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Before looking into the future to give you my views on the prospects for postal legislation affecting rates and classifications, I would first like to discuss the past. A very good historian, Richard Kielbowicz, has written extensively on the Postal Service from colonial days through the present. He tells us that business interests since the beginning of the country, continually lobbied the Congress for favorable rate and classification treatment. At first newspapers lobbied for and won free or nominal postage rates. Later advertising mailers lobbied for better rates while newspapers opposed them. Mail order firms lobbied for low priced parcels and the express companies opposed them. Bulk mailers lobbied for lower rates while First-Class mailers lobbied not to be stuck with the bill. Throughout the history of the post office, large and important political forces opposed each other and battled for influence. Congress was forced to make difficult and painful choices. It did so reluctantly. Every time Congress made a decision, it alienated powerful constituencies. A recent example occurred in the mid 1950s when Postmaster General Arthur Summerfield inaugurated unaddressed advertising mail. Although it would have generated much needed revenue for the Post Office Department which Congress dearly wanted and it would have benefited advertising mailers at the time, newspapers mounted such furious opposition that Congress made Summerfield back down.

Since postal rates have involved large sums of money, bribery of congressmen was always a potential problem. Just before the passage of the Postal Reorganization Act, a senator who sat on the Post Office Committee was convicted of taking bribes to set favorable rates for catalogs.

When postal reorganization was being considered at the end of the 1960s, Congress took the opportunity to extricate itself from its no win involvement in postal ratesetting. The Presidential Commission on Postal Reorganization, the Kappel Commission, made recommendations that were widely followed by the Congress, but the process for setting rates was a notable exception. While the Kappel Commission recommended the creation of an internal rate board within the new Postal Service, Congress instead set up an independent regulatory agency, the Postal Rate Commission.

Why did Congress do this? Its action must be seen in the context of the continuing postal letter mail monopoly. Congress wanted to prevent the abuse of monopoly power by postal management, so it set up checks and balances. Most of all, Congress feared that the Postal Service, if unregulated, might abuse its monopoly to exploit First-Class mailers and the general public. The record shows that Congress feared that large mailers with much at stake in postal rates would seek and receive special treatment from the Postal Service. Therefore, Congress decided that rates and classifications should be set by disinterested commissioners supported by an expert staff. It wanted an open ratesetting process which allowed the public to participate. Congress even wanted Aunt Minnie to be represented in rate proceedings and wanted this paid for by the government.

The Senate Post Office Committee Report on the legislation stated:

"Most of the money in the postal system comes from first-class mail. A 100-percent increase in the rates for all second-class mail would not produce as much revenue as a 5-percent increase in the first-class rate. The temptation to resolve the financial problems of the Post Office by charging the lion's share of the operational costs to first class is strong; that's where the money is. The necessity for preventing that imposition upon the only class of mail which the general public uses is one of the reasons why the Postal Rate Commission should be independent of operating management."

Congress also wanted to prevent unfair competition. It was concerned that the Postal Service might use its monopoly to finance unfair competition with taxpaying businesses. It wrote the legislation in such a way that the Commission had to set rates high enough for each class of mail to recover all costs caused by that class of mail. It also required that the rates for each class of mail should contribute a reasonable amount for overhead. Congress of course was most concerned with fair competition in parcel delivery.

Finally, Congress required the Commission to develop a public record for its decisions. It did not want rates to be set in the dining room of the Hay Adams Hotel. It required the Commission to follow the Administrative Procedures Act, a set of rules designed to insure that all parties to a proceeding get due process. Congress knew that this would require a fairly lengthy proceeding each time there was opposition to a Postal Service proposal. But Congress felt that due process was worth the time it took.

The Postal Service has been arguing that it needs new rate and classification authority to successfully compete. But if you examine the legislative proposals being put forward, you will find they give the Service great freedom to set rates in all classes, both competitive classes and those where it has a legal or a *de facto* monopoly. If meeting competition were the aim, why aren't these proposals restricted to competitive classes? When the Postal Service argues that it needs to be deregulated to be able to compete, the Postal Service is attempting to stand the notion of deregulation on its head. The purpose of deregulation is to get the government off the backs of business. Deregulation is not meant to encourage a \$55 billion government monopoly to compete unregulated with the private sector.

Today, many of the same political forces that lobbied the Congress for the first two hundred years of the republic are back at it again. Large second-, third- and fourth-class mailers sense that they can get better deals from postal management than they have been able to get at the Commission. They are backing legislation to give the Postal Service more power to set rates and classifications and to reduce the authority of the Rate Commission.

Volume discounts and negotiated rate proposals being put forward by advertising mailers are a particularly thorny problem. Proponents argue that private sector businesses are free to do this. On the other hand, opponents of these proposals claim that a government monopoly should not be able to engage in these practices because only the largest mailers will benefit from volume discounts. They say that a ten percent discount to the dozen or so largest mailers would mean savings to them of scores of

millions of dollars annually and could be offset by a small increase in everyone else's rates. The rest of the mailers would hardly notice, while the largest would see sizable sums flow to their bottom lines. The opponents say that this is taxing the masses for the benefit of the few.

Third-class mailers have stated that they would like the Postal Service to have more say over rates. Recent Postal Service proposals have been more favorable to them than the Commission's decisions. The Commission has sought to prevent an ever increasing amount of overhead costs being shifted onto First Class.

In the \$55 billion zero sum ratesetting arena, it is not surprising that these legislative proposals would encounter much opposition. Those against reducing the authority of the Rate Commission include small and large newspapers, First-Class mailers, smaller volume magazines, and Postal Service competitors.

Newspapers are alarmed over their loss of advertising market share to the Postal Service. Since 1977, the Postal Service's share of the advertising market has grown from 13.5 percent to over 20 percent. Much of this gain has been at the expense of newspapers. Needless to say, newspapers also were not pleased when this past September the Postal Service dusted off Arthur Summerfield's old neighborhood mail concept.

First-Class mailers fear that they will have to pay more so everyone else can pay less.

Small volume periodicals are afraid that they will suffer increased rates so that large volume periodicals can get reduced rates.

Direct competitors of the Postal Service, most importantly UPS, regard the proposals to give more ratesetting authority to the Postal Service with loathing.

Many observers see no way to bridge the gap between the opposing factions and believe that no consensus can be forged. Because of this, they think that it is unlikely that new legislation affecting rate and classification will emerge from committee and pass both houses of Congress. These observers think that this legislative stalemate will continue over the near future and most probably through the next Congress. I personally share this view and don't expect significant legislation to pass in this Congress or the next.

If we try to look into the distant future, say ten years from now, it is hard to see any change in the political balance. All the issues that were with us before, that are with us today, will in all probability be with us ten years from now. However, many postal observers believe that within ten years, postal volume will probably be declining. This view gains credibility when we see that so far this decade of the 1990s has had the lowest volume growth of any decade this century excepting the decade of the great depression.

We are all familiar with the rapid advances in electronic competition for messages and transactions; Fax,

EFT, EDI, EMail and the Internet. They are having an impact on First-Class volume growth. A major shock to First-Class volume would be the general acceptance of electronic bill paying. If electronic payments, why not electronic posting of bills?

What will be the consequence of declining volume overall and declining First-Class volume in particular? The Postal Service will have to manage carefully to decrease its direct costs or those which vary with volume. It will be very tough for an organization accustomed to ever increasing volume to shrink its variable costs. Because First-Class Mail pays for three-quarters of the Postal Service's overhead, the Postal Service will have to obtain additional revenues to cover fixed costs. In order to replace the lost contribution to overhead, rates will have to increase.

If the Service can manage to decrease its volume variable costs in line with its lost volume, the increase in rates necessary to cover fixed costs should be modest. A ten percent volume decline should cause a four percent increase in rates. Thus, if the Service is well managed, declining volume should not cause too much of a problem. Of course, if the Service cannot downsize, then its "Katy, bar the door."

Failure to downsize in the face of declining volume will have large rate consequences or will require new federal subsidies. With the cost of baby boomers' retirement, it is doubtful that the U.S. Treasury will subsidize postal rates. Managing the Postal Service is a formidable challenge. The Postal Service's total factor productivity figures indicate that it will be very difficult for the Service to downsize in the near term. I believe this is the most serious problem confronting the Postal Service.

Assuming that volume turns down during the next ten years, how will the legislative issues fall out? The Postal Service will still enjoy a lucrative monopoly, but there will be pressure to increase revenues from nontraditional sources and by obtaining additional volume. The Service is now free to seek additional revenues from nonpostal businesses, unencumbered by regulation from the Rate Commission. Unfortunately, the Postal Service pays a very high hourly productive wage. This frequently limits its options. Moreover, the Service has no risk capital. This means First-Class monopoly rate payers bear the risk of new ventures.

When it comes to obtaining new revenues through additional mail volume, we should all keep in mind that lowering rates does not lead to increased revenues for any postal product which has little price sensitivity (or more technically speaking, with price elasticities smaller than one). Moreover, lowered rates do not lead to an increased contribution to fixed costs unless a product has a price elasticity at least greater than two. Express Mail has a price elasticity less than two and all the other categories of mail have a price elasticity smaller than one. So we should understand that given the current demand for the classes of mail, the Postal Service can't make money by lowering rates. When the rate for Category A goes down, rates for Category B, C or D have to go up to replace the lost contribution to overhead. So beware when someone says that the Postal Service needs to be able to lower rates in order to compete. You may well get the bill to pay for the other guy's rate reduction.

What effect will declining volumes have on postal legislation? The same conflicting interests will be

with us. Postal ratesetting will still be a zero sum game. Advocates of volume discounts and contract rates will argue that giving the Postal Service the authority to lower rates will generate more volume. First-Class mailers, small volume magazines, newspaper publishers and competitors will still oppose giving the Postal Service this kind of flexibility because they fear it will drive their rates upward. The legislative stalemate will continue.

I believe, however, that much can be done under the current statute to address the needs of the Postal Service. The Commission has recently issued an experimental rate decision which allows the Service to offer discounts at certain facilities for First-Class and Priority parcels with appropriate bar codes. The decision was issued in 85 days. It was only the second time in 15 years that the Postal Service has taken advantage of Commission rules for expedited consideration of experiments. The Commission can respond rapidly to many Postal Service requests, although highly controversial proposals require more time under the Administrative Procedures Act because all parties must be afforded due process.

The Commission is now conducting a rulemaking designed to make it easier for the Service to conduct experiments, make limited classification changes, and to recognize that new products with high start-up costs may need an extended time to break even. The Commission should issue its decision by the end of April. It will then turn to more difficult issues involving contract rates, volume discounts and flexibility to change competitive rates. I believe the Commission and the Postal Service can work together to make the current statute work better.

In conclusion, let me reiterate that the current battle over legislation is a replay of the same old postal issues and competing forces that lobbied Congress for almost two hundred years before the postal system was reorganized in the 1970s. When it got the opportunity, Congress was only too glad to turn ratesetting over to an independent commission. What is past is prologue. It is not likely that Congress will readily want to take sides among the politically powerful opponents now or even ten years from now. What Churchill said about democracy may well be true of the current postal ratesetting processes - it's the worst way to do it, except for all the others.