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Congress of the United States

House of Representatives

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MEMORANDUM

April 25, 2019

To: Members, Committee on Oversight and Reform

Fr: Committee Staff

Re: Hearing on "The Financial Condition of the Postal Service"

On **Tuesday, April 30, 2019, at 10:00 a.m., in room 2154 of the Rayburn House Office Building,** the Committee will hold a hearing to review the current financial condition of the Postal Service, as well as the urgent need for reform legislation.

The Postal Service's financial condition has been deteriorating over the past decade for three primary reasons: (1) a decline in first-class mail; (2) expenses increasing at a faster rate than revenues; and (3) requirements put in place by Congress in 2006 to make billions of dollars of payments each year to pre-fund retiree health benefits.

As a result of these factors, one of the most pressing concerns for the Postal Service is its dwindling liquidity. As its expenses continue to grow more rapidly than revenues, and as it continues to default on payments required by Congress in 2006, the Postal Service faces challenges with having enough cash on hand to conduct its operations.

For all of these reasons, the Government Accountability Office (GAO) has placed the Postal Service's financial condition on its "high-risk list" since 2009.

I. UNIVERSAL MAIL SERVICE

Prior to 1970, "mail delivery in the United States was the responsibility of the U.S. Post Office Department, a Cabinet-level department in the executive branch."[1] In 1970, Congress passed the Postal Reorganization Act, which created the United States Postal Service (USPS) "as an independent establishment of the executive branch of the Government of the United States."[2]

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[1] Congressional Research Service, *Reforming the U.S. Postal Service: Background and Issues for Congress* (Aug. 25, 2016) (online at www.crs.gov/reports/pdf/R44603).

[2] Pub. L. 91-375.

The Postal Service is "the only delivery service that reaches every address in the United States." The Postal Service provides mail delivery "to nearly 159 million city, rural, Post Office Box (PO Box) and highway delivery points."[3] According to 39 U.S.C. §101(a):

> The Postal Service shall have as its basic function the obligation to provide postal services to bind the Nation together through the personal, educational, literary, and business correspondence of the people. It shall provide prompt, reliable, and efficient services to patrons in all areas and shall render postal services to all communities.

The Postal Regulatory Commission has referred to this statute as setting forth the Postal Service's "universal service obligation" (USO).[4]

The Postal Service Inspector General has described the USO as "a set of requirements put in place to ensure that all users receive a minimum level of service, regardless of the cost to the provider." However, the Inspector General has explained the "USO is not clearly defined in legislation, but instead is only broadly defined through various forms of legislation and by convention."[5]

The nature of universal service has changed over time. For example, direct delivery of mail to homes in urban areas did not begin until 1863, "followed by free home delivery for rural areas in the 1890s." In addition, although mail is now delivered to delivery points just one time per day, mail was often delivered to homes several times a day prior to 1950.[6]

The Postal Service does not receive tax dollars for operating expenses, but instead funds its operations "solely on the sale of postage, products and services." The Postal Service participates in federal pension and health plans, including the Civil Service Retirement System (CSRS), the Federal Employees Retirement System (FERS), and the Federal Employees Health Benefits Program (FEHB).[7]

II. DETERIORATING FINANCIAL CONDITION

In Fiscal Year 2018, the Postal Service's operating revenues were $70.7 billion, an increase of $1 billion, or 1.5%, from the prior year. Its operating expenses were $74.4 billion, an increase of $2.2 billion, or 2.9%, from the previous year. As a result, the Postal Service ended the fiscal year with a net loss of $3.8 billion.[8]

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[3] United States Postal Service, *Fiscal Year 2018 Annual Report to Congress* (online at https://about.usps.com/who-we-are/financials/annual-reports/fy2018.pdf).

[4] Postal Regulatory Commission, *Annual Report to the President and Congress, Fiscal Year 2018* (Jan. 10, 2019) (online at www.prc.gov/docs/108/108025/PRC%202018%20Annual%20Report-FINAL-Digital.pdf).

[5] United States Postal Service, Office of Inspector General, *Guiding Principles for a New Universal Service Obligation* (Nov. 17, 2014) (online at www.uspsoig.gov/sites/default/files/document-library-files/2015/rarc-wp-15-001_0.pdf).

[6] *Id.*

[7] United States Postal Service, *Form 10-K For the Fiscal Year Ended September 30, 2018* (online at https://about.usps.com/who-we-are/financials/10k-reports/fy2018.pdf).

[8] *Id.*

Over the past five years, the Postal Service's revenue has increased by $2.8 billion, while total expenses have increased by $1.3 billion. Over that time, operating losses have ranged from a high of $5.4 billion in 2016 to a low of $2.7 billion in 2017.[9]

A. Decline in First-Class Mail

According to GAO, the Postal Service's financial condition is deteriorating in part due to declining mail volume, particularly in first-class mail, which is the Postal Service's "most profitable product."[10] Although the Postal Service's revenues are increasing overall, particularly with package deliveries, growing revenues are not keeping pace with expenses.

In fiscal year 2018, first-class mail and marketing mail comprised 58.7% of the Postal Service's revenue and 91.5% of its total mail volume. Due to "a decline in combined volume of nearly 3.2 billion pieces" in these two mail classes, the Postal Service's "combined revenue from First-Class Mail and Marketing Mail declined by $827 million for the year ended September 30, 2018 compared to the prior year."[11]

In 2017, GAO reported that first-class mail volume is "41 percent below its peak in fiscal year 2001." GAO found that "although the rate of decline has slowed," mail volume "will continue to decline in future years with the migration to electronic alternatives resulting from technological change."[12]

In fiscal year 2018, the Postal Service's "Shipping and Packages revenue grew by 10.1% on volume growth of 6.8%, compared to the prior year." However, because of the complexities of moving packages through the mail system, the costs "are higher than the costs associated with First-Class Mail on a per-piece basis." These services comprised only 30% of the Postal Service's revenues.[13]

B. Increase in Expenses

According to GAO, another factor contributing to the Postal Service's financial condition is growing expenses, which include salaries and work hours "due in part to growth in shipping and packages, which are more labor-intensive." Compensation and benefits comprised approximately 67% of the Postal Service's total operating expenses in fiscal year 2018. These costs grew by 1.8% in fiscal year 2018 over the costs in fiscal year 2017.[14]

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[9] *Id.*

[10] Government Accountability Office, *U.S. Postal Service: Key Considerations for Restoring Fiscal Sustainability* (Feb. 7, 2017) (online at www.gao.gov/assets/690/682534.pdf).

[11] United States Postal Service, *Form 10-K For the Fiscal Year Ended September 30, 2018* (online at https://about.usps.com/who-we-are/financials/10k-reports/fy2018.pdf).

[12] Government Accountability Office, *U.S. Postal Service: Key Considerations for Restoring Fiscal Sustainability* (Feb. 7, 2017) (online at www.gao.gov/assets/690/682534.pdf).

[13] United States Postal Service, *Form 10-K For the Fiscal Year Ended September 30, 2018* (online at https://about.usps.com/who-we-are/financials/10k-reports/fy2018.pdf).

[14] Government Accountability Office, *U.S. Postal Service: Key Considerations for Restoring Fiscal Sustainability* (Feb. 7, 2017) (online at www.gao.gov/assets/690/682534.pdf).

In an effort to reduce personnel costs, the Postal Service has made deep cuts in its workforce. According to GAO, between 1999 and 2013, the Postal Service's "workforce decreased by more than 288,000."[15] The Postal Service has also negotiated with its labor unions to allow the increased use of non-career employees. In fiscal year 2018, the Postal Service's workforce totaled approximately 634,000 employees, of whom there were "approximately 497,000 career employees and approximately 137,000 non-career employees."[16]

C. New Congressional Requirements in 2006

In addition to declining first-class mail volume and growing expenses, the Postal Service has been struggling to comply with requirements put in place by Congress in 2006 to make billions of dollars of payments each year to pre-fund retiree health benefits.

Before 2006, the Postal Service maintained a "pay-as-you-go" system for retiree health benefits, under which it paid its annual share of premiums for employees participating in the FEHB.

In 2006, Congress enacted the Postal Accountability and Enhancement Act (PAEA). PAEA required the Postal Service "to start fully 'prefunding' retiree health benefits" by making "annual prefunding payments to a newly established fund to build up funds to cover USPS's share of future retiree health benefit costs" for all employees—not just those who are eligible to retire.[17] No other federal agency is required to pre-fund retiree health benefits, and it is not a normal practice in the private sector.

PAEA required the Postal Service to pay annual amounts ranging from $5.4 billion to $5.8 billion into the Retiree Health Benefits (RHB) Fund between 2007 and 2016. At the end of that ten-year period, these pre-funding payments ended, and the Postal Service was allowed to return to lower annual payments based on a 40-year amortization schedule for postal retiree health benefits and the "normal costs" of retiree health benefits for current employees.[18]

PAEA was enacted in 2016 after the Postal Service had earned "modest profits from FY2004 through FY2006" and with the expectation that the Postal Service would continue to be on relatively sound financial footing.[19]

D. Liquidity Challenges

The Postal Service ceased its annual payments to the RHB Fund in 2012 "in order to preserve liquidity and to ensure that our ability to fulfill our primary universal service mission

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[15] *Id.*

[16] United States Postal Service, *Form 10-K For the Fiscal Year Ended September 30, 2018* (online at https://about.usps.com/who-we-are/financials/10k-reports/fy2018.pdf).

[17] Government Accountability Office, *Postal Retiree Health Benefits: Unsustainable Finances Need to be Addressed* (Aug. 2018) (online at www.gao.gov/assets/700/694188.pdf).

[18] *Id.*

[19] Congressional Research Service, *The Postal Accountability and Enhancement Act: Overview and Issues for Congress* (Dec. 14, 2009) (online at https://fas.org/sgp/crs/misc/R40983.pdf).

was not placed at undue risk." The Postal Service currently owes $42.6 billion in missed payments.[20]

Including defaulted debts, the Postal Service "has lost a total of $62.4 billion since fiscal year 2007." Its "unfunded liabilities and debt have become a large financial burden, increasing from 99 percent of USPS revenues at the end of fiscal year 2007 to 169 percent of revenues at the end of fiscal year 2016," and the Postal Service's financial condition "makes it unlikely it will be able to fully make its required retiree health and pension payments in the near future."[21] As a result, "The RHB Fund is on an unsustainable path and is projected to be depleted in 12 years under the status quo."[22]

The Postal Service defaulted on these payments in order to conserve cash to pay for expenses to provide postal services. At the end of fiscal year 2018, the Postal Service reported that it "held unrestricted cash and cash equivalents of $10.1 billion," and its "average daily liquidity balance during the year ended September 30, 2018, was $11.3 billion, which represents approximately 54 days of liquidity available." However, the cash provided by operating activities "decreased by nearly $1.1 billion, or 27.6%, for the year ended September 30, 2018, compared to the previous year."[23] The Postal Service has a significant need for unrestricted cash (e.g. it has a bi-weekly payroll commitment of $1.8 billion) and it is unclear that it would have enough cash on hand to meet its commitments in the event of an economic downturn that accelerated the decline in first-class mail.

III. PREVIOUS EFFORTS TO PASS REFORM LEGISLATION

During the 115th Congress, the Committee passed by voice vote H.R. 756, the Postal Service Reform Act of 2017. This bipartisan legislation would have required Postal Service retirees who were over the age of 65, but who had not enrolled in Medicare, to enroll in Medicare. The bill also would have imposed a two percent increase in postal rates and required increased delivery of mail to centralized delivery points (cluster boxes).

According to the Congressional Budget Office, the bill would have saved taxpayers nearly $6 billion over ten years.[24] However, the legislation was never brought before the House of Representatives for consideration.

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[20] United States Postal Service, *Form 10-K For the Fiscal Year Ended September 30, 2018* (online at https://about.usps.com/who-we-are/financials/10k-reports/fy2018.pdf).

[21] Government Accountability Office, *U.S. Postal Service: Key Considerations for Restoring Fiscal Sustainability* (Feb. 7, 2017) (online at www.gao.gov/assets/690/682534.pdf).

[22] Government Accountability Office, *Postal Retiree Health Benefits: Unsustainable Finances Need to be Addressed* (Aug. 2018) (online at www.gao.gov/assets/700/694188.pdf).

[23] United States Postal Service, *Form 10-K For the Fiscal Year Ended September 30, 2018* (online at https://about.usps.com/who-we-are/financials/10k-reports/fy2018.pdf).

[24] Congressional Budget Office, *H.R. 756, Postal Service Reform Act of 2017* (June 1, 2017) (online at www.cbo.gov/system/files/115th-congress-2017-2018/costestimate/hr756.pdf).

IV. POSTAL SYSTEM TASK FORCE REPORT

On April 12, 2018, President Trump signed an executive order establishing a task force chaired by the Secretary of the Treasury and including the Directors of the Office of Management and Budget and the Office of Personnel Management. On December 4, 2018, the task force submitted its report and recommendations, including:

- Distinguishing between commercial mail and "mail and packages for which a strong social or macroeconomic rationale exists for government protection ... (essential services)";
- Giving the Postal Service more flexibility to determine the pricing of items not deemed essential services;
- Changing the current cost allocation methodology between market dominant and competitive products;
- Aligning the wages of postal workers more closely with other federal employees;
- Changing the actuarial calculation of the RHB Fund to be based on the number of employees at or near retirement age; and
- Exploring new business opportunities so the Postal Service can leverage its existing assets and business lines.[25]

V. BOARD OF GOVERNORS LACKS QUOROM

The Postal Service is supposed to be overseen by a Board of Governors with 11 members. Nine are nominated by the President and confirmed by the Senate, and they appoint the Postmaster General, who becomes a member of the Board. Then, the nine Governors and the Postmaster General appoint the Deputy Postmaster General, who also becomes a voting member of the Board.[26]

A quorum of the Board for most matters is generally "any 6 members present."[27] The Board has lacked a quorum since 2014. To prepare for that possibility, the Board voted in 2014 to establish a Temporary Emergency Committee, which has been exercising the power of the Board of Governors for more than four years.[28]

The Board currently has four members. They include the Postmaster General, the Deputy Postmaster General, and two Governors who took their seats on August 30, 2018, following their

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[25] Task Force on the United States Postal System, *United States Postal Service: A Sustainable Path Forward* (Dec. 2018) (online at https://home.treasury.gov/system/files/136/USPS_A_Sustainable_Path_Forward_report_12-04-2018.pdf).

[26] 39 U.S.C. §202.

[27] 39 U.S.C. §205.

[28] United States Postal Service, *Form 10-K For the Fiscal Year Ended September 30, 2018* (online at https://about.usps.com/who-we-are/financials/10k-reports/fy2018.pdf).

confirmation by the Senate. Two additional nominees have received a hearing in the Senate, but no vote has been scheduled. The Administration nominated a third Governor on March 11, 2019.

VI. WITNESSES

The Honorable Megan J. Brennan
Postmaster General
United States Postal Service

Margaret M. Cigno
Director, Office of Accountability and Compliance
Postal Regulatory Commission

Joel Quadracci
Chairman, President and CEO
Quad/Graphics

Fredric V. Rolando
President
National Association of Letter Carriers

Chris Edwards
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