National Association of Letter Carriers
100 Indiana Ave. NW
Washington, DC 20001-2144
202.393.4695
www.nalc.org
Fredric V. Rolando, President

Testimony of

Fredric V. Rolando

President, National Association of Letter Carriers

to a hearing titled "Outside the Box: Reforming and Renewing the Postal Service, Part II – Promoting a 21st Century Workforce" by the

Senate Committee on Homeland Security and Governmental Affairs

September 26, 2013

My name is Fred Rolando and I am the elected President of the National Association of Letter Carriers (NALC), a union that represents nearly 200,000 active City Letter Carriers who live and work in every state and jurisdiction of the United States. Thank you for the opportunity to testify today on ways to promote a high quality postal workforce in the 21st Century. I will note that the members of my union are also very interested in the service and rate-setting issues addressed in the first part of this hearing, which was conducted on September 19, 2013.

In this written testimony, I will address the origins of the current crisis, provide our views on the bill proposed by the Chairman and Ranking Member of this committee (S. 1486, the Postal Reform Act of 2013) and address all the issues raised in both the first and second parts of your hearing. In my oral statement, I will focus more narrowly on the workforce issues you have asked me to address in your invitation. Both statements are submitted on behalf of the nearly 270,000 active and retired letter carriers who have voluntarily joined our union, including more than 90 percent of all active City Letter Carriers.

I. Introduction

As the Postmaster General said at last week's hearing, the Postal Service is in a financial crisis. We've heard this now for more than six years, and, to a casual observer, it probably sounds like nothing has changed. However, the reality is that the actual operating results of the Postal Service – the best indicators of organizational health – have improved remarkably this year. Indeed, while the Postal Service's last quarterly financial statement reported a $3.9 billion loss for the year so far, the uniquely onerous Congressional mandate to pre-fund future retiree health benefits accounted for more than 100% of the loss ($4.2 billion). In other words, the USPS has returned to operational profitability following the worst recession in 80 years.

This year we are finally seeing some promising signs in the business of the Postal Service. As the current frustratingly slow economic recovery struggles to take hold, total mail revenue actually increased by 3.6% during the quarter, compared to last year, while expenses declined. A slight loss in letter mail revenue (-0.9%) was more than offset by the 8.8% increase in shipping revenue. Nothing better illustrates the double-edged nature of the internet when it comes to the Postal Service – yes, it is displacing some letter mail (for paying bills), but advertising (Standard Mail) volume is now growing and e-commerce is driving a major surge in package deliveries. At the same time, thanks to a lot of hard work by the employees of the Postal Service who have endured massive job cuts since 2007 (200,000 jobs) and who have driven productivity to record highs, and thanks to a round of collective bargaining that has dramatically cut labor costs for the Postal Service, the Postal Service has adapted to reduced mail volume. On city letter carrier routes, for example, letter carriers are now serving an average of 616 delivery points per route per day, 25% more than they did in 2007, as the number of routes has been slashed in response to the loss of volume. But this downsizing has come at a cost of slower delivery times and reduced access to retail services. Fortunately, Congress has rejected the Postal Service's worst ideas for service cuts – the elimination of Saturday and door delivery. This committee should do so too.

I raise these points not to claim that the Postal Service is entirely out of the woods, but rather to remind the Members of this Committee that it is not 2009 anymore. The Postal Service is not in a free fall. The Great Recession is mostly over and the internet promises to create business, not just destroy it. Now is not the time to radically dismantle the Postal Service or undermine its invaluable first-mile and last-mile networks. Now is the time for intelligent reform that will promote innovation and preserve the high-quality workforce and networks that have made the Postal Service both the most popular and trusted agency in the Federal government as well as a major boon to the national economy.

Indeed, you have asked us to think outside of the box. We urge you to do the same. Congress should consider the following questions: What other national needs might the Postal Service meet with its unmatched universal networks? How else can we use post offices and letter carriers to satisfy civic and commercial needs? We have suggested promoting democracy by expanding voting by mail across the country. We have called for using letter carriers to read utility meters instead of asking households to pay for the installation of expensive smart-readers. We support helping the 40 million Americans who the FDIC says are "unbanked or under-banked." We could offer inexpensive electronic payment systems and low-cost savings accounts at post offices in rural and urban communities that lack access to private banks. Such postal savings accounts might be used to voluntarily fund a National Infrastructure Bank that has broad bipartisan support. Let's not just debate downsizing proposals, let's debate how we can find ever more useful ways to serve the American people and the American business community as we have done for more than 235 years.

II. Origins of the Crisis

The crisis facing the Postal Service is now in its seventh year. Although there are some serious technological factors at play, the scale and severity of the crisis is largely due to actions taken by Congress in the recent past. In 2006, the Congress passed and President George Bush signed the Postal Accountability and Enhancement Act (PAEA) of 2006. That legislation mandated a massive level of pre-funding of future retiree health benefits with a schedule of annual payments totaling $59 billion over the first 10 years with additional pre-funding thereafter to be amortized over the next 40 years. The PAEA also placed strict price controls on the postage rates charged for magazines, catalogues, and letter mail (so-called market-dominant products). The new law gave the Postal Service a one-time-only option to adjust postage rates in 2007 to build the cost of the new pre-funding mandate into its prices before the new price index system kicked in (in an omnibus rate proceeding before the Postal Regulatory Commission). But the onset of what turned out to be the worst recession in 80 years led the USPS to forego that option. So USPS pre-funding costs soared at a time when the economy crashed and its revenues plummeted.

Though enacted at a time when the Postal Service was earning profits, the PAEA had a disastrous effect on the Postal Service. In a kind of perfect storm, the agency's finances were devastated by the pre-funding mandate, the price controls and the Great Recession -- which decimated the housing and finance industries that generate so much mail volume. On top of all this, surging fuel costs and the loss of First Class Mail to electronic bill-paying and internet communication exacerbated the losses.

In the popular media and, unfortunately in many of the statements issued by Members of

Congress, the fiscal crisis at the Postal Service is often portrayed as a simple story of technological change. Although internet diversion is a serious problem, it has not been the main driver of USPS losses in recent years. As the table below indicates, nearly 80% of the Postal Service's $41 billion in reported losses stem from the $32 billion in pre-funding costs since 2007:

The Policy Legacy of the 2006 Postal Reform Bill (PAEA)

Pre-funding Payments to the Postal Service Retiree Health Benefit Fund (PSRHBF) vs. Reported Net Income

2007-2012*

Year	PSRHBF Expenses ($bil)	Reported Net Income ($bil)	Assets in PSRHBF ($bil)
2007	$8.358	-$5.142	$25.4
2008	$5.600	-$2.806	$31.8
2009*	$1.400	-$3.794	$34.2
2010	$5.500	-$8.505	$40.6
2011*	$0.000	-$5.067	$42.5
2012	$11.1	-$15.900	$45.0
Totals	**$31.958**	**-$41.214**	----

Prefunding expenses account for nearly 80% of reported USPS losses over the past six years since they were first imposed in 2007.

Notes: * Legislation adopted in 2009 reduced the 2009 pre-funding expense from $5.4 to $1.4 billion. Legislation adopted in 2011 deferred the $5.5 billion payment for 2011 until August 2012. USPS was unable to make the $11.1 bil. payment in 2012.

Source: Annual Reports of the Postmaster General, 2007-2012.

The negative impact of these costs continues. In the first three quarters of the current fiscal year, the Postal Service earned an operating profit of $330 million, but reported a loss of $3.9 billion after recognizing a $4.2 billion expense for pre-funding. That is, pre-funding accounts for more than 100% of the reported loss so far this year. Meanwhile, as other delivery companies were able to raise rates to handle rising gasoline prices and other overhead costs, the Postal Service was prohibited from raising rates above the very low levels of inflation experienced during the Great Recession:

Consumer Price Index:
CPI-Postage vs. CPI-Private Delivery

Year	CPI-Postage	CPI-Delivery Services (private delivery)
2007	2.5%	6.4%
2008	3.4%	14.7%
2009	4.9%	-6.2%
2010	2.8%	14.2%
2011	3.9%	11.7%
2012	3.5%	5.3%
Avg. Inc. (2007-2012)	**3.5%**	**7.7%**

Source: Bureau of Labor Statistics, Consumer Price Index.

- Postage rates for most USPS volume were capped at the general rate of inflation even though the pre-funding mandate caused costs to soar.
- Shared sacrifice requires the use of a more relevant price index: CPI for Delivery Services which tracks delivery prices in the private sector.

The pre-funding mandate, <u>which no other business or independent agency faces</u>, not only crippled the Postal Service's finances, it also led the Postal Service to pursue relentless downsizing and service cuts that drove even more mail volume out of the system. Rather than use its borrowing authority to retool and to capture new volume in the booming e-commerce industry, or to develop new products to offer through its unmatched first-mile and last-mile delivery networks, the Postal Service has used it all to cover pre-funding costs. Worse, postal management has been hunkered down in crisis mode ever since the mandate took effect, devising ever more draconian reductions in service that threaten to plunge the Service into a death spiral -- where declining volume begets service cuts, prompting further volume losses and more service cuts.

Over the past few years, the USPS has removed tens of thousands of collection boxes and has reduced the operating hours in more than 10,000 post offices, weakening its first-mile network and driving away more business. And it wants to degrade its last-mile delivery network by cutting Saturday delivery for most of its customers. Indeed, last week the Postmaster General renewed his request to reduce delivery to five days a week, after Congress blocked his earlier plan to unilaterally override the law and the will of Congress by implementing five-day service for letter mail and six-day service for packages in August. Thanks to the leaders and Members of this Committee, he did not get away with his brazenly illegal plan.

As the Committee deliberates over postal reform, we urge you to repeal or fundamentally modify the PAEA's unintentionally destructive policies on pre-funding and pricing, and to take action to prevent the Postal Service from downsizing itself into a death spiral by saving six-day delivery. These steps alone will go a long way toward saving the Postal Service. Other reforms, such as a fundamental restructuring of the Postal Service's Board of Governors, executive management and regulatory environment would also help the Service better compete for e-commerce volume and to use its unmatched networks to offer new services. Sadly, on virtually all these counts, S. 1486 fails to propose what is necessary.

III. NALC's Views on S. 1486

The National Association of Letter Carriers strongly opposes the adoption of S. 1486 as currently drafted. We do so because S. 1486 would effectively double down on the disastrous Bush administration policy to mandate massive prefunding of future retiree health benefits at the expense of service and the Postal Service's ability to innovate and grow in the future. It also provides for major downsizing measures to pay for this prefunding policy.

The relief provided by the three-year moratorium on pre-funding payments in S. 1486 is more apparent than real since the USPS has not been able to make the unaffordable payments in recent years; it won't be able to do so in the future when the pre-funding mandate is re-imposed with both normal cost and amortization payments for future retiree health benefits. The bill replaces one form of unaffordable pre-funding (the PAEA's scheduled payments) with another form of unaffordable pre-funding. Other businesses and agencies do not have to prefund retiree health at all; it is unreasonable to make the Postal Service do so. These normal and amortization payments, when combined, will certainly exceed the scheduled payments required under current law (which now average $5.6 billion annually) in 2016 and thereafter. At that point, the USPS would default and we'd be right back where we are today.

S. 1486 fails to protect the Postal Service's unique networks, which hold much promise for future growth, and instead calls for major downsizing even before the savings negotiated in the most recent round of collective bargaining have been allowed to materialize. Worse, rather than permanently addressing this crushing pre-funding burden, and from our standpoint, to add insult to injury, the bill would give USPS tools to slash postal employees' pension and health benefits by making these federal employee benefits subject to interest arbitration. This would set up a morale-killing two-tier workforce and poison the productive and innovative culture needed to strengthen USPS. Astonishingly, we were not consulted about these proposed changes to our rights as federal employees or to our collective bargaining process -- before the bill was introduced. That bargaining process has been hugely successful for more than 40 years and has produced huge benefits for the country and the Postal Service's stakeholders: Postage rates have remained among the lowest in the developed world, taxpayer subsidies have been eliminated and the quality of service has remained excellent – as both consumer surveys and public opinion surveys have confirmed.

S. 1486 would facilitate the dismantling of the Postal Service's mail processing and delivery networks, weakening both our first-mile (post office) and last-mile (delivery) capacity, in order to preserve a pre-funding policy that makes no sense. This would seriously harm the 7.5 million Americans who work in private companies that rely on the USPS. The bill would:

- destroy 80,000 full- and part-time jobs in both cities and rural areas, after a one-year delay, by eliminating Saturday mail delivery (harming millions of businesses who want it) and give the Postmaster General authority to eliminate additional days of delivery in the future;

- slash tens of thousands of additional jobs, after a two-year delay, by allowing USPS to reduce service and delivery standards and to close hundreds of mail processing facilities and thousands of post offices;

- mandate the elimination of door-to-door delivery of mail for all businesses and new households, and call for the phase out of door delivery to millions of established households – threatening at least 16,500 additional jobs; and

- impose unfair reforms to the FECA workers compensation program that would leave injured federal workers with the worst long-term injuries vulnerable to impoverishment when they reach their Social Security retirement ages.

This massive down-sizing and the bill's assault on postal employee benefits are not necessary. They are being driven by an extreme retiree health financing policy that no rational business would adopt. The Postal Service has already pre-funded decades of retiree health premiums, more than perhaps any other enterprise in America. Indeed, USPS has already set aside an estimated $49 billion for such premiums, approximately 50% of total expected costs over the next 90+ years.

As noted above, the Postal Service had been making great progress over the past year -- its package business is booming, and commercial mail is recovering as the housing market and the national economy show signs of revival. It should not be forced to forgo new vehicles and investments in new technology, new innovations and new products in order to put even more money into the Postal Service Retiree Health Benefits Fund (PSRHBF). Just as the budget sequester has thwarted a strong economic recovery, the adoption of more misguided austerity through a bad postal reform bill would make things worse, not better.

We need postal reform that will create jobs and innovation, not cut more jobs and reduce service for the American people. The 30 members of the Senate who have co-sponsored S.316, the Postal Service Protection Act of 2013, have taken the right approach. That bill would strengthen the Postal Service, promote innovation and, most importantly, resolve the retiree health and pension policies that have crippled the Postal Service in recent years. We urge the Committee to use that bill as a starting point for debate over postal reform.

There are many policy alternatives to the negative proposals in S. 1486 – measures to increase postal revenues, cut costs and cover future retiree health liabilities without massive service and job cuts. I am happy to outline a number of these alternatives here.

IV. NALC Proposals to Promote Growth and Innovation

A. Reform the Mandate to Prefund Future Retiree Health Benefits

The Postal Service is the most financially sound, supposedly failing company in America. Its pension obligations (under CSRS and FERS) are nearly fully-funded (95%), even in the face of outdated pension cost allocation methods developed by OPM in the 1970s that are grossly unfair to the Postal Service (according to independent, private sector audits that are discussed below) and the use of federal-wide actuarial assumptions that over-state likely postal liabilities.

As mentioned previously, the Postal Service has also prefunded nearly 50% of its future retiree health benefits. No other civilian agency in the executive branch has pre-funded these costs at all, and according to a recent Towers Watson survey of Fortune 1000 companies, only 38% of such private companies prefund at all and the *median* level of funding is just 37%. In the private sector, pre-funding is voluntary. Responsible companies pre-fund when they are profitable or use their surpluses in their pension funds to cover such costs, as encouraged by the tax code.

Unfortunately, the PAEA's uniquely burdensome prefunding mandate is slowly killing the Postal Service. The excessive level of pre-funding required by the PAEA has consumed all of the Postal Service's borrowing authority and has pushed the agency to the verge of insolvency. No private company would have funneled tens of billions of dollars into a retiree health fund in the midst of a deep recession. The Postal Service needs immediate and significant relief from this mandate – without it, no other reform will make a difference.

There are three major reforms that Congress should adopt to resolve the pre-funding menace to the Postal Service:

1) <u>Cover the Cost of Retiree Health with the True CSRS Postal Pension Surplus</u>. During the 112^{th} Congress, bills offered in both the House and Senate, sought to protect future taxpayers from future postal retiree health liabilities by permitting the Postal Service to use postal pension surpluses in the Civil Service Retirement and Disability Fund (CSRDF) reported by independent audits (USPS-OIG/Hay and PRC/Segal) to cover the cost of future pre-funding. Indeed, the only-bipartisan postal bill considered by the

House of Representatives (H.R. 1351) in the 112th Congress, which drew 230 co-sponsors from both parties, called for fairly and accurately measuring the Postal Service's pension surplus in the postal CSRS account of the CSRDF and transferring the surplus to the PSRHBF. That bill never got a vote in the House. In the Senate, the original bills offered by Sens. Carper and Collins (S. 1010 and S. 353) that were later combined to create S. 1789 contained similar language on the CSRS surplus. However, concerns that transferring funds from the CSRDF to the PSRHBF would present budget scoring problems led to the elimination of the provision from S. 1789 – not because the USPS receives any taxpayer money, but because the Postal Service is "off budget" under the arcane (and in this case misguided) accounting rules used by CBO and OMB. Senators Carper and Collins may have also have been swayed by a September 2011 GAO report that deemed the OPM's methods as acceptable. However, the same report acknowledged that the PRC and OIG methods were "reasonable" and that the choice of methods used for pension allocations is rightly a "policy decision" for Congress.

The decision to leave the CSRS transfer provision out of S. 1789 prevented significant relief from the pre-funding burden – which may have driven the bill's authors to target the elimination of 18% of all postal jobs and to lay the groundwork for the elimination of Saturday delivery two years from now. It is crucial to reverse these legislative decisions, and to address the problems that led to them, as we tackle postal reform in the 113th Congress. However, as I outlined in the testimony I submitted to this Committee in February, this can be done in a way that minimizes the seeming impact on the deficit that would result from a large transfer from the CSRDF to the PSRHBF. Indeed, it may not be necessary to transfer any funds at all to significantly reduce the cost of pre-funding. I will briefly summarize how this can be done (for details please refer to my February testimony):

a) Congress should instruct the Office of Personnel Management to adopt modern, private sector actuarial methods when conducting its annual valuation of the CSRS postal sub-account within the Civil Service Retirement and Disability Fund and use Accounting Standard Codification No. 715. (FASB -ASC 715, *Compensation—Retirement Benefits* from the Financial Accounting Standards Board), as recommended by the Postal Regulatory Commission's report *on Civil Service Retirement Cost and Benefit Allocation Principles* prepared by respected experts of the Segal Company (June 29, 2010).

b) In order to minimize any budget impact of mandating the use of fair actuarial methods and assumptions, Congress should repeal Section 1848(h)(2)(C) of USC Title 5, which requires the transfer of any postal pension surplus to the USPS Retiree Health Benefit Fund following valuations in 2015, 2025, 2035 and 2039.

A repeal of the transfer provision would minimize any budget score associated with a policy of accurately and fairly defining the Postal Service's pension obligations and give policy-makers up-to-date and accurate information on the Postal Service's legacy costs. It makes sense because the PSRHBF will not need the surplus funds for decades – and the surplus pension funds might never be needed if Congress enacts the reforms outlined below to properly invest the PSRHBF (reform 2) and to find ways to reduce future retiree health benefit costs (reform 3).

c) Congress should repeal the PAEA's fixed schedule of pre-funding payments and replace it with the two-tier prefunding payments called for in S. 1789 (normal cost and amortization costs), but establish a right to access the fairly calculated CSRS postal surplus in the future to cover the cost of retiree health benefits if the PSRHBF should ever be exhausted. (The 80% funding target and the immediate access to the PSRHBF to cover current retiree health premiums in S. 1486 should be retained in any new legislation.)

d) Congress should require the OPM Board of Actuaries to take the accurately measured CSRS postal surplus into account when calculating the unfunded liability for postal employee retiree health benefits, a step that would eliminate the need to make amortization payments over the next ten years or more. (In practical terms, the USPS would make a normal cost payment each year to the PSRHBF and the PSRHBF would cover the cost of current postal retiree health premiums – resulting initially in a growing PSRHBF, before taking into account the fund's earnings.) This instruction would apply the best practice of private-sector pension funds to the Postal Service. Indeed, the tax code allows companies to apply surplus pension funds to the cost of post-retirement health liabilities (see section 420 of the Internal Revenue Code).

e) In order to address false claims that might be raised by some that reforms such as those described above represent "taxpayer bailouts," Congress should adopt the Statutory PAYGO reforms proposed by the Obama administration to the Super Committee established by the 2011 Budget Control Act. Section 104 of the administration's submission called for an amendment to the PAYGO act to treat the transactions of the Postal Service Fund as "budgetary effects," thereby measuring Postal Service transactions on a unified budget basis for PAYGO purposes.

2) Invest the PSRHBF in the Thrift Savings Plan. The PSRHBF is unique in the federal government. No other independent agency has a retiree health fund. Although it differs

from so-called VEBA plans (Voluntary Employee Benefit Associations) in the private sector because retired postal employees are guaranteed retiree health benefits by the FEHBP law even if the balance in the PSRHBF goes to zero, it is very similar to such plans since its assets are dedicated to cover benefits for a specific group of people with a tie to a single employer. In this case, the PSRHBF is dedicated to pay the Postal Service's share of health insurance premiums for retired postal employees -- starting in 2017 (under current law).

Unfortunately, the PSRHBF is invested solely in low-yielding Treasury securities – and given that long-term health care costs are expected to grow faster than the interest rates payable by Treasury securities for the foreseeable future, the unfunded liability will almost certainly keep growing over time. No VEBA in the private sector would invest its assets so conservatively, especially since the annual cash requirement for the PSRHBF ($3 billion per year) is a fraction of the $49 billion in assets. The GAO has warned about the risk of investment losses if the assets of the PSRHBF were invested in securities other than Treasury securities. But with the several-decade-long investment horizon involved and the small annual cash flow needs of the PSRHBF, this risk is minimal. (A real world test of this occurred with the collapse of financial markets in 2008-2009 – huge losses incurred by the TSP's funds were recovered within a few years.)

In an ideal world, the PSRHBF would be held on the Postal Service's books and invested appropriately (in a properly diversified portfolio of stocks, bonds, real estate, etc. overseen by a professional investment manager) to minimize the PSRHBF's unfunded liability – and therefore minimize any amortization payments from the USPS in the future. Transferring the PSRHBF to the off-budget Postal Service would present massive budget scoring problems (unless the budgetary effects proposal outlined above is adopted before the postal reform bill is enacted) and the Treasury Department has traditionally opposed the investment of government trust funds in private securities.

However, NALC believes there is a way for the PSRHBF to earn higher, private sector-based returns without moving it from the OPM's books – which should actually reduce the federal deficit. The PSRHBF could be invested in the index funds offered by the Thrift Savings Plan. The Federal Retirement Thrift Investment Board already invests a pool of nearly $300 billion of federal and postal employee retirement savings in these funds – so investing the funds of the PSRHBF, which also holds assets dedicated to post-retirement benefits, would not be setting a new precedent. Towers Watson has estimated that the PSRHBF would earn more than 7% annually if it were invested in the TSP's Lifecycle 2050 Fund over the long term. That is much greater than the 3 -3.5% returns paid lately on Treasury bonds.

3) <u>Take steps to reform FEHBP to reduce the cost of retiree health costs.</u> Generally, the OPM and the FEHBP program have done a relatively good job in controlling health care costs. Indeed, the federal government's health care costs are lower than those of other large employers in the private sector, and the FEHBP program has restrained health care inflation better than employer plans in the private sector. Nevertheless, there is more that could be done to significantly reduce health care costs – which could reduce the cost of prefunding retiree health benefits.

The Postal Service has asked Congress to let it leave the FEHB Program and set up its own health care program. The postal unions, including the NALC, oppose leaving FEHBP since virtually all the savings the USPS thinks it can achieve outside of FEHBP could be achieved inside the program. We are currently engaged in very productive discussions with the Postal Service and other stakeholders to develop proposed reforms to FEHBP that would apply private sector practices and significantly reduce or even eliminate the unfunded liability for future retiree health benefits.

It is urgent that Congress take action to repeal or reform the pre-funding mandate. We cannot imagine any member of the Senate, regardless of party or ideology, who would accept such a mandate being applied to a single private sector employer in his or her state. Yet because it is applied to a federal agency, it is ignored. But the negative impact it has on the Postal Service is hurting the entire postal industry. Of the eight million workers in our industry, just over a half-million work for the USPS. The vast majority of the workers in our industry work in private companies across the country. The pre-funding mandate is not just dragging the USPS down; it's weakening an entire industry that employs workers in every state of the union.

B. Embrace Six-day Last Mile Delivery as a Core Function

The core competence and core asset of the Postal Service as an enterprise is its unmatchable, six-days-per-week, last-mile delivery network. It is a strategic asset that must be protected as we seek ways to return the Postal Service to financial health. It should not be sacrificed to maintain the disastrous pre-funding policy introduced in 2006, or even the modified pre-funding policy that is proposed by S. 1486 because degrading the Postal Service's core asset makes no business sense.

Indeed, we urge the Committee to mandate six-day delivery in Title 39 – and remove the possibility that Congressional appropriators might inappropriately seek "unified budget" savings by eliminating the six-day requirement even though the USPS receives no taxpayer money.

The Postmaster General has put forth a number of flimsy arguments in support of his five-day mail delivery proposal, even as he has failed to be fully forthcoming on the job losses his plan will entail. I fully addressed all these arguments in the testimony I submitted to the Committee's hearing in February. That testimony showed that the PMG has:

- Overstated the potential savings of going to 5-day delivery – a conclusion confirmed by the PRC – and understated the potential revenue loss (according to its own consultants and market research);
- Wrongly suggested that the move to 5-day delivery would not slow the delivery of mail, even though mail would not be collected or processed on Saturdays;
- Offered incomplete and misleading market research in support of the cut in delivery service -- failing to fully acknowledge that millions of businesses say they want and need six-day delivery;
- Failed to admit that delivering packages-only on Saturdays would drive up its parcel prices to uncompetitive levels by foregoing the benefits of shared networks that spread overhead costs across all products (parcels, letters, periodicals, etc.); and
- Misled the Congress on the number of jobs to be lost under his plan to eliminate Saturday delivery – saying it would cost 22,500 jobs when he informed the postal unions that nearly 82,000 jobs would be eliminated.

The Congress should not permit the Postal Service to commit managerial malpractice by allowing it to devalue its most important and unique asset – the ability to reach 152 million households and businesses every-day, six days a week. It makes no sense as a business strategy and it would endanger the long-term viability of the Postal Service by driving away customers.

C. Pricing and products reform

In the absence of the pre-funding mandate, the introduction of a streamlined system of rate regulation would have made a lot of sense in 2006. Replacing the costly and time-consuming system of setting postage rates through months of expensive litigation between competing sets of mailers was a laudable goal. Unfortunately, the Congress saddled the Postal Service with a huge new mandate at the same time it implemented the price cap on its rates. The cost of the pre-funding mandate was never built into the Postal Service's prices because the USPS did not conduct the one-time, final omnibus rate case called for in the PAEA. (The USPS did not want to raise rates in the midst of the recession.) Even without the crushing burden of pre-funding, the cost of mail delivery on a unit basis is bound to rise as internet diversion reduces mail volume, but the Postal Service cannot charge mailers the true cost of delivering the mail. This pricing regime is not sustainable and is contributing to the self-defeating downsizing that threatens to destroy a key part of the nation's economic infrastructure.

At a minimum, the Postal Service should be given the right to adjust its rates with a one-time proceeding before the Postal Regulatory Commission. The omnibus postage rate review and adjustment that was authorized by the PAEA, but that did not happen in 2007, should be conducted in 2013. If Congress insists on the prefunding mandate, then it is only fair that at least some of its cost should be built into the postage rates the Postal Service charges its customers. Such a one-time rate case is needed to provide reasonable balance to the huge sacrifices postal employees have made in recent years.

But in addition, the Postal Service must be able to generate greater revenues to balance the cost-cutting it will continue to pursue. No struggling enterprise can mindlessly downsize its way back to health. It must have a growth strategy and be able to generate new revenues.

There are three ways that the Postal Service can increase revenue: grow the existing business in sectors of the mailing industry that are expanding (package delivery, returns and e-commerce), better align prices to reflect costs (pricing reform), and find new uses of the Postal Service's networks that can help finance and preserve the valuable last mile delivery networks that the country depends on for commerce, communication and voting. The USPS is already doing the first and will continue to succeed so long as it does not destroy its own comparative advantage by degrading its last-mile network. But Congress must enact reforms to help USPS increase revenues in the second and third ways.

First, on pricing reform, the case can be made to eliminate the price cap altogether, as the regulator in Great Britain did in 2012. Postal operators no longer have the ability to abuse their monopolies – there is an electronic or physical alternative to every service they provide. The USPS has no market power whatsoever – if it raises rates too high, customers will leave the mail system. There is market discipline in place. On the other hand, mailers legitimately want some protection against capricious rate increases and desire predictability when making volume decisions. Despite this the USPS needs greater flexibility to set rates that will cover its costs.

This could be achieved by reforming the price index use for market-dominant products. It should be updated and must be based on an appropriate benchmark index. The Consumer Price Index for All-Items is not the correct index. The Postal Service is part of the national delivery industry, a transport-based, energy-intensive industry that has unique characteristics. Although the USPS is by definition more labor-intensive than private companies like FedEx and UPS – we deliver to 150 million addresses six days a week, not 15 million addresses five days a week – the USPS faces the same cost pressures as those companies. At a time of soaring energy costs, the rates charged by private companies that provide delivery services have increased at more than twice the rate of postage -- see the table in section II above. If the

USPS is to preserve its networks, it must be given pricing flexibility. Congress should modernize the price indexing system and replace the CPI-All Items with a different index. The mailing industry has objected to the CPI for Delivery Services as too volatile to provide the kind of predictability needed. NALC therefore recommends that Congress limit postage prices to a more stable, yet appropriate index – the Producer Price Index for Delivery and Wharehouse Services (PPI-DWS). This sector of the economy includes the Postal Service in the Bureau of Labor Statistics' classification system. As such, the PPI-DWS is an appropriate private sector benchmark. Its adoption would also help with the "budget score" of postal reform legislation.

Second, on products, the overly restrictive definition of a postal product contained in the PAEA should be liberalized. The reforms proposed in S.1789 in 2012 show the way. Opening the mail to beer and wine sales makes sense. But the range of services the Postal Service could provide is much greater and it should be given the right to find new uses for its networks. Whether its meter reading for utility companies as an alternative to expensive smart meters, or partnerships with private banks to serve Americans in rural and depressed urban areas where commercial banks have no presence, or recycling computer parts in partnership with private companies, the Postal Service needs greater commercial freedom. We believe an innovation commission as proposed by Senator Sanders makes great sense. That commission should study the possibility of using the nation's post office network as the backbone of a National Infrastructure Bank, and Congress should consider giving every American the right to vote by mail in federal elections. A more entrepreneurial Postal Service could do what the Post Office has done since it was mandated by the Constitution – evolve to meet the changing needs of the country. But to achieve a more entrepreneurial culture, the governance structure of the Postal Service needs to be reformed. I will turn to this topic next.

D. Governance reform

At a moment when the Postal Service faces the gravest crisis in its history, its Board of Governors will soon have five vacancies. The gridlock that has hampered the appointment process in general has really damaged the Postal Service in particular. When you consider that the terms of two of the five commissioners on the Postal Regulatory Commission have also expired, the appointments problem is even deeper. But what truly makes the problem a crisis is that the PAEA's guidelines for appointments to the Board have not been followed.

The PAEA amended the law to require that "at least 4 of the Governors shall be chosen solely on the basis of their demonstrated ability in managing organizations (in either the private or the public sector) that employ at least 50,000 employees. Although all of the governors who serve are honorable people, none of them meet this requirement. As our advisers at Lazard Co. reported to us, the Postal Service lacks a Board with the kind of business experience needed to create a vision for a revitalized Postal Service – nor does it have the kind of executive talent needed to execute such a vision. Instead, the Board has approved the "shrink to survive' strategy that Lazard believes is doomed to fail.

NALC calls on Congress to overhaul the governance structure of the Postal Service to give it the best chance to achieve growth and innovation. NALC will work with any leadership team that is equipped to develop a strategy for growth and to partner with postal employees and their unions to secure the long-term viability of the Postal Service.

E. Addressing the Cash Crisis: Return of the FERS Pension Surplus

The reforms we have advocated in this testimony are essential to the survival of the Postal Service well into the 21st Century. But we also face a short-term solvency crisis, even though it has been largely manufactured. (Let us not forget that there is now nearly $49 billion in the PSRHBF, which could be tapped to avert insolvency.) Sadly, the prefunding mandate, the Great Recession, and the misguided business plan of current postal management have left the Postal Service seriously short of cash and starved of needed investments. A good example of this damage is the Postal Service's recent decision to lease new vehicles rather than permanently replace its aging fleet of delivery trucks – a penny-wise, pound-foolish decision driven by the lack of investment capital and borrowing authority.

In order to prevent an economically damaging interruption of service and to give the reforms outlined above the time they need to work, Congress must also restore the liquidity the Postal Service needs to operate. Fortunately, there is a surplus in the Postal Service's FERS pension account that nobody disputes. That surplus declined from $11.4 billion in 2011 to $3.0 billion in 2012 due to a decline in the OPM's discount rate, but is expected to rise again this year as interest rates have increased. It would rise further if S. 1486's proposal to use postal-specific assumptions in the valuation process is adopted. Congress should change the law to allow for this transfer from the FERS postal account in the CSRDF to the Postal Service – to pay down its debt and make the investments it needs to serve the country and remain healthy.

V. Conclusion

Thanks again for inviting NALC to testify at this hearing. NALC is committed to working together with both parties to fashion a bi-partisan reform bill that will preserve a strong and vibrant Postal Service for decades to come. Thank you for considering our views.