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# United States Senate

COMMITTEE ON  
HOMELAND SECURITY AND GOVERNMENTAL AFFAIRS

WASHINGTON, DC 20510-6250

August 9, 2010

MICHAEL L. ALEXANDER, STAFF DIRECTOR  
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Sent via Online Filing at [www.prc.gov](http://www.prc.gov)

Ms. Shoshana Grove  
Commission Secretary  
Postal Regulatory Commission  
901 New York Avenue NW, Suite 200  
Washington, D.C. 20268-0001

Postal Regulatory Commission  
Submitted 8/9/2010 3:20:33 PM  
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## **RE: Docket No. R2010-4, Rate Adjustment Due to Extraordinary or Exceptional Circumstances**

Dear Ms. Grove:

The purpose of this letter is to comment on the circumstances under which an exigent rate case is authorized under current law. As the author of the Postal Accountability and Enhancement Act of 2006 (PAEA), which grants the Postal Service the limited authority to file an exigent rate case, I want to make the congressional intent regarding the provision completely unambiguous as the Postal Regulatory Commission considers the pending Postal Service request. Neither the language nor the legislative history of the PAEA authorizes the United States Postal Service to file an exigent rate case under the current circumstances.

During the 2007 rulemaking process for the exigent rate case authority, Senator Tom Carper and I sent a letter to the Postal Regulatory Commission (PRC) explaining that the exigent rate authority in the PAEA was intended to be used sparingly. (Attachment 1). Specifically, the letter explained that the "extraordinary or exceptional circumstances" required to initiate an exigent rate case under the PAEA exist only if "terrorist attacks, natural disasters, and other events ... cause significant and substantial declines in mail volume or increases in operating costs that the Postal Service cannot reasonably be expected to adjust to in the normal course of business."

This letter lays out the express intent of the legislation, along with supporting legislative history. I urge the PRC to rely on it as you consider the Postal Service's request. As the author of the exigent rate authority, I can attest that the provision was *not* intended to be used under the current circumstances. Indeed, the Postal Service's current financial condition is largely the result of its own failure to sufficiently update its business model to adapt to predictable and natural cyclical changes in the economy and mail usage. The Postal Service's financial condition is not the result of "extraordinary or exceptional circumstances" required by law to initiate an exigent rate case. As such, I urge the PRC to dismiss the case.

### **Basis of Exigent Rate Case Authority**

In 2003, the PAEA created a rate-ceiling mechanism that allows prices for non-competitive products to be adjusted upward within the strict limit of the Consumer Price Index (CPI), averaged

over the prior 12 months. This rate cap was based on a recommendation the President's Commission on the United States Postal Service ("the Commission") included in its 2003 report to Congress. The Commission recommended that the ceiling be set below inflation in order to restrict revenue growth to motivate the Postal Service to pursue a far higher standard of efficiency. (Attachment 2). Ultimately, the PAEA set the cap at inflation, but the intent remains clear – the cap, in addition to creating stability and predictability, was set to induce the Postal Service to improve its business model and, ultimately, its effectiveness.

Recognizing the need for some degree of flexibility in extreme circumstances given the price cap, I included the provisions in the PAEA to allow the Postal Service to file an exigent rate case with the PRC. This provision, which allows the rates for market-dominant products to exceed CPI, was intended to provide the Postal Service with an extremely limited safety valve. The exigent rate case authority could *only* be used under "extraordinary or exceptional circumstances." Moreover, even if the strict standard were met, the proposed rate increases also must be "reasonable and equitable and necessary to enable the Postal Service...to maintain and continue the development of postal services to the kind of quality adapted to the needs of the United States."

Prior to enactment of the PAEA, I included a similar provision in a 2004 postal reform bill. *See* S. 2468 (104<sup>th</sup> Congress). As then-PRC Chairman George Omas stated in 2004 testimony before the Senate Governmental Affairs Committee (which I chaired), the availability of exigent rate authority "represents an enormous exception to the general thrust of postal ratemaking reform...." Chairman Omas further explained why any exigent rate authority granted must be available only under limited circumstances: "***A mechanism for regularly exceeding the rate levels around which postal management is expected to make its operational plans could completely undermine this central objective [of ratemaking reform].***" (Attachment 3 (Emphasis Added)). The Committee report for the 2004 version of the postal reform bill makes clear that exigent rate authority is intended to be used only for unexpected and extraordinary circumstances. (Attachment 4). The report further states that "The Committee hopes that these procedures will never be needed; however, it would be unwise not to recognize the potential need for rapid changes to the postal rate structure ***in the event of a national emergency.***" (Emphasis added). These were the standards I applied in drafting the 2004 version of postal reform – standards I incorporated when we revisited postal reform in the next Congress.

### **Purpose of Exigent Rate Case Authority**

When drafting the exigent rate case authority provision for the PAEA, I intended the provision to be used only in truly "extraordinary or exceptional" circumstances. As Congress considered postal reform in the 109<sup>th</sup> Congress, there was significant debate and discussion about the appropriate standard for allowing exigent rate changes. The Postal Service Board of Governors advocated for a lower standard – a standard similar to the "reasonable and necessary" authority included in a House-passed version of the postal reform bill. *See* H.R. 22 (109<sup>th</sup> Congress). The Congress ultimately rejected this less demanding standard and adopted the Senate's more stringent "extraordinary and exceptional circumstances" standard in the bill signed by the President.

Given the adoption of the Senate exigent rate case standard, legislative history before the Committee on Homeland Security and Governmental Affairs (the successor to the Governmental Affairs Committee) is particularly instructive. During a 2005 hearing before the Committee, the

Assistant Secretary of the Treasury for Financial Markets testified in support of the Senate standard, explaining that it establishes a “very high bar to increase rates above CPI.” (Attachment 5).

In 2006, when the exigent rate case authority was included in PAEA, it was intended to provide the Postal Service with an exception to the rate cap *only* when the Postal Service faces emergency situations. The standard was set high purposely to avoid excessive use of the flexibility and to prevent use of exigent rate cases as a tool to circumvent the rigid rate cap. Specifically, I envisioned that this authority would be limited to very few and extreme instances, such as terrorist attacks, the anthrax case, and natural disasters. For example, the terrorist attacks of September 11, 2001, or the anthrax attacks later that year could serve as the basis for an exigent rate case. These events had profound effects on the Postal Service well outside normal business cycles. No similar circumstances exist today.

Again, quoting former Chairman Omas during a 2004 Senate Governmental Affairs Committee hearing, “...exigent rate requests are appropriate to accommodate only those unanticipated cost increases that are truly extraordinary. Variances in volume levels and ordinary recurring costs should not qualify as a source of ‘exigent’ circumstances; these are contingencies for which postal management can reasonably be expected to plan, and for which it must be expected to adjust. Only those kinds of unexpected cost increases for which vigilant management could not reasonably have planned should provide grounds for ‘exigent’ rate requests.” (Attachment 6).

### **Application of Exigent Rate Case Authority to Current Circumstances**

As the author of the PAEA, I can unequivocally state that the law does not provide for an exigent rate case based on the rationale that the Postal Service provides in its current exigency case filing. The Postal Service attributes its need for an exigent rate increase to electronic diversion of the mail and the struggling economy. As set forth above, these circumstances fail to meet the “extraordinary or exceptional circumstances” standard clearly specified in the PAEA.

The Commission recognized in its 2003 report that electronic diversion threatens to accelerate a long-term decline in mail use as communication trends toward electronic alternatives. The Commission also identified that a weak economy is a cyclical factor that is a contributing threat to the Postal Service’s decline. These factors are reasonably predictable. When considering the PAEA over the course of the next three years, Congress was well aware of the fiscal challenges the Postal Service faced due to the cyclical nature of the economy and diversion of mail to electronic alternatives. Nonetheless, the Committee chose not to cite these predictably challenging circumstances in its explanation of “extraordinary and exceptional circumstances” standard that applies to exigent rate cases. As such, the legislative history does not support the Postal Service’s broad interpretation of the exigent rate case standard.

Although the language of the PAEA and its legislative history make clear that the Postal Service lacks the authority to pursue this case, I would be remiss if I did not mention the effect such price increases would have on the Postal Service and mailing community. After all, even if the Postal Service had the authority to pursue its exigent rate case (authority it lacks under these circumstances), the PRC is still required to consider whether the proposed exigent rate increases are “reasonable and equitable and necessary.” The exigency rate increases proposed by the Postal Service in this case fail to meet these requirements as well.

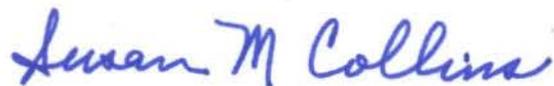
Even as far back as 2003, the Commission recognized that “[f]ar more emphasis must be placed on restoring fiscal stability not by ratcheting up rates or scaling back service, but by aggressively rooting out inefficiencies throughout the Postal Service.” (Attachment 7). This exigent rate case defies that direction from the Commission. Postmaster General John Potter himself acknowledged in a 2005 Homeland Security and Governmental Affairs Committee hearing, that, “Above all, we must have the ability to offer attractive and affordable rates.” (Attachment 8). Use of the exigent rate case as proposed by the Postal Service would not create affordable rates, which are essential to the Postal Service’s survival.

As you well know, the outcome of this case will have a significant effect on the \$1 trillion mailing industry, which supports approximately 7.5 million jobs nationwide. If approved, the rate increases would impose substantial costs on the mailing industry, would hurt small businesses and local newspapers, and undoubtedly would accelerate further decline in mail volume and revenues. The Postal Service will permanently lose business from catalog companies, publishers, and others. Some small newspapers may be forced to completely abandon their relationship with the Postal Service because of the increased costs, coupled with the possible decline in service proposed by the Postal Service.

The PRC’s approval of an exigent rate increase under these circumstances would be inconsistent with the law and would undermine the intent of PAEA to provide predictability and stability in postal pricing. In light of the express requirements of the statute and its supporting legislative history, I urge you to follow the letter of the law and reject the Postal Service’s exigent rate case proposal.

I appreciate your careful review and consideration of these matters.

Sincerely,



Susan M. Collins

CC: The Honorable Ruth Goldway, PRC Chairman  
The Honorable Tony Hammond, PRC Vice Chairman  
The Honorable Dan Blair, PRC Commissioner  
The Honorable Mark Acton, PRC Commissioner  
The Honorable Nanci Langley, Commissioner

Attachment 1.

JOSEPH I. LIEBERMAN, CONNECTICUT, CHAIRMAN

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**United States Senate**  
COMMITTEE ON  
HOMELAND SECURITY AND GOVERNMENTAL AFFAIRS  
WASHINGTON, DC 20510-8250

April 6, 2007

The Honorable Dan C. Blair  
Chairman  
Postal Regulatory Commission  
901 New York Avenue, NW  
Suite 200  
Washington, D.C. 20268

Dear Chairman Blair:

We write as the co-authors in the Senate of the Postal Accountability and Enhancement Act (Public Law 109-435, the Act) to provide comments on the ratemaking portion of that bill in response to the Advanced Notice of Rulemaking that the Postal Regulatory Commission (the Commission) issued on January 30, 2007.

In hearings and in discussions with postal management, postal employees, the mailing community, and other stakeholders, we learned that the current rigid and overly litigious rate-setting process limits the Postal Service's ability to adjust rates as needed and to adapt postal prices and products to a changing marketplace. We also heard from the mailing industry about the importance of predictability and stability in pricing. Predictability and stability, we were told, allows mailers to better plan their mailing and could allow them to increase the amount of business they do with the Postal Service. It was of primary importance to us in drafting the Senate version of the Postal Accountability and Enhancement Act and negotiating the final bill that the President ultimately signed that the new rate system offer the Postal Service maximum pricing flexibility while requiring, for Market-Dominant products, that they live within a tight, inflation-based rate cap.

The section of the Act calling for the creation of a new system for regulating the Postal Service's Market Dominant products lays out the nine major objectives of the new system. It also lists fourteen factors that the Commission should consider when developing the new system. The primary requirement, however, is the requirement that, for at least ten years, the system "include an annual limitation on the percentage changes in rates to be set by the Postal Regulatory Commission that will be equal to the change in the Consumer Price Index for All Urban Consumers." We intended the objectives to supersede the factors in issues affecting the system's design.

Page 2 of 2  
April 6 2007

In drafting the rate-setting section of the bill, we did choose to allow the Postal Service to carry unused rate authority over into future years, even if using such authority may result in a breach of the Consumer Price Index cap. We also chose to call for the development of a mechanism whereby the Postal Service may raise rates above the cap under "extraordinary or exceptional circumstances" that may hinder the Postal Service's ability to fulfill its universal service obligation or its ability to provide high quality service standards. We intended for this mechanism to be used sparingly, however.

In our view, the "extraordinary or exceptional circumstances" referenced in the language may include terrorist attacks, natural disasters, and other events that may cause significant and substantial declines in mail volume or increases in operating costs that the Postal Service cannot reasonably be expected to adjust to in the normal course of business. We expect that, in accordance with the requirement written into the bill, the Commission will closely examine any request from the Postal Service for permission to raise rates above the cap and hold public hearings in which the public may comment.

So long as a rate change put forward by the Postal Service is within the Consumer Price Index cap, it was our intention that the Postal Service should have significant flexibility to price their products in the manner they deem most appropriate to meet their needs and the needs of the mailing public. The 45-day period that the Act gives the Commission to review rate filing is largely intended to be used to determine whether or not a rate filing is within the rate cap.

Sincerely,



Susan M. Collins  
Ranking Member



Thomas R. Carper  
Chairman  
Subcommittee on Federal Financial  
Management, Government  
Information, Federal Services,  
and International Security

**Attachment 2.**

# EMBRACING THE FUTURE



MAKING THE TOUGH CHOICES TO PRESERVE UNIVERSAL MAIL SERVICE

Report of the President's Commission on the United States Postal Service

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## The Postal Service Requires Broader, Constructive Oversight

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The Commission proposes transforming the narrowly focused Postal Rate Commission ("PRC") into an independent Postal Regulatory Board with broad authority to safeguard the public interest without micromanaging day-to-day postal operations.

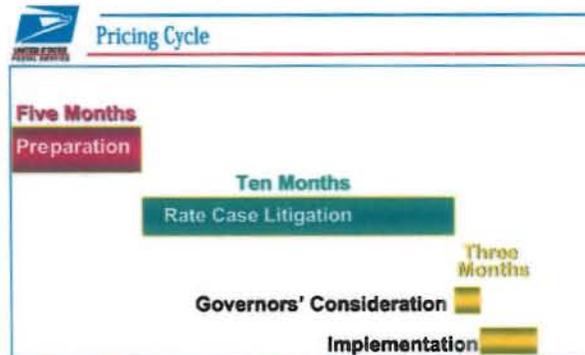
Rather than a sole focus on rate-setting and mail classifications, the Postal Regulatory Board would be tasked with broad public-policy oversight, including: ensuring financial transparency; guarding against the cross-subsidization of competitive products; reviewing the scope of the postal monopoly; limiting the prices charged for non-competitive products; overseeing the scope of the universal service obligation; reviewing worksharing and other discounts; reviewing changes to service standards that may have a substantial and negative national impact; and ensuring the Postal Service meets its statutory obligation to compensate its employees at a level comparable to (but not exceeding) the private sector.

The Commission envisions a Postal Regulatory Board that is an independent establishment of the executive branch of the U.S. government and is composed of three individuals of significant stature, appointed by the President of the United States and confirmed by the Senate.

Once assembled, the Postal Regulatory Board should move quickly to improve the rate-setting process for both postal customers and managers. The current process is far too cumbersome and time-consuming, with rate changes taking as long as 18 months, an impossible situation for an institution charged with the responsibility of acting in a businesslike manner.

As an alternative to the current process, the Commission proposes the establishment of a rate-ceiling mechanism that would allow prices for non-competitive products to be adjusted upward within strict limits, subject to an after-the-fact review by the Postal Regulatory Board. Specifically, the Commission proposes setting the ceilings below inflation, thereby restricting revenue growth to motivate the Postal Service to pursue a far higher standard of efficiency.

A well-designed rate ceiling could produce a Postal Service much more aligned with the interests of ratepayers, who would prefer that the Postal Service aggressively tackle unnecessary costs before asking them to pay more for stamps. However, designing this mechanism is an intricate undertaking. Fortunately, recent legislation signed into law by President Bush strongly discourages the Postal Service from increasing rates before 2006, providing ample time for the Postal Regulatory Board to fine-tune a workable rate-ceiling mechanism.



Source: USPS.

**Attachment 3.**

**United States Senate  
Committee on Government Affairs  
Testimony of George Omas  
Chairman, Postal Rate Commission  
April 7, 2004**

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Chairman Collins, members of the Committee, thank you for providing me with the opportunity to testify on ways to achieve meaningful postal reform. The Committee has already heard from a number of thoughtful witnesses about the need to modernize the structure of the Postal Service to foster best management practices and more efficient and economical operations.

I agree that postal reform is necessary. Furthermore, I think that the five principles for postal reform outlined by the Administration, following receipt of the Report of the President's Commission on the Postal Service, provide a sound policy foundation for effective reform.

I believe that the two pieces of postal reform legislation drafted in the last Congress, S. 1285 and H.R. 4970, were for the most part consistent with those five principles. I suggest that they provide a good basis for developing an effective vehicle for achieving real reform.

My testimony today will focus on how those earlier efforts can be clarified and improved to be even more consistent with the Administration's five principles. I will also mention several ways to improve on suggestions made by the President's Commission on the Postal Service where they vary from the model developed in those earlier bills and are unlikely to foster results consistent with the Administration's principles. I will restrict my testimony to areas where, as Chairman of the Postal Rate Commission, I have developed first-hand expertise.

Postal reform should provide a balanced and flexible approach for establishing postal rates and fees. The flexibility inherent in the previously proposed provisions should be retained, including a "safety valve" opportunity for the Postal Service to recoup costs resulting from extraordinary, unforeseeable expenses that would otherwise drive rates above the price caps. The mechanism for doing so would be an extraordinary or "exigent" rate request by the Postal Service. For example, H.R. 4970 would allow the rates for a market-dominant product to increase beyond the comparable rise in the Consumer Price Index if the regulator finds such increase "reasonable and equitable and necessary to enable the Postal Service ... to maintain and continue the development of postal services of the kind and quality adapted to the needs of the United States."

If an "exigent" rate request mechanism is likely to remain a feature of postal ratemaking reform, several observations must be made.

The availability of any such mechanism represents an enormous exception to the general thrust of postal ratemaking reform as it has been considered to date. Incentive-based ratemaking, and the management discipline it is intended to enforce, have been central to the vision of a reformed Postal Service.<sup>3</sup> A mechanism for regularly exceeding the rate levels around which postal management is expected to make its operational plans could completely undermine this central objective.

If ratemaking reform is to achieve the intended purposes of heightened management vigilance over costs and enhanced operational efficiency, the "exigent" request mechanism must not be allowed to erode or ultimately supersede the new system of incentive rates. For this reason, final authority to establish the appropriate

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<sup>3</sup> As one analyst has noted, "[Congressman McHugh's] Subcommittee's reform proposal advocating price cap pricing regulation for the USPS became the central vision around which the reform discussion turned." Reisner, Robert A. F., *Price Caps and the US Postal Service: Prospects, Perils and the Public Interest*, p. 3, presented to the President's Commission on the United States Postal Service, May 29, 2003.

Calendar No. 674

108TH CONGRESS }  
2d Session

SENATE

{ REPORT  
108-318

POSTAL ACCOUNTABILITY AND  
ENHANCEMENT ACT

REPORT

OF THE

COMMITTEE ON GOVERNMENTAL AFFAIRS  
UNITED STATES SENATE

together with

ADDITIONAL VIEWS

TO ACCOMPANY

S. 2468

TO REFORM THE POSTAL LAWS OF THE UNITED STATES



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U.S. GOVERNMENT PRINTING OFFICE  
WASHINGTON : 2004

29-010

appropriate for different product groupings. However, establishment of schedules for rate changes should be designed to provide a necessary and appropriate level of predictability; it should not be designed to unreasonably restrict the ability of the Postal Service to adjust prices within the rate cap.

To provide for adequate review of any proposed changes in market-dominant product price, a 45-day prior review period is established. This period begins with the Postal Service's public notice of a price adjustment affecting a market-dominant product or products and will provide the Postal Regulatory Commission an opportunity to review the adjustment. If the Postal Regulatory Commission finds that the price adjustment is not in compliance with the established statutory and regulatory requirements, it must notify the Postal Service within the 45-day notice period. In response to this notice, the Postal Service shall describe the actions to be taken to ensure that the rate change is in compliance with the statutory and regulatory requirements. While the Postal Service is expected to respond adequately to any Postal Regulatory Commission determination of noncompliance prior to the scheduled rate implementation, the burden is on the Postal Regulatory Commission to provide adequate notice of noncompliance permitting a Postal Service response prior to the expiration of the 45-day period. If either intentionally or inadvertently, the Postal Regulatory Commission does not notify the Postal Service of any noncompliance, the Committee believes that there would be no impediments to the Postal Service implementing the rate adjustment as noticed at the end of the 45-day period. The Committee clearly recognizes that the 45-day review period is short and has determined that a short review period is consistent with the goals of increasing Postal Service pricing flexibility. To facilitate review of rate adjustments, the Committee presumes that extremely clear and well-defined standards will be established by regulation allowing the Postal Service and the Postal Regulatory Commission to make a rapid determination of whether a rate adjustment meets the applicable criteria. The review period is not intended to be used to evaluate the regulatory structure; if a full review of the regulatory structure is deemed to be necessary, the Committee expects that, during the period of any review of the regulatory structure, the Postal Service will be permitted to adjust rates under the regulatory requirements in effect as of the date of public notice of the adjustment. Therefore, any changes in the regulatory structure will be applicable only to rate adjustments noticed by the Postal Service after the date the new regulations are established.

The Committee believes that the rate cap system to be established under this statute by the Postal Regulatory Commission should give the Postal Service the flexibility to respond to all circumstances it is likely to face in the normal course of business. However, the terrorist attacks of September 11, 2001 and the subsequent use of the mail to transmit anthrax highlight the need to address unexpected and extraordinary circumstances and their effect on the Postal Service and its financial requirements. Therefore, the Postal Regulatory Commission shall establish procedures under which the Postal Service can adjust rates on an expedited basis due to unexpected and extraordinary circumstances. The Committee hopes that these procedures will never be needed; however, it

would be unwise not to recognize the potential need for rapid changes to the postal rate structure in the event of a national emergency.

#### *Workshare discounts*

The Committee has heard testimony from many parties describing the benefits of the Postal Service's worksharing program. This program was developed by the Postal Service and the Postal Rate Commission to enable customers to pay lower rates when they perform mail preparation or transportation activities such as presorting, prebarcoding, and certain other mail handling activities that would otherwise be performed by the Postal Service. This worksharing program has induced mailers to invest in equipment and processes that facilitate the Postal Service's automation program, has reduced mailing costs, and has otherwise made mail a more economically attractive medium.

The Committee agrees with the principle, supported by the Postal Service, the Postal Rate Commission, and postal employees, that workshare discounts should generally not exceed the costs that the Postal Service avoids as a result of the worksharing activity. When discounts are kept below the costs saved by the Postal Service, mailers have a financial incentive to do work more efficiently than the Postal Service can do it, yielding savings to the participating mailers, to the Postal Service, and to other postal customers whose rates are kept down by the Postal Service's savings under the program.

However, there are four circumstances under which workshare discounts in excess of avoided costs have historically been allowed by the Postal Rate Commission and are warranted, and the Committee has codified these exceptions in the legislation:

- The first exception applies when a discount is associated with a new or changed postal product and is needed, for up to 4 years, to induce mailer behavior that furthers the economically efficient operation of the Postal Service. Such a discount can encourage mailers to invest in new technologies or practices that will save the Postal Service money, and can then provide the Postal Service an opportunity to achieve the resulting efficiencies. For discounts already in effect on the date of enactment, the 4-year period begins on that date.

- The second exception provides that a workshare discount may exceed costs avoided if a reduction in the discount would—(i) lead to a loss in volume of the affected category of mail and thereby reduce the aggregate contribution to institutional costs, (ii) result in a further increase in rates paid by mailers not able to take advantage of the discount, or (iii) impede the efficient operation of the Postal Service.

- The third exception allows a workshare discount to exceed costs avoided if that excess portion of the discount is necessary to mitigate rate shock and will be phased out over time. Discounts under this exception, like those under the first exception, are time-limited.

- The fourth exception applies to discounts that are provided in connection with subclasses of mail consisting exclusively of material having educational, cultural, or scientific value. Discounts

**Attachment 5.**



**DEPARTMENT OF THE TREASURY  
OFFICE OF PUBLIC AFFAIRS**

Embargoed Until 10 a.m. EST  
April 14, 2005

CONTACT: Mary Diamond  
(202) 622-2960

**HEARING TESTIMONY  
THE HONORABLE TIMOTHY S. BITSBERGER  
ASSISTANT SECRETARY OF THE TREASURY FOR FINANCIAL MARKETS  
ON REFORM OF THE UNITED STATES POSTAL SERVICE  
BEFORE THE  
COMMITTEE ON HOMELAND SECURITY AND GOVERNMENTAL AFFAIRS  
UNITED STATES SENATE**

Madam Chairman and distinguished Members of the Committee, thank you for the opportunity to testify today on the need for comprehensive postal reform. I welcome this opportunity to underscore the Administration's strong interest in enacting comprehensive legislation to reform the United States Postal Service.

**The Administration Supports Enactment of Postal Reform**

The President has consistently articulated the need for comprehensive reform to set the Postal Service on sound, long-term operational and financial footing. The Administration has been holding regular meetings with Congress and many stakeholders to ensure that we hear everyone's perspective and that our message is heard as well. I would like to extend the Administration's thanks to the Members and leadership of this Committee for working with us on postal reform legislation and we look forward to continuing that productive dialogue going forward. The Administration also appreciates Postmaster General Jack Potter's strong leadership and hard work to drive change within the Postal Service, and we have enjoyed working closely with him and his staff.

I would like to begin my testimony by outlining the five principles of reform that the Administration has supported. These principles are as follows:

- **Self-Financing** - The Postal Service should be self-financed. This was the intent of the 1970 Postal Reorganization Act, but thus far it has never been accomplished. Today we are at a point, due in no small part to the Postal Civil Service Retirement System Funding Reform Act of 2003 (hereafter "the Postal CSRS Funding Reform Act"), P.L. 108-18, where we can ensure that the Postal Service covers all of its costs, including its massive unfunded liabilities, without potentially crippling effects on ratepayers.

2. that productivity at the Postal Service has lagged the private sector by large margins since 1972 and therefore significant opportunities for a more productive Postal Service exists and this would enable it to operate within CPI;
3. to give the Postal Service stronger incentives to control its costs by discouraging it from simply passing costs on to ratepayers through a cost-based regulatory structure ; and
4. that wages generally rise faster than prices over time. This is largely due to increases in labor productivity. This difference in productivity allows firms to raise real wages without passing along costs to consumers through price increases. Generally, productivity improvements are expected to reduce prices.

We support the Committee's intent to establish a hard cap at CPI, and further support the Senate's version of an "escape clause," or exigency rate case, which establishes a very high bar to increase rates above CPI. This pricing flexibility will undo the current practice of irregular and lengthy rate cases that offer the Postal Service little managerial discretion and little or no predictability for the ratepayers.

We also seek to provide the Postal Service with flexibility on its cost side as well. We note that the Postal Service's \$66 billion cost base provides significant opportunity for cost reductions without jeopardizing service quality or its universal service obligation. While some may dispute the absolute size of the potential reductions, it is indisputable that productivity at the Postal Service has lagged the private sector by large margins and that more effective management practices should be able to make significant progress in this area. One opportunity is in the underlying processing and distribution network and the potential to use this network in a more efficient manner.

Flexibility is not a blank check though. The Postal Service currently has the ability to negotiate its portion of the premiums for health and life insurance for its employees. The Postal Service has taken advantage of this ability and negotiated benefits beyond those offered by the U.S. Government. For instance, the Federal government pays 72 percent of an employee's health insurance premium while the Postal Service pays 85 percent of an employee's health insurance premium. Through this flexibility, the Postal Service has increased its costs by an additional \$734 million. With respect to Basic life insurance, the Federal government pays 33 percent of an employee's Basic life insurance premium while the Postal Service pays 100 percent of an employee's Basic life insurance premium. Combined, the Postal Service has increased its costs for health and life insurance premiums by over \$870 million annually above what the Federal government pays for most of its other employees.

We believe that it would be counter-productive to provide a list of specific cost reductions in statute, and instead have focused on a model where management has the flexibility to operate as a business within the constraints of a rate cap. This provides the right incentives for management without Congress or the Executive Branch micro-managing the business. In this way, the rate cap also drives greater board and management accountability, which is an important principle for the Administration.

#### **Ensuring Self-Financing – Unfunded Liabilities**

The Administration believes that comprehensive postal reform must require the Postal Service to cover all of its financial obligations, including its on and off-balance sheet unfunded liabilities. This is consistent with the statutory requirement that the Postal Service meet its responsibilities in a businesslike fashion by ensuring that revenues from the sale of products and services are sufficient to cover all operating costs. This concept of self-financing ensures that the Postal Service will operate in a manner that strengthens the financial and operational health of the Postal Service. It is important to recognize that since the 1970 Postal Reorganization Act, the Postal Service has never satisfied the statutory mandate of being fully self-financed. The Postal Service has accumulated approximately \$75 billion of unfunded post-retirement health, pension and workers' compensation liabilities. Additionally, the Postal Service received approximately \$27 billion of taxpayer funded appropriations since the 1970 Postal Reorganization Act.

**Attachment 6.**

**United States Senate  
Committee on Government Affairs  
Testimony of George Omas  
Chairman, Postal Rate Commission  
April 7, 2004**

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Chairman Collins, members of the Committee, thank you for providing me with the opportunity to testify on ways to achieve meaningful postal reform. The Committee has already heard from a number of thoughtful witnesses about the need to modernize the structure of the Postal Service to foster best management practices and more efficient and economical operations.

I agree that postal reform is necessary. Furthermore, I think that the five principles for postal reform outlined by the Administration, following receipt of the Report of the President's Commission on the Postal Service, provide a sound policy foundation for effective reform.

I believe that the two pieces of postal reform legislation drafted in the last Congress, S. 1285 and H.R. 4970, were for the most part consistent with those five principles. I suggest that they provide a good basis for developing an effective vehicle for achieving real reform.

My testimony today will focus on how those earlier efforts can be clarified and improved to be even more consistent with the Administration's five principles. I will also mention several ways to improve on suggestions made by the President's Commission on the Postal Service where they vary from the model developed in those earlier bills and are unlikely to foster results consistent with the Administration's principles. I will restrict my testimony to areas where, as Chairman of the Postal Rate Commission, I have developed first-hand expertise.

level of revenues to be recovered through exigent rate increases should reside with the regulator, not the Postal Service. Judicial review of such determinations should be made available to ensure appropriate oversight and relief.

Further, there should be a shared understanding that "exigent" rate requests are appropriate to accommodate only those unanticipated cost increases that are truly extraordinary. Variances in volume levels and ordinary recurring costs should not qualify as a source of "exigent" circumstances; these are contingencies for which postal management can reasonably be expected to plan, and for which it must be expected to adjust. Only those kinds of unexpected cost increases for which vigilant management could not reasonably have planned should provide grounds for "exigent" rate requests.

In my opinion, in the last 25 years there has been only one circumstance that would have justified an exigent rate increase, namely the combined effects of the 9/11 terrorist and anthrax attacks of late 2001. Because of the urgent nature of exigent requests, I would expect them to be considered with extreme expedition, with the focus exclusively on the nature of the emergency, and on quantification of the need for emergency financial relief.

#### ***Prior Review of Market Dominant Rates***

Although S. 1285 and H.R. 4970 would leave it to the regulator to determine what substantive criteria to emphasize in setting market-dominant rates (price cap, cost of service, etc.), it is not entirely clear what procedural latitude they would give the regulator to implement the rate-setting system that it selects. Section 3653 requires the regulator each year to prepare a report, with public input, determining whether the rates that the Postal Service charged during the past year were in compliance with the statute and implementing regulations. Section 3662 requires the Commission to review third-party complaints that current rates and services do not comply with the statute or its implementing regulations. These forms of review of Postal Service rates and service performance are the only ones mentioned. S. 1285 and H.R. 4970 do not, by their terms, make these forms of review exclusive; however, one might argue that by not

# EMBRACING THE FUTURE



MAKING THE TOUGH CHOICES TO PRESERVE UNIVERSAL MAIL SERVICE

Report of the President's Commission on the United States Postal Service

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## Universal Postal Service Is at Risk

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First-Class Mail volumes appear to be on the brink of long-term decline as more Americans take advantage of cheaper electronic alternatives. The rates of growth for First-Class Mail and Standard Mail, that together generate more than 75% of all postal revenues, have been in long-term decline since the 1980s. Electronic diversion threatens to accelerate this trend significantly. Unless Postal Service expenses can be similarly reduced, it is questionable whether affordable universal mail service via a self-financing public institution is sustainable.

With its debt reaching destabilizing levels and its traditional revenue streams in retreat, the Postal Service's transformational efforts and long-term outlook were placed on the U.S. General Accounting Office's "high-risk list" in 2001. At the request of Congress, the Postal Service began developing its Transformation Plan to adapt to the future. Since the Plan's release in April of 2002, the Postal Service has reduced its workforce by more than 40,000 career positions and will deliver \$2.5 billion in annual cost savings by September 30, 2003. However, even with this substantial progress, it is quite possible that the Postal Service will experience significant (and rapidly ballooning) deficits within just a few years' time, even if stamp prices continue to rise with inflation. This prospect points to the urgent need for a far more sweeping set of reforms.

Even if the Postal Service were not in financial jeopardy, however, the inefficiency of its operations and legacy network today causes billions of dollars in unnecessary costs that should be eliminated rather than passed on to ratepayers. **Far more emphasis must be placed on restoring fiscal stability not by ratcheting up rates or scaling back service, but by aggressively rooting out inefficiencies throughout the Postal Service.**

Unfortunately, a cumbersome regulatory and rate-setting model, the entrenched cost of an aging infrastructure, inflexible work arrangements, and other significant

obstacles clutter the path to a fundamental overhaul of the Postal Service. As a result, the institution urgently requires broader flexibility to adjust to increasingly dynamic markets and to pursue new strategies to bring revenues and expenditures into balance without sacrificing quality of service and the ability to meet the nation's evolving postal needs. In short, the Postal Service needs a new business model for the modern world and the changing postal needs of the nation.



Source: USPS.

**Attachment 8.**

**TESTIMONY OF  
JOHN E. POTTER, POSTMASTER GENERAL/CEO,  
BEFORE A HEARING OF THE  
COMMITTEE ON HOMELAND SECURITY  
AND GOVERNMENTAL AFFAIRS  
UNITED STATES SENATE  
APRIL 14, 2005**

Good afternoon, Chairman Collins and Committee members. I am pleased to be with you today as we continue the critical discussion about the need for comprehensive reform of the legislative framework governing the Postal Service.

We appreciate the Committee's leadership in hearing from a broad range of postal stakeholders as part of its work in attempting to develop reform legislation that protects universal service – our ability to provide quality, affordable, accessible mail service to every household and business in America.

That has been, and continues to be, the role of the United States Postal Service. And we are proud of that role. We are, perhaps, the most tangible daily link between the people of America and their government. Yet we are profoundly different from other government agencies. That's because postal operations are funded by the sale of postal products and services – not by tax dollars. In fact, the Postal Service is self supporting and has not received a public service appropriation since 1982, saving American taxpayers more than \$11 billion, the amount authorized by law.

This has not always been the case. Until today's Postal Service was created in 1971, 18 percent of the annual costs of operating the former Post Office Department were paid by direct appropriations – tax dollars. A self-supporting Postal Service – one that has broken even over its 34-year history – is among the significant legacies of the landmark 1970 legislation that created today's Postal Service.

At the same time, we recognized the obligation of the Postal Service to push business effectiveness and operational efficiency to the limits permitted by current postal laws. We were encouraged in this direction by Congress and by the Government Accountability Office.

The result was our comprehensive Transformation Plan. With wide-ranging stakeholder input, we created the Plan to help us meet the challenges of long-term technological and commercial trends that are fundamentally reshaping the postal landscape here and throughout the world.

As the process of legislative reform continues, the Postal Service understands that it cannot relax its efforts. We must continually work to offer better value than ever. We must continue to offer a favorable return on our customers' investment. We must continue to offer ease of use. We must continue to offer the solutions our customers need. Above all, we must have the ability to offer attractive and affordable rates. This is why one of our key transformation strategies is fostering growth by continuing to increase the value of postal products and services to our customer.

To do that, we have challenged our managers to "think outside the box." And they have come through. They responded with creative approaches to pricing and to products. Across the entire organization – in every functional area – our people understood the need for change. They made implementation of our Transformation Plan their focus, and they delivered results.