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American Bankers Association

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Before the
POSTAL REGULATORY COMMISSION
WASHINGTON, D.C. 20268-0001

STATUTORY REVIEW OF THE SYSTEM FOR REGULATING RATES AND CLASSES FOR MARKET DOMINANT PRODUCTS	Docket No. RM2017-3

COMMENTS OF AMERICAN BANKERS ASSOCIATION
(March 1, 2018)

The American Bankers Association (ABA),[1] on behalf of its member banks, is pleased to provide the following comments to the U. S. Postal Regulatory Commission (PRC) in response to the second phase of the statutory review of the system for regulating rates and classes for market dominant products. We ask that the PRC reconsider its decision to make the statutory consumer price index (CPI) cap the floor for future rate increases, rather than the ceiling as the statute requires.

While the PRC trumpeted that it maintained a price cap in its press statements announcing the results of Phase 1 of these proceedings, the details suggest otherwise. By allowing the Postal Service to set rates above CPI, especially when coupled with supplemental rate increases which the PRC would also permit, the net effect is that postal rates can rise *much faster than the rate of inflation* going forward. Each time the Postal Service raises rates, the increase gets added the previous base and

[1] The American Bankers Association is the united voice of America's hometown bankers—small, regional and large banks that together employ more than 2 million women and men, hold nearly $17 trillion in assets, safeguard $12.8 trillion in deposits and extend more than $9 trillion in loans. Through a broad array of information, training, staff expertise and other resources, ABA supports America's hometown bankers as they perform their critical role as drivers of America's economic growth and job creation.

compounded over time. Accounting for compounding, postal rates could get dramatically more expensive under the PRC's proposal. **It is not difficult to imagine postal rates 25-30% higher than they are today once American mailers travel down the five-year toll road the PRC would build through this proceeding.**

This is not what Congress intended, it does not match the plain language of the statute, and most of all it will very likely hurt the Postal Service in the long run in the form of reduced demand for postal services. The PRC is attempting to solve a problem (pre-funding obligations) that was caused by, and that should be solved by, Congress. Banks of all sizes and charters across America ask the PRC to reconsider.

Banks and the Mail

Whether through periodic statements or marketing communications, every single day banks reach out to customers through a variety of communication channels to provide them with information to assist them with their financial interests. Technological innovation and costs drive banks to consider alternative forms of delivery in the service of our customers, yet mail still remains an important vehicle of distribution. Banks are one of the largest customers of the Postal Service, accounting for a significant amount of mail volume and postal service revenue annually. From the Postal Service's perspective, the billions of pieces of mail banks annually send are generally highly-profitable commercial mail, and light-weight, automation-compatible letter mail, making banks a key stakeholder for the Postal Service. The ABA and its member banks highly value the Postal Service and its services, and are committed to working constructively with all stakeholders to identify long-term solutions that ensure an efficient, self-sustaining, and affordable U.S. postal system.

Should it Continue on its Current Course, the PRC Will Accelerate the Use of Digital and Other Alternative Communication Channels, Hastening the Decline of the Postal Service

The PRC fails to appreciate the potential unintended consequences that may come from this rulemaking. Even if the PRC had the authority to modify the statutory price cap (as discussed below, it does not), it would be imprudent for it to do so. Trying to solve the financial problems of the Postal Service by means of price increases alone poses a significant risk for the system. As postal rates rise, the cost-benefit calculation made by mailers of all sizes, including many large and small banks across the United States, changes.

The banking industry is a large overall mail volume industry in part because it is a convenient and cost-effective way for banks to communicate with their customers, and for customers to remit payments to banks. However, the banking industry's demand for postal services is not completely inelastic. Alternatives to the postal service exist – and, in many cases, are preferred by consumers. With the advances in technology and security that have occurred since passage of the Postal Accountability and Enhancement Act (PAEA),[2] consumers are increasingly using electronic means to conduct banking and other financial transactions for ease, speed, and convenience. Innovations in smart phones, tablets, and mobile internet communications have facilitated growth in financial technology, and are increasingly becoming the standard

[2] P.L. 109-435 (2006).

for banking transactions.[3] Large, unpredictable postage price increases provide banks the incentive to aggressively work at driving consumers toward online platforms and away from the mail. This drives volume out of the system, and hastening USPS's financial decline. For the banking industry, there is a particular risk that the PRC may inadvertently accelerate diversion trends that are already underway.

On the other hand, stable postage rates that remain at or below the Consumer Price Index (CPI) provide the predictability necessary for banks to plan for the robust direct and standard mail programs in which bankers want to continue to invest. As discussed below, the current CPI cap system also provides an important additional feature: effective external motivation for the Postal Service to control costs and scale to today's mail volume. Quality, dependable service is another reason for banks to continue to invest in the system, and an important complement to cost.

We believe that the very best thing the PRC could do in connection with the review is nothing at all. As we outlined in our Phase 1 comments, the current system is working as intended. We encourage the PRC to reconsider its Phase 1 decision.

The Commission's Phase 1 Findings Should Be Revisited, as the Commission's Scope of Review is Overbroad and Not Supported by the Plain Language of the Statute

The Commission does not have the authority to turn the statutory CPI price cap into a floor, rather than a ceiling, and any attempt to do so would amount to a dramatic

[3] We note that these trends are likely true outside of the banking industry as well – for example, under the PRC's rules, comments must be filed online, rather than through the mail, unless a waiver is obtained. Although the PRC regulates the Postal Service, it prefers electronic filing because "[f]iling online increases security, stability and functionality for dockets processing." https://www.prc.gov/how-to-participate; *see also* 39 CFR 3001.9(a).

and unsupportable regulatory overreach. The Commission has previously and correctly held that the CPI price cap is "central" and "indispensable."[4] The PRC's proposal would be inconsistent with this prior interpretation, and an unreasonable interpretation of the plain language of the statute.

The CPI cap is just that—a cap—and is a prominent feature of the statutory architecture. Indeed, the very first requirement of the rate system contemplated by PAEA is the CPI cap. *See* 39 U.S.C. 3622(d)(1) ("The system for regulating rates and classes for market-dominant products <u>shall</u> (A) 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") (emphasis added).

Nor can the statutory requirement that the Commission undertake this proceeding suggest that the CPI cap applied only to the *first* rate system the Commission might establish. If that were true, Congress would have said so. Rather, the consistent use of the word "system" throughout the section, rather than qualifiers such as "first system" or "initial system" or "system preceding the 10 year review," suggests Congress contemplated the same requirements applying to any and all rate structures the Commission would create. At all times there is only one system—the CPI price cap <u>shall</u> apply to the first system, and <u>shall</u> apply to any system created thereafter. *See* 39 U.S.C. 3622(d)(1). The passage of time and a requirement for notice and comment rulemaking does not change this fact.

Moreover, by its terms, this review is limited to "the system for regulating rates and classes for market-dominant products established under this section," 39 U.S.C. 3622(d)(3), which is the "modern system for regulating rates and classes for market-

[4] Docket No. R2010-4, Order No. 547 (Sept. 30, 2010) at 49.

dominant products" the PRC created "within 18 months after the date of enactment of" PAEA. 39 U.S.C. 3622(a). In other words, Congress instructed the Commission to review the system the *Commission* created, not the limitations on that system *Congress* created. The Commission correctly recognized in 2007 that any system must accommodate the statutory CPI price cap. The Commission has an obligation to provide a reasoned basis for departing from its previous position.

A single floor statement from a single Senator does not change the plain language of the statute. Moreover, a floor statement from a single Senator – even a Committee Chairman – does not constitute definitive legislative history of this bill. There is no committee report or other authoritative legislative history to discern Congressional purpose. Where, as here, the text of the statute is clear, that begins and ends the inquiry.

Applying a Statute Involves Using All of the Words, Not Just Some of Them

The Commission elected to take the nine objectives defined by the statute and, instead of applying each of them independently, separately create out of whole cloth "three principle areas of the PAEA system as set forth by the objectives."[5] Those three areas, and this approach, find no support in the statute. The three factors – (1) the structure of the ratemaking system; (2) USPS financial health; and (3) service – impermissibly leave a significant amount of the statute on a regulatory cutting room floor.

Importantly, this approach elevates the USPS financial health to a much higher position than Congress intended. When viewed in full, the nine objectives defined by

[5] Order at 17.

the statute demonstrate that Congress intended the PRC to consider, but not find determinative, the financial condition of the USPS. The nine objectives are:

> Objective 1: to maximize incentives to reduce costs *and* increase efficiency.
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> Objective 2: to create predictability *and* stability in rates.
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> Objective 3: to maintain high quality service standards established under section 3691.
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> Objective 4: to allow the Postal Service pricing flexibility.
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> Objective 5: to assure adequate revenues, including retained earnings, to maintain financial stability.
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> Objective 6: to reduce the administrative burden and increase the transparency of the ratemaking process.
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> Objective 7: to enhance mail security and deter terrorism.
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> Objective 8: to establish and maintain a just and reasonable schedule for rates and classifications, however the objective under this paragraph shall not be construed to prohibit the Postal Service from making changes of unequal magnitude within, between, or among classes of mail.
>
> Objective 9: to allocate the total institutional costs of the Postal Service appropriately between market-dominant and competitive products.[6]

Only one objective deals with adequate revenue, while the others demonstrate that Congress intended the PRC to force the Postal Service to reduce costs and increase both operational efficiencies and service. The "principal areas" approach thus gives disproportionate weight to Objective 5 relative to the rest of the statute.

As the PRC itself noted, "[a] key principle in statutory interpretation is to give proper meaning to all provisions of the statute."[7] The PRC separately found that it

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[6] 39 U.S.C. § 3622(b) (emphasis added).
[7] Order at 15.

must give all of the objectives equal weight.[8] That is especially important where, as here, it is likely that each objective is based on different Congressional motivations or desires. The PRC should review each objective independently.

For bankers, stability, predictability, and just and reasonable rates are paramount, and it is not directly clear from this record how the PRC has considered these factors. The core of the PAEA system are protections that ensure USPS accountability, affordability, reliability and stability. Historical context sheds light on this fact. The fundamental compromise of the PAEA was granting the Postal Service increased pricing flexibility in exchange for granting mailers the certainty and security of affordable, predictable postal price increases in the form of a statutory limitation on rate increases through the CPI price cap. In the absence of competition, the cap is intended to serve as a surrogate or proxy for competitive market forces by providing a control on inefficiency in the Postal Service. In order to keep growth in prices equal to or under the rate of change in the CPI while earning net income, the Postal Service must keep its costs down through efficient management of its resources. It also must focus its attention on available opportunities for growth, and providing service that creates a strong value proposition for postal customers.

Instead, the effectively Commission gives the USPS a free pass on these fronts.

- **The PRC's proposal would lead to rate increases that are neither just nor reasonable (Objective 8; Factor 4).** In fact, the Commission's proposal would allow USPS to recover substantially more than the Commission says is necessary as a result of its design. It is designed to

[8] Docket No. ACR2008, Annual Compliance Determination, March 30, 2009, at 36 (rejecting argument that certain objectives should be given a "higher priority" over the others) (FY 2008 ACD); Docket No. ACR2015, Annual Compliance Determination, March 28, 2016, at 5 (FY 2015 ACD).

recover the PRC's assessment of the need with the 2% and there is no commitment to remove these increases. Any increases after the five years would build upon this based and create recovery beyond what the PRC has determined as necessary.

- **The PRC's proposal fails to create stability (Objective 2).** Stable prices increase at the rate of inflation. Limiting rate increases to CPI through the price cap has succeeded in moderating and smoothing out postal price increases, providing commercial mailers the certainty they need to make business and investment decisions concerning the mail.
- **The PRC's proposal fails to create predictability (Objective 2).** Section 3622(d)(3) allows the Commission to change the rate system whenever it choses "as appropriate thereafter."[9] Even assuming the current proposal lasts the full 5 years, the uncertainty of future unconstrained rate increases will undermine the commitment and investment in the mail.
- **The PRC's proposal fails to provide incentives for the USPS to control costs (Objective 1; Factor 12).** Very simply, supplemental rate authority will be seen by USPS as the equivalent of found money. It will be all too easy for USPS to use this as the easiest option to increase cash flow, instead of taking more difficult steps that could increase productivity and profitability. Even if it were permissible to elevate objective 5 and the goal of financial stability above all others (it is not), this is simply a band

[9] 39 U.S.C. § 3622(d)(3).

aid over larger problems. Without cost reductions and efficiency improvements, additional revenue alone will only give the appearance of stabilizing the system. Over the long run this may be counterproductive, given the very real diversion risks noted above.

The Commission's proposal does not balance competing objectives as required by law. In fact, the Commission fails to cite *any other objective* in support of the "supplemental" rate authority. This is impermissible under the plain language of section 3622(b) and is inconsistent with the Commission's acknowledgement that it is required to treat all objectives equally.

The PRC's Assessment of the Postal Service's Financial Stability Was Unsound and Incomplete

The Commission's financial assessment should have been limited to the Postal Service's duties as prescribed by law – the ability to continue to provide universal, affordable mail service. *See* 39 U.S.C 403. By any analysis, the Postal Service is strong in this area and getting continuously stronger.

PAEA and the associated CPI price cap have helped to drive efficiency and cost discipline in the Postal Service's operations. By focusing on the growth of e-commerce and package delivery, the Postal Service has offset much of the decline in volume for First Class and Standard mail. As a result, the Postal Service maintained continuous operations despite significant mail volume declines associated with electronic diversion and the Great Recession. The effectiveness of the price cap is also demonstrated by the fact that the Postal Service continues to generate significant revenues on an operating basis, and by the dramatic recent growth in shipping and package delivery. While it recorded a loss in FY 2017, the Postal Service reported positive controllable income for the three prior years.[10] The Postal Service held approximately $10.5 billion of unrestricted cash entering FY 2018.[11] The Postal Service has recently recorded a pension benefit funding level of 93% -- higher than the average funding level for the Fortune 1000.[12] The Postal Service also has significant assets, including a real estate portfolio which the USPS Inspector General estimates is worth as much as $85 billion.[13] These positive metrics are occurring despite the restrictions on postal rate increases. Indeed, one could argue that given the incentive the rate cap puts in place for USPS efficiency, these results are occurring *because* of them.

To be sure, the Postal Service continues to face significant financial challenges, but these challenges are caused primarily by statutorily-mandated and uncontrollable expenses related to prefunding requirements for retirement and retiree health benefits obligations. The Commission recently stated that Congress should address unfunded liabilities, rather than rate payers.[14] We agree.

Indeed, ABA strongly supports Congressional efforts to enact meaningful postal reform legislation to address these unfunded liability issues, and has actively sought

[10] United States Postal Service 2017 Annual Report to Congress at 14, *available at* https://about.usps.com/who-we-are/financials/annual-reports/fy2017.pdf.
[11] *Id*. at 6.
[12] Testimony of Megan J. Brennan, Postmaster General and Chief Executive Officer, U.S. Postal Service, Before the Senate Homeland Security and Governmental Affairs Committee, Jan. 21, 2016 at 10.
[13] U.S. Postal Service Office of Inspector General, *Considerations in Structuring Estimated Liabilities* at 3, Jan. 23, 2015, *available at* https://www.uspsoig.gov/sites/default/files/document-library-files/2015/ft-wp-15-003_0.pdf.
[14] Section 701 Report, Analysis of the Postal Accountability and Enhancement Act of 2006 at 7, *available at* https://www.prc.gov/sites/default/files/reports/Section%20701%20rpt.pdf.

enactment of proposals that provide meaningful reform.[15] These issues must be addressed, but the solutions for these problems are multi-faceted. The Postal Service's inability to meet its prefunding obligations has been an issue for nearly 10 years. The failure by Congress to act demonstrates that it does not view this as an urgent matter. There is no reason for the Commission to treat the issue differently.

The Proposed Revisions to Workshare Pricing Will Help Achieve Operational and Pricing Efficiency

While the PRC missed the mark through much of its Phase 1 decision, the Commission correctly held that USPS had not used its pricing authority to improve efficiency as required by Objective 1. As the Commission has found, "[w]orkshare discounts set substantially above or substantially below avoided costs are problematic because they send inefficient price signals to mailers and therefore reduce productive efficiency in the postal sector." ABA agrees that setting workshare prices consistent with Efficient Component Pricing ("ECP") maximizes efficiency and results in the lowest combined total costs for the postal system. ABA supports the Commission's proposal to require that workshare discounts be set closer to avoided costs. The proposed bands should be more narrowly drawn to "maximize" incentives to reduce costs and increase efficiency as required by Objective 1. The proposed band of 85-115 percent is too loose. The bands should be narrowed to 95-105 percent.

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[15] *See, e.g.*, letter of the American Bankers Association and Financial Services Roundtable to the House Committee on Oversight and Government Reform, March 16, 2017, *available at* http://www.aba.com/Advocacy/LetterstoCongress/Documents/LetterforOGRPostalMarkup.pdf (advocating support for legislation that would address Postal Service legacy benefit obligations).

Workshare pricing is an especially important issue for banks. The Postal Service offers discounts on postage to mailers if they perform certain activities that reduce the Postal Service's costs (e.g., mail sortation, transportation, etc.). The significant majority of the mail that banks send is presorted commercial mail. This mail is among the most profitable of all postal products. Banks should be rewarded for the work they perform that ultimately saves USPS money. Discounts that reflect the full value of the work our members perform means lower effective prices. Lower effective prices means mail remains a more attractive commercial medium and sales channel. Efficient workshare prices stimulate mail volume growth, stem erosion, and help Postal Service outsource the cost of mail processing operations, thereby minimizing costs and maximizing operational efficiency.

Conclusion

The ABA respectfully requests that the PRC leave the current structure of the rate system in place. It is working, and has provided the Postal Service with the incentives necessary to modernize its operations in a way that should be commended. ABA values the Postal Service and stands ready to work with the USPS to discuss legislative solutions that address the fiscal pressures the Postal Service currently faces, and which continue to maximize the efficiency of the Postal Service, while stabilizing rates so demand for postal services remains strong. A decision by the PRC to radically change the rate structure will have short and long term consequences for the Postal Service that can and should be avoided.

Respectfully Submitted,

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