

APPENDIX R — Postal Regulation

The Postal Rate Commission

This appendix provides a brief explanation of the Postal Rate Commission (PRC) and its statutory powers. It also compares this authority to the regulatory models of selected foreign posts and traditional U.S. regulatory agencies. When Congress approved the Postal Reorganization Act of 1970, Title 39, U.S. Code, it also created the Postal Rate Commission, Title 39, Chapter 36, as an independent establishment of the executive branch to provide independent expertise in setting postal rates. The Senate proposal envisioned an independent commission within the Postal Service itself, while the House bill created an independent agency. The House version prevailed in conference, and the Commission was directed to provide recommended decisions to the Governors of the Postal Service on rates, fees, and mail classifications; the Postal Service was directed to provide funding for the new Commission.

The Commission thus has jurisdiction over changes in domestic postal rates, fees and mail classifications proposed by the Postal Service, but not over rates and classifications for international postal services. It issues Recommended Decisions to the nine Presidentially appointed Governors of the Postal Service, who in turn have four options: 1) approve the recommended rates; 2) allow the recommended rates to go into effect but under protest; 3) reject the recommendations and request reconsideration by the Commission; or 4) after rejection and reconsideration, and upon unanimous vote of all Governors then holding office, modify the recommendations to balance revenue with costs. Twice, in rate cases filed in 1980 and in 2000, the nine-member Board of Governors has modified the rate recommendations of the Commission.

The President appoints five Commissioners, no more than three of whom may be from the same political party. The President also designates the Chairman, either from sitting members of the Commission or through a new appointment. Members are confirmed by the Senate for six-year terms, subject to an additional “hold-over” year in absence of a new confirmation. The Commission, which has about 55 full-time employees, operates with a multi-disciplined professional staff of about 25 who are trained in law, economics, statistics, and cost accounting.

The ratemaking process attempts to answer two key questions: 1) how much revenue is needed to operate the postal system in a “test” year? and 2) what rates and fees are appropriate to raise this amount? The Postal Reorganization Act establishes the guiding ratemaking principle that “Postal rates and fees shall provide sufficient revenues so that the total estimated income and appropriations... will equal as nearly as practicable total estimated costs of the Postal Service,” 39 U.S.C. 3621. This provision is referred to as the *break-even* requirement.

Another ratemaking principle of the Act requires “that each class of mail or type of mail service bear the direct and indirect postal costs attributable to that class or type plus that portion of all other costs of the Postal Service reasonably assignable to such class or type,” 39 U.S.C. 3622(b)(3). This provision requires the Commission to identify the

costs caused by providing the various classes of service and to attribute those costs to the respective classes and subclasses. The remaining institutional, or overhead, costs of the Postal Service are assigned by reference to the other eight factors specified in 39 U.S.C. 3622(b). These criteria are: fairness and equity; value of service; effect of rate increases; available alternatives; degree of preparation; simplicity; the “educational, cultural, scientific, and informational value to the recipient of mail matter”; and other factors the Commission “deems appropriate.” The statutory factors that apply to classification decisions are similar.

Most rate and classification proceedings are initiated by a Postal Service request, although the Commission itself may also initiate classification proceedings. The request must contain supporting evidence demonstrating why the Service believes its proposals are consistent with the policies established by Congress.

Setting postal rates involves five major elements: 1) costing; 2) volume forecasting; 3) revenue requirement; 4) pricing; and 5) rate design. These elements are interrelated, and changes in the results of one may affect other elements. For example, a new volume forecast will affect both the costs of operating the postal system and the revenues generated by a given set of rates. Similarly, a change in the attributable cost estimate for a service may require a change in rates that will affect the volume of that service.

Prior to 1970, prices for mail services were set by law by the Congress. With enactment of the Postal Reorganization Act in 1970, Congress wanted to ensure that all interested segments of the public would have an opportunity to be heard before the Postal Service changed its rates or services. Thus, it wrote into the Act the requirement that the Commission “shall not recommend a decision until the opportunity for a hearing on the record under sections 556 and 557 of title 5 [the Administrative Procedure Act] has been accorded to the Postal Service, users of the mails, and an officer of the Commission who shall be required to represent the interests of the general public.” The Commission’s Office of Consumer Advocate carries out this latter function, 39 U.S.C. 3624(a).

Under the Administrative Procedure Act (APA), relevant and material evidence must be considered in Commission proceedings. The evidentiary record developed in omnibus rate cases reaches 35,000 to 40,000 pages of prepared testimony, oral and written cross-examination, and related exhibits. Another 350,000 or more pages of material, primarily data sets known as Library References, are also provided. These data involve myriad costing, pricing, market analysis, and public policy issues. In 1976, Congress enacted legislation responding to the Commission’s delayed decision in the second omnibus rate case, during which time the Postal Service sustained significant losses. The 1976 amendments to the Postal Reorganization Act required the Commission to issue its decision within 10 months.

This rate-setting procedure is highly technical and costly. Some active participants (known as “intervenor”) report spending \$1.5 million or more per case on witnesses and attorneys to represent their interests. As a result, while 100 or more parties may intervene in an omnibus rate case, the proceedings are most closely followed by a relatively small number of companies and associations that are able to devote significant resources to the process.

How the role of the Postal Rate Commission differs from that of foreign postal regulators and traditional U.S. regulatory agencies

The regulatory role of the PRC can be contrasted to the role of postal regulators in other countries. In so doing, however, one must appreciate the fact that other countries have substantially different traditions with respect to economic regulation and political systems. In other industrialized countries, postal reform has advanced by transforming the incumbent postal operator into a business, in some cases partially owned by private parties, and by narrowing or eliminating the postal monopoly. In adopting these measures, other countries have generally concluded that some form of independent regulator is needed to help ensure that the incumbent postal operator maintains an appropriate degree of universal service and does not use remaining legal privileges or a dominant market position to compete unfairly against private companies. However, the degree of authority vested in the regulator and tools of regulation vary substantially.

In countries without a tradition of strong, independent regulation, the regulator's role is more that of an enforcer of public policies set by government than that of a definer of public policy. Thus, in Germany, for example, the government, by means of an administrative decree, establishes detailed criteria for universal service, measures for reasonableness of rates, and initiates procedures for rate review. The German regulator's role is limited to administration of these standards, a more ministerial function than that vested in the PRC. Similarly, members of the German regulatory authority do not appear to enjoy the same level of insulation from political pressure traditionally accorded American regulators. Likewise, in the Netherlands, the regulator's role is to administer directives issued by the minister. In the United Kingdom, whose regulatory tradition is closer to that of the United States, the postal regulator has been given broad discretion to regulate entry and price in the delivery services sector according to general public policy criteria set out in the statute. Indeed, the U.K. regulator acts more like a traditional U.S. regulator of private utilities than does the PRC. In Sweden, the regulator's authority falls between these two models.

Regardless of the level of discretion vested in the regulator, tools of regulation vary. The regulator may enforce price regulation either before rates go into effect (similar to the approach of the PRC) or after they have gone into effect (i.e., on complaint). Regulators may set rates according to actual costs or according to efficient costs not actually achieved by the post office. The regulator may employ price caps or set specific rates. In most countries (for example, Germany, Sweden, and the United Kingdom), the role of the regulator, unlike the role of the PRC, is to regulate the entirety of the licensed delivery services sector, not just the incumbent postal operator. Even in these countries, however, the burden of regulation falls more heavily on operators with a dominant position, a category that naturally includes the incumbent postal operator and may (for now) exclude all other operators.

Still another approach towards postal regulation is exemplified by New Zealand where the postal law has been revised, so that the delivery services sector is, in effect, just another industry, with no monopoly, no licensing, no universal service obligation, and no industry regulator. The law obliges all postal services to respect minimum public interest criteria, such as privacy of letters. These criteria are enforceable by the courts. Beyond this, the government of New Zealand ensures provision of universal service by

means of a contract between itself and New Zealand Post, a corporation, all of whose shares are owned by the government.

The regulatory role of the PRC may also be contrasted with that of a more traditional independent regulatory agency in the United States. The prototypical regulatory agency in the United States is the (now abolished) Interstate Commerce Commission, created in 1887. The ICC was the model for the Federal Power Commission (1920), Federal Communications Commission (1934), and the Civil Aeronautics Board (1938), among others. The general scheme of regulation administered by such agencies may be summarized as follows.

Typically, the most basic power of the regulator is the authority to control market entry for an entire industry. The law first prohibits all private firms from providing a certain type of business without a certificate from the regulator. The regulator then grants certificates to private firms for provision of specific services or services on specific routes. The limited nature of certificates allows the regulator to maintain control over the structure of the industry. Typically, a regulator would not grant certificates to new entrants in a given area or for a given route unless it was convinced that new entry would not undermine the services of incumbent firms. The regulator is further authorized to attach conditions to a firm's certificate to ensure that it serves the public interest. Indeed, the regulator may be authorized to compel a regulated firm to extend service to certain areas if it considers such service necessary for the public interest. Alternatively, the regulator may be authorized to issue contracts for necessary public services in areas not adequately serviced by the market.

In a traditional regulatory scheme, the regulator also has authority to regulate prices, conditions of service, and agreements among market participants. The regulator must not deny a firm a fair opportunity to earn a reasonable return on its investment, or take its property without due process. Thus, regulated firms are legally prohibited from charging rates that are unreasonably high or unreasonably discriminatory. In an investigation initiated either by complaint or by its own initiative, the regulator may suspend rates that it finds to be illegal under these standards. It may, or may not, be authorized to set new rates. In some cases, the regulator may be authorized to approve changes in rates before they could go into effect. The regulator may require regulated firms to provide certain services to meet perceived public needs or respond to customer complaints. The regulator is also typically empowered to approve agreements between regulated firms (or even between corporate units of a single firm) based on public interest criteria and to exempt such agreements from further scrutiny under the antitrust laws.

In contrast to this “standard model,” the role defined for the PRC is significantly more limited. The PRC does not regulate entry into the industry. The PRC does not regulate all firms in the delivery services sector; its responsibilities relate to only one undertaking, the Postal Service. Even for this one firm, the PRC does not have plenary authority, but rather shares oversight power with the Governors of the Postal Service, who are also Presidential appointees representing the public interest. The PRC has authority to review price changes prior to implementation, and provide a recommended decision to the Governors. Under limited circumstances, Commission recommendations can be modified by a unanimous vote of the Governors. Once rates are approved, the PRC’s ability to review and reject existing rates on investigation is limited. Nor does the PRC have general authority to regulate the services of the Postal Service or agreements between the Postal Service and other participants in the sector. The PRC also lacks powers, such as subpoena and cease-and-desist authority, that other regulators typically wield in regulating the private sector. Compared to “classic” regulatory agencies, the PRC has been established as a special purpose agency with a narrower focus and more limited functions.

