriations Act [of] 2010. President Barack Obama signed the bill into law the next day (P.L. 111-68). Section 164 of the law reduced the USPS's FY2009 payment to the RHBF from $5.4 billion to $1.4 billion. The legislation did not relieve the USPS of this $4

[10] Respectively, see U.S. Postal Service Inspector General, *Final Management Advisory Report–Estimates of Postal Service Liability for Retiree Health Care Benefits* (Washington: USPSOIG, July 22, 2009), at http://www.uspsoig.gov/foia_files/ESS-MA-09-001R.pdf; and Postal Regulatory Commission, *Postal Regulatory Commission Review of Retiree Health Benefit Fund Liability as Calculated by Office of Personnel Management and U.S. Postal Service Office of Inspector General* (Washington: PRC, July 30, 2009), at http://www.prc.gov/Docs/63/63987/Retiree%20Health%20Fund%20Study_109.pdf.

billion obligation; rather, it deferred USPS's payment. Come FY2017, the $4 billion will be added to whatever remaining outstanding health care obligation may exist, and will be amortized over a 40-year period.

The USPS's report proposes ending the prefunding of future retiree health benefits through annual payments. Instead, the USPS would like Congress to transfer the $75 billion in purported overfunding of its Civil Service Retirement System pension to the RHBF.[11] Doing this, the USPS contends, would ensure that future retiree health benefits are fully funded. (The CSRS issue is addressed later in this testimony.)

The USPS's Proposal to Switch to Five-day Mail Delivery

The USPS's report states that it "must have the authority to reassess and adjust the frequency of delivery" because of the recent drop in mail volume.[12] The USPS has said that it would like to end six-day delivery of mail on Saturday, as that day "has the week's lowest daily volume, and more than a third of U.S. businesses are closed."[13] Post offices would remain open for customers who wanted to purchase postal services and collect mail from post offices boxes. Possibly, some post offices will permit residential customers to pick up packages requiring a signature.[14]

Nothing in federal postal law (Title 39 *U.S. Code*) requires the USPS to deliver mail six days per week. However, since 1984 Congress has included a provision in its annual appropriation to the USPS stating that "6-day delivery and rural delivery of mail shall continue at not less than the 1983 level" (e.g., P.L. 117-111; 123 Stat. 3200). Although the precise meaning of this mandate is not clear, the USPS to date has treated the language to mean that it lacks the authority to move to five-day mail until Congress ceases including the six-day mail provision in annual appropriations.

Since 2008, three studies (two by the USPS and one by the PRC) have examined the possible financial effects of a switch from six-day to five-day delivery.[15] The studies all estimate that the USPS would save money by reducing the days of delivery from six to five, as the cost savings (largely due to reduced labor expenses) will exceed any decline in revenues due to lower demand for mail prompted by a reduced delivery schedule. The studies suggest an annual improvement to the USPS's financial condition that would be between $1.9 billion to $3.5 billion.[16]

On March 30, 2010, the USPS asked the PRC for an advisory opinion on reducing delivery to five days. By law, the USPS must ask the PRC for an opinion when the USPS "determines that there should be a change in the nature of postal services which will generally affect service on a

---

[11] U.S. Postal Service, *Ensuring a Viable Postal Service for America*, p. 11.
[12] Ibid., p. 12.
[13] U.S. Postal Service, "Five-Day Delivery" web page, at http://www.usps.com/communications/five-daydelivery/.
[14] U.S. Postal Service, *Delivering the Future: Five-Day Delivery is Part of the Solution* (Washington: USPS, March 2010), p. 13, at http://www.usps.com/communications/five-daydelivery/plan/5day_plan_delivery.pdf.
[15] U.S. Postal Service, *Report on the Universal Postal Service and the Postal Monopoly* (Washington: USPS, October 2008), at http://www.usps.com/postallaw/_pdf/USPSUSOReport.pdf; Postal Regulatory Commission, *Report on the Universal Postal Service and the Postal Monopoly* (Washington: PRC, December 19, 2008), at http://www.prc.gov/Docs/61/61628/USO%20Report.pdf; and U.S. Postal Service, *Delivering the Future: Five-Day Delivery is Part of the Solution.*
[16] CRS Report R40626, *The U.S. Postal Service and Six-Day Delivery: Issues for Congress*, by Wendy R. Ginsberg, p. 16.

nationwide or substantially nationwide basis... within a reasonable time prior to the effective date of such proposal" (39 U.S.C. 3661). Under PRC rules, a "reasonable time" is defined at "not less than 90 days" (39 CFR 3001.72). PRC Chairman Ruth Goldway suggested in a recent hearing that the PRC may require six to nine months to issue its opinion.[17]

The USPS's Proposal to Close Post Offices

In its report, the USPS states that it needs additional flexibility to close "redundant retail facilities."[18] The report does not say whether it would target post offices' where costs exceed revenues; nor does it provide a target figure for the optimum number of retail facilities that the USPS should operate.

As of FY2009, the USPS had 35,823 retail postal facilities, including post offices, post office branches and stations, community post offices, and contract postal units. This is 16.9% fewer facilities than existed in 1970 when the USPS was established as an independent establishment of the executive branch (**Table 3**).[19]

Table 3. The Number of USPS Retail Postal Facilities, FY1970 vs. FY2009[20]

Retail Postal Facility Type	1970	2009	% Change
Post Offices	32,002	27,161	-15.1%
Post Office Branches and Post Office Stations	3,869	4,828	25.3%
Community Post Offices and Contract Postal Units	7,241	3,834	-47.1%
Total	43,112	35,823	-16.9%

Source: U.S. Postal Service, *Annual Reports*, 1970-2008, and "Form 10-K," November 16, 2009.

Additionally, the report also does not explain what laws would need to be amended to accomplish this objective of fewer "redundant" facilities. 39 U.S.C. 101, which sets the nation's postal policy, states—

---

[17] Statement of Ruth Goldway, Chairman of the Postal Regulatory Commission, in U.S. Congress, Senate Committee on Appropriations, Subcommittee on Financial Services and General Government, hearing, *Hearing on the Postal Service*, 111th Congress, 2nd sess., March 18, 2010. Commissioner Goldway's statement came at minutes 91.55 to 92.15 of the hearing, a video of which may be viewed at http://appropriations.senate.gov/webcasts.cfm?method=webcasts.view&id=0ab901bd-d6f5-40c0-8f6e-49bb6fca1f69.

[18] U.S. Postal Service, *Ensuring a Viable Postal Service for America*, p. 12.

[19] CRS Report R40719, *Post Office and Retail Postal Facility Closures: Overview and Issues for Congress*, by Kevin R. Kosar, p. 8.

[20] A post office is the USPS's basic organizational unit. Generally, each post office has primary responsibility for collection, delivery, and retail operations in a specific geographic area. A post office branch is a unit of a main post office that is outside the corporate limits of the city or town of the main post office. A post office station is a main post office that is within the corporate limits of the city or town of the main post office. U.S. Postal Service, *Publication 32: Glossary of Postal Terms* (Washington: USPS, July 5, 2007), at http://www.usps.com/cpim/ftp/pubs/pub32/pub32h_p.html.

> The Postal Service shall provide a maximum degree of effective and regular postal services to rural areas, communities, and small towns where post offices are not self-sustaining. No small post office shall be closed solely for operating at a deficit, it being the specific intent of the Congress that effective postal services be insured to residents of both urban and rural communities.

Additionally, a provision in the annual Financial Service and General Government Appropriation Act declares that "none of the funds provided in this Act shall be used to consolidate or close small rural and other small post offices in [this] fiscal year" (e.g., P.L. 117-111; 123 Stat. 3200).

Postal law also requires the USPS to follow statutory procedures when it closes a post office. The USPS must "provide adequate notice of its intention to close or consolidate such post office at least 60 days prior to the proposed date of such closing or consolidation to persons served by such post office to ensure that such persons will have an opportunity to present their views" (39 U.S.C. 404(d)(1)). In deciding whether to close a post office, the USPS must consider:

> (i) the effect of such closing or consolidation on the community served by such post office;
>
> (ii) the effect of such closing or consolidation on employees of the Postal Service employed at such office;
>
> (iii) whether such closing or consolidation is consistent with the policy of the Government ... that the Postal Service shall provide a maximum degree of effective and regular postal services to rural areas, communities, and small towns where post offices are not self-sustaining;
>
> (iv) the economic savings to the Postal Service resulting from such closing or consolidation; and
>
> (v) such other factors as the Postal Service determines are necessary (39 U.S.C. 404(d)(2)(A)).

If the USPS decides to move forward with a closure, it must notify the persons served by the post office of its decision and the findings used to arrive at this decision. The USPS must wait at least 60 days before proceeding with the closure, and any person served by the post office slated for closure may appeal the closure to the PRC, which has 120 days to consider the appeal.

The PRC may fault the USPS's decision to close a post office only if the PRC finds the decision to be "(A) arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with the law; (B) without observance of procedure required by law; or (C) unsupported by substantial evidence on the record" (39 U.S.C. 404(d)(5)). The PRC may require the USPS to reconsider its decision, but the ultimate authority to close a post office rests with the USPS.

The Postal Service does not use this process for closing all postal facilities. It argues that the law applies to post offices but not post office stations or branches.[21] The Postal Regulatory Commission has criticized this interpretation of the law but has no power to require the USPS to apply the full statutory process to post office branches and stations.[22] Since postal customers frequently cannot discern the difference between a post office and a post office branch or station,

---

[21] CRS Report R40719, *Post Office and Retail Postal Facility Closures: Overview and Issues for Congress*, pp. 13-14.

[22] Postal Regulatory Commission, *Advisory Opinion Concerning the Process for Evaluating Closing Stations and Branches*, Docket No. N2009-1, March 10, 2010, pp. 52-53, at http://www.prc.gov/%28S%28ha30pf555fp1gs45di5vym45%29%29/Docs/67/67174/Advisory_Opinion_031010.pdf.

the use of a expedited process can cause confusion among the public.[23] During the past two Congresses, Representative Albio Sires has introduced two bills (H.R. 6217 and H.R. 658) that would require the USPS to use the same statutory process for the closure of post offices and post office branches and stations. One hundred Members of the 110th Congress cosponsored H.R. 6217, and 100 members of the 111th Congress have cosponsored H.R. 658 (as of April 5, 2010).

As Congress further considers the USPS's request to have increased flexibility to reduce its retail network, it may wish to ask the Postal Service to provide further clarification as to what types of facilities it may close, what public input and notification processes it intends to use, and which laws would need to be amended to provide this flexibility.

The USPS's Proposals to Have Additional Flexibility in Pricing and Introducing Products

The USPS report argues that the Postal Service lacks sufficient authority to set its prices in response to "market dynamics." The USPS proposes altering some of the ratemaking policies enacted in the 2006 Postal Accountability and Enhancement Act.

The PAEA streamlined the former postage-pricing system and increased the USPS's discretion over pricing. The law separates the USPS products into "market-dominant" and "competitive" classes. Market-dominant products make up the bulk of the mail-stream and the USPS's revenues. These products are called "market-dominant" because few if any private sector competitors exist to provide these products and services.[24] Market-dominant products include (1) first-class mail letters and sealed parcels, (2) first-class mail cards, (3) periodicals, (4) standard mail, (5) single-piece parcel post, (6) media mail, (7) bound printed matter, (8) library mail, (9) special services, and (10) single-piece international mail (39 U.S.C. 3621).[25]

The PAEA established a rate cap on postage increases for market-dominant products (39 U.S.C. 3622(D)(1)(a)). The USPS may raise the rates (prices) of any market-dominant product by no more than the annual increase of the Consumer Price Index for All Urban Consumers (CPI-U).[26]

The USPS wants this price cap revised to apply only to market-dominant products as an entire class, rather than to individual market dominant products. If given this authority, the USPS could raise the postage rates of one or more market-dominant product (e.g., periodicals) more than the CPI-U, and keep the dominant class as a whole under the CPI-U by holding steady or lowering postage rates for other market-dominant products.

The apparent objective of this proposed change to rate-setting would be to empower the USPS to raise rates on those mail classes (non-profit mail, media mail, library mail, periodicals, etc.) that

[23] The Postal Service has admitted this occurs. See "Direct Testimony of Alice M. Vangorder on Behalf of the United States Postal Service," *Postal Regulatory Commission, Docket No. N2009-1*, p. 4, footnote 2, at http://www.prc.gov/Docs/63/63567/FINAL.VANGORDER.W.ATTACH.pdf.
[24] E.g., the USPS possesses a legal monopoly over the delivery of first-class mail (18 U.S.C. 1693-1999 and 39 U.S.C. 601).
[25] Competitive products include those for which a competitive market exists. They include (1) priority mail, (2) expedited mail, (3) bulk parcel post, (4) bulk international mail, and (5) mailgrams (39 U.S.C. 3631). The prices of competitive products are not rate-capped.
[26] On the CPI-U, see CRS Report RL30074, *The Consumer Price Index: A Brief Overview*, by Brian W. Cashell.

currently cost the USPS more to deliver than their postage.[27] In FY2009, these money-losing mail classes cost the USPS at least $1.7 billion.[28] Both the 1970 Postal Reorganization Act (84 Stat. 760) and the 2006 PAEA (120 Stat. 3201) require all mail classes to cover their costs.[29] However, this requirement probably never has been met because federal postal law (36 U.S.C. 3622 and 39 U.S.C. 3626) also provides for "reduced rates" for certain classes of mail (e.g., non-profit mail, media mail, periodicals, etc.)

Thus, in addition to requiring the PAEA's provisions to be amended, the USPS's proposal for pricing flexibility would require amending 39 U.S.C 3622 and 39 U.S.C. 3626.

The IG's Report on CSRS Pensions[30]

On January 20, 2010, the U.S. Postal Service Office of Inspector General (IG) published a report on the USPS's funding of pension costs for postal workers who were employed by both the U.S. Post Office Department (prior to 1971) and its successor, the U.S. Postal Service.[31] The report criticizes the allocation of the pension costs between the USPS and the federal government for employees who had service both as employees of the Post Office Department and later as employees of the Postal Service.

The IG report notes that the Postal Service is currently responsible for meeting all pension costs under the Civil Service Retirement System (CSRS) for employees hired after 1971. For employees with service both before and after 1971, the federal government and the Postal Service share responsibility for CSRS pensions. The federal government pays for service through 1971, and the USPS pays for service after 1971.

The IG report contends that the allocation of CSRS costs between the USPS and the federal government is unfair because the Postal Service is fully responsible for increases in pension costs that result from pay raises granted after 1971. Because CSRS pensions are based on both an employee's years of service and the average of an employee's highest three consecutive years of pay, pension costs rise as employee pay rises. As a consequence, the percentage of CSRS pension costs allocated to the USPS for an employee who worked for both the Post Office Department and the USPS is greater than the proportion of the worker's career that he or she spent as an employee of the USPS. The IG report notes, for example, that for a person who worked for the Post Office Department for 20 years prior to 1971 and for the USPS for 10 years thereafter, the USPS is obliged to fund about half of this person's pension costs. (The other half is paid for by the U.S. government.)

---

[27] U.S. Postal Service, *Ensuring a Viable Postal Service for America*, p. 14.

[28] Postal Regulatory Commission, *FY2009 Annual Compliance Report* (Washington: PRC, March 29, 2010), p. 28, at http://www.prc.gov/prc-docs/home/whatsnew/ACD%20Report_2009_FINAL_Combined_747.pdf. This $1.7 billion figure only refers to attributable costs; if institutional costs were included, the figure would be higher.

[29] Specifically, postal law requires each mail class to cover its "attributable cost." The term "attributable cost" refers to the cost to the USPS to process a particular class of mail. This is to be contrasted with the term "institutional cost," which refers to the fixed costs of the USPS (e.g., the compensation of a mail carrier, who delivers all classes of mail). The law does not require each mail class to cover its institutional cost.

[30] The author thanks Patrick Purcell, Specialist in Income Security, Domestic Social Policy Division, Congressional Research Service, for his assistance in writing this section.

[31] U.S. Postal Service Office of Inspector General, *The Postal Service's Share of CSRS Pension Responsibility*, RARC-WP-10-001 (Washington: USPSOIG, January 20, 2010) at http://www.uspsoig.gov/foia_files/RARC-WP-10-001.pdf.

The IG report suggests that the USPS's share of CSRS pension costs should be proportional to employees' length of service as USPS employees relative to their total length of service with the Post Office Department and the USPS. If an employee had spent 15 years as an employee of the Post Office Department and 15 years as an employee of the USPS, for example, the federal government and the USPS each would be responsible for half of the cost of that individual's CSRS pension. The IG's report estimates that under the current method of allocating the costs of CSRS pensions, the Postal Service has paid $75 billion more into the Civil Service Retirement and Disability Trust Fund than it would have paid if costs were divided between the federal government and the USPS strictly in proportion to length of service.

In 2004, the Postal Service requested the OPM, which administers the Civil Service Retirement System, to reconsider the method by which it allocates CSRS pension expenses between the Postal Service and the U.S. Treasury. The OPM denied the request on the grounds that the allocation method it had developed was consistent with federal law. The OPM cited P.L. 93-349 (July 12, 1974), which required the USPS to finance all increases in retirement liabilities that are attributable to salary increases granted by the USPS. The House committee report accompanying the bill that was enacted as P.L. 93-349 (H.R. 29, 93rd Congress) states that the "purpose of this legislation is to clearly establish the responsibility of the U.S. Postal Service to finance increases in the liability of the Civil Service Retirement and Disability Fund, caused by administrative action of the Postal Service, as apart from increases in unfunded liabilities which are incurred by act of Congress." The committee report further states that with respect to any increase in CSRS pension expense that results from future pay raises received by USPS employees, "the cost of this liability should properly and equitably be borne by the Postal Service."

A reduction in the proportion of CSRS pension expenses allocated to the Postal Service would increase the unfunded liability of the Civil Service Retirement and Disability Fund. Absent a reduction in the cost of financing CSRS pensions, changing the allocation of CSRS pension expenses between the Postal Service and general fund of the U.S. Treasury is a zero-sum game. A reduction in the amount of CSRS pension expenses allocated to the USPS would result in an equal increase in CSRS pension expenses borne by the U.S. Treasury.

On March 2, 2010, the Postal Regulatory Commission said it will conduct its own review of the USPS's pension liability.[32]

Conclusion: Short-term and Long-term Challenges

The USPS has asked Congress to alter a number of provisions of current postal law because these statutes are viewed as impeding the USPS's ability to stem its financial losses. As Congress considers the USPS's proposals and other options, it may wish to consider the USPS's financial condition within the frameworks of the short-term (now until FY2011) and the long-term (now until 2020).

Short-term

The USPS has run significant deficits since FY2007 and may reach its statutory debt limit ($15 billion) in FY2011 (39 U.S.C. 2005(a)).

[32] Postal Regulatory Commission, "PRC Initiates Review of USPS Pension Liability," press release, March 2, 2010, at http://prc.gov/prc-docs/home/whatsnew/PRC%20Review%20of%20USPS%20CSRS%20liability_604.pdf.

Additionally, the USPS may face a liquidity problem at the end of FY2010 or the beginning of FY2011. The USPS's FY2010 first quarter financial filing (10-Q) indicates that its financial position is unenviable. The USPS went from having $4.1 billion to $0.8 billion in cash, which is a low level for an agency with an average weekly operating expense over $1 billion. In part, this decrease in available cash was an effect of the USPS's retiring some of its debt. The USPS reduced its debt by $2.7 billion, from $10.2 billion (as of the end of FY2009) to $7.5 billion.[33]

Unless second quarter revenues exceed second quarter expenses, the USPS will have to borrow money to continue operations. Since the USPS finished FY2009 with outstanding debt of $10.2 billion, it is permitted by law to finish FY2010 with $13.2 billion in debt. So, at the end of its first quarter (December 31, 2009), the USPS could borrow up to an additional $5.7 billion from the Federal Financing Bank (FFB) to help it cover its operating expenses.[34] Combining this with the $0.8 billion that it already had, the USPS could have begun the second quarter with $6.5 billion in cash.

Yet, it is questionable whether even this amount of cash will suffice. If one were to assume the USPS financially will break even for the rest of FY2010 (which the USPS itself doubts) and it can retain this $6.5 billion in cash, the USPS still may face a cash shortage at the beginning of FY2011. The agency must pay $5.5 billion to the Retiree Health Benefits Fund on September 30, 2010, and pay $1.1 billion to the Department of Labor for workers' compensation in October 2010.[35]

In its FY2010 first quarter 10-Q filing, the USPS stated that in the event of a liquidity crisis it would pay less than the required amount into the Retiree Health Benefits Fund.[36] The consequences of the USPS failing to abide by the PAEA's mandated payment schedule are unclear; the PAEA is silent on this matter.

Of the four proposed USPS changes to postal law considered in this written testimony, only two would appear to be capable of addressing the USPS's short-term financial challenge—reducing the USPS's annual payment to the RHBF, and permitting the USPS to draw back some of its contributions to the CSRS pension.[37]

Long-term

In its report, the USPS described its plight as a "rapidly worsening crisis," and claimed that the USPS "will continue to face declining volume, stagnant revenue, large fixed costs, and rising workforce costs. Without additional action to address these trends, the Postal Service would face annual losses as great as $33 billion by 2020."[38] The USPS suggests it might suffer cumulative losses of $238 billion between FY2010 and FY2020.

---

[33] Ibid., pp. 4, 10-11.
[34] Since the USPS ended FY2009 with $10.2 billion in debt, by law it may conclude FY2010 with debt of up to $13.2 billion. Current debt of $7.5 billion + $5.7 billion in new debt = $13.2 billion in maximum permissible debt at the end of FY2010.
[35] U.S. Postal Service, "Form 10-Q," pp. 8-9.
[36] Ibid., p. 9.
[37] This does not exhaust the options for Congress. It might pursue other measures, such as providing an emergency FY2010 appropriation to the USPS, raising the USPS's debt limit, or an amalgam of policies, such as providing the USPS with additional debt authority but requiring that a portion of that authority be used to fund an effective USPS employee retirement incentive program.
[38] U.S. Postal Service, *Ensuring a Viable Postal Service for America*, p. 6.

While the USPS's short-term financial condition is clearly problematic, its long-term financial condition is less obvious. The USPS report's admonition of a possible $238 billion in cumulative debt by 2020 has been repeatedly mischaracterized as a "prediction" by the media.[39] The report's admonition of $238 billion in cumulative losses is a projection—an estimate of what could happen if certain assumptions hold over the next decade. These assumptions are not certitudes.

First, as noted earlier in this testimony, postal law caps the Postal Service's total debt at $15 billion. For the USPS to reach $238 billion in cumulative losses would require a change in current circumstances. Congress would need to abolish the USPS's statutory debt limit, and then do nothing for 10 years as the USPS borrowed $231 billion from the U.S. Treasury. (As of the end of FY2010 quarter one, the USPS had $8 billion in debt, and $1 billion in cash. Hence, the USPS would need to borrow $231 billion to achieve $238 billion in cumulative debt.)

Second, the $238 billion in cumulative losses could occur only if the USPS took no further actions to reduce its expenses. This is implausible, especially as the USPS's plan states that it intends to use its own existing authorities to reduce the projected $238 billion shortfall by $123 billion (leaving a projected $115 cumulative debt).

Third, the report's 2020 projection assumes that mail volume will continue to fall, sliding another 15% over the coming decade. In this scenario, the USPS's annual revenues would be no higher in 2020 than in FY2010. This assumption of falling mail volumes is based upon a study commissioned by The Boston Consulting Group (BCG).[40] According to the BCG's analysis, the USPS

> will experience profound declines in its volumes of mail.... Notably, volumes will not revisit the high-water-mark of 213 [billion] pieces in 2006—on the contrary, the trajectory for the next 10 years is one of steady decline, which will not reverse even if the current recession abates.[41]

The major cause of this decline, according to the BCG, is the movement of communications to the World Wide Web.

According to the BCG's analysis, the recent mail volume declines of the past two years should not be viewed as primarily an effect of the nation's general economic downturn. Instead, as the USPS puts it, the recession simply "accelerated the volume decline," which is the result of a "fundamental and permanent change in mail use by households and businesses."[42]

This prediction about the future demand for hard copy mail is striking as it would mean the end to an at least 80-year long trend. Since 1930 mail volumes have grown nearly every year, the exception being during the period of 1933 to 1936 when mail volume plunged one year then returned to its previous height over the succeeding three years (**Figure 1**). The BCG prediction would have the USPS of 2020 delivering slightly less mail than the USPS of 1987 (**Figure 2**).

---

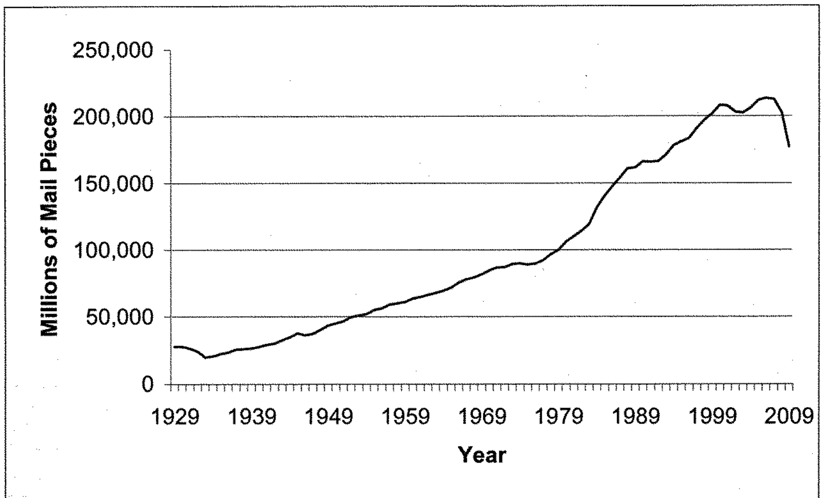
[39] E.g., "A $4.8 million study made public on March 1 predicts the Postal Service will lose $238 billion over the next decade as consumers and businesses conduct more transactions online." Donna Leinwand, "Senators Challenge U.S. Postal Service's 10-Year Rescue Plan," *USA Today*, March 18, 2010, at http://www.usatoday.com/news/washington/2010-03-18-postal-service-hearing_N.htm.

[40] The Boston Consulting Group, *Projecting US Mail Volumes to 2020: Final Report—Detail* (BCG: March 2, 2010, at http://www.usps.com/strategicplanning/_pdf/BCG_Detailed%20presentation.pdf. See also The Boston Consulting Group, "Projecting Mail Volumes to 2020," March 2, 2010, at http://www.usps.com/strategicplanning/_pdf/BCG_Narrative.pdf.

[41] Ibid., p. 2.

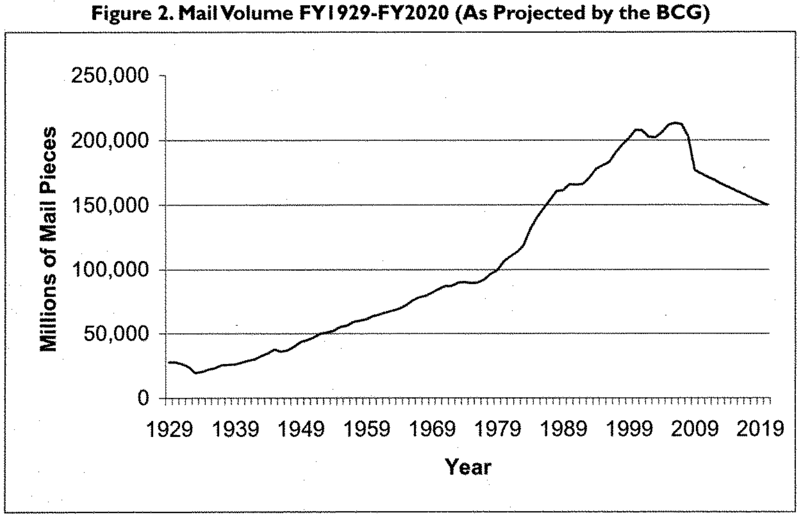
[42] U.S. Postal Service, *Ensuring a Viable Postal Service for America*, p. 4.

Figure 1. Mail Volume, FY1929-FY2009



Source: U.S. Postal Service Historian, "Pieces of Mail Handled, Number of Post Offices, Income, and Expenses, 1789 to 2009," at http://www.usps.com/postalhistory/PiecesofMail1789to2009.htm.

Figure 2. Mail Volume FY1929-FY2020 (As Projected by the BCG)



Source: U.S. Postal Service Historian, "Pieces of Mail Handled, Number of Post Offices, Income, and Expenses, 1789 to 2009," at http://www.usps.com/postalhistory/PiecesofMail1789to2009.htm; and The Boston Consulting Group, "Projecting Mail Volumes to 2020," at http://www.usps.com/strategicplanning/_pdf/BCG_Narrative.pdf.

A critic of the BCG's projected 2020 scenario might raise two points.

First, the movement of communications to the World Wide Web has been occurring since the mid-1990s. During this time, the composition of the mail volume changed—less of the mail sent was first-class mail, and more of it was advertising mail. Yet, the total amount of mail sent rose. So, thus far it does not appear that there is a simple inverse relationship between the demand for electronic means of communications and hard copy mail volume. (I.e., if demand for electronic communications goes up, demand for hard copy communications must go down.) Indeed, as noted earlier, the BCG's analysis shows demand for USPS package delivery rising between 2010 and 2020.

Second, the USPS's mail volume peaked in FY2006 at 213.1 billion mail pieces, and was nearly the same in FY2007. In the first two quarters of FY2008 (October through December and January through March), mail volume was higher than in the same quarters in FY2007. It was not until the third quarter of FY2008 (April through June) that the USPS reported a decline in mail volume relative to the same quarter in the previous year.[43] By the end of FY2008, mail volume had dropped from 212.2 to 202.7 billion mail pieces. The U.S. economy entered a recession in December 2007, and mail volume began falling four to six months later. It seems at least plausible that the economic downturn, not electronic migration, was the more significant factor in instigating the sudden mail volume decline of the past two fiscal years.[44] And if that is the case, then arguably the USPS's mail volume might rise again as the economy improves. (The BCG's analysis and the USPS's report do not admit this possibility. Both unequivocally declare that the demand for sending hard copy mail has been permanently weakened in the past two or three years.)

Hence, Congress may wish to further study the recent declines in mail volume to see if the BCG and the UPS are correct that total mail volume is likely to fall during the next decade, or if the demand for only certain classes of mail can be expected to drop. Knowing whether the USPS likely faces a 2020 future with mail volumes of 150, 200, or 250 billion mail pieces would appear to be an important factor in determining whether to significantly alter the structure of the USPS.

That said, it is worth noting that the USPS likely does face long-term financial challenges, although neither the magnitude of the challenges nor the timeline for their onset and maturation is clear. The Government Accountability Office (GAO), for one, long has warned that the USPS faced financial difficulties due to its limited ability to control its labor costs and reduce its mail processing and delivery network.[45]

Moreover, the recent developments in communications technologies may be undermining the nation's stated rationale for having a U.S. Postal Service. The 1970 Postal Reorganization Act declared the USPS was "to bind the Nation together through the personal, educational, literary, and business correspondence of the people." Because of e-mail, cellular phones, and the World Wide Web, personal communication via hard copy mail has declined. As The Boston Consulting Group's analysis indicates, only 4.5% of FY2009's 177 billion mail pieces were person-to-person letters or postcards. Periodicals, which may include educational and literary content, make up 4%

---

[43] U.S. Postal Service, "Revenue, Pieces and Weight" reports for Postal Quarter IV FY2007 through Quarter I FY2008, at http://www.usps.com/financials/rpw/welcome.htm.
[44] CRS Report R40198, *U.S. Economy in Recession: Similarities To and Differences From the Past*, by Marc Labonte, p. 1.
[45] Government Accountability Office, *U.S. Postal Service: Bold Action Needed to Continue Progress on Postal Transformation*, GAO-04-108T, November 5, 2003.

of the mail. Most of the mail volume today consists of advertising mail and business-related correspondence.[46]

Thank you.

[46] The Boston Consulting Group, *Projecting US Mail Volumes to 2020: Final Report—Detail*, p. 5.

Mr. LYNCH. Thank you, Mr. Kosar. I actually want to thank all of the witnesses. This was a very impressive and credible group, very competent group of witnesses, and I appreciate your willingness to come before the committee and help us with our work.

Let's get right to it. I will yield myself 5 minutes.

How do we resolve this difference between OPM and the Postal Service regarding what is owed here? I mean, I understand it from a basic point of view that there should be some type of equity in divided service, that the Postal Service should not be asked to pay more than its share in an employee who had divided service between the old department and the new. This seems to be a basic sense of fairness in that, and I think that was more or less Congress' intent, speaking quite over-simplified.

How do we resolve this difference? It is a huge number, $75 billion, and it is made much more important, given the urgency of the Postal Service's situation right now.

Mr. Williams, how do you think we should resolve this?

Mr. WILLIAMS. Congress directed that OPM and OMB and the Postal Service go into a room and try to decide and try to resolve the differences, and it could be that there are a number of solutions to this. The simplest, the easiest would be to reset the two funds. There are other alternatives.

The emergency arises from the $7 billion annual payment. I think that needs to be dealt with first, and then I think the funds can be reset in a way that doesn't devastate the Federal fund, which would be a bad thing, but recognizes that the postal employees and the mailers have paid in enough. The funds are fully funded, and it is time to stop putting money into them.

The same thing happened back in 2002 when we realized there was a mistake and we were about to over-fund by $78 billion. As soon as that payment disappeared, OPM showed up and tried to introduce a new bill for us to pay military pensions. Obviously, we don't have a military, and the Government is already financing its military.

I think the first thing to do is to remove the emergency and stop the bleeding, and then sort out, in the fullness of time, which of the solutions before us is the right solution.

Mr. LYNCH. Mr. O'Brien.

Mr. O'BRIEN. Yes. Just to comment, I mean, one of the difficulties in this issue is that we tend to move between two funds. The CRS, the funding for the retiree benefits, not your health benefits but your retiree benefits, is essentially fully funded right now. That is not in question. The $7 billion payment to the fund that is referred to is actually the payments to the retiree health benefits they are separate issues, and they are real easy to conflate the two.

So part of it is, though, $7 billion payments are in the law, $5 billion of them are—last year OPM, with Congress, reduced those payments from roughly $5 billion to about $1.5 billion, and those two issues continue on. The challenge again with the retiree benefits as we do this is simply changing the scope of the retiree and saying we are going to fund those less. This kicks this down the can a bit.

One of the complicated parts from our end is that these are not sort of stand-alone issues. The implications of the decisions you make regarding how we fund the retiree service will affect how you fund the retiree health benefits, which have larger budgetary implications.

Ms. GOLDWAY. If I might just add that there is an opportunity to look solely at the health care retirement benefit fund issue and look at how to recalculate what that total payment should be. Should it be the 75 percent approximately of estimated liability? Is the liability the right amount? And what should the payments be over a period of years?

I believe that it certainly is possible to come up with a very credible arrangement to significantly reduce the payments that the Postal Service is obligated to make on a yearly basis by looking solely at the decisions around that health care retirement benefit fund, reducing the liability and spreading out the payments. I think that is an alternative, as well, that needs to be considered.

Mr. LYNCH. Thank you.

Mr. Kosar, I don't assume you have a horse in this race, but——

Mr. KOSAR. Absolutely not. No horse within this race.

I am not an expert on pensions, and so I won't try to offer any solutions.

Mr. LYNCH. Have you looked at this for CRS, though? Have you looked at this?

Mr. KOSAR. Yes. I provide an overview in my report.

Mr. LYNCH. What do you think?

Mr. KOSAR. I don't recall any accusation of OPM's current approach as being against the law, and in which case, if it is not against the law, then it is an equity question, and an equity question inevitably is going to involve lots of calculations that inevitably, I think, are probably going to be political; namely, it will have to go to the judgment of Congress to see what it thinks fair.

I think a key point is that, as best I can tell, this is a zero sum gain. If the Postal Service is allowed to, say, claw back some of that $75 billion, then somebody else is going to have to pony that up, and that somebody else I believe would be the U.S. Treasury or the public.

Mr. LYNCH. The problem is, though, it is the work hours of the individuals who have earned that, and so they are entitled to the full measure of the benefit that they have earned, and as well the mailing community has paid in for service for which it appears they have over-paid.

My time has expired and I yield to the gentleman from Utah, Mr. Chaffetz, for 5 minutes.

Mr. CHAFFETZ. Thank you, Mr. Chairman.

Thank you all for being here.

Mr. Chairman, I do agree with you that we do need to come to some sort of consensus as to what the accurate numbers are so we can all deal from the same playing field. I hope we can ferret that out as we go along.

Chairwoman Goldway, I am quite frankly and directly, deeply concerned by your testimony and the perception, perhaps, that you have of your role and responsibility. I find your testimony to be shocking, quite frankly, that you would inject so much subjective analysis, if you can call it that, as opposed to participating in my understanding of the Postal Regulatory Commission's role and responsibility. You are the regulatory body and regulatory head of this type of agency. The statements that I read within your testimony are very subjective, and I am very curious to understand why and how you think it is within your duties and responsibilities to inject that sort of personal testimony.

Let me give you an example here. You say in your testimony, "The consultants hired by the Postal Service and the GAO analysis should have begun by looking at what it will take to keep open as many post offices and stations and branches as possible." Why would you—you are coming to a conclusion by yourself without allowing the process to move forward, and I believe, based on your role and responsibility, coming up to a conclusion without allowing them to do the analysis. Why and how? Where do you think in the Regulatory Commission's responsibilities that is the type of statement that you should be making?

Ms. GOLDWAY. I appreciate your concern. I believe that the law requires that the Postal Regulatory Commission define and enforce the universal service obligation. We have to make a report on it. We determine that every year with our compliance determination. Is the Postal Service meeting its universal service obligation?

There are two specific areas in which the Postal Regulatory Commission doesn't have discretion. One is the law that says post offices can't be closed for solely economic reasons, and, two, that service has to be provided 6 days. So I feel that the responsibility of any agency that is operating under the law is to address their problems assuming that they have to meet the law before they then provide other alternatives, and I felt——

Mr. CHAFFETZ. Thank you. Let me read another statement from you.

Ms. GOLDWAY [continuing]. The consultants didn't do that.

Mr. CHAFFETZ. In your written statement here, "Now is not the time for sweeping changes to the Postal Service." How can you come to that conclusion? You went on to say that we need to deal with the—"before the Congress agrees to major cuts in service, it should resolve the pension and retiree benefit issues to determine manageable payment schedules for the Postal Service, and the Commission should be allowed to complete its analysis of the 5-day delivery proposal and present it to you."

Now, the numbers, based on what we hear now, we are dealing with a $238 billion shortfall over 10 years. We are talking about a $75 billion issue. It is a significant issue, it is a big issue, but it won't solve all of the issues. And we talk about moving from 6-day delivery to 5-day delivery, based on the testimony of Postmaster General Potter, in its best-case scenario that is going to be a $30 to $36 billion fix over a 10-year period, only accounting for about 15 percent of the problem.

So if we have such a significant problem, by the hundreds of billions of dollars, how do you, at the beginning of this process, come to the conclusion that "now is not the time for sweeping changes at the Postal Service?" When do you think we should get to sweeping changes at the Postal Service?

Ms. GOLDWAY. What I am proposing, which I don't think is very different from some of the colleagues here on the panel with me, is that——

Mr. CHAFFETZ. Well, they have different jobs. They have different jobs, roles, and responsibilities.

Ms. GOLDWAY. Well, I believe that the Postal Service could meet its obligations for the year with an adjustment to the health care retiree benefit fund.

Mr. CHAFFETZ. You think that would solve the entire problem?

Ms. GOLDWAY. I don't think it will solve the entire problem, but I think it will provide us, given that and the economic turn-around, an opportunity to come up with proposed changes that are of greater acceptance to the country and that meet a universal service obligation. You, yourself, are concerned about cutting 6 to 5-day——

Mr. CHAFFETZ. Yes, I have a different job, role, and responsibility than you do as a regulator.

Ms. GOLDWAY [continuing]. And my written testimony includes, in reviewing the 6 to 5-day issue, which the Commission will be doing and doing very thoroughly, that we would consider such things as a pilot project or alternatives and——

Mr. CHAFFETZ. Let me move on. Let me read another quote from you.

Ms. GOLDWAY [continuing]. And we would consider that.

Mr. CHAFFETZ. I am going to move on, please.

Quote: "But ask the small towns of America if they think the Government business should be conducted in Wal-Mart. Why would any rational person compare the functions of a post office to Wal-Mart as the Postal Service consultants did?" I do not understand why or how you are injecting your personal opinion. Are you speaking for yourself? Are you speaking for the administration? Are you speaking for the Postal Regulatory Commission?

Ms. GOLDWAY. I am certainly using the opportunity to speak as the chairman with my own point of view.

Mr. CHAFFETZ. So this is your personal point of view? It is not from the Postal Regulatory Commission?

Ms. GOLDWAY. In my testimony I have a specific line in terms of the Commission's support for adjusting the health care retiree benefit fund, and that is a Commission position.

Mr. CHAFFETZ. And you don't think the——

Ms. GOLDWAY. And I have pointed out that the Commission will be reviewing the 6 to 5-day delivery and making a considered opinion on it. But I do, quite frankly, feel that the Postal Service's response to its universal service obligation to provide service through post offices, offering a substitute which would allow those services in some fashion or another to be provided at a Wal-Mart and close post offices in communities is not an acceptable part of the responsibility of the universal service obligation, and I don't think that is in violation of the law, and I think it is certainly consistent with my role as chairman to lead the Commission in evaluating what universal service is.

Mr. CHAFFETZ. Well, Mr. Chairman, my time has expired. I appreciate it. I am deeply concerned by these personal conclusions prior to the analysis and the recommendations of what has to be a creative process, and I hope we further explore this.

I thank you for the time and yield back. Thanks.

Mr. LYNCH. I thank the gentleman.

The Chair recognizes the gentleman from Virginia, Mr. Connolly, for 5 minutes.

Mr. CONNOLLY. I thank the Chair, and, gosh, I am surprised that my friend who is so concerned about personal conclusions would cite a bogus number, $238 billion. We have already established in this hearing at best that is a theoretical number. GAO admits, and the Postmaster General, himself, admitted under questioning by this Member that it assumes they are not going to make the $123 billion cuts he announced this morning they are going to make, and so it is a made-up number designed to scare us into breaking faith with communities across the United States, breaking faith with organized labor and the work force, breaking faith with consumers in order to make decisions they have decided a priori they want to make, irrespective of whether there is an empirical basis to justify making those decisions or not. That is what that $238 billion figure is—it is made up. It assumes nothing will happen. Nothing will happen over 10 years.

Mr. Kosar, you detailed this really well in the CRS report. Could you refresh our memories, going to page 11 of the CRS report? I assume that is your writing?

Mr. KOSAR. Correct. Are there particular aspects on it, or is it the three main points? Are there particular aspects of the point I made, or just kind of generally encapsulate what I was getting at here?

Mr. CONNOLLY. Well, if I recall your analysis, it says in order to believe $238 billion, you have to believe, A, this Congress will lift the statutory debt ceiling limit, right?

Mr. KOSAR. Correct.

Mr. CONNOLLY. Which right now is $15 billion?

Mr. KOSAR. Correct.

Mr. CONNOLLY. Second, you have to assume this Congress will take no action whatsoever for 10 years with respect to any kind of fiscal red ink problem the Postal Service might experience; is that correct?

Mr. KOSAR. Correct.

Mr. CONNOLLY. Absolutely no action?

Mr. KOSAR. Absolutely no action.

Mr. CONNOLLY. Third, you would have to assume that the $123 billion of cuts that the Postmaster General announced today and said is already within his authority, he doesn't need new legislation or legislative authority to make those decisions, will, in fact, be rescinded, will not be made; is that correct?

Mr. KOSAR. Absolutely correct.

Mr. CONNOLLY. And then you would have to assume that everything goes to hell in a handbasket. Apparently, there is no economic recovery that could influence up or down the volume of mail, even though we know from history that, as a matter of fact, the opposite is true: economic conditions most certainly do influence whether mail goes up or down volume; is that not correct?

Mr. KOSAR. That is correct.

Mr. CONNOLLY. Other than that, the $238 billion number is real.

Mr. KOSAR. Depends how you define real, I suppose.

Mr. CONNOLLY. Would you refresh our memory, Ms. Goldway, in terms of the statutory role of the Postal Regulatory Commission?

Ms. GOLDWAY. The Postal Regulatory Commission is a regulatory body overseeing the activities of the Postal Service to ensure that it does provide universal service at a fair and efficient level for all citizens. We provide an annual compliance determination every year, and should we determine that they don't meet universal service obligations we can institute proceedings to require them to change their activities to meet universal service obligations.

Mr. CONNOLLY. Apparently, because we don't like some of your testimony, we want to relegate it to the realm of personal opinion. Does the statute in any way invite the Postal Regulatory Commission to comment on proposals with respect to quality of service or fiscal savings? Is that a role under the statute for the Postal Regulatory Commission?

Ms. GOLDWAY. Yes. Our reports do that and we are asked to do studies, to report to Congress, to suggest legislation, and to make changes in—suggest changes in the universal service obligation over a period of up to 10 years.

Mr. CONNOLLY. Were you invited here today in your capacity as chairman of that Commission?

Ms. GOLDWAY. Yes, I was. Thank you.

Mr. CONNOLLY. And did the committee ask you to, in fact, share your views on the pending proposals, good, bad, and indifferent, with respect to savings and cost efficiencies?

Ms. GOLDWAY. Yes, they were. Thank you.

Mr. CONNOLLY. Thank you.

Thank you, Mr. Chairman.

Mr. LYNCH. I thank the gentleman.

The Chair recognizes the gentleman from Illinois, Mr. Davis, for 5 minutes.

Mr. DAVIS. Thank you very much, Mr. Chairman.

I want to thank the witnesses for being here.

Chairwoman Goldway, let me just kind of followup with you. Mr. Potter has made a series of recommendations that he thinks would help get us beyond the dilemma that we are in. Has the Commission taken any position on any of those? Or let me ask it another way——

Ms. GOLDWAY. I don't think the Commission has been in a position to take a formal action on any of these proposals. They are not presented to us in a way in which we would act upon them formally. But I have consulted with my colleagues, and we have agreed that we, all five of us, believe that the health care retiree benefit fund should be adjusted, so that I can speak on behalf of the whole Commission with regard to that position.

With regard to 6 to 5-day delivery, we are in the process of hearing that case and are committed to having a full and open discussion where we will hear all points of view and consider all of the concerns that were raised here at the congressional hearing this morning and many others. In particular, we are going to look at the question about how much cost savings there really will be. There is a dispute between the initial figures we had, and the Postal Service's, about how much savings you could have from closing post offices—excuse me, from 6 to 5-day delivery.

So we will thoroughly review that, and I hope we will be able to make a considered advisory opinion to the Postal Service on what we believe is the right way to go, and we will share that opinion with the Congress, and our hope is that you will wait to hear our opinion and advice and the expert testimony that we can develop in that case before making your own decision about whether to change from 6 to 5-day.

Mr. DAVIS. It would appear to me that some of these, as I look at them, really aren't that difficult to—for example, shift in retail sales to some place other than a facility doesn't seem to me to create that much angst.

Ms. GOLDWAY. I don't think anyone is concerned with increasing the amount of stamps that are sold at supermarkets and expanding as much as possible the access to Postal Services on line, but you can't ship a parcel out of a supermarket and you can't do it online. The law says anything over 13 ounces has to be handed personally to the post office. You can't get your passport that way. You can't do a whole range of special services that are integral to the universal service of the Postal Service at a grocery story unless the Postal Service is presenting a plan to open a full retail facility in a supermarket. They haven't presented that plan to us, and if that is an option to substitute for post offices, I don't think the Postal Service would—I don't think the Postal Regulatory Commission would feel that was any change at all in universal service.

So the question is the level of service that is currently provided that we feel represents universal service for the country, and to make sure that is maintained.

The one other thing I would say is that there are many post offices around the country, not just in the smallest rural towns but in many areas, that see the post office as a neighborhood icon, and as an anchor for other economic activities in their community, and for you to close that post office and move it into a big box retailer at the suburban fringe of the city is not——

Mr. DAVIS. Let me just ask Mr. Kosar, though——

Ms. GOLDWAY [continuing]. Something that most people would support.

Mr. DAVIS [continuing]. A question before my time runs out. I appreciate it.

Mr. Kosar, how important do you think it is that we stabilize the service on a short-term basis as we pursue long-term solutions?

Mr. KOSAR. Well, my understanding is essentially that once the Postal Service runs out of cash that it can't keep operating. I don't know of any sort of emergency line that it would be able to access. It is possible it exists, but I have never heard of it spoken of, and if it doesn't have the cash, then I don't know how it could go forward meeting payroll and continuing operations.

Mr. DAVIS. So it is absolutely essential that we continue to operate while we pursue long-range solutions that might take much more time?

Mr. KOSAR. Whether Congress decides to choose to pursue a short-term solution or a long-term solution or a solution that is a hybrid that can do both is not for me to call, but if Postal Services are to be continued, as I understand it, the liquidity issue will have to be dealt with.

Thank you.

Mr. DAVIS. Thank you very much. Thank you, Mr. Chairman.

Mr. LYNCH. Thank you.

Let me ask Chairman Goldway, Section 701 of the Postal Accountability and Enhancement Act requires that the Postal Regulatory Commission present recommendations to Congress and the President for legislative changes or improvements to the postal law by December 2011.

Ms. GOLDWAY. Yes.

Mr. LYNCH. Still a ways away, but have you begun that process?

Ms. GOLDWAY. Well, I initiated a study to help us pursue the notion of the social value of the mail, and we want to flesh that concept further.

Mr. LYNCH. So you are not very far along the road then?

Ms. GOLDWAY. And then we will combine that with our next universal service obligation study, which we probably will do within the next year.

Mr. LYNCH. Yes. Well, time's a-wastin'.

Ms. GOLDWAY. I appreciate your interest.

Mr. LYNCH. We are going to have some changes.

Ms. GOLDWAY. I will try to get a——

Mr. LYNCH. Yes. You might want to ramp up that part. It says you need to make it by December 2011. That is the drop-dead date. But you can certainly make it before, and I think the circumstances would probably dictate that you would probably want to make those recommendations sooner rather than later.

Mr. Williams, you indicated that Congress had directed you and OMB and OPM to go in a room and hash this thing out. Have you gone into that room?

Mr. WILLIAMS. We would not represent the Postal Service. There has been an initial——

Mr. LYNCH. Well, yes. OK.

Mr. WILLIAMS [continuing]. Meeting, and it involved the principals and some staff, and I think they are now preparing for a second round of talks to try to come to agreement on which of the solutions would be the proper solution for the issues.

Mr. LYNCH. Yes. This $75 billion question, we have to fish or cut bait here.

Mr. O'Brien, what would happen if the post office didn't make the payment to OPM?

Mr. O'BRIEN. Again, for the retirement services the payments have already been made. The retirement fund is fully funded, or virtually fully funded at this time. What the IG report suggested was that if you change the allocation methodology that has been used, funds would be freed up from the retirement pension system that could go to other purposes specifically to address the health retirement fund. So, again, the two funds are somewhat——

Mr. LYNCH. Are you talking about the annual payments?

Mr. O'BRIEN. The annual payment is for the retirement health fund. If those payments are not made, specifically what would be the issue in terms of the retirement payment. I need to get back to you on the health fund. But, again, I want to stress that the retiree fund and the benefits to retirees for their retirement payment, those are funded, or virtually fully funded right now, and there is no threat to a retiree getting their retiree pension.

Mr. LYNCH. Right. Right. We are talking about the imbalance of payments relative to service here. I must confess I sort of come down on the side of the Postal Service on this argument, at least the way it has been argued thus far. I would just encourage you to reconcile. We will just be following you on that line of progress, OK?

I will yield to the ranking member.

Mr. CHAFFETZ. Thank you, Mr. Chairman.

Mr. Kosar, I want to make sure I understood you properly. I mean, part of the challenge that is before the Postal Service is the economic downturn that is happening in this country, but to what percentage or to what degree do you also acknowledge the move to e-commerce and electronic communications and those types of things? Is that part of what you have looked at along the way? I just notice that you kind of didn't mention that portion of it, and it just raised some curiosity, that is all.

Mr. KOSAR. Sure. And I apologize for any omission. It, I think, is pretty clear that the most lucrative postal product amongst the mail classes, first class mail, is being eroded by e-commerce. People are switching to electronic bill paying, and so your high-margin product—and first class mail is a high margin product because it is sealed against inspection, you need a warrant to open it, not like lower classes of mail.

Mr. CHAFFETZ. Right.

Mr. KOSAR. So that is being eroded, and that is a long-term trend, and I think it is perfectly believable that trend will continue, and that creates an interesting revenue situation.

At the very end of my written testimony, I note that there—I mention this because there is a changing composition to the mail volume. More and more of it is becoming advertising mail, which is a lower margin product, and so that has revenue implications, and it also has policy implications because the Congress created the Postal Service to deliver mail for a number of purposes—literary, binding up the Nation, etc.—and if it is only delivering mail in 2020 for business purposes, well, it is a different scenario.

Mr. CHAFFETZ. OK. So Chairwoman Goldway said, “Now is not the time for sweeping changes to the Postal Service.” If we don't have any changes, what is the effect?

Mr. KOSAR. I don't know, because everything is so contingent upon the mail volume question. Mail volume equals revenue, and revenue versus cost is——

Mr. CHAFFETZ. Do you see e-commerce declining over the course of time? Do you see us moving less? I mean, do you see us doing less e-commerce and less electronic communication?

Mr. KOSAR. No, I don't see us doing less e-commerce. I would presume we would do more and more absent some sort of peculiar incident.

Mr. CHAFFETZ. Right.

Mr. KOSAR. An attack on our cyber system. But the relationship between the growth in e-commerce versus hard copy mail demand strikes me as rather complex. I don't know if the PRC has studied and tried to figure out how the elasticities work, but, just based upon the historical data, I don't see a clear relationship.

Mr. CHAFFETZ. But if we don't do anything, based on historical data that we have now, the trajectory is not very pretty, is it?

Mr. KOSAR. The trajectory of mail volume or the trajectory based upon a financial——

Mr. CHAFFETZ. The trajectory of financial situation, financial viability of the Postal Service.

Mr. KOSAR. Yes. I would be—realizing the large payments going forward that are required under the Postal Accountability and Enhancement Act, these are very significant payments, and I know that the Postal Regulatory Commission has suggested that instead of $5.5 billion a year the Postal Service should be paying $3.4 billion, and the Inspector General has suggested $1.9 billion. This has large cumulative effects over the long run, and so yes, I think it is an issue to be addressed.

Mr. CHAFFETZ. Interestingly enough, as the mail volume has decreased, we see this 80 percent labor cost is not necessarily diminished. It is such a huge portion of what is going on. My understanding is that this 80 percent number, even though the volume has gone down, has not certainly been adjusted. Can you give further insight or things that you found in terms of the labor cost as a ratio to the overall expenses, and the implications of that, because you are going to have to deal somehow, some way, with these massive labor costs, are they not?

Mr. KOSAR. If the Postal Service must either control or lower its costs over the long term, then obviously the large target is the labor cost, because, as you noted, and as GAO has noted, it is about 80 percent. And the Postal Service has had some success in contending with this. I know since fiscal year 1999 they have reduced the size of their work force from over 900,000 to just under 600,000. Of course, many of these people are moving into being retirees, and so there is that obligation.

Mr. CHAFFETZ. Right.

Mr. KOSAR. But at least in terms of salaries, that is lowering it.

Mr. CHAFFETZ. Right.

Mr. KOSAR. But their options are rather limited because they have collective bargaining agreements with the vast majority of these groups, and I believe at least two if not three of the contracts forbid layoffs. Of course, they have other provisions in there which curtail the Postal Service's ability to excise what they consider to be extra persons.

Mr. CHAFFETZ. OK. Thanks, Mr. Chairman. I am right near the end of my time. Thanks.

Mr. LYNCH. Thank you.

Let me ask, we had asked the Postal Service, as part of their presentation, part of their report that was delivered today, to actually look at comparable mail systems and what other countries are doing, and that part has not been included. They are going to do that a little bit later, although Mr. Potter did offer a few suggestions anecdotally.

I know that one of the Scandinavian countries, I think it might be Sweden or Finland, has a system in place now where you can actually, it is like a virtual mailbox. Your computer screen, whether it is a laptop or even a BlackBerry or desktop, you can actually click on your mail that is at the post office and you can actually click on the stuff you want delivered. I don't like the term junk mail, but you can also flag stuff for non-delivery; in other words, you don't want it delivered.

It just seems a matter of time until that type of technology software is going to be available to the American public. If mail volume has dropped already, I can imagine what is going to happen when we have that type of technology available to us. It is certainly not going to go up.

Have you thought about the implications, Ms. Goldway especially. You seem to have an optimistic view of what the future might hold for normal mail.

Ms. GOLDWAY. Well, since I spent 4 years in Finland, I will just comment that this experiment that the Finns are doing is in one of what they call their big cities, which is about 200 people. It is a small experiment that they are trying on this product. But the Finns are way ahead in terms of technology, and it certainly may catch on there.

I was speaking with the head of Deutsche Post yesterday and they still provide 6-day delivery, and what they were valuing most about their mail was the privacy of the mail. E-mail does not provide privacy.

Mr. LYNCH. What is the cost for a——

Ms. GOLDWAY. It is 80 cents.

Mr. LYNCH. Eighty cents.

Ms. GOLDWAY. They pay 80 cents, and it is a smaller country. The delivery costs are less. I am sure that they are making more profit on their mail than we do.

They haven't had billing in their mail for 20 years, so the declines they have had are much smaller, the European declines. Every country is quite different. But what struck me was his argument that the letter carried against inspection is of such value in a country that has experienced the political regimes that they had in the 20th century, the Nazis and then the eastern Germany regimes, and you cannot have a system, at least not yet, and it doesn't look likely, an e-mail system where person to person you have the same privacy. We now have systems where you can bank with fairly good security systems. There are walls and protections. But person to person correspondence is simply very risky on the Internet.

So I think there are still great values for the mail we have, and in my testimony the first thing that I suggested the Postal Service do—I certainly don't want them to stand still—is to change the focus from volume to value, and if they create a series of products that are of great value to people in the mail, they are more likely to get the high margins they need to keep the mail system and the other services that are part of the universal service available to people.

Mr. LYNCH. I understand what you are saying, but——

Ms. GOLDWAY. And, by the way, in regard to European comparisons——

Mr. LYNCH. Let me——

Ms. GOLDWAY [continuing]. We are intimately involved with those.

Mr. LYNCH. Will you just let me speak?

Ms. GOLDWAY. I am sorry.

Mr. LYNCH. The person to person mail, though, is microscopic in the current mail system, people sending letters to each other. It is really a microscopic part of the——

Ms. GOLDWAY. It is about 5 to 6 percent of the mail, and when you consider what the potential is for growth in small businesses, which are quite comparable in terms of the transactions that are happening—and everyone agrees that there is a great deal of growth potential in small businesses.

Mr. LYNCH. I think business has remittances and commercial activity.

Ms. GOLDWAY. No. Think of all the people who are setting up businesses in their homes, and in addition to the electronic communications that they have there, there is personal correspondence, individual pieces of material.

Mr. LYNCH. I know. Yes. Businesses can be located in a home. That is still a business, though.

Ms. GOLDWAY. It is still a business, and——

Mr. LYNCH. It is just a different driver than——

Ms. GOLDWAY [continuing]. And it can——

Mr. LYNCH [continuing]. Social interaction.

Ms. GOLDWAY. Yes. And it can create volume, but I think it would be volume—if the Postal Service focuses it right, it is volume that is of high enough value that you can charge more for it and keep your margins up so you don't have to rely on advertising mail.

Mr. LYNCH. OK. My time has expired.

As I understand, we are about to have votes. I want to thank you all for your willingness to come before this committee and help us with our work. We, I am sure, are going to have more hearings on this and more discussions. Thank you for your cooperation and your assistance. Have a good day.

[Whereupon, at 1 p.m., the subcommittee was adjourned.]

[The prepared statements of Hon. Gerald E. Connolly and Hon. Diane E. Watson, and additional information submitted for the hearing record follow:]

Statement of Congressman Gerald E. Connolly

"Continuing to Deliver:

An Examination of the Postal Service's Current Financial Crisis and its Future Viability"

April 15th, 2010

This is an opportune time to hold a hearing, as there are some misconceptions that this Committee has a responsibility to correct, misconceptions rooted in a Postal Service campaign to proscribe its public services in a manner that could be devastating to its customers and employees. We will hear testimony today about a falling sky, first from Postmaster General Potter and second from the Government Accountability Office (GAO). Mr. Potter will claim that USPS is on the verge of insolvency and that the only way to avert disaster is to curtail services dramatically and impoverish its workforce. GAO, taking at face value the recommendations of three well-compensated private consulting firms who were retained by USPS, will affirm the Postal Service's claim that only draconian cuts in services and wages can save the Postal Service. Fortunately, we will also hear from the Congressional Research Service and the Postal Regulatory Commission about balanced options for reform that protect consumers, businesses, and employees. In response to this very real fiscal crisis, we can no longer use ad hoc cost cutting to protect the Postal Service, but rather must construct a whole new business model.

Let us start from the very beginning. Article 1, Section 8 of the Constitution provides Congress with the power to establish Post Offices and Post roads, demonstrating the Founders' cognizance of the importance of convenient communication to facilitate commerce and develop national identity. The notion that such services are incidental or unimportant to the nation is inconsistent with our most important founding document. This is the first problem with the Postal Service's assumption that the only way to solvency is to cut service and employee benefits.

The second problem with the Postal Service's focus on service cuts is that it does not address *increased* revenue in a balanced manner. Yes, as the Postal Service suggests we must grant greater pricing authority for market-dominant products. Unfortunately, the Postal Service dismissed the possibility of new revenue sources without sufficient investigation of the possibility for new revenue sources. Recognizing that many aspects of USPS services are cost-negative, we must allow the Postal Service to make money in other areas, even if that means creating competition with existing private enterprises.

The third problem with the Postal Service's proposal is that it assumes employees can suffer pay cuts with no associated costs to the federal government or society generally. To the contrary, slashing wages and benefits for Postal Service employees would have dramatic negative impacts on our communities, employee productivity, and the federal government. Postal Service proposals to reduce wages and benefits through unprecedented regulation of arbitration would impoverish federal employees and represent a departure from eighty years of labor policy dating to passage of the Wagner Fair Labor Standards Act.

Finally, the Postal Service seems to assume the worst case scenario for future revenues, as Kevin Kosar notes in his Congressional Research Service written testimony. The Postal Service's assertion that it may face a cumulative $238 billion shortfall, Mr. Kosar notes, "could occur only if the USPS took no further actions to reduce its own expenses," an eventuality that he correctly describes as "implausible." Mr. Kosar also documents historical data showing that increasing internet traffic does not always correlate to declining mail volume, in contrast to what the Postal Service's consultants have implied. In fact, the possibility of stabilizing mail volume after this recession could avert the need for the deepest cuts recommended by the Postal Service. The specter of disaster should not compel us to rush into poorly designed restructuring legislation when more accurate revenue projections and more comprehensive plans could avoid the most painful decisions that the Postal Service would have Congress make blithely.

There is no absence of guidance on more thoughtful long range planning for the Postal Service. The distinguished Chairwoman of the Postal Regulatory Commission, Ruth Goldway, makes a sensible suggestion in her written testimony: Undertake a "detailed, innovative new retail strategy." Instead of just cutting service, let us embark together on an effort that will explore creative new revenue sources with the goal of protecting that Constitutionally-mandated service upon which our constituents rely. Chairwoman Goldway also makes several suggestions for new revenue, including voting by mail, which would have the added benefit of strengthening our democratic process.

One creative proposal that Ms. Goldway mentions is replacing gasoline with electric delivery vehicles, which the Postal Service Inspector General and GAO say could create a new "vehicle to grid" revenue source. I appreciate Ms. Goldway's support for my bill, the Postal Service Electric Motor Vehicle Act, to replace the aging gasoline fleet with state of the art electric vehicles. It is a shame that the Postal Service, in its zeal to cut, has not adequately explored the alternatives recommended by the Chairwoman of its regulator. Not surprisingly, in light of Ms. Goldway's thoughtful and apparently unwelcome suggestions, one of the Postal Service's recommendations is to curtail the Postal Regulatory Commission's authority.

Such an exploration of new retail strategies could provide critical support to the Postal Service's customer base: American businesses. Businesses, not individuals, provide 90% of the Postal Service's mail-based income stream. Companies ranging from Netflix to local newspaper weeklies rely on regular mail. At a recent forum hosted by Chairman Steven Lynch, one member after another of the Coalition for a 21st Century Post Office expressed their concerns about reducing mail service. This business organization recognizes that cutting service will not only harm our constituents, but also reduce business opportunities associated with high quality service. For example, how will weekly papers distributed by mail fare if their readers can't receive them on the weekend? Will Netflix be able to maintain its customer base? Will magazine companies be able to maintain their demand if readers can't receive Time and other periodicals on Saturday? We must consider the impact of Postal Service policy on the business climate before rushing into major restructuring, with the understanding that businesses pay far more for postage than any other part of the Postal Service's customer base.

Thank you again, Mr. Chairman for this timely hearing. There is no better time to reorient the Postal Service away from a myopic effort to cut costs in a manner that would permanently cripple a public service envisioned by this country's founding fathers. This requires a new business model in the future.

Opening Statement

Congresswoman Diane E. Watson

"Continuing to Deliver: An Examination of the Postal Service's Current Financial Crisis and its Future Viability"

Full Committee on Oversight and Government Reform
Thursday, April 15, 2010
2154 Rayburn HOB
10:00 A.M.

Thank you Mr. Chairman and Chairman Lynch for working together on today's important joint hearing on the economic sustainability and long-term strategic plan of the United States Postal Service. This hearing occurs at a critical time, as the Postal Service faces a dire financial situation that must be addressed, but for which there is no simple or singular solution.

In recent years the transition to electronic communications combined with the economic recession has

lead to a severe decline in mail volume. Due to these losses the Postal Service lost $3.5 billion in 2009, is projected to lose another $7.8 billion in 2010, and without comprehensive long-term action, total cumulative losses are projected to reach $238 billion by 2020.

While all stakeholders are in agreement that the Postal Service is on an entirely unsustainable path, there is not the same level of consensus regarding how to solve the crisis. Media accounts have focused on the debate over whether to reduce service to only 5-days of delivery, while internally deliberations have focused on the burdensome payment structure of the Postal Service's retiree health benefits and the Civil Service Retirement System pension fund. As this debate continues over how to craft a viable long-term strategic plan it is important that the needs of the Postal

Service's customers are kept in mind, the reality of economic conditions are considered, and that the collective bargaining rights and needs of the Postal workforce are respected.

I look forward to hearing the testimony of today's witnesses, and I sincerely hope that these proceedings will bring us closer to the development of an acceptable, long-term, comprehensive plan to preserve the quality and viability of the United States Postal Service.

Thank you Mr. Chairman, and I yield back the remainder of my time.

Hearing before the Committee on Oversight and Government Reform and the Subcommittee on the Federal Workforce, Postal Service, and the District of Columbia
United States House of Representatives

OFFICE OF
INSPECTOR
GENERAL
UNITED STATES POSTAL SERVICE

Written Statement
On
Continuing to Deliver: An Examination of the Postal Service's Current Financial Crisis and its Future Viability

April 15, 2010

David C. Williams
Inspector General
United States Postal Service

Mr. Chairman and members of the Committee, I appreciate the opportunity to submit my written testimony concerning the overcharge of the United States Postal Service (Postal Service) for its Civil Service Retirement System (CSRS) obligations. This issue has a significant impact on the Postal Service's financial viability, its compliance with the Postal Accountability and Enhancement Act (PAEA), and thus its ability to provide world-class universal service to the nation.

On July 1, 1971 the United States Post Office Department (POD), then an agency of the federal government, became the Postal Service, a new self-financing independent government entity. Although the Postal Service is self-financing, it is subject to the Office of Personnel Management (OPM) for health care and pension obligations. The administration of these programs resulted in the Postal Service being overcharged four separate times.

Congress has continually untangled and corrected funding problems:

- In 2002, it was discovered that the Postal Service's pension fund would be overfunded by $78 billion. Congress corrected this in 2003.
- In 2003, the Postal Service was made responsible for $27 billion in military service pension obligations for Postal Service employees. Congress corrected this in 2006.
- In 2009, we found that the OPM used an exaggerated 7 percent health care inflation forecast instead of the 5 percent industry standard, resulting in an overpayment of $13.2 billion by 2016. In response Congress urged the Postal

Service to coordinate with the OPM and the Office of Management and Budget to develop "a fiscally responsible legislative proposal."

Lastly, the Postal Service pension fund was overcharged $75 billion, so that employees could retire at promised levels. When the POD became the Postal Service, employees that belonged to the federal pension fund now contributed to the Postal Service. Retirement costs were divided according to the number of years employees had belonged to each fund. However, the federal pension fund paid for retirements based on 1971 salaries, not final salaries. The federal pension fund collected full contributions, but paid only partial benefits.

The OPM has explained that these mischarges were in response to what they believed to be the will of Congress expressed in 1974 legislation. However, the 1974 language was repealed by Congress in 2003, when large overpayments were discovered. At that time the OPM inexplicably had not detected a 41 percent overfunding error in this $190 billion pension fund. Congress directed the OPM to use its authority to oversee the reforms using accepted "dynamic assumptions" that include pay increases and inflation. The OPM switched to dynamic funding for the Postal Service portion, but did not for their share. The Postal Service was forced to pay the $75 billion difference.

In 2009 my office began working with the Hay Group, an actuarial firm, to review the OPM's CSRS methodology and found that it unfairly burdens the Postal Service:

- In calculating the federal government's share, the OPM methodology assumes that all salary inflation after 1971 should be paid by the Postal Service instead of being divided with the federal pension fund and associated with the respective years of service. This has caused the Postal Service to be overcharged $75 billion for its share of the CSRS pension payments. In essence, for almost 40 years the Postal Service paid all of its and all of the federal government's share of inflationary costs.

- It is instructive that the OPM in this case ignores its own formula which includes final salary and inflationary adjustments for federal and military funds to determine Postal Service pension benefits.
- The OPM methodology of calculating the federal fund's share was constructed using a "freeze frame"[1] approach which allows the federal government to escape the effect of salary increases mostly due to inflation and the growth of the economy on pension costs in violation of accepted accounting practices. It is completely unrealistic to assume employees would receive no pay adjustments for almost a 40-year period, yet the OPM uses just such a methodology in paying its share for former POD employees. This does not comply with the use of dynamic assumptions that the OPM was directed to use in 2003.
- Using the OPM methodology, an employee who worked 15 years for the POD and 15 years for the Postal Service causes the Postal Service to be responsible for 70 percent of the pension obligation, while the federal funds share would be 30 percent, instead of an even division.

[1] To assume former Post Office Department employees retired in 1971 and received no inflationary salary adjustments or the use of a final salary.

- In 2004 the Postal Service appealed the OPM's methodology and it was denied by OPM. Their denial relied on repealed 1974 legislation that made the Postal Service responsible for the pension costs of salary increases. The new legislation in 2003 directed the OPM to abandon the 1974 legislation and use "dynamic assumptions" that include inflation and pay increases. This is the same methodology the OPM uses with its other funds including the cost of retiree health care premiums for the Postal Service.
- A methodology based on dynamic assumptions — the same methodology the OPM uses to split the cost of retiree health care premiums between the Postal Service and the federal government — would comply with accepted accounting standards. That proposal would finally align the pension and health care methodologies for the OPM.
- Using dynamic assumptions, the federal government and the Postal Service would each be responsible for 50 percent of the pension obligations for an employee who worked half their career for the federal government and half for the Postal Service. The current methodology relies on the Postal Service to pay all of its pension obligations and much of the federal government's share.

Lastly the Postal Service was given a funding target of 100 percent for both pension and health care pre-funding. In contrast the OPM has pension funding premium levels of 41 percent for federal employees and 24 percent for the military. The OPM's own health care prefunding for federal employees is 0 percent. The Standard & Poor's 500 companies' (S&P 500) pension funding is 80 percent.

Correcting <u>either</u> the overcharge <u>or</u> the target pre-funding level would result in the ability to pay off the Treasury debt associated with meeting the overcharges. Annual costs and premiums could be financed out of the interest earnings and surplus. PAEA has a provision to monitor fund levels annually to determine if contributions are adequate to meet target levels.

The vision of the Postal Service in the PAEA was to create a more corporate entity subject to efficient market forces. That cannot be done if the Postal Service continues to be subjected to annual payments of more than $7 billion a year before it enters the market place. Mr. Chairman, I would be hard pressed to name a corporation that could do well in the market place if $7 billion a year were taken from it before it could open its doors for business. The current overcharges of $75 billion have been seen by many in the mailing industry as an unauthorized tax on Americans. Ironically the postal trade press has termed this the "stamp tax."

The mischarges should be backed out and fund balances reset to proper levels to achieve the retirement reforms Congress enacted in 2003. In addition, another option for the Postal Service could be to use the $75 billion to pledge to the retiree <u>health</u> fund instead of making payments. The details concerning the 3 possible solutions can be found in the appendix.

Timely action by Congress and the OPM will provide the Postal Service immediate relief from this financial burden, but it will not wholly close the financial gap. Almost $4 billion will remain to be dealt with by the Postal Service through the reduction of 93 million workhours in FY 2010. Based on the latest projections, the Postal Service is on pace to cut the necessary workhours as they try to meet the loss.

APPENDIX:
My office would like to elaborate on three alternative solutions to correct the excessive pre-funding levels. Our first solution is designed to correct the OPM's current CSRS pension funding methodology that has overcharged the Postal Service $75 billion from 1972 to 2009. This can be simply fixed by taking the following steps:

- First, the Postal Service's CSRS pension obligations should be calculated using a years-of-service methodology to allow for the return of the $75 billion the Postal Service has already overpaid and going forward.
- Second, $10 billion of the $75 billion CSRS surplus should be used to pay off the Postal Service's Treasury debt, since this debt was incurred making payments to pre-fund retiree health care. This would save the Postal Service over $150 million a year in debt service.
- Third, another $10 billion of the CSRS surplus should be used to pay the total outstanding CSRS pension liabilities, which have increased over its life.
- Fourth, transfer the remaining $55 billion of the CSRS surplus to the retiree health care fund. The $55 billion combined with the already set aside $35 billion will provide a retiree health care fund of $90 billion. The OPM has determined that $87 billion is needed to fully fund the Postal Service's retiree health care liability as of 2009. In addition, under the PAEA any CSRS pension surplus is already scheduled to be transferred to the retiree health care fund at the end of 2015. We propose that the schedule be accelerated so that the transfer occurs immediately.

- Fifth, stop the required payments of more than $5 billion under the PAEA because the account would be funded. This would allow the Postal Service to use the fund for its intended purpose to pay this year's $2 billion retiree premium.
- Most of these simple changes only advance the timing of provisions already in existing law and do not fundamentally alter the funding structure established by the PAEA. The Postal Service's pension and retiree health care obligations would be determined with the same methodology. The Postal Service's pension and retiree health care obligations would be fully funded; unlike the federal government that relies on federal pension funding of 41 percent, military pension funding of 24 percent, federal retiree health benefits at 0 percent and military retiree health benefits at 29 percent.

As I said before, there is no established funding goal. An established goal by Congress of around 80 percent as suggested by the S&P 500 and my office would allow for a second solution to the $75 billion overcharge to the Postal Service for its share of the CSRS pension payments from 1972 to 2009. This solution would be optimal if the $75 billion could not be repaid to the Postal Service. This solution would consist of four parts:

- First, the Postal Service's pension fund obligation would be reduced from 100 percent to about 80 percent. This would make about $52 billion available to the Postal Service.
- Second, $10 billion of the $52 billion should be used to pay off the Postal Service's Treasury debt, since this debt was incurred making payments to

prefund retiree health care. This would save the Postal Service over $150 million a year in debt service.

- Third, transfer the remaining $42 billion to the retiree health care fund to achieve more than an 80 percent funding level.
- Fourth, stop the required payments of more than $5 billion under the PAEA because retiree health care would be funded. This would allow the Postal Service to finally use the funds and its interest income for its intended purpose — paying for retiree health care.

The third solution could be used once the OPM acknowledges the Postal Service's $75 billion overpayment to the CSRS pension fund. This overpayment should not be incorrectly categorized as a "surplus," as the Postal Service is *immediately* entitled to this overpayment. The surplus CSRS funds, on the other hand, are due to the Postal Service on September 30, 2015, and will be comprised of any excess funds that exist once the CSRS pension is fully funded.

An OPM acknowledged $75 billion overpayment becomes an asset of the Postal Service which allows the Postal Service to pledge the excess retiree pension funding to the retiree health fund instead of making payments. The Postal Service can acquire this asset to pledge through the Treasury's issuance of a bond on behalf of the OPM that is payable to the Postal Service. A special Treasury bond, without market value, issued to the Postal Service would allow the Postal Service to pledge this bond (asset), pursuant to 39 C.F.R. § 2005(b) (1) to satisfy its retiree health fund obligations.[2] Under 39 USC 2005(b),

> *"The Postal Service may pledge the assets of the Postal Service and pledge or use its revenues and receipts for the payment of the principal of or interest on obligations issued by the Postal Service under this section, for the purchase or redemption thereof, and for other purposes incidental thereto, including creation of reserve, sinking and other funds which may be similarly pledged and used, to such extent and in such manner as it deems necessary or desirable…."*

The $75 billion Treasury bond, at some undetermined time in the future, would result in a transfer of actual funds to the retiree health fund obligations. This transfer could be coordinated with the PAEA mandated 2015 transfer of funds between the retiree pension fund and the retiree health fund.

---

[2] The issuance of an interagency debt instrument is exemplified by the arrangement between the Social Security Administration (SSA) and the Treasury.

- The surplus SSA tax revenues are maintained in a SSA Trust Fund which, like the Postal Service Fund, is an off-budget fund.
- Because the Treasury had spent SSA's tax-generated revenues, it has since provided SSA with $2.5 trillion in special-issue Treasury bonds that SSA may redeem, as necessary, when its annual tax revenues no longer cover its disbursements.
- This fiscal year, SSA will begin redeeming some of its Treasury bonds.

Post-Hearing Questions for the Record
Submitted to PMG John E. Potter

"Continuing to Deliver: An Examination of the USPS's Current Financial Crisis and Its Future Liability"

April 15, 2010

Q1. GAO's April 12 Report discusses the fact that *the Postal Accountability and Enhancement Act of 2006* provided the Postal Service with increased flexibility with respect to entering into contracts with mailers.

a) How many domestic market dominant negotiated service agreements has the Postal Service entered into since the passage of that law?

The Postal Service is, and has been, involved in ongoing discussions with mailers, both those who use our competitive and market-dominant products, about possible Negotiated Service Agreements (NSA) and innovative pricing and product solutions. Although we remain open to developing and implementing new NSAs with customers of our market-dominant products, we have not been able to craft a structure that satisfies our customers and still provides a compelling business case for the Postal Service since the implementation of the *Postal Accountability and Enhancement Act.*

b) Do you believe entering into these types of contracts will increase volume and revenue for the Postal Service?

In certain circumstances, yes. There are cases where the necessarily broad-brush approach used in setting list prices can be fine-tuned to provide better incentives to individual mailers, and in some of these cases, the additional contribution generated by this fine-tuning could make a meaningful difference to the Postal Service. However, in practical terms, it may be a more efficient use of resources to develop pricing structures that improve the incentives to groups of mailers, rather than individual customers.

Q2. Are you concerned that reducing service to 5-day delivery might significantly increase the trend in the amount of mail that will move to electronic alternatives? If so, how do you propose to deal with that possibility?

No. We do not expect to see significant decreases in mail volume due to implementing five-day delivery operations. We believe any increase in the amount of mail moving to electronic alternatives would, for the most part, occur independent of five-day delivery. In fact, we expect a moderate increase in volume in 2011 as the anticipated economic recovery begins to positively affect the mail. However, it is likely that this increase will be temporary. Over the next decade, mail volume is expected to decrease as electronic diversion continues to negatively affect First-Class Mail. Total mail volume is expected to be 150 billion

mail pieces in 2020, which represents a 15 percent decrease from the 2009 volume of 177 billion.

Our conclusion that mail volume will not significantly decrease due to the implementation of five-day delivery operations is based on qualitative and quantitative market research conducted on behalf of the Postal Service by Opinion Research Corporation from August to October 2010. Most consumers and small businesses in the qualitative market research said that elimination of Saturday delivery to street addresses and the collection of mail on Saturday would have little impact on their use of the mail. They said they would adapt to the change. This is not to imply it would have no impact. Rather, they will adapt by mailing on days other than Saturday. Or they will use alternatives, including the Internet. Most felt that as long as Post Offices were open on Saturday, they would be able to adapt.

Most small businesses said that they had a regular routine for receiving and sorting mail Monday through Friday when they are open or when they normally handle mail. Elimination of Saturday delivery would not affect these small businesses. Almost all larger businesses said that they would accept five-day delivery operations as being necessary to help solve the Postal Service's financial problems. They said they would be able to adapt if given a sufficient lead time of up to six months.

That customers would adapt to five-day delivery operations is confirmed in the quantitative market research. It shows that the impact of implementing five-day delivery operations would be a reduction of -0.7 percent of total volume or 1.238 billion pieces, most of it First-Class Mail. The loss in contribution resulting from this loss of volume would be almost $200 million. This includes the loss of mail volume to electronic alternatives and is not significant overall.

Of course, we continue to work to increase mail volume and are doing everything we can to make that happen within the current law. Here are a few of the actions we are now taking to increase mail volume.

- We are now, and plan to continue advertising Priority Mail. We launched a new campaign connected with "Toy Story 3" this month.

- We have launched innovative First-Class Mail and Standard Mail sales programs where mailers receive a rebate on postage based on their use of the mail.

- We are reconstructing our website, *usps.com*, to make it easier for customers to use the Postal Service online. This effort will result in increased revenue as users of postal products and services will be able to do more on *usps.com*.

- We are increasing the value of letter and flat mail by using advanced technology — our Intelligent Mail Barcode — to offer visibility and tracking of this mail. These strategies are designed to encourage businesses to continue using the mail.

- **We are exploring new products to help advertisers make better use of mail.**
- **We are exploring offering remittance mailers new pricing for their bills where they would pay the one ounce price, currently 44 cents, for items that weigh up to 1.2 ounces if they achieve a volume threshold.**
- **We have several initiatives to make it easier to mail greeting cards, including a 64 cent butterfly stamp for non machineable cards and a planned test of postcards with a prepaid postage indicia which will be counted using IMb technology.**

Q3. Since one of your suggested cost-cutting measures is to reduce the size of the workforce, please describe the steps you are taking to encourage retirement and early retirement of employees.

A more flexible workforce would better position the Postal Service to respond to changing demand patterns. Through 2020, about half of the current workforce (roughly 300,000 employees) will be eligible to retire. The large number of expected retirements, coupled with upcoming labor negotiations, presents a unique window of opportunity to establish a more flexible workforce while minimizing personnel impact.

In 2009, we offered retirement incentives to eligible employees represented by the American Postal Workers Union (APWU) and National Postal Mail Handlers Union (NPMHU), and more than 20,000 employees accepted the offer. At present, given our deteriorating financial situation and the large number of retirement eligible employees service-wide, we do not plan to offer any incentives.

Q4. Have you considered allowing mailers to advertise using unaddressed mail? This type of mail is used successfully in several European countries such as France.

The Postal Service has considered allowing mailers to advertise using unaddressed mail and we continue to evaluate this option. The Postal Service does offer certain kinds of customers and mailings an alternative known as simplified addressing. This is an alternative addressing format used when delivery of identical mail is requested to every customer on a rural route or highway contract route, or to all post office box customers at a post office without city carrier service. Instead of listing the name and address of the addressee, the mailer may use "postal customer." It may also be used by government agencies for official mail sent to all stops on city routes and post office boxes at post offices with city delivery service. In such cases, these formats may be used: "Postal Customer," "Residential Customer," and "Business Customer," depending on the type of coverage requested.

We continue to research the possibility of expanding the usage of simplified addressing to our city routes. Expanding this option to all of our delivery routes could simplify the use of mail for customers and encourage additional use of mail for advertising and promotion – especially for small businesses. The Postal Service is reviewing the operational and legal implications, stakeholder impacts, and consumer reaction, as well as volume and revenue growth opportunities as part of its review of expanding simplified mailing options.

Q5. A significant portion of your written testimony discusses regulatory and legal reforms. Section 701 of the *Postal Accountability and Enhancement Act* tasks the Postal Regulatory Commission (PRC) with the responsibility of providing recommendations to Congress and the President for legislation to improve the effectiveness of postal law every five years. Have you collaborated with the PRC with respect to your suggested reforms? If so, what was the result of those collaborations?

The Postal Service and the Commission have had informal discussions regarding legislative proposals. These discussions have centered on the fixed schedule of payments into the Retiree Health Benefits fund required by the PAEA, as well as the need to clarify the respective roles of the Commission and the Governors of the Postal Service.

Additionally, the Postal Service has requested, pursuant to section 802(c) of the PAEA, that the Commission retain an actuary to review what it believes is an inequitable apportionment of CSRS obligations between the Postal Service and the Federal Government related to CSRS credit earned during employment by the Post Office Department. Several intervenors in this docket (SS2010-1) have moved that the Commission initiate a parallel proceeding under section 701 of the PAEA so that in addition to the actuary's report, along with comments by the Commission thereon, the Commission would also submit to the Congress a recommendation for legislative change consistent with the actuary's report, should that prove advisable.

The Postal Service expects to continue discussions of these matters in the near future.

Q6. Given the financial problems faced by the Postal Service, has consideration been given to the possibility of increasing the amount of advertising by outside commercial entities in retail facilities, or permitting such advertising on postal vehicles? If so, has the Postal Service gauged public reaction and possible revenues from such endeavors, and what were the results?

The idea to utilize postal assets, such as postal trucks for advertising, has a long and mostly unsuccessful history in the Postal Service. The most comprehensive effort, Postal Ad Network, dates back to Fiscal Year 2001. After operating the program for more than a year and spending millions of dollars in development and operation, the financial performance fell far short of projections.

At its conclusion, the program identified and documented significant adjustments that would have to be implemented for this program to succeed. Among the major concerns identified were: artificially high minimum purchases for local and regional advertisers; the need to streamline the process for review and clearance of advertisements; a more effective means to replace and remove advertising from postal trucks, issues around choosing which advertisers would be allowed to advertise on our assets without getting into First Amendment violations; and the costs and structure needed to run the program.

Since the introduction and cessation of the Postal Ad Network, this business idea has resurfaced on a regular basis, and been suggested as a means for the Postal Service to generate revenue. However, a review of USPS history in these

ventures, and extensive analysis of the revenue opportunity balanced against the costs of operations, does not support proceeding with this line of business.

Similar issues were identified when reviewing the opportunity to leverage retail post offices for commercial advertising. While we do allow the use of our retail space for some commercial advertising, it is generally around either a public service (White House Memorial Day poster) or tied to the mail (Census mailings). In addition to the issues highlighted above, the foot traffic in post offices combined with the amount of time that customers would be in line viewing an ad is too low to enable the Postal Service to charge very much. The cost to implement a digital signage network, complete with an advertising management system, would be significant and most likely advertising revenues would barely cover costs, if at all.

Q7. How much is the Postal Service losing on catalog mail?

Catalog mailers use a variety of Postal Service products to deliver their mail, predominantly Standard Mail Flats and Standard Mail Carrier Route. Although the Standard Mail flats product fails to cover its attributable cost (82.4 percent cost coverage in FY2009), Standard Mail Carrier Route does make a positive contribution (144.6 percent cost coverage in FY2009), and given the distribution of catalogs between the two products, the Postal Service estimates that commercial catalogs as a whole generate enough revenue to cover their attributable cost, although they may not make a large contribution to institutional cost.

###

OFFICE OF THE INSPECTOR GENERAL
UNITED STATES POSTAL SERVICE

Responses to Questions for the Record

House Committee on Oversight and Government Reform and

Subcommittee on Federal Workforce, Postal Service, and

the District of Columbia

May 24, 2010

1735 N LYNN STREET
ARLINGTON, VA 22209-2020
(703) 248-2100
FAX: (703) 248-4626

1. ***In part, the Office of Personnel Management (OPM) appears to be suggesting that the Postal Service previously supported OPM's position on the proper funding allocation in a letter written by the Postal Service that was reprinted in the 1974 committee report that they cited in their written testimony. Do you agree with that assessment? What weight should now be given to that letter?***

   The March 27, 1973, letter from Louis A. Cox, the U.S. Postal Service's then-General Counsel, states that the Postal Service agreed postal ratepayers should bear the pension costs associated with salary increases. Mr. Cox, however, also noted that the proposed legislation making the Postal Service responsible for salary increases would "involve enormous costs that will have to be passed on in the future to postal ratepayers." Moreover, the amount due would accrue with each pay increase "leading to a cumulative annual liability of a tremendous magnitude."

   In describing the Postal Service's decision, Mr. Cox stated that "[p]roperly understood, the principle of postal self-sufficiency calls for those who use postal services to bear the cost of those services." We disagree that making the Postal Service's responsible for *all* of the pension costs associated with salary increases appropriately reflects that principle, as the Postal Service was made responsible for the increase in benefits occurring before the Postal Service was formed.

   The Office of Inspector General (OIG) is independent from the Postal Service. Our independent conclusion is that a proper funding allocation should not force the Postal Service to bear all of the pension costs of salary increases. We reached our conclusion after we reviewed the issue on its technical merits The 1973 letter -- written more than 37 years ago – is a product of a different age, when the postal market was very different. This is 2010; the Postal Service is facing an unprecedented financial crisis and changes in the business of the mail that could never have been anticipated in 1973. OPM selectively references postal support, but not the limits of support Mr. Cox noted. The letter is an interesting historical footnote; but we do not see it in any way binding OPM, the Postal Service, or Congress from a common sense solution to a distinctly 21st century problem..

2. ***Please explain why you believe that OPM currently has the legal authority to use a years-of-service methodology for calculating the Postal Service's CSRS pension obligations.***

Quite simply, OPM has failed to implement the congressionally-directed dynamic model, based on years-of-service methodology, for funding postal pensions. The responsibility to fund the CSRS pensions for individuals who transferred employment from the Post Office Department (POD) to the Postal Service on July 1, 1971, is a responsibility shared by the Postal Service and the Office of Personnel Management (OPM).[1] This responsibility has been shaped by two pieces of legislation: P.L. 93-349, the Postal Reform Act enacted in July 1974, and P.L. 108-18, the CSRS Funding Reform Act of 2003, enacted in April 2003.

In 1974, Congress required the Postal Service to contribute the full "normal cost"[2] of its retirees' benefits *plus* any unfunded CSRS liability resulting from merit-based or inflation-based salary increases.[3] Essentially, this 1974 Act required the Postal Service to fund the additional CSRS liability for pay increases in the year those pay increases were actually awarded. But in April 2003, Congress changed that methodology. Under PL 108-18, the CSRS Funding Reform Act of 2003,[4] Congress transformed CSRS postal pension calculations from requiring payment based on current year salaries, raises, inflation and retiree COLAs, to requiring payment based on actuarially *anticipated* costs in the future. With this change in premise, Congress transformed the system to a dynamic rather than static pension fund.

The legislative history behind the enactment of P.L. 108-18 reveals the intent to repeal the 1974 postal model. Specifically, the Senate Report states:

> Paragraph (1) would rewrite section 8348(h). It would *repeal* the existing provisions requiring Postal Service payments for costs "attributable to any benefits payable from the Fund to active and retired Postal Service officers and employees, and to their survivors, when the increase results from an employee-management agreement...."[5]

Although the Postal Service has followed the congressional directive to dynamically fund its CSRS liability, to this day OPM calculations remain

---

[1] This responsibility is codified at 5 U.S.C. § 8348(h).

[2] "Normal cost" is a calculation of the pension benefit earned for the year based solely on the employee's current salary. The normal cost model is notably the same pension funding principle used by other federal government agencies. HayGroup, *U.S. Postal Service: Evaluation of the USPS Postal CSRS Fund for Employees Enrolled in the Civil Service Retirement System*, p. 3 (Jan. 11, 2010).

[3] P.L. 93-349 (1974), amending 5 U.S.C. § 8348(h).

[4] P.L. 108-18 (2003), amending 5 U.S.C. § 8438(h).

[5] S. REP. No. 108-35, at 6 (2003) (emphasis added).

unchanged. Due to this inequitable split in contributions, OPM has forced the Postal Service to dynamically fund CSRS liability for both the Postal Service *and* OPM. This has caused the Postal Service to overfund the CSRS fund by approximately $75 billion from 1971 through 2009.[6] The attached copy of our March 4 letter to OPM expands on this analysis.

[6] Risk Assessment Research Center, U.S. Postal Service Office of Inspector General, *The Postal Service's Share of CSRS Pension Responsibility*, RARC-WP-10-001 (Jan. 20, 2010). The Postal Service is frequently the victim of overfunding, with a $27 billion overcharge for military service CSRS liability in 2003, and a $13 billion overfunding of future healthcare liability in 2009.

3. ***OPM appears to be taking the position that the dynamic scoring approach used in the 2003 pension law requires the Postal Service to pay the costs of salary increases and inflation. Please address this contention.***

A dynamic approach includes taking into account future salary increases, inflation, and the expected rate of return on investments. When two parties are sharing pension costs for employees who worked for both, both should pay the dynamic costs including the costs of salary increases and inflation associated with the respective service. For example, an employee hired in 1966 might be expected to retire with a final salary much greater than the employee's salary in 1971, but under OPM's methodology, the Postal Service is responsible for paying the pension costs for any salary increases after 1971. We advocate a years-of-service methodology that would split pension costs, including the costs of salary increases and inflation, evenly according to years of service. This is the same methodology OPM uses to split the cost of retiree health benefits, and the methodology formerly used to allocate responsibility for cost-of-living adjustments prior to 2003.

From a compliance standpoint, OPM's methodology does not comport with FASAB accounting standards requiring inflationary adjustments. OPM's liability calculation, based on a static 1971 salary, does not account for inflation that occurred after cessation of the POD. This liability makes the Postal Service fund CSRS dynamically on behalf of both agencies -- requiring postal contributions of 3.5% COLA for annuitants, 4.25% general salary increase and a 6.25% interest rate for fiscal year 2009.

4: Chairman Goldway testified that she supports product innovations by the Postal Service. With such support from the regulator, should the Postal Service move faster to generate revenue in these areas?

Yes. We believe that the Postal Service should move as quickly as possible to generate additional revenue. We are currently reviewing the Postal Service's efforts to grow the competitive business, and will comment on the length of time it takes the Postal Service to launch new products and services. GAO recently commented that the Postal Service needs to:

- Revise pricing for market-dominant products, such as First-Class Mail and Standard Mail.
- Address loss-making products by better aligning prices and costs.
- Provide volume incentives for certain types of bulk business mail.
- Develop new postal products and product enhancements.
- Provide incentives by simplifying complex rules for mail preparation.[7]

In addition to developing new products and services we believe that the Postal Service should continue its efforts to improve its market intelligence, by better understanding the needs of its current customers, and identifying new markets into which it could expand.

In the short term the Postal Service should improve its ability to measure the results of any product innovations. For example, the Postal Service's 2009 Standard Mail Volume Incentive Pricing Program was designed to grow volume and revenue by offering a 30 percent discount on incremental volume above a threshold volume tailored to each mailer. The PRC reported that while the Postal Service asserts that the program was a success, the Postal Service could not provide data to support its assertion.[8]

Some stakeholders have suggested that the Postal Service could play a larger role in electronic communication. If electronic diversion is a significant threat to postal revenues, perhaps there are opportunities for the Postal Service to act as a national facilitator of electronic communication and commerce. Such a role would be in keeping with the Postal Service role of binding the nation together.

---

[7] U.S. POSTAL SERVICE: Strategies and Options to Facilitate Progress toward Financial Viability, GAO-10-455, April 12, 2010 (highlights).
[8] PRC, FY 2009 Annual Compliance Determination, pages 90-93.

5. ***Are you aware of how much [money] companies comparable to the Postal Service that prefund retiree health benefits pay into their retiree health funds as a percentage of total revenues and/or profits? At what levels (of prepayments relative to revenues and/or profits) do such companies feel the need to lower or postpone such payments? Do you have any suggestions on how to design and apply a metric to the Postal Service's retiree health benefits payments that takes into account both actuarial considerations as well as ability to pay in a given year?***

A 2009 Watson Wyatt Survey Report analyzing Fortune 1000 companies found that 89 percent of those surveyed had post-retirement health benefit plans, but 63 percent of companies offering post-retirement benefits did not prefund them. Most companies have closed their plans and do not offer them to new employees.

Both of the Postal Service's competitors made relatively small contributions for retiree health benefits compared to revenue. UPS paid $91 million in contributions to employee post retirement health benefits in 2009. This is equivalent to 0.2 percent of revenue or 4 percent of profits, and UPS's prefunding level fell from 11 percent to 9 percent. FedEx contributed $21 million in its fiscal year ending May 31, 2009, to pay current beneficiaries. This is equivalent to 0.1 percent of revenue or 21 percent of profits; FedEx's prefunding level for retiree health benefits remains zero. In contrast, the Postal Service's average $5.6 billion annual contributions constitute 8 percent of fiscal year (FY) 2009 revenue..

We do not have specific information on the levels of prepayments relative to revenue and profits that will cause a company to reduce its contributions. However, companies suffering losses frequently choose to stop funding or even end their retiree health benefit programs. For example, Sunoco, a petroleum company with $31 billion in revenue in FY 2009, after suffering a $312 million loss in the third quarter last November announced it would freeze its defined benefit pension programs and phase out retiree health benefits for most future retirees.

The Postal Service needs to contain its liability for future retiree health benefits and take into account its ability to pay. To do so, we suggest requiring the Postal Service cover the increase in liability due to current employees (the normal costs) and make amortized payments for unfunded liabilities. We suggest payments for past unfunded liability be limited to half of net postal income each year. No payments for unfunded liability would be needed if OPM returned the $75 billion overcharge to the Postal Service pension fund and the pension surplus were transferred to the health fund.

6. ***Do you have a position on whether the Postal Service should allow mailers to advertise using unaddressed mail? This type of mail is used successfully in several European countries such as France.***

The OIG suggested the Postal Service explore the idea of offering unaddressed mail in its *Semiannual Report to Congress* for April 1, 2004, to September 30, 2004, but we have not completed any definitive work on this issue. We continue to believe that this would be an idea worth exploring in the U.S. market.

Attachment: March 4 letter

OFFICE OF INSPECTOR GENERAL
UNITED STATES POSTAL SERVICE

March 4, 2010

John Berry
Director
Office of Personnel Management
1900 E Street, N.W.
Washington, D.C. 20415

Daniel A. Green
Deputy Director
Planning & Policy Analysis
Office of Personnel Management
1900 E Street, N.W.
Washington, D.C. 20415

Thomas Richards
Deputy Director
Congressional & Legislative Affairs
Office of Personnel Management
1900 E Street, N.W.
Washington, D.C. 20415

SUBJECT: Postal Service CSRS Pension Liability Split

Dear Messrs. Berry, Green and Richards:

The responsibility to fund the Civil Service Retirement System (CSRS) pension for those individuals who transferred employment from the Post Office Department (POD) to the United States Postal Service (the "Postal Service") on July 1, 1971, is a responsibility that is shared by the Postal Service and the Office of Personnel Management (OPM).[1] This responsibility has been shaped by two pieces of legislation: P.L. 93-349, passed in July 1974, and P.L. 108-18, passed in April 2003.

In 1974, Congress required the Postal Service to contribute the full "normal cost"[2] of its retirees' benefits *plus* any unfunded CSRS liability resulting from merit-based or

[1] This responsibility is codified at 5 U.S.C. § 8348(h).
[2] "Normal cost" is a calculation of the pension benefit earned for the year based solely on the employee's current salary. The normal cost model is notably the same pension funding principle used by other

inflation-based salary increases.[3] Essentially, this 1974 Act required the Postal Service to fund the additional CSRS liability for pay increases in the year those pay increases were actually awarded.

I. Congress Changed the Postal Service CSRS Funding Model

In April 2003, the CSRS Funding Reform Act of 2003[4] transformed CSRS pension calculations for Postal Service employees from requiring payment based on current year salaries, raises, inflation and retiree COLAs, to requiring payment based on an *anticipation* of these costs in the future, thereby becoming a dynamic pension fund instead of a static pension fund. The legislative history behind the enactment of P.L. 108-18 unmistakably addresses the repeal of the 1974 law. Specifically, the Senate Report states:

> Paragraph (1) would rewrite section 8348(h). It would *repeal* the existing provisions requiring Postal Service payments for costs "attributable to any benefits payable from the Fund to active and retired Postal Service officers and employees, and to their survivors, when the increase results from an employee-management agreement under title 39 of the United States Code, or any administrative action by the Postal Service taken pursuant to law, which authorizes increases in pay on which benefits are computed."[5]

Currently, under 5 U.S.C. § 8348(h)(1), the 1974 law has been repealed and replaced by a formula where "Postal surplus or supplemental liability" is defined as the total present value of future pension benefits minus the sum of: (i) employee salary withholdings for CSRS contributions; (ii) the balance, plus interest, that the Postal Service has previously contributed to the CSRS fund; and (iii) any other appropriate amount, in accordance with "generally accepted actuarial practices and principles."[6]

---

federal government agencies. HayGroup, *U.S. Postal Service: Evaluation of the USPS Postal CSRS Fund for Employees Enrolled in the Civil Service Retirement System*, p. 3 (Jan. 11, 2010).

[3] P.L. 93-349 (1974), amending 5 U.S.C. § 8348(h).

[4] P.L. 108-18 (2003), amending 5 U.S.C. § 8438(h).

[5] S. Rep. No. 108-35, at 7 (2003) (emphasis added).

[6] 5 U.S.C. § 8348(h)(1) (emphasis added). The full text of this section reads:

> **(1)** In this subsection, the term "Postal surplus or supplemental liability" means the estimated difference, as determined by the Office, between—
>
> **(A)** the actuarial present value of all future benefits payable from the Fund under this subchapter to current or former employees of the United States Postal Service and attributable to civilian employment with the United States Postal Service; and
>
> **(B)** the sum of—
>
> **(i)** the actuarial present value of deductions to be withheld from the future basic pay of employees of the United States Postal Service currently subject to this subchapter under section 8334;
>
> **(ii)** that portion of the Fund balance, as of the date the Postal surplus or supplemental liability is determined, attributable to payments to the Fund by the United States Postal Service and its employees, minus benefit payments

Because CSRS funding requires Postal Service funding for *Postal Service* employees, the federal government, through OPM, remains responsible for POD employees. This final provision of Section 8348(h)(1)(iii) includes an appropriate contribution by OPM for former POD employees. The calculation of that contribution for POD employees presents a critical issue for Postal Service solvency.

Regardless of Congress's repeal of its 1974 law, the manner in which OPM calculates its share of the CSRS pension for former POD employees has remained unchanged since 1974. OPM calculates its contribution based on former POD employees' 1971 salaries, effectively treating the former POD employees as though they retired on June 30, 1971. The Postal Service's contribution, on the other hand, is calculated on the average of the employee's three highest annual salaries earned since 1971, including inflationary adjustments on the POD salary. Due to this inequitable split, the Postal Service has overfunded the CSRS fund by approximately $75 billion from 1971 through 2009.[7]

As discussed above, the 2003 enactment of P.L. 108-18 unequivocally repealed the 1974 version of 5 U.S.C. § 8348(h)(1) and replaced it with the requirement that OPM calculate its portion of liability for CSRS payments "in accordance with generally accepted actuarial practices and principles."[8] Generally accepted actuarial practices and accounting principles do not validate the static CSRS liability calculation OPM has used since 1974.

OPM's CSRS payment based on the static 1971 salaries of the POD employees ignores that those employees would otherwise have received merit-based salary increases and the *same* salary inflation had they not transferred employment from the POD to the Postal Service.[9] Although with the Postal Reorganization Act of 1971, Congress got out of the business of directing Postal Service pay policy, it did anticipate that salaries would rise in the normal course. Under the Postal Reorganization Act, Congress mandated that the Postal Service peg salary and benefits for Postal Service employees to those received by employees in the private sector.[10] Since 1969, private sector

---

> attributable to civilian employment with the United States Postal Service, plus the earnings on such amounts while in the Fund; and
>
> **(iii)** any other appropriate amount, as determined by the Office in accordance with generally accepted actuarial practices and principles.

5 U.S.C. § 8348(h)(1).

7 Risk Assessment Research Center, U.S. Postal Service Office of Inspector General, *The Postal Service's Share of CSRS Pension Responsibility*, RARC-WP-10-001 (Jan. 20, 2010). The Postal Service is frequently the victim of overfunding, with a $27 billion overcharge for military service CSRS liability in 2003, and a $13 billion overfunding of future healthcare liability in 2009.

8 5 U.S.C. § 8348(h)(1)(B)(iii). The Senate Report directs OPM to subtract from Postal Service supplemental liability OPM's share of CSRS liability determined "under generally accepted actuarial practices and accounting principles." S. REP. No. 108-35, at 7 (2003).

9 HayGroup, *U.S. Postal Service: Evaluation of the USPS Postal CSRS Fund for Employees Enrolled in the Civil Service Retirement System*, at 6 (Jan. 11, 2010).

10 39 U.S.C. § 101(c). "As an employer, the Postal Service shall achieve and maintain compensation for its officers and employees comparable to the rates and types of compensation paid in the private sector of the economy of the United States . . . ." *Id.*

salaries have risen an average of 5% per year.[11] Under the terms of the Federal Employees' Pay Comparability Act of 1990,[12] Congress has adopted the model of tying federal, non-postal salaries to the private sector as well. While Congress may not directly control postal pay policy, it has adopted the same model for inflationary pay increases for civilian federal employees and Postal Service employees.

The Postal Service's opposition to the manner in which the CSRS pension funding is split with the OPM for those former POD employees is not a recent development. In January 2004, the Postal Service asked the Board of Actuaries of the Civil Service Retirement System (the "Board") to reconsider the Postal Service's supplemental CSRS liability and the manner in which OPM calculates its share of CSRS liability for those employees who transferred employment from the POD to the Postal Service.[13] The Postal Service voiced its position that CSRS liability should be split between the two agencies based on the number of years an employee worked for each entity.

In September 2004, OPM responded to the request on behalf of the Board.[14] Relying on the Board's review, OPM's position was that the 1974 law, placing the burden on the Postal Service to pay CSRS liability for all salary increases and inflationary costs from July 1971 forward, was still valid law. OPM argued that Congress's enactment of the 1974 law showed Congress' intent not to apply a years-of-service split in dividing CSRS liability between the federal government and the Postal Service.

II. Congress Directed A Dynamic Model, Including Inflation

Interestingly, OPM's response letter refers to the "static funding method" of the CSRS fund that was continually in effect from 1971 until the passage of P.L. 108-18 in 2003. Although OPM acknowledged that the prior legislation effectuated a static funding model, the agency did not waiver in its decision to continue to fund its share of CSRS liability through the static method Congress permitted in 1974. This decision to maintain a static funding model is contrary to the reports issued by the House of Representatives[15] and the Senate[16] pertaining to the enactment of P.L. 108-18.

The Senate Report speaks to funding the CSRS pension through "dynamic assumptions," and states that a "dynamic valuation of CSRS liabilities is a more accurate measure of the present value of future CSRS annuities."[17] The intention of the Senate could not have been to place responsibility *only* on the Postal Service to create a dynamically-funded CSRS pension. Notably, the word "dynamic" appears 13 times within the Senate Report and 8 times within the House of Representatives' Report.

[11] Patrick Purcell, Congressional Research Service, *Federal Employees: Pay and Pension Increases Since 1969,* (Jan. 20, 2010), Appendix.
[12] P.L. 101-509.
[13] Letter from John E. Potter, Postmaster General, United States Postal Service, (Jan. 26, 2004).
[14] Letter from Ronald P. Sanders, Associate Director for Strategic Human Resource Policy, Office of Personnel Management (Sept. 16, 2004). This Board is under the jurisdiction of the OPM.
[15] H.R. REP. NO. 108-49 (2003).
[16] S. REP. NO. 108-35 (2003).
[17] S. REP. NO. 108-35, at 4 (2003).

Congress clearly intended to replace the static pension funding model that had been in place since 1974.

Furthermore, the House of Representatives' Report stated that P.L. 108-18 "strengthens the Postal Service, lowers the Postal Service' (sic) debt, and protects postal consumers."[18] In reality, P.L. 108-18 could fulfill these intentions of Congress only if the entire liability calculation were based on dynamic assumptions, not just for the Postal Service's share. Instead, the Postal Service's CSRS obligations drain its resources, weaken its financial stability and burden postal ratepayers.

III. Inflation Should be Attributed Equitably

The "dynamic assumptions" about which both the House and Senate commented is defined in the 2003 Act. "Dynamic assumptions" are defined in 5 U.S.C. § 8331(29) as: "[E]conomic assumptions that are used in determining actuarial costs and liabilities of a retirement system and in anticipating the effects of long-term future— (A) investment yields; (B) increases in rates of basic pay; and (C) rates of price inflation." Furthermore, the 2003 Act amended the definition of the term "normal cost" by replacing it with "normal-cost percentage" and directing that OPM calculate the normal-cost percentage for CSRS liability "using dynamic assumptions."[19] The static model currently in use does not apply any inflation to the POD salaries, attributing all inflationary factors to the Postal Service contribution.

As discussed, Congress directed that OPM's calculations be in accordance with generally accepted actuarial and accounting principles. The federal government is subject to the regulations of the Federal Accounting Standards Advisory Board (FASAB), which has established accounting standards that govern federal pension liabilities.[20] According to these standards, the impact of inflation on an employee's wages is crucial in determining pension liabilities, as this is what creates a dynamic pension funding model versus a static pension funding model.

OPM's current methodology of calculating its pension liability for former POD employees does not comply with FASAB accounting standards concerning inflation. FASAB standards require that pension funding calculations include inflationary adjustments. OPM's liability calculation based on a static 1971 salary does not account for inflation that occurred *after* cessation of the POD. This liability has unfairly been placed upon the Postal Service to fund as part of its CSRS share, making the Postal

[18] H.R. REP. NO. 108-49, at 27 (2003).

[19] 5 U.S.C. § 8331 (17). The full text reads: "'normal-cost percentage' means the entry-age normal cost computed by the Office of Personnel Management in accordance with generally accepted actuarial practice and standards (*using dynamic assumptions*) and expressed as a level percentage of aggregate basic pay . . . ." *Id.* (emphasis added).

[20] Federal Accounting Standards Advisory Board, *Pronouncements as Amended as of June 30, 2009*, at 553, http://www.fasab.gov/codifica.html. FASAB standards suggest that an aggregate entry age normal (AEAN) plan is used for calculating pension liability. The benefit to utilizing an AEAN plan is that it equates one dollar of salary with a fixed percent of pension costs, thereby ensuring that inflation is automatically calculated in pension liability. *Id.*

Service fund CSRS dynamically on behalf of *both* agencies, while OPM continues to fund CSRS through a static calculation. Specifically, OPM directs the Postal Service to fund CSRS dynamically, by requiring it to contribute 3.5% COLA for annuitants, 4.25% general salary increase and a 6.25% interest rate for fiscal year 2009.

Postal ratepayers should not be forced to bear federal government liabilities, which is undeniably a result of OPM's current methodology. One commentator has called the current model under which OPM operates a "skewed methodology" that is not only "devoid of the force of law" but "even more manifestly devoid of merit."[21] Commentators have overwhelmingly voiced support for a years-of-service split, highlighting this division of liability as the "more equitable, reasonable and financially stable model"[22] that would serve as an "appropriate benchmark for allocating responsibility"[23] between both agencies.

OPM has the authority to relieve the Postal Service from continuing to shoulder federal government liabilities. Given the Postal Service's current financial situation, the agency is requesting that OPM reconsider its present calculation of CSRS pension liability for former POD employees. To effectuate significant and immediate relief for the Postal Service, no act of Congress is required. Relief would be immediate upon OPM's realignment of its resources to accurately reflect its share of CSRS liability under a years-of-service model.

We look forward to working with you on these issues. Please feel free to contact me if we can be of assistance or if you would like to further discuss this matter.

Sincerely,

David Williams

David C. Williams
Inspector General

cc: E. Kaplan, General Counsel, OPM

---

[21] Thomas W. McLaughlin, *Annual Compliance Report: Reply and Comments of Valassis Direct Mail, Inc. and the Saturation Mailers Coalition Concerning Postal Service Financial Stability*, Docket No. ACR2009 (Feb. 23, 2010).
[22] Postcom, *A Postal Rate-Payer's Perspective: Retiree Health & Pension Benefit Reform*, www.postcom.org/public/2010/RHPB.pdf.
[23] Thomas W. McLaughlin, *Annual Compliance Report: Reply and Comments of Valassis Direct Mail, Inc. and the Saturation Mailers Coalition Concerning Postal Service Financial Stability*, Docket No. ACR2009 (Feb. 23, 2010).

GAO
Accountability * Integrity * Reliability

United States Government Accountability Office
Washington, DC 20548

May 27, 2010

The Honorable Edolphus Towns
Chairman
Committee on Oversight and Government Reform
United States House of Representatives

The Honorable Stephen F. Lynch
Chairman
Subcommittee on Federal Workforce, Postal Service,
and the District of Columbia
Committee on Oversight and Government Reform
United States House of Representatives

Subject: *Responses to Questions for the Record; April 15, 2010, hearing on the U.S. Postal Service*

Dear Chairman Towns and Chairman Lynch:

This letter responds to your April 28, 2010, request that we address questions submitted for the record related to the April 15, 2010, hearing entitled, *Continuing to Deliver: An Examination of the Postal Service's Current Financial Crisis and its Future Viability.* Our answers to these questions are attached and are based on our previous work, updates to that work, and our knowledge of the areas addressed. Our previous work was conducted either in accordance with GAO's quality assurance framework or generally accepted government auditing standards. Because our responses are based in large part on previously issued products for which we sought and incorporated agency comments, we did not seek agency comments on our responses to these questions.

If you have any questions or would like to discuss the responses, please contact me at (202) 512-2834 or herrp@gao.gov.

Sincerely yours,

Phillip Herr
Director, Physical Infrastructure Issues

Enclosure

Responses to Post-Hearing Questions for the Record
Continuing to Deliver: An Examination of the Postal Service's Current Financial Crisis and its Future Viability
April 15, 2010 Hearing
Committee on Oversight and Government Reform
United States House of Representatives

Questions for Phillip Herr, Director
Physical Infrastructure Issues
U.S. Government Accountability Office

<u>Questions from Chairman Towns and Chairman Lynch</u>

1. One of GAO's recommendations is to simplify mail preparation requirements. One type of simplified mail that is used in other countries is unaddressed mail. What is GAO's position on the Postal Service delivering unaddressed mail?

The possibility of the United States Postal Service (USPS) delivering unaddressed mail deserves careful consideration given the potential benefits, risks, and operational implications. As we recently reported,[1] USPS may have opportunities to increase volume not only by reducing mailers' costs to prepare, address, and enter mail, but also by allowing for more creative use of mail for advertising and communications. Some parties caution, however, that USPS needs to strike a balance between requirements necessary for its operations and the need to provide mailers with flexible, low-cost methods for preparing and submitting their mail.

To this end, USPS and mailers have long engaged in collaborative efforts to help define appropriate requirements. A joint USPS-mailing industry work group recently met to identify USPS regulations or requirements that hinder growth of mail volume and add no value for USPS or its customers. The work group, which consisted of nearly 80 members of the mailing industry and USPS officials, recommended in February 2010 to modify or eliminate these barriers. One work group recommended USPS relax restrictions on simplified addressing for city delivery routes. Some team members felt that this might encourage additional mailers to increase mail volumes. However, the work group reported that this recommendation was not fully supported by all team members, and in fact, some strongly opposed it. Specifically, others felt that this could erode the value of the mail piece and mailing lists that many mail service providers own and maintain. The work group report added that using an address list allows for more controlled mailings (e.g., not mailing to those that have requested to be removed). A USPS marketing manager, however, reportedly mentioned research that shows many customers do not respond negatively to

---

[1]GAO, *U.S. Postal Service: Strategies and Options to Facilitate Progress toward Financial Viability*, GAO-10-455 (Washington, D.C.: Apr. 12, 2010).

simplified address mail pieces. The USPS manager said that his group is looking into this concept, but has no timeline for making changes.

2. Many of GAO's suggestions involve changing the compensation and benefits structures of Postal Service employees. Other than your proposal to have the financial condition taken into account by an arbitrator, are you advocating other changes to the collective bargaining process, or are the compensation and benefits changes you propose supposed to be made between the Postal Service and its unions at the bargaining table?

In addition to the proposal for revising the statutory framework for collective bargaining to require that USPS's financial condition is taken into account during arbitration, our report provided some other options: specifically, we pointed out some changes in compensation and benefits that would require congressional action, while other options could be addressed in collective bargaining. For example, Congress would need to make statutory changes for certain benefits, such as those for retiree health or workers compensation. Aside from statutory changes to the collective bargaining process, we believe that USPS and postal unions must work together to control wage and benefit costs, which continue to comprise 80 percent of USPS costs—a percentage that has remained similar over the years despite major advances in technology and automating postal operations. Going forward, USPS has a window of opportunity to reduce the cost and size of its workforce through attrition and a large number of upcoming retirements. These efforts will require collaboration with the unions to determine appropriate adjustments to the number, skills, and the deployment of USPS employees. The parties can also address the need for more workforce flexibility—including reviewing the mix of full-time and part-time employees and work rules that govern what tasks employees can perform—and the appropriate USPS contribution for certain employee benefits. Current collective bargaining agreements include provisions to reduce USPS's contribution to health care premiums by 1 percent a year—from 85 percent in fiscal year 2007 to 81 percent in 2011 or 80 percent in 2012—depending on the agreement. Even with these adjustments, USPS still would cover a higher proportion of employee premiums for health care and life insurance than most other federal agencies. According to USPS estimates, reducing USPS's share of its health and life insurance premium payments to those paid by most federal agencies would have saved USPS about $615 million in fiscal year 2009.

3. GAO suggests that the Postal Service revise its pricing for Market Dominant products, such as First-Class Mail and Standard Mail. Can you elaborate on what types of pricing structure revisions should be made? Can these changes be made under current law, or will they require legislative action?

Certain options related to USPS's pricing structure discussed in our recent report could be implemented under current law, although other options—such as revising statutory pricing preferences for certain types of mail—would require legislative action. Under current law, rate increases for market-dominant products, such as First-Class Mail and Standard Mail, could be used to better align rates and discounts with the costs, profitability, and price-sensitivity of mail. In addition, PRC recently identified several instances where USPS rates and discounts do not satisfy the provisions of the law and discussed remedial actions.[2] However, stakeholders have raised questions regarding whether all postal products, including those that receive preferential rates, should be required to cover their costs. The PRC reported that market-dominant products lost $1.7 billion collectively in fiscal year 2009, primarily from Periodicals and Standard Mail Flats such as catalogs. Losses from these products were exacerbated by preferential pricing requirements.

Looking forward, rate increases for market-dominant products up to the price cap could raise significant revenues over the next decade, since these products currently generate 88 percent of revenue, while competitive products generate nearly all other revenue. To improve its financial viability, USPS announced in March 2010 that it would seek "a moderate exigent price increase" for its market-dominant products that would be effective in 2011. An exigent rate increase over the price cap may produce a large short-term revenue boost. However, a very large rate increase could be self-defeating by encouraging mailers to further accelerate diversion to electronic alternatives, thereby lowering revenues in the long run and adding to USPS's excess capacity. Since USPS has never requested an exigent rate increase, it is not clear whether such an increase would be authorized under the provision of the Postal Accountability and Enhancement Act of 2006[3] (PAEA) that limits use of this measure to extraordinary or exceptional circumstances.[4]

<u>Questions from Representative Maloney</u>

1. How much should the Postal Service be paying into the Retiree Benefit Health Benefit Fund each year on an actuarial basis?

Our April 2010 report[5] provides the estimated annual payments that USPS would make into the Postal Service Retiree Health Benefits Fund (PSRHBF) under one actuarial approach for prefunding its retiree health obligations.[6] This approach uses the actuarial methods and assumptions that the Office of Personnel Management (OPM) adopted for reporting retiree health obligations and costs in the 2009 Consolidated Financial Report of the United States and workforce projections supplied by USPS. There are numerous other actuarial approaches for prefunding retiree health obligations that, for example, utilize different methods for allocating future benefit costs and/or a different number of years over which unfunded obligations are to be paid.

---

[2]Postal Regulatory Commission, *Annual Compliance Determination of U.S. Postal Service Performance: Fiscal Year 2009* (Washington, D.C., Mar. 29, 2010).
[3]Pub. L. No. 109-435, 120 Stat. 3198 (Dec. 20, 2006).
[4]39 U.S.C. §3622(d)(1)(E).
[5]GAO-10-455, pages 24-25.
[6]Obligation, in this discussion, refers to the actuarially determined liability.

2. How does that actuarial payment schedule compare to the current payment schedule?

GAO's April 2010 report also discussed how the actuarial payments discussed in Question 1 compare to the schedule provided in current law for fiscal years 2010 through 2020.[7] In brief, over this 11-year period, current law is estimated to require USPS contributions of approximately $90 billion, which amounts to about $9.7 billion more than the actuarial approach we used. USPS has already said that it cannot afford its required prefunding payments under the current schedule. As we stated in our report, any proposals to modify these payments should be structured so that USPS funds its retirement health benefit obligations—including prefunding these obligations—to the maximum extent that its finances permit.

Question from Representative Burton

1. Currently, the USPS is required to prefund their 75 year retiree health benefit obligations over the course of the 10 years. In a given year, if the entirety of the federal government had to do the same, how much would that cost?

Using the same actuarial approach we used in our April 2010 report, we estimated that the annual payment in fiscal year 2010 to prefund the non-postal portion of the federal government's civilian retiree health obligation would be approximately $27 billion. This payment has two components: the cost of currently accruing benefits, or "normal costs," and the amortization of the unfunded obligation in payments over 40 years. Using OPM's health care cost inflation trend rate for fiscal year 2010 of 8 percent, we estimate that the fiscal year 2010 normal cost for non-postal employees would be approximately $10 billion. Further, over 40 years, an annual payment of over $17 billion would be required, using OPM's assumptions of gradually declining health care cost inflation and an interest rate of 6.25 percent compounded annually, to amortize the non-postal, civilian retiree health obligation of nearly $252 billion that GAO derived from OPM's estimates[8] as of the end of fiscal year 2009.

In comparing USPS to the rest of the federal government, it is important to recognize that, unlike most of the federal government which is funded through direct appropriations, USPS operates under a fundamental principle that it should be financially self-supporting. Thus, it strives to generate enough revenues from products and services to cover its costs. Congress, with the enactment of PAEA, required USPS to begin prefunding its retiree health benefit obligations. Requiring USPS to prefund its retiree health obligations to the maximum extent that its finances

[7] GAO-10-455, page 25.
[8] The non-postal retiree health obligation was calculated by subtracting USPS's obligations as of September 30, 2009, (as calculated by OPM) from the total obligations that OPM reported in its fiscal year 2009 financial statements for the Federal Employees Health Benefits (FEHB) program.

permit will help ensure that funds generated from ratepayers, not taxpayers, will be available to pay for the benefits of USPS retirees.

Lastly, as a matter of clarification, PAEA did not require USPS to fully prefund its retiree health obligation over 10 years, but only to begin prefunding its existing obligations. USPS's reported obligation is the amount of costs that have accrued as of the current date but does not include benefit costs that have yet to accrue for USPS's current or future employees. Assuming that USPS were to make all of its remaining prefunding payments from fiscal years 2010 through 2016 under current law, USPS would still have a remaining unfunded obligation of $27 billion at the end of fiscal year 2016. In comparison, USPS's unfunded obligations for retiree health benefits were $75 billion on September 30, 2006, shortly before PAEA was enacted.

Dr. Michael J. Riley
431 Pinewood Lake Drive, Venice, FL 34285
Tel: (941) 244-0416 home (703) 338-9635 cell Michael@Riley.net

May 31, 2010

Representative Stephen F. Lynch
Chairman
Subcommittee on Federal Workforce, Postal Service
And the District of Columbia
2157 Rayburn House Office Building
Washington, DC 20515

Dear Representative Lynch,

Thank you for allowing me to testify before your committee. Below are my answers to your questions:

Question 1:
Are you advocating that workshare discounts should be set so that they are less than the costs avoided so the Postal Service shares in the benefits of worksharing?

Answer: YES! I also wish to add that when, as now, discounts are set too high the Postal Service suffers not only by losing revenue but also due to the fact that its operations are made less efficient. Worksharing began as a transition to automation. Automation has been installed at great expense. By siphoning off volume, excessive discounts not only make the entire postal industry less efficient, they have a direct adverse effect on the efficiency and return on investment (ROI) of postal automation.

Question 2 :
With the assistance of Dr. John Panzar, the Postal Service's Office of Inspector General recently released a report which found that the current law provides the Postal Service with a strong economic incentive to set workshare discounts below avoided costs. Do you believe that the Office of Inspector General and Dr. Panzar are correct in their assessment?

Answer:
I have not read the study by John Panzer and the IG, nor am I a lawyer, but I believe that the Postal Service acts as if it had a strong incentive to set discounts above avoided costs, not below them. If the OIG and Dr. Panzer have concluded that the natural economic incentive is to set discounts below costs avoided, that would seem to confirm my judgment that it should be done. The goal should be to preserve the Postal Service and preserve postal services.

Question from Rep. Kucinich:
Your testimony echoes my concern that much of the Postal Service's proposals for a healthy USPS focus on cost reduction through cuts in essential services, rather than addressing current policies that result in the loss of desperately needed revenue. PRC

Dr. Michael J. Riley

431 Pinewood Lake Drive, Venice, FL 34285
Tel: (941) 244-0416 home (703) 338-9635 cell Michael@Riley.net

Chairwoman Ruth Goldway and national postal worker unions have also expressed this concern. They have provided excellent ideas for revenue generation that warrant further examination. Examples of these proposals include providing government services at local post offices, providing retailers a space to sell their service or products, implementing a vote-by-mail system, and having a range of products that are trackable and traceable to compare with private companies that provide that service. You provide some of your own ideas to increase mail volume, and as a result, revenue. Your proposals pertain specifically to mail products, while previous discussions in this Subcommittee pertain to revenue-generation ideas outside of the USPS' historical mission. Have you considered the viability of the revenue-generation methods that have been proposed, including the ones I just mentioned? Which proposals do you believe have the most promise, and why?

Answer:
I have considered many proposals to increase revenue and believe that those with the most promise of new profitable revenue should be considered and tried. At present, the Postal Service lacks the availability of money to spend on these ideas. New ideas for service are closer to the postal mission and fit better with existing systems than selling products. In the 1990s, the Postal Service experimented with selling products and it lacked the infrastructure of a retail operation that was necessary to make this a success. Many Post Offices lack the space for such operations.

Nevertheless, it is possible for a healthy Postal Service to build or buy facilities much like the strategic acquisitions of Kinkos by Fed Ex and of Mail Boxes, Etc. by United Parcel Service. My opinion is that there are significant opportunities to quickly grow profitable revenue in parcel delivery such as the Priority Mail, "If it fits it ships" advertising. Providing an enhanced service for "Snowbirds" and for all Americans who travel and want their mail seems to me to be the idea with the best immediate potential.

I learned long ago, that no one of us is as smart as all of us. I have great respect for postal employees and the members of the PRC. Many have offered suggestions with high potential that fit with existing systems. If the postal Service can maintain long term profitability and use the funds for investment, then far more opportunities become possible. Each idea must be fully integrated into marketing, operations, finance and customer perception. These ideas must also be politically acceptable.

Sincerely,

Michael J. Riley

UNITED STATES OFFICE OF PERSONNEL MANAGEMENT
Washington, DC 20415

Congressional and
Legislative Affairs

MAY 28 2010

The Honorable Edolphus Towns
2157 Rayburn House Office Building
Washington, DC 20515-6143

The Honorable Stephen F. Lynch
B-349A Rayburn House Office Building
Washington, DC 20515-6143

Dear Chairman Towns and Chairman Lynch:

This is in response to your letter dated April 28, 2010 regarding questions in follow-up to the April 15, 2010 "Continuing to Deliver: An Examination of the Postal Service's Current Financial Crisis and Its Future Viability" hearing. The questions and our responses are as follows:

Question #1- Please provide complete copies of the Office of Personnel Management's (OPM's) actuarial reports outlining how it implemented the audits/valuations of the postal CSRS account required by both P.L. 108-18 in 2003 and the Postal Accountability and Enhancement Act of 2006. Please ensure that your submissions include a complete description of the methodology and assumptions used and well as all supporting worksheets and documents.

Response
Attached is OPM's July 31, 2003, report to the Congress[1] outlining the methodology for allocating CSRS obligations under P.L. 108-18. The report states:

> "The Federal share is assumed to be zero for employees hired by the Postal Service on or after July 1, 1971. For employees hired before this date, the Federal share is the benefit that would be payable if the employee received no pay raises and did not accrue any additional service after June 30, 1971."

In 2006, the Postal Accountability and Enhancement Act (P. L. 108-435) provided for the Treasury to take responsibility for the cost of military service credit in the computation of CSRS annuities, resulting in a $28 billion dollar savings to the Postal Service, and relieving it from making further CSRS employer contributions based upon a percentage of salary. P.L. 108-435 made no other changes to the CSRS allocation methodology.

Attached is the most recent statement of liabilities which OPM provided to the Postal Service for fiscal year 2009.

Question #2- Your testimony cites the 1974 Committee Report for support for your interpretation of the proper CSRS pension allocation. In the same provision that you quoted, the Committee Report says that "the Postal Service will be required to make payments for that portion of any future

[1] The attached document is a final draft as prepared for submission to Congress. The original document is unavailable.

UNITED STATES OFFICE OF PERSONNEL MANAGEMENT
Washington, DC 20415

Congressional and
Legislative Affairs

increases in the unfunded liability ... (other than cost-of-living increases)." What does that "other than cost-of-living increases" provision mean? How do you reconcile that committee report statement with your interpretation of the 1974 law?

Response
It is somewhat confusing in that the term "cost-of-living increase" is used for two different purposes in regard to Postal benefits. The cost-of-living increases referred to in this section are the cost of living adjustments (COLAs) to annuitants' benefits. "Other than cost-of-living increases" refers to pay increases granted by the Postal Service to its employees that were denominated as cost-of-living increases. Thus, it was the stated intent that the Postal Service fund the CSRS costs associated with its pay increases.

Question #3- Why does OPM rely on a pension funding methodology for the Postal Service's portion of the CSRS pension fund that assumes no pay increases and is inconsistent with the years-of-service methodology used by OPM to allocate the cost of retiree health premiums?

Response
Postal CSRS funding is made in accordance with the provisions of 5 U.S.C. §8348. The Postal Service's portion of the CSRS liability includes responsibility for CSRS costs associated with pay increases granted by the Postal Service after its inception.

Postal CSRS funding provisions are not related to retiree health funding provisions. Postal funding of retiree health is governed by 5 U.S.C. §§ 8906, 8909, and 8909a.

The CSRS benefit formula is based on the employee's number of years of service and the employee's highest 3-year average salary. With each year of work and with each increase in pay the employee accrues a greater CSRS benefit. Thus, the benefits can be allocated directly to the time period in which they accrue. With retiree health benefits, a retiree with five years of service receives the same health benefit as does a retiree with 35 years of service, and there is no variation according to salary. Because there are no incremental accruals for retiree health benefits, it is common to allocate retiree health accruals by a year-of-service method.

Question #4- Is an inflation factor used in OPM's other funds (Federal, military, and health)? How is inflation handled with respect to the Postal Service's health fund?

Response
Under 5 U.S.C. 8348, only the Postal Service share of CSRS obligations is determined to include future inflation and salary increases. By statute, the funding of all other obligations for the Civil Service Retirement System assumes no future inflation or salary increases. There is no direct funding of CSRS inflation increases. Payments to fund the cost of salary increases begin only as each salary increase is authorized.

Future inflation and salary increase assumptions are employed in the determination of funding payments for the Federal Employee Retirement System (FERS), both for the Postal Service as well

UNITED STATES OFFICE OF PERSONNEL MANAGEMENT
Washington, DC 20415

Congressional and
Legislative Affairs

as the rest of the Federal government. With the exception of the Postal Retiree Health Benefits Fund, there is no pre-funding of health benefits under the Federal Employees Health Benefits (FEHB) Program. Under current law, actuarial funding of Postal retiree health begins in 2017 and will include the effect of future health cost inflation.

OPM does not oversee the funding of military programs.

Question #5- Prior to 2003, the Postal Service made a few different pension payments. It made separate payments for the pension costs of salary increases and made separate payments for the Cost of Living Adjustments (COLAs).

a. Do you know how the COLAs were split prior to 2003? Was it based on a years-of-service methodology?
b. Is a years-of-service methodology currently used? If not, what is the reason for the inconsistency?

Response
5a. The Postal Service financing of the cost of COLAs was instituted through a series of enactments in the early 1990's[2]. The Postal Service was required to amortize increases in the cost of retirement benefits due to COLAs that were attributable to civilian service after 1971, through 15-year amortization payments.

5b. P.L. 108-18 repealed the statutory COLA payments.

Question #6- The April 12 Government Accountability Office report includes actuarial calculations of future health care liabilities based on OPM's work. There has been some disagreement in the past about what assumptions are appropriate. Can you please explain OPM's assumptions about (1) size of the workforce, (2) rate of inflation, and (3) interest rates.

Response-
6-1. At GAO's request, OPM developed projected Postal Service retiree medical costs, using workforce assumptions provided to GAO by the U.S. Postal Service.

6-2. For the GAO estimates, OPM assumed the future inflation rates it used in reporting FEHB retiree medical liabilities in its Fiscal Year 2009 financial statements. These rates were based on an assumed Consumer Price Index rate of 3.50% and grade down from approximately 8% in the first year of the projection to roughly 5.5% in the final year of the projection.

6-3. For the GAO estimates, OPM assumed the interest rate it used in reporting FEHB Program

[2]Prior to the enactment of P.L. 108-18, in addition to the provisions codified in title 5, United States Code, there were a number of non-codified provisions requiring Postal retirement payments. A list of such provisions is attached. The provisions still remaining in effect were repealed by P.L. 108-18. In evaluating Postal CSRS obligations, credit was given for all payments under those statutory provisions.

UNITED STATES OFFICE OF PERSONNEL MANAGEMENT
Washington, DC 20415

Congressional and
Legislative Affairs

retiree medical liabilities in its Fiscal Year 2009 financial statements, which was a 6.25% annual interest rate.

Question #7- How much should the Postal Service be paying into the Retiree Health Benefits Funds annually on an actuarial basis?

Response
Current law does not require payment on an actuarial basis until fiscal year 2017. Funding payments will be based on actual program costs and expected trends at that time. Prior to 2017, current law requires a series of fixed funding payments to the Postal Retiree Health Benefits Fund, plus Postal Service payment of its share of current retiree health premiums.

The GAO report describes feasible approaches for other funding arrangements if the Congress were to explore changes to current law.

Question #8- If the annual retiree health benefit payments are not made, what will OPM do?

Response
There are two retiree health payments the Postal Service is currently making: one for pre-funding, the other for payment of current premiums. Were the Postal Service to default on payment of its $5.5 billion pre-funding payment, it would be in technical violation of current law. In the long term, the impact would be to make it even more difficult for the Postal Service to meet its future obligations. The failure to make the payment would cause there to be a lower balance in the Postal Service Retiree Health Benefits Fund, which thus would require higher Postal amortization payments beginning in FY 2017. If the Postal Service share of current retiree health premiums was not paid, there are no other appropriated funds that would be available for the premium payments for Postal retiree health benefits.

Failure to make either of these required payments would be a very serious matter. OPM believes that a determination of what actions should be taken could only be made in the context of the overall circumstances at that time, and would require circumspect consideration by the Administration before a course of action could be determined.

I hope that these responses to your questions are helpful and I appreciate the opportunity to be of assistance to the Committee. If you have any questions, please contact Director of Congressional and Legislative Affairs, Tania Shand, at 202-606-1300.

Sincerely,

John O'Brien
Director
Office of Planning and Policy Analysis

Report on Methodology for Postal Service Funding Study

Under Public Law 108-18, which was signed by the President on April 23, 2003, the Postal Service is required to finance the Civil Service Retirement System (CSRS) benefits for Postal workers under a dynamic funding methodology. Section 3 (b) of this law states:

(1) IN GENERAL. – The amounts representing any savings accruing to the Postal Service in any fiscal year as a result of the enactment of this Act shall be computed by the Office of Personnel Management for each such fiscal year in accordance with paragraph (2).

(2) METHODOLOGY. – Not later than July 31, 2003, the Office of Personnel Management shall –

(A) formulate a plan specifically enumerating the actuarial methods and assumptions by which the Office shall make its computations under paragraph (1); and,

(B) submit such plan to the Committee on Government Reform of the House of Representatives and the Committee on Governmental Affairs of the Senate.

(3) REQUIREMENTS. – The plan shall be formulated in consultation with the Postal Service and shall include the opportunity for the Postal Service to request reconsideration of computations under this subsection, and for the Board of Actuaries of the Civil Service Retirement System to review and make adjustments to such computations, to the extent and in the same manner as provided under section 8423(c) of title 5, United States Code.

This paper constitutes the Office of Personnel Management's (OPM's) report to Congress under this statute.

Background

Prior to P.L. 108-18, the Postal Service contributions to CSRS were determined under a "static" funding methodology that was first adopted in 1969. When the Postal Service became independent in 1971, the Congress enacted a provision that required the Postal Service to finance the retirement costs associated with the salary increases for Postal workers. Later, under the Omnibus Budget Reconciliation Act of 1990 (P.L. 101-508), a requirement was added for the Postal Service to finance the extra costs due to Cost of Living Adjustments (COLAs) for Postal annuitants. The Congress also specified additional payments for past Postal annuitant COLAs under the Omnibus Budget Reconciliation Act of 1987 (P.L. 100-203) and the Omnibus Budget Reconciliation Act of 1993 (P.L. 103-66). However, none of these pieces of legislation provided for a separate calculation of the overall assets or liabilities that were specifically attributable to the Postal Service.

In a report on the United States Postal Service (USPS) retirement plan costs issued December 31, 2001, the General Accounting Office (GAO) raised the question of whether these payments from the Postal Service were adequate to meet its past and future obligations for benefits paid from

CSRS for service performed since the agency became independent in 1971. The staff at GAO subsequently asked OPM to assess the adequacy of these payments in May of 2002.

Our analysis showed that the net accumulated value of Postal Service payments already received was currently approaching the value of its projected future CSRS benefits and that if the current funding provisions remained in place, the Postal Service would pay $71 billion more than would be needed to fund future benefits. . The preliminary cost estimate and a description of the methodology was reviewed by experts at both the U.S. Office of Management and Budget (OMB) and the U.S. Department of Treasury and they concurred with the analysis. To correct this situation OPM prepared a legislative proposal for dynamic funding of CSRS by the Postal Service, where the Postal Service would contribute the dynamic normal cost and amortize any supplemental liabilities over 40 years. Once OMB and Treasury approved the methodology, all work was shared with the Postal Service.

OPM continued to work closely with the GAO staff to refine this cost analysis, and an updated analysis was completed in January 2003. In this analysis, the projected over-funding was increased to $78 billion. GAO released a review of OPM's analysis on January 31, 2003, which basically agreed with OPM's findings, but raised some additional policy questions about whether the Postal Service or the Treasury should be responsible for the cost of benefits attributable to military service.

Basic Methodology

Our analysis of Postal Service financing of CSRS involved calculating a Postal balance in the Civil Service Retirement and Disability Fund (CSRDF). This estimated CSRS Postal balance was credited with the actual contributions made by the Postal Service and its employees to CSRS each year since June 30, 1971, and with interest earnings based on the rate of return earned by the entire CSRS fund, and reduced by the amounts paid out in benefits to Postal employees less the Federal share of those benefits.

We also estimated the future liabilities as of September 30, 2002, using the most recent economic and demographic assumptions selected by the Board of Actuaries and using the same methodology as is used in the annual dynamic actuarial valuations of CSRS and Federal Employees' Retirement System (FERS).

A year-by-year summary of the income, disbursements, and Postal balance is shown in Appendix A. These figures were reviewed by GAO in its report as of January 31, 2003. This summary will be used as the basis for determining the "actual" CSRS Postal balance in the fund as of September 30, 2002, that OPM will use in all future actuarial valuations, except for some very minor adjustments such as using actual disbursements for fiscal year 2002 rather than estimated disbursements. The Postal balance will be updated as of September 30, 2003, and each succeeding year thereafter, based on this methodology but using actual data as it becomes available. The present value of future benefits will also be determined as of September 30, 2003, and each year thereafter, based on updated Postal employee and annuitant populations using actual data from the Postal Service and the annuity roll.

The supplemental liability as of September 30, 2003, will be used to determine a 40-year amortization payment with the first payment due on September 30, 2004. On September 30, 2004, a new actuarial valuation will be performed, and a new amortization payment will be determined to amortize the supplemental liability as of September 30, 2004, over 39 years, and this payment will be due on September 30, 2005. This process will be repeated each year in the future in accordance with the statute.

OPM and the Postal Service will also continue to determine what the Postal Service payments would have been under the old law. The savings each year will be the difference between the actual payments under the new law and the payments as determined under the old law.

Specific Methodology

The Postal contributions to CSRS were derived from accounting data which included USPS accounting statements showing Postal agency contributions since 1971, OPM accounting records of Postal employee and agency contributions since 1982, and records of actual Postal payments for the 30-year and 15-year amortization payments, including any special payments made by the Postal Service under the various OBRA statutes. There also were adjustments to account for contributions under the Federal Employees' Retirement Contribution Temporary Adjustment Act of 1983, and a transfer of $170 million to the Postal FERS balance as of September 30, 1988, due to the 1987 FERS Open Season. In order to estimate the Postal employee contributions before 1982 when actual data was not available, we determined the relationship between the Postal employee and agency contributions using the OPM data, which starts in 1982, and applied this relationship to the Postal agency contributions obtained from the USPS accounting data, which started in 1971.

The estimates of the total benefit disbursements to Postal employees, and the Federal share of those benefits, are based principally on CSRS annuity roll file extracts which contain data on all annuitants who have been on the rolls since 1969. This data includes: agency where the employee last worked; current amount of the annuity (or the amount at death, or when otherwise dropped from the rolls); date of death, or drop, if applicable; annuity commencing date; total service at retirement; military service; amount of sick leave included in the total service at retirement; date of birth; final salary; and high-3 average salary. Records for spouse survivors contain the above mentioned data for the primary employee or retiree, along with the amount of the survivor annuity, commencing date of the survivor annuity, and date of death (or drop) of the survivor.

Based on this annuity roll data, and on records of the historical COLA's paid to annuitants each year, we reconstructed the amount paid out each year to each retiree and each spouse survivor for the entire CSRS, and for the Postal Service, by discounting the current benefit amount back to the annuity commencing date based on the annual COLA's. Postal annuitants were identified based on the last agency, which is the only data available.

We compared the reconstructed outlays for the entire CSRS annuity roll (Postal and non-Postal combined) with the actual payments to all CSRS retirees and survivors derived from historical accounting records, and the results were quite close. However, to obtain a more accurate estimate of the total payments to Postal retirees, we adjusted the reconstructed payments to Postal retirees each year by multiplying them by the ratio of the actual payments to all CSRS retirees for that year to the reconstructed payments to all CSRS retirees. Similarly the payments to Postal survivors were adjusted by the ratio of actual payments to all CSRS survivors each year to the reconstructed payments to all CSRS survivors. This technique greatly improves the accuracy of the estimates of the payments to Postal retirees and survivors, assuming that any discrepancies between the reconstructed and actual payments apply equally to Postal and non-Postal annuitants.

One such problem with the reconstructed annuity payments is that retiree and survivor records that were dropped for reasons other than death before 1989 had been purged from the annuity rolls without any backup, and thus payments to these annuitants cannot be reconstructed. Examples would be disability annuitants who recovered and survivor annuitants who remarried before 1989. This problem would be expected to affect Postal and non-Postal annuitants equally, so the adjustment described above should accurately correct for these deficiencies in the reconstructed Postal annuity payments. Also, because of the complexities involved, we did not attempt to reconstruct payments to child survivors. Since the accounting records of total payments to survivors for all of CSRS include payments to child survivors, the adjustment described above should provide an appropriate correction.

The payments to Postal retirees and survivors were also adjusted to account for payments of refunds, lump sums, alternative annuity refunds, and administrative expenses, based on the ratio of these amounts each year for all of CSRS contained in the annual accounting statements to the total payments to retirees and survivors for all of CSRS.

The annuity roll data was also used to estimate the Federal share, or the portion of the payments to Postal annuitants that is attributable to service with the old Post Office Department before the Postal Service became independent on July 1, 1971, and which is considered to be an obligation of the Treasury. The Federal share is assumed to be zero for employees hired by the Postal Service on or after July 1, 1971. For employees hired before this date, the Federal share is the benefit that would be payable if the employee received no pay raises and did not accrue any additional service after June 30, 1971.

The amount that would be payable assuming no pay raises since July 1, 1971, can be determined by multiplying the actual benefit by the ratio of what the high-3 average salary would have been if there had been no post-1971 pay raises to the actual high-3. The high-3 assuming no post-1971 pay raises would be the same as the salary as of June 30, 1971, (except for retirements in FY 1972 through FY 1974). Although the annuity roll generally does contain data on the high-3 average salary and the final salary, it does not include the complete salary history for employees, and so the 1971 salary must be estimated. For purposes of this analysis, the 1971 salary was estimated based on the final salary discounted by historical general salary increases and by individual merit and longevity increases.

The total amount of the general Postal salary increases each year is included on the worksheets provided by the Postal Service that are used in determining the thirty-year amortization payments made by the Postal Service to finance the increase in liability due to these pay raises. To get the percentage increase, this total increase in pay was divided by the payroll at the beginning of the year. The total payroll during each year was obtained by dividing the amount of the Postal 7 percent agency contributions (from Postal Service accounting statements) by 7 percent. The payroll at the beginning of the year was estimated by taking the average of the payrolls for the prior and the current fiscal years. The development of these general salary increases is shown in Appendix B.

A salary scale containing average individual merit and longevity increases by age and service was determined using Postal employee data files that the Postal Service had been providing to OPM each year for use in the annual actuarial valuations. The total percentage increase in basic pay during the year (for employees who were working at both the beginning and end of the year) was determined for each fiscal year from 1983 through 1998, for each age and service combination. Average individual merit and longevity increases over this 1983-1998 period were then found by subtracting the average general salary increase over this period (based on the historical general salary increases described above) from the average total salary increase, at each age and service combination.

The Postal Service also provided the complete salary histories for each of 72,000 Postal employees who were still working in 2002 and who had service computation dates before July 1, 1971. We reconstructed the full salary history for each of these employees using the general salary increases and the scale of individual merit increases described above, and compared this reconstructed salary history with the actual salary history. The results were very close, but we found that, with some very minor adjustments to the salary scale, the average difference between the reconstructed salary history and the actual salary history could be reduced nearly to zero, where the average was taken over all the years of salary history provided for each employee, for all 72,000 employees. The final salary scale that was used included these minor adjustments and is shown in Appendix C.

In summary, for purposes of determining the Federal share for employees and annuitants who were hired before July 1, 1971, we estimated the salary as of June 30, 1971, by indexing the final salary back to this date, based on the general salary increases and the salary scale of individual merit and longevity increases, based on that employee's age and service.

As was mentioned, the Federal share of the benefits for employees hired before July 1, 1971, is the benefit that would be payable if the employee had no pay raises after June 30, 1971, and did not receive credit for additional service after this date. The amount of service that is included in determining the Federal share is referred to as the "Federal service". It is equal to the pre-1971 civilian service plus a pro-rata share of the military service, where the pro-rata share is based on the ratio of pre-1971 civilian service to total civilian service. The amount of military service, and total service, is included on the annuity roll file. We have assumed that the date of civilian hire is the annuity commencing date less the civilian service at retirement (not including sick leave), and that the military service is performed immediately before this assumed date of civilian hire. The amount of sick leave for employees hired before July 1, 1971, was allocated between the Federal and the Postal share similarly to military service. The annuity roll only contains the final agency where the retiree was working at time of retirement, and we have assumed that all of the civilian service was with this final agency. Some employees may have transferred to the Postal Service from other agencies in mid-career, and vice-versa, and we have, in effect, assumed that the effects of these two trends offset each other.

For non-disability retirement benefits, the benefit payable based on the Federal service is found directly using the benefit formula. For example, an employee who has 5 years of Federal service would be credited with a benefit of 7.5 percent of the high-3 average salary assuming no post-71 salary increases (where the benefit formula is 1.5 percent for each of the first 5 years of service, 1.75 percent for each of the next 5 years of service, and 2 percent for years of service over 10 years). For disability benefits, and benefits for survivors of employees (which are based on the disability formula), the Federal share is found by multiplying the benefit that would be payable assuming no post-1971 salary increases by the ratio of the Federal service to the total service. Since there is a minimum disability benefit, disability benefits do not accrue directly in relation to the amount of service like non-disability benefits do.

The reconstructed Federal share was also adjusted the same way that the reconstructed total Postal benefits were adjusted, based on the accounting data for the entire CSRS fund as described above.

Reconsideration

The Postal Service has the opportunity to request reconsideration of the computations described above. The procedure for such review is set forth in OPM regulations at 5 CFR Part 841, Subpart D.

Appendix A

Updated Postal Service Funding Projections

The following pages contain updated output of the Postal Funding Projections showing the OPM option where the Postal Service is responsible for all military service for Post-71 hires, and a pro-rata share for pre-71 hires. These were sent to GAO and formed the basis for the GAO Report. They reflect GAO suggestions and OPM refinements that were made after the original projections that were first provided to OMB in August 2002.

Postal Service Responsible for all Military Service, including a pro-rata portion for pre-71 hires

	Employee and Agency Contrib.	30-yr Payments	15-yr Payments	Total Benefits	Federal Share	Interest Rate	Postal Balance
1972	898.900	0.000	0.000	911.427	910.820	0.0603504	925.399
1973	911.899	0.000	0.000	1073.161	1063.414	0.0564137	1905.203
1974	1043.200	0.000	0.000	1337.106	1306.990	0.0607163	3064.719
1975	1097.600	561.300	0.000	1648.542	1588.381	0.0648389	4895.804
1976	1599.700	385.000	0.000	2427.404	2283.063	0.0873750	7227.515
1977	1262.000	507.200	0.000	2182.650	1982.985	0.0668428	9315.661
1978	1319.300	470.400	0.000	2466.128	2160.077	0.0722324	11508.797
1979	1482.600	657.800	0.000	2798.551	2358.227	0.0715308	14069.385
1980	1572.700	697.100	0.000	3277.354	2648.344	0.0807272	16884.047
1981	1608.900	722.200	0.000	3872.128	2980.510	0.0879055	19839.257
1982	1742.900	850.200	0.000	4258.777	3176.952	0.1124855	23619.341
1983	1784.200	967.000	0.000	4509.832	3252.452	0.1084400	27703.003
1984	1805.300	917.400	0.000	4746.727	3275.910	0.1088976	31989.889
1985	1996.700	1355.400	0.000	5043.582	3311.940	0.1171254	37372.695
1986	1963.899	1353.100	0.000	5359.668	3350.868	0.1150738	42978.928
1987	1992.600	1353.100	0.000	5573.609	3315.954	0.1026309	48464.336
1988	2041.600	1618.000	350.000	6092.621	3441.394	0.1056442	54740.482
1989	2011.700	1617.500	0.000	6410.715	3445.600	0.1045163	61076.016
1990	1935.899	1658.500	73.600	6811.164	3474.102	0.1013078	67523.457
1991	1893.500	1752.200	636.966	7247.395	3493.575	0.1009639	74775.819
1992	1953.200	1918.800	756.779	7203.758	3347.554	0.0974439	82742.122
1993	1723.600	1938.300	866.728	8056.855	3349.568	0.0931438	90131.424
1994	1719.800	1995.899	1036.035	8142.254	3265.114	0.0879041	97790.168
1995	1744.700	2133.800	1159.676	8250.816	3203.450	0.0876421	106206.785
1996	1815.899	2362.200	980.856	8294.102	3094.608	0.0866424	115221.674
1997	1799.300	2395.899	1048.289	8530.742	3040.302	0.0758235	123571.296
1998	1754.400	2434.800	1090.139	8676.262	2937.833	0.0788211	132695.225
1999	1725.000	2508.800	902.735	8771.070	2807.511	0.0738429	141510.305
2000	1700.100	2601.900	980.238	8966.781	2692.284	0.0714624	150467.262
2001	1611.300	2628.700	1125.919	9285.430	2604.849	0.0703278	159556.380
2002	1543.400	2635.135	1239.837	9592.016	2477.731	0.0675000	168442.507

Valuation as of September 30, 2002

Present Value of Future Benefits	190.478
CSRS Postal Balance 9/30/2002	168.443
Present Value 14% Contributions	9.454
Present Value Military Deposits	0.738
Present Value 30-year Payments	33.335
Present Value 15-year Payments	56.216
Potential Overfunding	77.708

Unfunded Liability

Present Value of Future Benefits	190.478
CSRS Postal Balance 9/30/2002	168.443
Present Value Military Deposits	0.738
Present Value Normal Cost	16.477
Unfunded Liability	4.820

Appendix B

Development of Salary Index

1. Fiscal Year
2. Salary increase during the year, based on data provided by Postal Service and used in determining the 30-year payments, in millions of dollars
3. Payroll at beginning of year, based on average of payroll for current and previous year, payrolls obtained by dividing agency contributions by .07, in millions of dollars
4. Percentage increase in salaries ((2) / (3))

(1)	(2)	(3)	(4)
1972	504.	6113.	0.082434
1973	348.	6410.	0.054229
1974	573.	6919.	0.082783
1975	275.	7583.	0.036302
1976	1308.	8294.	0.157713
1977	510.	8961.	0.056922
1978	296.	9161.	0.032258
1979	1171.	9946.	0.117690
1980	390.	10854.	0.035956
1981	240.	11311.	0.021233
1982	1187.	11924.	0.099526
1983	204.	12536.	0.016265
1984	128.	12854.	0.009946
1985	2305.	14484.	0.159121
1986	405.	16479.	0.024568
1987	323.	16071.	0.020090
1988	1004.	14816.	0.067743
1989	304.	14436.	0.021049
1990	231.	14087.	0.016383
1991	635.	13666.	0.046443
1992	504.	13706.	0.036764
1993	193.	13088.	0.014739
1994	277.	12309.	0.022514
1995	617.	12438.	0.049573
1996	1060.	12791.	0.082911
1997	144.	12994.	0.011088
1998	202.	12792.	0.015775
1999	179.	12405.	0.014453
2000	398.	12013.	0.033150
2001	84.	11659.	0.007176

Appendix C

Salary Scale Derived from Data for 1983-1998.

The average total salary increase, including both general salary increases and individual merit and longevity increases, was determined over the 1983-1998 period for each of the age and service categories. Then the average general increase of .03844 was subtracted from each of these average increases. The average general salary increase of .03844 is the arithmetic average of the general increases over this period, based on the salary increase data used in determining the 30-year payments.

After comparison with the file containing the actual salary history for 72,000 Postal employees currently working with service computation dates before July 1, 1971, this salary scale based on actual data was adjusted by first changing the rate at ages 55+ and service of 20+ from .0014 to .0059, and then the amount .0005 was added to the value shown at all ages and lengths of service.

Adjusted Salary Scale

	Age Interval					
Serv.	17-24	25-29	30-34	35-44	45-54	55+
0	0.0441	0.0399	0.0392	0.0373	0.0378	0.0468
1	0.0690	0.0733	0.0760	0.0777	0.0795	0.0749
2	0.0694	0.0730	0.0753	0.0744	0.0699	0.0631
3	0.0491	0.0494	0.0497	0.0494	0.0493	0.0558
4	0.0377	0.0346	0.0335	0.0355	0.0393	0.0476
5	0.0351	0.0281	0.0244	0.0255	0.0300	0.0385
6	0.0462	0.0323	0.0253	0.0235	0.0251	0.0312
7	0.0386	0.0333	0.0258	0.0236	0.0244	0.0276
8	0.0000	0.0313	0.0230	0.0213	0.0214	0.0208
9	0.0000	0.0242	0.0203	0.0196	0.0179	0.0156
10	0.0000	0.0269	0.0194	0.0176	0.0162	0.0143
11	0.0000	0.0421	0.0222	0.0121	0.0114	0.0125
12	0.0000	0.0351	0.0121	0.0046	0.0049	0.0070
13	0.0000	0.0000	0.0112	0.0048	0.0037	0.0067
14	0.0000	0.0000	0.0184	0.0099	0.0082	0.0105
15	0.0000	0.0000	0.0195	0.0124	0.0102	0.0117
16	0.0000	0.0000	0.0148	0.0105	0.0085	0.0091
17	0.0000	0.0000	0.0154	0.0104	0.0075	0.0077
18	0.0000	0.0000	0.0000	0.0116	0.0090	0.0081
19	0.0000	0.0000	0.0000	0.0085	0.0074	0.0063
20+	0.0000	0.0000	0.0000	0.0053	0.0065	0.0064

Non-Codified Provisions Relating to USPS Retirement Fund Payments

PAYMENTS BY POSTAL SERVICE RELATING TO CORRECTED CALCULATIONS FOR PAST RETIREMENT COLAS

Pub. L. 103-66, title XI, Sec. 11101(a), Aug. 10, 1993, 107 Stat. 413, provided that: "In addition to any other payments required under section 8348(m) of title 5, United States Code, or any other provision of law, the United States Postal Service shall pay into the Civil Service Retirement and Disability Fund a total of $693,000,000, of which -

"(1) at least one-third shall be paid not later than September 30, 1996;
"(2) at least two-thirds shall be paid not later than September 30, 1997; and
"(3) any remaining balance shall be paid not later than September 30, 1998."

PRE-1991 COST-OF-LIVING ADJUSTMENTS

Section 7101(c) of Pub. L. 101-508, as amended by Pub. L. 102-378, Sec. 5(a)(1), Oct. 2, 1992, 106 Stat. 1358, provided that:

"(1) For the purpose of this subsection -

"(A) the term 'pre-1991 COLA' means a cost-of-living adjustment which took effect in any of the fiscal years specified in subparagraphs (A)-(N) of paragraph (3);

"(B) the term 'post-1990 fiscal year' means a fiscal year after fiscal year 1990; and

"(C) the term 'pre-1991 fiscal year' means a fiscal year before fiscal year 1991.

"(2) Notwithstanding any other provision of law, an installment (equal to an amount determined by reference to paragraph (3)) shall be payable by the United States Postal Service in a post-1990 fiscal year, with respect to a pre-1991 COLA, if such fiscal year occurs within the 15-fiscal-year period which begins with the first fiscal year in which that COLA took effect.

"(3) Notwithstanding any provision of section 8348(m) of title 5, United States Code, or any determination thereunder (including any made under such provision, as in effect before October 1, 1990), the estimated increase in the unfunded liability referred to in paragraph (1) of such section 8348(m) shall be payable, in accordance with this subsection, based on annual installments equal to -

"(A) $6,500,000 each, with respect to the cost-of-living adjustment which took effect in fiscal year 1977;

"(B) $7,000,000 each, with respect to the cost-of-living adjustment which took effect in fiscal year 1978;

"(C) $10,400,000 each, with respect to the cost-of-living adjustment which took effect in fiscal year 1979;

"(D) $20,500,000 each, with respect to the cost-of-living adjustment which took effect in fiscal year 1980;

"(E) $26,100,000 each, with respect to the cost-of-living adjustment which took effect in fiscal year 1981;

"(F) $28,100,000 each, with respect to the cost-of-living adjustment which took effect in fiscal year 1982;

"(G) $30,600,000 each, with respect to the cost-of-living adjustment which took effect in fiscal year 1983;

"(H) $5,700,000 each, with respect to the cost-of-living adjustment which took effect in fiscal year 1984;

"(I) $19,400,000 each, with respect to the cost-of-living adjustment which took effect in fiscal year 1985;

"(J) $7,400,000 each, with respect to the cost-of-living adjustment which took effect in fiscal year 1986;

"(K) $8,500,000 each, with respect to the cost-of-living adjustment which took effect in fiscal year 1987;

"(L) $36,800,000 each, with respect to the cost-of-living adjustment which took effect in fiscal year 1988;

"(M) $51,600,000 each, with respect to the cost-of-living adjustment which took effect in fiscal year 1989; and

"(N) $63,500,000 each, with respect to the cost-of-living adjustment which took effect in fiscal year 1990.

"(4) Any installment payable under this subsection shall be paid by the Postal Service at the same time as when it pays any installments due in that same fiscal year under section 8348(m) of title 5, United States Code.

"(5) An installment payable under this subsection in a fiscal year, with respect to a pre-1991 COLA, shall be in lieu of any other installment for which the Postal Service might otherwise be liable in such fiscal year, with respect to such COLA, under section 8348(m) of title 5, United States Code."

(Amendment by Pub. L. 102-378 to section 7101(c) of Pub. L. 101-508, set out above, effective Nov. 5, 1990, see section 9(b)(6) of Pub. L. 102-378, set out as an Effective Date of 1992 Amendment note under section 6303 of this title.)

PAYMENTS RELATING TO AMOUNTS WHICH WOULD HAVE BEEN DUE BEFORE FISCAL YEAR 1987

Section 7103 of Pub. L. 101-508 provided that:

"(a) Definition. - For the purpose of this section, the term 'pre-1987 fiscal year' means a fiscal year before fiscal year 1987.

"(b) For Past Retirement COLAs. - As payment for any amounts which would have been due in any pre-1987 fiscal year under the provisions of section 8348(m) of title 5, United States Code (as amended by section 7101) if such provisions had been in effect as of July 1, 1971, the United States Postal Service shall pay into the Civil Service Retirement and Disability Fund -

"(1) $216,000,000, not later than September 30, 1991;
"(2) $266,000,000, not later than September 30, 1992;
"(3) $316,000,000, not later than September 30, 1993;
"(4) $416,000,000, not later than September 30, 1994; and
"(5) $471,000,000, not later than September 30, 1995.

CERTAIN POSTAL SERVICE ANNUITANTS; SIZE OF ANNUAL INSTALLMENTS TO FUND PREVIOUS YEARS' COLAS

Section 4002(b)(2) of Pub. L. 101-239, which provided that notwithstanding any provision of section 8348(m) of this title the estimated increase in the unfunded liability referred to in section 8348(m)(1) was to be payable based on annual installments equal to specified amounts for fiscal years 1987 to 1989, was repealed by Pub. L. 101-508, title VII, Sec. 710(b), Nov. 5, 1990, 104 Stat. 1388-331.

CERTAIN POSTAL SERVICE ANNUITANTS; ADDITIONAL AMOUNT PAYABLE

Section 4002(b)(3) of Pub. L. 101-239, which provided that first payment made under provisions of section 8348(m) of this title was to include, in addition to the amount which would otherwise have been payable at that time, an amount equal to the sum of any amounts which would have been due under those provisions in any prior year if this section had been enacted before Oct. 1, 1986, and which provided the method of computation, was repealed by Pub. L. 101-508, title VII, Sec. 7101(b), Nov. 5, 1990, 104 Stat. 1388-331.

SECTION 4002 OF P.L. 101-239

SEC. 4002. FUNDING OF COST-OF-LIVING ADJUSTMENTS FOR CERTAIN POSTAL SERVICE ANNUITANTS AND SURVIVOR ANNUITANTS.

(a) IN GENERAL- Section 8348 of title 5, United States Code, is amended by adding at the end the following:

"(m)(1) Notwithstanding any other provision of law, the United States Postal Service shall be liable for that portion of any estimated increase in the unfunded liability of the Fund which is attributable to any benefits payable from the Fund to former employees of the Postal Service who first become annuitants by reason of separation from the Postal Service on or after October 1, 1986, or to their survivors, or to the survivors of individuals who die on or after October 1, 1986, while employed by the Postal Service, when the increase results from a cost-of-living adjustment under section 8340 of this title.

(2) The estimated increase in the unfunded liability referred to in paragraph (1) of this subsection shall be determined by the Office after consultation with the Postal Service. The Postal Service shall pay the amount so determined to the Office in 15 equal annual installments with interest computed at the rate used in the most recent valuation of the Civil Service Retirement System, and with the first payment thereof due at the end of the fiscal year in which the cost-of-living adjustment with respect to which the payment relates becomes effective.

"(3) In determining any amount for which the Postal Service is liable under this subsection, the amount of the liability shall be prorated to reflect only that portion of total service (used in computing the benefits involved) which is attributable to civilian service performed after June 30, 1971, as estimated by the Office.'.

(b) EFFECTIVE DATE; SIZE OF ANNUAL INSTALLMENTS TO FUND EARLIER COLAS; ADDITIONAL AMOUNT INITIALLY PAYABLE-

(1) EFFECTIVE DATE- This section and the amendment made by this section shall be effective as of October 1, 1986.

(2) SIZE OF ANNUAL INSTALLMENTS TO FUND PREVIOUS YEARS' COLAS- Notwithstanding any provision of section 8348(m) of title 5, United States Code (as added by subsection (a)), the estimated increase in the

unfunded liability referred to in paragraph (1) of such section 8348(m) shall be payable based on annual installments equal to--

(A) $100,000 each, with respect to the cost-of-living adjustment which took effect in fiscal year 1987;

(B) $6,000,000 each, with respect to the cost-of-living adjustment which took effect in fiscal year 1988; and

(C) $15,000,000 each, with respect to the cost-of-living adjustment which took effect in fiscal year 1989.

(3) ADDITIONAL AMOUNT PAYABLE-

(A) GENERALLY- The first payment made under the provisions of section 8348(m) of title 5, United States Code (as added by subsection (a)) shall include, in addition to the amount which would otherwise be payable at that time, an amount equal to the sum of any amounts which would have been due under those provisions in any prior year if this section had been enacted before October 1, 1986.

(B) COMPUTATION METHOD- Subject to paragraph (2), the additional amount payable under this paragraph shall be computed in accordance with section 8348(m) of title 5, United States Code (as added by subsection (a)), and shall include interest. Interest on an amount--

(i) shall be computed at the rate used in the most recent valuation of the Civil Service Retirement System;

(ii) shall accrue, and be compounded, annually; and

(iii) shall be computed for the period beginning on the date by which such amount should have been paid (if this section had been enacted before October 1, 1986) and ending on the date on which payment is made.

Funded Status of the Postal Service's CSRS Obligations

Present Value of Benefits as of 9/30/2008	$206.8 billion
- Present Value of Employee Contributions	- 2.7
Actuarial Accrued Liability	204.1 billion
- Postal CSRS Fund 9/30/2008	- 195.1
Unfunded Liability 9/30/2008	$9.0 billion

2. Components of Net Change

Analysis of Pension Expense for Postal Service - CSRS Liabilities Based on Post-1971 Civilian Service

Actuarial Accrued Liability as of 9/30/2007 (Present Value of Benefits less Present Value of Future Employee Contributions)	$196.9 billion
+ Expected Employee Contributions during FY2008	+ 0.5
- Expected Benefit Disbursements	- 9.4
+ Interest Expense	+ 12.0
+ Total Actuarial Loss during FY2007	+ 4.1
Actuarial Accrued Liability as of 9/30/2008	$204.1 billion

For the valuation as of 9/30/2007, the CSRS COLA for FY2009 was assume to be 3.5%, but the actual COLA for FY2009, which was reflected in the valuation as of 9/30/2008, was 5.8%. Also in the valuation as of 9/30/2007, a general salary increase of 4.25% was assumed for FY2008, but in the valuation as of 9/30/2008, the actual salary increases during FY2008 were reflected in the actual employee population as of 9/30/2008.

Analysis of Change in Net Assets during FY2007

	Expected	Actual
Net Assets as of 9/20/2007	$193.763	$193.551 billion[1]
+ Employee Contributions	+ 0.521	+ 0.516
- Benefit Payments	- 9.377	- 9.314
+ Investment Income	+ 11.837	+ 10.313
Net Assets as of 9/30/2008	$196.744	$ 195.066

[1] In the statement for last year, the assets in the Postal Fund as of 9/30/2007 were reported as $193.763 billion. This year these assets were re-stated to be $193.550 billion. The actual rate of interest earned during FY2008 was 5.45081%, which is the rate earned by the entire CSRS fund, Postal and non-Postal combined.

CSRS Unfunded Liability Projected to 9/30/2009, Based on Long Term Assumptions

Actuarial Accrued Liability as of 9/30/2008	$204.1 billion
+ Employee Contributions for FY2009	+ 0.5
- Projected Benefit Payments for FY2009	- 10.0
+ Interest Expense	+ 12.5
Projected Actuarial Liability 9/30/2009	$207.1
- Projected Postal Fund 9/30/2009	197.5
Projected Unfunded Liability as of 9/30/2009	$ 9.6 billion

3. Cost Methods and Assumptions Underlying the Actuarial Valuations

The actuarial cost method is Entry Age Normal

The long term economic assumptions are as follows:

Rate of inflation: 3.5%
FERS COLA: 2.8%
Annual general salary increases: 4.25%
Interest Rate: 6.25%

The Board of Actuaries decided to incorporate an assumption for additional future mortality improvement for the actuarial valuation as of September 30, 2007. This caused the dynamic normal cost of CSRS to increase from 25.2% of pay to 25.8%, and the FERS normal cost to increase from 12.0% to 12.3%. It also caused an increase in the actuarial liabilities. The Postal Service is not required to make any agency contributions to CSRS. Because of Budgeting considerations, the agency contribution to FERS will continue at the current rate of 11.2% of pay (the employee contribution is 0.8% of pay) until October 1, 2010, when it will change to the new rate of 11.5% of pay.

4. Actual and Projected Contributions to and Payments from the Postal Accounts for CSRS, Including Rates of Return

Postal CSRS Unfunded Liability as of September 30, 2008
As Determined Under P.L. 109-435,
The Postal Accountability and Enforcement Act

Present Value of Benefits	$206.8 billion
- PV Future Contributions	2.7
- Postal Fund 9/30/2006	195.1
Supplemental Liability	$9.0 billion

The long term economic assumptions of a 3.5% COLA for annuitants, 4.25% general salary increase, and 6.25% interest are assumed to apply in FY 2009 and all future years.

Surplus Transferred to Postal Retiree Health Fund on June 30, 2007: $17.1 billion

	Employee +Agency Contrib	30-yr Payment	15-yr /40-yr Payment	Total Benefit	Federal Share	Interest Rate	Postal Fund
1972	898.900	0.000	0.000	905.483	904.178	0.0603504	924.680
1973	911.899	0.000	0.000	1048.657	1037.775	0.0564137	1903.277
1974	1043.200	0.000	0.000	1294.540	1264.763	0.0607163	3063.025
1975	1097.600	561.300	0.000	1591.558	1532.690	0.0648389	4895.336
1976	1599.700	385.000	0.000	2327.077	2187.338	0.0873750	7231.809
1977	1262.000	507.200	0.000	2083.439	1891.180	0.0668428	9327.897
1978	1319.300	470.400	0.000	2342.468	2053.100	0.0722324	11539.202
1979	1482.600	657.800	0.000	2641.720	2229.904	0.0715308	14131.491
1980	1572.700	697.100	0.000	3078.699	2492.671	0.0807272	16995.884
1981	1608.900	722.200	0.000	3634.974	2808.045	0.0879055	20028.457
1982	1742.900	850.200	0.000	3981.763	2986.905	0.1124855	23921.681
1983	1784.200	967.000	0.000	4212.648	3051.195	0.1084400	28139.259
1984	1803.100	917.400	0.000	4427.320	3066.955	0.1088976	32587.798
1985	1990.400	1355.400	0.000	4691.945	3093.871	0.1171254	38175.355
1986	1948.499	1353.100	0.000	4971.812	3122.085	0.1150738	44025.891
1987	1983.800	1353.100	0.000	5166.777	3088.140	0.1026309	49797.702
1988	2035.900	1618.000	350.000	5638.027	3199.696	0.1056442	56432.850
1989	2005.699	1617.500	0.000	5933.184	3202.695	0.1045163	63185.835
1990	1930.399	1658.500	73.600	6295.832	3225.157	0.1013078	70121.116
1991	1887.600	1752.200	636.966	6691.879	3240.076	0.1009639	77946.814
1992	1946.300	1918.800	756.779	6683.266	3100.051	0.0974439	86501.162
1993	1712.900	1938.300	866.728	7445.691	3092.292	0.0931438	94599.764
1994	1714.300	1995.899	1036.035	7465.383	3007.164	0.0879041	103082.882
1995	1738.800	2133.800	1159.676	7573.031	2948.294	0.0876421	112398.355
1996	1809.899	2362.200	980.856	7631.105	2848.742	0.0866424	122378.639
1997	1793.300	2395.899	1048.289	7854.016	2794.391	0.0758235	131711.845
1998	1747.500	2434.800	1090.139	8000.723	2698.485	0.0788211	141923.626
1999	1717.500	2508.800	902.735	8098.297	2574.942	0.0738429	151868.836
2000	1692.100	2601.900	980.238	8293.406	2465.362	0.0714613	162019.998
2001	1603.600	2628.700	1125.919	8600.602	2382.814	0.0703249	172392.221
2002	1543.600	2635.100	1239.837	8863.883	2281.482	0.0680155	182782.349
2003	1918.199	0.000	0.000	9075.348	2153.580	0.0665783	189781.560
2004	2389.699	0.000	240.000	9434.527	2014.949	0.0606814	196355.281
2005	2233.020	0.000	290.000	9816.254	1929.388	0.0584889	202310.698
2006	2117.895	0.000	257.000	10242.656	1845.712	0.0573286	207706.858
2007	612.021	0.000	0.000	10656.566	1758.849	0.0563231	193550.668
2008	515.795	0.000	0.000	10966.293	1652.069	0.0545081	195065.716
2009	502.966	0.000	0.000	11610.258	1593.638	0.0625000	197450.880
2010	459.070	0.000	0.000	12220.949	1507.435	0.0625000	199221.529
2011	412.439	0.000	0.000	12783.949	1412.388	0.0625000	200376.480
2012	364.979	0.000	0.000	13346.969	1318.014	0.0625000	200877.066
2013	318.525	0.000	0.000	13893.223	1224.995	0.0625000	200702.108
2014	273.814	0.000	0.000	14414.707	1133.975	0.0625000	199838.779

2015	232.148	0.000	0.000	14899.859	1045.484	0.0625000	198287.246
2016	195.303	0.000	0.000	15332.074	960.050	0.0625000	196067.178
2017	163.320	0.000	0.000	15710.324	878.141	0.0625000	193201.066
2018	135.792	0.000	0.000	16035.027	800.114	0.0625000	189712.328
2019	112.434	0.000	0.000	16306.453	726.247	0.0625000	185625.546
2020	92.852	0.000	0.000	16526.941	656.757	0.0625000	180964.253
2021	76.404	0.000	0.000	16700.445	591.777	0.0625000	175748.846
2022	62.433	0.000	0.000	16832.355	531.406	0.0625000	169994.882
2023	50.502	0.000	0.000	16922.039	475.602	0.0625000	163719.028
2024	40.500	0.000	0.000	16966.957	424.283	0.0625000	156941.422
2025	32.219	0.000	0.000	16968.043	377.302	0.0625000	149682.135
2026	25.434	0.000	0.000	16925.277	334.489	0.0625000	141962.105
2027	19.923	0.000	0.000	16839.230	295.648	0.0625000	133802.545
2028	15.411	0.000	0.000	16710.219	260.565	0.0625000	125225.184
2029	11.760	0.000	0.000	16535.473	229.002	0.0625000	116255.565
2030	8.811	0.000	0.000	16317.277	200.699	0.0625000	106918.038
2031	6.396	0.000	0.000	16051.695	175.432	0.0625000	97242.138
2032	4.488	0.000	0.000	15737.301	152.981	0.0625000	87260.457
2033	3.028	0.000	0.000	15372.840	133.125	0.0625000	77008.632
2034	1.941	0.000	0.000	14957.398	115.645	0.0625000	66525.151
2035	1.161	0.000	0.000	14489.773	100.335	0.0625000	55851.885
2036	0.641	0.000	0.000	13969.895	87.002	0.0625000	45033.142
2037	0.323	0.000	0.000	13399.016	75.459	0.0625000	34114.444
2038	0.143	0.000	0.000	12779.629	65.543	0.0625000	23141.371
2039	0.052	0.000	0.000	12114.629	57.090	0.0625000	12159.136
2040	0.019	0.000	0.000	11409.168	49.940	0.0625000	1210.285
2041	0.007	0.000	0.000	10669.348	43.939	0.0625000	-9666.478
2042	0.004	0.000	0.000	9903.031	38.954	0.0625000	-20438.281
2043	0.003	0.000	0.000	9119.082	34.851	0.0625000	-31079.473
2044	0.003	0.000	0.000	8327.047	31.510	0.0625000	-41572.774
2045	0.002	0.000	0.000	7536.758	28.813	0.0625000	-51910.076
2046	0.002	0.000	0.000	6757.977	26.649	0.0625000	-62092.936
2047	0.002	0.000	0.000	6000.387	24.932	0.0625000	-72133.096
2048	0.001	0.000	0.000	5273.320	23.580	0.0625000	-82052.714
2049	0.001	0.000	0.000	4585.059	22.519	0.0625000	-91883.962
2050	0.001	0.000	0.000	3942.674	21.688	0.0625000	-101668.368
2051	0.000	0.000	0.000	3351.876	21.033	0.0625000	-111455.994
2052	0.000	0.000	0.000	2816.798	20.510	0.0625000	-121304.341
2053	0.000	0.000	0.000	2339.749	20.082	0.0625000	-131276.919
2054	0.000	0.000	0.000	1921.146	19.720	0.0625000	-141441.671
2055	0.000	0.000	0.000	1559.651	19.400	0.0625000	-151869.430
2056	0.000	0.000	0.000	1252.422	19.101	0.0625000	-162632.547
2057	0.000	0.000	0.000	995.290	18.806	0.0625000	-173803.617
2058	0.000	0.000	0.000	783.526	18.506	0.0625000	-185454.907
2059	0.000	0.000	0.000	611.819	18.192	0.0625000	-197657.736
2060	0.000	0.000	0.000	474.719	17.859	0.0625000	-210482.265
2061	0.000	0.000	0.000	366.802	17.500	0.0625000	-223997.458
2062	0.000	0.000	0.000	282.928	17.116	0.0625000	-238271.292
2063	0.000	0.000	0.000	218.664	16.703	0.0625000	-253371.424
2064	0.000	0.000	0.000	170.054	16.263	0.0625000	-269365.662
2065	0.000	0.000	0.000	133.710	15.796	0.0625000	-286322.560
2066	0.000	0.000	0.000	106.867	15.301	0.0625000	-304312.104
2067	0.000	0.000	0.000	87.233	14.781	0.0625000	-323406.293
2068	0.000	0.000	0.000	72.890	14.238	0.0625000	-343679.643
2069	0.000	0.000	0.000	62.483	13.674	0.0625000	-365209.933
2070	0.000	0.000	0.000	54.903	13.092	0.0625000	-388078.651
2071	0.000	0.000	0.000	49.385	12.495	0.0625000	-412371.592