



**Testimony of Ruth Y. Goldway
Chairman**

Postal Regulatory Commission

before the

**U.S. Senate Committee on Homeland Security
and Governmental Affairs**

September 19, 2013

Chairman Carper, Ranking Member Coburn, and members of the Committee, thank you for the opportunity to testify today. I am pleased to represent the Postal Regulatory Commission and to share its views on the important topic of postal reform. We appreciate your leadership in shaping the debate on what must be done to assist the United States Postal Service and ensure its sustainable future.

The Postal Service has an impact on the everyday lives of virtually every citizen in the Nation and will continue to do so well into the future. Even in this age of digital communications, a healthy, viable Postal Service remains an essential part of our Nation's infrastructure. A sizable portion of the U.S. population still depends on the mail

to help manage their lives, and to communicate with businesses, governments, and social institutions.

In 2012, the Federal Communications Commission (FCC) reported that in rural areas, nearly a quarter of the population —14.5 million people—lack access to fixed broadband service at threshold speeds, while in tribal areas, nearly one-third of the population do not have access. In total, approximately 19 million Americans—6 percent of the population—lack access. The FCC also found that even in those areas where broadband is available, approximately 100 million Americans do not subscribe.

The fact is that mail remains the one universal service connecting all American people. And Americans place great trust in the Postal Service. In Ponemon Institute's Most Trusted Companies for Privacy Study, the Postal Service was ranked fourth, and it has been named the "Most Trusted Government Agency" for seven years in a row. The Commission is proud of its role in ensuring that the Postal Service functions as an open, transparent agency that is accountable to the public it serves.

The Committee has convened this hearing to explore how the Postal Service can be renewed and reformed to thrive in this changing environment, and to examine the solutions set forth in S. 1486. The Committee asks that the Commission's testimony focus on postal services, particularly regarding delivery schedules, delivery standards, and post office services. It also requests that the Commission's testimony address possible changes to the ratemaking system and innovation at the Postal Service, including new products and services. My testimony emphasizes the importance of transparency and accountability in the efficient provision of postal services and addresses the Commission's experience and views.

Key Elements of Renewal and Reform

There is broad agreement that legislative changes are needed to place the Postal Service on more sound financial footing. However, the Postal Accountability and Enhancement Act (PAEA) contained numerous reforms that were a positive force for change toward modernizing the Postal Service and that provide a solid foundation for the future. In many respects, the PAEA has been largely successful in improving postal policy and accomplishing a number of laudable Congressional goals. Efforts to renew and reform the Postal Service need not, and should not, replace the many positive provisions included in the PAEA.

The PAEA sought to increase the transparency and accountability of the Postal Service. The Postal Service is required to file periodic financial reports with the Postal Regulatory Commission within 90 days of the end of each fiscal year. The Commission is required to review the Postal Service's Annual Compliance Report and public comments. The Commission must publish its findings and, if any violations are found, order remedial action. This public process has significantly improved the transparency and accountability of the Postal Service.

Another important improvement made by the PAEA was to increase the accuracy and integrity of the Postal Service's internal controls over financial reporting. The PAEA implemented this goal by requiring the Postal Service to comply with certain Sarbanes-Oxley Act's reporting requirements and submit such reports to the Commission. Compliance with these requirements has aided in the standardization and streamlining of the Postal Service's business practices, processes, and systems. It also has enabled

timely identification and remediation of weaknesses, increased accountability, and fostered ownership of controls. The strengthening of controls over business mail processes, including the prevention of lost revenue, has produced substantial indirect financial benefits.

Delivery Schedules

The Commission's experience with potential changes to the Postal Service's delivery schedules has occurred as a part of a Postal Service request to the Commission for an advisory opinion on a change in the nature of postal services. In Docket No. N2010-1, the Commission reviewed a Postal Service request to discontinue delivery of mail to street addresses on Saturdays. Based on extensive public contributions, the Commission provided advice to the Postal Service highlighting the impact of the proposal on rural, remote, and non-contiguous areas, and the importance of retaining delivery of prescription medications. The Postal Service has taken these concerns into account in developing its most recent proposals for altering delivery schedules.

This demonstrates the value of examination by an independent third party of a public record that includes comments from both senders and recipients of mail. This process contributes significantly toward ensuring that far reaching changes to postal services are consistent with the public need and avoid unintended negative consequences to those dependent on the Postal Service.

The current process is not without flaws. There was valid criticism that the quasi-judicial process used to conduct this and other Commission advisory opinion cases could be too time consuming, and that Commission advice would be more useful if it could be provided in a more timely manner. The Commission is responding to these concerns. We issued a Notice of Proposed Rulemaking requesting comments on procedures designed to condense the time for Commission analysis and decision making to three months. The final date for comments was August 28, 2013. We have received many thoughtful comments and suggestions relating to our proposal and have been actively evaluating them. Consistent with our other responsibilities, we plan to establish new rules that streamline the process in the near future.

Delivery Standards

The Commission's experience with potential changes to the Postal Service's delivery standards has occurred in two areas. First, the PAEA provided the Commission with a role to increase the Postal Service's accountability and transparency regarding service performance and measurement. Second, the Commission has conducted an advisory opinion proceeding regarding a Postal Service request to alter its delivery standards on a nationwide or substantially nationwide basis.

The PAEA sought to place a new emphasis on service performance and measurement to ensure that the Postal Service's quality of service does not deteriorate under the CPI price cap system. Degrading service is not an acceptable means of saving costs to offset lower revenue from price cap requirements. The PAEA

implemented this goal by requiring the Postal Service to greatly enhance service measurement and reporting. It also required the Commission to review these reports as part of its Annual Compliance Determination.

Consistent with the aphorism “what is measured is what is fixed,” the Postal Service’s reports of on-time performance have shown improvement since the passage of the PAEA.

The Commission has found in its Annual Compliance Determinations that service performance for most market dominant products has been moving toward meeting their respective annual on-time targets. The fourth quarter of FY 2011 was the first quarter that the Postal Service reported service performance results for the majority of its market dominant products. In its FY 2011 ACD, the Commission noted that the level of Full Service Intelligent Mail participation was impacting the reliability of many service performance results but that it appeared the Postal Service was having difficulty meeting its service standard goals for most market dominant products. The Commission stated that it regards low performance results for speed of delivery an important issue the Postal Service must resolve.

In its FY 2012 ACD, the Commission found that most market dominant products showed improvement toward meeting annual on-time targets. The majority of First-Class Mail products, Special Services products, and Package Services products either approached or exceeded annual service performance targets. Although many Standard Mail products did not meet annual on-time targets, service performance improved throughout the fiscal year.

As of the third quarter of FY 2013, both First-Class Single-Piece and Presort Letters and Cards are meeting the service performance targets. Standard Mail products have continued to make strides toward meeting their on-time targets. Both Standard High-Density and Saturation Letters and Flats are meeting their targets and Standard Letters is achieving 88.4 percent on-time performance, within 2 percentage points of its 90 percent target.

The Postal Service and the Commission are continuing to work together to improve the Postal Service's service performance measurement systems. As measurement systems become more robust, the Postal Service should become better able to quickly identify and resolve service problems.

In Commission Docket No. N2012-1, the Postal Service requested an advisory opinion on a proposal to consolidate mail processing and transportation operations that were expected to result in changes to its service standards for First-Class Mail, Periodicals, Package Services and Standard Mail. The evidence submitted by participants in the Commission's public proceeding identified potential service and efficiency problems with the proposal. The Commission found that network rationalization, if implemented properly, could realize substantial cost savings while preserving most current service levels. It recommended the Postal Service add more structure to its phased approach. This would allow the Postal Service to evaluate the success of each phase prior to implementing subsequent phases in order to incorporate lessons learned from earlier phases.

Post Office Services

The Commission's experience with potential changes to the Postal Service's retail services has occurred in connection with several Postal Service requests for advisory opinions regarding changes in the nature of postal services and the numerous appeals filed following one of those proposals. In Commission Docket No. N2009-1, the Postal Service requested an advisory opinion on a proposal to close thousands of its station and branch retail facilities. Through a transparent and open public process, the Commission provided guidance, identifying weaknesses of the proposal and making constructive recommendations to improve the Postal Service's retail facility optimization plans and discontinuance processes. Subsequent Postal Service retail facility optimization plans submitted to the Commission for review, including the most recent efforts known as "POStPlan," incorporated this prior Commission advice by allowing Post Offices to remain in operation with modified retail hours and implementing improved procedures to obtain public input before closing retail facilities.

The proposed legislation clarifies that patrons served by stations and branches can appeal to the Commission when their post office is closed. This resolves a long-standing disagreement between the Postal Service and the Commission and should eliminate confusion on this point.

Ratemaking System

The Commission has significant experience regarding implementation of a modern system of rate regulation for postal services. A major focus area of the PAEA was postal ratemaking. It sought to end the Postal Service's reliance on unpredictable price increases and concerns that the Postal Service was passing along the costs of less than optimally efficient operations to mailers through cost-of-service ratemaking. The PAEA achieved these goals by introducing a regulatory price cap regime for Postal Service products over which it enjoys a statutory monopoly or possesses market power. The Postal Service's rate adjustments for these so-called market dominant products are now completed at predictable intervals, and rate increases for each class of mail are capped at the rate of inflation.

This rate cap approach has had positive impacts in many areas. Most importantly, it has protected ratepayers from large, unpredictable rate increases that were permissible under the old law. This ability to accurately budget for rate increases has reduced disruption to mailer operations and permitted mailers to plan their mail programs with regular reliability.

Moreover, the requirement that the Postal Service justify price increases based on extraordinary or exceptional circumstances to an independent, impartial regulatory body has guarded customers from unwarranted exigent price increases. This protection is particularly important in a government mandated monopoly environment.

The PAEA sought to eliminate the lengthy and expensive rate case litigation that occurred under prior law. The PAEA implemented this goal by providing the Postal

Service with increased flexibility to set prices within the bounds of the inflation-based price cap regime, and requiring the Commission to design and implement a modern system of rate regulation. The Commission developed a simplified process that replaced the 10-month adversarial proceeding required under prior law. The new process has made rate cases relatively uncontroversial and has significantly decreased litigation-related expenses for both the Postal Service and the mailers and organizations that formerly participated in rate cases.

Since passage of the PAEA the Commission has reviewed rate adjustment proposals to assure compliance with the law promptly and efficiently. Negotiated service agreement reviews have taken an average of only 18 days. Excluding the one exigent rate case, rate requests were completed, on average, in 37 days. The Commission completed its one exigent rate request in 86 days. No mailer has filed a complaint related to a rate reviewed and approved by the Commission.

The PAEA also sought to modernize postal ratemaking by placing the Postal Service on a more level playing field with respect to its private sector competitors in those areas where it faces direct competition. To implement this goal, the PAEA divided Postal Service products into market dominant and competitive categories, and tasked the Commission with maintaining an accurate division between these categories as the Postal Service's product mix changes. This system has provided the Postal Service with significant flexibility to price its competitive products at market rates. The Postal Service has taken advantage of this increased flexibility and the growth in the package delivery industry to increase its revenues. In the first nine months of FY 2013,

the Postal Service's shipping and package product revenue increased by 7.5 percent and volume increased by 5.7 percent.

The price cap also has successfully motivated the Postal Service to implement extensive cost-cutting strategies and increases in efficiency.

One of the largest contributors to Postal Service cost savings are reductions in employee workhours. While some of these reductions are related to the declines in Postal Service volumes, they also reflect improved total factor productivity.

The recent history of wage negotiation also seems likely to have been strongly influenced by the PAEA's strict limitations on allowing the Postal Service to increase prices above the rate of inflation. During the first three quarters of FY 2013, the Postal Service took advantage of flexibilities negotiated with its employee organizations, and reduced career employee workhours by approximately 41 million hours (equivalent to the work of over 34,000 employees) while increasing non-career employee workhours by approximately 30 million hours. Similarly, during FY 2012, the Postal Service reduced total employee workhours by approximately 27 million hours, or 2.3 percent from 2011.

In addition to workhour savings, the Postal Service reports that it realized other significant cost savings during the first three quarters of FY 2013 through consolidation of 104 mail processing facilities; a reduction in operating hours at 7,397 Post Offices as part of the Postal Service's "POStPlan;" and the consolidation or reduction of 1,156 delivery routes.

Between 2006 and 2012, the Postal Service closed more than 180 mail processing facilities, disposed of nearly 4,000 pieces of equipment, reduced city

delivery routes by 21,000, and decreased its career employee rolls by more than 110,000. As of June 30, 2013, the Postal Service's career workforce size is at a level last seen in 1966.

Innovation

The Commission's experience with Postal Service innovation has occurred through the Postal Service requests for approval of market tests of experimental products.

The PAEA provided the Postal Service with streamlined authority to introduce experimental products, allowing the Postal Service to innovate to make its products more valuable to customers. Since the passage of the PAEA, the Commission has reviewed and approved nine market tests under applicable statutory requirements allowing for comment by interested persons, mailers, and other stakeholders in the postal community. Through this process, the Commission, the Postal Service, and the mailing community have worked cooperatively and expeditiously to facilitate market tests of experimental products as envisioned by the PAEA while preserving proper safeguards to protect both customers and competitors.

The statutory authority and rules governing market tests of experimental products have worked well, providing the Postal Service with the appropriate level of flexibility to develop and conduct market tests of new postal products. To further encourage innovation, in its Section 701 Report, the Commission recommended allowing the Postal Service to experiment with larger market tests by raising the maximum revenue

limitation. Section 302 of S. 1486 would provide this statutory authorization. This should allow the Postal Service to advance more ideas aimed at increasing the Postal Service's revenue streams.

S. 1486 would allow the Postal Service to offer new, nonpostal services in addition to those grandfathered nonpostal services allowed under the PAEA. If Congress decides to allow the Postal Service to offer such services, it should include adequate safeguards to reduce the potential for unprofitable nonpostal business ventures. In addition, such safeguards should ensure that the Postal Service's entry into nonpostal markets will not distort private markets or divert Postal Service resources from its core responsibilities. Toward that end, the Commission recommends that if the Postal Service is allowed to offer certain new, nonpostal services, these services be subject to the regulatory review established by the PAEA. Adding these regulatory review and oversight mechanisms for new nonpostal services will help ensure that the Postal Service offers profitable, new nonpostal services. This will minimize the likelihood of a repeat of the problems of nonpostal service offerings in the late 1990s and early 2000s when the Commission had no regulatory review or oversight of nonpostal services.

Financial Condition

The financial wellbeing of the Postal Service has broad consequences for the U.S. economy. According to Direct Communications Group's March 2011 Mailing Industry Job Study, the Postal Service is at the core of an approximately \$1 trillion

industry that employs approximately 8 million Americans. The entire economy benefits from a healthy and viable Postal Service. Printing and mailing services allow the targeted delivery of news and commercial information. Individuals and small businesses rely on the Postal Service for timely delivery of millions of check payments, letters, and packages.

This is a critical time for the Postal Service. Due in large part to changing technologies and electronic diversion, the Postal Service suffered a net loss of \$3.9 billion through the end of the third quarter of FY 2013. These losses have occurred despite the Postal Service's efforts to increase productivity and lower its costs. The overly optimistic schedule of payments to the Retiree Health Benefits Fund is a principal reason for the multi-billion dollar losses in recent years. The Committee will be addressing issues related to the manner in which the Postal Service funds its obligations relating to pensions and healthcare in a hearing later this month.

As a consequence of the Postal Service's deteriorating financial condition, it has had to restrain its capital spending well below average historical levels. The Postal Service's most recently filed 10-K report shows that as of September 30, 2012, capital commitments (consisting of building improvements, equipment and sustaining infrastructure investments) totaled \$644 million. This marks the lowest level of Postal Service capital commitment since 1988. Similarly, the Postal Service's most recent 10-Q report shows that, as of June 30, 2013, commitments to acquire capital assets were down even further to \$535 million.

These periodic reports, required to be filed with the Commission, revealed that inadequate capital investment may be putting postal operations at risk. For example,

the Postal Service is currently operating within the confines of aging facilities, equipment, and transportation fleets and does not have funds for investing in technology improvements. This could inhibit its ability to deliver high-quality services, and meet the communication needs of the American public.

Timely, heightened awareness of situations such as these is valuable for all decision makers with responsibilities involving postal issues.

Lessons and Accomplishments

As a result of the reforms enacted in the PAEA, the Postal Service and the mailing industry are in a better position than they would have been under the governing standards of the previous postal law, the Postal Reorganization Act of 1970. The Commission has been an integral part in carrying out the requirements of the PAEA and making it an effective piece of legislation. The Commission's role was not to make policy, but rather to enforce many of the Congressional policies embodied in the statute. It also was given the responsibility to review certain types of policies developed and proposed by Postal Service management to ensure consistency with those standards established in the law.

An independent expert organization serves to uphold the integrity of the law by functioning as an unbiased arbiter to ensure that Congressional policy is being followed. The Postal Service plays the chief role in implementing postal policy, but without dedicated independent oversight, there will be justifiable concern that expedience may cause Congressional postal policies to not be as strictly enforced.

There are many innovative ideas being circulated for improving the Postal Service and its business model. In considering and debating those proposals, it is important not to lose sight of the fact that prompt, meaningful and focused legislative action is essential. The Commission is pleased that important issues raised in the Commission's first periodic report to the President and Congress on how well the PAEA is operating and our recommendations to improve the effectiveness and efficiency of postal laws have been addressed in S. 1486.

The Commission stands ready to assist stakeholders, the Postal Service, and members of this Committee as necessary to ensure the Postal Service can meet its challenges now and well into the future. When postal reform is enacted, the Commission will swiftly and responsibly implement the new law to ensure the Postal Service remains an effective part of the overall American communications network.

Thank you again for providing me the opportunity to testify today. I would be pleased to respond to any questions Committee members may have.