The American Consumer Institute
Center for Citizen Research

Comments of American Consumer Institute Center for Citizen Research Regarding Docket No. ACR2018 Submitted to the United States Postal Regulatory Commission January 31, 2019

The American Consumer Institute (“ACI”) hereby submits these comments to address the actions of USPS management and discuss reforms that best meet the public interest objectives for a modern postal system.

The culmination of the USPS’ 2018 fiscal year, as detailed by the recent Annual Compliance Report (ACR), reveals a discouraging continuation of well-documented debt growth. Further, the agency’s prevailing bureaucratic inertia has proven insufficient in identifying paths towards achieving fiscal competency and orienting its rulemaking to serve the interests of consumers.

In the past, ACI has documented that the core mission of the USPS – to deliver mail – has become subordinated by delivery of its competitive services. Despite a clear mandate to provide monopoly postal services universally throughout the country, private market initiatives have steadily accelerated in the form of noticeable shifts in labor utilization, capital expenditures, and neglect for previously held priorities.

Our organization has routinely monitored the efficiency and performance quality of the USPS’ core monopoly services amidst eroding consumer confidence.[1] Previously discussed failures to realize goals in on-time delivery accelerated in 2018 as USPS fell short of objectives for all segments of First-Class Mail. Notably, the Commission, for reasons that are unclear, has abdicated enforcement responsibilities to assess appropriate penalties on the USPS, despite similarly observing the downward trend in service quality and performance.

ACI also acknowledges that the USPS’ letter mail service deterioration has been, in part, intentional due to the implementation of the "Operational Window Change" initiatives. These efforts starting in 2015 involved slashing First-Class Mail performance standards and eliminating overnight mail in order to scale back costs and apply savings towards debt reduction. During the same period, USPS established Sunday deliver services for packages only – a clear indication of its shift away from its core mission in support competitive services.

[1] “Comments of American Consumer Institute, Center for Citizen Research,” Docket No. ACR2017, submitted to the Postal Regulatory Commission, January 30, 2018.

In 2018, an analysis by the USPS Office of the Inspector General (OIG) revealed that the Postal Service had failed to deliver on much of the savings that were promised.[2] Only 5 percent of $1.6 billion projected savings were achieved in (FY) 2016 and 2017. Further details of the OIG's findings include:

- $1.61 billion in projected savings, but only $90.65 million was achieved;
- $65.7 million in projected premium pay reductions, but only $15.5 million was achieved;
- $268 million in projected transportation savings, but $0 was achieved;
- $430 million in projected cost avoidance, but only $232.8 million was verified;
- In terms of on time performance, 2.5 billion pieces of mail were delayed in 2018; and
- As for operational efficiency of mail processing, productivity was 4 percent lower in 2018 compared to the start of OWC.

In place of accruing savings as planned, the USPS has sought alternative remedies to boost its revenue – predominantly by targeting the prices for monopoly letter mail services. Since 2016, the USPS has successfully obtained approval for three rounds of rate hikes, amounting to a 17 percent increase overall (from 47 cents to 55 cents).

The arguments previously put forth by ACI in comments to the Commission on the importance of maintaining the existing rate cap mechanism are equally applicable to the latest historic rate increase that went into effect on January 28, 2019:

> "Allowing for rates to increase faster than inflation amounts to a negative productivity offset, which eliminates incentives to reduce costs and undermines the first goal of the Act. The price cap mechanism has not failed; the USPS has failed. It has failed because it cannot properly evaluate the profitability for its lines of business. This deficiency invites cost, revenue, profit and risk shifting, effectively subjecting its dominant market services to prop up competitive activities."[3]

Our organization further maintains that the described cross-subsidization is implicit within the intertwined monopoly and competitive service lines. Because USPS does not use a full cost accounting method and does not disclose sufficient financial detail for the public to measure the full extent of the shift of cost from competitive services to market dominant services, examples clearly show this is occurring in violation of the he Postal Accountability and Enhancement Act of 2006 (PAEA).[4]

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[2] "Operational Window Change Savings," United States Postal Service Office of Inspector General, October 15, 2018.
[3] "Comments of American Consumer Institute Center for Citizen Research," Docket No. RM2017-3, submitted to the Postal Regulatory Commission, February 23, 2018.
[4] 39 U.S. Code § 3633.

For example, the USPS financial results for 2018 report that packages now account for 50% of the delivery weight,[5] which means that packages (which tend to be less dense than letters) now occupy more area within delivery vehicles used in the last mile, compared to market dominant services. From this fact, we should expect the USPS' competitive services to financially support most of the capital expenditures and depreciation expenses associated with these last-mile delivery vehicles. In fact, with the additional of Sunday delivery for packages, competitive services should, in fact, be allocated a much greater share of these capital expenditures and depreciation expenses.

Yet, there is no data available to the public to demonstrate that competitive services carry their fair share of these and other expenses. By not allocating these costs appropriately, as our simple example above shows, one can reasonably conclude that the USPS is clearly and unequivocally violating the PAEA.[6]

Unlike many public utilities and state price-cap regulated local exchange telephone companies, the USPS does not have the same affiliate transaction rules in place to monitor the proper allocation of costs between competitive and monopoly services.

Moreover, despite the of the Commission's assertion that USPS has held to the requirements of the statute, the U.S. Treasury Department's Postal Task Force has affirmed the presence of an inherent subsidy, while also providing a favored remedy to deter it: "The USPS should retain the package business but establish a separate balance sheet for packages to help prevent cross-subsidization between the mail and package business units."[7] The report further recommends "that the USPS and the PRC develop a new cost allocation model with fully distributed costs to all products, services, and activities."[8]

ACI concurs with this conclusion and reemphasizes its arguments on the appropriate share of USPS's institutional costs that its competitive products must bear.[9] With respect the Commission's Order No. 4963, our organization urges use of a full cost allocation model, which would provide USPS' leadership and the Commission with the correct information to judge whether market dominant services need price increases or whether certain competitive services should be discontinued or expanded.

In addition to the stated adjustment needs in pricing and cost allocation, the Treasury Report further cites additional matters the Commission can explore to help revitalize the Postal Service's business model, including employing rigorous cost controls and leveraging the USPS

[5] "FY2018 Annual Report to Congress," USPS, December 12, 2018, p. 9, http://about.usps.com/who-we-are/financials/annual-reports/fy2018.pdf.
[6] 39 U.S. Code § 3633.
[7] "United States Postal Service: A Sustainable Path Forward," United States Treasury, December 2018, p. 55, https://home.treasury.gov/system/files/136/USPS_A_Sustainable_Path_Forward_report_12-04-2018.pdf.
[8] Ibid.
[9] "Comments of American Consumer Institute Center for Citizen Research," Docket No. RM2017-1, submitted to the Postal Regulatory Commission, April 16, 2018.

monopoly mailbox access to generate added revenue. Similarly, a recent study provides a path for a $3.3 billion reduction in postal expenditures.[10]

As we pointed out before, the Commission's latest formula-based approach uses two components that are not relevant in explaining the variation in the appropriate share of institutional costs, as well as excluding more pertinent variables. Specifically, the formula is focused on deterring the USPS from setting prices that are too high, while the PAEA is focused on prohibiting the USPS from setting prices that are too low. As such, the formula does not incorporate any component or factor that identifies institutional costs uniquely associated with competitive products, as required by the PAEA – specifically, "the degree to which any costs are uniquely or disproportionately associated with competitive products."

Despite the USPS' adherence to the formula's mechanisms, the agency's service costs still substantially outpace total service revenues. Such outcomes are not acceptable for any federally-affiliated institution.

Given the Postal Service's dire fiscal position and clear deterioration of core services – from both a performance and pricing standpoint – all options for reform must be on the table for consideration.

Respectfully submitted,

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[10] "postal Perils and Promise: A Primer on Reform," Taxpayers Protection Alliance, January 2019, https://www.protectingtaxpayers.org/useruploads/files/TPA+Postal+report.pdf.