

Proposal: Support Fund for Universal Postal Delivery

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Agenda

- **Introduction:** Challenges Facing the USPS
Solutions suggested in Europe
- **Overview of USPS' situation**
- **Details of the topics to be addressed**
- **Proposal**
- **Conclusion**

Basic Challenges Facing the USPS

- Financial sustainability
 - Mail volumes declined by 39% since 1984
 - Delivery points increasing by 1 million per year
 - Parcel growth cannot cross-subsidize mail
 - Parcels and mail becoming separate markets -- European experience

Basic Solutions Suggested in Europe

- Europe – develop a support program
 - Estimate the net cost of the universal service obligation
 - Verify that the program creates the least distortion to competition and to user demand
 - Appoint an independent body to administer the fund and for collecting contributions
 - Choose state aid or industry contributions as the funding source

Overview of USPS's Situation

Basic questions and short answers

- Can a Provider of Last Resort operate like a normal business?
 - Not completely. Has obligations that are not economic.
- Is the Postal Service like other POLRs, such as telecom companies?
 - No, much stricter demands on funding, operations, and markets.
- Should its pricing strategy follow that of other POLRs? Yes
 - Postal Service revenue should not be tied to volume of traffic delivered alone.
- How should society recover Postal Service shortfalls in a fair and efficient way?
 - Through a universal service fund

Overview

Premise: 1. The Option Value of Delivery

- Three groups benefit from the Postal Service:
 - Senders
 - Recipients
 - Government
- Senders are shouldering the entire load, instead of paying incremental costs for what they send.
- Recipients are paying nothing, but it is awkward to collect from them.
- Delivery to the door is valuable and should have a price.
 - If it were not provided automatically at birth, it would be the equivalent of having an option value of directly connecting to the network.
 - It also has a social value associated with delivering ballots and medicine.

Overview

Premise: 2. Cross-subsidies exist

- Although service categories cover average incremental cost, they still contain subsidies among customers.
 - The cost of delivery increases with distance and decreases with density.
 - Specific rural areas likely produce economic losses even if wide rural geographic areas do not.
 - Same may be true of specific urban areas where physical delivery is difficult

Overview

Recommendation, Benefits, and Realism

- Estimate the social value of to-the-door delivery and estimate internal service category cross-subsidies. Use them to size a universal service fund.
- Benefits
 - Cost causative pricing
 - Fair pricing – not relying on price increases for least price elastic services to cover costs.
- Realism
 - Telecom and transportation have support funds

Details of the Topics to be addressed

Standard POLR Requirements

- Typical POLR obligations
 - universal availability of a service
 - comparable quality in all areas
 - Resilient
 - Recent Requirement: comparable services at comparable rates in rural and urban areas

Details of the Topics to be addressed

Postal Service's POLR Obligations in rural areas

- U.S. Code Section 101 – Postal Policy clearly states that the Postal Service is not expected to be self-sustaining in many geographical areas.
 - The Postal Service shall provide a maximum degree of effective and regular postal services to rural areas, communities, and small towns where post offices are not self-sustaining.
 - No small post office shall be closed solely for operating at a deficit, it being the specific intent of the Congress that effective postal services be insured to residents of both urban and rural communities.

Details of the Topics to be addressed

The Postal Service has targets that are hard to evaluate,
unlike other POLRs

- The Postal Regulatory Commission has ten objectives and fourteen factors for evaluating Postal Service performance. The examples show that the value propositions are hard-to-measure.
 - Objective 7: to enhance mail security and deter terrorism.
 - Factor 3: the effect of rate increases upon the general public, business mail users, and enterprises in the private sector of the economy engaged in the delivery of mail matter other than letters;
 - Factor 8: the relative value to the people of the kinds of mail matter entered into the postal system and the desirability and justification for special classifications and services of mail.
 - Factor 11: the educational, cultural, scientific, and informational value to the recipient of mail matter.

Details of the Topics to be addressed

The Postal Service is not organized and run like other POLRs

- Unusual constraints
 - No Stockholders
 - Limits on borrowing -- \$15B
 - Limits on service expansion – need to be approved.
- Sidebar: The Postal Service has a monopoly on mail that it appears no one wants (at least in Europe)

Proposal Details

Proposed Pricing and Support Fund strategy

- Support Calculation Strategy is Consistent with European Net Cost Methodology
 - Use Average Incremental Cost (AIC) pricing for service categories but make them more geographically granular.
 - Estimate the price of access (to-the-door delivery)
 - Fund shortfalls through a support fund.
- How to estimate the price of access and support requirements?
 - For access: Special studies? Simulation model?
 - For Support: Top-down approach as a starting point?
 - $\text{Revenues from usage and retirement funds} - \text{Cost of usage (AIC)} - \text{Other joint and common costs} - \text{Cost of retirement funds} = \text{funding shortfall}.$

Proposal Details

Is Universal Service Funding Atypical?

- Telecom
 - Federal Government Devotes Billions to Internet Access: A Community Guide to Current Broadband Funding. Source: <https://muninetworks.org/content/federal-government-devotes-billions-internet-access>
- Transportation
 - Highway Trust Fund is roughly \$50B per year and growing. Source: <https://www.taxpolicycenter.org/briefing-book/what-highway-trust-fund-and-how-it-financed>

Proposal Details Details

Other Funding Issues

- How to Fund is an ongoing problem for POLRs.
 - Don't want it determined politically each year.
 - Telecom: Basic calculation each year to determine shortfall.
 - Perhaps for the Postal Service a line item on income tax.
- Should it be limited to the Postal Service?
 - Yes, because it shoulders the POLR obligations?
- Should funding piggyback on other programs? Yes
 - Tap into EV funding

CONCLUSION

- A Universal Support Fund for the Postal Service has many advantages
 - It recognizes that the Postal Service requires funds to meet targets that an ordinary business would not be required meet
 - It is consistent with economic theory that places a value on the option to have mail and parcels delivered to every door.
 - It is consistent with support funding of other essential services
- The challenges are to size it correctly and fund it in a way that allows the Postal Service to plan effectively
- It will be important to find a solution which does not create distortions in the competitive environment
- A possible solution should encompass the views of all involved stakeholders similarly to what happened to the Mailing Industry Task Force two decades ago which led to the Postal Act of 2006