BEFORE THE
POSTAL RATE COMMISSION
WASHINGTON, D. C. 20268-0001

POSTAL RATE AND FEE CHANGES, 2000	:	Docket No. R2000-1

DIRECT TESTIMONY OF
JAMES O'BRIEN

ON BEHALF OF
ALLIANCE OF NONPROFIT MAILERS
AMERICAN BUSINESS MEDIA
COALITION OF RELIGIOUS PRESS ASSOCIATIONS
DOW JONES & COMPANY, INC.
MAGAZINE PUBLISHERS OF AMERICA, INC.
THE McGRAW-HILL COMPANIES, INC.
NATIONAL NEWSPAPER ASSOCIATION
AND
TIME WARNER INC.

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Autobiographical Sketch

My name is James O'Brien. I am the Director of Distribution and Postal Affairs for Time Incorporated, a division of Time Warner.

I have been employed by Time Inc. since 1978 and have been involved in the manufacturing and distribution of magazines for over 30 years. At the beginning of my career in 1969, I worked for R.R. Donnelley & Sons, where I prepared mail for shipment and loaded postal vehicles with mail sacks. During college, I worked part-time for United Parcel Service and supervised a parcel re-loading operation. In the late 80's, as Time Inc.'s Director of Field Operations, I was responsible for magazine production and distribution throughout the United States. From 1990 to 1996, I was CEO of Publishers Express, an alternative delivery company that serviced 1000 zip codes in 32 cities nationwide. Today, I am responsible for the newsstand and subscriber distribution of all Time Inc. magazines. These titles generate approximately 750 million pieces of Periodicals class mail annually with a USPS revenue value of approximately $145 million. In the course of my employment, I have visited numerous printing plants, lettershops, freight forwarders and consolidators, U.S. Postal Service facilities, foreign posts, and Postal Service competitors, such as Federal Express.

I am currently the Chairman of the Postal Committee for the Magazine Publishers of America, Chairman of the Postal Policy Committee for PostCom (Association for Postal Commerce; formerly AMMA), a member of the PostCom Executive Committee and Board of Directors.

I served as a member of the joint USPS/Industry Periodicals Operations Review Team. I also participated in the MTAC (Mailers Technical Advisory Committee) Package Integrity Task Force. The work performed on these task forces forms the main basis for my testimony.

Purpose

The purpose of my testimony is to describe some of the causes of the inefficiencies in the current mail processing system and identify opportunities for improvement in the test year and beyond. In addition, I will discuss the inadequacy of the current rate structure and introduce an alternative structure that would provide incentives for more efficient mailer behavior.

I. The Joint Industry/USPS Periodicals Review Team

The concept of a joint industry/USPS Periodicals Mail Processing Review Team ("Periodicals Task Force") was conceived immediately after the Docket No. R97-1 decision was issued. Periodicals mailers had been litigating the issue of mail processing costs since the R90-1 case. Their primary concern was the sharp increase in Periodicals mail processing costs that began in FY 1986.[1] These costs have increased at a rate exceeding inflation, postal wages, and mail processing costs for all other classes of mail since 1986. In its Docket No. R97-1 decision, the Commission stated its conclusions on the issues we had raised:

> The presort mailers argue that the rapid growth in mixed mail and not handling costs reflects automation refugees or other inefficiencies associated with automation. The Commission finds that the circumstantial evidence for this inference is inconclusive, but warrants systematic investigation. It makes a similar finding with respect to the rising unit processing costs of Periodical mail. . . . The Commission urges the Postal Service to make a more systematic inquiry into the causes of rising not handling costs, as these witnesses suggest.[2]

In recognition of these as well as other problems, the Commission lowered the Periodicals Class markup to the minimum level allowable under the Statute. While the publishing industry was grateful to the Commission for addressing this issue, many realized that a low markup was a temporary solution at best. It was obvious to both mailers and the Postal Service that something needed to be done to understand these out-of-control cost increases and to eliminate their causes

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[1] See Docket No. R97-1, Testimony of Halstein Stralberg (TW-T-1): Tr. 26/13811, 13820-23.

[2] PRC Op. R97-1, ¶¶ 3148, 3187.

prior to the next rate case. If costs could not be reduced, the publishing industry could expect no further relief from the Commission, and Periodicals Class mailers would see rates increase in lock step with increasing mail processing costs.

The mail processing cost issue unified the publishing industry. As a result, the Task Force included representatives from both the American Business Media and the Magazine Publishers of America. The Postal Service provided representatives from Operations and Finance, and a consultant from Christiansen and Associates. As a member of the Task Force, I visited a total of 16 Postal Service facilities, including BMC's (Bulk Mail Centers), P&DC's (Processing And Distribution Centers), Annexes, and Associate Offices. Overall, the Task Force visited sites that collectively handle 14% of all flat mail processed in the United States. The Postal Service allowed us to view all operations and ask facility managers any question that pertained to mail processing. However, it must be noted that the Postal Service ruled the topics of IOCS (In-Office Cost System) procedures and cost attribution assumptions off limits. The Report of the Periodicals Operations Review Team is on file as part of Library Reference I-193.

The Task Force began its evaluation of mail processing in the fall of 1998 and completed all visits by December 1998. The Task Force incorporated observations from a broad range of geographic locations and all three Postal Service tours. Facilities were visited in the East, Midwest, South, and West.

The Task Force produced a total of fifteen recommendations, each of which contains short and long term action items for local postal operations, national postal operations, and/or mailers. In the remainder of my testimony, I summarize each of the recommendations, describe my personal observations from the field visits, and comment on the potential impact of the action items on Periodicals Class mail processing costs.

Issue 1: Preparation standards for Periodicals should more closely match postal processing configurations

At many of the facilities we visited, we noticed that Periodicals mail was being transported by USPS contracted vehicles between the P&DC's and their respective annexes. In addition, there were a number of associate offices that processed mail for multiple zip codes. Unaware of this processing configuration, mailers sometimes ship their mail to the wrong facility. For example, the primary plant in Milwaukee, WI, is located in the center of the city, yet Periodicals mail is processed in an annex several miles south of the city. When mailers ship their mail to the downtown facility, the Postal Service must unload the trailer, cross-dock the publications into a trailer destined for the annex, unload the trailer at the annex, and take the mail to the processing area. Needless to say, this is not an efficient process. But it is not a difficult problem to correct. If the Postal Service could develop a national mail processing scheme and facility list indicating where Periodicals mail is actually processed, mailers could tailor their mail preparation and transportation to match the USPS operations. Once mailers begin to ship product to the facilities where the mail is processed, unnecessary allied labor and transportation operations will be eliminated. From a mailer's perspective, this can be accomplished by incorporating the facility database into our presort and dropship software programs. I am confident that this program could be implemented very quickly if it became a DMM requirement.

The Task Force also noticed that current USPS regulations require the separation of bar-coded and non-bar-coded bundles destined for the same 5-digit zip code into separate containers. A container, such as a sack or pallet, designated for a 5-digit zip code is not opened until it arrives at the 5-digit facility. At the same time, there is no automation equipment to take advantage of the barcodes at the 5-digit facility. So the exercise of putting barcoded and nonbarcoded mail in separate containers is pointless and adds unnecessary cost. We recommended that the USPS consider allowing barcoded and non-barcoded flats to be combined in the same 5-digit container. On February 29, 2000, the USPS published in the Federal Register a proposed rule allowing

barcoded and non-barcoded flats to be placed in the same 5-digit container. It is my understanding that the Postal Service expects to enact and fully implement the regulation change by year-end.

Since the Task Force recommendations have been issued, the Postal Service and MTAC have been working on several other initiatives that will allow the Postal Service to capture savings in these areas. First, the USPS has created the L001 labeling list that provides a directory of facilities that process multiple 5-digit zip codes. If compliance with L001 is made mandatory, as I believe likely, the Postal Service expects that approximately $3.6 million in Periodicals mail processing costs would be saved in Test Year 2001.[3]

It is my understanding that the current list of L001 zip codes represents only 14% of the total available zip codes in the United States. If the Postal Service provides L001 data for the remaining 86% of the zip codes, the number of L001 opportunities will increase significantly. As more facilities that process multiple zip codes are incorporated into Periodicals presort programs, it will result in an even greater number of 5-digit pallets.

Next, an MTAC work group is in the process of creating a facility database that reflects where Periodicals mail is actually processed. Peter Moore, who is the industry co-chair of this MTAC initiative, has indicated that the database will be operational by December 31, 2000. Once this database is finalized, Time Inc. will incorporate it in our shipping manifests and dropship our mail to the proper facilities, thus lowering Postal Service costs.

Issue 2: Optimization of containerization can help reduce costs

One of the more resounding themes that we heard from P&DC and delivery unit managers was a desire for more 5-digit pallets. In fact, we heard this from every P&DC manager except one (who happened to have a sack sorter in her facility). It is much easier and more cost effective for them

[3] See USPS response to TW/USPS-8 (filed May 9, 2000).

to cross-dock a 5-digit pallet than to bring the mail into their facilities for processing. Bundles of mail in a sack or pallet that has less than a 5-digit sort must be unloaded from the trailer and, typically, taken to an SPBS (small parcel and bundle sorter) machine, dumped or loaded by hand onto the SPBS, keyed by zip code into the machine and sorted into a 5-digit container. Someone must sweep the machine, and the 5-digit container must eventually be taken to the shipping dock to be loaded onto an outbound truck. If mail arrives at a P&DC on a 5-digit pallet, it is simply cross-docked to the outbound 5-digit truck, and there is just one handling of that pallet.

Pallets are the container of choice for the P&DC's. Once this became clear, we focused our attention on how to create more palletized mail without negatively impacting the smaller facilities downstream. Our first recommendation was to allow the multiple stacking of small pallets up to four tiers high. This suggestion was implemented by the Postal Service on August 12, 1999. We also recommended a review of the operational impact of initiatives such as package reallocation and lower pallet minimums.

I have also supplied the Postal Service with samples of pallets that Time Inc. uses for small newsstand shipments. These are basically smaller versions of a full-size pallet, but allow more effective trailer loading. The width of a standard trailer can accommodate a maximum of two full-sized pallets. Our smaller pallets can be loaded three wide on the same vehicle. What's more, these smaller pallets can be handled with a standard forklift or pallet jack with no modifications. No new material handling equipment is required. If the Postal Service adopts this option for creating smaller, more efficient pallets, it will mean some increase in inventory expense but more than compensating savings in transportation and in handling and mail processing costs at the P&DC's.

Issue 3: Encouraging good address quality can significantly reduce rehandling costs

The Task Force raised two key issues related to barcoding and address quality. Obviously, if mailers take the barcode discount, the Postal Service needs to have the ability to capture the

savings through automation. We saw many flats that were being rejected by barcode readers and would need to be manually keyed by an FSM clerk. To improve barcoding, the USPS Business Mail Acceptance Units must provide feedback to mailers that submit unreadable barcodes. In addition, mailers need to conduct more barcode testing prior to entering the mail. Time Inc. is currently developing a new process for binding magazines. A prototype of this machine has been in testing for over one year, and we expect the production version to be operational by September 2000. To ensure that this machine produces readable barcodes, I have asked the Director in charge of technology development to have barcode readers installed on every one.

Second, we suggested that all mail pieces should contain a carrier route designation. With a carrier route code on all pieces, clerks in both plants and delivery units would not need scheme knowledge to sort copies to individual carrier routes. Periodicals mailers have the ability, with some programming changes, to apply carrier route barcodes to copies within a 5-digit or lower bundle. The Postal Service would have to train its employees to recognize the carrier route designation, since it would not be in the standard position on the endorsement line. This improvement in address quality is entirely possible and needs to be pursued; in fact, McGraw-Hill already applies carrier route designations to copies not contained in carrier route bundles.

Issue 4: Enforcement of entry/acceptance requirements and communication of problems with irregularities to the publisher, as well as the printer, are important

During our visits we saw numerous examples of mail that had not been prepared according to the DMM regulations, yet it had been accepted by BMEU (Business Mail Entry Unit) personnel. The Postal Service developed two separate initiatives to address this problem. First, Ed Wronski and the staff at the New York Rates and Classification Service Center (RCSC) have created a program called "Getting Closer to the Mailbox." The program consists of printed and video reference material that shows the proper way to prepare mail. This program has been offered to publishers throughout the country by the various Postal District Offices. In addition, this program is required reading/viewing for all USPS acceptance personnel.

The second program was developed by the New York RCSC in conjunction with Marketing, Operations, Delivery, and Core Business. This is called the "Periodicals Awareness Program." It consists of roughly two hours of training including a 60 minute video. The training program is being given to all craft and supervisory personnel involved in the processing of Periodicals. The program is currently being rolled out to the field and should be completed within the next two months.

While I have not seen the Periodicals Awareness Program, I have reviewed the Getting Closer to the Mailbox program and have made this required reading and viewing for all new people in my department. The material is clear, very basic, and easy to understand. The Postal Service has indicated that they issued a survey that requested feedback on the program and have received approximately 900 responses from mailers, most of which were an endorsement of the program. Overall, I feel that this is an excellent program that can help to improve mail preparation practices.

Issue 5: Further develop and communicate the flats operation plan

Our visits taught us one very clear lesson. No two facilities process Periodicals in the same manner. Each operation is driven by facility configuration, available equipment, local work rules, mail mix, and what at times appeared to be a "We always do it this way" mentality. One facility encourages mailers to prepare sacks because they have a sack sorter. Another has an SPBS but lacks roller extensions for the individual run-outs, and so only sorts to 50% of the available positions. Staffing levels on the SPBS machines range from 11 to 18 people. Some facilities do not have an SPBS but instead process on a LIPS (Linear Integrated Parcel Sorter) machine, which is commonly referred to as the "poor man's SPBS." In some facilities, flats are sorted into sacks rather than rolling stock because of a rolling stock shortage. In short, flats mail processing is a complete hodgepodge that requires some systematic evaluation and change.

Since the Task Force's visits, Postal Service personnel have attempted to formulate a systemwide flats automation plan. This plan was widely discussed at a joint USPS/Periodicals industry meeting on February 8, where participants observed the AFSM 100 in action and discussed ways that mailers could work with the Postal Service to further reduce costs. One excellent example of how mailers could help reduce costs came from Tom Tully of McGraw-Hill. The new AFSM 100 machine has a feeding mechanism that inducts flats very quickly. To help the feeders keep up with the machine, a number of people were preparing the mail for the feeders: removing any bundle wrap or straps, facing them in the same direction, and placing the magazines in a special cart that made things quite easy for the feeder. Seeing the amount of allied labor required to prepare the mail for this high speed machine, Tom suggested that mailers could prepare products destined for the AFSM 100 without any bundle strapping or shrink wrap, since this material was removed prior to processing. In this way, AFSM 100 allied labor costs for mail preparation could be dramatically reduced or eliminated.

The Task Force also took note of some very good practices taking place in some postal facilities. In Baltimore, for example, the Postal Service took an aging, multi-story facility and transformed it into what appeared to be a well-run, efficient operation. USPS management needs to thoroughly explore best practices in its mail processing operations and encourage those practices in its less efficient operations. Best practices are discussed in greater detail in the following section.

Issue 6: Separation of mail classes is of questionable value and may add to costs without necessarily improving service

In many facilities, the Task Force observed tremendous efforts being taken to separate Periodicals Class mail from other classes, "in order," we were told, "to protect service." While that is a worthy goal, it does not always play out as planned. By segregating classes in certain mail processing operations, facility managers may be adding costs without improving service. According to witness Unger, "A supervisor will work the class with the largest volume available

on the machinery and will move the smaller-volume classes to the manual operations."[4] The problem he describes is not attributable to the length of run but the fact that the classes of mail are segregated. If mail classes could be combined on the equipment, the result would be more effective equipment utilization, a streamlined operation, and a reduction of cost.

Coming from a publisher of four national weekly magazines, the concept of combining mail classes in processing may sound like heresy, but it is not. In Baltimore, we saw an example of how to combine mail classes yet protect service. In this operation, the facility processed two streams of mail on its flat sorting equipment. The first consisted of First Class mail and time sensitive Periodicals, commonly referred to as "hot pubs," such as daily and weekly publications. The second was a combination of Standard A mail and lower frequency Periodicals, such as monthly or quarterly publications. The system worked because the people delivering products to the machines for processing had a very clear understanding of what mail goes to each machine. As a result, the "hot pubs" go to one machine and the monthly pubs to another without adding any cost. In terms of service, there really is no delay for either mail stream since managers attempt to "sweep" the facility each night, so that there is no mail remaining in the facility. Any decision to defer mail because of volume considerations is made at the delivery unit, not the P&DC. The delivery unit is in the best position to make that decision. The letter carrier can clearly see that a tote contains both Periodicals and Standard A, and deliver that mail according to the service standard of the highest mail class in the container. If mail needs to be deferred, the delivery units all have adequate quantities of deferrable mail in carrier route bundles that can easily go out the following day and still meet the service standard.

Was this system perfect? Absolutely not. For example, in one of the delivery units outside of Baltimore we saw a clerk segregating Periodicals and Standard A pieces that were combined into one tote at the P&DC. This practice not only slowed down both classes of mail but also introduced another level of handling and expense. It would have been far more efficient for the

[4] USPS-ST-43, at 9, ll. 10-13.

clerk to case all of the mail and allow the letter carrier to make a decision on what to defer. This was a clear example of a lack of communication between the P&DC and the delivery units, but it is not a difficult problem to correct.

According to witness Unger, "Service tends to be a dominant factor in the Postal Service's approach to Periodicals, and it substantially affects Periodicals processing costs."[5] This does not need to be the case. The Baltimore best practice demonstrates that service can be maintained in a cost effective operation. After seeing this operation in action, I'm convinced that, if replicated, it could have a significant positive impact upon cost. Senior management at the Postal Service should recruit someone like the Baltimore P&DC Manager, Jerry Lane (who is no longer in Baltimore), to develop a specialized process improvement program for each P&DC in the country.

In its final report, the Periodicals Operations Review team stated:

> Based upon observations in the sites we visited, the review team believes that cost savings and better use of automated equipment can generally be achieved, without compromising service standards, by combining Periodicals flats with other mail streams in the incoming processing at a processing plant and its associated Distribution/Delivery Units.[6]

The USPS agreed and issued the following Addendum to Periodicals Standard Operating Procedures (SOP) on February 4, 2000:

> This SOP indicates the following: "The option of commingling Periodicals and Standard Mail (A) flats may occur at the incoming secondary level, as long as service for the Periodicals can be maintained. When Periodicals are mixed with Standard Mail (A) flats, the dispatch container must be labeled as "Periodicals." Any facility that opts for this type of commingling must ensure that service performance for Periodicals is strictly monitored and enforced.[7]

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[5] USPS-ST-43, at 7, ll. 10-11.

[6] Report of the Periodicals Operations Review Team, at 21.

[7] See response of USPS to POIR No. 9, item 8 (filed May 1, 2000).

The challenge for the Postal Service is rolling this best practice out to other P&DC's prior to the test year. According to USPS Processing Operations personnel, they are encouraging plants to incorporate the merging of classes and expect that this practice is being widely adopted.

Issue 7: Improved bundle preparation by mailers and improved materials handling by the Postal Service will reduce bundle breakage – which appears to increase Periodicals Costs significantly

As the Postal Service strives to automate mail processing and make it more efficient by reducing labor costs, it sometimes creates an unwanted by-product. Thus the SPBS and mechanized sack sorting operations apparently resulted in an increase in broken bundles. In several facilities, the Task Force observed pallets of unbroken Periodicals bundles tilted on their sides and dumped onto an SPBS feeding belt. For the bundles at the bottom of the pile, the effect was like being in an avalanche. They were designed to maintain their integrity through mail processing, but not to withstand a 2000 lb. lateral force. As a result, some–but surprisingly, not that many–were broken. The SPBS belts that used pallet dumpers also had one or two people who used sticks to relieve the congestion on the belt once a pallet was dumped. Overall, it appeared to be a process that could use some evaluation and improvement.

The Task Force also visited facilities that use sack sorters, machines that consist of numerous overhead belts that route sacks into containers destined for other facilities and that seemed to damage a good deal of mail in the process. In Chicago, we saw the operation where containers of damaged mail from the sack sorters were processed, which consisted of an opening belt staffed by six people, where the mail was dumped and each piece manually processed. The people that were processing this mail had experienced injuries or disabilities, and this operation was a way to keep them busy.

Acting on the Task Force's recommendations, the Postal Service in conjunction with MTAC created a Package Integrity Task Force, the purpose of which was to observe various SPBS and sack handling operations to determine the cause of bundle breakage. As a member of that Task

Force, I visited the SPBS and sack opening operations in Boston, MA, where I spent the better part of a day at a sack-opening belt where one mail handler dumped sacks of Periodicals onto a belt and three others sorted that mail into containers destined for local delivery units. There were broken bundles coming out of just about every sack. The method of strapping did not seem to matter. On the other hand, I spent roughly one hour at an SPBS pallet dumping operation where pallets were being dumped using the new procedures and did not see any broken bundles. While the complete report of the Bundle Integrity Task force has not been issued, the preliminary data indicate that palletized bundles break 0.5% of the time while sacked mail breaks 17% of the time.[8]

To its credit, the Postal Service took quick action on the SPBS dumping problem. Under the current SOP (standard operating procedure), pallets are no longer dumped in their entirety but layer-by-layer.[9] This significantly reduces the force of the avalanche. In addition, the Postal Service has modified many of the SPBS machines to improve the bundle feeding mechanisms. These improvements include eliminating turns which force products to change direction and possibly break. Side guards were modified to eliminate catch points that could break bundles. To improve the transition of the bundles onto the SPBS belts, extensions were made to the chutes that bundles travel down once they are dumped. The list of improvements is more extensive than discussed here. Of the 345 SPBS machines in the field, the feed systems have been improved on 271 machines. The remaining 74 machines cannot be improved because of space constraints or lack of economic feasibility. Overall, the Postal Service has created an improved process which should result in a significant reduction in bundle breakage.

We saw many cases of broken bundles where the SPBS keying clerk simply keyed in each piece individually. The Postal Service has taken steps to curtail this obviously inefficient practice. Under instructions issued to the field by Postal Service Headquarters, SPBS personnel now

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[8] USPS response to TW/USPS-2 (filed April 13, 2000): Tr. 21/9281-83; LR-I-297.
[9] See note 7.

attempt to reconstitute broken bundles using rubber bands if the pieces are still together and can be easily picked up. If the pieces are loose, they are put into a container and sent to a flat sorting operation for processing.[10] This new procedure, under which individual pieces will be keyed on an SPBS only as a last resort, should significantly reduce the extra costs generated in those instances when bundles are inadvertently broken.

Issue 8: Focus operations management on the importance of efficiently managing processes and equipment

At every facility that the Task Force visited, we asked the senior managers what they would do if they were required to reduce Periodicals mail processing costs by 10% and empowered to change any rule, regulation, or process. To our surprise, many responded that they have never given the matter much thought, or their answers related to service. As a manufacturing and distribution oriented person, I feel that it is essential that local management be focused upon cost control and productivity improvement if the problem of flats mail processing inefficiency is not to perpetuate itself.

In Charlotte, NC, we visited the General Mail Facility during the beginning of Tour 1 to see their Tray Management System (TMS) in action. While the TMS appeared to provide an efficient means of handling a large volume of letter trays, I was not convinced that the system resulted in significant labor reductions. The people who were loading the trays onto the various APC's and nutting trucks did not appear to be working very hard throughout the tour. We returned to the facility at 5 a.m. to observe the "dispatch of value." This is the final dispatch of the day to the Associate Offices and determines what mail will get delivered on that day. In preparation for this dispatch, people came out of the woodwork and there was a great deal of activity on the shipping dock. There were people and equipment everywhere, and everyone was hustling to get the products on the trucks. While we viewed this operation, it was obvious that the people who

[10] See response of witness Kingsley to MPA/USPS-T-6, Attachment (filed February 29, 2000); see also Tr. 5/1707.

were not moving very quickly throughout the evening were there simply because they were needed to process the dispatch of value.

In other facilities without TMS, we saw similar examples of people working at manual Periodicals Class bundle sorting operations at a very slow pace. While we did not return to these facilities to view the dispatch of value, it is my assumption that these people were called into action at 5 a.m. to get the final shipment of mail out the door.

In my opinion, there is a great deal of opportunity for cost reduction in flat mail processing if the Postal Service can develop a smooth, efficient process and then place managers in a position to evaluate the performance of the process. The report of the Periodicals Operations Review Team actually states it best:

> While these observations could also apply to operations working mail other than Periodicals Class, it appears to be a significant opportunity for process improvement, and the team believes that focusing on supervisor effectiveness, machine utilization, performance measurement and accountability, and mail flow to process in the lowest-cost method consistent with service requirements would help reduce periodical costs while actually improving service performance.[11]

Issue 9: There appear to be cost reduction opportunities by better utilizing transportation cubic capacities, and by reducing redundant "hot" service trips

On many of our visits to mail processing facilities, the Task Force observed Postal Service contracted or owned trucks that were shipping and arriving half empty. Whenever we asked about truck capacity, the answer was, "We never worry about capacity, there's plenty." We also saw inter-BMC and inter-SCF trucks loaded in a way that used all of the vehicle's floor capacity but substantially less than its full weight capacity. A great deal more product could have been placed on the same vehicles by stacking pallets. In private industry, pallet stacking on shipments is a common practice.

[11] Report of the Periodicals Operations Review Team, at 29.

Witness Unger asserts: "There is a transportation cost that somewhat offsets the value realized in pallets, because pallets take up more space on trucks."[12] I could not disagree more. The President of Hassett Air Express once told me that his company loves handling Periodicals because they have the same density as bricks; that is, magazines provide high weight and low cube (as opposed to boxes of popcorn that have high cube and low weight). Time Inc.'s experience has been that if you stack pallets to a reasonable height, you will exceed the trailer's weight capacity well before you exceed its cube capacity. It doesn't matter if you reach the 2,000 lbs. per floor position by one skid or four small stacked pallets. The bottom line is that pallets don't necessarily take up more space on trucks.

The Task Force also recommended a reduction in redundant "hot" service trips, which Time Inc. supports, because we do not expect hot service trips for our magazines.

Issue 10: Use of annexes to deploy additional equipment and accommodate increased mail volumes results in additional costs, which may fall disproportionately on Periodicals

Periodicals mail volume has remained static for the past 10 years, while overall mail volume continues to grow. As a result of the volume growth and space required for automation, many postal facilities have opened annexes, located anywhere from one block away to several miles away from the main P&DC. Most of these annexes do not have direct transportation to the delivery units. So any product that is processed in an annex must be handled at least twice more than it would if it had continued to be processed at the P&DC.

The Task Force observed Periodicals being shipped back and forth between the P&DC's and annexes and wondered why Periodicals should be responsible for this additional expense. The movement of Periodicals into annexes was not requested by Periodicals mailers, nor was it caused by growth of Periodicals mail volume. So why should Periodicals be paying for it?

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[12] USPS-ST-43, at 5, line 3.

While improved drop shipping tactics along the lines discussed above in Issue 1 will help to reduce transportation into the annexes, the cost of handling and transportation in getting Periodicals back to the P&DC and out to the delivery units will remain. The Postal Service needs to develop a more equitable method of attributing the costs of annexes, since this is one item that helps to drive up Periodicals Class costs.

Issue 11: There is opportunity for cost reduction by more effective utilization of automated flat sorting equipment

On the Task Force's first facility visit, we were told that flat sorting equipment is used 20 hours per day and that the remaining four hours is required for maintenance. This sounded plausible, but we discovered that it is not the case. Each of our visits was scheduled to ensure that we would be in the facility when Periodicals mail was actually being processed. We were disturbed to find that flat sorting machines were often idle or understaffed, in spite of frequent complaints that so many machinable flats are being sorted manually because of insufficient FSM capacity. As we visited more and more facilities with idle FSM's, it became a standing joke that we once again "happened" to arrive during the four hour maintenance period, even though we were scheduled to view peak mail processing periods.

Our observations indicated that FSM's are far from fully utilized. In fact, the Review Team members from the Postal Service were so concerned with the machine downtime that they ran a report showing national FSM run times. We were told that the report indicated FSM utilization nationally at approximately 12 to 14 hours per day. If that is correct, there are six to eight hours of unutilized FSM capacity per machine per day, and FSM capacity is not the reason why Periodicals mail is being processed manually.

The Task Force was also surprised at and disturbed by the amount of time and effort spent preparing mail for automated processing. One facility had someone taking individual pieces from a hamper and sorting them into other hampers based upon their ability to run on automated

equipment. This appeared to be a complete waste of time. In another facility, people were removing shrink-wrap and straps from bundles and placing them on a "Phoenix cart," which would then be wheeled over to an FSM for processing. None of these prep operations was well managed, nor were the people working very hard. In my opinion, these people are once again the personnel buffer for other operations within the P&DC, such as the dispatch of value, yet they will be charged to Periodicals for the majority of their tour.

Issue 12: There may be interclass cost impacts that require further study. What may be the best for the USPS operations' "bottom line" may not be best for Periodicals

The Task Force Report commented:

> In some instances, the team observed costs incurred to separate mail based on machinability. We then observed that all of it was worked manually anyway. While these actions may make sense for all classes taken as a whole, they contributed to periodical [sic] cost without adding value. The Postal Service should study cost causality in these instances to insure accurate marginal cost estimates.[13]

Many facility managers told us that Periodicals mail is often handled manually because it is a short-run product and they would prefer to use the machines for longer Standard A runs in order to reduce setup time for the machines and increase efficiency. As a result, Periodicals are charged with two additional costs: the wasted costs of allied labor used in preparing their mail for automation, and the costs of their actual processing in manual operations, which are slower and involve more labor (and more opportunities for IOCS tallies).

If witness O'Tormey is correct, the coming deployment of AFSM 100s will virtually eliminate this problem.[14] In the meantime, to avoid unfairly saddling Periodicals with mail processing costs that are not incurred for their benefit, the Commission should carefully reevaluate the distribution of mail processing costs, along the lines recommended in the testimony of witnesses Halstein Stralberg (TW-T-1) and Rita Cohen (MPA-T-1).

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[13] Report of the Periodicals Operations Review Team, at 36.
[14] See, e.g., Tr. 21/8364-66.

Issue 13: An immediate step can be taken to publicize and emphasize that cost and service are not mutually exclusive, and both are important

During our facility visits, the Task Force constantly heard that service is the primary reason why Periodicals costs are rising. But our observations persuaded us, to the contrary, that the increasing costs were the result of a lack of focus on costs by Postal Service management. In the final analysis, both are equally important and need to be monitored and managed, and it is often the case that greater efficiency leads to a lower cost and improved service.

In reality, controlling costs and maintaining service are not mutually exclusive. Yet for some reason the Postal Service management feels that they are. For example, witness Unger states:

> Service tends to be a dominant factor in the Postal Service's approach to Periodicals, and it substantially affects Periodicals processing costs. The experience of the last two years is most indicative of that service commitment. In 1997, USPS headquarters initiated a joint MTAC-USPS service task force that worked to identify causes of service problems and remedy those problems. Now in its third year of operation, the service task force has identified and initiated several remedies to fix service.[15]

While I did not directly participate in that task force, I have reviewed some of their solutions, which they refer to as "QI stories." Of all the QI stories, not one has been shown to increase cost. In fact, a number of them actually reduce cost. An excellent example comes from Mr. Unger's area at the Jacksonville P&DC, where the service improvement team developed a process for reducing instances of mail being sent to the wrong facility. This process improvement will not only improve service but produce an annual projected savings of $245,000 in reduced work hours in the Jacksonville facility.

Another QI story from the DVD (Dominick V. Daniels) facility in New Jersey identified misdirected sacks and trays as an item that affected service. The countermeasures adopted to resolve the problem resulted in a savings of $5348, in addition to a service improvement.

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[15] USPS-ST-43, at 7, l. 10.

Clearly, if thoughtful, analytical, process-control approaches are taken to resolving service problems, cost control and service are not mutually exclusive. The task force created a process flow for each facility and then analyzed that flow to determine how the facility could improve service without adding cost, rather than placing a band-aid on service problems, or throwing money or personnel at them. Simply pointing to service does not begin to explain rising Periodicals costs.

One other point in witness Unger's testimony requires clarification. He states:

> Periodicals are time-sensitive, and there is an infrastructure in place to reinforce the importance of service. Mailers regularly (and entirely appropriately) send Postal Service managers reports that score on-time performance for some newspapers and magazines.[16]

Time Incorporated is one of the companies that provide this data to the Postal Service, and there is much more to this program than meets the eye. The program is called DELTRAK, which stands for delivery tracking. The system consists of 700 monitors throughout the country who report the actual day of delivery for Time Inc. titles. The actual delivery dates are compared to USPS service standards, and if a facility meets the standards 70% of the time or better, it is deemed acceptable (just like a passing grade in school). If the facility falls below 70%, Time Inc. adds that facility to our list of problem postal districts, and a Time Inc. Regional Distribution Manager works with the facility to resolve the problem. If for any reason Time Inc. fails to make a critical entry time at the facility, the system automatically changes the scheduled in-home date, so that the Postal Service is not being asked to do more that its service standard requires. I can't understand why being asked to operate within the Postal Service's stated standards should add costs, particularly within the past two years.

I'm very optimistic that the types of initiatives illustrated by the Service Improvement Team's QI stories will continue to expand in the coming months and years as we work with the Postal

[16] USPS-ST-43, at 5, l. 29.

Service to reduce costs throughout the system while simultaneously coming closer to attainment of the Postal Service's stated service standards.

Issue 14: Cost attribution methodologies should be reviewed in light of operational observations

To be honest, cost attribution methodology is not my area of expertise. But here is what the Task Force said in its Report:

> There is strong evidence that in many operations added volume could be absorbed without causing proportional increases in labor cost. It is clear that the capacity to absorb added volume generally varies from one operation to another. Finally, it appears that the cost of allied operations reflects operations to prepare mail for individual piece distribution within the facility as well as operations to transfer mail in bulk to another facility where it may receive individual piece distribution. Hence, further study of allied operations is needed to better understand both cost behavior and the appropriate distribution of cost to the various mail classes and subclasses.[17]

Issue 15: The Periodicals rate structure should be reviewed to ensure that it is consistent with the overall Periodicals processing strategy and induces appropriate mailer behavior

During the Task Force's visits, it was obvious that similar bundles of mail were being handled in a different manner depending upon what type of container they were in. For example, a five-digit pallet entered at the SCF is cross-docked to the delivery unit; a carrier route bundle on that pallet receives no processing at the SCF. An ADC or three-digit pallet coming off the same truck is taken to an SPBS for processing; a carrier route bundle on these pallets would take an entirely different (and probably more costly) route to the delivery unit. Under the current Periodicals rate schedule, the carrier route bundles on the ADC, the 3-digit and the 5-digit pallets would pay exactly the same postage, in spite of the fact that they require different processing and must incur very different costs.

[17] Report of the Periodicals Operations Review Team, at 38.

II. A Rate Grid Model for Periodicals Pricing

Between facility visits, I thought long and hard about what type of rate structure could be developed to more accurately reflect the actual costs of mail processing. The result was the development of a rate grid that reflects all of the various mail processing permutations and combinations. Sufficiently accurate or detailed cost information does not currently exist to permit fully populating the grid with rates that reflect the costs of all of these various permutations. However, the concept of the grid provides, I believe, the right model for future development of correct postal prices that will give mailers incentives to change their behavior in order to minimize combined mailer and Postal Service costs.[18]

The grid begins with a rate cell in the upper left hand corner that reflects the least costly mail that Periodicals Class mailers can submit to the Postal Service, namely carrier route bundles on a five-digit pallet, entered at the Destination Delivery Unit (DDU). At the opposite corner of the grid are non-barcoded pieces in a mixed ADC bundle, in a mixed ADC sack, entered at a printing plant distant from their ultimate destination.

The goal of the grid is twofold: first, to reflect the true cost of each required mail processing operation; second, to allow the Postal Service and the Postal Rate Commission to send very clear pricing signals to Periodicals mailers based upon operational efficiencies or inefficiencies, to the extent that such pricing signals are consistent with the ratemaking criteria of the Postal Reorganization Act.

The grid concept also presents three potential problems. The first is rate complexity. If fully implemented as a ratesetting tool, the grid would produce more individual rate cells for Periodicals Class mail. This should not be a significant burden to Periodicals mailers, however, since the vast majority calculate their postage by computer. Once a mailer's sortation is

[18] ABM, CRPA and McGraw-Hill take no position at this time on the rate grid concept discussed herein.

completed, plugging quantities into a rate grid is a simple, easily automated task. Therefore, rate complexity should not be a substantial barrier to adopting a rate grid for Periodicals Class mail.

The second potential problem is the thorny issue dealt with in the MC95-1 case. In that case, a proposal was made to divide Regular Rate Periodicals mail into two subclasses. One of the subclasses would have received lower rates and the other a rate increase. This resulted in a division within the industry of the "haves" versus the "have-nots". A rate grid would also shift some rates in ways that would help or hurt individual mailers, depending upon their level of mail preparation. While this may seem a drawback and could undoubtedly cause debate within the industry, the fact is that all mailers prepare some mail that is more efficient, and some that is less efficient, than other types of mail. If a grid were employed for postal pricing, all mailers would pay for what they use, but the Postal Service and the Commission would retain the ability to phase in changes or otherwise assure that implementation of this concept would not produce rate impacts that are too severe.

The third potential problem with a rate grid is that, in order to populate the cells of the grid, there must be concerted efforts to refine and make more accurate the distribution of in-office costs and the mail flow cost models used in rate design.

The costs to the Postal Service for more and less efficient mail need to be passed along to mailers in a manner that causes them to react to those costs and, where necessary, improve mailing practices. A grid would show the true cost of each operation and provide the mailing industry with a clear incentive to change behavior. It is my firm belief that a number of desirable industry changes would take place, given the proper rate structure. These include a significant increase in DDU deliveries, co-mailing, co-palletization, and drop shipping by a great many Periodicals. To verify this prediction, one simply needs to look at Standard A. Correct rate incentives have produced a substantial increase in drop shipping, and equipment manufacturers are now

producing flat sorting machines so that lettershops can merge separate mailings into one mail stream, a practice that will improve presort for all mailers in the co-mailing pool.

Over my years in the printing and publishing industry I have observed that very little change takes place without the proper financial incentives. If Periodicals class mailers and the Postal Service truly want to lower the costs of the system, there needs to be an incentive. A rate grid approach could provide the type of rate structure that would cause desirable changes in mailing practices.

The following page illustrates how a rate grid could be structured:

PERIODICALS CLASS RATE STRUCTURE DISCUSSION DOCUMENT

PIECE	BUNDLE TYPE	CONTAINER	ENTRY				
			DDU	SCF	DESTINATING TRANSFER HUB	ORIGINATING TRANSFER HUB	OTHER
NON-BARCODED	CARRIER ROUTE	5 DIGIT PALLET					
NON-BARCODED	CARRIER ROUTE	CARRIER ROUTE SACK					
NON-BARCODED	CARRIER ROUTE	5 DIGIT SACK					
NON-BARCODED	CARRIER ROUTE	3 DIGIT PALLET					
NON-BARCODED	CARRIER ROUTE	SCF PALLET					
NON-BARCODED	CARRIER ROUTE	ADC PALLET					
BARCODED	5 DIGIT	5 DIGIT PALLET					
BARCODED	5 DIGIT	5 DIGIT SACK					
BARCODED	5 DIGIT	3 DIGIT PALLET					
BARCODED	5 DIGIT	3 DIGIT SACK					
BARCODED	5 DIGIT	SCF PALLET					
BARCODED	5 DIGIT	SCF SACK					
BARCODED	5 DIGIT	ADC PALLET					
BARCODED	5 DIGIT	ADC SACK					
NON-BARCODED	5 DIGIT	5 DIGIT PALLET					
NON-BARCODED	5 DIGIT	5 DIGIT SACK					
NON-BARCODED	5 DIGIT	3 DIGIT PALLET					
NON-BARCODED	5 DIGIT	3 DIGIT SACK					
NON-BARCODED	5 DIGIT	SCF PALLET					
NON-BARCODED	5 DIGIT	SCF SACK					
NON-BARCODED	5 DIGIT	ADC PALLET					
NON-BARCODED	5 DIGIT	ADC SACK					
BARCODED	3 DIGIT	3 DIGIT PALLET					
BARCODED	3 DIGIT	3 DIGIT SACK					
BARCODED	3 DIGIT	SCF PALLET					
BARCODED	3 DIGIT	SCF SACK					
BARCODED	3 DIGIT	ADC PALLET					
BARCODED	3 DIGIT	ADC SACK					
BARCODED	3 DIGIT	MIXED ADC SACK					
NON-BARCODED	3 DIGIT	3 DIGIT PALLET					
NON-BARCODED	3 DIGIT	3 DIGIT SACK					
NON-BARCODED	3 DIGIT	SCF PALLET					
NON-BARCODED	3 DIGIT	SCF SACK					
NON-BARCODED	3 DIGIT	ADC PALLET					
NON-BARCODED	3 DIGIT	ADC SACK					
NON-BARCODED	3 DIGIT	MIXED ADC SACK					
BARCODED	ADC	MIXED ADC SACK					
NON-BARCODED	ADC	MIXED ADC SACK					
BARCODED	MIXED ADC	MIXED ADC SACK					
NON-BARCODED	MIXED ADC	MIXED ADC SACK					

NOTE: ALL PIECE RATES ARE SUBJECT TO THE EXISTING EDITORIAL PIECE DISCOUNT FORMAT FOR ADVERTISING AND EDITORIAL WEIGHT REMAINS THE SAME AS TODAY.

It should also be noted that costs for many of the grid cells needed to be calculated in order to develop the cost savings projections being submitted by witness Cohen. Christiansen & Associates, in conjunction with the Postal Service and industry, prepared the grid data used in witness Cohen's testimony.[19]

While I fully understand that it is not possible to implement a grid structure in Docket No. R2000-1, the Commission, the Postal Service, and the publishing industry should be thinking along these lines for the future.

III. Additional Developments Since the Report of the Periodicals Operations Review Team

Since the issuance of the Report of the Periodicals Operations Review Team in March 1999, I have observed two encouraging developments. First, Harvey Slentz, Manager of Strategic Operations Planning, U.S. Postal Service, and Co-chair of the Periodicals Operations Review Team, told me that in his 20 plus years with the Postal Service, he has never seen the organization so energized by a single issue as it is today by Periodicals costs. His observation has been reinforced by the numerous follow-up meetings and conference calls I have participated in with the Postal Service in an effort to forge ahead with cost evaluation and implementation of the Review Team's recommendations. This single-minded focus should translate into cost saving ideas and new lower cost processes for Periodicals Class mail.

The second key development has been the support of Postal Service senior management. On February 9, 2000, the Postal Service hosted a six-month review meeting with the Periodicals Operations Review Team, where Postal Service employees presented a status report on the progress of each of the team's fifteen recommendations. Postmaster General Henderson, other top executives of the Postal Service and senior managers from the publishing industry attended this meeting. It was obvious that people from the Postal Service and industry are serious about

[19] See LR-I-332 (filed May 15, 2000).

change and committed to implementing the recommendations. This type of cooperation and commitment at the senior management level is critical to achieving our cost control goals.

Summary

The Periodicals Operations Review Team invested a great deal of time and effort in attempting to determine why Periodicals costs are rising so rapidly. While there is no "silver bullet" solution to the problem, we developed a host of realistic recommendations that could help reverse this trend. It is unfortunate that we could not develop the related cost savings for these initiatives prior to the rate case, so that the Task Force's recommendations could have been included in the Postal Service's proposal. However, it now appears that we have the full attention of Postal Service management and that change is taking place very quickly in an effort to implement many of these recommendations prior to the test year.

It is my understanding that testimony from Rita Cohen, representing a broad coalition of Periodicals mailers, will provide supporting cost data for their recommendations. I hope our testimony will demonstrate to the Commission that the savings are realistic and can be implemented by the test year for this case. More importantly, the changes recommended by the Review Team need to form the basis for a change in behavior when Periodicals Class mailers prepare their mail, not only when the Postal Service processes it. No business can tolerate 15% rate increases every two years. The Postal Service and the publishing industry are cooperating to remove costs from the system in order to end the years of excessive Periodicals cost increases. But more needs to be done, by following up on the Review Team recommendations, carefully evaluating the fairness of the current Postal Service method of distributing mail processing costs, and exploring the possibilities of a rate structure that reflects actual costs and thus encourages economical mailing practices.

CERTIFICATE OF SERVICE

I hereby certify that I have this day served the foregoing document on all participants of record in this proceeding in accordance with section 12 of the Rules of Practice.

Timothy L. Keegan

May 22, 2000