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ON WORKSHARING DISCOUNTS

There are two fundamental points that I would like to make in the next few minutes. First, worksharing is the heart of the private sector/Postal Service "partnership". Worksharing has literally saved the Postal Service from complete collapse over the past decade and a half. Second, the barriers to full realization of the benefits of the private sector-Postal Service partnership – some of which are statutory, others the result of excessive regulation by the Postal Service itself, and still others cultural – can and should be removed. Realization of the lowest combined Postal-private sector costs through worksharing is the cornerstone of transformation of USPS into an efficient, responsive and financially stable public enterprise.

These conclusions flow from the following considerations:

* Simply put, worksharing discounts are the rate incentives offered by the Postal Service to encourage mailers to perform functions – sorting, barcoding, transportation of mail -- that would otherwise have to be performed by the Postal Service. In 1999, according to a study prepared by members of the Postal Rate Commission Staff, worksharing rate incentives yielded savings of 15.3 billion dollars to the Postal Service. That was nearly one-quarter of its total costs for that year. It is difficult to imagine what the current volume crisis would be like if postage rates were, on average, 25% higher than they are now.

* Unfortunately, worksharing has not realized its full potential. It will not do so until changes in the system are made. The first major barrier is the rate making process. The break-even requirement diverts attention from the amount of money that worksharing saves the Postal Service to the issue of "revenue leakage" -- how much the Postal Service will lose in gross revenues when it adds a new, or increases the depth of an existing, discount. Further, the costing and modeling systems used to estimate avoided costs are inaccurate and unreliable; and the decisions as to how much of the (imperfectly and incompletely) measured avoided costs should be "passed through" in rate incentives is judgmental at best. Inadequate incentives to engage in worksharing result in imperfect responses by mailers. The system of rate regulation needs to be streamlined and modernized.

* The second major barrier to full realization of worksharing is over regulation by the Postal Service itself. Rules which arbitrarily restrict the volume of mail that can qualify for an incentive -- usually in the name of avoiding revenue leakage -- and rules which are designed for the sole purpose of satisfying Postal Services operational preferences are self defeating. Mailers and their service providers have made, and are prepared to continue to make, very substantial investments in facilities, equipment, software and manpower to qualify for worksharing rate incentives; but they will do so only if the incentives are sufficient to allow them to recover the costs they incur. Mail preparation and service standards need to be established and judged on the basis of whether they further the lowest <u>combined</u> private sector-postal costs.

* The final principal barrier to full realization of the potential that worksharing offers is the compensation cap that is imposed upon senior Postal Service officials. The financial rewards to those officials are so limited that the only measure of success is risk-avoidance, thus stifling innovation and creativity. The dedicated, hard working men and women in postal management are managing an enterprise that yields nearly 70 billion dollars in revenues annually; they are entitled to the same rewards for success and the same sanctions for failure that senior management in other governmentally sponsored enterprises have.

* The question of whether worksharing discounts do or should exceed 100% of avoided costs sometimes arises in proceedings before the Rate Commission. Under the current legal structure there is simply no way to reliably know whether the worksharing incentives are greater than, equal to or less than the full measure of benefit the Postal Service derives from worksharing. As a result, there is no way to meaningfully decide whether worksharing incentives do or should exceed full avoided costs. Implementation of activity based costing under a rate structure with fully unbundled network elements would enable us to decide which worksharing incentives, if any, do exceed full avoided costs and to meaningfully address the question of whether – as a matter of either or both economic theory or public policy –any such incentives should do so.