Comments of the Postal Rate Commission
Concerning the President’s Commission on the Postal Service
Submitted to the
Committee on Governmental Affairs

November 19, 2003

The Postal Rate Commission provides these comments to the Committee on Governmental Affairs in the hope that they will assist the Committee in developing legislation to strengthen the nation’s postal system. The Committee has held hearings to evaluate the Report of the President’s Commission on the Postal Service, dated July 31, 2003. That report, subtitled Making the Tough Choices to Preserve Universal Mail Service, identified numerous current and expected challenges facing the Postal Service, and suggested a sweeping overhaul of the nation’s postal system.

The President’s Commission suggests that the Postal Rate Commission (PRC) play an important role in the revamped system. It recommends that “the Postal Rate Commission should be transformed into a new Postal Regulatory Board with the responsibility to protect the public interest and promote public confidence in the fairness and transparency of postal operations.” (Recommendation C-3.) The PRC wishes to assure the Committee that it fully supports efforts to improve the likelihood that the nation will continue to receive superior postal service in the coming decades, and that it stands ready to fulfill whatever role may be found appropriate and necessary to achieve that goal.

The PRC believes that the President’s Commission has done an extraordinary job of synthesizing a huge amount of information from diverse sources into an understandable and persuasive call for reform. The Report is particularly timely, as recent volume trends have made the need for action clear to all those concerned with the preservation of a healthy, self-sufficient, ubiquitous Postal Service.
I. Broad Considerations

A. Historical Background

The Final Report of the President’s Commission recommends the continuation of several policies that have been constants in the nation’s postal system for years, such as universal service, a strong federal presence in the postal system, and certain related monopoly features. The President’s Commission’s endorsement of these policies provides an important bridge to the future. It also sends a strong message to the American public about the stability and strength of one of our nation’s most enduring institutions.

At the same time, the Commission qualifies continuation of some of these longstanding policies by further suggestions that would, if adopted, fundamentally alter the balance the Postal Reorganization Act of 1970 struck in important areas. This may be found to be necessary and appropriate, but it warrants careful examination.

Currently, the PRC is charged with providing opinions developed in an open, public forum in which all affected interests can participate to assure that postal rates and services are consistent with the policies established by Congress, and with recommending postal rates and classifications that meet those criteria. It is also responsible for hearing appeals of certain post office closings and consolidations.

The PRC is proud of its history of promoting more efficient postal operations through rates that have encouraged worksharing with the private sector. These comments reflect the PRC’s view that the current system can be, and should be, improved; but that care should be taken to assure the preservation of the Postal Service’s honored tradition of binding the nation together by making affordable service readily available to all. Americans trust their Postal Service to meet their needs, regardless of geographic location or economic circumstances. This trust has been earned through decades of dedicated service, and it must not be squandered.

It is important to remember that the current system is not a bundle of freestanding provisions, but rather a unified compromise developed in the 1970 Act’s intricate network of policies outlining the broad contours of our modern postal system. In some instances, such as in the area of regulation, there was wholesale adoption of
other areas of law, such as the Administrative Procedure Act. This law codifies many
important safeguards the American public has come to associate with its government,
such as an opportunity to be heard; fair and open hearings; and reasoned, record-
based decisions. It is the basis for our operating regulations at the PRC, most notably
for rate and classification proceedings.

As many years have elapsed since 1970, some might not fully appreciate that the
regulatory framework the PRC and the Postal Service operate within was the product of
a hard-fought compromise. The PRC firmly believes that the President’s Commission
has identified many essential improvements for our postal system. We also believe that
public acceptance will be strongest if all affected interests again are given a “seat at the
table” to express their concerns and fashion an acceptable final product that
incorporates these needed changes. This Committee’s commitment to further hearings
and open process goes a long way to assuring broad support for legislation modernizing
Postal Service business practices.

Your predecessors struggled with how to fund a federal postal system that could
maintain a universal service commitment. Before reorganization, postage rates were
hammered out in the halls of Congress, and some commercial mail was simply sent for
free. Taxpayers picked up a large portion of the tab. The tools and time essential to
developing a fair and equitable set of rates and products were simply not ready at hand.
Those legislators hit upon a broad delegation of revenue-raising power to Postal
Service management, the Governors, and the PRC, with judicial review as an important
check. This delegation, however, was tempered with concern about the public interest.
For example, the PRC currently is required to explain how its rate recommendations
accommodate the value of mail service to senders and recipients, and the effect of rate
increases on the general public, business mail users, and private sector enterprises that
deliver parcels.

B. Safeguarding the Public Interest: Then and Now

Safeguarding the public interest is a touchstone of the 1970 Act, and finds
expression in myriad policies and procedures that inform the everyday workings of the
system that has been in place since 1970. “Universal mail service” is perhaps the best-
known example on everyone’s short list of significant Reorganization Act policies. This concept has never been fully spelled out, although this mandate generally has come to be viewed primarily in terms of providing every physical address in the United States with some form of regular, basic postal services. The directive that “no post office shall be closed solely for running a deficit” was a means of fulfilling that goal.

Now, more than 30 years later, the President’s Commission has concluded that universal service “remains vital to the nation and its economy at the dawn of the 21st century.” (Executive Summary at vii.) It also recommends a new approach for closing post offices, which may entail eliminating the proviso against closing offices simply for not paying their way.

Regardless of one’s position on the advisability of adopting these suggestions, it is worthwhile to remember that they, like the regulatory mechanisms mentioned above, were not freestanding provisions. Instead, they were part of the much broader, pervasive conclusion that the Postal Service should play a “nation binding” role.

The President’s Commission viewed its purpose as to identify and recommend things that would further a primarily economic goal: “to ensure the efficient operation of the United States Postal Service while minimizing the financial exposure of the American taxpayers.” (Forward, at iii.) It believes that a more flexible and empowered management could make great progress toward this goal. To counterbalance more independent management, the President’s Commission recommends that a Postal Regulatory Board be vested with “broad authority to set the public-policy parameters within which the Postal Service is allowed to operate.” The Commission emphasizes that its recommendations are contingent on a strong, independent Board with a clear mandate to protect the public interest. (Report at 53, 55, and 70.)

The Commission envisions a Postal Regulatory Board which will, among other functions, exercise broad public policy oversight to ensure that revenues from non-competitive products are not used to subsidize the provision of competitive services. This recommended duty appropriately recognizes the importance of preventing such cross-subsidies to both users of monopoly services such as First-Class Mail, and to private sector firms that should be protected from unfair competition from their government.
The Regulatory Board would also oversee Postal Service cost distribution, ensuring that it is appropriately allocating costs across its competitive and non-competitive products and services. The PRC’s institutional experience confirms the importance of this analytical function. In addition to verifying that cross-subsidies between services are not occurring, such analysis is necessary for assessing the fairness of the rates the Postal Service is currently charging, or proposes to charge.

The Commission also recommends that the Regulatory Board should ensure the financial transparency of the Postal Service, obtaining information from the Service — if need be — through the use of subpoena power. Financial transparency is indispensable for two reasons: (1) it promotes public confidence in the Postal Service’s business performance, and (2) it makes feasible the system of rate and other regulatory oversight recommended in the Commission’s report.

Under the Commission’s recommendations, the Regulatory Board would exercise two new forms of oversight regarding services the Postal Service provides. First, the Board would monitor the types of products and services offered by the Service to ensure it does not exceed its core mission. Second, the Board would review changes in service standards proposed by the Service that might have a substantial negative national impact.

The first function presumes that new legislation will clarify national policy on the appropriate areas of Postal Service business. The Postal Service’s provision of “non-postal” services, and their relation to the Service’s core postal functions, have given rise to vexing policy questions — and several contentious PRC proceedings — in recent years. The second function would expand a jurisdictional duty currently performed by the PRC, and would affirmatively contribute to safeguarding the public interest in preservation of the quality of services provided by the Postal Service.

The Commission further recommends that the Regulatory Board exercise public policy oversight over two fundamental features of the nation’s postal system: the appropriate scope of the Postal Service’s monopoly, and that of the universal service obligation. Again, these proposed functions involve issues of national postal policy appropriate for Congressional deliberation. Board oversight would assure neutral third-party review of questions on the scope of these legal obligations where legislative intent
is not clear. The Commission is to be commended for formulating an innovative regulatory approach for resolving these potentially contentious policy determinations as the Postal Service evolves in the future.

The President’s Commission recommends that “the Postal Rate Commission should be transformed into a new Postal Regulatory Board with the responsibility to protect the public interest and promote public confidence in the fairness and transparency of postal operations.” (Recommendation C-3.) The PRC notes that this statement of responsibility is somewhat different than the overall economic goal enunciated by the President’s Commission (Forward at iii) cited above. Therefore, the PRC presents the following specific comments focusing on areas: (1) where it has particular expertise, and (2) where prospective legislation may have to consider balancing the overarching economic focus of the President’s Commission Report, with providing a workable system for protecting the public interest and preserving public confidence in the Postal Service.
II. Prerequisites of Successful Postal Transformation

The President’s Commission recommends that the Postal Service be transformed in several important respects to enable it to meet present and future challenges while continuing to provide affordable universal service. The Postal Service would continue to be an independent establishment within the executive branch of the Federal Government, and would retain its current monopoly over letter mail and sole access to customer mailboxes for the immediate future. The Commission further recommends that the Service be granted greater operational and pricing autonomy under enhanced regulatory oversight, while being encouraged to maximize use of outsourcing to the private sector.

The Postal Rate Commission recognizes that a variety of competing approaches have been offered — in legislative initiatives since the mid-1990s and now by the President’s Commission — to adapting postal laws to the changing circumstances in which the Postal Service finds itself. Undoubtedly the Commission’s recommendations and other proposals will be debated as Congress moves to consider the issue of postal reform. However, whatever specific changes may ultimately be included in legislation, the PRC views certain changes as crucial to the success of postal reform. These critical changes are identified and discussed below.

A. Financial Transparency

Among several changes intended to protect the public interest through enhancing the accountability of the Postal Service and the public-policy oversight it receives, the President’s Commission recommends measures to ensure the financial transparency of the Service. It recommends that the Service voluntarily comply with pertinent Securities and Exchange Commission reporting requirements. It also recommends strong enforcement of financial transparency by a Postal Regulatory Board, in part by requiring the Postal Service to report periodically on allocation of costs among mail products and services for auditing purposes.

The Postal Rate Commission agrees wholeheartedly with these recommendations. Indeed, in our view enhanced financial transparency requirements
are essential to assuring that the Postal Service functions as a successful, performance-driven public service in the future.

The President’s Commission report envisions “a healthy and efficient Postal Service that consistently operates at a high standard of excellence and delivers service quality, productivity and performance on a par with the nation’s leading corporations.” (Report at 36.) As the Commission also recognizes, assurance of financial transparency provides the essential framework for public confidence in the empowered, accountable managers and strong Board of Directors charged with achieving this vision. This is because timely, detailed and verifiable financial data will serve as a principal resource for documenting the Postal Service’s business performance.

Furthermore, financial transparency — in the form of immediately accessible basic data about Postal Service finances and operations — will be an indispensable tool for implementing effective oversight of a transformed Postal Service.

The President’s Commission recommends strong regulatory oversight performed with extreme expedition; in the case of ratemaking for non-competitive postal products, it recommends that all final determinations be rendered within 60 days. The availability of highly detailed, frequently-updated cost and other financial data are a practical imperative for conducting meaningful regulatory review of both complaints and proposed rate changes within the recommended timeframe.

B. Regulatory Oversight Commensurate with Postal Service Autonomy

The President’s Commission’s report concludes that: “The Postal Service’s need for oversight today is as broad as the PRC’s authority is narrow.” (Report at 55.) On the basis of this assessment, the Commission recommends that a Postal Regulatory Board be vested with substantially expanded regulatory authority. The Board’s authority would encompass not only ratemaking matters such as appropriate cost allocations, the prevention of cross-subsidies, and rate increases for non-competitive products and services, but also oversight of the appropriate scope of the postal monopoly, proposed changes to service standards, and the scope of the universal service obligation. The Board would also be tasked with ensuring the Postal Service’s financial transparency, the comparability of its employee compensation to private sector benchmarks, and the
consistency of its level of accumulated retained earnings with the public interest.
(Report at 56, Exhibit 4-1.)

The PRC fully agrees with the Presidential Commission’s premise in this area: that the enhanced level of autonomy it recommends for the Postal Service in its future operations should be matched by a correspondingly rigorous degree of public policy oversight. Particularly in light of the Postal Service’s retention of the letter and mailbox monopolies, the PRC views strong regulatory oversight as a crucial element of comprehensive postal reform. Further, in our view the successful operation of the recommended system of regulatory oversight will depend on vesting the regulator with sufficient discretion to achieve a balance between potentially competing interests and objectives.

The system of regulation recommended by the President’s Commission would present challenges on several fronts. First, because the strongest form of rate regulation would apply to non-competitive services (including First-Class Mail), there would be a natural incentive to control costs by all means available — including measures that might compromise the level of service provided to users. While the President’s Commission recommends that the Postal Regulatory Board be assigned jurisdiction over proposed changes in service standards that may have a substantial negative national impact, it does not explicitly address potential erosion in service levels that might result from cost-cutting programs. In the PRC’s view, the regulator should also have authority to ensure that appropriate levels of service are maintained.

Another essential responsibility involves the recommended oversight of both the scope of the Postal Service’s monopoly and that of its universal service obligation. The Commission report recommends that the Postal Regulatory Board’s roles include “defining the scope of the postal monopoly, refining the appropriate components of the universal service obligation, and establishing the bright-line boundaries between the postal monopoly and competitive markets.” (Report at 62.) The Commission provided sound public policy rationales for assigning these functions. (Report at 65.) However, the general criteria for defining the appropriate scope of Postal Service operations may merit further clarification before legislation is enacted.
Historically, an unstated premise of postal policy has been that the purpose of the monopoly is to assure the preservation of a satisfactory level of universal service. The PRC suggests that any legislation effecting postal reform should explicitly direct the regulatory body to consider preservation of an adequate level of universal service as the principal criterion when reviewing the scope of the postal monopoly.

Finally, the regulator’s ability to perform the functions envisioned by the President’s Commission will depend critically on the availability of adequately detailed data to enable informed review. This could encompass both information the Postal Service has on hand for its own operational purposes and other specialized data required for regulatory review. For this reason, it is our view that the regulator should be vested with authority not only to compel the production of information already prepared by the Postal Service (i.e., subpoena power), but also to compel the collection and reporting of additional data reasonably required to perform its regulatory functions.

C. New, Streamlined Rate-Setting Process

The President’s Commission charges the new Postal Regulatory Board with moving quickly to implement a new ratemaking system that would allow Postal Service managers significant flexibility to rapidly adjust rates. (Report at 57, Exhibit 4-2.) Management would be authorized to charge whatever rates it chooses for competitive products, so long as those rates are not cross-subsidized by non-competitive products.

The rates for non-competitive (monopoly and market-dominant) products also could be set at whatever level management chooses so long as they meet two tests: rates for each product must cover its costs, and rates for a product may not increase faster than an inflation-related metric established by the regulator. The first test exists today, and is well understood. The second test is new, and the Commission views it as an important incentive to make the Postal Service manage itself more efficiently.

The essential, albeit implied, tenet of this rate system is that even mailers of non-competitive products have no need to participate in a formal rate-setting process so long as their rates have not risen faster than inflation. After a “base case” rate is set for each product, rate levels for that product would be at the sole discretion of management unless rate increases exceeded increases in inflation from the date that the base case
rates took effect. Of course, as any other business, the Postal Service would maintain contacts with its customers and be expected to try to consider customer views before establishing rates.

This is a significant departure from the current system. The current system allows before-the-fact public participation to assure that rate increases are justified; requires consideration of the impact of increases on mailers, and whether the institutional burdens of the Postal Service are being fairly divided among mailers; provides for a rate decision in which the rationales for the increases are explained; and allows judicial review of arbitrary or capricious acts. None of those protections would be retained.

The Postal Regulatory Board is to establish a limit on the amount of retained earnings the Postal Service can accumulate, but so long as retained earnings do not exceed that amount, rates for each product may be increased up to the inflation-determined limit.

If the Postal Service wishes to increase rates for a product above the inflation-related ceiling, or establish rates for a new product, it would have to obtain before-the-fact authorization from the Board. The Board also is to hear complaints from mailers that contend rates are below costs, or have increased faster than inflation.

The rate case to establish the “base” rates that would serve as the benchmark for inflation-justified future increases is likely to be the most complex and contentious case ever heard by this body. It would establish relative contributions to overhead that would remain the standard for an indefinite period. Thus, participants could be expected to challenge every cost allocation and raise every policy consideration that effects rate levels. All types of mailers would be likely to consider it in their best interests to actively participate.

The President’s Commission suggests that this case be processed under current PRC rate case rules. This is a sound suggestion. The Postal Service and many mailers are thoroughly familiar with these rules. Although the case would be complex, and would require extraordinary efforts by both the PRC and participants, there is no ready alternative that is more likely to produce a sound and reasoned decision in a reasonable period of time. Hopefully, the Board of Governors would be able to
schedule implementation of new rates at the beginning of a month so as to facilitate subsequent measurements of inflationary growth.

After base rates have been established, the President’s Commission suggests that no major rate cases would be necessary. It proposes that all rate cases before the Postal Regulatory Board be limited to written submissions and be conducted in 60 days. The Board would then direct the Postal Service to implement whatever rate changes are found appropriate.

This system has several important virtues. It is not burdensome to either mail users or the Postal Service, and it will rapidly resolve the potential uncertainty of “proposed” rate changes. The PRC is fully prepared to face the challenges of providing available due process under this system. Nonetheless, we recognize that however well-intentioned the Board may be, it may err, and recourse through judicial review may help assure adherence to the public policies established by Congress.

Additionally, we suggest that while this process may generally be sufficient, Congress should hear from mailers whether they think this single, limited procedure is appropriate to protect their interests in all types of rate cases. It is reasonable to presume that the Postal Service will want to avoid having to request authority to raise rates above the inflationary caps. This should motivate management to restrain costs and avoid inefficient practices. However, the desire to avoid rate requests also could have unfair impacts on some mailers. The inflation-based cap on rates for each product is most fair if the costs associated with each product change together. Over the years, this has not been the case. During the last decade there were periods when Postal Service costs, in total, generally tracked inflation; however, the cost of processing certain products rose precipitously. Thus, the Service sought substantial rate increases for those products. Mailers participating in rate cases used discovery and oral cross-examination of Postal Service witnesses to identify areas where savings might be attained, and thus hold down proposed rate increases.

Should the Postal Service seek to raise rates for non-competitive mail above the inflation-based cap, there may be sound policy reasons for allowing captive customers to do more than submit written protests. The President’s Commission believes that there are so many cost cutting opportunities available to the Postal Service that years
should pass before rates might have to increase above the rate of inflation. However, if this view turns out to be overly optimistic, captive mailers could be subject to repeated increases in excess of inflation with no opportunity to explore the causes of those increases.

The President’s Commission seems to believe that as long as rate increases are moderate, even captive monopoly mailers have no grounds for complaint. When increases exceed the rate of inflation however, the justification for allowing postal management to impose ever-increasing burdens with only minimal user participation largely disappears.

This is not a purely theoretical problem. In a recent case (PRC Docket No. R94-1) the Postal Service proposed a rate increase of 34% for In-County publications. These mailers had been in discussions with the Service about data discrepancies before that case was filed, but without satisfactory resolution. After the Postal Service filed its request, affected mailers intervened and directed discovery to the Postal Service that forced it to acknowledge data collection errors. The Postal Service eventually altered its proposal and requested a rate reduction for this mail — but this change took place more than 60 days after the initial request was submitted. Thus, mailers may wish to comment on: (1) how much public participation should be permissible when large rate increases are involved; and (2) whether a 60-day written-submissions-only case will provide meaningful participation.

D. Hearing and Resolving Complaints

The President’s Commission recommends that the Postal Regulatory Board hear and resolve a variety of complaints from the public. The Board would consider complaints that rates are unlawful either because of alleged cross-subsidy, or because rates are inconsistent with applicable ceilings. Additionally, the Commission contemplates the Board hearing complaints that the Postal Service is acting unlawfully, for example by entering a market outside the scope of its mission. (Report at 65, 68.)

Prompt action on complaints is appropriate. When cross-subsidy exists, the aphorism “justice delayed is justice denied” is applicable. The Commission foresees
that as a result of the focus on Postal Service transparency, significant amounts of data on Postal Service costs will be publicly available. The PRC agrees that this should facilitate fast action on complaints.

The Commission suggests that complaint proceedings also should be limited to written submissions. Nonetheless, it recognizes that there may be instances where a rate complaint can not be evaluated without information on actual Postal Service operations. This type of information will not be regularly reported. In such instances, the strict time limits suggested by the Commission for rate cases might prevent the evaluation of valid complaints. Therefore, it recommends that complaint cases “should be completed promptly” setting 60 days as a goal. (Report at 68.)

The Complaint process envisioned by the President’s Commission supplies a substantial amount of public protection not present in the current law. The Postal Regulatory Board would be expected to promptly hear, and resolve, complaints that the Postal Service was acting contrary to public policy. Providing the Board with authority to order appropriate remedial action when a complaint is found justified, (Recommendation C-4) should substantially eliminate current concerns that the Postal Service is not held accountable for its acts.

Public protection would be strengthened even more if the complaint process suggested in the President’s Commission Report were augmented by authorizing the Postal Regulatory Board to initiate proceedings whenever it has good cause to believe that existing rates are contrary to law. This might occur if rates for a product have fallen below properly allocated costs, or if Postal Service retained earnings grow to exceed applicable limits. Even with the expedited procedures recommended by the Commission, many small and medium sized mailers might not wish to commit resources to pursuing an administrative complaint. Mailers’ confidence in the fairness of the system will be enhanced by the knowledge that an independent agency is authorized to initiate proceedings to assure that rates conform to statutory standards.

E. Cooperation with the Private Sector

The President’s Commission extols the benefits to the Postal Service of adopting corporate best practices in all of its component operations and activities. For example,
the Commission recommends that consideration be given to using local private contractors for functions such as real estate leasing, if doing so would reduce Postal Service costs. A natural extension of this policy is allowing mailers to perform mail processing or transportation functions in return for discounted postage. Such worksharing discounts have been strongly supported by the PRC, and a considerable portion of the mail already earns worksharing discounts.

The PRC currently develops discounts through application of the economic principle of Efficient Component Pricing. This results in discounts that reflect, as nearly as practicable, costs avoided by the Postal Service. Mailers are given the opportunity to benefit from reduced postage rates when they can perform operations more cheaply than the Postal Service. Discounts developed in this way have the added virtue that they do not disadvantage either the Postal Service or other mailers.

Commission Recommendation P-4 endorses this method for constructing discounts and suggests that the Postal Regulatory Board be authorized to hear complaints that new discounts exceed avoided costs. It further suggests that the Postal Service should ensure that the expected savings from worksharing discounts are actually captured in the form of reduced costs.

The PRC suggests that it would be consistent with the goals of accountability and public policy oversight to allow the Board to hear not only complaints concerning new discounts, but also complaints alleging that changes in processing procedures, or other events, have caused existing discounts to exceed savings to the Postal Service. Additionally, public confidence that rate discounts are fair would be enhanced by making the independent regulator, as well as the Postal Service, responsible for ensuring that worksharing discounts do not exceed actual savings. This responsibility could be exercised by initiating a complaint proceeding to evaluate questionable existing discounts.

The same considerations are applicable in the area of negotiated service agreements (Recommendation P-5). The Commission suggests that the Postal Regulatory Board should develop general criteria for such agreements and conduct after-the-fact reviews if a written complaint is filed. However, public confidence in the integrity of the system would be enhanced if the independent regulator was responsible
for assuring that every negotiated service agreement between mailers and the Postal Service is consistent with applicable policies, whether or not a private party files a complaint.