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

Introduction

Chairman Towns and Chairman Lynch, and Members of the Committee and Subcommittee, on behalf of the Congressional Research Service I would like to thank you for this opportunity to appear before you today to discuss the current financial crisis and its future viability of the U.S. Postal Service (USPS).

The Committee and Subcommittee requested that the CRS discuss the USPS's report, *Ensuring a Viable Postal Service for America*, and its proposals to:

(1) cease prefunding its retiree health benefits;
(2) switch to five-day mail delivery;
(3) close post offices; and
(4) have additional flexibility in pricing and introducing products.

The Committee and Subcommittee also asked the CRS to address the recent report by the U.S. Postal Service Inspector General (IG) alleging that the Postal Service has made overpayments related to its Civil Service Retirement System (CSRS) pension responsibility.

Accordingly, my statement presents a summary of the USPS's report, and it addresses the four aforementioned USPS proposals and the recent IG study. My statement concludes with observations on the Postal Service's short-term and long-term financial challenges.

A Summary of the U.S. Postal Service Report, *Ensuring a Viable Postal Service for America*

In March 2010, the USPS released a report titled *Ensuring a Viable Postal Service for America*.[1] The report claims that due to "underlying shifts in the business of mail," the USPS expects to continue losing money—$7 billion in FY2010, and $238 billion in cumulative losses by FY2020.[2] The "underlying cause" for these losses, according to the Postal Service, is a permanent drop in the demand for hard copy mail.[3] In FY2006, the USPS delivered 213.2 billion mail pieces; in FY2010, it delivered 177.1 billion pieces (16.9% fewer).[4] The Postal Service predicts mail volume will fall to 150 billion pieces in FY2020.[5]

To mitigate its financial distress, the USPS will use its own authority to undertake two broad actions: (1) increase its revenues by expanding "products and services across targeted mail and package segments," and (2) cut its costs by reducing its delivery network, shrinking its cohort of full-time employees through attrition, and lowering its transportation and vendor-related

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[1] U.S. Postal Service, *Ensuring a Viable Postal Service for America* (Washington: USPS, March 2010), at http://www.usps.com/strategicplanning/_pdf/Ensuring_Viable_USPS_paper.pdf.
[2] Ibid., p. 1.
[3] The USPS predicts that the demand for package delivery will be the lone exception to this trend. Demand might grow at a rate of 3% per year between FY2010 and FY2020. In FY2009, package delivery (including Priority Mail and other premium services) provides a small portion ($9.7 billion, or 14.2%) of the USPS's revenues. U.S. Postal Service, *Annual Report 2009* (Washington: USPS, 2009), p. 43, at http://www.usps.com/financials/_pdf/annual_report_2009.pdf.
[4] CRS Report R40626, *The U.S. Postal Service and Six-Day Delivery: Issues for Congress*, by Wendy R. Ginsberg, p. 13.
[5] U.S. Postal Service, *Ensuring a Viable Postal Service for America*, p. 7.

expenditures.[6] Between FY2010 and FY2020, the USPS suggests that these changes could reduce the predicted $238 billion shortfall by $123 billion.

To reduce the remaining $115 billion shortfall, the USPS argues that Congress must enact legislation to alter current postal law.[7] In particular, the USPS requests that postal law to be amended to:

(1) abolish the mandatory USPS annual payment to the Postal Service Retiree Health Benefits Fund (RHBF);
(2) remove the provision in the annual appropriation law that requires the USPS to deliver mail six days per week;
(3) permit the USPS to move more of its retail operations from post offices to private sector retail facilities (e.g., grocery stores);
(4) strengthen the USPS's power to bargain with its unions and increase the usage of part-time employees by requiring an arbitrator between the parties to consider the financial condition of the USPS in rendering decisions;
(5) increase the USPS's flexibility to price its products, especially those mail classes where postage is less than the costs to USPS to deliver them (e.g., periodicals[8] and library mail);
(6) provide the USPS with greater flexibility to offer new products by expanding the legal definition of "postal services;" and
(7) increase the USPS's ability to respond to changes in the market for its products and services by reducing the time the Postal Regulatory Commission (PRC) is permitted to review the USPS's actions and/or making the PRC's reviews post hoc.[9]

Per the Committees' request, the following sections address proposals (1), (2), (3), (5), and (6), as well as the IG's report on CSRS Pensions.

The USPS's Proposal to Cease Prefunding its Retiree Health Benefits

Sections 801 to 803 of the Postal Accountability and Enhancement Act (PAEA; P.L. 109-435; 120 Stat. 3198) changed the USPS from funding its retirees' health care costs from an out-of-pocket or pay-as-you-go basis to prefunding these obligations. To this end, the PAEA requires the USPS to pay more than $5 billion annually from FY2007 through FY2016 to build up a retirement fund from which USPS retirees' benefits will be paid starting FY2017 (**Table 1**).

Table 1. Postal Service Retiree Health Benefits Fund Payments Under PAEA

Fiscal Year	Payment (billions)
2007	$5.4
2008	$5.6
2009	$5.4[a]
2010	$5.5

[6] Ibid., p. 10.
[7] Most postal law may be found in Title 39 of the *U.S. Code*.
[8] On periodicals' failure to cover their mailing costs, see CRS Report R40162, *Postage Subsidies for Periodicals: History and Recent Developments*, by Kevin R. Kosar.
[9] U.S. Postal Service, *Ensuring a Viable Postal Service for America*, pp. 10-15.

Fiscal Year	Payment (billions)
2011	$5.5
2012	$5.6
2013	$5.6
2014	$5.7
2015	$5.7
2016	$5.8

Source: Postal Accountability and Enhancement Act (P.L. 109-435, Sec. 803; 120 Stat. 3251-3252; 5 U.S.C Sec. 8909(d)(3)(A).)

a. FY2009 payment amount of $5.4 billion was reduced to $1.4 billion with enactment of P.L. 111-68.

In FY2017, the USPS will amortize any remaining retiree health benefit obligation over a 40-year period.

On the one hand, prefunding future retirees' health benefits is prudent. Prefunding benefits can help ensure that the USPS does not default and leave its retirees without any health benefits. On the other hand, the USPS is the only federal agency required to do this, and the PAEA's ten-year payment schedule has been questioned.

The U.S. Postal Service Office Inspector General (IG), Office of Personnel Management (OPM), and the Postal Regulatory Commission (PRC) have disagreed on the size of the USPS's future retiree health benefits obligation (**Table 2**). Therefore, they came to different conclusions as to the amount the USPS should pay annually into the RHBF to adequately fund this obligation.

Table 2. Estimates of the USPS's Retiree Health Benefits Obligation and Required Annual Payments (billions)

	OPM	IG	PRC
Estimated obligation as of FY2016	$147.9	$90.5	$113.2
Required annual USPS payment	$5.5	$1.7	$3.4

Source: U.S. Postal Service Office of Inspector General and Postal Regulatory Commission.

These numbers vary greatly because each agency used different assumptions in making their calculations. For example, the IG assumes healthcare costs will rise 5% annually, while the OPM assumes they will rise 7%.[10]

The 111th Congress amended the PAEA's RHBF payment schedule by enacting H.R. 2918, the Legislative Branch Appropriations Act [of] 2010. President Barack Obama signed the bill into law the next day (P.L. 111-68). Section 164 of the law reduced the USPS's FY2009 payment to the RHBF from $5.4 billion to $1.4 billion. The legislation did not relieve the USPS of this $4

[10] Respectively, see U.S. Postal Service Inspector General, *Final Management Advisory Report–Estimates of Postal Service Liability for Retiree Health Care Benefits* (Washington: USPSOIG, July 22, 2009), at http://www.uspsoig.gov/foia_files/ESS-MA-09-001R.pdf; and Postal Regulatory Commission, *Postal Regulatory Commission Review of Retiree Health Benefit Fund Liability as Calculated by Office of Personnel Management and U.S. Postal Service Office of Inspector General* (Washington: PRC, July 30, 2009), at http://www.prc.gov/Docs/63/63987/Retiree%20Health%20Fund%20Study_109.pdf.

billion obligation; rather, it deferred USPS's payment. Come FY2017, the $4 billion will be added to whatever remaining outstanding health care obligation may exist, and will be amortized over a 40-year period.

The USPS's report proposes ending the prefunding of future retiree health benefits through annual payments. Instead, the USPS would like Congress to transfer the $75 billion in purported overfunding of its Civil Service Retirement System pension to the RHBF.[11] Doing this, the USPS contends, would ensure that future retiree health benefits are fully funded. (The CSRS issue is addressed later in this testimony.)

The USPS's Proposal to Switch to Five-day Mail Delivery

The USPS's report states that it "must have the authority to reassess and adjust the frequency of delivery" because of the recent drop in mail volume.[12] The USPS has said that it would like to end six-day delivery of mail on Saturday, as that day "has the week's lowest daily volume, and more than a third of U.S. businesses are closed."[13] Post offices would remain open for customers who wanted to purchase postal services and collect mail from post offices boxes. Possibly, some post offices will permit residential customers to pick up packages requiring a signature.[14]

Nothing in federal postal law (Title 39 *U.S. Code*) requires the USPS to deliver mail six days per week. However, since 1984 Congress has included a provision in its annual appropriation to the USPS stating that "6-day delivery and rural delivery of mail shall continue at not less than the 1983 level" (e.g., P.L. 117-111; 123 Stat. 3200). Although the precise meaning of this mandate is not clear, the USPS to date has treated the language to mean that it lacks the authority to move to five-day mail until Congress ceases including the six-day mail provision in annual appropriations.

Since 2008, three studies (two by the USPS and one by the PRC) have examined the possible financial effects of a switch from six-day to five-day delivery.[15] The studies all estimate that the USPS would save money by reducing the days of delivery from six to five, as the cost savings (largely due to reduced labor expenses) will exceed any decline in revenues due to lower demand for mail prompted by a reduced delivery schedule. The studies suggest an annual improvement to the USPS's financial condition that would be between $1.9 billion to $3.5 billion.[16]

On March 30, 2010, the USPS asked the PRC for an advisory opinion on reducing delivery to five days. By law, the USPS must ask the PRC for an opinion when the USPS "determines that there should be a change in the nature of postal services which will generally affect service on a

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[11] U.S. Postal Service, *Ensuring a Viable Postal Service for America*, p. 11.
[12] Ibid., p. 12.
[13] U.S. Postal Service, "Five-Day Delivery" web page, at http://www.usps.com/communications/five-daydelivery/.
[14] U.S. Postal Service, *Delivering the Future: Five-Day Delivery is Part of the Solution* (Washington: USPS, March 2010), p. 13, at http://www.usps.com/communications/five-daydelivery/plan/5day_plan_delivery.pdf.
[15] U.S. Postal Service, *Report on the Universal Postal Service and the Postal Monopoly* (Washington: USPS, October 2008), at http://www.usps.com/postallaw/_pdf/USPSUSOReport.pdf; Postal Regulatory Commission, *Report on the Universal Postal Service and the Postal Monopoly* (Washington: PRC, December 19, 2008), at http://www.prc.gov/Docs/61/61628/USO%20Report.pdf; and U.S. Postal Service, *Delivering the Future: Five-Day Delivery is Part of the Solution*.
[16] CRS Report R40626, *The U.S. Postal Service and Six-Day Delivery: Issues for Congress*, by Wendy R. Ginsberg, p. 16.

nationwide or substantially nationwide basis... within a reasonable time prior to the effective date of such proposal" (39 U.S.C. 3661). Under PRC rules, a "reasonable time" is defined at "not less than 90 days" (39 CFR 3001.72). PRC Chairman Ruth Goldway suggested in a recent hearing that the PRC may require six to nine months to issue its opinion.[17]

The USPS's Proposal to Close Post Offices

In its report, the USPS states that it needs additional flexibility to close "redundant retail facilities."[18] The report does not say whether it would target post offices' where costs exceed revenues; nor does it provide a target figure for the optimum number of retail facilities that the USPS should operate.

As of FY2009, the USPS had 35,823 retail postal facilities, including post offices, post office branches and stations, community post offices, and contract postal units. This is 16.9% fewer facilities than existed in 1970 when the USPS was established as an independent establishment of the executive branch (**Table 3**).[19]

Table 3. The Number of USPS Retail Postal Facilities, FY1970 vs. FY2009[20]

Retail Postal Facility Type	1970	2009	% Change
Post Offices	32,002	27,161	-15.1%
Post Office Branches and Post Office Stations	3,869	4,828	25.3%
Community Post Offices and Contract Postal Units	7,241	3,834	-47.1%
Total	43,112	35,823	-16.9%

Source: U.S. Postal Service, *Annual Reports*, 1970-2008, and "Form 10-K," November 16, 2009.

Additionally, the report also does not explain what laws would need to be amended to accomplish this objective of fewer "redundant" facilities. 39 U.S.C. 101, which sets the nation's postal policy, states—

[17] Statement of Ruth Goldway, Chairman of the Postal Regulatory Commission, in U.S. Congress, Senate Committee on Appropriations, Subcommittee on Financial Services and General Government, hearing, *Hearing on the Postal Service*, 111th Congress, 2nd sess., March 18, 2010. Commissioner Goldway's statement came at minutes 91.55 to 92.15 of the hearing, a video of which may be viewed at http://appropriations.senate.gov/webcasts.cfm?method=webcasts.view&id=0ab901bd-d6f5-40c0-8f6e-49bb6fca1f69.

[18] U.S. Postal Service, *Ensuring a Viable Postal Service for America*, p. 12.

[19] CRS Report R40719, *Post Office and Retail Postal Facility Closures: Overview and Issues for Congress*, by Kevin R. Kosar, p. 8.

[20] A post office is the USPS's basic organizational unit. Generally, each post office has primary responsibility for collection, delivery, and retail operations in a specific geographic area. A post office branch is a unit of a main post office that is outside the corporate limits of the city or town of the main post office. A post office station is a main post office that is within the corporate limits of the city or town of the main post office. U.S. Postal Service, *Publication 32: Glossary of Postal Terms* (Washington: USPS, July 5, 2007), at http://www.usps.com/cpim/ftp/pubs/pub32/pub32h_p.html.

> The Postal Service shall provide a maximum degree of effective and regular postal services to rural areas, communities, and small towns where post offices are not self-sustaining. No small post office shall be closed solely for operating at a deficit, it being the specific intent of the Congress that effective postal services be insured to residents of both urban and rural communities.

Additionally, a provision in the annual Financial Service and General Government Appropriation Act declares that "none of the funds provided in this Act shall be used to consolidate or close small rural and other small post offices in [this] fiscal year" (e.g., P.L. 117-111; 123 Stat. 3200).

Postal law also requires the USPS to follow statutory procedures when it closes a post office. The USPS must "provide adequate notice of its intention to close or consolidate such post office at least 60 days prior to the proposed date of such closing or consolidation to persons served by such post office to ensure that such persons will have an opportunity to present their views" (39 U.S.C. 404(d)(1)). In deciding whether to close a post office, the USPS must consider:

> (i) the effect of such closing or consolidation on the community served by such post office;
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> (ii) the effect of such closing or consolidation on employees of the Postal Service employed at such office;
>
> (iii) whether such closing or consolidation is consistent with the policy of the Government ... that the Postal Service shall provide a maximum degree of effective and regular postal services to rural areas, communities, and small towns where post offices are not self-sustaining;
>
> (iv) the economic savings to the Postal Service resulting from such closing or consolidation; and
>
> (v) such other factors as the Postal Service determines are necessary (39 U.S.C. 404(d)(2)(A)).

If the USPS decides to move forward with a closure, it must notify the persons served by the post office of its decision and the findings used to arrive at this decision. The USPS must wait at least 60 days before proceeding with the closure, and any person served by the post office slated for closure may appeal the closure to the PRC, which has 120 days to consider the appeal.

The PRC may fault the USPS's decision to close a post office only if the PRC finds the decision to be "(A) arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with the law; (B) without observance of procedure required by law; or (C) unsupported by substantial evidence on the record" (39 U.S.C. 404(d)(5)). The PRC may require the USPS to reconsider its decision, but the ultimate authority to close a post office rests with the USPS.

The Postal Service does not use this process for closing all postal facilities. It argues that the law applies to post offices but not post office stations or branches.[21] The Postal Regulatory Commission has criticized this interpretation of the law but has no power to require the USPS to apply the full statutory process to post office branches and stations.[22] Since postal customers frequently cannot discern the difference between a post office and a post office branch or station,

[21] CRS Report R40719, *Post Office and Retail Postal Facility Closures: Overview and Issues for Congress*, pp. 13-14.

[22] Postal Regulatory Commission, *Advisory Opinion Concerning the Process for Evaluating Closing Stations and Branches*, Docket No. N2009-1, March 10, 2010, pp. 52-53, at http://www.prc.gov/%28S%28ha30pf555fp1gs45di5vym45%29%29/Docs/67/67174/Advisory_Opinion_031010.pdf.

the use of a expedited process can cause confusion among the public.[23] During the past two Congresses, Representative Albio Sires has introduced two bills (H.R. 6217 and H.R. 658) that would require the USPS to use the same statutory process for the closure of post offices and post office branches and stations. One hundred Members of the 110th Congress cosponsored H.R. 6217, and 100 members of the 111th Congress have cosponsored H.R. 658 (as of April 5, 2010).

As Congress further considers the USPS's request to have increased flexibility to reduce its retail network, it may wish to ask the Postal Service to provide further clarification as to what types of facilities it may close, what public input and notification processes it intends to use, and which laws would need to be amended to provide this flexibility.

The USPS's Proposals to Have Additional Flexibility in Pricing and Introducing Products

The USPS report argues that the Postal Service lacks sufficient authority to set its prices in response to "market dynamics." The USPS proposes altering some of the ratemaking policies enacted in the 2006 Postal Accountability and Enhancement Act.

The PAEA streamlined the former postage-pricing system and increased the USPS's discretion over pricing. The law separates the USPS products into "market-dominant" and "competitive" classes. Market-dominant products make up the bulk of the mail-stream and the USPS's revenues. These products are called "market-dominant" because few if any private sector competitors exist to provide these products and services.[24] Market-dominant products include (1) first-class mail letters and sealed parcels, (2) first-class mail cards, (3) periodicals, (4) standard mail, (5) single-piece parcel post, (6) media mail, (7) bound printed matter, (8) library mail, (9) special services, and (10) single-piece international mail (39 U.S.C. 3621).[25]

The PAEA established a rate cap on postage increases for market-dominant products (39 U.S.C. 3622(D)(1)(a)). The USPS may raise the rates (prices) of any market-dominant product by no more than the annual increase of the Consumer Price Index for All Urban Consumers (CPI-U).[26]

The USPS wants this price cap revised to apply only to market-dominant products as an entire class, rather than to individual market dominant products. If given this authority, the USPS could raise the postage rates of one or more market-dominant product (e.g., periodicals) more than the CPI-U, and keep the dominant class as a whole under the CPI-U by holding steady or lowering postage rates for other market-dominant products.

The apparent objective of this proposed change to rate-setting would be to empower the USPS to raise rates on those mail classes (non-profit mail, media mail, library mail, periodicals, etc.) that

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[23] The Postal Service has admitted this occurs. See "Direct Testimony of Alice M. Vangorder on Behalf of the United States Postal Service," *Postal Regulatory Commission, Docket No. N2009-1*, p. 4, footnote 2, at http://www.prc.gov/Docs/63/63567/FINAL.VANGORDER.W.ATTACH.pdf.
[24] E.g., the USPS possesses a legal monopoly over the delivery of first-class mail (18 U.S.C. 1693-1999 and 39 U.S.C. 601).
[25] Competitive products include those for which a competitive market exists. They include (1) priority mail, (2) expedited mail, (3) bulk parcel post, (4) bulk international mail, and (5) mailgrams (39 U.S.C. 3631). The prices of competitive products are not rate-capped.
[26] On the CPI-U, see CRS Report RL30074, *The Consumer Price Index: A Brief Overview*, by Brian W. Cashell.

currently cost the USPS more to deliver than their postage.[27] In FY2009, these money-losing mail classes cost the USPS at least $1.7 billion.[28] Both the 1970 Postal Reorganization Act (84 Stat. 760) and the 2006 PAEA (120 Stat. 3201) require all mail classes to cover their costs.[29] However, this requirement probably never has been met because federal postal law (36 U.S.C. 3622 and 39 U.S.C. 3626) also provides for "reduced rates" for certain classes of mail (e.g., non-profit mail, media mail, periodicals, etc.)

Thus, in addition to requiring the PAEA's provisions to be amended, the USPS's proposal for pricing flexibility would require amending 39 U.S.C 3622 and 39 U.S.C. 3626.

The IG's Report on CSRS Pensions[30]

On January 20, 2010, the U.S. Postal Service Office of Inspector General (IG) published a report on the USPS's funding of pension costs for postal workers who were employed by both the U.S. Post Office Department (prior to 1971) and its successor, the U.S. Postal Service.[31] The report criticizes the allocation of the pension costs between the USPS and the federal government for employees who had service both as employees of the Post Office Department and later as employees of the Postal Service.

The IG report notes that the Postal Service is currently responsible for meeting all pension costs under the Civil Service Retirement System (CSRS) for employees hired after 1971. For employees with service both before and after 1971, the federal government and the Postal Service share responsibility for CSRS pensions. The federal government pays for service through 1971, and the USPS pays for service after 1971.

The IG report contends that the allocation of CSRS costs between the USPS and the federal government is unfair because the Postal Service is fully responsible for increases in pension costs that result from pay raises granted after 1971. Because CSRS pensions are based on both an employee's years of service and the average of an employee's highest three consecutive years of pay, pension costs rise as employee pay rises. As a consequence, the percentage of CSRS pension costs allocated to the USPS for an employee who worked for both the Post Office Department and the USPS is greater than the proportion of the worker's career that he or she spent as an employee of the USPS. The IG report notes, for example, that for a person who worked for the Post Office Department for 20 years prior to 1971 and for the USPS for 10 years thereafter, the USPS is obliged to fund about half of this person's pension costs. (The other half is paid for by the U.S. government.)

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[27] U.S. Postal Service, *Ensuring a Viable Postal Service for America*, p. 14.
[28] Postal Regulatory Commission, *FY2009 Annual Compliance Report* (Washington: PRC, March 29, 2010), p. 28, at http://www.prc.gov/prc-docs/home/whatsnew/ACD%20Report_2009_FINAL_Combined_747.pdf. This $1.7 billion figure only refers to attributable costs; if institutional costs were included, the figure would be higher.
[29] Specifically, postal law requires each mail class to cover its "attributable cost." The term "attributable cost" refers to the cost to the USPS to process a particular class of mail. This is to be contrasted with the term "institutional cost," which refers to the fixed costs of the USPS (e.g., the compensation of a mail carrier, who delivers all classes of mail). The law does not require each mail class to cover its institutional cost.
[30] The author thanks Patrick Purcell, Specialist in Income Security, Domestic Social Policy Division, Congressional Research Service, for his assistance in writing this section.
[31] U.S. Postal Service Office of Inspector General, *The Postal Service's Share of CSRS Pension Responsibility*, RARC-WP-10-001 (Washington: USPSOIG, January 20, 2010) at http://www.uspsoig.gov/foia_files/RARC-WP-10-001.pdf.

The IG report suggests that the USPS's share of CSRS pension costs should be proportional to employees' length of service as USPS employees relative to their total length of service with the Post Office Department and the USPS. If an employee had spent 15 years as an employee of the Post Office Department and 15 years as an employee of the USPS, for example, the federal government and the USPS each would be responsible for half of the cost of that individual's CSRS pension. The IG's report estimates that under the current method of allocating the costs of CSRS pensions, the Postal Service has paid $75 billion more into the Civil Service Retirement and Disability Trust Fund than it would have paid if costs were divided between the federal government and the USPS strictly in proportion to length of service.

In 2004, the Postal Service requested the OPM, which administers the Civil Service Retirement System, to reconsider the method by which it allocates CSRS pension expenses between the Postal Service and the U.S. Treasury. The OPM denied the request on the grounds that the allocation method it had developed was consistent with federal law. The OPM cited P.L. 93-349 (July 12, 1974), which required the USPS to finance all increases in retirement liabilities that are attributable to salary increases granted by the USPS. The House committee report accompanying the bill that was enacted as P.L. 93-349 (H.R. 29, 93rd Congress) states that the "purpose of this legislation is to clearly establish the responsibility of the U.S. Postal Service to finance increases in the liability of the Civil Service Retirement and Disability Fund, caused by administrative action of the Postal Service, as apart from increases in unfunded liabilities which are incurred by act of Congress." The committee report further states that with respect to any increase in CSRS pension expense that results from future pay raises received by USPS employees, "the cost of this liability should properly and equitably be borne by the Postal Service."

A reduction in the proportion of CSRS pension expenses allocated to the Postal Service would increase the unfunded liability of the Civil Service Retirement and Disability Fund. Absent a reduction in the cost of financing CSRS pensions, changing the allocation of CSRS pension expenses between the Postal Service and general fund of the U.S. Treasury is a zero-sum game. A reduction in the amount of CSRS pension expenses allocated to the USPS would result in an equal increase in CSRS pension expenses borne by the U.S. Treasury.

On March 2, 2010, the Postal Regulatory Commission said it will conduct its own review of the USPS's pension liability.[32]

Conclusion: Short-term and Long-term Challenges

The USPS has asked Congress to alter a number of provisions of current postal law because these statutes are viewed as impeding the USPS's ability to stem its financial losses. As Congress considers the USPS's proposals and other options, it may wish to consider the USPS's financial condition within the frameworks of the short-term (now until FY2011) and the long-term (now until 2020).

Short-term

The USPS has run significant deficits since FY2007 and may reach its statutory debt limit ($15 billion) in FY2011 (39 U.S.C. 2005(a)).

[32] Postal Regulatory Commission, "PRC Initiates Review of USPS Pension Liability," press release, March 2, 2010, at http://prc.gov/prc-docs/home/whatsnew/PRC%20Review%20of%20USPS%20CSRS%20liability_604.pdf.

Additionally, the USPS may face a liquidity problem at the end of FY2010 or the beginning of FY2011. The USPS's FY2010 first quarter financial filing (10-Q) indicates that its financial position is unenviable. The USPS went from having $4.1 billion to $0.8 billion in cash, which is a low level for an agency with an average weekly operating expense over $1 billion. In part, this decrease in available cash was an effect of the USPS's retiring some of its debt. The USPS reduced its debt by $2.7 billion, from $10.2 billion (as of the end of FY2009) to $7.5 billion.[33]

Unless second quarter revenues exceed second quarter expenses, the USPS will have to borrow money to continue operations. Since the USPS finished FY2009 with outstanding debt of $10.2 billion, it is permitted by law to finish FY2010 with $13.2 billion in debt. So, at the end of its first quarter (December 31, 2009), the USPS could borrow up to an additional $5.7 billion from the Federal Financing Bank (FFB) to help it cover its operating expenses.[34] Combining this with the $0.8 billion that it already had, the USPS could have begun the second quarter with $6.5 billion in cash.

Yet, it is questionable whether even this amount of cash will suffice. If one were to assume the USPS financially will break even for the rest of FY2010 (which the USPS itself doubts) and it can retain this $6.5 billion in cash, the USPS still may face a cash shortage at the beginning of FY2011. The agency must pay $5.5 billion to the Retiree Health Benefits Fund on September 30, 2010, and pay $1.1 billion to the Department of Labor for workers' compensation in October 2010.[35]

In its FY2010 first quarter 10-Q filing, the USPS stated that in the event of a liquidity crisis it would pay less than the required amount into the Retiree Health Benefits Fund.[36] The consequences of the USPS failing to abide by the PAEA's mandated payment schedule are unclear; the PAEA is silent on this matter.

Of the four proposed USPS changes to postal law considered in this written testimony, only two would appear to be capable of addressing the USPS's short-term financial challenge—reducing the USPS's annual payment to the RHBF, and permitting the USPS to draw back some of its contributions to the CSRS pension.[37]

Long-term

In its report, the USPS described its plight as a "rapidly worsening crisis," and claimed that the USPS "will continue to face declining volume, stagnant revenue, large fixed costs, and rising workforce costs. Without additional action to address these trends, the Postal Service would face annual losses as great as $33 billion by 2020."[38] The USPS suggests it might suffer cumulative losses of $238 billion between FY2010 and FY2020.

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[33] Ibid., pp. 4, 10-11.
[34] Since the USPS ended FY2009 with $10.2 billion in debt, by law it may conclude FY2010 with debt of up to $13.2 billion. Current debt of $7.5 billion + $5.7 billion in new debt = $13.2 billion in maximum permissible debt at the end of FY2010.
[35] U.S. Postal Service, "Form 10-Q," pp. 8-9.
[36] Ibid., p. 9.
[37] This does not exhaust the options for Congress. It might pursue other measures, such as providing an emergency FY2010 appropriation to the USPS, raising the USPS's debt limit, or an amalgam of policies, such as providing the USPS with additional debt authority but requiring that a portion of that authority be used to fund an effective USPS employee retirement incentive program.
[38] U.S. Postal Service, *Ensuring a Viable Postal Service for America*, p. 6.

While the USPS's short-term financial condition is clearly problematic, its long-term financial condition is less obvious. The USPS report's admonition of a possible $238 billion in cumulative debt by 2020 has been repeatedly mischaracterized as a "prediction" by the media.[39] The report's admonition of $238 billion in cumulative losses is a projection—an estimate of what could happen if certain assumptions hold over the next decade. These assumptions are not certitudes.

First, as noted earlier in this testimony, postal law caps the Postal Service's total debt at $15 billion. For the USPS to reach $238 billion in cumulative losses would require a change in current circumstances. Congress would need to abolish the USPS's statutory debt limit, and then do nothing for 10 years as the USPS borrowed $231 billion from the U.S. Treasury. (As of the end of FY2010 quarter one, the USPS had $8 billion in debt, and $1 billion in cash. Hence, the USPS would need to borrow $231 billion to achieve $238 billion in cumulative debt.)

Second, the $238 billion in cumulative losses could occur only if the USPS took no further actions to reduce its expenses. This is implausible, especially as the USPS's plan states that it intends to use its own existing authorities to reduce the projected $238 billion shortfall by $123 billion (leaving a projected $115 cumulative debt).

Third, the report's 2020 projection assumes that mail volume will continue to fall, sliding another 15% over the coming decade. In this scenario, the USPS's annual revenues would be no higher in 2020 than in FY2010. This assumption of falling mail volumes is based upon a study commissioned by The Boston Consulting Group (BCG).[40] According to the BCG's analysis, the USPS

> will experience profound declines in its volumes of mail.... Notably, volumes will not revisit the high-water-mark of 213 [billion] pieces in 2006—on the contrary, the trajectory for the next 10 years is one of steady decline, which will not reverse even if the current recession abates.[41]

The major cause of this decline, according to the BCG, is the movement of communications to the World Wide Web.

According to the BCG's analysis, the recent mail volume declines of the past two years should not be viewed as primarily an effect of the nation's general economic downturn. Instead, as the USPS puts it, the recession simply "accelerated the volume decline," which is caused by the "fundamental and permanent change in mail use by households and businesses."[42]

This prediction about the future demand for hard copy mail is striking as it would mean the end to an at least 70-year long trend. Since 1930 mail volumes have grown nearly every year, the exception being during the period of 1933 to 1936 when mail volume plunged one year then returned to its previous height over the succeeding three years (**Figure 1**). The BCG prediction would have the USPS of 2020 delivering slightly less mail than the USPS of 1987 (**Figure 2**).

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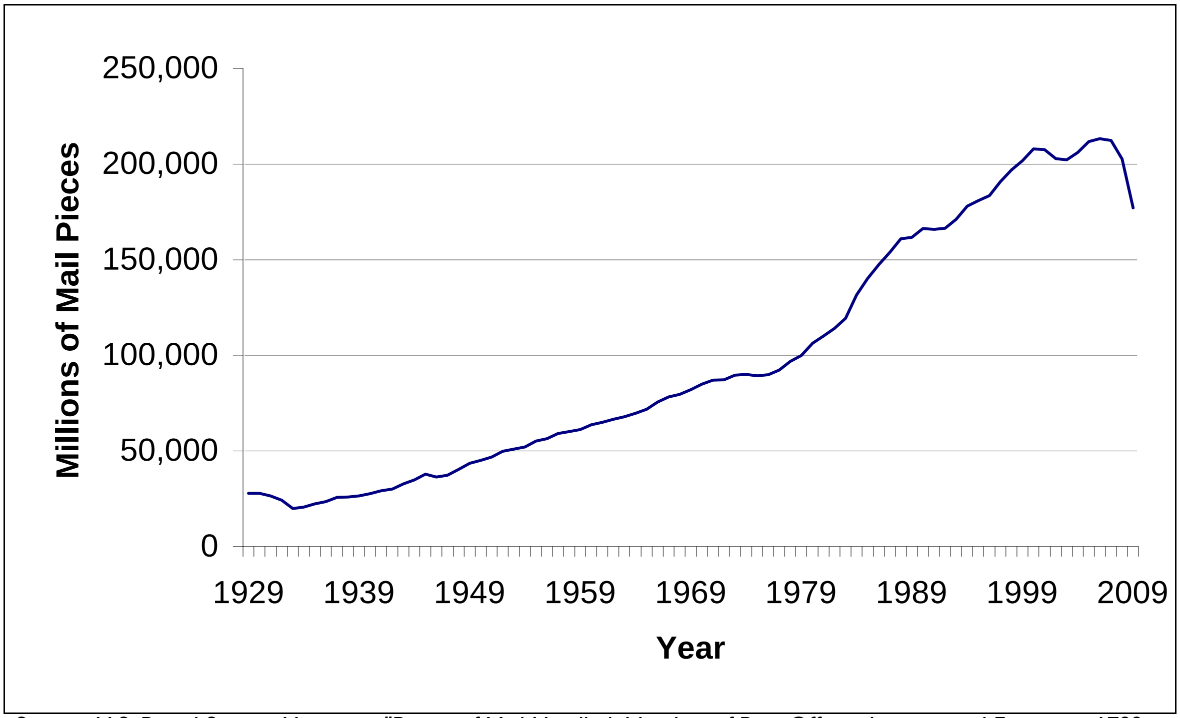
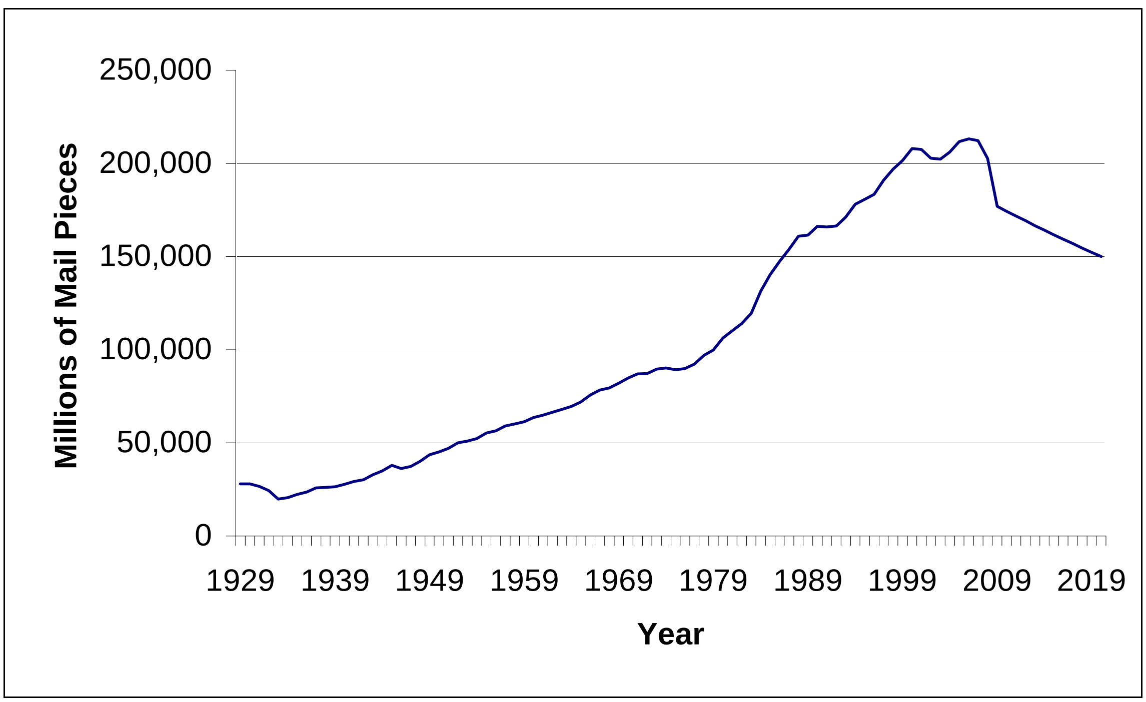
[39] E.g., "A $4.8 million study made public on March 1 predicts the Postal Service will lose $238 billion over the next decade as consumers and businesses conduct more transactions online." Donna Leinwand, "Senators Challenge U.S. Postal Service's 10-Year Rescue Plan," *USA Today*, March 18, 2010, at http://www.usatoday.com/news/washington/2010-03-18-postal-service-hearing_N.htm.
[40] The Boston Consulting Group, *Projecting US Mail Volumes to 2020: Final Report—Detail* (BCG: March 2, 2010, at http://www.usps.com/strategicplanning/_pdf/BCG_Detailed%20presentation.pdf. See also The Boston Consulting Group, "Projecting Mail Volumes to 2020," March 2, 2010, at http://www.usps.com/strategicplanning/_pdf/BCG_Narrative.pdf.
[41] Ibid., p. 2.
[42] U.S. Postal Service, *Ensuring a Viable Postal Service for America*, p. 4.

Figure 1. Mail Volume, FY1929-FY2009



Source: U.S. Postal Service Historian, "Pieces of Mail Handled, Number of Post Offices, Income, and Expenses, 1789 to 2009," at http://www.usps.com/postalhistory/PiecesofMail1789to2009.htm.

Figure 2. Mail Volume FY1929-FY2020 (As Projected by the BCG)



Source: U.S. Postal Service Historian, "Pieces of Mail Handled, Number of Post Offices, Income, and Expenses, 1789 to 2009," at http://www.usps.com/postalhistory/PiecesofMail1789to2009.htm; and The Boston Consulting Group, "Projecting Mail Volumes to 2020," at http://www.usps.com/strategicplanning/_pdf/BCG_Narrative.pdf.

A critic of the BCG's projected 2020 scenario might raise two points.

First, the movement of communications to the World Wide Web has been occurring since the mid-1990s. During this time, the composition of the mail volume changed—less of the mail sent was first-class mail, and more of it was advertising mail. Yet, the total amount of mail sent rose. So, thus far it does not appear that there is a simple inverse relationship between the demand for electronic means of communications and hard copy mail volume. (I.e., if demand for electronic communications goes up, demand for hard copy communications must go down.) Indeed, as noted earlier, the BCG's analysis shows demand for USPS package delivery rising between 2010 and 2020.

Second, the USPS's mail volume peaked in FY2006 at 213.1 billion mail pieces, and was nearly the same in FY2007. In the first two quarters of FY2008 (October through December and January through March), mail volume was higher than in the same quarters in FY2007. It was not until the third quarter of FY2008 (April through June) that the USPS reported a decline in mail volume relative to the same quarter in the previous year.[43] By the end of FY2008, mail volume had dropped from 212.2 to 202.7 billion mail pieces. The U.S. economy entered a recession in December 2007, and mail volume began falling four to six months later. It seems at least plausible that the economic downturn, not electronic migration, was the more significant factor in instigating the sudden mail volume decline of the past two fiscal years.[44] And if that is the case, then arguably the USPS's mail volume might rise again as the economy improves. (The BCG's analysis and the USPS's report do not admit this possibility. Both unequivocally declare that the demand for sending hard copy mail has been permanently weakened in the past two or three years.)

Hence, Congress may wish to further study the recent declines in mail volume to see if the BCG and the UPS are correct that total mail volume is likely to fall during the next decade, or if the demand for only certain classes of mail can be expected to drop. Knowing whether the USPS likely faces a 2020 future with mail volumes of 150, 200, or 250 billion mail pieces would appear to be an important factor in determining whether to significantly alter the structure of the USPS.

That said, it is worth noting that the USPS likely does face long-term financial challenges, although neither the magnitude of the challenges nor the timeline for their onset and maturation is clear. The Government Accountability Office (GAO), for one, long has warned that the USPS faced financial difficulties due to its limited ability to control its labor costs and reduce its mail processing and delivery network.[45]

Moreover, the recent developments in communications technologies may be undermining the nation's stated rationale for having a U.S. Postal Service. The 1970 Postal Reorganization Act declared the USPS was "to bind the Nation together through the personal, educational, literary, and business correspondence of the people." Because of e-mail, cellular phones, and the World Wide Web, personal communication via hard copy mail has declined. As The Boston Consulting Group's analysis indicates, only 4.5% of FY2009's 177 billion mail pieces were person-to-person letters or postcards. Periodicals, which may include educational and literary content, make up 4%

[43] U.S. Postal Service, "Revenue, Pieces and Weight" reports for Postal Quarter IV FY2007 through Quarter I FY2008, at http://www.usps.com/financials/rpw/welcome.htm.
[44] CRS Report R40198, *U.S. Economy in Recession: Similarities To and Differences From the Past*, by Marc Labonte, p. 1.
[45] Government Accountability Office, *U.S. Postal Service: Bold Action Needed to Continue Progress on Postal Transformation*, GAO-04-108T, November 5, 2003.

of the mail. Most of the mail volume today consists of advertising mail and business-related correspondence.[46]

Thank you.

[46] The Boston Consulting Group, *Projecting US Mail Volumes to 2020: Final Report—Detail*, p. 5.