

U.S. Postal Service
Postmaster General
Letter to John McHugh, Chairman,
Subcommittee on the Postal Service of the
House Comm. on Government Reform and Oversight
October 25, 1995

[Excerpts]

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Honorable John M. McHugh
Chairman, Subcommittee on the Postal Service
Committee on Government Reform and Oversight
House of Representatives
Washington, D.C. 20215-6246

Dear Congressman McHugh:

In response to your July 27 request, attached are the responses to the follow-up questions submitted for the hearing record following my June 28 appearance before the Subcommittee on the Postal Service.

If I can be of any further assistance, please let me know.

Best regards,
Marvin Runyon

QUESTIONS SUBMITTED TO THE POSTMASTER GENERAL
BY CHAIRMAN JOHN M. McHUGH
following the Postmaster General's testimony of June 28, 1995

1. Assume for a moment that Congress was unwilling to continue the Postal Service's monopoly over the carriage of any mail. Assume also that Congress wanted to direct the Postal Service to continue universal service. What sorts of changes do you believe Congress would also have to provide to ensure that the Postal Service could satisfy this mandate within a competitive environment?

ANSWER: With the complete elimination of the monopoly, the Congress would have to truly free the Postal Service of the price, product, and service regulation now performed by the Postal Rate Commission. At the same time, we would have to be freed from the forms of regulation and control

now exercised in the areas of financial management, personnel operations, transportation, etc., that are applied to the Postal Service, but not to private sector competitors. In other words, the "playing field must be leveled." There may be a need to retain some form of oversight on the universal service mandate.

Under the circumstances described—a truly competitive environment—serious thought must be given to the governance structure, the public service responsibilities of the United States Postal Service and the collective bargaining mechanism. In the case of governance, there may be a need to rethink now the U.S. Government, as sole owner of the enterprise, is represented and what the ongoing obligations of both the United States Postal Service and the government would be.

Today, the United States Postal Service performs a number of "public service" roles, the most common of which is the maintenance of an extended network of small post offices and retail facilities that would not normally be retained in a truly competitive environment. How such public service roles would be handled in the future would need to be addressed.

Finally, the collective bargaining mechanism would have to be designed to put both parties "at risk" A dispute resolution process, perhaps including the right to strike, would have to be fashioned to result in a proper balance of interests.

- A. I understand that the Postal Service has commissioned Price Waterhouse to evaluate the potential impact of repealing the Private Express Statutes. What is the status of this study and when do you expect it to be completed?

ANSWER: Price Waterhouse conducts a number of costing analyses for the Postal Service. As an adjunct to these activities, Price Waterhouse is assisting in the development of forecasting tools to assess the impact on postal revenues given changes in such variables as mail volumes, mail mix, and postal productivity.

"Study" is probably an inappropriate word to describe the Price Waterhouse work They have been engaged for some time now with USPS staff in building a model to evaluate the effects of various factors that could have a major impact on the financial success of the Postal Service. They include such factors as labor costs, regulatory process changes, market and technology diversion, and revisions in the monopoly. There is no definitive answer to the question of the financial impact of a relaxation of the monopoly. The model allows us to test various assumptions.

- B. Under what circumstances would you agree to a relaxation of the monopoly?

ANSWER: Only with a reasonable chance that USPS could continue to meet its universal service mandate, would I "agree" to a relaxation of the monopoly.

- C. Can the Postal Service—or any service provider for that matter—render universal mail service in an openly competitive environment? If not, why not?

ANSWER: The answer to this question really has not yet been determined, at least from the experiences of postal administrations in other parts of the world. An increasing number of foreign posts are liberalizing or even privatizing their postal systems, but only two Sweden and Argentina, have actually abandoned the monopoly. The circumstances in these two countries, as well as the relatively short time in place, probably make it too early to judge the impact of the change.

If the Postal Service were to face a fully competitive environment, then there are some basic conditions that would have to exist to ensure its success with a universal service mandate:

- Freedom from all regulation, not now applicable to private sector firms.
- Freedom from governmental restrictions on personnel, financial, and operations management.
- Conditions which put labor as well as management at risk in the collective bargaining arena.
- A transition period to adapt to the new conditions.

A fully competitive environment is uncharted territory for USPS and it is not possible to determine the eventual outcome with certainty. As we move forward in this discussion, there will have to be careful assessment of the risks and rewards associated with various change proposals.

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12. During the recent oversight hearings, the Subcommittee heard from postal competitors. One witness urged Congress to modify the urgent letter rule which requires alternative carriers to charge at least \$3 or double the otherwise applicable First-Class or Priority Mail postage. What is the rationale for the \$3 or double postage rule? Isn't it true that since this rule was adopted in 1979, the actual cost of providing nationwide express service for shipments of more than a few pounds has fallen to less than double the postage rate?

ANSWER: The "Extremely Urgent Delivery" suspension came about because of a widespread perception that First-Class Mail, combined with the limited Express Mail network which the Postal Service offered in 1979, did not fully address customers' needs. For business and other reasons, some letter materials required access to urgent, highly expedited, guaranteed service assuring delivery by next morning. Mostly, the postal system could not provide it. Of course, all mailers expect timely, reliable delivery, and the Postal Service, in fact, delivers most mail in a day or two. So, to implement the urgent letter suspension, it was necessary to have a way to distinguish between the truly urgent letters and others which are also important and need to be delivered on time.

In a public rulemaking, the Postal Service created the \$3 or double the postage rule as a simple, definitive, "bright line" test to demonstrate that the customer genuinely considers the piece "extremely urgent." If the sender is willing to pay that much of a premium over regular postage to get urgent private delivery, then the urgency of the shipment can simply be presumed. And in fact,

as the question suggests, published rates offered by the principal private delivery companies for the non-letter material which they had been carrying well exceeded the \$3 or twice postage measure.

It is difficult for the Postal Service to know what the actual charges are for most private carriage today, since the carriers extensively discount their prices to their most favored customers, which are business users shipping in bulk. Our impression is that increasing competition has tended to drive prices downward. But we doubt that a member of the public can very often send a single piece to arrive by next morning for less than \$3 or twice postage, even if the piece doesn't contain a letter and so is not affected by the Private Express Statutes.

Our impression is that much of the impetus for relaxation of the \$3 or twice the postage rule comes from those who would like to expand the suspension into an area it was never imagined to cover namely, second-day delivery services. In 1979, no one contended that a shipper who was willing to settle for a two-day delivery schedule had "extremely urgent" business which the postal system was ill equipped to handle. But as the overnight market has become more mature, and profit margins apparently have been reduced by increasing competition, private carriers understandably have been looking for fresh fields to plow. They have expanded their efforts interntionally; but domestically, it appears they may see the Postal Service and its revenues as the best available target for further inroads.

- A. What would be the effect on the U.S. Postal Service's revenue and market share if the double postage rule for extremely urgent letter mail were suspended or modified by Congress?

ANSWER: If the double postage rule for extremely urgent letter mail was suspended, all Postal Service letter and net mail could be diverted. This This jeopardize the Postal Service's mandate to provide universal service at uniform rates. Private competitors may elect to only serve high volume, lower cost business traffic.. Competitors may also decide to serve only high density business and residential areas in cities and suburbs. This would have the potential of leaving the Postal Service with servicing only households and small businesses in rural areas at substantially higher costs.

Any revenue and market share estimate is speculative and depends on several factors. First, the diversion would be different if the double postage rule were modified as opposed to suspended. Second, competitors' reaction to the modification or suspension is not known. However, in the ground parcel market where the Private Express Statutes are not in effect, UPS surcharges residential delivery and charges extra for deliveries to Alaska, Hawaii, Puerto Rico, and other U.S. territories and possessions. RPS has decided only to serve the business-to-business market.

The Postal Service has steadily lost market share in most of its principal markets for some time. If the Private Express Statutes were substantially weakened, so that more direct competition could be offered for two-day or regular services, that trend could be expected to accelerate, so long as the Postal Service is not allowed to use the same aggressive pricing and marketing techniques that are available in the private sector.

In 1979, in accordance with their authority under 39 U.S.C. § 601(b), the United States Postal Service Board of Governors authorized adoption of 39 C.F.R. § 320.6, the "extremely urgent suspension of the Private Express Statutes. Enacted at the conclusion of a public notice and comment rulemaking proceeding, the suspension strikes a balance between the public interest in a financially viable national postal system and the public interest in access to non-postal delivery of extremely urgent" letters. The purpose of the suspension was not to permit competition for the general delivery of letters, but to carve out a narrow exception for the limited circumstances where the nature of a letter was such that its value would be lost or greatly diminished if it did not receive expedited delivery. 39 C.F.R. § 320.6(b).

For the purpose of administrative convenience, the "double postage" rule or the cost test, 39 C.F.R. § 320.6(c), is an objective alternative to the subjective "value" test for extreme urgency. The "cost" test establishes that if the sender of a letter pays a certain price for its private carriage (the greater of three dollars or twice the applicable postage), there is a conclusive presumption that the letter is extremely urgent," *i.e.*, of such a nature that its value would be lost or greatly diminished if not delivered expeditiously.

Any objective "cost" test for extreme urgency, to be true to the purposes of the suspension, must establish a benchmark which conclusively differentiates extremely urgent letters from those which (with all due respect to the senders and recipients) are subjectively less "urgent" or "important" or "valuable." The "twice the applicable postage" standard fairly distinguishes extremely urgent" letters from those which are not.

Even assuming that some postal competitors currently charge less than twice the applicable First-Class Mail or Priority Mail postage for the private carriage of overnight and two-day express shipments of more than a few pounds, it should be emphasized that the "cost" test applies only to privately carried letters~ (as defined by 39 C.F.R. § 310.1(a)), and not to variety of other materials carried by private expedited shippers. No analysis of the impact of the suspension on private expedited delivery services would be complete without a determination of the proportion of their express shipments which actually consist of letters.

To be responsive to your question, such analysis also would materially flawed if it did not measure the proportion of private express shipments of more *than a few pounds* which actually constitute letters. Generally, in Express Mail and Priority Mail, there is a very significant drop-off in the proportion of letters among items which exceed the two-pound weight increment. A similar trend is likely to be true of privately carried expedited materials. If so, the "extremely urgent" suspension has an impact on only a relatively small portion of private expedited delivery shipments which weigh more than a few pounds.

We note that long after the adoption of the suspension, the major private carriers began to highlight the availability of two-day delivery at prices lower than those charged for their overnight services. One of the benefits of the "cost" test in 39 C.F.R. § 320.6(c) to the public and to postal competitors is that, unlike the ~value" test in § 320.6(b), it allows letters to qualify under the "extremely urgent suspension without regard to the degree of urgency employed by the private carrier in delivering the

letter. Thus, there is no expedited delivery requirement for "extremely urgent" letters which meet the "cost" test.

To fairly gauge the impact of the suspension on private expedited delivery providers, one also would need to consider such non-postal factors as the advent of facsimile and electronic information transmission services which now provide the public with alternatives to overnight delivery of letters, making the expedited letter delivery market less robust than it was when the suspension was adopted in 1979.

If the "cost" test in 39 C.F.R. § 320.6(c) were eliminated by Congress (and assuming the application of no other suspension or exception), then all private shipments of "extremely urgent" letters would be required to meet the subjective "value" test for "extreme urgency" in 39 C.F.R. § 320.6(b) or a comparable subjective standard adopted by the Congress, in order to avoid the payment of postage required by 39 U.S.C. § 601(a). To the extent that letters are now privately carried, because such carriage qualifies only under the "cost" test and not the subjective "value" test under 39 C.F.R. § 320, the elimination of the "cost" test could result in some of those letters returning to the mailstream or being diverted to alternative media (such as facsimile service or electronic transmission). The diversion of any such volume to the mailstream could be expected to have a positive effect on postal market share and revenues.

If the Congress eliminated the "extremely urgent" suspension altogether (and assuming the application of no other suspension or exception), an alternative result would be that some letters would still be privately carried, but that postage would be affixed, as required by 39 U.S.C. § 601(a). Such a consequence would not improve postal market share, but would have a positive impact on postal revenues.

If the "cost" test in the "extremely urgent" suspension were modified by the Congress in a manner which lowered the objective benchmark to some point significantly below "twice the applicable postage, the purposes of the suspension would be undermined and the degree of the adverse impact would depend upon the extent of the modification. The impact on postal market share in the delivery market for Express Mail and Priority Mail and First-Class Mail could be adverse and severe. The rates charged for Express Mail, Priority Mail, and heavier-weight First-Class Mail reflect relatively high per-piece contributions to postal institutional costs. If such mail were diverted from the mailstream, the institutional cost burden of the mail remaining in the system—primarily lighter-weight First-Class Mail and third-class mail—and the rates for this remaining mail would have to be increased. Upward pressure on the price of First-Class Mail and third-class mail would hasten the diversion of such mail from the mailstream and increase the institutional cost burden on the mail which remains. This would have a negative effect on postal volume and would accelerate postal rate increases.

Amendment of the suspension in a manner which allowed relatively unrestricted private delivery of letters without postage effectively would repeal the Private Express Statutes and seriously jeopardize the financial well-being of the Postal Service.

Notwithstanding the general revenue protection purposes of the Private Express Statutes, it is dear that the Board of Governors did not adopt the suspension or its "cost" component to increase Postal Service revenue or to protect Express Mail from competition. It is safe to say that adoption of the suspension surely has not decreased available alternatives to postal delivery of "extremely urgent" letters. It seems to have had the opposite effect, which is consistent with the public interest determination made by the Board of Governors in 1979 to allow private carriage of 'extremely urgent' letters without postage under circumstances where such activity, at the time, was not permitted.

With the exception of the most remote corners of the nation to which the expedited delivery of a letter (by the Postal Service, Federal Express, United Parcel Service, or others) is logistically difficult, the general public has access to a variety of non-postal alternatives for the delivery of its 'extremely urgent' letters at prices which are primarily governed by market forces, or in the case of the Postal Service, regulated by the Postal Rate Commission. The "cost" test continues to be a fair and simple standard for separating 'extremely urgent' letters from all others. The rule continues to equitably balance the important goals of maintaining a financially viable national postal system and promoting access to non-postal 'extremely urgent' letter delivery services.

13. The Postmaster General suspended the Private Express Statutes for international remail back in 1986. Given that international rates are not subject to PRC review, what checks and balances exist in order to prevent the Postal Service from engaging in price gouging of international mail customers? Or alternatively, from engaging in pricing practices whereby other monopoly protected classes cross subsidize international rates? Is this an area where the PRC should be reviewing the rate-setting procedure?

ANSWER: Since the Private Express Statutes were suspended to permit international remail, the international mail market has become very competitive. Participants in that market include private companies such as TNT Mailfast, which is jointly owned by TNT of Australia and the government postal administrations of Canada, France, Germany, The Netherlands, and Sweden; Global Mail, a U.S. company; and other postal administrations including The Netherlands and Great Britain. With the advent of competition, international mail customers have more options and can select any service provider they choose, and prices are held in check because charging too high a price loses customers. The market sets the price, and that is how customers are protected from paying prices that are too high.

Competitors are protected from unfair pricing by the law and by the courts. The Postal Service is obligated by law to charge reasonable, non-discriminatory rates that do not unfairly apportion the cost of postal operations. 39 U.S.C. §§ 101(a), 101(d), 403(a), 403(c). These legal requirements clearly prohibit charging rates that are below cost. Competitors have shown no reluctance to seek redress in the courts if they believe that rates are below cost. In addition, while there is a controversy with the PRC over the level of detail of cost, revenue, and volume data about individual international services that the Postal Service provides, the Postal Service provides adequate information separating aggregate international costs, revenues, and volume from domestic. These data show clearly that international mail covers its costs and makes a contribution to overhead comparable to or higher than other postal services that are provided in competitive markets.

There is no need for the Postal Rate Commission to review international rate-setting procedures.

- A. While the Rate Commission does not set international mail rates, international mail cost, volume and revenue data are of significance to the Commission in omnibus rate proceedings. The Commission told us that it needs the data to be assured that the Service's customers in the U.S. do not subsidize its overseas customers. Until last year's omnibus rate filing, the Postal Service had provided some data concerning international costs, volumes, and revenues as part of its filings and responded to questions concerning them. However, in last year's filing the Postal Service took the position that any supporting information on its forecast of total international mail costs, volumes, and revenues is irrelevant and qualifies for trade secret privilege. Must Congress and the public now accept on faith that international mail is covering its attributable cost? Should Congress completely exempt international mail from monopoly protection?

ANSWER: Neither Congress nor the public must accept on faith that international mail is covering its attributable costs. In its filing in the last rate case, the Postal Service provided adequate information on international mail service as a whole. Nothing material was withheld. What was not given was detailed information on individual services that could be used by competitors to take business away from the Postal Service. Having gotten all the information on international mail service as a whole, this level of detail is irrelevant for the purpose of setting domestic rates.

Congress should not completely exempt international mail from the Private Express Statutes because that would undermine the restrictions on competing with the Postal Service for the domestic delivery of letters. The purpose of having restrictions on competition is to allow the Postal Service to carry out its mission of providing universal service at uniform rates. Without those restrictions, mailers would pay different rates for letter mail service depending on where they live, where they are mailing letters to, and how many other service providers are interested in their business. This would be true regardless of what the Postal Service did in the way of rates, because competitors would get the low cost mail and rates for everyone else would have to go up, creating a price spiral that would leave the Postal Service with only the highest cost customers. At this point, the only international mail subject to protection is inbound letter mail. If that were exempted, domestic letters could be created or taken across the border and brought back for private delivery with no one knowing whether those letters were truly international or were domestic letters made up to look like international letters. Moreover, there would be no way to know whether any particular letter was ever anywhere but the United States.

14. The Postal Service has "suspended" the postal monopoly for newspapers, magazines, checks sent between banks, certain data processing materials, urgent letters, international remail, etc. Under what legal authority can the Postmaster General suspend the monopoly?

ANSWER: The principal civil provision of the Private Express Statutes is 39 U.S.C. 601, which enumerates six conditions under which letters may be carried outside the mails, including the

payment of postage by affixing stamps. Congress has included in 39 U.S.C. 601(b) authority to suspend "any part of" section 601 where required by the public interest. The Postal Service has considered that the plain meaning of this language permits it to suspend one or all of the conditions for outside carriage, including the requirement to pay postage. The section has been applied both in fairly narrow ways, for example, by permitting postage to be paid in bulk by check so that stamps do not have to be placed on letters carried privately, and more generally, by suspending all six conditions for certain categories of items such as those described in the question.

- A. If the Postal Service believes that Section 601 of title 39 (U.S. Code) provides the legal authority to suspend the monopoly, how do you respond to concerns raised by the testimony of Federal Express before this Subcommittee on June 14, 1995? Specifically, the witness stated that based on the legislative history of the cited provision (rooted in a 1864 postal act), Section 601(b) was never intended to confer authority to suspend the postal monopoly. According to this witness, the gist of section 601 (b) is to allow the Postmaster General to *reapply* the postal monopoly by suspending, on a selective basis, an exception to the postal monopoly allowing private carriage of letters in stamped envelopes (found at 601(a)). How do you respond?

ANSWER: This argument was offered by the same witness in Congressional hearings on the urgent letter suspension in 1979, but did not draw any support there, or in the very open public rulemaking process, in which all interested parties participated. We find it interesting that Federal Express was among the participants that did not support this argument at the time, and since then and to this day has apparently sheltered itself extensively under the umbrella of the suspension in order to expand its business.

It should be recognized that the "extremely urgent delivery" suspension is only one of the most recent suspensions added to the regulations. When the Congress considered the reforms enacted in the Postal Reorganization Act in 1970, it was unsure whether the Private Express Statutes, most of them unchanged since the 19th century, should be revised. It decided, in section 7 of the Act, Public Law No. 91-375; 39 U.S.C. 601 note, to require the Board of Governors to undertake a study of the matter and to submit "recommendations for modernization" to the Congress and the President. The Board issued a formal report, Statutes Restricting Private Carriage of Mail and Their Administration: A Report by the Board of Governors to the President and the Congress. Pursuant to Section 7 of the Postal Reorganization Act (1973). The report concluded that modernizing changes in administration of the Statutes were needed, and recommended that these updates be made by administrative action, including several suspensions under 39 U.S.C. 601(b), rather than by legislation. See especially pages 11-13, 68.

The text of certain proposed suspensions was included in the report. See pages 198-200. The Postal Service then proceeded to air these proposals through a public rulemaking, first seeking comments, 38 F.R. 17512 (July 2, 1973); then summarizing the comments and requesting further input, 39 F.R. 3968 (January 31, 1974); and subsequently publishing the final regulations, including suspensions,

39 F.R. 33209 (September 16, 1974). In the meantime, six days of Congressional hearings had considered the Board's report. While the hearing elicited extensive debate about the details of the proposed regulations and suspensions, the general approach recommended by the Board, to address needed reform or relaxation by administrative suspension under section 601 rather than through legislation, found broad support. The Private Express Statutes, Hearings Before the Subcommittee on Postal Service of the Committee on Post Office and Civil Service, House of Representatives, 93d Cong., 1st Sess., Serial No. 93-32 (1973).

Afterward, growth of the expedited delivery business brought additional pressures to relax the reach of the Statutes for urgent letters, by law or by administrative suspension. The Postal Service initiated further public rulemaking proceedings, and new Congressional hearings focused on the matter. Most of the testimony favored additional relaxation, either legislatively or by suspension. One witness made the argument embodied in your question, that 39 U.S.C. 601(b) authorizes suspension only in the direction of tightening, not relaxing, the statutory restraints. The Private Express Statutes, Hearings Before the Subcommittee on Postal Operations and Services of the Committee on Post Office and Civil Service, House of Representatives, 96th Cong., 1st Sess., Serial No. 96-39, p. 203 (1979) (testimony of James I. Campbell, Jr.). Unswayed by that contention, the chairman of the House postal oversight subcommittee left no doubt that his oversight recommendation to the Postal Service was to resolve the matter administratively, by adopting a suspension relaxing the sweep of the monopoly. *Id.*, at pp. 6, 13; Status Report on the Operation of the United States Postal Service and the Postal Rate Commission Hearings Before the Committee on Post Office and Civil Service, House of Representatives, 96th Cong., 1st Sess., Serial No. 96-21, pp. 4547 (1979). That is what the Postal Service did.

The Private Express Statutes are very old laws, changed very infrequently, with roots antedating the Constitution. Like the Constitution, they have had to stand the test of two centuries of the country's growth. While the Statutes have not performed perfectly, or fit perfectly every new development, they have proved adaptable in some respects. The suspension authority has helped meet that challenge, and its application as a safety valve to relax what came to be universally understood as unnecessary overreach of the monopoly in limited situations has been broadly accepted.

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