

President's Commission on the
United States Postal Service

Rebuttal Comments of

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PURPOSE

These rebuttal comments have two purposes:

(1) to respond to certain statements contained in the testimony submitted to the President's Commission by the **American Postal Workers Union** ("APWU") and its supporters regarding the discounts given to workshared mail; and

(2) to respond to certain statements contained in testimony by the **United Parcel Service** ("UPS") as concerns limits on the Postal Service's ability to engage in activities performed by the private sector.

I. APWU POSITION

In testimony submitted to the President's Commission on February 12, 2003, the APWU states:

Discounts have been used to unfairly subsidize large mailers at the expense of individuals and small businesses. These discounts exceed the cost saved by the Postal Service for presorted mail and far exceed the cost to the customer for the work. [Summary, p. ii.]

The Postal Service asks for the ability to give discounts to attract new customers. Yet, it already gives discounts to large mailers equal to about 25% of the price that individuals and small businesses pay for first class postage. It is especially troubling that these discounts exceed the costs that the Postal Service saves in its system and that these discounts are for mail that has no alternative delivery service. The current rate setting mechanism forces single piece users to subsidize large mailers and presort bureaus. This causes the Postal Service to lose contribution on each piece that switches to excessively discounted rates. As more mail takes advantage of these excessive discounts and switches to a presort category, this hurts profitability even more. [p. 13.]

Unfair Subsidies Exist: Intra-class subsidies exist within First Class rates. Single piece mailers subsidize large businesses with discounts well beyond the costs actually saved by the Postal Service. Banks, utilities and credit card companies sort mail in their computers at virtually no cost to themselves and receive discounts of as much as 9 cents off the 37 cent rate. Presort bureaus collect mail from smaller businesses, commingle it, and receive similar discounts. *These discounts are so large in comparison to their own costs that presort bureaus pass on the "lion's share" to the businesses that originate the mail pieces.* This places a burden of more than a billion dollars a year on individual mailers and small businesses. [p. 20, footnote omitted, emphasis added.]

In a companion piece of testimony submitted to the President's Commission, Kathryn Kolbe of Joel Popkin & Co.¹ states:

Although worksharing can benefit both the postal customer and the Postal Service, the wrong incentives sap postal revenues, reduce institutional cost coverage, undermine the Postal Service's efforts to fully utilize its capital and achieve a planned rate-of-return on its investments, and encourage inefficient entry into mail processing. The Postal Service must focus on keeping its own business viable in order to fulfill its universal service mandate. [p. 2.]

Under the right circumstances, worksharing can benefit both the postal customer and the Postal Service. However with the wrong incentives, worksharing saps Postal revenues, reduces institutional cost coverage, and undermines the Postal Service's efforts to fully utilize its capital. With the Postal Service facing financial

¹ Joel Popkin & Co. has testified in the past on behalf of APWU before the Postal Rate Commission.

pressures, it cannot afford a discount structure that overcompensates mailers for worksharing activities. [p. 6.]

Comments. Mailers may, for whatever reason, fail to take advantage of available discounts offered on intermediate “upstream” services, such as sorting or transportation. Instead, they can pay that amount to the Postal Service to have it provide the services for which the discount is offered. Each discount for worksharing thus represents the rate which the Postal Service charges for providing the indicated service, which now has become optional.

The most straightforward way to evaluate adequacy of the rates (“discounts”) charged for intermediate services is to inquire whether revenues generated by those rates cover the Postal Service’s cost of providing the service. That definitely is not the case. Revenues derived from the rates charged for intermediate services fall short of the cost by many billions of dollars.² This significant shortfall has several implications.

First, in order for the revenue from those rates (“discounts”) to cover the Postal Service’s cost of intermediate services that are now optional, the rates would have to be increased substantially, not reduced, contrary to what APWU asserts.

Second, until the revenue from those rates (“discounts”) does cover the Postal Service’s cost, the rate incentive for mailers and private sector intermediaries, such as presort bureaus, should be increased, contrary to what APWU asserts.

Third, since the rates (“discounts”) for intermediate services do not cover costs, if all workshared mail were to revert to non-workshared status and pay the higher rates, the Postal Service could expect costs to

² A complete study of the costs of the revenues and costs associated with workshared mail has recently been completed. The results of this study are contained in a paper entitled “Postal Revenues and Costs From Workshared Activities” by Dr. John Haldi and William J. Olson, Esquire. This paper will be presented at the Eleventh Conference on Postal and Delivery Economics, Rutgers University Center for Research in Regulated Industries, in Toledo, Spain, June 4-7, 2003. At a later time, a copy of this paper will be furnished to the Commission.

increase more than revenues. That would exacerbate the deficit, contrary to what APWU asserts.

Fourth, because the revenue from these rates (“discounts”) fails to cover the Postal Service’s cost of providing services that are now optional, those particular costs clearly are receiving internal cross-subsidies. These intra-class subsidies are derived from excessive charges on workshared mail, not single-piece mail, contrary to what APWU asserts.

Fifth, the mail whose rates are benefitting from an intra-class cross-subsidy is the mail that utilizes proportionately more of the Postal Service’s high cost services — *e.g.*, single piece mail, contrary to APWU assertions.

Sixth, APWU’s assertion that discounts exceed presort bureaus’ costs, while the same discount is less than the Postal Service’s costs, simply reflects that the Postal Service’s cost of providing intermediate services is too high, and not competitive with private sector costs.

Services provided by the upstream portion of the postal network are now in head-to-head competition with the private sector. This development represents a monumental change from the first 200 years of the Postal Service’s existence. Those within the Postal Service who are engaged in providing upstream services may not welcome this new competition. However, when the Postal Service is viewed as a whole — especially the “downstream” portion, or the delivery network, which carries the burden of the Universal Service Obligation — it is seen to have benefitted greatly from the enhanced competition.

For instance, there is no denying that the competition engendered by worksharing has significantly reduced the effective cost of mailing. That in turn has helped to maintain mail volume. This is pointed out by APWU’s own testimony, which states:

In fact the case can be made that the Postal Service is winning the war for advertising. [p. 3.]

Competition from the Private Sector is not new and will not mean the end of the Postal Service. [p. 9.]

It [the Postal Service] has held its own in advertising while most other participants have

seen their market share decline with new entrants from Telemarketing, Cable TV and Internet firms. [p. 10.]

Conclusion. APWU is correct that the Postal Service is attracting and retaining advertising mail. It should give credit to the competition engendered by worksharing, which has significantly reduced the cost of mailing advertising matter, and which has been an important contributor to maintaining mail volume. APWU also is correct that competition from the private sector is not new, and will not mean the end of the Postal Service. Leveling the playing field vis-a-vis the private sector, by increasing rate differentials (“discounts”) to the point where the revenue generated by such rate differentials covers the cost of optional activities, will encourage efficient entry of competitors into the market and further benefit the Postal Service.

II. UPS POSITION

Testimony given to the Commission on February 20, 2003 on behalf of United Parcel Service by its Chairman and CEO, Mike Eskew, includes the statement that:

UPS does not doubt that the USPS has been, and will in the foreseeable future be, the governmental infrastructure for physical delivery of written material supporting our nation’s communications and commerce. No clear lines are drawn for USPS activities outside its core letter mail role. *It need not, nor should it be, engaged in markets that are already well served by the private sector.* As a point of government philosophy and pragmatism, a threshold question is: *why is the Postal Service even engaged in competitive commercial activities?* [p. 3, emphasis added.]

Comments. The Postal Service has a Universal Service Obligation to provide six-day-a-week delivery that is ubiquitous to every residential and business address in the country. From its very inception, the Postal Service has been the nation’s delivery company for letters as well as small packets and parcels. Now, UPS seemingly would have the Commission redefine the Postal Service’s mission in a way designed to

preclude it from offering any service of engaging in activity that could be deemed to compete with the private sector.

For obvious reasons, the testimony of UPS focuses on end-to-end products such as parcel post, Express Mail, and Priority Mail. Its broad-ranging proposal, however, is not so confined. UPS fails to acknowledge the extensive private sector competition from letter shops, presort bureaus, consolidators, and others that now exists for upstream services. The private sector is now permanently ensconced in that turf.

It would be totally unrealistic to contemplate rolling back the clock and restoring the postal monopoly to cover all upstream services. Any attempt to do so would be disastrous. Likewise, it is equally unrealistic to contemplate having the Postal Service cease processing and transporting mail, which is the essence of the UPS proposal. Contrary to what UPS would have the Commission believe, competition between the Postal Service and the private sector is inescapable, regardless of whether the Postal Service is privatized or continues as a government-owned entity.

Conclusion. In our opinion, the Commission should help ensure a level playing field. The Postal Service should not be allowed to exploit its monopoly, nor should it be unduly constrained by laws and regulations that apply to it and not the private sector. Competition will be good for the Postal Service, and it in turn should learn to compete.