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Delaying the inevitable: Political stalemate and the U.S. Postal Service

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THE CHANGING NATURE OF THE MARKETPLACE

The U.S. Postal Service (USPS) was created more than 200 years ago and may be the country's oldest continuously operating business. Similar to the candlemakers and the buggywhip-makers that ran prosperous businesses back when Ben Franklin was the first Postmaster General, the core business of the post office, delivering first class mail, is fading away.

To understand this crisis of obsolescence, all you really need to do is to ask yourself: When was the last time you got an actual letter, addressed to you in the mail with a stamp on it? Even Christmas cards and wedding invitations are going electronic. The Internet began having an effect on mail almost as soon as Americans were online. Between 1998 and 2002, the number of first-class single piece letters dropped from 54.3 billion pieces to 49.3 billion pieces.[1] And the trends have continued. As the main business of the post office withers away, the result is increasing debt. In recent years, even when revenue grows, so do losses.

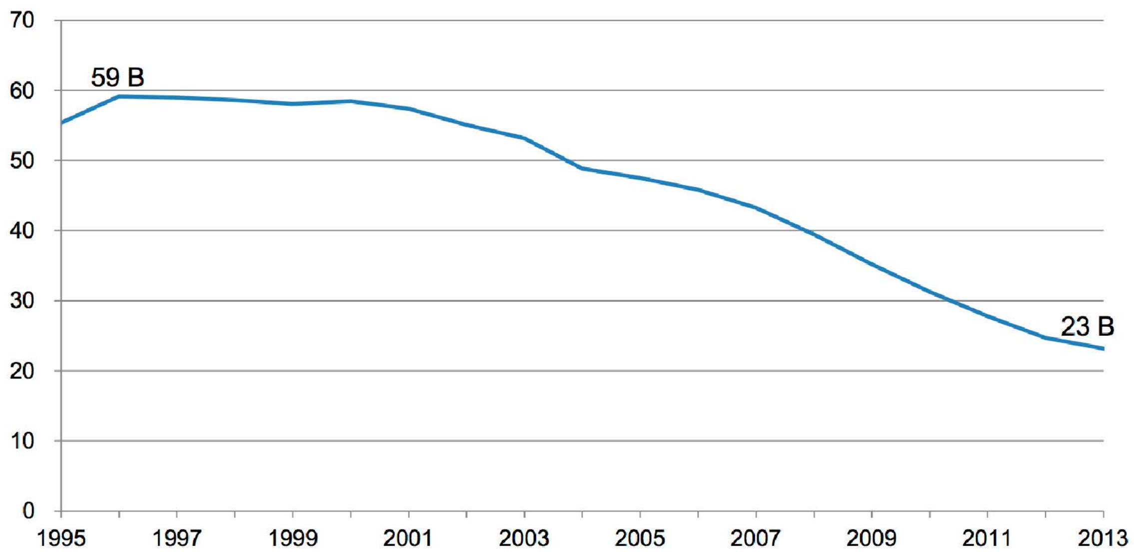
To understand the magnitude of the problem, have a look at Figure 1 taken from the 2015 report of the Post Office Inspector General.[2] It shows a dramatic decline in the volume of first class single-piece mail from 45.9 billion pieces in 2005 to 22.6 billion pieces in 2013. Not only do people use email or texting where they once used letters or greeting cards, but the move to electronic banking has meant that people stopped using first class mail to receive and to pay their bills.

1 President's Commission on the United States Postal Service, "Embracing the Future: Making the Tough Choices to Preserve Universal Mail Service," July 31, 2003, page 6. (http://govinfo.library.unt.edu/usps/offices/domestic-finance/usps/pdf/freport.pdf)

2 Office of the Inspector General, United States Postal Service Report No. RARC-WP-15-010, "Decline in U.S. Postal Service Mail Volume Vary Widely across the United States," April 27, 2015. (https://www.uspsoig.gov/sites/default/files/document-library-files/2015/rarc-wp-15-010.pdf)

Figure 1: Steep decline in originating first-class mail single-piece volume

First Class Mail Single-Piece volume dropped from a peak volume of 59 billion pieces in FY 1996 to 23 billion pieces in 2013 — a precipitous decline of 36 billion pieces, or 61 percent.



Source: OIG Analysis of U.S. Postal Service ODIS-RPW data.

While there are variations by geographic region and age, mail volume decline is happening at similar rates across many demographics. Decline in postal mail use is similar regardless of income, education and age as Figure 2 shows. The last one is especially significant since older people are assumed to use technology less. And although older Americans do send more mail than younger Americans, the decline in mail usage among the elderly is similar to other age groups.[3]

While first class mail has been in decline, package volume has increased and for the same reason – the internet. Shopping online has become such a big business that in recent years "Cyber Monday" the Monday after Thanksgiving, has come to rival "Black Friday" the shopping day after Thanksgiving, as one of the biggest shopping days of the year. Driven by giants like Amazon.com, the number of digital shoppers has gone from 172.3 million in 2010 to 201.7 million in 2015 and is expected to keep on growing (see Figure 3).[4]

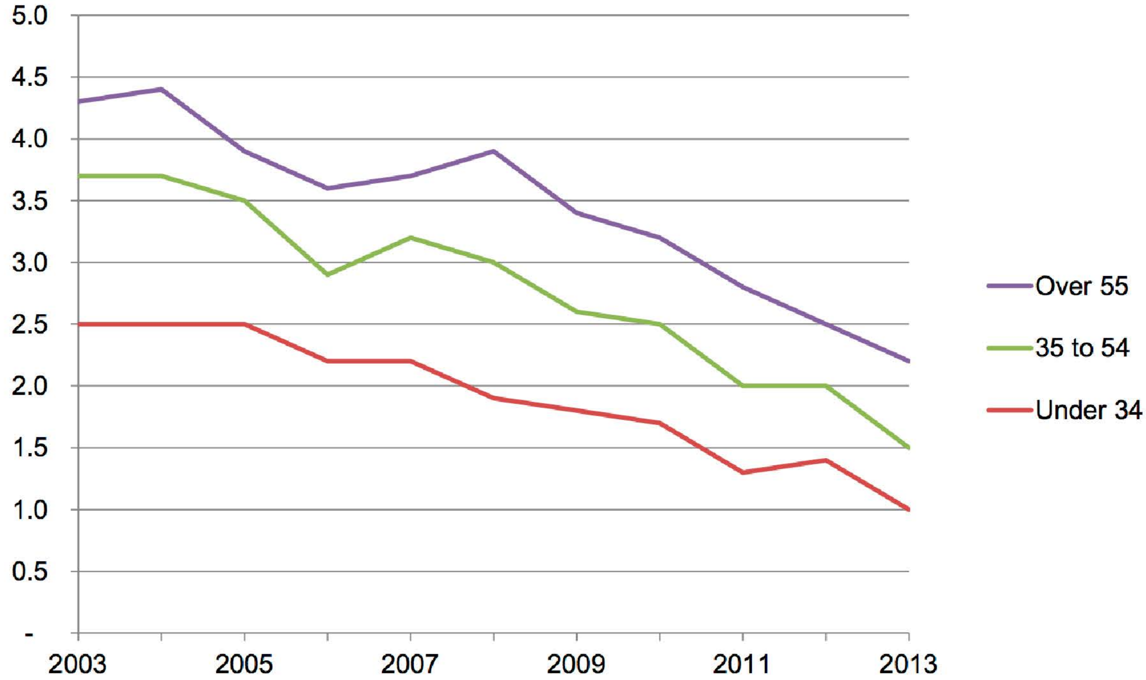
All these online purchases need to be delivered. This past Christmas the USPS teamed up with Amazon to deliver packages on Sunday during the Christmas season – a move that put them directly into competition with United Parcel Service, Fed Ex and other private delivery services, although the partnership with Amazon had been tested

3 Ibid.

4 See Statista, "Number of Digital Shoppers in the United States," 2015. (http://www.statista.com/statistics/183755/number-of-us-internet-shoppers-since-2009/)

Figure 2: Age does not explain mail volume decline

Older Americans continue to send more mail; however, volume is declining at a similar rate across all age groups.



Source: The Household Diary Study, Mail Use & Attitudes, U.S. Postal Service, 2003-2013.

Figure 3: Number of digital shoppers in the United States from 2010 to 2018 (in millions)

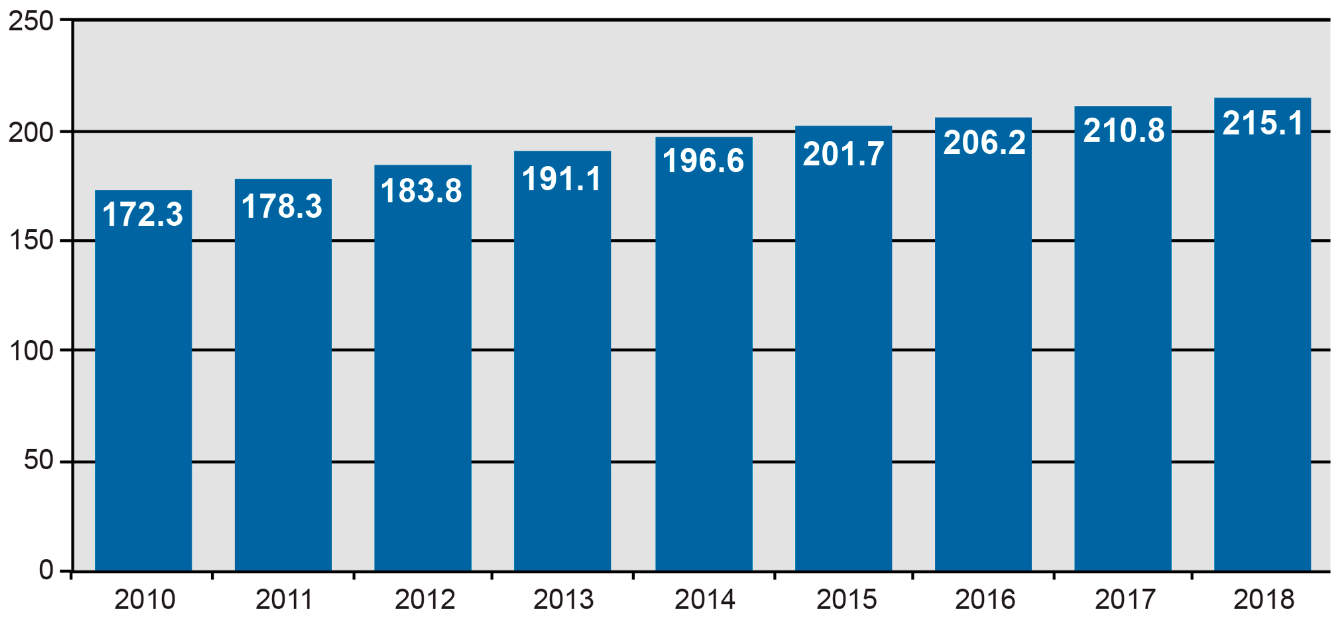
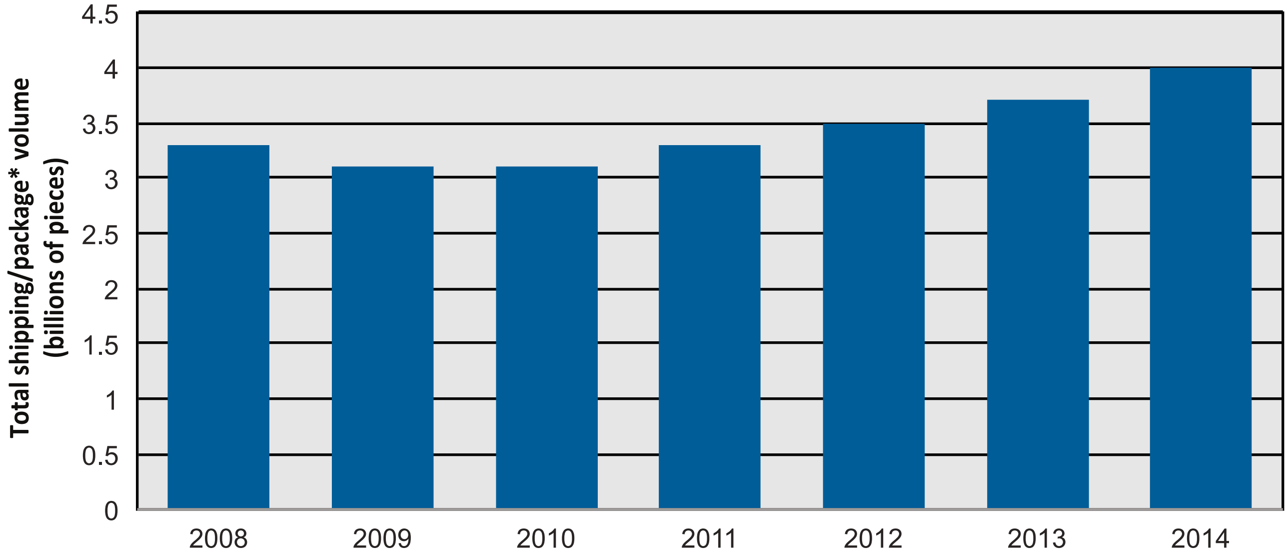


Figure 4: USPS growth in parcel delivery



*Includes Priority Mail, Priority Mail Express, First-Class Packages, Package Services, Parcel Return Service and Parcel Select.

in various cities beginning in 2013.[5] And when USPS announced rate changes for its Priority Mail Product back in the summer of 2014, *Forbes* was quick to point out that "Rate Reductions May Post a Threat to UPS and FedEx's Market Share."[6] To the consternation of companies in the package delivery business, the USPS is becoming a big player in the growing market for parcel delivery – total shipping and package volume has increased steadily from 2008 to 2014 as shown above in Figure 4.[7]

STALEMATE

Nonetheless, the USPS continues to lose money (see Figure 5). In 2014, the USPS lost more than $5 billion – its eighth consecutive annual net loss in a row. These losses occurred in spite of an uptick in operating revenue and in spite of a 9 percent increase in the shipping and packaging business. And given the profound changes in the market, no one thinks that the USPS's problems are going to be over anytime soon. Many believe that the prefunding requirement for retiree health benefits accounts for all of the Postal Service's financial problems. Although the pre-funding requirement does account for a large share of net losses, retiree health benefits caused $22,417 million in expenses out of a total net loss of $5.5 billion in fiscal year 2014.[8]

But the political system is stuck and unable to do anything about it. One of the few exceptions to the benign neglect shown by most of Congress is Senator Tom Carper (D-Del.) who, in 2014, drafted a comprehensive bill along with Senator Tom Coburn (R-Okla.) that went nowhere. Senator Carper summed up the situation last December as follows: "Because of Congress' inability to come to a consensus on post reform legislation this year, the Postal Service's fate

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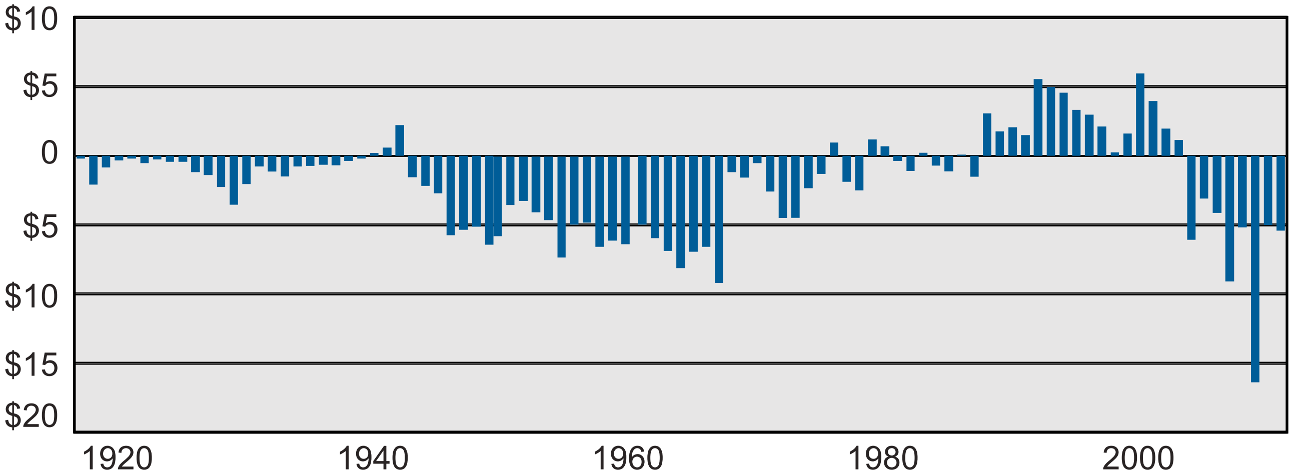
5 Tricia Duryee, "Amazon Sunday delivery: Key facts to know as USPS rols out service nationally," *GeekWire*, July 16, 2014. (http://time.com/3590662/usps-amazon-holiday-delivery-sunday-christmas/)

6 Trefis Team, "USPS' Rate Reductions May Post a Threat to UPS and FedEx's Market Share," *Forbes,* August 21, 2014. (http://www.forbes.com/sites/greatspeculations/2014/08/21/usps-rate-reductions-may-pose-a-threat-to-ups-and-fedexs-market-share/)

7 See United States Postal Service, A Decade of Facts and Figures, as of February 17, 2015. (https://about.usps.com/who-we-are/postal-facts/decade-of-facts-and-figures.htm)

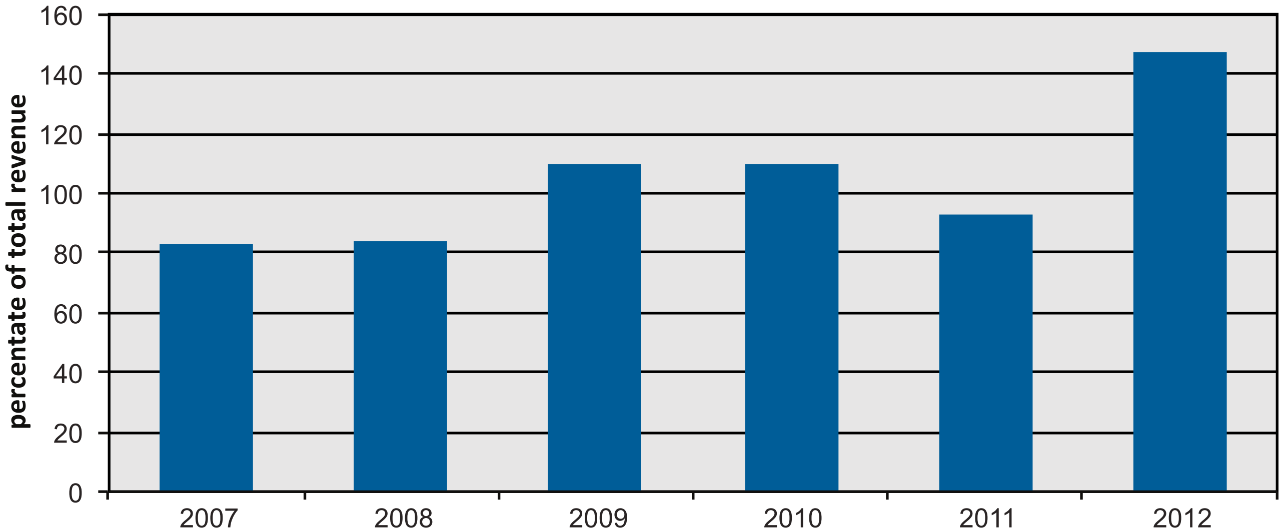
8 Postal Regulatory Commission, "Financial Analysis of United States Postal Service Financial Results and 10-K Statement," April 1, 2015. (http://www.prc.gov/sites/default/files/reports/Financial%20Report%202014.pdf)

Figure 5: USPS real net income, billions (2014 dollars)



Source: Robert J. Shapiro, “The Basis and Extent of the Monopoly Rights and Subsidies Claimed by the United States Postal Service,” March 2015 (Washington D.C.: Sonecon).

Figure 6: Selected USPS liabilities and unfunded pension and health benefit liabilities as a percentage of USPS revenues



Source: USPS

continues to twist in the wind.”[9] In 2013, a reform bill introduced by Congressman Darrell Issa (R-Calif.) also went nowhere. In 2011, another Issa bill and a bill introduced by Senator John MCCain (R-Ariz.) failed to come out of a committee as did a host of other proposed legislation. But repeated failure to take up the problem of the post office has not dampened Senator Carper’s persistence. In the fall of 2015 he introduced another postal reform bill –the 2015 Improving Postal Operations, Service and Transparency (iPost) Act. This one lacked co-sponsors. It addressed the health care funding problems but blocked downsizing in favor of even more studies.

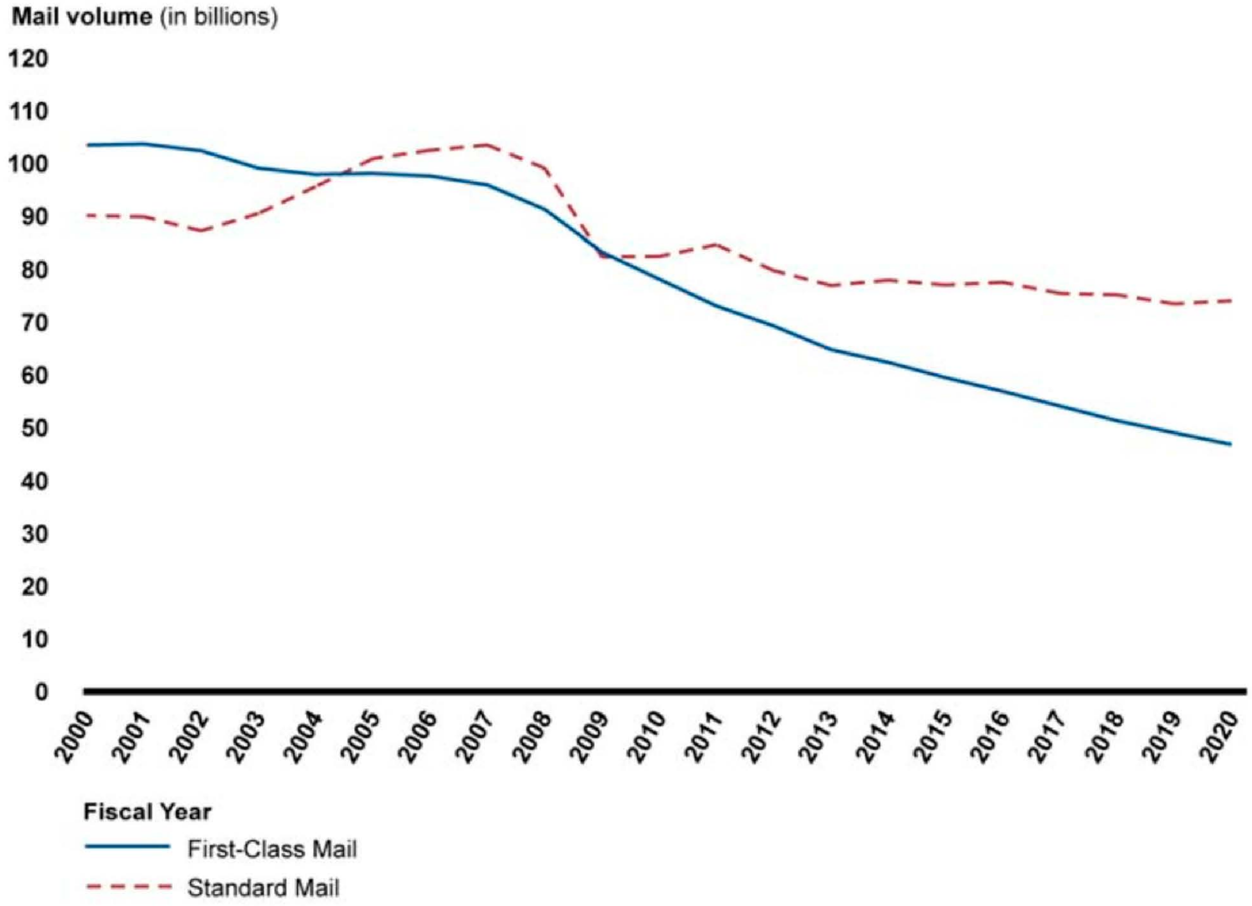
9 See U.S. Senate Committee on Homeland Security & Government Affairs press release, “Senator Carper: Reforming the Postal Service Should be a Top Priority for the 114th Congress,” December 22, 2014. (http://www.hsgac.senate.gov/media/majority-media/senator-carper-reforming-the-postal-service-should-be-a-top-priority-for-the-114th-congress)

The stalemate over the fate of the USPS has many causes. Some powerful groups, including the postal workers unions, insist that the requirement that the agency pre-pay the cost of its health benefits for current retirees is the biggest problem faced by USPS and that without it there would be no need for further action. Some background is in order: In the late 1980s, Congress started to get concerned about the fact that the Post Office would not be able afford to pay retirees' health benefits. And so, in 2006, Congress mandated that USPS pre-pay into a retiree health benefit fund. The required payments have increased each year – as mail volume and the revenue it brings has simultaneously decreased. In 2011, the USPS defaulted on payments of $5.5 billion and it has defaulted every year since then. It is expected to default in 2015 and 2016 as well. Even more important, in early 2013, USPS reached its $15 billion borrowing limit from the U.S. Department of the Treasury.

The enormous liabilities owed by USPS to their retirees are illustrated in a report from a GAO titled, (appropriately) "U.S. Post Service: Urgent Action Needed to Achieve Financial Sustainability." It includes Figure 6 that illustrates just how difficult it is for the Post office to keep its head above water. Unfunded liabilities increased from 83 percent of revenues in 2007 to 147 percent of revenues in 2012.[10] And they aren't going away.

Meanwhile, the volume of first class and standard mail volume is projected to continue its steep decline as Figure 7 illustrates.

Figure 7: Actual and projected first-class mail and standard mail volume, fiscal years 2000 through 2020



Source: USPS.

Nonetheless, while nearly every year in the past decade has brought losses, the political system continues to be stuck. The Obama administration included a provision in its most recent budgets that would allow for a rate increase, a restructuring of the pre-funding requirement, and the abolition of Saturday delivery. And yet, once again, in January 2015, Congress adjourned without passing reform.

When the USPS has taken it upon itself to cut costs, they've been blocked. Consider one such action: In the summer of 2014, Post Master General Patrick Donohoe planned to close 82 unnecessary mail-processing facilities in order to save money. Instead of congratulating him for taking steps to become more efficient, 50 Senators sent a letter to him seeking to disrupt the plans. To no one's surprise, in May 2015 the USPS announced it would not resume the second phase of its "network rationalization" plan and close facilities. A USPS spokesperson said the plan to defer closings was made "to ensure that the Postal Service will continue to provide prompt, reliable, and predictable service consistent with the published service standards."[11] Similar interventions have happened over the years with regard to other cost-saving measures – especially the proposal to stop Saturday delivery.

THE BIG QUESTIONS

The big issue is what comes next. If the USPS were a purely private entity, the changing shape of the marketplace wouldn't necessarily pose an existential threat. They could shrink the infrastructure created to deliver first class mail and increase their capacity to deliver parcels – a logical adaptation to the changes that have come about as Americans have moved from paper to the Internet.

But the USPS is not a private entity. It is an unusual governmental body that exists under a number of laws and requirements that constrain normal business judgements. On the other hand, it does not receive appropriations and is expected to make money. The USPS is actually in the Constitution of the United States. Article I Section 8 gives Congress the authority to "establish post offices and post roads." The Founding Fathers, including Ben Franklin, the nation's first Postmaster General, viewed a postal network as critical to nationhood. It's mission? "To bind the Nation together through the personal, educational, literary, and business correspondence of the people."[12]

The result is known as "the universal service obligation" – the obligation to deliver first-class mail to every citizen wherever they are, all the time, and at a fair and equitable rate. To fulfill it, Congress has given the Post Office two monopolies: one is over the delivery of letters and the other is exclusive rights to citizens' mailboxes. But the "universal service obligation" also means that the USPS has restrictions on it that impact everything from labor costs to the ability to contract out. It also is required by law to provide service six days a week and to continue rural delivery of mail at certain levels. It cannot close post offices or processing centers easily, and it cannot change its pricing quickly or easily.

Unlike a private sector business that would adjust to the changing market, the USPS cannot, for instance, move to five-day delivery – the most obvious market adjustment – without a recurring act of Congress. Congress continually blocks USPS from cutting Saturday delivery by attaching a rider on a spending bill. The six-day delivery rider was first introduced in 1983 and has been included in every annual appropriations bill since.[13]

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11 Eric Katz, "USPS Suspends Remaining Facility Closures Scheduled for 2015," *Government Executive*, May 26, 2015. (http://www.govexec.com/management/2015/05/usps-suspends-remaining-facility-closures-scheduled-2015/113743/)

12 39 U.S.C. 101 (a)

13 Eric Katz, "GAO to USPS: You Still Have to Deliver Mail Six Days a Week," *Government Executive*, March 21, 2013. (http://www.govexec.com/oversight/2013/03/gao-usps-you-still-have-deliver-mail-six-days-week/62020/)

Thus, the USPS is a highly regulated government entity, prohibited by its mission and by the laws defining its mission, from acting to adjust to the dramatic changes in its environment. On the other hand, the USPS has gone into areas of the economy in which it competes with the private sector. Some argue that the Post Office should get into more new lines of business – from delivering groceries to teaming up with retailers to deliver packages on the same day they are ordered. But this raises the thorny question of subsidies. To what extent do the U.S. government subsidies for the USPS create an unfair playing field for all those who are already in the private market place delivering everything from groceries to clothing?

The monopoly the USPS enjoys in the areas of mail delivery and mailboxes, as well as a host of other advantages, including tax subsidies, preferential interest rates on borrowing, and extensive real estate, means that when the USPS competes with the private sector, it enjoys an unfair subsidy. According to a recent study, these monopoly rights and privileges add up to an estimated $18 billion dollars in special annual savings and subsidies for the postal system.[14]

The result can be seen in market distortions on both ends. As the Federal Trade Commission noted: "From a market-wide perspective, the federally-imposed restrictions that impose economic burdens on the USPS and the implicit subsidies that provide the USPS an economic advantage should be viewed as two distortions that compound each other and negatively affect the provision of competitive mail products. The USPS's burdens cause it to utilize more resources than necessary to produce competitive products. Its implicit subsidies partially mask these inefficiencies from consumers, creating incentives for consumers to purchase more competitive mail products from the USPS than they otherwise would if the products were priced based on their full costs."[15]

This sums up the paradox of reform facing the USPS: One way then to begin to get out of the quagmire is to understand the complex legal knots and to sort them into a framework. Fortunately, among the legal complexities is a very useful distinction. The law formally divides USPS into two categories: "market dominant" and "competitive" products. The two reform discussions should be separated into these categories for one simple reason – the first is a monopoly, while the second is not. Eventually, the biggest reform of all might be to completely separate the two functions. Following are a list of questions that Congress will have to grapple with when determining how to best reform this troubled agency.

MARKET-DOMINANT ISSUES

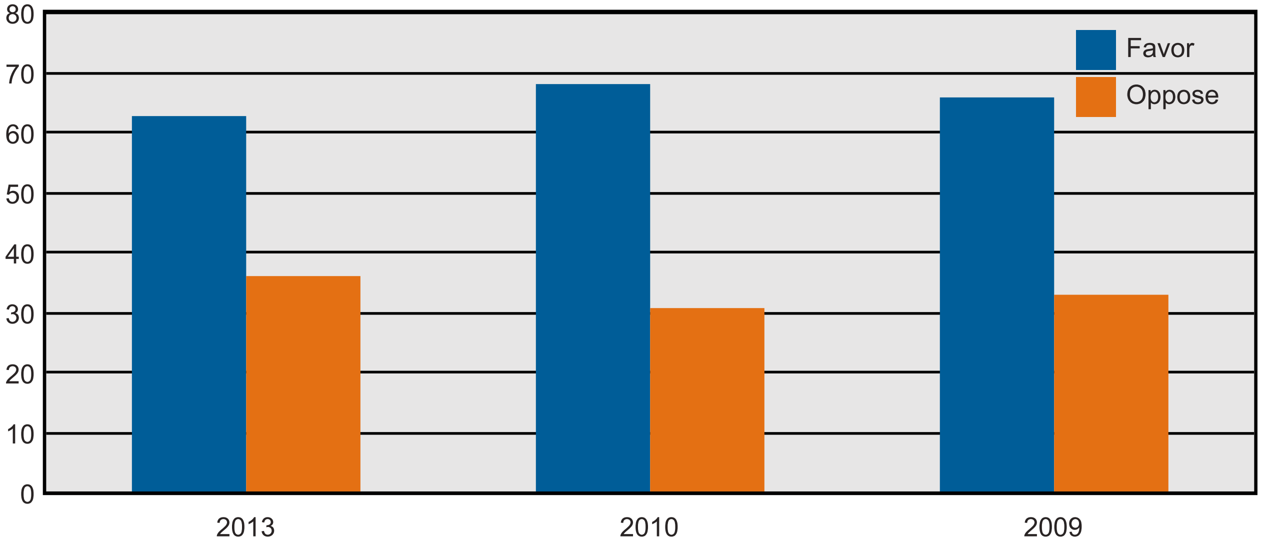
1. **Does the federal government still want to be committed to universal service?** Most people would answer yes to that question, especially those who live in rural or remote places where the true, unsubsidized cost of getting mail would be more expensive. Furthermore, the universal service mandate has been baked into the American value-system. Note how important it has been to successive information age presidents that broadband internet service be widely available to rural areas. The importance of the concept of "binding the nation together" seems to be as strong in the information age as it was in the beginning of the republic.

2. **If the political decision is to keep universal service, then the question must be asked: What is universal service in the information age?** This debate would take into account the reality of disappearing first-class

14 Robert J. Shapiro, "The Basis and Extent of the Monopoly Rights and Subsidies Claimed by the United States Postal Service," March 2015 (Washington D.C.: Sonecon) page 3. (http://www.sonecon.com/docs/studies/Study_of_USPS_Subsidies-Shapiro-Sonecon-March_25_2015.pdf)

15 Federal Trade Commission, "Accounting for Laws that Apply Differently to the United States Postal Service and Its Private Competitors," December 2007, page 9. (https://www.ftc.gov/reports/accounting-laws-apply-differently-united-states-postal-service-its-private-competitors) mail. The simple answer to this question would be to eliminate Saturday delivery. Interestingly enough, the public doesn't care. Gallup has been asking this question since 2009, and it has found consistently that the public favors reducing the days mail is delivered and reducing the days the local post office is open.[16] As Figure 8 below shows, the public is okay with fewer delivery days; after all, they're the ones getting emails and texts. But the postal unions are very much opposed to fewer delivery days and so a planned abolition of Saturday delivery for August 2013 was stopped in Congress. In 2014, the Congressional Budget office estimated that abolishing Saturday delivery but still allowing package delivery would save $1.5 billion a year.[17]

Figure 8: Public opinion on five-day delivery



In 2013, respondents were asked their opinion on "eliminating residential mail delivery on Saturdays." In 2009 and 2010, the question was framed as "reducing the number of mail delivery days from six days a week to five."

3. **Is it possible to innovate and create even more efficiencies in pursuit of the universal mandate?** While abolishing Saturday delivery would help save USPS money, more savings would be needed especially if the trends in mail continued. In 2013, Chief Financial Officer of the USPS, Joe Corbett, said, "Our productivity reached an all-time high in 2013, increasing 1.9% compared to 2012. This marks our fourth consecutive year of positive total factor productivity growth since the depths of the recession in 2009."[18]

And yet, comparisons to other, similar, private sector industries suggest that USPS productivity lags behind that in similar industries in the private sector.[19] And for good reason. Productivity in any public sector organization is

16 See Gallup poll on postal service changes, February 2013. (http://www.gallup.com/POLL/160421/SIX-AMERICANS-FAVOR-ENDING-SATURDAY-MAIL-DELIVERY.ASPX)

17 Congressional Budget Office Cost Estimate, H.R. 2748 Postal Reform Act of 2013, June 23, 2014. (https://www.cbo.gov/sites/default/files/hr2748.pdf)

18 United States Postal Service, press release no. 13-087 "Despite Revenue Growth and Record Productivity, Postal Service Loses $5 Billion in 2013 Fiscal Year," November 15, 2013. (https://about.usps.com/news/national-releases/2013/pr13_087.htm)

19 Robert J. Shapiro, "The Basis and Extent of the Monopoly Rights and Subsidies Claimed by the United States Postal Service," March 2015 (Washington D.C.: Sonecon) page 13. (http://www.sonecon.com/docs/studies/Study_of_USPS_Subsidies-Shapiro-Sonecon-March_25_2015.pdf) hampered by non-market restraints placed upon it by law. If the universal mandate is to remain viable, it will have to be accompanied by reforms that allow for steady increases in productivity.

COMPETITIVE-PRODUCTS ISSUES

If the USPS was a private sector entity, it would look for new revenues and new business opportunities that it could develop in the changing market. And over the years, Congress has encouraged the USPS to do just that.

However, for more than a century every entrepreneurial impulse of the USPS has been fought by private sector companies in the same market. A hundred years ago the Post Office Department waged a successful campaign to expand into the banking business and parcel post delivery, and fought a failed campaign to expand into the telegraph and telephone business. A brief recap of this history shows how, as the saying goes, the more things change, the more they stay the same. (The 1970 Postal Reorganization Act replaced the cabinet-level Post Office Department with the independent Postal Service.)

Richard Kielbowicz describes how “the financial panic of 1873, which brought the collapse of three leading securities firms and a ten-day closure of the New York Stock Exchange, prompted the Postmaster General to recommend a postal savings system.”[20] At the time the idea was intriguing for two reasons. First of all, the United Kingdom and Canada had recently established postal savings banks. Secondly, populists, disheartened by Wall Street’s excesses argued that a savings system was a logical extension of the post office’s responsibilities and that postal banks would “encourage thrift among immigrants, the working class, and rural inhabitants.”[21]

Not surprisingly, bankers lobbied aggressively against the establishment of a postal savings system even though its supporters argued that those most likely to use the postal savings institutions would be people, especially Southerners and Westerners, who lived hundreds of miles away from commercial banks. The initial efforts at postal banking failed until the next panic in 1907, when many more banks collapsed and brought a second wave of distrust in the financial system. At this point, President Theodore Roosevelt got behind the idea and in 1910 Congress enacted the Postal Savings Law. American bankers spent $1 million to block the legislation (more than $22 million at today’s prices). While they did not succeed at blocking the law, they did succeed in structuring the legislation so that the new postal savings program would not provide much competition. Interest rates were set at 2% (private banks then were offering twice that much) and Congress set a maximum deposit of $500.

Nonetheless, the new banks immediately attracted customers from rural areas and immigrants. They flourished during the Great Depression when, once again, Americans lost faith in the banking system. The program ended in 1966 when “the federal insurance of private savings accounts and the nearly universal access to banks had rendered postal savings superfluous.”[22]

A second example of postal entrepreneurship came when the USPS got into the parcel post business. At the turn of the last century, the Post Office Department was forbidden to accept any packages weighing more than four lbs. This prohibition spawned the creation of a series of four large express parcel post companies – Adams, American,

20 Richard Kielbowicz, “Testing the Boundaries of Postal Enterprise in the U.S. Free-market Economy 1880 – 1920,” in *More Than Words: Readings in Transport, Communication and the History of Postal Communication,* ed. John Willis (Quebec: Canadian Museum of Civilization Corporation, 2007) page 87.

21 Ibid.

22 Ibid, page 92

United States and Wells Fargo. These companies took advantage of their uniquely important status and the burgeoning market that resulted from the introduction of catalogues and catalogue sales. But they lost public support when Progressive era muckrakers discovered that the companies regularly cheated their customers through overcharging, sending packages by circuitous routes, and colluding with railroads to keep costs high.

Although the companies mounted an intense political campaign against "government takeovers," the Post Office Department was able to argue to Congress that "a full-fledged parcel post would develop profitable routes that compensated for the unprofitable ones found in any system promising universal service."[23] The Post Office Department was allowed to enter the parcel post business and within a year, the express companies stopped competing in small towns. They consolidated during WWI but they were, in the end, undercut by the postal presence in their business.

The third entrepreneurial venture of the last century was the Post Office Department's attempt to establish the postal telegraph and telephone. It was a natural place for the post office to go. After all, the first telegraph line had been built in 1844 with federal funds operated by the agency and at the time most other nations "regarded the telegraph and telephone as natural extensions of the state's mail monopoly and operated them under a postal ministry."[24]

But unlike the banks and express companies of the early 20th century that lost their battles against post office entrepreneurialism, the new private sector monolith, AT&T, was ready with a sophisticated campaign against any further expansion of the post office into telecommunications. The plan for postal telegraph died in Congress when Democrats, who had backed it, decided that new powers granted to the Interstate Commerce Commission to regulate the industry were sufficient. Shortly thereafter, however, WWI broke out and the federal government nationalized both the railroads and the nation's wire communications. However, "[b]ecause the authorizing legislation required government to pay equitable compensation to the telecommunication companies, Burleson [the Postmaster General] was forced to raise phone rates and institute service charges."[25] The public wasn't pleased. After one year as a government company, postal telegraph and telephone was returned to the private sector.

These three stories from a century ago contain important lessons for the 21st century-USPS. In times of economic uncertainty, the USPS has certain important assets – among them public trust. Even today when trust in government in general is at an all-time low – the post office enjoys a surprisingly high level of trust. Americans consistently rank USPS as the most trusted government agency, with 72 percent of the public giving it a job rating of excellent or good in 2014.[26] The USPS also ranks among the top ten most trusted companies, both private and public.[27]

While it is unlikely that USPS will attempt to get back into the banking business, its successful half-century in that business was built on public trust and on the ubiquity of its presence in every American community no matter how remote.

Second, the USPS can in fact put private sector companies out of business. The early express companies had not behaved very honestly in the marketplace and therefore no one missed them much when they were gone; but the

23 Ibid, page 92

24 Ibid, page 93

25 Ibid, page 95

26 See Gallup poll on ratings of government agencies, November 2014. (http://www.gallup.com/poll/179522/americans-ratings-cdc-down-ebola-crisis.aspx)

27 See Ponemon Institute 2014 Most Trusted Companies for Privacy Study, January 28, 2015. (http://www.ponemon.org/blog/ponemon-institute-announces-results-of-2014-most-trusted-companies-for-privacy-study) story is not the same for their modern counterparts. Thus, fears from the private sector that USPS will take over an industry segment it enters are justified and need to be taken seriously. And finally, the decision to keep USPS out of the embryonic telecommunications business kept the USPS from defining itself more broadly as a communications arm of the federal government.

The USPS has had an entrepreneurial past. Business schools teach that most successful businesses grow from their core – meaning that they recognize how to take advantage of their core strengths. Until now, the legacy infrastructure of the USPS has been seen as the primary obstacle to its future solvency. But what if we look at that infrastructure as creating a competitive advantage for the post office in the future? USPS has significant advantages that, under the right circumstances, could be leveraged into new sources of revenue.

Among its advantages is the fact that USPS enjoys high levels of trust among the American public, higher than any other government agency. In addition, it has an infrastructure that is unparalleled in America, with real estate everywhere in the country, including the very most rural outposts. And it has a network capable of last-mile delivery all over the country.

These are significant advantages in the market place and if the USPS were a private sector entity it would probably not be in the position in which it is now. But it is not a private enterprise. Thus, three large questions need to be answered before Congress can evaluate the innovation potential at USPS.

4. Can USPS develop new products and compete in the private marketplace? Are USPS leaders being distracted from the core mission of universal service by their attempts at expansion into other endeavors? Are USPS leaders and managers capable of the kind of innovation needed to compete in the private market?

Last year, regulators granted the USPS permission to partner with Amazon and test grocery delivery in San Francisco. The decision was immediately attacked for losing sight of the core mission of mail delivery and for unfairly competing with the private sector.

But behind the criticism is a broader concern. Can a semi-public sector organization like the USPS, which has operated for most of its existence under monopoly situations, actually compete in the private marketplace? Managing in a highly regulated environment is different from managing in a competitive environment. Every action USPS managers take is subject to regulatory and congressional oversight. Private sector managers are regularly appalled at the constraints under which public sector managers work. While there are some similarities, the fact is that these are different skills, and it is not at all clear that the same managers who run the monopoly on mail can innovate and compete in the private market.

5. If USPS competes more with the private sector, what is the actual US government subsidy and are there ways to compensate for that?

Assuming that the Post Office has the managerial talent to compete, private sector competition comes up against a second and more serious problem – the issue of cross-subsidization. The paradox of entities like the Post Office is that their monopoly status also gives them advantages that the private sector does not have. For instance, post offices don't pay state and local property taxes and offer the sale of first-class stamps and other activities associated with the monopoly portion of USPS. But post offices can also sell items and services that are in direct competition with the private sector. Yet stores that sell private sector packaging materials are not exempt from real-estate taxes. Hence, the subsidy.

No real reform of the USPS can move ahead without tackling the subsidy issue. Estimates will, of course, vary. Last year the President of the National Association of Letter Carriers appeared before Congress and argued that the USPS has received "no taxpayer subsidies since 1983." The Postal Regulatory Commission (PRC) estimates that USPS's special privileges amount to $4.9 billion per year. These include the monopoly on delivering letters, exclusive access to residential and business mailboxes, and exemptions from state and local taxes and fees.[28] Others, however, think this is low. In one recent report, Robert J. Shapiro estimates that "USPS monopolies and related special treatment produce effective subsidies worth nearly $18 billion per-year."[29] For instance, Shapiro argues that the PRC study undervalues the monopoly on access to personal and business mailboxes, since this monopoly applies not just to first class mail but to package delivery where it competes with the private sector. He also argues that the PRC's valuation of USPS's legal exemption for state and local taxes is undervalued. And he shows that the PRC estimate omitted other subsidies such as the USPS ability to borrow from the U.S. Department of the Treasury, its special arrangements for the federal taxation of profits from the USPS competitive products, and the value of the economies of scale and scope generated by the USPS monopoly.[30]

Any expansion of USPS into competitive products will have to take into account the issue of cross-subsidization. It will become a political, as well as an economic, imperative and ways to compensate for these subsidies in the competitive market will have to be explored.

6. Will Congress let the USPS compete?

Making the USPS into an entrepreneurial organization that attempts to increase revenue by leveraging its core competencies is a tall order. It involves a cultural shift on the part of managers and employees that are accustomed to working in a public sector organization, and it involves sorting out the subsidy issue with regard to actors already in the private sector. The more serious obstacle to an entrepreneurial USPS is the plethora of legal obstacles that they would have to overturn in order to be allowed to compete. Consider for instance, the fact that in order to test a new product the USPS has to first receive approval from the PRC. Under Subchapter III, Section 3641 of the 2006 Postal Accountability and Enhancement Act, the USPS is constrained in what they can test. For instance:

"MARKET DISRUPTION- The introduction or continued offering of the product will not create an unfair or otherwise inappropriate competitive advantage for the Postal Service or any mailer, particularly in regard to small business concerns (as defined under subsection (h)).

DOLLAR-AMOUNT LIMITATION- (1) IN GENERAL- A product may only be tested under this section if the total revenues that are anticipated, or in fact received, by the Postal Service from such product do not exceed $10,000,000 in any year, subject to paragraph (2) and subsection (g). In carrying out the preceding sentence, the Postal Regulatory

28 Postal Regulatory Commission, "Report on Universal Postal Service and the Postal Monopoly," December 19, 2008. (http://www.prc.gov/Docs/61/61628/USO%20Report.pdf)

29 Robert J. Shapiro, "The Basis and Extent of the Monopoly Rights and Subsidies Claimed by the United States Postal Service," March 2015 (Washington D.C.: Sonecon) page 3. (http://www.sonecon.com/docs/studies/Study_of_USPS_Subsidies-Shapiro-Sonecon-March_25_2015.pdf)

30 Ibid, page 4

Commission may limit the amount of revenues the Postal Service may obtain from any particular geographic market as necessary to prevent market disruption (as defined under subsection (b)(2)).

(2) EXEMPTION AUTHORITY- The Postal Regulatory Commission may, upon written application of the Postal Service, exempt the market test from the limit in paragraph (1) if the total revenues that are anticipated, or in fact received, by the Postal Service from such product do not exceed $50,000,000 in any year, subject to subsection (g). In reviewing an application under this paragraph, the Postal Regulatory Commission shall approve such application if it determines that—

(A) the product is likely to benefit the public and meet an expected demand;
(B) the product is likely to contribute to the financial stability of the Postal Service; and
(C) the product is not likely to result in unfair or otherwise inappropriate competition."

Note the inherent contradiction in the law. A new product should "contribute to the financial stability of the Postal Service" and yet, with deficits running into the billions the USPS can only test products expected to bring in $10,000,000 per year!

In addition to the explicit road blocks to competition in the law, the USPS is also saddled with a governance structure that seems at times, perfectly designed to stifle innovation. Any attempt at turning USPS into a competitive entity would have to streamline the regulatory entities that oversee it.

CONCLUSION: BREAK USPS INTO SEPARATE CORPORATE ENTITIES.

The USPS exists right now in never-never land. It is not fully public and it is not fully private. It is supposed to compete and innovate but it is stifled by law and saddled with a governance structure that impedes innovation. It is time to decide its future.

That future should begin with a decision to break the organization into two separate entities. One organization should be a public sector organization with the sole mission of delivering on the universal mandate – defined in a way that meets the reality of the information age. The other organization should be privatized so that it is out from under the laws and regulations that make innovation and flexibility all but impossible. This new organization should be allowed to compete with similar organizations in the private sector if and only if the subsidy issue can be worked out so that the new competitor does not have an enormous and distorting market advantage and if it is managed by people with private sector experience.

The future of the USPS raises an even bigger question and one to which there is no clear answer – when should the government compete with the private sector? This question is obviously contentious and the answer to it varies with the party of the President. The back and forth from the Bush administration to the Obama administration over OMB Circular A-76, which calls for competitive sourcing and requires decisions over what is "inherently governmental" and what is not, represents the very beginning of such a difficult discussion.

Nevertheless, while the government has never really come to grips with the big question, it has tackled the sorts of challenges that would be inherent in a comprehensive restructuring of USPS. For instance, the 1996 Telecommunications

Act effectively dismantled the AT&T monopoly and the Bell System and opened up local markets to competition. In constructing this plan, the government had to deal with the monopoly issue and with a full structural separation. In addition, the government has had to manage the full privatization of Comsat (Communications Satellite Corporation), the problems posed by municipal broadband monopolies and the ongoing issues surround the regulation of monopoly power companies. In all instances, a combination of structural remedies and accounting remedies were called into play in order to adjust an older, government supported or created monopoly to the realities of a new era.

Redefining the universal mandate for an information age will allow the United States to preserve its federal postal service and privatizing the rest of the organization will allow for fair competition in an already robust marketplace. The USPS has served the nation well over many years. There is no reason why it can't continue to do so.

GOVERNANCE STUDIES

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