

Remarks of
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POSTAL RATE COMMISSION
before the
MAIL ADVERTISING SERVICE ASSOCIATION
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Good morning, ladies and gentlemen. It is an honor and a pleasure to speak to you today. My thanks to the Board for extending this opportunity to me.

I will talk to two subjects today. I will, briefly, discuss the Postal Rate Commission: its responsibilities and procedures. Then I will give you impressions of the major developments in the postal world. Some of these developments are significant; some are less so. All are interesting.

Let me begin with the Postal Rate Commission for the benefit of those of you who don't know who we are or what we do.

Our responsibilities are straightforward, but not simple.

In 1970, the Postal Reorganization Act was passed by Congress. This act created the United States Postal Service and also the Postal Rate Commission as an independent, federal regulatory commission. Our functions are similar to those of a public service commission , but we are somewhat larger than most. There are five commissioners, appointed by the President and approved by the Senate. Our staff is approximately 50 and our budget is about \$5 million.

In pre-1970 days, Congress set postal rates. But since it was decided to remove politics from the ratemaking process, the Postal Rate Commission was established. It is our job to recommend rates to the Postal Board of Governors and I emphasize the word recommend because the Governors have the right to accept, reject or modify our recommended rates. In my opinion, however, the Postal Reorganization Act's objective to depoliticize the postal system would have been better met if the Postal Rate Commission had final ratemaking authority.

In any event, we are required by law to make our recommendations within a 10-month period. Although this sounds like a long time, it is not, if we are to be the independent forum that Congress envisioned us to be. If we are

to allow all parties ample time to present their cases then we must give everyone a chance to have their say.

In determining our recommended rates, we must accept the Postal Service's stated requirement for revenue. This is a "break even" requirement. The PRC, in establishing rates, must provide enough money for the Postal Service to break even. When rates are reduced for one class of mail then the rates of another class must be increased. The process is zero-sum. You should understand that it is the Board of Governors who determine the revenue requirement and the timing of rate increases.

In setting our recommended rates, we are guided in our decisions by nine criteria established by Congress. As I list these criteria, I ask you to consider whether these are the criteria that underlie the decisions that you as businessmen must make. I raise this point because I don't see how you can consider the Postal Service a business so long as these criteria govern its pricing. I will list these criteria without explanation at this time. They are largely self-explanatory. Should you wish further clarification, I will provide it during the question period. Here are the nine criteria for setting rates:

* Fairness and equity.

- * Value of service to sender and recipient.
- * Costs.
- * Effect on business users and general public.
- * Available alternatives.
- * Degree of mailer preparation.
- * Simplicity.
- * Educational, cultural, scientific, and informational value.
- * Other factors the Commission deems relevant.

You should know that there are also six other criteria that are to be used in considering classification issues. They are not unlike the criteria used in setting rates. Others would like us to disregard these criteria in our considerations. We cannot. We are obligated by statute to carefully consider them. It isn't easy. After all, what is "fair and equitable"?

Our Commission is far from the rubber-stamp organization some people would like it to be, but rather we are five independent individuals.

The way the process works is that the Postal Service proposes rate increases for all classes of mail that will generate enough revenue so that they supposedly will break even over time. This revenue request is based on projected costs and is not done arbitrarily. The Commission analyzes the

costing and volume projections to correct errors, but we may not tell the Service how it should spend its money.

It is the Postal Rate Commission's job to attribute to each class of mail those costs that we find are caused by each class of mail. These are called attributable costs. What is left over are called institutional or overhead costs, nearly 35% of total costs.

Based on evidence presented by the Postal Service, the mailers, and other interested parties, the Commissioners must apply the nine criteria that I mentioned earlier to decide how these institutional costs are to be distributed to each class of mail. I think you can see that this is where the rub comes between us, the Postal Service, and certain mailers.

Now, let us move on and talk about the developments in the postal world over the past several years.

First, let us look at performance - delivery standards, and financial management. After all, these are the bread and butter of the Postal Service. As an aside, I have always considered the Postal Service to be in the delivery business - We Deliver For You - seems to sum it up. However, the Mr. Runyon insists that the Postal Service is in the communications business. I am not sure.

Is Allied Van Lines in the furniture business? They sure deliver a lot of furniture.

Delivery is up. At least, overnight First Class is up nation- wide. Second and third day delivery is spotty and the Board of Governors recently directed the PMG to get these numbers up. I am sure that they will. But it isn't easy and patience is probably a virtue here.

For the standard classes of mail, we really don't know. To the extent that the Postal Service measures service performance in these classes, we don't know and the Postal Service isn't telling. However, there are indications that the delivery of standard mail is not what it might be. In a recent issue of Postal World, the results of a survey of delivery performance of Standard A, drop ship mail conducted by Hauser List Service indicates a wide variation in delivery days among BMCs, ranging from 2.3 days to 9.5 days. although one would expect that the Service would tell you the level of service that your are actually receiving, it may be that the mailers themselves will have to police delivery performance of standard mail.

The financial position of the Postal Service has improved dramatically in the past two and a half years. On January 1st, 1995, the effective date of the last across the board rate increase, the Postal Service had a negative net equity

of over 8 billion dollars. Today, it is approximately a minus 1.6 billion dollars. That is a tremendous improvement. Costs have been cut and increases in volume, especially in Priority Mail, are the explanation. Curiously, increased productivity has had little to do with this performance, and that is because that there has been almost no productivity growth since 1994. We are all waiting to see the pay off in the Postal Service's major investment in automation.

The PRC and the Postal Service have been working on the most comprehensive reclassification of the mail in this century. We still have the parcel classes to evaluate, and that should occur during the next rate case. I am not sure of how you regard these new classifications and the new requirements for work sharing discounts. From my perspective, it appears that the big volume mailers have been the primary beneficiaries. What we have today will change over time. Of this, I am certain.

Since the Postmaster General arrived in 1992, there has been a constant drumfire of criticism of the way the Postal Service rates are set. And we are talking primarily of the PRC here. The Postmaster General wants more flexibility (or independence of the PRC rate setting process) to set prices, to institute new services and to negotiate discount contracts with major mailers. He also wants to change the way that labor negotiations are conducted.

For the last two years, the House subcommittee on the Postal Service has held hearings under the auspices of the subcommittee chair, Congressman McHugh. In the last year, hearings have been held on his draft bill. There have been literally dozens testifying: large mailers, small mailers, presorters, newspapers, the Postal Service, the PRC and others. The results have been inconclusive - there is little real interest in the nation at large for major reform.

Whatever the short comings of the present system, people (and Congressmen) are inclined to stay with the devil they know rather than risk the consequences of a devil they don't know. Personally, I don't believe that there will be any major Postal reform legislation in the foreseeable future.

Unfortunately, representatives of some of the major mailers are busy trying to create an aura of crisis in the relationship between the PRC and postal management with the intent to justify major reform legislation. They state that there is bad blood between the PRC and postal management and the rate setting process is broken. There is not bad blood, at least on our part. And the process is not broken. In fact, it has never worked better in the past three years. An omnibus rate case, R-94, major reclassification, two experimental programs, and other postal requests have been handled expeditiously. In almost every case, in less time than allowed under current procedures.

Certainly, we have our differences. The law which governs postal rate setting almost guarantees an adversarial relationship. Those nine criteria which govern our deliberations often put us on a collision course.

Discussion of possible reforms have centered on two “fixes” to whatever the postal problem may be. The first fix is privatization. The second is control of postal rates through rate caps.

As to privatization, it is the Libertarians and those with a passionate belief in the free enterprise system that espouse the privatization of the Postal Service. Their views are not new, and although there are always fresh analyses of the virtues of privatization; there is in the nation no ground swell of support for these ideas.

The second approach is the regulation of rates through price caps on postal rates which would limit the amount postal rates could increase from an established base rate - to be established initially by an omnibus rate case. These caps would be adjusted every so often based on inflation indices. Every five or so years there would be an omnibus rate case to readjust rates according to postal costs. The fundamental virtue of caps would be to increase efficiency by increasing Postal Service flexibility. However, is interesting that the consensus

of a group of economists recently testifying before Congressman McHugh was that caps won't work for the Postal Service as presently constituted.

One of the provisions of the proposed legislation that has been generally overlooked in all of the discussion about the caps would give the Postal Service authority to give volume discounts, contract rates and negotiated service agreements. Authority that the Service wants in the worst way.

And who would benefit most from such reductions in rates? Surely the mega mailers would be first in line. Unless there is a large increase in volume to compensate for the lost revenues, reductions would be paid for by the other elements of the mailing community. Remember, the Postal Service is zero sum in its revenue requirements.

Now, I think that it is too late in the legislative game for this to happen this year. But maybe next year. Stay alert and read the fine print in any proposed reform legislation. Your financial well being is at risk.

But before I leave the issue of legislative reform, I want to share a question that I believe has been ignored in all of this discussion. What does reform, of whatever nature, have to do with the challenges that that are used to justify legislative reform? Will reform reduce the number of faxes, the number

of e-mails? Will there be fewer electronic funds transfers? A figure expected to grow by 12 billion in the next several years. Will postage rates go down? Will reform cause a dramatic increase in volume? Will there be dramatic increases in productivity? Will the loss in market shares be reversed? Maybe, but no where have I seen any analysis to support these possibilities.

At the recent Postal Forum in New Orleans, PMG Runyon is quoted as saying: "The Postal Service has come a long way in the past three years. We have taken overnight service scores to record levels. We have delivered financial surpluses beyond compare. We have moved forward with new technologies, overhauled the way we bring you products, and strengthened our product lines with more features and more choices." As Runyon was speaking, Postal Governor Einar Dyrkopp in an interview with the Washington Post said that the agency needs better management not legislation to steer it clear of problems. He went on to say that everyone just needed to do a good job under the current framework and all would be fine. The Governor concluded that the current effort to get legislation passed is an attempt by Runyon to privatize the Postal Service. I think that they are both right.

As to the future, I would suggest to you that if the Postal Service focuses on its primary responsibility of delivering the mail, and if they do it right, it will be hard to beat them. I am not saying that volume will forever increase, or that the Postal Service will always be as important to the nation's economy as it is today. But I do say that as long as there is mail to be delivered the Postal Service will be the organization of choice, provided it remains concentrated on its motto: We Deliver for You.

I am bullish for the long range future of the Postal Service. I am bullish because there are so many important players in the postal community, such as yourselves, who will loudly and frequently remind the Postal Service, the Congress and the PRC, should it go astray. The Postal Service is a 900 pound gorilla. It some times takes a big bat to get its attention. Keep swinging. Thank you so much for your attention. I will be pleased to answer your questions.