The Honorable Edward J. Gleiman

Speech

Before the

Graphics Communications Association

Chicago, Illinois

December 6, 2000

Good morning ladies and gentlemen.

This is the third time I have participated in a Graphics Communications Association conference.

My first GCA conference was in February of 1997, the 17th to be precise, in Coral Gables, Florida. Norm Scharf lured me to Florida with promises of sunshine, warm temperatures and the chance to follow Gene Del Polito on a panel. It was cloudy, the temperature never got above 45 degrees Fahrenheit and, after listening to Gene proselytize about postal reform, I tried to enlist!

Earlier this year, Norm invited me to the April 14th GCA conference in Clearwater, Florida. “How could I resist,” he asked, “ a chance to get a head-start on my summer tan?”
It rained---the entire time!

When Norm called in June to ask if I would participate in an R2000-1 postmortem conference, I agreed on the condition that (1) I speak before Gene and (2) that I not be subjected to Florida’s erratic weather.

Norm, I see that Gene’s performance is tomorrow---afternoon. So, I want to thank you on meeting my first condition.

On your meeting my other condition, what can I say Norm but thank you. It certainly is a pleasure to be here in Chicago---in December!

Now before you get upset with me, I think you need to know the real reason we are in Chicago---in December. How many of you know Neal Denton? Neal who is on the program tomorrow---with Gene---is rabid. Oops, I mean he is a rabid baseball fan. So much so that he tries to see at least one game at each major league diamond every year. Well, as I heard the story, Denton was leaning into the plate in fantasy baseball camp last winter when he took a high, inside, fast ball on the head. Ever since he has been more confused than usual. Apparently he thought the Cubbies and the Chisox had a home and home inter-league series this week. So, he convinced Norm to hold the conference out here so he could get a "two-fer" on that every ballpark every year deal.

By the way, for those of you who want the straight skinny on why I'm leaving the Commission, that's Denton's fault, too! He told me that there is a "three strikes and you're out" rule for commissioners on omnibus rates cases. And, judging from the comments some of you have been making, it appears that I didn't make it to first base in the R2000-1 game. I've got to tell you, though, that most industry comments pale by comparison to some of the suggestions I received from the general public on what I can do with the 34 cent stamp.

Seriously, though, I know some of you are not all that happy with a number of the Commission's recommendations. I will speak to some of the concerns of which I have become aware. And, while I do not mean to suggest that I view anyone's concerns as being parochial, I think it might be useful to set the broader stage of postal ratemaking---to lay out the general principles that guide the Commission's conclusions. I also plan to spend a few minutes discussing the state of USPS finances and mention a couple of other matters of more than passing interest---at least to me, and I hope to you.

The law that established the US Postal Service in 1970 provides that the Postal Service may, from time to time, request that the Postal Rate Commission recommend "rates and fees [that] shall provide sufficient revenue so that the total estimated income…to the Postal Service will equal as nearly as practicable the total estimated costs of the Postal Service."

But the Commission isn't free to make just any old recommendations so long as the numbers add up. It has to act in accordance with the general policies set forth in the Postal Reorganization Act and nine specific ratemaking factors.

§ 3622. Rates and fees

(1) the establishment and maintenance of a fair and equitable schedule;

(2) the value of the mail service actually provided each class or type of mail service to both the sender and the recipient, including but not limited to the collection, mode of transportation, and priority of delivery;

(3) the requirement that each class of mail or type of mail service bear the direct and indirect postal costs attributable to that class or type plus that portion of all other costs of the Postal Service reasonably assignable to such class or type;

(4) the effect of rate increases upon the general public, business mail users, and enterprises in the private sector of the economy engaged in the delivery of mail matter other than letters;

(5) the available alternative means of sending and receiving letters and other mail matter at reasonable costs;

(6) the degree of preparation of mail for delivery into the postal system performed by the mailer and its effect upon reducing costs to the Postal Service;

(7) simplicity of structure for the entire schedule and simple, identifiable relationships between the rates or fees charged the various classes of mail for postal services;

(8) the educational, cultural, scientific, and informational value to the recipient of mail matter; and

(9) such other factors as the Commission deems appropriate.

Factor number three deserves special mention as it is the mandatory factor. It is at the heart of many a difference of opinion between the PRC and the Service, the Service and mailers, mailers and the PRC, and between groups of mailers. It is the factor that causes the Commission to examine all operational costs, from collection to delivery and the processing that takes place in between. It is the bedrock on which rates are based. ***Each subclass must generate sufficient revenue to cover its costs***. This policy is important for another reason. It, combined with factor number six, forms the basis for the many, important work-sharing discounts that are on the books.

It seems to me that, at times, critics of Commission recommendations tend to take lightly the considerations embodied in 39 USC 3622(b)(3) and (6). "How come," they ask, "did we wind up with an increase that was larger than that proposed by the USPS, when almost everyone else got a break?"

There are usually a number of reasons that situations like this occur. For example, the Commission believes that costs vary more directly with volume than does the USPS. As a consequence, the PRC costing methodology generally attributes a larger portion of total operating costs than does the Service.

But why not even things out by ignoring cost differentials between, say, letters and flats; cost differential put on the table by the USPS a decade ago? Why not just look the other way on these cost differences, or level the playing field by passing on to some mail 300 percent of costs avoided by work-sharing? Why not give discounts based on cost avoidances promised in a previous rate or classification case but which savings were never captured by the Postal Service? Because it is one thing to encourage work-sharing, but quite another to ignore the law, and give revenue away. And, giving away revenue has an effect.

Keep in mind the requirement that a subclass has to generate revenue to cover its costs. Now, what happens when we give excessive discounts for some type of mail? Simple! We have to make up the revenue from other mail, for example, by bumping up, if you will, the benchmark from which those discounted rates are measured.

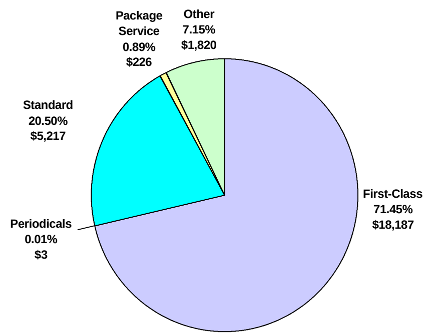
One rather formidable group of mailers whose members will benefit mightily from the Commission's recommendations, the periodicals mailers, pointed out in a press statement that the overall average increase for First-Class mail was much smaller than the average increase for mail their members send. Does it matter that the cost of processing their mail went way up and the cost of processing First-Class mail declined? Yes. By law, it must matter to the Commission!

What if the Commission chose to ignore this divergence in costs and hit First-Class mail with a larger increase? Whose interest would be served by our doing so and for how long?

PRC R2000-1

(Dollars in Millions)

Total Contribution to Institutional Costs: $25,453



	Percent Volume	Percent Revenue	Percent Contribution to Institutional Cost
First-Class[1]	51.4%	61.7%	71.45%
Periodicals	5.0%	3.5%	0.01%
Standard	42.4%	23.3%	20.50%
Package Service	0.5%	3.1%	0.89%
Other Mail	0.7%	8.4%	7.15%
Total	100.0%	100.0%	100.00%

1/ Includes Priority Mail

I want you to take a moment to look at this pie chart. I think it is important for everyone to understand the extent to which First-Class mail is already carrying a disproportionate share of the institutional cost or overhead burden of the postal system. Now, forget about this rate case and put aside any notion that I am suggesting others mailers should pay a larger share. Think instead about the discussion---the hand wringing--- that has been taking place since the fall of last year when the General Accounting Office unveiled an assessment prepared for the Postal Service by a Postal Service contractor concerning the extent to which transaction mail---First-Class mail---is likely to fall prey to electronic bill presentment and payment. Should we load up on that type of mail---give it heftier increases? Might not doing so just accelerate the departure of this mail from the system? When that mail leaves the system, who gets to eat that big slice of the institutional cost pie that First Class mail currently enjoys?

Now, remember a few minutes ago when I talked about the Commission and Postal Service difference of opinion on the matter of how costs vary with volume? In the USPS view of the world, institutional costs are a larger share of total costs and fewer costs can be expected to be shed, if and when, say, transaction mail leaves the system. This means, potentially, an even bigger slice of institutional pie for someone else---one of you, to swallow. Not a pleasant prospect and not one easily avoided---not even by any reform package or proposal that I've seen.

Well, I guess I have already crossed the line and gotten into some specifics of the R2000-1 case. And, I did not paint a horrific picture of the future, just so you might think the present PRC recommendation ain't so bad, after all. However, before I lose the forest---and a very important one it is---for the trees, I want to step back a bit.

In my almost seven years at the helm of the PRC, if I have learned nothing else, I've learned that each case presents a new challenge. In this case the challenge lay in evaluating the Service's request for additional funds over and above its expected operating expenses.

Last January the Postal Service proposed an array of rate increases designed to generate an additional $2.8 billion in revenue. What was unusual about this request was that roughly $1.7 billion of these dollars was for a contingency, a hedge against the unknown---to cover unforeseen events. Another quarter billion plus dollars of the total amount sought was earmarked to pay down operating debt accrued in past years.

The size of the contingency quickly became a cause celebre with many parties to the rate case. They sponsored evidence challenging the need for a cushion so substantially above and beyond the Postal Service's own best estimate of future increases in the cost of collecting, processing and delivering the mail.

And, as you probably know, in presenting estimates of its future needs, the Postal Service used financial and operational data from fiscal year 1998 as a benchmark. Unfortunately, by the time the Service filed its request, fiscal year 1999 had already come and gone. The Commission requested and the Postal Service completed an update of its original cost projections in mid-July.

To give you a flavor of the impact of this updating effort, which allowed the Commission to use more recent information than was in the Service's initial package, let's look at a few of the changes:

- Notwithstanding the comments of one of the Postal Governors at the November Board meeting about not being able to recover increased fuel costs and the need for flexibility to permit them to level a fuel surcharge, the USPS was able to factor into the update the increased costs of fueling its delivery fleet.
- Despite the comments of a Governor concerning costs associated with the NALC arbitration, the USPS was able to include these additional labor costs in the update.
- It also was able to take account of the dollars associated with actual cost-of-living adjustments, health insurance and the like, which were higher than earlier projected figures.

But the update was not one-sided, only adding new costs, some $450 million. The Postal Service also presented additional revenue and costing-cutting initiatives, such as the billion-dollar-a-year "break through productivity plan" announced by the Postmaster General this past spring. Unfortunately, the Postal Service was only willing to commit to saving slightly more than one half the highly publicized, promised amount.

The one item that did not change in the Postal Service update was the contingency. The $1.7 billion remained.

The many parties who had already argued that a $1.7 billion contingency was unreasonable before the update, were absolutely certain that amount was unjustified given the incorporation of new cost data and shorter time frame for prognosticating.

The evidence presented by the parties on the contingency issue was determinative. My colleagues and I, reduced the requested amount by $700 million, leaving a $1 billion contingency. We concluded that this amount more than met the reasonableness standard of the law.

Now, you should know that I put these remarks together over the weekend, before the December board meeting that took place Monday and Tuesday of this week. So, I had no idea of what action the Governors might take. It would not surprise me, however, if the governors returned the case because we cut the contingency, if for no other reason than that the USPS views the contingency as its private sandbox and doesn't want the PRC playing there. Nevertheless, I think the Governors should be quite happy with a billion dollar contingency since, after all, at the board meeting---at least some of the Governors apparently did not even know there was a contingency provision. One Governor is said to have remarked at the public meeting that he thought the Postal Service needed some mechanism for recovering unforeseen expenses!

You have already heard the doom and gloom projections about USPS finances generally and about this Recommended Decision not providing the Postal Service with sufficient revenue to breakeven in the current fiscal year. But think about this: if rate increases are implemented in January---which the Service has indicated is likely---and the Service's best estimate from just this past July is on target, the Postal Service should be sitting on a sizable cushion at the end of this fiscal year. Put another way, based on the evidence the Postal Service put on the record during rebuttal hearings as recently as this past August 30th, in the absence of the occurrence of unforeseen events costing more than---the portion of the full $1 billion contingency earned when new rates are implemented in January, $600 million, the Service should do quite well with what we recommend.

This is, I believe, a good point to do a comparison of the evidentiary record the Commission based its decision on and the financial picture postal officials are now painting just three months later.

UNEXPLAINED CHANGE IN USPS FY 2001 FINANCIAL POSITION
($ Millions)

	Effect on FY 2001 Net Income	FY 2001 Net Income (at USPS Proposed Rates)	
USPS Original Filing - 1/12/00		1,948	
Update per Order No. 1294 - 7/7/00	(425)	1,523	
Impact of Jan 2001 Delayed Rate Implementation	(892)	630	(at PRC Recommended Rates) 132
Operating Plan - 11/14/00 (Expected Net Loss)		(480)	(978)
Unexplained Swomg in Net Income (7/7/00 compared to 11/14/00)		$\boxed{\textbf{(1,110)}}$	**(1,110)**

UNEXPLAINED CHANGE IN USPS FY2001 FINANCIAL POSITION
($ Millions)

Net Income PRC R2000-1 Rate Decision - 11/13/00	1,342
Impact of Jan. 2001 Delayed Rate Implementation	(658)
Adjusted FY 2001 Net Income	684
Operating Plan - 11/14/00 (Expected Net Loss)	(480)
Unexplained Swing in Net Income: (11/13/00 compared to 11/14/00)	(1,164)

I have a couple of tables I want to share with you. Each carries the title "Unexplained Change in USPS FY 2001 Financial Picture."

The first table is based on USPS assumptions regarding rates, costs, volumes, contingency and recovery of prior years' losses.

- When the Service filed its case last January, we all were told the net income for FY2001, after covering increased operating costs, would be $1.9 billion---$1.7 billion for the contingency and $250 million for recover of prior years losses.
- When the Service filed its July update, which it could have modified during rebuttal in late August, we were told the net income for FY2001 would be $1.5 billion.
- When you adjust those figures for a January implementation, you get a positive $630 million on the bottom line.
- But the USPS operating plan presented to and approved by the Board in mid-November shows a deficit of almost $500 million even if the Commission had rubber-stamped the original Service request.

- When ones substitutes generally lower PRC rates and uses all other USPS assumptions, one still gets a positive, albeit much smaller, bottom line---the $132 million figure.
- Going from a plus $630 million to a minus $480 million is a swing of $1.1 billion.

The second table shows the numbers using PRC assumptions and recommended rates.

So, regardless of whether one uses the Service's updated assumption or the Commission's rates and assumptions, there has been an unexplained swing of $1.1 billion in the projected bottom line for FY 2001 in just a couple of months!

- Were the July-August updates that far off target? We now know one figure, the FY2000 ink was not as red as the USPS thought it would be---the loss is $199 million as opposed to the $325 million they projected last July. But that's good!
- Are the November operating plan figures wrong?
- Has that USPS commitment for half the promised "break though productivity" fallen through?
- Has something else happened?
- If so, what is the explanation?

I know that some of you are unhappy with the Commission's recommendations as they relate to your mail. I don't mean to be glib about your concerns, but if I were you, I might be more concerned about the near-term rate implications of this $1.1 bottom line swing. For those of you who have only disdain for the current ratemaking process---the length of time it takes and the cost of litigation---please keep in mind that the PRC process affords the only opportunity you may have to truly scrutinize this swing before you get the next $1.1 billion plus kick in your billfold.

Now, about our recommended rates:
Could we have made different recommendations? Most certainly!
Would they have been better recommendations? Maybe!

But let's look at the score card on how the several classes made out:

- By our count, roughly 87 percent of Standard mail will have rates that are less than or equal to those proposed by the Postal Service.
- Almost all Periodical mail rates will be lower than those proposed by the Postal Service.
- The average increase in Parcel Post, save the not so small matter of a non-machinable surcharge that impacts about 3 percent of total volume, is on target with the USPS request.
- Priority Mail, Bound Printed Matter and Media Mail---gosh I'm having a hard time keeping up with all these name changes---took a bit of a hit, 1 percent more, give or take, than the USPS requested, based primarily on cost updates.
- Nonprofits benefited from last minute legislation and will have smaller increases than would have otherwise been the case.

However, we did not, as you know, lower the Standard pound rate as much as the Service wanted and we did not raise the breakpoint. To those who choose to be supercritical of the Commission regarding our recommendations in these areas, I hope you will consider that ratemaking generally involves a zero sum situation where one works against a revenue target. Lowering pound rates or raising breakpoints may benefit some mailers, but it will also have a negative impact on others who find themselves dealing, for example, with higher piece rates and the like.

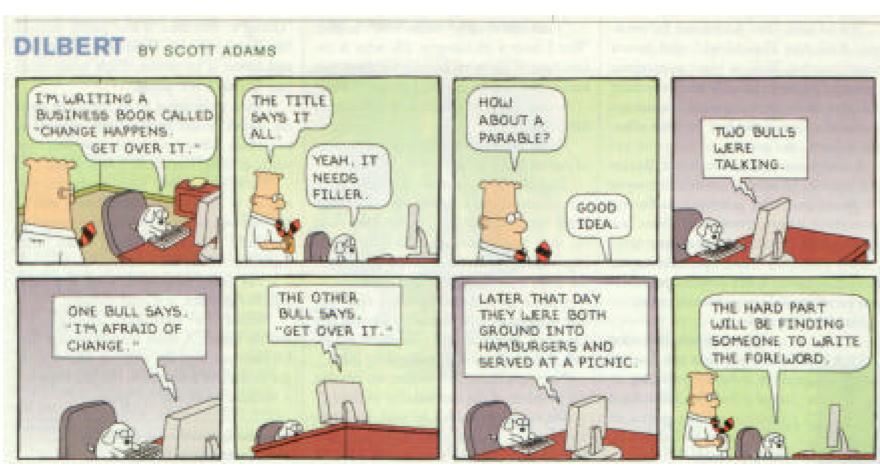
I have a host of one-liners I've collected over the years that I thought about using at this point in response to some of these critics who think we missed a "no-brainer," but I won't do that. One will suffice. It's the one that comes to mind when I think about how smart I was before I actually had to deal first hand with an omnibus rate case. It's the H.L. Mencken line I've used before: "For ever problem there is a solution that is simple, neat, plausible and wrong!"

Let's see now, where am I?

- Lay out guiding principles. Check!
- Talk about rate recommendations. Check!
- USPS finances—the $1.1 billion swing. Check!
- Saw barrel off shotgun and fire at critics. Check!
- I'm forgetting something. Ah, those other matters of passing interest.

I'll try not to take too long, but I get to do this because this may be my last shot as Chairman of the PRC. And, you know what they say---Today a peacock tomorrow a feather duster!   So, here goes-

(1) Postal or legislative reform or whatever you want to call it: I am NOT opposed to postal reform! I just believe, to quote his February 28, 2000, MIDS article, that that great American, Mr. Cary Baer, had it right when he said, "Before we develop solutions we need to reach some consensus on the problem." We've all got our campaign ribbons from the war of HR22. Some people want to pick up that very tattered battle flag, put on their brightest red coats, form into straight lines and march one more time up Jenkin's Hill. For those of you who may not know, Jenkin's Hill is the hill on which sits the U.S. Capitol. Price caps may sound more attractive with every passing rate case. But, as I have tried to explain to some of you, costs trumped caps in HR22; that is, you were still likely to see increases akin to those you



experience under current law. I propose that, rather than charging up the same hill with the same old, tired ammunition, let's all of us regroup---and rethink.

Dilbert kind of sums it up for me when it comes to postal reform.

(2) A better bet for legislation in the 107th Congress, and one that may be as important to the postal community as some perceive postal reform to be, is in the privacy area dealing with the collection and sharing of personal data. This is an area I know a bit about from a previous incarnation as the point man on information policy at the then Department of HEW in the 1970s. Overly restrictive privacy legislation at the federal level or, even worse, 50 different restrictive state bills could spell disaster for everyone up and down the chain from graphics and copy people to printers to cataloguers to envelope manufactures to banks and to shipping and logistics companies. You've got a split congress and an issue with bipartisan appeal. Convincing conservatives of the benefits of federal preemption and liberals of the benefits of limiting causes of action, both stumbling blocks in the past, might be doable as 107th searches for common ground. The result could be a framework everyone can live with.

(3) Negotiated Service Agreements.   Setting aside for the moment the pros and cons of notice versus pre-approval, for some time now I have been preaching that NSOs are by and large nothing more that narrowly drawn or niche classifications. We've already approved several such USPS proposals. I urge the Service to move forward with whatever proposals they have developed. If mailers, a small group of or even one of them, can perform some task that may drive costs out of the system, let's get on with it---now!

(4) And last but not least, another Ed Gleiman suggestion---I try to include at least one classification and/or cost savings proposal in each speech. This one is buried in a

concurring opinion to the R2000-1 decision. Certified Mail is costly to the Postal Service and the consumer. Along with Return Receipt, also not cheap, these old-fashioned offerings are frequent recipients of criticism from users. Delivery Confirmation, on the other hand, is a high tech, low cost service that works and works well. By extending Delivery Confirmation to First-Class mail as a replacement for Certified Mail, the potential exists to drive in excess of $300 million per year in window clerk and letter carrier costs from the system. I could be wrong about all this, and I don't want to fall into my old buddy H. L. Mencken's simple solutions trap, but that's a heap of money, and I think this one deserves some prompt consideration by the folks at postal HQ!

It's pretty clear that some of you are tired of hearing from me and others, I gather from the snoring, are just plain tired. So, I best wrap things up.

When I talked with Bill Hoyt the other day, he said I was obligated to wrap up with a story or joke. I told him I didn't have any new material. He offered that hardly anyone ever listens to what I say anyway, so you all would not even know that I was recycling old material. Let's see if he is right.

John Nolan and I were talking about some of his responsibilities. You know all those letters that kids write to Santa. Well, seems Bill Henderson used to handle the responses, personally. Bill has delegated that and now those letters all go to John. Turns out that Bill got one letter last year that just tore at his heartstrings. A little boy wrote that since his father's death, his mother was having a hard time making ends meet. The little fellow asked nothing for himself, only that Santa send his mother $100. Well, the PMG, being the kind soul that he is, reach in his pocket, pulled out one of those nice, crisp, new $50 dollar bills and mailed it to the boy's mother. The boy wrote Santa again this year, and the letter wound up in John's in box. He shared a copy and I would like to share it with you.

Dear Santa,

Thanks so much for all you did last Christmas. Things are still pretty rough for us, and my mom sure could use another $100. And, if you don't mind, Santa, when you send it to my mom, please don't route it through Washington. The last time they deducted 50 percent.

Actually, that is an old J. Edward Day joke, or so I’ve been told, not an Edward J. Gleiman joke. I thought it fit both the holiday season and the postal rate case post-mortem.