Postal Regulatory Commission
Submitted 2/3/2020 1:10:14 PM
Filing ID: 112159
Accepted 2/3/2020

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
(February 3, 2020)

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 Revised Notice of Proposed Rulemaking (RNPRM) for the statutory review of the system for regulating rates and classes for market dominant products. Although we appreciate that the Commission has made some positive changes to workshare pricing in the RNPRM, we are disappointed at the PRC's other changes. The PRC should reconsider its decision to effectively replace the key governor of United States Postal Service (USPS) pricing under the Postal Accountability and Enhancement Act[2]—the consumer price index (CPI) cap—and replace it with a system that, by its terms, rewards the USPS with the ability to *charge more* because there is reduced demand. The predictable consequence of the PRC's proposal will be less mail. Lower volumes will generate still more price increases; it is not an exaggeration that *this*

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

proposal will accelerate the Postal Service's decline. Many ratepayers will leave the system. As their customer populations age, they will never return.

We have a number of concerns about the RNPRM. We continue to question the Commission's legal authority, and believe the RNPRM is premised on an overbroad reading of the statute. The PRC's conception of financial stability is too narrow. With the exception of the proposed workshare regulations, none of the proposals advanced by the Commission will meaningfully incentivize efficiency and cost reductions, as required by the very first statutory Objective of the PAEA. Indeed, 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. The cap, in turn, is the statutorily mandated check on pricing to force the USPS to make hard choices that lead to efficiency, and a focus on the products that will make money. Rather than construction of a new Performance-Based Rate Authority that is not linked to actual improvements in performance, the cap can and should continue to fill that role (especially since that is what the statute requires). In sum, the proposals in the RNPRM are all carrots, with no stick.

The rates-only approach will exacerbate, not solve, the challenges confronting the postal system. The Commission's focus on the long-term financial security of the USPS—cleaning up the balance sheet and providing retained earnings—comes at the short-term expense of ratepayers such as banks, but over the long-run comes at the expense of the Postal Service itself. The PRC improperly elevates Objective 5 above all of the other statutory objectives and factors Congress required the agency to consider in this proceeding (especially Objectives 1 and 2), without giving serious consideration to consequences, and certainly without protecting the ratepayers, as the Commission is charged to do.

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. 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, customer preferences, 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 billions of dollars in USPS revenue. 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.

The PRC Continues to Misread Its Legal Authority, and Downplay the Facts on the Ground

As ABA has argued at each phase of this proceeding, the Commission does not have the authority to turn the statutory CPI price cap into a floor, rather than a ceiling. Any attempt to do so would amount to a dramatic and unsupportable regulatory overreach. The CPI cap remains just that—a cap—and 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 shall (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).

It is true that this proceeding is mandated by statute, but that does not give the PRC authority to *rewrite* the statute. Indeed, there is nothing in the text that suggests that the CPI cap applies only to the *first* rate system the Commission might establish. If that were true, Congress would have said so. Rather, as ABA has argued previously, 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 shall apply to the first system, and shall 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-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 approach the PRC takes in the RNPRM elevates the USPS financial health to a much higher position than Congress intended. As the PRC itself noted in its Phase One order in this proceeding, “[a] key principle in statutory interpretation is to give proper meaning to all provisions of the statute.”[3] We agree. When viewed in full, the nine objectives defined by 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.

[3] Order No. 4257 at 15.

> 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.[4]

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 PRC's approach in the RNPRM thus gives disproportionate weight to Objective 5 relative to the rest of the statute.

For bankers, stability, predictability, and just and reasonable rates are paramount, and it is not 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.

Instead, the Commission effectively 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 raise prices because of declining volumes, effectively taxing those ratepayers who continue to invest in the mail in the

[4] 39 U.S.C. § 3622(b).

face of technological alternatives that did not exist even when the PRC began this proceeding.

- **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."[5] 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, whether in the form of increases to address declining volumes or pre-funding, 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 aid over larger problems. Without cost reductions and

[5] 39 U.S.C. § 3622(d)(3).

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 USPS faces (but the PRC seems determined to refuse to find credible) in the modern age.

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 – rather than other factors, such as pre-funding obligations. *See* 39 U.S.C 403. By any analysis, the Postal Service is strong, and growing 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. 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 and sustained growth in shipping and package delivery over the past decade.

And below the surface, uncontrollable labilities—the pension and medical obligations—are not as bad as a quick review of the balance sheet might suggest. As the Postmaster General recently told Congress, "the Postal Service's percentage for CSRS pension funding is more than nine times the level of other civilian federal government entities and is higher than the average funding level for those few Fortune 1000 companies still offering traditional pension plans. In addition, the Postal Service's FERS pension funding is at nearly 87 percent. Likewise, our RHB funding is at a much higher level than those of other entities."[6]

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.[7] The PRC should work with the Postal Service to find creative ways to monetize this portfolio before dramatic changes in the rate system.

All of 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.

The PRC's Latest Proposal

Supplemental Rate Authority

Both elements of the supplemental rate authority proposal are seriously flawed and should be reconsidered.

Raising Prices is a Recipe to Have Fewer Customers, Not Address Declining Volume in a Sustained Manner

[6] Testimony of Megan J. Brennan, Postmaster General and Chief Executive Officer, U.S. Postal Service, Before the House Committee on Oversight and Reform, April 30, 2019, *available at* https://about.usps.com/news/testimony/2019/pr19_pmg0430.htm.

[7] 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.

The proposal to allow USPS to recover unlimited additional rate authority to address declines in mail density (volume) is a recipe for an accelerated collapse. The Commission's focus on the mechanics of the formula cannot hide the inescapable fact that the proposed rule would allow USPS to ***raise prices as volume falls***, placing more and more rate pressure on residual volumes, thus, precipitating further volume declines. What's more, tying rate increases to Postal Service volumes provides an element of unpredictability that makes it impossible to accurately plan for postal expense in advance.

Cost matters. 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 even since this proceeding began, 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 for banking transactions. The movement to 5G will accelerate these trends.

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

In other important ways, the PRC's approach falls flat. The PRC's approach is inconsistent with the goals of the PAEA and Objectives 1 and 2, because it would allow USPS to recover additional rate authority based on declines in mail density. This absolves USPS of any responsibility for mail volume declines (quality service is a reason for consumers to stay in the system) and disincentives USPS from reducing its delivery costs. In effect, the PRC is reintroducing a "cost of service" model of rate regulation that Congress rejected in enacting the PAEA. The proposed formula is also methodologically unsound and unexplained. In the Exigent Case and in all but the earliest rate cases under the Postal Reform Act, the PRC accepted USPS estimates of the additional costs of increased delivery points using a Rollforward Model, which estimate cost changes for all sources of change: volume, cost levels, additional delivery points, extra days, cost reduction programs, etc. Adjusting output from that model to reflect today's delivery points shows (and holding volume constant) results in a far smaller cost for the same number of additional delivery points than the density formula (again holding volumes constant) would allow the Postal Service to recover in extra rate authority from the density adjustment. At the very least, reasoned decision-making requires the PRC to explain why its new method, holding volume constant, produces far different results than its previous one.

Congress Should Address Prepayment Obligations

The additional supplemental rate authority earmarked for retirement obligations (RHB and pension) is also misguided. 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. As recently as December 2016, the Commission stated that Congress should address unfunded liabilities, rather than rate payers.[8] We agree.

The Commission should not interpose itself in the unfunded liability issues; this is an issue that Congress created and Congress must fix. A bill to repeal the prefunding obligations had nearly 300 cosponsors in the last session of Congress, and ABA strongly supports Congressional efforts to enact meaningful postal reform legislation to address these unfunded liability issues, actively seeking enactment of proposals that provide meaningful reform.[9] Although these issues must be addressed, the Postal Service's inability to meet its prefunding obligations has been an issue almost since the moment PAEA was enacted into law. The solutions for these problems are multi-faceted, requiring a complicated weighing of stakeholder interests. Congress, rather than a regulatory body with limited authority, is best positioned to perform this task.

The PRC is not a promotional agency for USPS. It is an economic regulator, charged with protecting captive ratepayers. However, the result of this proposal will be

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[8] 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.

[9] *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).

a further tax on current ratepayers to fund future unfunded liabilities unrelated to current operations. As above, granting supplemental rate authority to deal with retirement obligations on top of the authority granted in the CPI price cap is effectively letting USPS recover twice from ratepayers to cover the same cost basis and removing incentives for efficiency and cost reduction.

Performance-Based Rate Authority

The performance-based rate authority proposal is facially deficient because it is not linked to actual improvements in performance.

The performance-based rate authority seeks to incentivize the very same behavior the CPI price cap is designed to incentivize. 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 of simply leaving the cap in place, the PRC has designed a procedure that could allow USPS to recover additional rate authority under the proposal even if its net productivity declined over the 5-year period. The operation of the formula is such that under certain scenarios, USPS could recover more revenue for worse performance than it could with improved performance. A rule that produces arbitrary results inconsistent with the goals of the PAEA (Objective 1) cannot be sustained.

If the Commission persists with this rule, it should revise the proposal to ensure that USPS can only recover under the performance-based productivity component when there is an actual net improvement in productivity since the inception of the new authority. This sounds obvious, but by tying the productivity component to benchmarks, the PRC can reward USPS for the status quo. The service standards component suffers from the same inherent defects because it is not tied to actual service performance, but rather is conditioned on the maintenance of published service standards. Rewarding USPS with additional "performance-based" rate authority even if it fails to meet published service standards is arbitrary and fails to meet the basic APA standards for reasoned decision-making.

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

While the PRC missed the mark through much the RNPRM, the Commission correctly reaffirmed that USPS had not used its pricing authority to improve efficiency as required by Objective 1. Indeed, the proposed workshare rules are the only aspect of the RNPRM likely to improve efficiency and reduce costs.

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 mean lower effective prices for banks, which helps keep mail as an 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.

The Commission appropriately endorses the approach advocated by the majority of mailer comments in the last round (including ABA) to require that USPS move workshare discounts closer to 100 percent of the cost savings to maximize incentives to reduce costs and increase efficiency as required by Objective 1. The Commission was correct to reaffirm their Phase One order that "[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."[10] We appreciate that the Commission dropped the proposal for a 3 year grace period, although we do believe that the PRC's related efforts to provide USPS "transitional flexibility" could be improved.

The revised rules provide both (1) a safe harbor for discounts set between 85-100 percent of costs avoided, and (2) a waiver process for deviating from 100 percent passthroughs. The 85 percent floor as a standalone safe harbor is unnecessary. It risks frustrating the Commission's stated intent to encourage incremental improvement in pricing efficiency (the Commission's "do no harm" principle) by always moving workshare discounts closer to 100 percent of the cost savings. In practice, an 85 percent floor would cure the worst abuses of passthroughs set below avoided costs, but would likely result in the systematic understatement of many workshare discounts (with

[10] Order 4258 at 93.

the effective floor and ceiling of 85 percent), a result that is inconsistent with Objective 1 (to maximize incentives to reduce costs and increase efficiency).

The proposed waiver process provides sufficient flexibility. The waiver process is intentionally narrow (we anticipate waivers will be hard to obtain and infrequent), but the process provides flexibility such that USPS would not be required to move any workshare discount closer to 100 percent of the cost avoided if it can show that doing so would impede USPS operational efficiency. Some limitation on the waiver process is appropriate, thus, the 85 percent floor should operate as a constraint on the waiver process—not as a general safe harbor.

Finally, we appreciate that the Commission cites an independent legal basis for its authority to modify the workshare rules; even if a reviewing court later finds that the Commission did not have the authority to modify the price cap, it would not affect its ability to improve the workshare rules.

Enhanced Reporting

The enhanced reporting requirements on USPS costs and cost reduction efforts are welcome and will promote the PAEA objectives of enhanced transparency and accountability. That said, reporting alone is insufficient to satisfy the pro-efficiency objectives and factors of the PAEA. Under the Commission's interpretation of its own authority, it has the opportunity to meaningfully condition new rate authority on real cost, productivity and service performance. It should do so. For the reasons discussed throughout, the Commission should use the enhanced reporting data to meaningfully regulate USPS.

Procedural Changes

In a single paragraph at the end of the Order (pp. 239-240), the Commission announces that it no longer plans to assess whether actual rate adjustments achieve the statutory objectives or take into account the statutory factors in connection with a notice to adjust market dominant rates. This is a significant change in approach that is inconsistent with the PAEA's overriding goal of enhanced accountability. The Commission offers no explanation for the change. It merely asserts that "notwithstanding" the recent decision by the DC Circuit (*Carlson v. PRC*, 938 F.3d 337 (D.C. Cir. 2019)) the Commission has the "authority to construe how to apply the provisions of 39 U.S.C. 3622."

In *Carlson* the court vacated the R2019 First-Class Mail rates, among other reasons, because the Commission had failed to adequately explain how those proposed rate adjustments complied with the statutory objectives and factors. The *Carlson* decision specifically held that "the Commission must apply the relevant objectives and factors to individual rate adjustments." In a footnote the Commission seeks to downplay the significance of the *Carlson* case, but it does not follow that because the court in *Carlson* recognized that the PAEA grants the Commission discretion in the "application" of the statutory objectives and factors, that the Commission need not apply them at all.

The Commission's citation to *Brand X* presupposes that the language of section 3622(d)(3) is ambiguous and thus the Commission is entitled to deference on its expansive interpretation of its own authority that allows it to ignore the exhaustive list of requirements, objectives and factors codified in the statute. This also misreads the

Carlson case because there is nothing in the *Carlson* decision that suggests the court found the statute ambiguous. Even if the Commission's interpretation was consistent with the *Carlson* case (it is not), more is required to change the existing rules. *Brand X* confirms that an agency must provide a reasoned basis for reversing a prior interpretation. A failure to do so that results in an unexplained inconsistency that is a hallmark of arbitrary and capricious agency action. The Commission has not provided a reasoned basis for reversing its position here.

As a matter of policy, it makes no sense that at the same time the Commission is giving USPS increased discretion to raise rates above the statutory price cap, the Commission is retreating from its obligation to assess whether the actual rates proposed comply with the objectives and factors.

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,

Robin Cook
Vice President and Senior Counsel
Office of Legislative Affairs and Chief Counsel
American Bankers Association
1120 Connecticut Avenue NW
Washington, DC 20036
(202) 663-5339
rcook@aba.com