

Refinancing USPS Retiree Health Benefits



The battle to refinance retiree health benefits is in full swing on Capitol Hill. H.R. 22 has been introduced in the House and, to date, there is no Senate companion. There was some talk of trying to get this into the stimulus package, but that just didn't work out for a variety of reasons. Consequently, we are looking first for appropriate champions for the issue in the Senate as well as appropriate vehicles in both houses.

As you know, we are seeking to have the Postal Service relieved from \$2.3 billion of its annual \$8 billion obligation to fund and prefund retiree health benefits for the next eight years. This would leave the Postal Service with \$5+ billion of annual payments. About half of this remaining annual payment would go toward funding current retiree health benefits, while the other half would continue to prefund your future retiree health benefits. All payments would go into an existing trust fund that was created for this purpose. That fund has about \$32 billion in it today. Payments for current retiree health benefits would come from the fund in the future.

One of the problems we face, however, is GAO's belief that the Postal Service should only get relief from making the full \$8 billion per year payment for two years—until the recession is over. Others, particularly in the Senate, share that view. Should the recession last longer than that—God help us—GAO would probably be amenable to stretching the "relief" for another year. Other proponents of this point of view assume that all the volume the Postal Service is losing now is not coming back. They also reject the Postal Service's view that most (but not all) of the volume that is being lost because of the recession will come back after the recession.

Thus, proponents of this point of view assume that the post-recession Postal Service will have to be significantly smaller than it is now, and they want the Postal Service to reduce its processing network now. They are also not happy that the Postal Service is not using its pricing flexibility to get through this crisis more easily. Consequently, those holding this point of view feel that it is necessary to hold back from providing "full relief" for the Postal Service until it gets its act together. By doing so, they hope to maintain leverage over the Postal Service so that it can be forced—much like Detroit—to do what it needs to do and has not done.

Two things need to be said about this point of view:

Volume Loss During the Recession

First, in terms of volume loss, the assumption that the volume being lost today will not return is not realistic. While it is possible that the volume lost will not return, it is not probable. The significant volume loss today is in First Class and Standard Mail. Most of First Class and almost all of Standard should come back. Of course, if the Postal Service would only use the pricing flexi-

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bility in the market-dominant side of the house that it has now—something it has not done to date—Standard mail volumes could not only come back, but also could come back well above prior levels. Intelligent use of pricing flexibility could also grow other categories of advertising mail. Let's look at some details. In terms of First Class, the volume loss is in several categories—bill payment, bill presentment and advertising mail.

In terms of bill payment, this is the only area in which the volume loss is permanent. Paying online is simple, safe and dependable, and over time it will beat out the Postal Service. That is what common sense would indicate, and that common sense point of view is substantiated by mailers' experience and research. However, some research indicates the growth of electronic bill payment is slowing significantly. In any case, all this is happening fairly slowly and there isn't really an indication that the recession is quickening the pace.

In terms of bill presentment, it is not at all clear that over time bill presentment will move to electronic form. Companies are finding that people generally do not want to get their bills via e-mail, even though they are willing to pay their bills online. As a Pitney Bowes study found out several years ago, "participants were asked how they prefer to receive financial-type mail such as bills, bank statements and financial reports. The overwhelming majority (86 percent) indicated that they prefer to receive these reports via regular mail."

This dichotomy between bill payment and bill presentment turns on the differences in the technology. Bill payment is done online through secure Web pages and it always works. Bill presentment is done through e-mail, and e-mail delivery doesn't always work. E-mail is nowhere near as reliable on postal delivery, and is not going to be. A fair amount of e-mails just never go through. Moreover, the clutter in the electronic inbox is increasing and, unlike the clutter in the mailbox, people simply do not want to waste time sorting through inbox clutter. Adding to this is the fact that all sorts of anti-spam and anti-junk e-mail filters are becoming more adept at keeping e-mails out of your inbox.

Moreover, research has shown that people want to keep their paper statements as records. Even when people do receive bills electronically, Pitney Bowes research shows that two-thirds print their statements out and keep them for more than a year in files. That speaks well to the lasting value of paper as a storage and reference medium. It is also probably the reason that large numbers of consumers that do view bills online continue to receive them in the mail. Given all

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this, it is reasonable to assume bill presentment is going to remain in the postal system for a long time.

In terms of advertising mail, it used to be that somewhere around 18 percent of First Class Mail was advertising mail. That number has decreased significantly in the last several years. I believe that much of it will not come back, for companies have found that the current cost of First Class—even at an automated letter level—simply does not justify the higher lift one would receive from using First Class Mail.

But, unlike bill payments, there are other postal options that are worth less to the Postal Service than First Class but more than Standard mail that could be created for advertising mailers that would provide the positive cost/life ratio that they seek. The Postal Service just has to go try and find out what they are, and use its pricing flexibility to do so.

In terms of Standard mail volumes, I don't see why all the volume being lost will not come back once the economy is healthy. Advertising mail is a very powerful advertising channel and it is standing up well in the test of time against electronic advertising. That is not going to change.

Pricing Flexibility

In terms of the pricing flexibility, I agree with the point of view that laments the fact that the Postal Service has never even tried to use its pricing flexibility in the market-dominant area. When one plays to win, sometimes one wins and sometimes one loses. But if one never tries—if one *never plays* to win—one never wins. I don't want to get too much on a soapbox here, but one thing in life that really irritates me is when I see someone who doesn't even try. That is what the Postal Service has done, or not done. The Postal Service has not even tried—much less succeeded—to use its pricing flexibility in the market-dominant area since postal reform became law.

If I were the congressmen and senators who spent the better part of a decade of their legislative lives fighting to give the Postal Service this freedom, I would be mightily upset at the Postal Service and its cavalier dismissal of the pricing flexibility tool that I

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gave it. The Postal Service really needs to get its house in order in this area.

Now, to be fair about this, I think the Postal Service believes that, despite the passage of the Postal Accountability and Enhancement Act, the Postal Regulatory Commission (PRC), particularly the staff, does not trust the Postal Service to wisely use its pricing flexibility and that the PRC has done everything it can to block any effort by the Postal Service to use its pricing flexibility on the market-dominant side. I think the Postal Service has a point.

The commission and its staff, particularly in the NSA area, have set up regulatory tests and models that are almost impossible to pass and are based upon theoretical economics rather than business reality. Instead of acting like a business, the commission's staff wants to channel the Postal Service to act as theoretical economists think businesses should (but never do) act. That is to say, the PRC wants no risk-taking behavior at all and bases its view of the Postal Service's behavior on economic models that mechanically use formulas to predict possible behavior, based solely on past performance. Such models do not take into account change and behavioral modification that proper economic incentives—and NSAs—create. The truth of the matter is that incentive regulation takes a much different technical mindset than rate-of-return (or cost of service) regulation, and the PRC mindset has not made

that change. It needs to do so.

Someone on the Hill told me a great story that is relevant here. AT&T was once asked what was the most difficult thing it had to do after AT&T was deregulated. Its answer was "dealing with the economists." It found that it had to fire all of its rate-of-return economists and replace them with incentive economists because the mindset of the rate-of-return economists was simply incapable of operating in an incentive environment. While I don't think that is quite necessary at the PRC, I do think mindset needs to change.

Two Years Versus Eight

Returning to the refinancing issue, the Senate seems willing to give the Postal Service relief, but not beyond two years. I look at this as one might view having a mortgage with a huge balloon payment due in two years. Huge balloon payments on mortgages are seldom paid and lenders seldom, if ever, expect them to be paid. Rather, they are something to be refinanced.

GAO and the Senate need to realize this and understand what position they would put the Postal Service in by creating a \$2+ billion balloon payment for the Postal Service after two years.

The Postal Service has enough to do to over the next eight years to meet the very real challenges that it will have to face. It doesn't need to face a huge balloon payment in addition to those. •

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