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TESTIMONY OF
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BEFORE
HOUSE COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM

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Mr. Chairman, Ranking Member Cummings, and members of the Committee, thank you for your invitation to discuss the President's proposal for reform of the U.S. Postal Service.

The Administration recognizes the value the Postal Service adds to the Nation's commerce and communications, and its essential role in stitching together the vast expanse of our country and connecting America with the global economy. For years the Postal Service has ranked among the most trusted Federal agencies, and it provides reliable and affordable universal service to millions of Americans.

Unfortunately, the Great Recession exacerbated the financial pressures the Postal Service has been facing for many years, resulting in a financial gap that the Postal Service estimates at $20 billion by 2017[1] as well as large unfunded liabilities, as recently estimated by the Government Accountability Office (GAO) and Postal Service. Given these challenges, the Administration believes there is a vital need for legislative changes to help ensure the future viability of the Postal Service.

The proposals in the Administration's FY 2015 Budget seek to provide a responsible path to future viability focusing on four key principles:

- First, the proposal provides the Postal Service with near-term financial relief, largely through the restructuring of some key retiree liabilities, to avoid destabilizing or draconian near-term measures that could undermine the Postal Service's core strengths.
- Second, the proposal provides the Postal Service with flexibility to adjust to changing consumer demand, including the authority to gradually reduce mail delivery frequency to five days and to shift to centralized and curbside delivery where feasible.
- Third, the proposal gives the Postal Service flexibility to generate additional revenue over the long-term by allowing it to enter into partnership agreements with State and local governments, ship wine and beer, subject to regulations, and extend the exigent rate increases currently in effect.

[1] See, United States Postal Service Form 10-K for Fiscal Year 2013, page 8.

- Fourth, the proposal seeks to make these reforms in a manner that improves the quality of services and strengthens the institution of the Postal Service for the American people, including in rural America, while at the same time protecting American taxpayers.

Though the Administration has laid out a proposal of its own, we are heartened by the serious work of this Committee as well as the Senate in addressing these issues, and by the parallels we see between our proposal and those being considered in Congress. We look forward to working with members of Congress to enact bipartisan reform that will strengthen the Postal Service over the long-term and ensure it can continue providing the American people with trusted, reliable, and affordable service. In my testimony I will touch on the relevant factors that brought the Postal Service to the business environment it faces today and discuss the major elements of the Administration's proposal that we look forward to working with Congress and other stakeholders on this year.

Background

The Postal Service is an independent, self-funding business operation of the Federal Government. Over the last several years, it has struggled to adapt its operations and cost structure under current law to match evolving market conditions. Since 2007, as electronic communication has increased, total mail volume has declined by over 25 percent, and first-class mail volume has declined by over 28 percent. In FY 2012, the Postal Service fully exhausted its borrowing authority with Treasury and defaulted on $11.1 billion in statutory payments to prefund its retiree health benefits (RHB). In FY 2013 it defaulted on another $5.6 billion RHB payment.

To the credit of the Postal Service and its dedicated employees, it has undertaken significant administrative reforms under existing authority to reduce expenses, such as by consolidating mail processing facilities and reducing hours in some post offices to better match customer demand. It has reduced its workforce by more than 200,000 – or nearly 30 percent – over the last decade without resorting to layoffs or Reductions in Force. It has piloted means to expand its operations through same-day delivery and partnerships with the private sector, including online retailers, and has realized positive gains in certain business segments such as package delivery. These efficiency gains and innovations have helped narrow the gap between the Postal Service's revenues and expenses, and enabled it to end FY 2013 with a small positive operating cash position, although it was not able to make its $5.7 billion RHB payment owed that year. The Postal Service's financial position has also improved due to the Postal Regulatory Commission's (PRC) recent decision to increase postage rates across market-dominant products, including the exigent rate increase requested by the Postal Service resulting in a total three cent increase in first class stamps.

However, the recent improvements do not eliminate the need for comprehensive legislative reforms. The postage rate increase is time-limited to only the next two years; first-class mail volumes continue to decline; and the Postal Service's unfunded liabilities are not going away. In the near term, the Postal Service carries a $5.7 billion liability on its balance sheet for the annual RHB payment that is due in September 2014, and the Postal Service projects net accrual deficits through at least 2016. Given its financial position, the Postal Service has said that, unless legislative reforms are enacted, it will likely default on all of its remaining RHB payments owed through 2016 as a means of retaining a positive cash position to sustain operations. The Postal Service has worked to close its financial gap to the extent it can under existing authorities, but it needs additional legislative authorities.

Near-Term Financial Relief

The Administration's proposal would improve the Postal Service's near-term cash position by more than $20 billion through FY 2016, providing time for key legislative reforms and operating efficiencies to take effect. The major component of this relief is through a sensible and balanced restructuring of some key retiree liabilities. Under current law, the Postal Service is directed to make specified annual payments to prefund future RHB of current employees. Starting in 2017 under current law, it will begin paying into the RHB Fund the estimated accruing retiree health care costs of current employees (i.e., the "normal cost"), and its remaining unfunded liability (UFL) for current and future retirees will be amortized over a 40-year period.

The Administration's proposal would restructure the Postal Service's RHB payment schedule to improve its near-term cash position and long-term fiscal sustainability. In the near-term, it would defer the full $5.7 billion RHB payment in FY 2014 and half of the RHB payment amounts in fiscal years 2015 and 2016 ($2.85 billion and $2.9 billion, respectively). These deferred RHB payments would be incorporated into the 40-year amortization schedule starting in 2017. The proposal would authorize the payment of health benefit premiums for current retirees to come from existing balances in the RHB Fund rather than from its annual cash flow beginning in 2014 rather than 2017 as under current law. To ensure long-term fiscal sustainability, it would require the Postal Service to begin making annual "normal cost" prefunding contributions starting in 2014, accelerating by three years what would happen under current law in 2017.

Under the Budget's proposed restructuring of RHB payments, the Postal Service is not being relieved of its RHB responsibilities or the requirement to pay its liabilities. Instead, the Budget proposal temporarily reduces Postal Service expenses over the next three fiscal years by deferring a portion of its intra-governmental payments to provide the necessary cash flow to implement additional reforms.

The Administration also proposes to provide near-term relief by returning to the Postal Service an OPM-calculated FERS surplus from its previous payments, using "Postal-specific" demographic factors, rather than the government-wide calculation that is currently used. The Administration believes this alternative methodology is appropriate given the size of the Postal workforce (approximately 500,000 employees) and demographic characteristics of Postal annuitants relative to those among the broader Federal employee population. While we understand from OPM that doing this calculation would take approximately six months following enactment, the Budget reflects an estimate of $5 billion for this surplus,[2] which is proposed to be returned to the Postal Service over a period of two years.

[2] This estimate is based on an estimate provided by the Postal Service Office of Inspector General in December 2012 (using Postal-specific factors including investment returns, salary growth rates, cost of living adjustments granted to Postal retirees, and Postal Service demographic trends).

Flexibility to Adjust to Consumer Demand

In addition to the Postal Service's ongoing administrative initiatives to consolidate mail distribution centers and reduce staff positions through separation incentives and attrition, the Administration's proposal would provide the Postal Service with market-based authorities to realign its business and operations strategies.

First, the Administration's proposal would provide the Postal Service with authority to gradually reduce mail delivery frequency from six days to five days. This authority would give the Postal Service the flexibility to make changes to the delivery schedule based on its assessments of business conditions and consumer demand. The Postal Service has indicated that it would retain a six-day delivery standard for mail services that are profitable, such as package delivery, maintain some Saturday post office window service, and otherwise flex its operations based on demand. The Postal Service has also indicated that, to address consumer-related issues associated with the transition to five-day delivery, it would take common sense business approaches to implementing a modified delivery schedule – including continuing to deliver to P.O. Boxes six days per week and continuing to deliver Express Mail seven days per week. The President's proposal and budget estimates assume the Postal Service would implement these measures in modifying its delivery schedule.

Second, the proposal would allow the Postal Service to begin shifting to centralized and curbside delivery for businesses and new residences. This authority, as described by the Postal Service, would require conversion for business addresses receiving door delivery, though package delivery would still continue to the door. In addition, the Postal Service would develop a program of voluntary conversion to centralized or curbside delivery for some residences currently receiving door delivery, but would not mandate a minimum amount or specific target for residential conversions. The Budget estimates that the Postal Service's exercise of the authority to streamline delivery in this fashion could save the Postal Service $500 million a year when fully implemented.

Flexibility to Generate Revenue

For the Postal Service, the flexibility to adjust to consumer demand is necessary but not sufficient – it also needs the necessary tools to generate revenues that match its expenses. To that end, the Administration's proposal would increase Postal Service revenues by allowing it to enter into leasing agreements with State and local governments for the joint use of its property and services. In addition, the proposal would allow the Postal Service to ship wine and beer, subject to regulation. The Budget proposal would direct the Postal Service to examine the potential expansion of retail alternatives to post offices, which have the potential to yield further operating cost savings.

Finally, the Budget proposal would sustain greater postal revenue by permanently extending the PRC's December 2013 exigent rate increase.

Maintaining Quality and Strengthening the Institution

While the Postal Service's financial position demonstrates the need for legislative reform, the Administration believes that any reform must build on, rather than undermine, the Postal Service's core strengths. Despite difficult financial circumstances, the Postal Service delivered 158 billion packages and pieces of mail to almost 153 million delivery points in 2013. It did so in a reliable and affordable manner, while maintaining the privacy and security of the items delivered and making innovations that continue to drive growth in certain areas.

The Administration's proposal will strengthen the Postal Service's quality of service, the responsiveness of its product offerings, and bring greater security to its workforce over the long-term by giving it the near-term financial relief it needs and the authority to realign its business and operations strategy to better match market conditions. The President believes any reform to the Postal Service must have as a central principle a commitment to maintain high quality service and to continue strengthening the institution over the long-term.

Conclusion

The Administration supports strengthening the Postal Service through balanced reforms that provide it with the operational flexibility to undertake structural changes that will help put it on a sustainable trajectory. Coupled with financial relief in the near term, the Postal Service would have time to undertake these reforms without continually defaulting on its obligations or forcing draconian steps that could endanger the Postal Service over the long-term.

The Administration understands the important role that the Postal Service and its employees play in providing universal service throughout the country and supporting American businesses and jobs. We are encouraged by recent activity in both the House and Senate that focuses on these important issues. We look forward to working with the Congress and Postal stakeholders on balanced legislation that puts the Postal Service on a path towards long term sustainability.

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Brian Deese is the Deputy Director of the Office of Management and Budget. Prior to this role, Mr. Deese served as Deputy Director of the National Economic Council. In this role, Mr. Deese was charged with coordinating policy development on several Administration economic priorities including tax policy, financial regulation, housing, clean energy, manufacturing, and the automotive industry. Before he joined the Administration, in January of 2009, Mr. Deese worked as a member of the Economic Policy Working Group for the Obama-Biden transition team and was the Deputy Economic Policy Director to the Obama Campaign, where he helped craft the 2008 economic campaign platform. Prior to this Mr. Deese served as Economic Policy Director for Hillary Clinton’s presidential campaign.

Previously, Mr. Deese spent three years at the Center for American Progress where he worked as a Senior Policy Analyst for Economic Policy. His work centered on fiscal policy, international trade, and globalization. Mr. Deese has also worked at the Center for Global Development where he co-wrote the book, Delivering on Debt Relief. In addition, his writing has appeared in numerous publications including the Washington Monthly, International Herald Tribune, and the Atlantic Economic Journal. Mr. Deese is a graduate of the Yale Law School, where he received J.D., and Middlebury College.