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**HOW TO MOVE THE POSTAL SERVICE
TRULY OFF BUDGET**

Ronald Utt
John M. Olin Fellow

INTRODUCTION

The bipartisan budget agreement between Congress and the Bush Administration includes a proposal to remove the United States Postal Service (USPS) from the unified federal budget. By transferring the USPS's expected fiscal 1990 loss of \$1.8 billion to the nether world of off-budget accounting, the government would create the illusion of reducing the deficit without having to cut spending or boost revenue.

This is accounting gimmickry that simply tries to achieve deficit reduction targets by pretending that parts of the deficit do not really exist. It violates the principle of the government's unified budget: to be a thorough accounting of federal activities and outlays. Removal from the budget of any program for purposes of transitory convenience only misleads the public and undermines important principles of full disclosure.

Failing the Test. There are, of course, legitimate reasons to consider conferring off-budget status on certain government-related enterprises. Chief among them, according to the 1987 President's Commission on Budget Concepts, is that the enterprise be "completely privately owned." The Federal National Mortgage Association is an example of an off-budget, privately owned, government-sponsored enterprise. Obviously, the USPS fails this test.

Off-budget status also could be considered for enterprises attaining genuine financial independence. For the USPS, this would require the

termination of all existing taxpayer subsidies, eliminating access to future subsidies, and an end to all borrowing from the U.S. Treasury.

At present, with its \$1.5 billion in annual taxpayer subsidies and its \$10 billion line of credit with the U.S. Treasury, the USPS receives considerable financial support from the government. However, through a series of management improvements recommended by the General Accounting Office (GAO), the President's Commission on Privatization, and the Postal Rate Commission, the USPS easily could eliminate the need for these subsidies, generate surpluses, and shift its borrowing to the private sector.

With these reforms, USPS could be moved off budget in good conscience. Without these reforms, the effort to remove the USPS from the budget is merely a budgetary gimmick and should be rejected. To move USPS off budget without reforms may forfeit forever the opportunity for genuine reform as an off-budget USPS becomes even less responsive to government oversight.

HOW THE USPS IS PART OF THE GOVERNMENT

While the USPS tends to portray itself as having become an independent, business-like enterprise, since its creation in 1970, it is an integral part of the federal government. Its board is appointed by the President and approved by Congress, as are the members of the independent Postal Rate Commission that reviews USPS rate increases. The USPS receives three forms of direct subsidy from the taxpayer – full payment of retirees' cost of living adjustments (COLA), almost full payment of retirees' health care, and payments to provide below cost rates for preferred mailers. These combined subsidies will amount to nearly \$1.5 billion in fiscal 1990 and are expected to rise to \$2.5 billion by 1994.

The USPS has two other tight links to the government. One is its open claim on the U.S. Treasury through what are called "Transitional Appropriations." These were provided by the Postal Reorganization Act of 1970 to smooth the transition from the old Post Office Department to a government corporation. Its other link to government are the "Public Service" appropriations, last used in 1982, to reimburse the USPS for losses incurred in communities where post offices are not self-sustaining. The USPS also has the privilege of borrowing up to \$10 billion from both the Federal Financing Bank (a part of the U.S. Treasury) and the Treasury itself at interest rates well below what its private counterparts pay in the market.

Exclusive Right to Deliver. Other federal privileges also abound for the Postal Service. The USPS is exempt from all income taxes – federal, state, and local – and it is exempt from local property taxes, although it indirectly pays some where it leases facilities. Moreover, it gets to decide who can and cannot compete with it by virtue of its authority to interpret the Private Express Statutes. These laws, first enacted in 1792, reserve to the USPS the exclusive right to deliver a "letter" and to use the mail box attached to or

incorporated in each private dwelling. Under the statutes, the USPS alone decides when citizens are violating the Private Express Statutes, an infraction that is subject to criminal proceedings.

Finally, as is appropriate for a federal entity, USPS is subject to oversight by subcommittees of both houses of Congress and these subcommittees are not shy about exercising their authority over the smallest management details. Likewise, the subcommittees often serve the interests of USPS, as when they used their investigative powers in 1987 to harass the then Chairman of the Federal Trade Commission, Daniel Oliver, when he criticized the USPS on behalf of American consumers.

HIDING THE USPS DEFICIT

As a wholly owned enterprise of the federal government, the USPS surplus or deficit, measured on a cash basis, is included as part of the federal government's unified budget. It is included in calculations used to determine whether the federal budget achieves the Gramm-Rudman-Hollings deficit reduction targets. Despite the recent postal rate increase, the expenses of the USPS exceed its revenues and the difference between the two contributes to the federal deficit. Even with the \$1.5 billion in taxpayer subsidies, the USPS deficit in fiscal 1989 will be an estimated \$142 million; the gap is expected to widen in fiscal 1990 to \$2.2 billion.

The current debate about the budget status of the USPS has its origin in the 1987 Omnibus Budget Reconciliation Act (OBRA) which directed the USPS to save \$510 million in fiscal 1988 and \$735 million in fiscal 1989 and counted those savings as part of the effort to meet the Gramm-Rudman-Hollings targets for those years. The USPS strongly opposed these requirements and mounted a campaign to get Americans on its side by cutting back on mail service. The strategy backfired, and instead led to public and congressional demand for reforms in the way the USPS managed its affairs.

Union Pressure. Recognizing that the pressures to cut spending would persist as long as it was part of the unified budget, the USPS responded by proposing that it be excluded from the unified budget. Under intense pressure from postal unions, legislation to do this – S. 302 and H.R. 982 – has been introduced and co-sponsored by more than two-thirds of the members of both houses of Congress. Also in response to pressure, the Bush Administration agreed to include in the budget the proposal to move USPS off budget if Congress consents to USPS cost savings.

For the USPS and its unions off-budget status would be the best of worlds. The Postal Service still would receive all of its extant benefits, including its monopoly protection from competition and access to the Treasury for subsidies and loans. But freed from the spotlight of the unified budget, it no longer would have any incentive to act fiscally prudent. It could continue to run a deficit in its operations, but because the deficit would not show up in

the unified budget, there would be less pressure from lawmakers and the President to keep costs under control. Ultimately, these costs would be borne by the mail users and the taxpayer.

When George Bush agreed to remove the USPS from the budget, he called for USPS reforms and the absorption by the USPS of \$500 million of its expenses now covered by the U.S. Treasury. Congress and the Administration will attempt to achieve a total of \$2.9 billion in postal-related deficit "reductions." Yet \$1.8 billion of this is phony and occurs only because the USPS losses will no longer be included in the unified budget. Even the \$500 million saving is little more than an exercise in hope over experience.

HOW TO ELIMINATE USPS SUBSIDIES

Unless the President is prepared to dig in his heels and insist on genuine reform, he is likely to end up with no real reform and the continued hemorrhage of taxpayer dollars to subsidize an off-budget USPS. The USPS should be removed from the unified budget only if the Postal Service becomes financially independent of the taxpayer and the U.S. Treasury. This can be accomplished.

The reforms to do so include:

1) Forcing reductions in federal subsidies to the USPS.

Currently the USPS can dip into the taxpayers' pocket for billions of dollars in subsidies, year after year, to cover its losses. Office of Management and Budget Director Richard Darman proposes that the USPS give up \$500 million in subsidies this year. This amounts to about a third of the likely direct taxpayer support in fiscal 1990. But if additional, similar reductions in subsidies were made in each of the next two years, then the retiree and preferred mail subsidies would be cut to zero. This would break the first link in the chain binding the taxpayer to the USPS.

2) Closing the back door channels to the Treasury.

To foreclose the opportunity for the USPS to take advantage of its other forms of access to federal support, the USPS also should lose its special access to the Treasury through Transitional and Public Service appropriations.

3) Ending the pipeline to Treasury credit.

The Postal Service should be weaned from subsidized Treasury borrowing by having its \$10 billion line of credit reduced by one-third in each of the next three years until all USPS borrowing is conducted through private financial markets at market interest rates.

HOW TO ELIMINATE THE USPS OPERATIONS DEFICIT

For the savings to achieve financial independence without a postal rate increase, the USPS should embark on an aggressive financial reform program that includes contracting out selective maintenance, delivery, sorting, and retail functions.

Janitors would be a good place to start. Citing a General Accounting Office study, Ronald Reagan's Privatization Commission noted that cleaning costs using USPS janitors are \$1.88 per square foot, whereas private contractors could do the job for \$.77 a square foot in USPS buildings of less than 10,000 square feet.¹ The GAO study estimated that the shift to private contractors in the three (of five) regions studied would save \$15 million per year. The GAO further estimated cost savings of 20 percent to 30 percent in buildings over 10,000 square feet. Hiring private firms to clean these structures would save between \$45 million and \$77 million per year in 1982 dollars. Adjusting the GAO findings for current costs, OMB estimates that \$180 million per year would be saved by contracting out all janitorial functions.²

Closing and Contracting. Significant savings also could be achieved in USPS retail functions. Of the roughly 29,000 post offices operated by the USPS, the Postal Rate Commission (PRC) contends that 25,000 are little more than mailboxes that sell stamps and perform limited clerical functions. A 1982 GAO study concluded that about 7,000 post offices could be closed or the retail functions contracted to private firms with no significant deterioration in service.³ Data from the Postal Rate Commission suggest that contracting out such limited service facilities to private sector retail stores could be half as costly as continuing to provide service through post offices. An analysis last year by the Office of Management and Budget concludes that \$240 billion could be saved annually by contracting out the 7,000 limited service post offices in rural areas and the 6,200 limited service post offices in metropolitan areas.⁴

A USPS pilot project in Chicago through Sears Roebuck and Company, offers the full range of retail window services at twelve Sears stores. This project should be replicated nationwide with other retail establishments. Currently there are approximately 1,700 contractor-operated post offices in

1 "The Postal Service Can Substantially Reduce Its Cleaning Costs," Report by the U.S. General Accounting Office, December 28, 1982, GAO-AMD-882-23, pp. 5, 8.

2 "U.S. Postal Service Cost Reduction Proposals," Office and Management and Budget, 1988.

3 Comptroller of the United States, "Replacing Post Offices with Alternated Services, a Debated, but Unresolved Issue," September 2, 1982, GAO Report GGD-82-89.

4 OMB, *op. cit.*

the U.S. Making greater use of existing retail outlets would save money and provide customers with more convenient hours and locations.

Saving \$5 Billion. Expanding the use of private contractors (called "star" routes) to deliver rural mail would lead to significant savings. OMB's 1988 analysis estimates that \$55 million could be saved annually for each additional 10 percent of rural deliveries contracted out.⁵ The President's Commission on Privatization estimated that as much as \$2 billion per year could be saved if all deliveries were contracted out.⁶ And a recent USPS internal study discovered that the savings could be even higher. A July 1988 study by the Postal Inspection Service found that private carrier service is half as expensive as that performed by USPS employees.⁷ Based on the estimated \$10 billion now spent on delivery by USPS, savings through contracting could be as high as \$5 billion.

Likewise, the use of part-time employees to satisfy peak-load needs could save another \$2 billion per year, according to OMB estimates.⁸ Currently, part-time and casual labor is limited to no more than 10 percent and 5 percent, respectively, of the USPS work force covered by the collective bargaining agreement. Efforts to remove these limits during the 1987 labor contract negotiations with the postal worker unions were unsuccessful and the limits remain in place.

Profit for Private Firms. Another money saver would be to let the private sector begin delivering third-class mail to rural addresses. Several firms are eager to do this. The USPS contends that it can provide rural mail delivery only at steep losses. If private firms can deliver this mail at a profit, the USPS should step aside and let the taxpayer and mail user save some money.

In addition, contracting out the sorting operations of all new mail volume could save as much as \$130 million per year.⁹ The USPS has already fostered a private sorting industry by offering four cent discounts on first class mail when a letter is presorted by zip code. The presorting industry easily could expand to do much more.

The above recommendations would save much more than would be needed to offset the loss of the USPS taxpayer subsidy. Such reforms also mean better service to the customers and would limit the postal rate increases soon likely under today's inefficient USPS structure. Even with the current \$1.5 billion annual subsidy, escalating costs will force the USPS to request at least a five cent increase in the price of a first class stamp late next year or in early 1991.

5 OMB, *op. cit.*

6 *Privatization: Toward More Effective Government*, Report of the President's Commission on Privatization, April 1988, p. 121.

7 "Delivery Costs," Postal Inspection Service, July 1988.

8 OMB, *op. cit.*

9 OMB, *op. cit.*

In addition to granting a financially independent USPS off-budget status, the Bush Administration could sweeten the offer by granting the USPS management the right to set its own rates for all those classes of mail where a competitive market exists, provided, however, that the USPS can demonstrate that monopoly profits from other lines are not used to subsidize rate reductions in competition with private firms. The USPS would then be subject to the review of the Rate Commission only in those classes where it maintains a monopoly under the Private Express Statutes. Under this plan, rate setting independence for first and third class eventually might be attained, but only if the USPS were to relinquish its monopoly power in these lines of business and all subsidies from the government.

CONCLUSION

The USPS's campaign to remove itself from the federal budget and from the financial discipline of the budget process poses a challenge and an opportunity to George Bush and a grave risk to the taxpayer. Absent effective action, the \$1.5 billion taxpayer subsidy will rise to \$2.5 billion by fiscal 1994, and postal rates will rise just as dramatically as other USPS costs careen out of control. This year, for example, USPS payroll costs are \$1 billion more than anticipated.

Forcing the Issue. If Bush sticks to his guns on demanding these real reforms, what many now correctly characterize as "blue smoke and mirrors" deficit reduction could turn out to be one of his Administration's most significant economic reforms. No doubt the USPS management and unions, and their Capitol Hill allies, would fight any effort to sever their access to the taxpayer's pockets. For this reason it is essential that Bush force the issue by announcing that he will veto any off-budget proposals unless accompanied by fundamental reforms.

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