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DISCUSSING THE HISTORICAL RELATIONSHIP OF THE POST OFFICE AND PERIODICALS IN THE U.S.
FEDERAL TRADE COMMISSION WORKSHOP
“HOW WILL JOURNALISM SURVIVE THE INTERNET AGE,”
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I am really delighted to be part of this workshop, and to have reconnected with Jon Leibowitz (FTC Chairman) after many years, and to find many areas in which the FTC and the Postal Regulatory Commission can work together in the future.

For today's workshop, I will do my best to provide a survey of some of the history of the Nation's post office and its relationship to periodicals. The post and the press share an impressive common ancestry. They are both pillars of the founding democracy that we call our home. The U.S. Constitution's First Amendment requires freedom of the press, and article 1, section 8, gives Congress the power to establish post roads and post offices. The Postal Service is the only nationally-owned government monopoly in federal government. We have some regional organizations like the TVA or rural electric co-ops, but it is the only national government-owned monopoly. And it is as a result of article 1, section 8.

Of course, Ben Franklin is the personification of this relationship, a founding father, a signer of the Declaration of Independence. He was a leading publisher and printer in his day. And he was the first Postmaster General in 1775, by designation of the Continental Congress. I like to say that because he was a magazine publisher, he made sure that the government would take care of his business in the future. But he also, I think, recognized the unique value of both the content of communication, and its ability to be spread evenly and fairly through a neutral agency that created the symbiosis that we have in our Nation's history. You need a full range of open ideas in a democratic society, and you need them to be distributed in a way that they will be available to everybody. So the post and the press are brothers in a commitment to having an educated, democratic and participatory citizenry.

The first major postal law heavily favored the press in 1792. Postage for letters ranged from 6 cents to 25 cents, which was a lot in those days, if you think that we now charge 44 cents for a first class letter. Postage for newspaper subscribers, however, was one cent up to 100 miles and 1.5 cents for distances of more than 100 miles. The law also let printers send each other newspapers for free.

And the symbiotic growth developed throughout the Nation's history. In 1800, there were 903 post offices and 200 newspapers. In 1850, there were 18,417 post offices and 2,200 newspapers. According to Alexis de Tocqueville when he visited the country, it appeared that Americans, spread out across half the continent were better connected than the citizens of a single province of France.

Through the mid-1800s, the postage deal for the press was often sweetened. One example is a New York City to Washington delivery: subscriber postage was 1.5 cents in 1850, 1 cent in 1852, and just a half cent if prepaid. That was a pretty good deal.

In 1863, mail was divided into classes, an approach that still works today. We then had first-class letter mail and second-class mail, which included periodicals, and third-class which we now call standard mail. But for periodicals, the service they received was still first-class service, and that remains today. There is a preference for periodical mail in the delivery stream. Also pricing by the pound was initiated; you differentiated between the piece rate and the pound rate. By 1911, second-class publishers paid one cent a pound, but the post office's costs were about five to eight cents a pound. So subsidies began to develop.

There were Congressional commissions in 1906 and 1911 calling for higher rates, but the system stayed the same. In 1951, President Truman pointed out to Congress that 80 percent of magazine and newspaper postage costs were paid by the public, but the Congress was very reluctant to raise rates. They did it slowly. They did rate increases in 1951 and 1958. And there were rate increases again in 1962 and 1967. But second-class rate deficits kept climbing, from under \$200 million in 1950 to \$435 million in 1968.

By 1971, there were pressures from both postal unions and from Congress – postal unions wanting raises and Congress not wanting to raise postal prices – to set up an independent agency, for the Postal Service to be independent of the federal government, but wholly owned by the federal government. And for a Postal Rate Commission to bear the burden of the controversies of setting rates for different classes of mail. The Postal Service, as it was then called, as opposed to the Post Office, was given the mandate of breaking even. Its revenues had to cover all of its costs. So there were eliminations of direct subsidies for various classes of mail.

Before the Postal Reorganization Act of 1971, you had direct taxpayer subsidies for newspapers and magazines that had a history that went back to the founding of the country. But after 1971, what happened was that periodicals became part of a system where, if there were subsidies, they would be rate-payer subsidies. And what we have now is a system where, to the extent that magazines and newspapers get subsidies, they are subsidized by other payers for the Postal Service, not by the general public. And that is a very fundamental distinction in the debate we have about future subsidies for the post.

Under the new law of 1971, the Commission was directed to oversee a rate-setting process that would bring rates into balance over time so that all mail would pay its own way. And attributable costs – that is the basic cost of the actual handling of the mail and delivery of the mail – would have to be paid for by the rates. But different classes of mail would be allowed to cover a different percentage of what were called overhead or institutional costs, based on a series of factors that were provided in the law. We call them the ECSI factors: educational, cultural, scientific and informational qualities. And as a result, the Postal Rate Commission could say that while letter mail contributed as much as twice its rate into the overhead pool, that periodicals could simply pay only for their basic costs and did not need to contribute to the operating overhead of the Postal Service. So even after the rates were stabilized, and that, by the way, did not occur until about 1980, the Congress provided direct subsidies on a declining basis over time, so that periodicals would not have a rate shock. By about 1980, periodicals were balanced, so that the rates they were paying pretty much covered the costs that you could attribute to their operations in the mail. But periodicals got a free ride when it came to post offices, or institutional costs, or administrative costs, or the infrastructure of the system that they were relying on to use the mail.

There are three key points in the old law that I think are important to remember, and for the most part, they remain in the law that was enacted in 2006. The law recognized the historic value of the press. Periodicals would not have to bear a proportionate share of their overhead costs. The key goal was to cover only attributable costs. They were given a subsidy that spread out over many years to avoid a rate shock. And then the ECSI factors were institutionalized in the law, memorialized in the law, so that the Rate Commission would have to refer to them and make sure that those factors were in place whenever decisions were made about rates in the future.

Until about the year 2000, periodical rates, more or less, covered their costs; although 1996 was probably the year where periodical rates began to slip under that 100 percent coverage. But the Postal Rate Commission was able to adjust the rates, and make a few changes here or there, so that at least on the record, it looked like periodicals were covering their costs to about the year 2000. After the year 2000, there is only one year in which periodicals appeared to have covered their costs, and that was in 2003.

Part of the reason is that the Postal Service actually created a system of great savings and efficiency for letter mail, as letter mail became automated. But magazines and periodicals were not automated, so a greater share of the labor costs of the Postal Service – a greater share of what otherwise would be overhead costs – were then attributable to the magazines and newspapers because they still had to be handled manually, whereas the efficiencies were gained in letters. And letters – even when rates were not going up – because of the efficiencies, created a great deal of revenue for the Postal Service.

I think the other thing that I would like to mention is that one of the reasons that the Postal Service and the periodicals did so well through the year 2000, was that they made a deal with the devil; they agreed that most of the costs would be covered by advertising. And so the mail system in the United States grew exponentially from the mid-1980s through the mid-2000s, because of expanding advertising. The volumes could grow and the relative amount of profit for each piece of mail could decline because there were greater volumes.

We relied on a system that was coming to us because there was more and more advertising in the mail. Magazines did the same thing. You relied on advertising to cover your costs, for the most part. Advertising was the major cash cow for periodicals, as well. So the real cost of the transportation and communication system of the Postal Service, and the real cost of newspapers and magazines, were hidden by the subsidy that we were both getting from being used by the advertising world – for better or worse.

But the recession of 2001 and the anthrax scare put the first dent in that, what seemed to be a perfect devil's bargain, and there was a huge decline in volume. And as a result, the Postal Rate Commission allowed the Postal Service to have a rate increase that did not include any of the careful

review that we would do to balance rates. We had what was called a settled rate case. And the only rate case we have after that was 2005 – another settled rate case – which, in that case, was just a small percentage, across the line, for every rate. So by 2007, when we were required to do the last rate case under the old regime, where we were looking at each rate to pay its cost, we had to make rather significant adjustments in the rates that periodicals were paying, and especially what flats were paying.

Flats got a much bigger hit than periodicals. But both classes of mail, which were still more or less handled by hand, that had not had the benefit of automation, had to have rate increases to cover their costs. So in 2007, there was a big rate increase for periodicals. While periodicals were shocked by it and troubled by it, it was from the Rate Commission's point of view, the only fair thing to do, because, after all, we had single-piece users of the mail – people who are paying bills and using correspondence – who were subsidizing other uses of the mail unwittingly. And under the law, that is our obligation, to try and spread the responsibility for the costs more fairly.

After that rate case in 2007, we averaged that periodicals were covering about 97 percent of their costs. But with a CPI price cap in the new law – the Postal Accountability and Enhancement Act, PAEA, as we say, not the Spanish rice dish, but the new law – the PAEA requires that the Postal Service have a rate-setting process that gives them an increase based on the cost of living, a CPI price cap regime. And that means that periodicals, as a class, can only go up by the price cap.

However, periodical costs were going up far greater than the price cap, and now we are in a situation where we have a negative CPI, so the Postal Service cannot raise prices at all. And we are in a situation where it appears that cost coverage for periodicals is now at 76 percent. So there is a subsidy that periodicals now have: Only 76 percent of attributable costs of magazines and newspapers are being paid for by magazines and newspapers and none for the overhead costs and 25 percent of the attributable costs. We believe in the current estimate of costs we have that this amounts to \$641 million.

That is a pretty big subsidy. And it is something that the letter mailers in the system are complaining about constantly. They very much want the Postal Regulatory Commission to address this issue. So we have a complex problem here that has to be solved. Under the current rate regime, which we inherited from the Postal Rate Commission, periodicals have rates that are very complicated and set on a very wide range of characteristics. You have a rate that you are charged for the editorial content of

your mail, a rate that you are charged for the weight of your mail, a rate that is charged for your advertising, and a rate that is charged for the distance that you send your magazines.

Furthermore, you get discounts on your editorial rates. You get discounts if you work share, which means presenting the material to the Postal Service in some sort of package order, and further discounts if you drop ship, in other words, deliver the mail to a location where it is closer to where it is going to be delivered. And for the editorial rate, you do not pay a distance fee; there is no distance surcharge; it is just a flat fee. But for the advertising rates, you pay a surcharge; and for the pound rates, you pay a surcharge. So it is a very complex matrix.

What I can say fairly generally is that the higher the editorial content of the publication, generally the higher the subsidy; the more editorial content, the higher the subsidy. There are about 9,000 publications with what we call medium editorial content, somewhere between 51 percent and 85 percent as a whole. That group, we think, costs the Postal Service about \$350 million a year. The lowest work sharing groups, those with the smallest circulation and with the highest editorial content, actually cost the Postal Service on average about 19 cents per piece. Those periodicals are often the ones that journalists are most concerned about. Those are often the periodicals of opinion, and they are the ones that are distributed nationwide, as opposed to a particular region. So it is very difficult for them to do any work sharing or any drop-shipping, and the cost of the postal service is greater. Even though their rates may be higher than some of the largest magazines, the subsidies they are getting, if you are looking at the costs to the Postal Service, are greater.

That is another important principle that I think has to be addressed in any future discussion about what we do about supporting periodicals in the future. It is the periodicals that are the most expensive to the Postal Service that are the ones that are asking for the subsidy but actually get the largest subsidy now. I think what we have to do about the future is to have a discussion that really comes to grips with the contradictions that are in the current law, and in the arrangements we now have for a relationship between post and periodicals.

The postal law, the PAEA, requires that all rates cover their costs and it also provides us with guidelines for the ECSI factor, but it provides a very limited way in which rates can cover costs. It has also put this enormous additional financial burden on the Postal Service of prepaying its retiree

healthcare benefit fund to the tune of \$5.5 billion a year, so that the Postal Service is now running enormous deficits. Last year, it was a \$3.8 billion deficit. It would have been \$7.8 billion if the Obama Administration had not forgiven \$4 billion of that payment, basically tacked it on to a later year. The Postal Service is estimating that it will have losses of between \$6 billion and \$7 billion this year. So for us to be asking the Postal Service to absorb \$641 million of subsidies to periodicals, which are a very small portion of the volume of the mail, is a very difficult proposition for us. And it does not make sense financially if we are concerned about the overall financial survival of the Postal Service. We have a dilemma.

Now, there are some things the Postal Service is doing. It is trying to cut its overhead costs. You read about that. They have cut 20-to-25 percent of their employees already. They want to cut delivery one day a week. They are talking about closing post offices. They also have a huge investment in an automation project for flats and periodicals which has been delayed for many years. I think by next year, if not the end of this year, it will be up and running with 100 machines throughout the country that will be able to sort flats and periodicals much more quickly. The system will be more like the system they have for letters. Now, they have been promising this automation improvement for many, many years, since I have been on the Commission. So, it is a long time. We are hopeful that they will actually be able to have some really documented cost savings, so that there will be less overhead, and less cost requirements, for periodicals to meet in the future. There also may be reductions in their general overhead through these other cost savings that will save the Postal Service some money.

I think that it is only fair for both the periodical community and postal community to approach Congress with the notion that there is this symbiotic relationship and that support for both parts of this communications network that supports democracy are necessary. I think if the Congress understands this unique relationship, arguments can be made for finding financial support in one way or another that may address both of our concerns.

We have not been that successful to date in getting the Congress simply to focus on addressing the concerns of the Postal Service on its own. But I think together we have a case for what is an essential part of American infrastructure, and something that the Congress really does want to maintain, not only for its own personal desire to get reelected every year. They want to make sure that there is a

vibrant political dialogue in the country. So, I do not have all the answers for you, other than to say that I am delighted to be here and that you have my pledge in my role as a regulator to participate in these discussions to see if we cannot find ways in which both the post and the periodicals can work together to ensure our future.

Thank you.

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