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WILL INCREASED POSTAL RATES PUT MAILERS OUT OF BUSINESS?

HEARING

BEFORE THE

SUBCOMMITTEE ON FEDERAL WORKFORCE, POSTAL SERVICE, AND THE DISTRICT OF COLUMBIA

OF THE

COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM

HOUSE OF REPRESENTATIVES

ONE HUNDRED TENTH CONGRESS

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WILL INCREASED POSTAL RATES PUT MAILERS OUT OF BUSINESS?

TUESDAY, OCTOBER 30, 2007

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON FEDERAL WORKFORCE, POSTAL SERVICE, AND THE DISTRICT OF COLUMBIA,
COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM,
Washington, DC.

The subcommittee met, pursuant to notice, at 10:01 a.m. in room 2154, Rayburn House Office Building, Hon. Danny K. Davis (chairman of the subcommittee) presiding.

Present: Representatives Davis of Illinois, Norton, Sarbanes, Cummings, Marchant, McHugh, and Jordan.

Staff present: Tania Shand, staff director; Lori Hayman, counsel; Cecelia Morton, clerk; Eleanor Hudson, intern; Ed Puccerella, minority professional staff member; and Benjamin Chance, minority clerk.

Mr. DAVIS OF ILLINOIS. The subcommittee will come to order.

Welcome Ranking Member Marchant, members of the subcommittee, hearing witnesses, and all of those in attendance. Welcome to the Federal Workforce, Postal Service, and the District of Columbia Subcommittee hearing, "Will Increased Postal Rates Put Mailers Out of Business?"

The hearing will examine the process for rate increases, the recent decision by the U.S. Postal Service Board of Governors to increase postal rates, and the impact of the new postal regulation on future rate increases.

The hearing will also examine the impact the new rate increase will have on mailers.

Hearing no objection, the Chair, ranking member, and subcommittee members will each have 5 minutes to make opening statements, and all Members will have 3 days to submit statements for the record.

We are going to do our opening statements and then I am going to introduce the first panel.

Ranking Member Marchant, members of the subcommittee, and hearing witnesses, welcome to the subcommittee's hearing on the 2005 postal rate increase, "Will Increased Postal Rates Put Mailers Out of Business?" Today's hearing will examine the Postal Governor's decision to increase postal rates, the process for rate increases, and the impact of new postal regulations on future rate increases.

The hearing will also review the impact the rate increases had on various small and large mailers.

The U.S. Postal Service submitted a request for a rate increase through the Postal Regulatory Commission in February 2007. The PRC, an independent agency, issued its decision on this request after a lengthy process that involved an open administrative proceeding involving mailers, employee organizations, consumer representatives, competitors of the Postal Service, as well as the public, on the recorded hearings broadcast over the Internet.

On March 19, 2007, the PRC submitted its rate recommendations, which was endorsed by the Board of Governors. As part of this endorsement, it was decided that the new rates for periodicals would be delayed to allow for adjustments to mailers' software.

The cost inefficiencies inherent with the handling of periodicals have long plagued the Postal Service. I know that the PRC has sought to keep periodical postage rates as low as possible in the face of declining magazine mail volume and increasing postal handling costs. The notion of implementing a rate structure based on paying for what you use was established to encourage better operational practices and eliminate unnecessary costs. This is the basis for the new rate structure.

But the question is: is it working? In 1995, Time Warner, Inc., proposed that the periodical class be split into two segments and that rates be redistributed. This proposal would have effectively eliminated the historic policy of cross-subsidization of low-volume periodicals by high-volume periodicals. Small magazines state that the new rates, which they feel were based on the proposal submitted by Time Warner, Inc., transferred the burden of postal costs from magazines with large circulation and heavy advertising to smaller publications with heavy editorial content.

In 2004, Time Warner once again submitted a rate proposal that many mailers believe shifted the burden of mailing cost on to small publications.

As a result of this controversy, the PRC recommended and ultimately endorsed a proposal where small publications with circulations of 15,000 or less received lower increases than the rates recommended in the proposals submitted by the large magazine publications, Time Warner, or the Postal Service. Small magazine publishers are not consoled by the lesser-endorsed amount because they feel they bear the brunt of the proposed postal rate increase. Today we will hear from the rate setters and the small and large mailers a the need for the increase and its impact on mailers.

A number of constituents have contacted the subcommittee and voiced their concerns regarding the Postal Service's elimination of an entire class of international surface mail. For decades this service has been the means by which thousands of Americans economically shipped books, professional and medical journals, and other materials overseas to support humanitarian projects. Today the only way to ship these reprimands overseas is by airmail, which has tripled and even quadrupled in shipping costs. The elimination of international surface mail has severely curtailed or in some cases shut down charitable programs which have demonstrated America's goodwill to people and nations around the world.

I would like the Postal Service to address these concerns during its testimony.

I want to thank all of our witnesses today, and look forward to your testimony on this important issue.

I would now yield to the ranking member, Mr. Marchant, for his opening statement.

Mr. MARCHANT. Good morning, Mr. Chairman. Thank you for holding this hearing today on the U.S. Postal Service's recent rate increase. As we continue our role on the subcommittee in providing oversight of the Postal Service, I am reminded that, as it has been said in the past, the Postal Service is not a perfect system, but one which is ever-changing and expanding.

With recent enactment of postal reform legislation, I am sure we can expect many more changes as both the Postal Service as well as the mailing community adjust to a hopefully more robust and financially stable USPS.

I look forward to hearing from all the witnesses today and hearing from all parties affected by the recent rate increase and what impact the new rate has had on cost and profits.

Thank you.

Mr. DAVIS OF ILLINOIS. Thank you very much, Mr. Marchant.

Ms. Norton.

Ms. NORTON. Just a brief statement.

Mr. Chairman, I appreciate that you have called this hearing. In a real sense, the mailers and the Postal Service suffer the same problem: the world is changing from underneath them, with technology, and somehow both entities have to find a way through it if they are to exist with efficiencies and, in the case of the Postal Service, with the burden, and the very important burden of understanding that a mail system is still a public service and an indispensable one in this country.

Thank you again for this hearing, Mr. Chairman.

Mr. DAVIS OF ILLINOIS. Mr. McHugh, do you have any opening remarks?

Mr. MCHUGH. Nothing formal for the record, Mr. Chairman. Just let me thank you for your continued leadership in these critical areas and to add my words of welcome to this and the following panels. We look forward to their comments. Obviously, we wish to ensure that, from our oversight perspective, as the rate-setting process transitions from the old 1970's system into a new one, it is done in a way that is equitable and is fair and inflicts as little pain and as much benefit as possible. I think this hearing can add to that effort.

Thank you. I would yield back.

Mr. DAVIS OF ILLINOIS. Thank you very much, Mr. McHugh.

We will now hear from our first panel. I will introduce the witnesses.

Panel One, Mr. James C. Miller III, was elected chairman of the Board of Governors of the U.S. Postal Service in 2005. In addition to serving on the Board, he is senior advisor to the international law firm of Blackwell, Sanders, Pepper and Martin.

Chairman Miller, we welcome you and thank you very much.

Our next witness is Mr. John Potter. Mr. Potter was named 72nd Postmaster General of the United States of America on June 1, 2001. He has served as chief operating officer, vice president of

labor relations, and in a number of other senior operational positions, both at Postal Headquarters and in the field.

Mr. Dan Blair, our third witness, serves as the first chairman of the Independent Postal Regulatory Commission, the successor agency to the formal Postal Rate Commission. He was unanimously confirmed as a Commissioner of the formal Postal Rate Commission on December 9, 2006, and designated chairman by President George W. Bush on December 15, 2006.

Gentlemen, it is the policy of this committee that all witnesses be sworn in, so if you will rise and raise your right hands.

[Witnesses sworn.]

Mr. DAVIS OF ILLINOIS. The record will show that each witness answered in the affirmative.

Your entire statement is in the record. Of course, the green light indicates that you have 5 minutes to summarize your statement. The yellow light means that your time is running down and you have 1 minute remaining to complete your statement, and the red light means that your time is expired.

We will begin with Chairman Miller.

STATEMENTS OF JAMES C. MILLER III, CHAIRMAN, BOARD OF GOVERNORS, U.S. POSTAL SERVICE; JOHN POTTER, POSTMASTER GENERAL, U.S. POSTAL SERVICE; AND DAN G. BLAIR, CHAIRMAN, POSTAL REGULATORY COMMISSION

STATEMENT OF JAMES C. MILLER III

Mr. MILLER. Thank you, Mr. Chairman.

I note I have some of my family here.

I would like to thank the Board of Governors of the Postal Service, whose testimony I represent today. Thank you, Jack Potter, the CEO and Postmaster General, and Chairman Dan Blair and his fellow commissioners at the Postal Rate Commission for all their work.

I have a short statement with tables, which I ask to be submitted and included in the record.

I would like to summarize this statement and extend it just a bit.

The first point I want to make is that we Governors take very, very seriously our work in rate setting. We note that we are required by law to charge at least attributable cost for commercial services, but we note that if everyone paid simply attributable costs, our annual revenues would be only $44 billion. Since our total cost is about $75 billion per year, we would be some $31 billion in the red, contrary to law. So the question is the amount of markup to apply to each class of service.

Conventional approaches economists use in trying to figure out the best approaches often yields prices that are inversely related to the price elasticity of demand. Now, we believe that this policy should be tempered by business judgment.

The second point I would like to make is with respect to the old versus the new law. Under the old law, the Postal Reorganization Act of 1970, the ratemaking process was long and tortured. Under the new law, the Postal Enforcement Accountability Act of 2006, ratemaking process is shorter and more streamlined. It is divided into two parts: competitive products of a 30 day wait period for

published rates, or 15 day wait period for contract rates. And the PRC can establish minimum rates.

In the market dominate products area, which is 90 percent of our business, we have a 45 day notice, and the PRC—the Postal Regulatory Commission—has a look-back provision. Under the new law, we have until December 19th of this year to decide whether to propose a new rate package under the old law or under the new law, either one. After that we, of course, would be under the new law.

The third one is with respect to the ratemaking case that is so controversial here, that is R–2006–1. I would like to make several points.

First, the Board of Governors engaged in a lengthy process in determining the rate package that we proposed in responding to the Postal Rate Commission's recommended decision. We began to look at this issue back in December 6, 2005. We had board meetings on January 10, 2006, February 7th, March 22nd, and May 2nd, all addressing in part the question of a rate case, and that we initiated the rate case on May 3, 2006. Then we had Board meetings, a Board meeting on June 6th, we had a teleconference on July 12th, we met on September 11th, November 14th, and December 5th, all addressing this issue in part. And on January 9th we had a Board meeting.

On February 26th the Postal Regulatory Commission issued its opinion and recommended decision. On February 27th we had a Board teleconference, another one on March 6th, another one on March 14th, another one on March 16th, another one on March 19th. And we had Board meetings on March 28th, on May 1st. We are dealing with a second opinion, etc. And then we had a teleconference on June 19th and a teleconference on June 10th. All told, we had 12 Board meetings and 8 teleconferences, for a total of 20 such meetings addressing in part this issue.

I point this out simply to note that we laid a lot of attention to this matter and spent a lot of time on it.

The second point is that our overall objectives in putting this package together was to meet the requirements of the old law, the revenue need, and to cover attributable costs, to apply the principles I just described and laid out in my prepared statement, including the inverse elasticity and business judgment, to differentiate by shape as well as weight, because the differences are substantial, and encourage mailers to use less-costly means of mailing.

The result was mostly increases, some minor decreases, and some restructuring of rates, as described in table one of my submission. On the whole, our package and the Postal Rate Commission's recommended opinion are very similar, as you will see in table one.

Now, last, with respect to publications, I would just like to make two points. First, they are the only class of mail that pays nothing toward overhead cost. Under the new system, the new set of rates, they pay just barely cover attributable costs, and before that they did not cover attributable costs, and the law requires everyone to cover attributable costs.

The second point is that I have heard it said that somehow by raising the price or raising the rates on publications we are trampling on their first amendment rights. I have a copy of the Con-

stitution. I read it very differently. I think that charge is really bogus.

Thank you, Mr. Chairman. I would be glad to respond to questions.

[The prepared statement of Mr. Miller follows:]

BOARD OF GOVERNORS

UNITED STATES
POSTAL SERVICE

STATEMENT OF
JAMES C. MILLER III
CHAIRMAN
BOARD OF GOVERNORS
U.S. POSTAL SERVICE
BEFORE THE
SUBCOMMITTEE ON FEDERAL WORKFORCE, POSTAL SERVICE,
AND THE DISTRICT OF COLUMBIA
COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM
U.S. HOUSE OF REPRESENTATIVES

October 30, 2007

Chairman Davis, Ranking Member Marchant, and Members of the Committee: thank you for inviting my colleagues and me today. We welcome this opportunity to discuss Postal ratemaking principles and processes. As you well know, we are entering a new era under the Postal Accountability and Enhancement Act of 2006 ("new law"), and it is appropriate that we pause to consider where we have been and where we are going. Our hope is to share our thinking not only with you but with others in the Postal community. And we welcome an opportunity to obtain your guidance and to consider any and all inputs from those most immediately affected by our rate decisions -- those who actually pay for our services.

Ratemaking Principles

My fellow Governors and I recognize that Postal rate setting is inherently controversial. Inevitably, some customers will consider Postal charges too high. Some will protest that their rates are too high relative to those charged for other classes of mail. This is especially true because of the substantial common costs so characteristic of postal enterprises. As you probably know, the U.S. Postal Service has an elaborate cost attribution system, but with that is only able to attribute some 59 percent of its costs to various classes of mail. The rest – 41 percent – is "overhead." Thus, we start from the basic proposition that even if each and every class of mail just covered its attributable cost, the Postal Service would still be in the red some $31 billion ($75 billion annual cost X 0.41). Since the new law (as well as the old) requires the Postal Service to cover all costs and, with exceptions, that each class of mail cover its attributable costs, the ratemaking challenge is thus how much to "mark up" each class of mail.

In a competitive market, the non-attributable costs of a firm are "allocated" by relative demands. Those demands that are large and relatively inelastic (with respect to price) are allocated larger shares of overhead costs. This is a problem/solution that can be found in any modern economics textbook.

But the market for postal service is not perfectly competitive. In fact, only a minor portion -- only 10 percent -- of USPS's business is competitive, as recognized under the new law. On 90 percent of its business the USPS is market-dominant.

One approach to pricing problems such as this that is utilized in many public utility proceedings is "Ramsey pricing," an example of which is the application of the "inverse elasticity rule." Briefly, if the objective is to maximize economic efficiency, given costs and demands, the markup over attributable cost should be inversely related of the price elasticity of demand. In other words, those who have

UNITED STATES POSTAL SERVICE
475 L'ENFANT PLAZA, SW
WASHINGTON, DC 20260-1000
WWW.USPS.COM

little alternative but to use the service in question should pay a higher markup, and those who have alternatives should pay a lower markup.

While the principles are sound, the application of such an approach to USPS ratemaking is not so straightforward. First, the structure of demand by class of mail is constantly changing. Second, the price elasticity for one class of mail may depend on the price charged for another class (or subclass), as some mailers have the option of choosing among classes (or subclasses). Third, important modifications in service characteristics can affect demand elasticities. Fourth, as with any good business, the USPS should consider the effects of price changes on its consumer base – too rapid an increase can drive away customers who find themselves unable to adjust quickly to such higher distribution costs. Finally, a myriad of other factors, or principles, must be applied in making rate decisions. For the most part, it comes down to a simple matter: business judgment. And since we are all committed to making sure that, insofar as possible, the U.S. Postal Service operates as an efficient business enterprise, business judgment is especially important.

Despite these problems, within the discretion afforded by the new law, it is possible to glean from these and other applicable approaches some basic principles for postal ratemaking. Each class of service should cover, at a minimum, its attributable costs. Everything else equal, the markup over attributable cost should be inversely related to an informed judgment regarding the price elasticity of demand. Finally, rate changes should be tempered by business judgment.

Ratemaking Processes

Under the Postal Reorganization Act of 1970 ("old law") the Board of Governors (BOG) proposed rate changes whenever, despite cost-cutting, it found a need for new revenue and asked the (old) Postal Rate Commission (PRC) for its review. After a protracted process, often lasting the statutory limit of 10 months, the PRC would offer its opinion and the rates it recommended. The BOG could accept the PRC's rate recommendations, adopt them while appealing all or part of the PRC's decision, or reject them outright -- at which point it could refile the initial rate package and after further consideration by the PRC could accept the PRC's final decision or, if the rates recommended by the Commission would not generate the revenue requirement, then by unanimous vote the Governors could adopt the original package.

Under the new law, there is a distinction between competitive markets (packages and express services) and market-dominant markets (everything else). In competitive markets, the BOG may determine rate changes, and these will go into effect reasonably promptly. However, such changes are subject to challenge to the new Postal Regulatory Commission (PRC) on grounds that they would result in rates that are "too low." As an aside, it is highly unlikely that the USPS would ever engage in "too-low pricing." It is not our intention to engage in predatory pricing (that is, pricing below costs in order to drive out competition), since such an effort, in the long run, would be self-defeating. All of our rate proposals in the competitive area will be cost-justified.

With respect to market-dominant services, the BOG notices rate changes, but cannot implement increases for any class (as opposed to subclass) of mail which would result in a weighted-average increase exceeding the most recent increase in the consumer price index (CPI). While such a rate ceiling puts pressure on the USPS to control costs, it also means that, absent some truly significant reductions in real costs, it is unlikely that the BOG will propose rate decreases for individual classes as a whole. The reason is simple arithmetic: to propose a rate decrease, or even a rate increase less than the increase in the CPI, means that the overall increase will be *less* than the increase in the CPI.

The review process in the market-dominant area is also faster under the new law. After giving the PRC advance notice of rate changes, the Postal Service is allowed to put them into effect – unless the PRC determines that the increase actually exceeds the permitted (CPI) limit. Moreover, the

increases – both their levels and their structure – can be appealed to the PRC and perhaps overturned.

I hope this stylized characterization of the two processes is enough to convey our appreciation for the opportunities for ratemaking afforded by the new law, but also our concerns over how the new law will work in practice. Having said that, I want to express our appreciation to PRC Chairman Dan Blair and his fellow commissioners for their thoughtful, independent review of our proposals in the past and the Commission's just-released rules governing the review process under the new law. Indeed, I do not think it excessive to say the Governors view the Commission as having great expertise on Postal pricing, and that we look forward to and value the Commission's opinions.

Ratemaking Principles and Process in the Recent Rate Case

Mr. Chairman, I understand from your letter of invitation that a focus of this hearing is the recent rate case, R-2006-1. On May 3, 2006, after considerable discussion among ourselves, based in part on a thorough review of our financial situation and forecasts, from which we concluded we required additional revenue to meet our legal mandate, and after thorough debate over proposals made by Postal Service management – which, in turn, reflected extensive discussions with Postal customers -- the BOG approved a sweeping revision in Postal rates, announced its details, and send the package over to the PRC for review. This was the first such initiative since the omnibus rate filing of 2001.

The PRC held extensive hearings on our rate package and on February 26, 2007 issued its opinion and recommended decision. After several meetings about the PRC's response and vigorous debate among Board members, on March 19, 2007 the BOG accepted the PRC's recommended decision in major part, but appealed three items and concluded that because of (in)feasibility problems it would postpone for two months implementation of the rate increases for publications. On April 27, 2007 the PRC issued its recommendations about two of the three matters, and on May 1, 2007 we approved these recommended rates. Then, on May 25, 2007 the Commission saw merit in our request for some type of rate relief for flats, but since it did not offset the loss of revenue with increases in other classes or subclasses of mail, on June 19, 2007 we were forced to reject the new recommendation and left the original recommended rates in effect.

Then-existing rates (measured as revenue per piece), along with the rates the Governors submitted to the PRC and forecast cost coverage (expressed as a percent of attributable cost), are summarized in Table 1. The most significant characteristic of our initial package was to move from pricing by weight to pricing by shape as well as weight. For example, in First Class Mail we proposed distinct rates for letters, flats, and parcels, to recognize the cost differences among these shapes. In Priority Mail, we proposed pricing that takes the size of a parcel into consideration, along with its weight, since size often drives the transportation costs we incur. These "shape-based" rate approaches encourage efficiency and were included in the PRC's recommended decision.

Also, Table 1 summarizes the PRC's recommended rates, along with the forecast cost coverage. As you can see, the Commission's recommended decision tracks reasonably closely with our own package, at least at the level of detail depicted in the table. The differences were primarily at the rate design level and were the subject of the request for reconsideration mentioned earlier. The Commission also recommended a different rate structure for Periodicals, which led to its delayed implementation.

I would like to provide two additional tables for your consideration. Table 2 summarizes for major classes and subclasses of mail the forecast revenue share, the revenue per piece, the forecast attributable cost per piece, the contribution (that is, the markup over attributable cost), and cost coverage. As you will see from this table, the cost coverage ranges from 100 percent for Periodicals to 212 percent for First Class letters. The average cost coverage is 179 percent.

Table 3 is similar, but provides information on rates that would exist under Ramsey pricing. These figures are only approximate for the reasons cited above and because they are based on rather preliminary estimates of demand price elasticity by class and subclass. It is worth noting, however, that the structure of rates in Table 3 is reasonably close to the structure of actual rates in Table 2. In terms of (attributable) cost coverage they range from 100 percent for Express Mail to 233 percent for First Class letters. The major exceptions are that under Ramsey pricing the rates for Periodicals would be considerably higher, and the rates for Express Mail would be considerably lower.

There is one final matter I would like to address, and that is prompted by the results just discussed. From what I have heard about this hearing and from the lineup of witnesses, I gather a major issue is the effect of Postal rate increases on publications. There are two points I wish to make. First, under current rates, *the only* class of mail that pays *only* its attributable costs, making no contribution to overhead whatsoever, is publications. Before the recent rate case publications actually paid *less* than attributable cost, meaning they were *subsidized* by other classes of mail. As we interpret the new law, we *had no choice* but to raise rates on publications. Second, I am aware of the argument made by some that raising Postal rates infringes on publications' First Amendment rights. As the Committee is aware, however, the U.S. Constitution guarantees freedom of expression, not low-cost, and certainly not subsidized, access to a system of distribution.

Thank you, Mr. Chairman, Mr. Ranking Member, and Members of the Committee. That completes my statement. I shall be happy to address any questions you might have.

# # # #

Table 1: Then-Existing Rates, BOG Rates, PRC Rates, and Cost Coverage

	Then-existing revenue per piece ($)	BOG revenue per piece ($)	PRC revenue per piece ($)	BOG Cost Coverage (%)	PRC Cost Coverage (%)
First-Class Mail					
Letters (all shapes)	0.392	0.418	0.419	212	212
Cards	0.220	0.242	0.233	161	155
Total First-Class	**0.381**	**0.407**	**0.407**	**210**	**209**
Priority Mail	**5.513**	**6.265**	**6.263**	**150**	**150**
Express Mail	**16.583**	**18.656**	**18.656**	**171**	**170**
Periodicals					
Within County	0.095	0.118	0.112	98	100
Outside County	0.266	0.297	0.297	100	100
Total Periodicals	**0.253**	**0.283**	**0.282**	**100**	**100**
Standard Mail					
Enhanced Carrier Route	0.172	0.187	0.184	209	206
Regular	0.211	0.231	0.230	170	171
Total Standard Mail	**0.198**	**0.218**	**0.216**	**179**	**179**
Package Services					
Parcel Post	3.334	3.912	3.884	113	114
Bound Printed Matter	1.079	1.205	1.205	120	119
Media & Library Mail	2.153	2.538	2.538	104	104
Total Package Services	**1.991**	**2.231**	**2.230**	**113**	**114**
International Mail	2.240	2.438	2.438	125	125
Total All Mail	**0.323**	**0.349**	**0.347**	**179**	**178**
Special Services					
Registry	11.882	17.848	13.578	86	132
Certified	2.400	2.650	2.650	148	148
Insurance	2.625	2.480	2.478	105	130
COD	6.522	7.216	7.037	113	110
Money Orders	1.336	1.498	1.454	153	150
Stamped Cards	0.020	0.020	0.020	135	135
Stamped Envelopes	0.053	0.046	0.046	104	104
Post Office Box	53.010	58.368	58.367	156	157
Total Mail & Services				**178**	**179**

Table 2: Revenue Shares and Cost Coverage Under Current Postal Rates

	Revenue Share (%)	Revenue per piece ($)	Attributable cost/piece ($)	Contribution (rev - cost) per piece ($)	Cost coverage (%)
First-Class Mail					
Letters (all shapes)	46.8	0.419	0.198	0.221	211.6
Cards	1.8	0.233	0.150	0.083	155.4
Total First-Class	**48.6**	**0.407**	**0.195**	**0.212**	**208.9**
Priority Mail	**6.8**	**6.263**	**4.181**	**2.082**	**149.8**
Express Mail	**1.0**	**18.656**	**10.946**	**7.710**	**170.4**
Periodicals					
Within County	0.1	0.112	0.112	0.000	100.1
Outside County	3.1	0.297	0.297	0.000	100.2
Total Periodicals	**3.2**	**0.282**	**0.281**	**0.000**	**100.1**
Standard Mail					
Enhanced Carrier Route	7.8	0.184	0.089	0.095	206.3
Regular	22.9	0.230	0.135	0.095	170.8
Total Standard Mail	**30.7**	**0.216**	**0.121**	**0.095**	**178.5**
Package Services					
Parcel Post	1.9	3.884	3.410	0.474	113.9
Bound Printed Matter	1.0	1.205	1.009	0.196	119.4
Media & Library Mail	0.6	2.538	2.448	0.090	103.7
Total Package Services	**3.5**	**2.230**	**1.962**	**0.268**	**113.7**
International Mail	2.5	2.438	1.951	0.487	124.9
Total All Mail	**96.3**	**0.347**	**0.195**	**0.153**	**178.4**
Special Services					
Registry	0.1	13.578	10.282	3.296	132.1
Certified	0.9	2.650	1.792	0.858	147.9
Insurance	0.1	2.478	1.913	0.565	129.5
COD	0.0	7.037	6.377	0.660	110.3
Money Orders	0.3	1.454	0.969	0.485	150.0
Stamped Cards	0.0	0.020	0.015	0.005	135.2
Stamped Envelopes	0.0	0.046	0.044	0.002	104.1
Post Office Box	1.3	58.367	37.262	21.104	156.6
Total Mail & Services	**100.0**	**0.364**	**0.203**	**0.161**	**179.3**

Table 3: Existing Rates vs. Ramsey (Inverse Elasticity) Rates

	Current revenue per piece ($)	Price Elasticity of Demand	Ramsey revenue per piece ($)	Current Cost Coverage (%)	Ramsey Cost Coverage (%)
First-Class Mail					
Letters (all shapes)	0.419	-0.155	0.462	212	233
Cards	0.233	-0.426	0.168	155	112
Priority Mail	6.263	-1.023	4.299	150	103
Express Mail	18.656	-1.645	10.958	170	100
Periodicals					
Within County	0.112	-0.141	0.165	100	148
Outside County	0.297	-0.276	0.356	100	120
Standard Mail					
Regular	0.230	-0.298	0.253	171	188
Enhanced Carrier Route	0.184	-1.020	0.093	206	104
Package Services					
Parcel Post	3.884	-1.086	3.558	114	104
Bound Printed Matter, Media, Library	1.474	-0.659	1.397	113	107
Special Services					
Registry	13.578	-0.170	14.032	132	136
Insurance	2.478	-0.243	2.346	130	123
Certified	2.650	-0.179	2.404	148	134
COD	7.040	-1.344	6.604	110	104
Money Orders	1.454	-0.600	1.023	150	106

Mr. DAVIS OF ILLINOIS. Thank you very much, Mr. Miller.
Mr. Potter.

STATEMENT OF JOHN POTTER

Mr. POTTER. Good morning, Mr. Chairman and Ranking Member Marchant and other members of the subcommittee. I appreciate the opportunity to discuss the Postal Service's approach to setting rates for periodicals, both under the Postal Reorganization Act of 1970 and the Postal Act of 2006.

Because of the length and complexity of the price change process under the Postal Reorganization Act, prices have changed every few years. As a result, periodical mailers budgets and business models have been negatively impacted by some sharp increases in those years when rates were changed. Our most recent price adjustment is a good example of the weaknesses inherent in the old system. For a number of important reasons, before our 2006 rate filing, it had been 6 years since the mailing community had the opportunity for a full examination of the relationship between the price of our services and the cost of providing them. Despite the fact that we improved network efficiencies and introduced more productive technologies to manage cost growth, our costs continued to rise over that period.

Unlike other classes of mail and consistent with the long-term pricing strategies that recognize the important role of magazines and newspapers in the intellectual, social, and political life of our Nation, periodical rates have been designed to just cover their costs. By 2006, relative cost coverage for some classes of mail had become markedly skewed. in the periodicals category, the revenue was less than our cost, a situation that did not meet the requirements of the law.

There were many individual magazines that were significantly below their cost. Even for periodicals that did cover their cost, it was not significant enough to make up for those titles that were below our cost.

In preparing our 2006 rate filing, we worked to make the cost coverage comply with the law, while doing our best to be sensitive to the pricing needs of smaller periodicals. Our proposal accommodated both of these needs, bringing cost coverage for that class to more appropriate levels, with price adjustments for publishers of all sizes held to a relatively narrow variance around the mean of about 12 percent.

Our proposal encouraged more efficient mail preparation, with an $0.85 charge for each container, large or small. Our intention was to move as much mail as possible from expensive-to-handle sacks to more efficient containers such as pallets, which hold about 40 times more mail than sacks and are more efficient to manage.

Following the hearing process, our proposal for the single, simple charge had been expanded by the Postal Regulatory Commission to 55 different rates for different types of containers and different levels of preparation, leading to wider variations in overall prices.

During the course of the rate case, we communicated frequently with mailers. We wanted to help them understand our proposal and have time to prepare for the changes. However, the outcome was unexpected. It was historically unusual, in my opinion, for the

Commission's recommendation to differ so greatly from our original proposal. After careful consideration, taking into account the complexity of the Commission's recommendation, our Board voted to defer implementation for 4 months, twice the time period allotted for other mailers.

Keeping the needs of periodical mailers in mind, we are focused on minimizing magazine and newspaper processing costs, and with the implementation of our state-of-the-art flat sequencing system, we expect to reduce costs by automating the sorting of this mail into delivery sequence.

Mail rates are a product of the mailing industry and the U.S. Postal Service working together, committed to achieving the least possible combined cost.

We are working with the periodical mailers to lower their rates by eliminating sacks and shifting their mail to pallets. Co-palletization, where you allow multiple titles on the same pallet, can be an effective strategy for smaller publishers, and co-mailing, which means you put two titles in the same bundle, for small mailers can increase the opportunity for them to take advantage of work share discounts.

Ultimately, the new price-setting process contained in the Postal Act of 2006 can prevent the difficult and contentious rate situations we experienced this year. It will also address their underlying causes and offer a welcome degree of predictability and simplicity long sought by the mailing community as we transform from a break-even financial model to one that encourages retained earnings. The new law will eliminate the irregular and sometimes sharp price increase of the old system for our market-dominant products, primarily first-class mail, standard mail, and periodicals. That is because the new law anticipates annual price adjustments that are capped at the class level by the rate of inflation.

This will allow incremental changes which will minimize the business impact of dramatic price adjustments in a single year. While the Postal Regulatory Commission has a far broader role than that of the formal Postal Rate Commissions, its role in pricing has changed considerably. Prior to a price change, the Commission reviews the new prices for compliance with the rate cap. The Commission also has the authority to adjudicate and direct the Postal Service to resolve any issues raised by customers after the new rates have been implemented.

Without the inordinately lengthy review and hearing process, the Postal Service will have the flexibility to adjust prices and product offerings promptly in response to the dynamic market conditions and changing customer needs.

This is important to our long-term success in providing everyone in America with affordable, universal mail service. The Postal Regulatory Commission, under the leadership of Chairman Dan Blair, has just taken an important step in helping us do that. Yesterday's publication of new rate regulations for our market-dominant and competitive products takes us a giant step closer to moving from an infrequent, primarily cost-based pricing model, to an annual one that is market based. We are grateful for the Commission's quick action in this area, many months ahead of their statutory deadline, and we look forward to moving toward this new pricing model soon.

In closing, I would like to thank the subcommittee for the opportunity to discuss these issues with you today, and I would be pleased to answer any questions that you might have.

[The prepared statement of Mr. Potter follows:]

UNITED STATES
POSTAL SERVICE

STATEMENT OF
JOHN E. POTTER
POSTMASTER GENERAL/CEO
BEFORE THE
SUBCOMMITTEE ON FEDERAL WORKFORCE, POSTAL SERVICE
AND THE DISTRICT OF COLUMBIA
OF THE
COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM
UNITED STATES HOUSE OF REPRESENTATIVES
WASHINGTON, DC

OCTOBER 30, 2007

Good morning, Mr. Chairman and members of the Subcommittee. I appreciate the opportunity to meet with you today to discuss the Postal Service's approach to setting prices – both from the perspective of the requirements of the Postal Reorganization Act of 1970 and the vastly changed pricing structure established by the more recent Postal Act of 2006.

Over the last decade, the Postal Service, virtually all elements of the mailing community, Congress – including members of this Subcommittee – and the Administration, have recognized the compelling need to modernize an outdated postal pricing regulatory model. It was a model created for another time, a simpler time, a time when the postal monopoly had not become virtually irrelevant through the explosion in electronic communications and the development of an intensely competitive package and document delivery market, one that includes domestic as well as international competitors.

That model was marked by a cost-of-service pricing regime, with each subclass of mail required to cover its full attributable costs and make a contribution to overall system overhead costs. It was a contentious model, with each omnibus rate adjustment marked by up to ten months of litigation before the former Postal Rate Commission, during which a wide range of intervenors would be heard, each offering data, testimony, and other information in support of their positions regarding the Postal Services' pricing proposal.

Because that pricing model was, essentially, a zero-sum game, if an intervenor was successful in influencing the Commission to recommend that its prices be less than those proposed, the difference had to be made up by obtaining those revenues from other classes or subclasses of mail. The Commission's role was to produce a recommended decision that met the Postal Service's specific, stated revenue requirement, but, significantly, the Commission was not required to adhere to the Postal Service's allocation of that requirement among the various categories of mail through its proposed prices.

There may be no better example than the most recent rate case, of the drivers that ultimately made it abundantly clear that a simplified, modern, and far more accountable pricing system was needed. This was the system established by the Postal Act of 2006.

As I mentioned, the Postal Reorganization Act required that the prices we charge for our products and services match the overall direct and overhead costs of providing those services. Over time, and for a number of reasons, we had seen some deterioration in the cost coverage of some products – most notably Periodicals, which includes newspapers and magazines. Prior to our rate filing of 2006, which led to our current price structure, we did not have a traditional rate case since 2000.

In 2001, the nation experienced a swift economic downturn following the terrorist attacks of 9/11. This affected mailing patterns and mail volume, resulting in a significant and almost immediate downturn in revenue. Only weeks later, this was exacerbated by extraordinary and pressing revenue needs for the decontamination of a number of our facilities and the protection of our network following its breach by the deadly anthrax mailings. We were fortunate that Postal Rate Commission Chairman George Omas was sensitive to our needs. Through his leadership, he influenced the greater part of the mailing community to agree to a settlement, eliminating months from the hearing process, allowing us to implement new rates quickly.

As some members of this Subcommittee may recall, the enactment of a 2003 law changed the Postal Service's funding obligations to the Civil Service Retirement System, to avoid a considerable, long-term overpayment. While this was a welcome event, it did require that, beginning in 2006, the "savings," the difference between the old payment schedule and the new, be placed in an escrow account, pending Congress' direction on how those funds would be used. To fund the escrow account – which came to $3 billion in 2006 – we filed for an across-the-board rate increase of 5.4 percent, an amount sufficient to satisfy the escrow requirement. Absent the requirement to make a cash payment into the escrow account by a date certain, we had not intended to file a regular omnibus rate case before 2006.

Because the method of disposition of both of these rate cases – each based on unique and compelling circumstances – there was not an opportunity for a full examination by the mailing community of the relationships between the rates charged for our various products and services, and our costs of providing them. During that period from 2000 to 2006, our costs continued to rise, as they did for all businesses.
At the same time, we continued to improve network efficiencies and implement more productive technologies that helped to limit cost growth for some of our higher volume products. While, in many cases, these efficiencies – including more efficient preparation by some mailers – helped to avoid large variances in cost coverage, for some categories, this was not the case.

By the time we filed our 2006 omnibus rate case, relative cost coverages had become markedly skewed, with some revenues actually below our costs – which meant we lost money on every piece handled – a situation at variance with the requirements of the law. Even for those Periodicals that were covering their costs, their institutional contribution remained significantly below that of other classes. This was consistent with the long-term actualities of Periodicals pricing strategies, which, recognizing the important role played by these publications in the intellectual, social, and political life of our nation, generally resulted in lower overhead contributions. This also reflected the Postal Reorganization Act's requirement that such factors be considered in establishing rates.

On average, the Postal Service experienced relatively steady mail volume growth from 2000 to 2006. With some year-to-year variations, total volume of 208 billion pieces in 2000 grew to a record 213 billion pieces six years later. However, a deeper examination of volume trends over that period showed that Periodicals mail declined by some 13 percent, an average of two- to three-percent a year, as publishers faced the ongoing and disruptive innovations of the internet and the increasing ubiquity of alternate sources of information and advertising.

This situation is not unique to publications whose primary distribution channel is the mail. It is also affecting some of America's largest and best known newspapers, which utilize alternate means of home and office delivery, as well as the not inconsiderable newsstand component of magazine and newspaper distribution. And print publications – both large and small – have been taking advantage of the internet by posting on-line editions of their publications, with some or all of their content available without cost.

While some larger publishers, because of the mail volumes they enter, even though tempered by some circulation declines, have been able to better manage their postal costs through more efficient mail preparation and presentation, this is not the case for all mailers. The publishers of many smaller circulation Periodicals, which do not individually have sufficient circulation density in many postal delivery areas to prepare their mail with similar levels of efficiency, have not had the same success in cost management.

As an example, many smaller publications are presented to the Postal Service in sacks containing only a small number of pieces. Because of the high degree of manual handling required to process sacked mail when compared to other, more efficient containers such as pallets, which contain far greater pieces and are less prone to bundle breakage, our labor costs for handling sacked mail are much higher. We must account for these costs in our rates.

Over the years, we have worked closely with Periodicals mailers to work toward more efficient preparation and presentation, with the intention of reducing the costs associated with handling this product, which would be reflected in the prices paid by these mailers. Significantly, in 2003, we began a co-palletization experiment – supported by a rate structure that reduced per-piece prices by less than one cent – to encourage the mixing of multiple publications from multiple publishers on pallets. This very small price incentive contributed to a 50 percent increase in the use of pallets for Periodicals by 2005.

As we prepared our 2006 rate filing, one important goal was to continue to try to correct the imbalances in cost coverage that had developed over the years. Through our day-to-day contacts and communications with publishers, particularly those with smaller circulations, they were clear in explaining their understandable sensitivity to larger rate increases. As we developed our pricing proposal for filing with the former Postal Rate Commission, we were able to accommodate both of these needs. Cost coverage would have been revised to more appropriate levels and price increases – not only for small publishers, but for medium and large ones as well – would have been limited to a relatively narrow variance around the mean.

Another goal was to provide mailers with incentives to move to more efficient mail preparation and presentation. To accomplish this goal, we proposed a container rate of $0.85 for Periodicals. In practice, this would mean that the container rate for a sack would be the same as the container rate for a pallet – which holds about 40 times more mail than a sack. Mailers could save by moving to fewer and larger containers.

However, as I noted earlier, the rate-setting process established by the 1970 law is complex, with any gain for one mailer involving a loss for another. By the time the Postal Rate Commission issued its recommended decision, the process had expanded the rate bands of our original Periodicals pricing proposal considerably, with the greatest variances for smaller publications. Our proposal of a price adjustment of about 12 percent was accepted. However, some smaller publications saw prices increase by as much as 25 to 30 percent, with prices lowered for other publishers.

Following the long months of hearings, our proposal for a simple container charge of $0.85 was expanded to 55 different rates for different types of containers and different levels of preparation, which led to the wide variation in price increases experienced by different publishers.

During the course of the rate case, we communicated frequently with the mailing community about the Postal Service's rate proposal to assist in their understanding of what they might expect so they had sufficient time to begin preparing for the changes. We also provided an unprecedented number of opportunities to comment on the proposed mail preparation requirements that would be necessary to support the Postal Service's proposed new rate structure. While it would be unrealistic to expect any customer to be pleased with a price increase – for mail or any other product or service – it was our intention to provide as much information as possible to ease the transition to the new rates and preparation requirements when the process was complete and rates were ultimately adjusted.

In this instance, however, I believe it is fair to say that the outcome was unexpected. It was historically unusual for the Commission's price recommendations, produced through ten long months of the litigious 1970 rates process, to differ so markedly from our original proposals. Because of the extraordinary complexities of the recommended Periodicals pricing decision, the Board of Governors voted to defer implementation for four months – granting Periodicals mailers twice the amount of preparation time provided to other mailers. We did not believe it would be possible for either mailers or the Postal Service to complete rates software and supporting mailing standard changes more quickly than that.

Another contentious element of the outcome of the 2006 rate case involved Standard Mail flats – primarily catalogs. As our processing and transportation networks continue to evolve and become more sensitive to the shape of an item rather than its weight, we crafted our pricing proposal to encourage mailers to align their mail with the changed capabilities of today's processing system.

Over the past two decades, we have made a tremendous investment in letter mail automation, including sorting mail into the delivery sequence on each carrier route, unlike Periodicals, which are entirely flats. Because letter mail volume (156 billion pieces in 2006) and its attendant revenue is significantly higher than that of flats mail (54 billion pieces) or packages (3 billion pieces), our technological advances in mail processing have focused primarily on development in this area, as it has offered the greatest return on investment.

Our pricing proposals reflected this fact, with rates more closely aligned with the actual costs of processing mail of various shapes, with the lowest costs for letters, even those of the same weight as differently shaped pieces. In some cases, such as heavier letters, our proposal actually called for lower prices. From the time we first announced our rate proposal, through the review and hearing process, and well into implementation, we have been advising mailers to shift to more advantageous shapes – when appropriate, based on their business needs – to benefit from this new approach to pricing.

We were optimistic that the merits of this technique would gain the acceptance of the Postal Rate Commission, which turned out to be the case. However, neither we nor the larger mailing community anticipated that the recommended decision would take to this approach far more aggressively than we had proposed. As a result, rates for Standard Mail flats far exceeded those we had proposed. It was our intention that this process of promoting a shift to more efficient shapes be more gradual.

Like the catalog mailers, the Governors of the Postal Service felt the more moderate pace represented by our proposal was preferable, addressing the needs of the Postal Service and better representing the needs and abilities of mailers, and avoiding the disruptive effects of rate shock. And, because catalogs generate a great deal of additional mail through orders, payments, and order fulfillment, we did not want to place catalog volume at risk. That would have been damaging to our business, to the catalog business, and to the suppliers and partners of the catalog companies. As a result, the Governors requested that the Commission reconsider its decision, suggesting a reduction in flat rates and a slight increase for letters.

The Commission's response recommended a limited rate reduction that would last for an eight week period. Rates would then have reverted to the higher levels previously recommended.

Unfortunately, this would have cost the Postal Service some $100 million in revenue and many mailers would have been unable to make necessary system and software adjustments in time to take full advantage of the reduction. The Governors reluctantly voted to proceed with the Commission's original recommendation. In addition, despite the Periodicals and Standard Mail recommendations, the Commission met the Postal Service's revenue requirement – although assigning revenue burdens differently than our proposal – which was within its authority, limiting the basis of any objections on our part.

Looking ahead, we will continue our work with the industry to help find ways to manage our costs and those of the mailing community. The development and implementation of the Intelligent Mail Bar Code is one tool we have been using. Used by an increasing number of mailers each day, this code will contribute to better address practices, improving address accuracy, and reducing undeliverable pieces. There are billions of dollars in potential savings in this area.

As we focus on shape-based processing, we are making better use of our equipment by commingling Periodicals Mail and Standard Mail. While this does not affect the delivery standards or delivery performance for either class of mail, it does reduce our processing costs by increasing the throughput and efficiency of our automated sorting equipment. Mailers of both classes will benefit.

By the end of the year, we will be deploying the first production model of our state-of-the-art automated Flats Sequencing System. This will sort larger envelopes, Periodicals, and catalogs into the actual sequence mail is delivered on each carrier route, greatly enhancing sorting and delivery efficiency. This operation is currently performed by costly manual sortation. As we work toward full deployment of this equipment, its efficiency gains should improve the outlook for flats prices.

The ultimate success of all of these initiatives will depend on strong participation by the mailing industry. This transformation will take time to complete, but the Postal Service believes these steps will result in a more efficient, responsive, and business-like organization, as foreseen by the Postal Act of 2006.

But beyond the changes we are making to our own operations to offset costs, mailers will also benefit by the new rates process established by the new postal law. We welcome these changes.

We also believe that there are actions that can be taken by Periodicals mailers to lower their mailing costs. Eliminating sacks and shifting mail to pallets is one example. By doing this, mailers would see an immediate reduction in their total container charges and could qualify for deeper drop-shipping discounts. In the longer term, because palletized mail can be handled more efficiently than sacked mail, savings to the Postal Service would be reflected in future price changes. Where palletization may present challenges to publishers with smaller circulations, we encourage co-palletization, which would bring the cost benefits of palletization to each participating mailer. And co-mailing with other mailers can increase opportunities for workshare discounts.

Overall, the new rate regime offers a degree of predictability and simplicity that will be advantageous to mailers. We also believe it can avoid the contentious situations we experienced this year.

Pricing postal services will no longer be an adversarial process. Granting the Postal Service the ability to transform from a break-even financial model to one that encourages retained earnings for reinvestment means that the rates process will no longer be a zero-sum exercise.

Price changes for our market dominant products – primarily First-Class Mail, Standard Mail, and Periodicals – will now be capped by the rise in the Consumer Price Index on an annual basis, eliminating the irregular and sharp increases under the old system.

The role of the new Postal Regulatory Commission before the implementation of new prices will be to review them to be sure that they have not exceeded the cap. The Commission will also have the authority to accept and adjudicate issues raised by customers after new rates have been implemented, and direct the Postal Service in their resolution.

And without an inordinately lengthy review and hearing process, the Postal Service will have the needed flexibility to adjust prices and product offerings quickly in response to dynamic market conditions and customer needs.

In closing, I would like to thank the Subcommittee for the opportunity to discuss these issues with you today. The Postal Service would also like to acknowledge the untiring efforts of the Postal Regulatory Commission in helping to implement the provisions of the new law, and we look forward to implementing a new pricing structure as envisioned by Congress.

I would be pleased to answer any questions the Subcommittee might have.

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Mr. DAVIS OF ILLINOIS. Thank you very much, Mr. Potter.

Chairman Blair.

STATEMENT OF DAN G. BLAIR

Mr. BLAIR. Chairman Davis, Ranking Member Marchant, members of the subcommittee, last April I had the opportunity to appear before you in an oversight hearing with the two gentlemen to my side to take questions on the operations of the new Postal Regulatory Commission. At that time, the rate case was still fresh, and I had announced an ambitious schedule for the PRC to have in place by October new rules for a new price cap system, as envisioned by the enactment of the Postal Accountability and Enhancement Act.

Mr. Chairman and members of the committee, I am pleased to report that the Commission has accomplished that goal. The rules were posted on our Web site yesterday. I am extremely proud the Commission has completed its task 8 months ahead of the statutory deadline. I want to thank my fellow Commissioners, two of whom are in the audience today—Commissioner Mark Acton and Commissioner Don Tisdale—and the staff of the Commission for their hard work and dedication to accomplish this substantial goal.

I know many Members still have questions regarding the previous rate case under the old system. I am happy to answer them from the Commission perspective. In my opinion, that case highlighted many of the problems of the old system: lengthy in time, litigious in format, and a zero sum gain. The ratemaking structure provided little incentive for the Postal Service to contain costs.

This subcommittee led the 10-year fight for postal reform because you believed that the system needed reforming. Some fought hard against that reform, but the leadership of Representative McHugh, Chairman Davis, full committee Chairman Waxman, and then-Chairman Tom Davis paid off. Together with the Senate and the administration, a bill came forward that the President signed last December.

This last omnibus rate case was the first fully litigated case since 2000. It was preceded by two subtle rate cases which, because they are a negotiated nature, prevented the Commission, the Postal Service, and mailers from addressing the growing cost imbalances, operational concerns, or the Postal Service's desire to move to shape-based pricing.

While lengthy and litigious, the last case presented ample opportunity for public participation and comment. Sixty parties participated in the hearings, which were open to the public and broadcast live by way of the Internet. Thirty-nine witnesses filed 139 submissions of testimony, all of which remain available for public review. In fact, most of the witnesses appearing today participated in our proceedings, either individually or through their business or professional associations.

Our recommended decision in this case had the unanimous backing of all five of the Commissioners.

The contrasts between the old and new systems are quite stark. Under the old system, the Postal Service set forth its revenue requirement. The Commission then had to apportion the required

revenue among the classes of mail. That system produced winners and losers.

The new, modern system of ratemaking is designed with an eye toward predictability and stability and doesn't play the zero sum gain. For most postal products, rate increases will be tied to consumer inflation, thereby giving incentive to the Postal Service to keep its costs at or below increases in inflation.

The Postal Service has the flexibility to increase rates for its market-dominant products, subject to the price cap; however, its actions will be monitored and regulated by newly empowered Postal Regulatory Commission. The Commission and the Postal Service have a full agenda ahead in implementing the requirements of the act. Having the new system in place sooner rather than later allows us the opportunity to focus on the task ahead and hopefully avoid an old cost of service rate case.

We are now in the 9th month following our recommended decision. While some are still battling the old case, I am very pleased that we can present you with a new system that will avoid the pitfalls of the past and provide a stable and predictable rate environment for mailers. I suspect that, had the Commission done things different in the last case, a different set of witnesses would be here today airing their concerns over how the Commission had done its work.

My written statement fully addresses our actions in this hopefully last rate case under the old regime.

I look forward to working with Members of Congress, Chairman Miller, Postmaster General Potter, and the mailing community to ensure that this new law and the new structure which it produced benefits our entire postal system.

I look forward to responding to your questions.

[The prepared statement of Mr. Blair follows:]

Testimony of

The Honorable Dan G. Blair, Chairman

On behalf of the

Postal Regulatory Commission

Before the

U.S. House of Representatives

Committee on Oversight

And Government Reform

Subcommittee on Federal Workforce,

Postal Service, and the District of Columbia

October 30, 2007

Postal Regulatory Commission Chairman Dan Blair
Statement before the House Subcommittee on Federal Workforce,
the Postal Service, and the District of Columbia
October 30, 2007

Chairman Davis, Ranking Member Marchant, and members of the Subcommittee, thank you for inviting me to testify today. I appreciate the opportunity to discuss with you the Postal Regulatory Commission's Recommended Decision to the Postal Governors on the R2006-1 rate case.

Before doing so, however, I am pleased to report that yesterday afternoon the Commission issued its final order establishing regulations governing the modern ratemaking systems for market dominant and competitive products. The rules are posted on our website and have been submitted to the Federal Register for publication. My fellow Commissioners and I are extremely proud to have completed this essential and critical requirement of the Postal Accountability and Enhancement Act (PAEA) a full eight months ahead of the statutory deadline. On behalf of the Commissioners, I thank all who participated in shaping these regulations – commenters, witnesses at our field hearings, the Postal Service, and most importantly, the Commission's hardworking staff.

Having these new regulations in place allows everyone whose lives are touched by the U.S. Mail to move squarely into the flexible environment offered by the PAEA. These rules provide the Postal Service with the ability to adjust rates immediately for market dominant products, such as those under discussion today, within a Consumer Price Index (CPI) cap. The Postal Service now has the tools to balance their near term needs with future goals.

No longer will the Postal Service be constrained by the old cost of service regime. I am hopeful that the early release of these regulations will obviate the need for one last omnibus rate case under the 1970 law. Transitioning now into this new ratemaking system will let the Commission and the Postal Service devote our resources to other mandates of the PAEA, including service standards and service performance goals.

Let me now turn to the subject of today's hearing – the rates recommended by the Commission and approved by the Postal Governors. First, it is important to understand that the last omnibus rate case, Docket No. R2006-1, was the first fully litigated case since 2000. It was preceded by two settled cases, which provided the Postal Service with needed revenue, but did not address growing costing imbalances, operational concerns, or the Postal Service's long-term interest in moving to shaped-based pricing because of the negotiated nature of these settled cases.

As background, in May 2006, the Postal Service filed a request with the Commission for a recommended decision on proposed changes in postage rates. Between the time of this filing and our decision on February 26, 2007 – when we sent our recommended decision to the Postal Governors – 60 parties participated in open hearings and public comment periods before the Commission. We reviewed 139 submissions of testimony from 99 witnesses. In fact, most of the witnesses to appear before the Subcommittee today participated in our proceedings either individually or through their business associations. Three weeks later, on March 19, 2007, the Governors adopted the Commission's rate recommendations with three limited exceptions: the rate for the Priority Mail Flat Rate Box, the First-Class Mail nonmachinable letter surcharge, and rates for Standard Mail flats.

Understanding that the rates recommended by the Commission to the Governors in this past rate case were based on the 1970 law is significant. We were guided by the principles that:

- Rate differences should reflect cost differences;
- Rates should be based on paying for what you use;
- Rates should generate efficient mail streams that help control costs and keep postage rates reasonable; and
- Rates should be fair and equitable.

For example, costs for First-Class and Standard Mail letters have remained essentially flat over the past 10 years and as a result, the rates for that mail have been fairly stable. This is in sharp contrast to the spiraling costs associated with the handling of Periodicals. For many years, the Commission has sought to keep Periodicals postage rates as low as possible in the face of declining magazine mail volume and increasing Postal Service handling costs. The cost inefficiencies inherent with Periodicals were not new, and the Commission, the Postal Service, and mailers have sought alternatives for years to deal with these rising costs and declining

volumes. Despite increased incentives and cost reduction programs, little progress was made in restraining Periodicals cost increases.

Both mailers and the Postal Service have pushed the Commission to resolve this problem. By the late 1990s, it became apparent that the rate structure for Periodicals needed to recognize better the cost drivers contributing to the spiraling costs of processing this class of mail.

Knowing that magazines make the lowest contribution to overhead of any class of mail – roughly $3.6 million to fund almost $35 billion in overhead costs – was a factor in our recommending a rate structure based on paying for what you use, that will encourage better operational practices, and help eliminate unnecessary costs. This new rate structure has evolved over time through the Commission's open and transparent ratemaking and complaint process. The five Commissioners were unanimous in their support for a refinement of Periodicals rates, which we believe will stem the tide of rising costs for a class of mail whose revenue falls far short of supporting its costs to the Postal Service.

The Commission's decision was grounded in the need to balance any new rate structure with our long-standing principle of promoting the free flow of ideas. This principle would be compromised should this class of mail become unsustainable due to rising costs and declining volume. We believe this principle is firmly embedded in our decision. Our recommended decision continues to preserve and foster the continued widespread dissemination of political and cultural thought.

In our recommended decision, we increased the editorial discount available to all magazine mailers. In fact, under our approach – and based on the sampling of publications information provided by the Postal Service during the rate case – we found that our recommendation allowed small publications, those with circulations of 15,000 or less, lower increases than under proposals made by the Postal Service or large magazine interests. The Commission exercised its discretion by increasing the editorial discount, protecting the smallest publications, and minimizing the institutional cost burden for all magazine mailers.

Another area of interest to the Subcommittee is the Commission's decision on Standard Regular flats. As with Periodicals, the Commission's recommendation was based on evidence developed in open administrative proceedings, in which all interested parties had ample opportunity to intervene. Our decision properly relied solely on the evidence presented.

In its previous rate decision, the Commission emphasized its concern that because of two consecutive settled rate cases, the misalignment of rates and costs in Standard Mail was getting worse. We warned the postal community that the upper bounds of "normal" rate increases might have to be extended in the next case to allow for the re-alignment of rates with costs. In R2006-1, the Presiding Officer issued an information request focused on whether cost differentials justified proposed rate differentials, and the Commission issued two Notices of Inquiry asking the postal community to provide comments on how to design rates that would best align rates with costs, especially, shape-based cost differences. The Commission was open to all suggestions, but in the end, the principle of productive efficiency overwhelmingly dictated that, to the extent practicable, rate differences should reflect cost differences within a product line like Standard Regular mail. No party to R2006-1 should have been surprised that the rates recommended by the Commission began to move toward this goal.

The Postal Governors asked the Commission to reconsider its recommendations in three areas, including Standard Regular flats. On March 29, 2007, the Commission issued an Order establishing procedures for further consideration of these issues and invited public comments from interested parties. On April 27, 2007, the Commission recommended to the Governors that the rate for the Priority Mail Flat Rate Box be lowered and that letter-shaped First-Class Mail nonmachinable surcharge be expanded. The Governors accepted these recommendations. We also issued a separate Order granting late notice of intervention filed by the Coalition of Catalog Mailers allowing this party to intervene in the reconsideration of the Commission's recommendations on Standard Regular flats.

On May 25, 2007, we issued a Second Opinion and Recommended Decision on Reconsideration which recommended a transitional, temporary rate reduction of three cents ($0.03) for all Standard Mail Regular flats and two cents ($0.02) for Standard Regular Nonprofit flats to address concerns raised by the Governors. The difference between Standard Mail Regular flats and Standard Regular Nonprofit flats is due to a 2000 law that sets the average revenue per piece for nonprofit mail at 60 percent of the average revenue for commercial mail.

The Commission's May 25, 2007, proposal was rejected by the Governors. Our recommendation would have accomplished several goals, including leaving Standard letter rates untouched while allowing the Postal Service's projected revenues to meet expected costs. In addition, the Commission's proposal would have provided mailers with additional time to adjust to the higher new rates, just as with the new Periodicals rates that went into effect two months after the general rate increases. We were also mindful that a number of those who commented on the issue, strongly argued that it would be improper to shift the financial burden associated with lowering catalog and flats rates to other, less costly-to-process mail. The Commission agreed unanimously with that concern.

In summary, the Commission believes its recommended rates under the R2006-1 decision provide the foundation for future rate setting under the CPI-based ratemaking system required by the PAEA. With the new ratemaking systems in place early, the Commission is providing the Postal Service with the means to adjust rates quickly in light of changes occurring in the industry, as well as adjustments to meet financial needs. We look forward to working with Members of Congress and the Postal Service to ensure that this new law benefits both individual mailers and business mailers.

Thank you again for the opportunity to appear today before the Subcommittee, and I look forward to responding to your questions.

Mr. DAVIS OF ILLINOIS. Thank you very much, Mr. Blair.

We will now proceed with questions for the witnesses.

I would like to begin with you, Chairman Miller. The Postal Service has a program in place to automate the carrier sequencing of flat mail. That is the flat sequence and sorting called FSS system. Do you anticipate that this will significantly decrease the cost of handling periodicals? What is the timeframe for the deployment and full implementation of the FSS system?

Mr. MILLER. Thank you, Mr. Chairman.

A couple of years ago the Board visited a plant in Indianapolis where they were beta testing the system. We have approved major acquisitions of flat sequencing systems, and we anticipate those coming on-board in sequence over the next several years.

We think it has the potential of lowering the cost, as well as improving the service offered to publications. In that event, of course, it at least holds out potential of giving some rate relief to publications, but we will just have to see how that system works.

We have confidence that it will pay off handsomely, but how handsomely we are not sure, and we are not sure how differentially it will affect each of the various classes of mail. But there is a great deal of potential there for publications.

Mr. DAVIS OF ILLINOIS. The subcommittee has had a tremendous amount of inquiry relative to international charitable mail. What is the Board's position on international charitable mail?

Mr. MILLER. Well, as a business proposition, we think that all mail, whether it is charitable or not, should cover the relevant attributable cost plus some contribution to overhead. We have addressed the question of international mail. I suspect what you have heard is about the so-called M-bags that is of great controversy. I think that would be best addressed by the Postmaster General.

Mr. DAVIS OF ILLINOIS. In a recent case involving review of a negotiated service agreement, the Bank of America, NSA, the Postal Service gave the Postal Regulatory Commission data that was 8 years old. Of course, the PRC rejected that data as not being data that they could effectively use.

Mr. MILLER. Right.

Mr. DAVIS OF ILLINOIS. As chairman of the Board, would you agree with me that the PRC must get the best possible data to make use of when they are trying to evaluate and make a determination?

Mr. MILLER. I absolutely agree, and I think that was a serious oversight, and the Board of Governors is not happy about that. We are addressing that issue in a serious manner.

Mr. DAVIS OF ILLINOIS. You indicate that you are addressing it. Would you amplify a little bit?

Mr. MILLER. I have asked the Inspector General to look into the matter and to give us a report, and he anticipates giving us a report in the next several weeks.

Mr. DAVIS OF ILLINOIS. Thank you very much.

Mr. Potter, does the Postal Service intend to introduce a new rate case before the end of this year?

Mr. POTTER. The Board of Governors decides whether or not we are going to implement a new rate case or introduce one this year. Just yesterday, late yesterday afternoon, we received a final rules

and regulations for the rates process under the new law. We are in the process of evaluating that and giving a summary of that information to the Board so they can render a decision, hopefully at their Board meeting in November, as to what path we will choose. But it is not my decision; it is the decision of the Board of Governors, and we will, after evaluation of the rules that have been published, make a recommendation to them, but it would be premature for me to say right now.

Mr. DAVIS OF ILLINOIS. Let me ask you, regarding the elimination of international surface mail and its negative impact on some of the humanitarian issues and causes, how can the Postal Service address these concerns?

Mr. POTTER. Mr. Chairman, if I could just describe, international mail is probably our most complex rate area. M-bag service is a service that was designed to move on ships around the world. Over the last few years, the volume of mail that was sent on the M-bags has been declining. In addition to that, our ability to get service to many of the countries where the charitable organizations sent their books has been eliminated or limited severely. So in many cases we found ourselves flying mail just to make sure that it got there.

So as we looked at the international rates, we decided to recommend to the Governors that we eliminate those surface movements because of a lack of market interest, as well as the fact that we had, in many cases, been forced to fly the mail and were losing money on it.

That is not to say that we are not insensitive to the needs of the charitable organizations, and we are looking at ways under the new rate structure that we might be able to accommodate them. But suffice it to say it is a very difficult market, a declining market, and one where service simply is not available to us.

Mr. DAVIS OF ILLINOIS. We are going to have a second round, and so I am going to shift and go to Mr. Marchant.

Mr. MARCHANT. Thank you, Mr. Chairman.

This will be a question for all panel members. With the continuing pressure on postal mail being lost to electronic means, what measures is the Postal Service taking to attempt to minimize these losses?

Mr. POTTER. Well, first of all, the Postal Service is doing everything it can to increase the level of service that we provide to America, because if we provide a good level of service we are obviously providing value, and that will help us keep the mailers that we have and grow new mailers.

In addition to that, we are looking to take cost out of our system wherever it is practical, so efficiency is a paramount issue for us.

Third, we are looking to grow and take advantage of the inherent value of the network that we are very proud and honored to be able to work for.

So over the course of time you have seen people who traditionally have not used mail, such as folks who rent DVDs. It is now a market advantage to use us to deliver DVDs. We are looking at other places where we can do that.

The key going forward for us, though, is to ultimately improve the quality of the product we have, the efficiency of the product we have. One of the big steps we are going to take is to introduce an

intelligent mail bar code that will allow us to track and trace every piece of mail. Once we are able to do that, I think it is going to open up a world of opportunities for new products and will increase the use of mail.

The threat from the Internet is very real. It is not something that we can compete with head-on because of costs. But I think we can complement the Internet and find places in the market where we fit and where people will value the service that we provide.

Mr. MARCHANT. Mr. Blair.

Mr. BLAIR. I think a good way to answer that question is how it turns on to ensuring the viability of the postal system in the United States. From the regulator's perspective, we are moving in the right direction in that area. First we introduced the new rate structure for market-dominant, competitive products yesterday. I think that will help us lead toward an environment that will see more predictable and stable rates, and that way the customers can better plan their business cycles according to how those rates are going to be increased. Generally speaking, they will be capped at inflation.

We are also looking at how you bring value to the mail. From the regulator's perspective, we have been joined with the Postal Service over the course of this past summer in consultations over the development of service standards and how to measure those service standards. If you have a product, you need to know how it is going to perform and you need to be able to measure it, so the Commission has been bringing value to that respect by working with the Service to ensure that these standards are, in fact, realistic, don't impose new costs on the system, but are viable and allow customers a realistic idea of how well their mail is going to be received into the system.

Also, from the regulator's viewpoint, we are going to bring transparency and openness to the system. We will be looking at financial data. We will be looking at the competitive playing field. And we will be looking at the ways the Postal Service is offering its new products and a whole host of other things down the line. We are charged with doing numerous new studies, as well.

I think that from that perspective I don't know if it will stem the loss so much as you may bring value to the mail and bring value to the system, ensuring the viability of that system as an integral part of our economic sector.

Mr. MILLER. Mr. Marchant, first I want to assure you the Board of Governors is committed to growth as well as cost cutting. Growth means new innovations, service improvements, just the kind of thing that the Postmaster General was speaking about.

The second thing is there is an empirical question, and that is to what extent has the e-mail phenomenon or the electronic bill-paying and all sort of run its course. Is it going to accelerate or is it going to bend over in terms of the rate of its growth. That is something that, frankly, I am frustrated because I don't have good numbers on. I am asking some of the people at the Postal Service to do some more research about.

Keep in mind that electronic communications both create new messages as well as divert messages. And, as Jack I think referred to, there are ways in which electronic mail and electronic commu-

nications can be complementary to Postal Service, and vice versa. I mean, a lot of people order things electronically and get them delivered by us. A lot of mail comes and suggests people to order things electronically. So there is a symbiosis here that we need to explore, as well.

Mr. MARCHANT. Well, I will tel you, from my personal observation, that there are at least three different ways now that I use the mail that I didn't use even a year ago. The movies is one of them. I am now finding that a lot of the stuff that I am ordering on the Internet is coming by the Postal Service instead of UPS or one of the other dreaded three or four. And I am finding that—maybe it is because I am getting older or I don't know what it is—I am getting about twice the amount of print mail, the catalog mail, than I was a year ago.

In my household, the growth of our mail is actually growing. Our kids are out of the house now, but our mail is now actually growing and we are getting more mail now than we did a year ago and are using the Postal Service more heavily.

Mr. MILLER. The loss is really in the first-class mail. That is really where it is limited.

Mr. MARCHANT. Yes. The first-class mail is fairly non-existent, except for those constituents that feel like it is the most effective way to get to me. And it is.

Mr. MILLER. Yes.

Mr. DAVIS OF ILLINOIS. Well, I'm glad that you get time to watch a movie every once in a while.

Mr. MARCHANT. Yes, between 2 and 4 a.m.

Mr. DAVIS OF ILLINOIS. Right on for you.

Ms. Norton.

Ms. NORTON. Well, we, of course, have to accept and indeed have pressed the business model that is being used now and obviously will have differential effects. I am concerned about the difference between mass periodicals that have advertisers and small periodicals that thrive simply on what they have to say and for whom, therefore, the postal rates are a large cost of doing business.

Rates have reflected this difference before, and you now have some saying that essentially you are raising rates at such a rate some allege that they expected rate hikes, for example, for catalogers and small periodicals, in the range of 9 to 12 percent, and that it could be as much as 20 to 40 percent.

It seems to me very important to encourage efficiencies of these periodicals, as well as everybody else, including the Postal Service, but I wonder if you truly believe that the special circumstance of small publications with little or no advertising has been taken fully into account, and that these rates are bearable by such publications with efficiencies. Or do you envision that perhaps they are going to go out of business and so be it?

Mr. MILLER. Ms. Norton, let me reply by saying first of all we delayed the implementation of the increases to give the publications a time to gear their software to the new rate system. Second——

Ms. NORTON. To do what?

Mr. MILLER. To give the publications time to change their software to reflect the new rates.

Ms. NORTON. Does that respond to my question? Will any kind of adjustments of software make up for the difference between what very small periodicals who have no advertising can do with large increases that come at one time, and mass mailers or periodicals like Time Warner, for example, who depend on advertising as much as or far more, and who have, of course, a great deal of advertising.

Mr. MILLER. I am trying to be responsive, Ms. Norton. I am saying that our delay in implementing the new rates helped the small as well as the large.

In terms of the small, we have recently changed our rules to make small publications eligible for the lower rates, depending on editorial content versus advertising, and so forth. We have bent over backward to accommodate them in that fashion.

But we are required by law to charge attributable costs, and so we did raise the rates.

You settle on an important point here, or you focus on an important point, and that is that under this new rate package—and I am sure that Chairman Blair wants to explain this, as well—some of our rate packages to which larger publications can more easily be accommodated or could pool their publications, they weren't hit as hard as some of the smaller ones. But the prices do reflect. I mean, we might have some differences here and there, but, I mean, by and large the prices do reflect the cost, the higher cost that the Postmaster General was alluding to earlier that palletized costs are lower than individual cost handling bags, and so forth. We had to make them reflect those differences in cost.

Mr. POTTER. Ms. Norton, if I could?

Ms. NORTON. Yes, Mr. Potter.

Mr. POTTER. I am concerned about periodicals, in general, and moving forward. We are very concerned about our ability to live within the rate cap for periodical mail.

There are a number of ways that I think we have to go about the business of addressing them. First, we have to help periodical mail grow, because overall in the industry there is a debate about editorial versus advertising content—and don't get me wrong, it is a laudable debate and it is one that you could easily get into. From the person who is trying to, again, run it as a business, I prefer to have very thick periodicals that pay a higher rate.

Ms. NORTON. But how do you get periodicals to grow in the Internet and technological climate we have today? That is an interesting notion.

Mr. POTTER. Well, it is, but there have been things that would preclude you from putting a periodical into the mail, and what prices they could charge. For example, there used to be a nominal rate that said that you had to charge somebody for a subscription if you used the mail at least 50 percent of what the newsstand price was, the basic rate was. So whatever the basic subscription rate is, you had to charge at least 50 percent of that for the folks that bought the publication. We have lowered that to 30 percent to give them pricing flexibility so they can help grow the number of magazines they had.

As the chairman was just saying, we ended up, and we have worked with them to try and improve those magazines that are

starting a new launch to enable them to take advantage of using the periodical mail stream long before they have sufficient publications to qualify. So it is a way of easing their way into new hard-copy magazines.

In addition to that, we want to make the system as efficient as we possibly can, and so the notion is that everybody is going to have to change. The Postal Service will change by trying to make its operations more efficient. As the chairman alluded to, we have a flat sequencer, and I said earlier to try and make that more efficient.

In addition to that, we have a committee that we work with, Postal Service one-on-one, a periodicals advisory group that has newspapers and magazines of all sizes to come together and to look at the issues from an industry standpoint, and it involves not only the Postal Service and the periodicals as well as the suppliers, because there are printers out there, logistics companies. The notion if we could bring the mail together and process it in bulk, more of the work could be done during the printing process.

Change is tough. I am not trying to negate the fact that this change will be difficult.

We also have a broader group called the Periodical Operation Advisory Group that is part of the Mailers Technical Advisory Committee, where we have people from outside of periodicals who are helping us trying to address this problem. But the notion that the business challenge is we have a declining mail base because, as you alluded to, magazines are going online now, as well as in the mail. We have a declining mail base, and that mail is being delivered to a growing delivery base. It is a very challenging issue.

Ms. NORTON. As I said in my own opening statement, I think you and most of these periodicals are in the same boat.

Mr. MILLER. Right.

Ms. NORTON. Indeed, the very small opinion periodicals I am talking about who don't rely on any advertising do seem to me to be an alternative, particularly since they often cater to fairly high income and educated people, and that is go online. It seems to me that one of the challenges you face, just as they face the challenge of meeting the postal rates—and I am the first to understand the challenge you face. You, in fact, serve the public, and that has to be my first concern. But, just as you face those challenges, it seems to me that for these periodicals the technology is a much more viable alternative than for many of your customers.

Mr. Blair.

Mr. POTTER. I would agree with that.

Mr. BLAIR. I think two points I would like to bring out. One fundamental question is why are these costs so high in the first place. We have seen in first class and standard class over the last 10 years the cost remain fairly constant. In periodicals they have shot up by about 50 percent.

Over the last 10 years, periodicals as a class has lost about $3 billion. They failed to cover $3 billion of their direct costs, and they have made virtually zero contribution to the institutional costs of the Postal Service.

So it is not that it was a robust class of increasing volumes and increasing revenues; it is just the opposite. So with that you need to ask the second fundamental question of: then who pays?

Ms. NORTON. Who pays? And how much do each pay?

Mr. BLAIR. Exactly. And do you ask the smaller periodical? It is really not a question of size so much, although size does have a bearing on it, but it is efficient versus inefficient, or lack of efficiencies. Let's put it that way. And the question is who pays.

If you can't engage——

Ms. NORTON. You can talk efficiencies when you are talking about large periodicals. It is very hard to talk efficiencies when you are talking about these small opinion periodicals and magazines——

Mr. BLAIR. You are correct.

Ms. NORTON [continuing]. For whom efficiencies of scale are simply unavailable, sir.

Mr. BLAIR. You are correct, and so the question then still becomes fundamentally who pays. Do you ask other mailers to pick up those costs?

Ms. NORTON. Well you ask them to pay. As I say, the question is I don't think they expected not to pay any of the institutional costs; I think the question is how much can we reasonably expect them to pay without driving them either out of business or into another mold which would not be available to the Postal Service at all.

Mr. BLAIR. But who picks up the deficit? That is the question. Do you ask other mailers? Do you ask the postal system to absorb it? Do you ask rate-payers? Do you ask taxpayers? That is the question.

The rates that we recommended in the last case were cost-based, and those were consistent with the Postal Reorganization Act in 1970. We now have a new system. Hopefully you won't see the rate spikes, the rate shocks under the new system because it is capped at the class. But the fundamental question is: who pays when you have these high costs?

Mr. DAVIS OF ILLINOIS. Thank you, Ms. Norton. We are going to have another round, and I am going to go to Mr. McHugh.

Mr. MCHUGH. Thank you, Mr. Chairman.

Let's talk about costs. How much costs are we talking about here if this Congress decided, because I think there is a lot of sympathy that there is a political content value of these mailers, and we wanted to hold them harmless, how much money would have to be found either from the taxpayers or from within the system? I suspect about $500 million, but is that about right?

Mr. POTTER. Well, under the recently adjusted rates, there is nothing. I mean, they are going to cover their cost. The question is how much relief do you want to give. I think at that point you can decide what the number is.

Mr. MCHUGH. But the rate increase for this group that was put into place, as we have been told ranging from 5 to 45 percent, depending on where they fell on the efficiency spectrum, all told, the information I had was around $500 million, ball park.

Mr. POTTER. I think it is probably half that.

Mr. MCHUGH. Half that?

Mr. POTTER. Yes.

Mr. MCHUGH. So $250 million?

Mr. POTTER. And if you talk about the difference between that and the average price increase, it would be half that again, so it would be about $125 million.

Mr. MCHUGH. So what we would be reassessing and what Mr. Blair and his Commission would have to do is reassess that $100 million if the law provided you the flexibility to do that, assess that $100 million across others, yes? That is a question, Dan.

Mr. BLAIR. I would have to go back and look at the figures on that. Mr. Potter is correct that the class, as a whole, now covers all its cost, how you apportion it within that class. if you capped it for some mailers and not for other mailers, I would have to go back and check the record to see exactly how much that would be.

Mr. MCHUGH. Well, it seems to me as a Congress, if we are going to consider the totality of this challenge, we need to understand how much money we are talking about, so maybe we ought to do that. It would be of interest.

As to these mailers, I know you have heard, as we have heard, that, while suggestions like co-mailing and co-palletization and other efficiency measures sound nice, that when it comes to these particular publications it is really efficiencies beyond their ability—in fact, beyond their printers' ability.

Dan Blair, I would ask you, sir, to what extent did you look at the reality of the accessibility of true efficiencies as a way for these mailers to address their concerns? Is that something you looked at?

Mr. BLAIR. Well, when we assessed these rates we did it based on a data base that was provided to us by the Postal Service and accepted by the parties in the litigation. We saw that there were small mailers who were very efficient. We saw that there were large mailers who were inefficient. So there is ability among some to do that.

We are also seeing that there are changes, in fact, going on in the system. You are going to be hearing from two panelists after us who represent printers who are talking about responding to the market realities and making themselves available.

But besides making it a cold, hard determination based on efficiencies, the Commission tried to ameliorate that by saying when we upped the editorial discount available for these small magazines of opinion or for magazines, in general.

Second of all, according to our study, the smallest circulation magazines, those under 15,000, saw the smallest percentage increase overall, as well.

Third, even though it is not making an institutional contribution as a class, that does relieve mailers across the class from additional burdens in terms of rates.

Mr. MCHUGH. Help me understand, if, as Chairman Miller has said a number of times this morning, and if, as the law has stated at least since 1970 that these publications, as other classes of mail, have to cover costs, I am assuming they have through the various rate-setting procedures; is that correct? I am curious why 45 percent fell upon some of these mailers and not others if they were, indeed, covering cost under previous rate cases.

Mr. BLAIR. I don't know if the individual mailer was covering those costs. The recommends were tied to what are called rate elements, which are tied to particular mailing practices.

We looked at how a mailer prepares his or her mail, how they present it, what kind of container it is in. Is it in a bundle? Is it in a sack? Is it in a lightweight sack? Can it be palletized? Where is it entered into the mail stream? Where is it going? Is it going to a business? Is it going to a household? Is it going to a classroom? The editorial percentage discount, a whole host of factors go into that. So each mailer's rate will differ depending on his or her practices. In fact, the number of pieces they mail at the time will also determine.

The old structure was premised on pieces and pounds. Now what we have done is we have introduced other cost elements, including pieces, pounds, sacks, bundles, and pallets. Those we identified as different cost drivers, and, depending on how they are utilizing them will determine how much an individual mailer pays.

Mr. MCHUGH. One final question, if I may, Mr. Chairman.

Under the bill that this Congress passed and you published your ratemaking regulations on yesterday, there is a requirement, because I think we all understood in the Congress that, as has been said, periodicals has been a troubled class for some time, that the Postal Service and the Postal Rate Commission shall study and submit to the President and Congress a full report on the accuracy, the quality, the completeness of information that you used in assessing rates against periodicals and other requirements of that study.

I am assuming that you will follow that part of the law, but I am wondering, have you had a chance yet, either individually as the Postal Service or the Rate Commission, to talk about how and when you might go forward on that study?

Mr. BLAIR. Your assumption is correct. That is something that we would hope to start working on with the Postal Service soon. We have been working with them on the establishment of the rate system, as we have with other members of the community. We have been working on the service standards and focusing on those aspects of the bill that had a time deadline. But this is something, given your concerns or the committee's concerns or something, that we will look forward to working with Mr. Potter and Mr. Miller on.

Mr. MCHUGH. Mr. Miller.

Mr. MILLER. Yes, sir. Could I just make three quick points? One, when we are talking about Dan or Jack or I talking about covering costs, I want to make sure we understand that we are talking about covering attributable cost, which is only 59 percent total cost. The rest is overhead. We have said that the publications are not, under the new regime, publications as a whole would not cover anything, would not contribute anything to overhead.

Second, in the past, because we did not break out the cost differences, not for the larger publications but the kind of service that we have, by kind of service, palletized and otherwise, those that were using the bags and otherwise were being subsidized by other publications and other users of mail. So we made this reality check, and that is a reason that the rate structure for a publication is a little more complicated today.

Finally, I read some of the testimony from some of the publishers and also the letters that we received—we received hundreds of letters in response to our rate proposal. I don't recall anybody talking about, well, we could raise rates. It is always, We will suffer this loss, that loss, and so forth. But, I mean, if these publications—and I subscribe to some of these very small publications—I think that the consumers could bear higher costs, as well. So I don't see that they would go out of business. Maybe some cutbacks or whatever, but I think that the allegations that the sky is falling are simply that.

Mr. MCHUGH. Thank you.

Thank you, Mr. Chairman.

Mr. DAVIS OF ILLINOIS. Thank you very much, Mr. McHugh.

Mr. Sarbanes.

Mr. SARBANES. Thank you, Mr. Chairman.

I am going to follow the same line of questioning for a couple of minutes in terms of the impact on the small mailers.

Mr. Blair, you said that there are small mailers that you have discovered are quite efficient, and there are large mailers that are inefficient. The theme of your remarks and the answers to your questions seem to be that the same expectations of efficiency ought to be brought to the large mailers as to the smaller mailers. I think what you are hearing up here is that I am not sure we agree with that; that there shouldn't necessarily be the same expectation, the same standard applying, because, as a class or group or category, the smaller mailers are going to be inherently less efficient and, as has been said by others, can't expect to achieve the kinds of efficiencies across the board that the larger mailers can.

I don't claim to be an expert on the PRA, but a number of you referred to the fact that the law requires you to recover these costs and so forth, but the law doesn't say that you can't group people together in a way that some cross-subsidization is occurring, does it?

Mr. BLAIR. Well, the law basically directs that mail cover its cost, and the Commission has certainly followed, over the course of the 37 years, that when cost drivers have been identified, they have applied it to those mailers. That seems to be the question of who pays. If you do have inherently inefficient—and I don't want to make that a value judgment—inherently inefficient, small mailers who just can't avail themselves of this, then the question is: who pays the difference between what would have been an affordable rate and what the real rate is?

Mr. SARBANES. Right.

Mr. BLAIR. And you can ask the big mailers to do that, and you are going to be hearing from some big mailers after us. I think that they are going to certainly have an opinion.

Mr. SARBANES. Well, you are always going to hear from someone.

Mr. BLAIR. Exactly.

Mr. SARBANES. I guess the concern is we are hearing from small mailers who have high levels or high amounts or high volume of political content in them, editorial comment, and we are particularly concerned that gets crowded out over time. So maybe we would choose to hear more from the large mailers and the small mailers. I think that is kind of what the discussion is.

But I don't buy the idea that a situation where you draw the line at a place that still allows for reasonable cross-subsidy is something that can't continue to be part of the approach and thinking of the regulatory commissions.

Mr. BLAIR. I think that some would say there is still a reasonable cross-subsidy. The full efficiencies weren't completely passed through on to the small mailers in this case.

Mr. SARBANES. And we talked about overhead versus attributable cost.

Mr. BLAIR. Right.

Mr. SARBANES. And I am talking about within the attributable cost we really——

Mr. BLAIR. Even within that class, so you are talking of who is going to pay those attributable costs, not all the efficiencies were completely passed through to the more efficient mailers. More-efficient mailers are still paying for the cost of the less-efficient mailers, to some degree. Not as much as they were before the old structure.

Mr. SARBANES. OK.

Mr. BLAIR. And I am sympathetic to where you are coming from, but I would ask you to understand that if this was a robust class where you had growing revenues, I think that you could say let's level the playing field a little bit more. But it is not. I mean, having not attributed $3 billion over the last 10 years, plus made no contribution to the overhead cost of the Postal Service says something has to be done.

The old rate structure sent out the wrong messages. It is my understanding that under the old rate structure incentives were given to mailers to use what are called lightweight sacks. Oftentimes those sacks would spill or break, causing more hand processing, which added to cost. Why were incentives given to using those sacks?

Those things had to be re-adjusted. So you are right that there is more of a burden placed on these smaller publications who can't reach these efficiencies, but then the question then comes down to who pays for those. At this point, I think it is consistent with the PRA that once those cost drivers are identified, that you go forward and you ask those mailers to pay for those costs.

Mr. SARBANES. Well, the fact that you are describing a group of mailers, generally periodicals, that you seem to say may be going ultimately the way of the dinosaur in terms of their declining base and all the rest of it, I guess whether that is true or not, as they head in whatever direction they are heading in, we are just saying that the burden ought to be spread a little bit more.

Can I ask one more question, Mr. Chairman? I am going to completely switch gears and get back to this issue of other sources of revenue and so forth and other uses of the Postal Service.

I have been intrigued for a long time, ever since I read about the response after Katrina, where you had U.S. Postal Service in places where no one else dared to go, and understanding and knowing everybody in a community and being able to reach out to them, and in some instances were the first responders on the scene. Could you just talk briefly about the extent to which the Postal Service is thinking about how it becomes part of a first responder network

and whether—I mean, there wouldn't be commercial sources of revenue from that, presumably, but you might be able to convince other agencies that are keen on being prepared in a disaster scenario to contribute toward that kind of effort. If you could just speak to that.

Mr. BLAIR. I will defer to the Postmaster General on that one.

Mr. POTTER. Well, first of all, we are very proud of our people and the way they respond to any emergency situation that occurs anywhere in the country. We are very proud of the fact that we have service back up and running in California, and, for those people that have lost their homes, we have managed to provide temporary delivery as convenient as we possibly can to them.

I personally was in Florida after Hurricane Charlie, and then was down in New Orleans and Mississippi after Katrina. I have to tell you that I think we can bring a level of coordination to something that is extremely important after a disaster, and that is to help find others get connected with each other when it comes to family members.

I was a little surprised when I walked the streets in Florida with a letter carrier to see people from other agencies, Federal agencies and private concerns, out doing reconnaissance when it came to what homes were occupied, where the residents might be. Those folks didn't even know what street they were on. Our letter carriers had the day before not only gone out to determine which homes were occupied, but had forwarding information, knew where they were located.

Likewise, in the Katrina situation people came and registered with us, gave us change of address, and we were able to again help people get connected.

We are very proud of the work we are doing right now with Health and Human Services and Homeland Security around what might happen if there was a biological attack in different parts of the country, and we have done tests in major cities around the country, most recently in Boston, where the Postal Service, working with our unions, volunteered to help with the delivery of medications to people who would be recommended to stay homebound.

We would like to even go farther than we did. We showed that we could deliver in a matter of a couple of hours medications to every address in a geographic area because our people have assigned routes, they have assigned routes, they know who is behind the door.

The one thing I would like to do is allow the carriers the flexibility to determine how much medication is left on a door because they are more knowledgeable about how many folks reside in a residence than a data base might give you.

So I think there are numerous ways that we can do this. First and primarily is to help locate people after a disaster, but I think it would require some change in the law to allow us to share information.

Today there are all sorts of restrictions about our ability amongst agencies and private sector folks to share information about what they know about the whereabouts of folks after a disaster, and that could be very helpful. And then, working with the Federal Government, we can be an active participant in the logistics around mov-

ing supplies to needed areas, as well as to provide contact, whether that is the hand delivery of information in written form if other communications are down, or the delivery of medications.

Basically, if it is hard copy or physical, I think you have a ready resource. The Federal Government has a ready resource in the Postal Service to provide service.

If I could go and burden you a little bit to go beyond that, I view the Postal Service as the presence of the Federal Government in every community. When you think about the Federal Government, we are the piece of the Federal Government that touches everybody at their door every day. I would love to engage in a conversation about how the Postal Service could help the Federal Government interface with its constituents, whether that is today we work with the Secretary of State with the issuance of passports. We would invite all thought on how we could better serve the American public as the arm of the Federal Government in every community and every door.

Mr. SARBANES. And I think you should be paid for that service. Thank you, Mr. Chairman.

Mr. DAVIS OF ILLINOIS. Thank you very much, Mr. Sarbanes.

Mr. Jordan.

Mr. JORDAN. Thank you, Mr. Chairman.

I want to thank the gentlemen for joining us this morning. I am just beginning to get my arms around this issue, but, with respect to the periodical issue, how long were we functioning under the old structure, the kind of two-tiered or cross-subsidization, whatever you want to call it? How long did that go on?

Mr. BLAIR. That old structure was in place since 1970.

Mr. JORDAN. And then someone mentioned earlier the lead time you were giving periodicals and companies today. How much lead time was given to those individuals?

Mr. POTTER. Well, the Postal Service would consult with mailers as we were formulating a rate proposal. We would file a rate proposal with the Postal Regulatory Commission, and they had 10 months under that law to preside over a rate case with an evidentiary procedure. At the end of 10 months they made a recommendation to the Board of Governors regarding the rate proposal that was put forth in front of them.

Basically, the Board of Governors could make a decision to go along with the recommendation. At the end of the day, the Board of Governors has, I guess, the ability to overrule the Commission when it comes to the revenue requirement; however, when it comes to rate structure, the rate structure is pretty much under the domain of the Postal Regulatory Commission.

Generally, after that recommendation is made and the Board of Governors has made their decision, there was a 2 month to 3 month period of time to allow for mailer implementation. Whether it was 2 months or 3 months was largely determined by the financial position of the Postal Service. If there was an ability to allow them to go 3 months, it would. In the case of this past rate case, we chose to implement within 2 months because the new law basically had us lose $5 billion last year, so it was not a good year to give anybody charity.

Mr. JORDAN. Are the numbers thirty-seven years under the old structure, 2 months lead time? Is that accurate?

Mr. BLAIR. No, 37 years under the old law. From time to time the Postal Service would come in with a new rate case. Last year—was it January or February?

Mr. POTTER. No, it was May. May 2006. Let me just describe it to you a little bit. In effect, when we file our rates we are putting people on notice that a year from that date they can expect a rate change.

Now, historically what we file is in the ballpark of what the outcome is. By in the ballpark, I am talking a couple of percent high or low.

In this case what happened was we filed a rate case. The Postal Service was working with mailers saying here is what we filed, here's the new rules and regulations around that filing, and we published them and had regular meetings with them on that so that they could begin to anticipate their software requirements and build those costs into their budgets.

What happened was we had an outcome that varied rather dramatically for some mailers from what the Postal Service had filed.

Mr. JORDAN. Is it fair to say in that 37 year timeframe that there have been several occasions like what we are discussing here today, so several times this thing has happened, but this particular time it is to a larger degree than in previous occasions? Is that accurate?

Mr. POTTER. My experience was there wasn't as dramatic a difference in the rate structure. It generally followed along the lines of what the Postal Service had proposed. In this case there was a big difference for some mailers.

Mr. JORDAN. OK.

Mr. POTTER. So we might have proposed an increase of 20 percent and it went to 40 percent. In other cases, mailers' rates dropped versus our proposal. It is that change and the width or the breadth of that change that has a lot of mailers concerned. That is one of the reasons they are concerned. They are also concerned because the nature of just you raise any rates they are going to be concerned.

Mr. JORDAN. I understand. And in that 37 years, there has always been some degree of what has been called cross-subsidization or different tiers. In fact, I forget which one of you gentlemen said it earlier, you said something about with new periodicals you have some kind of different structure that is in place.

Mr. POTTER. Well, if I could respond, first of all, there always has been cross-subsidization within every class, because there is a different cost to the Postal Service for handling different mailings. Let's take periodicals. If you take a periodical mailer and you produce a magazine that stays within your local area, if it is a Washington, DC, magazine and 95 percent of the recipients are right here in Washington, it is a lot easier to handle that mail than it would be if you had that magazine and it went to a dispersion of people around the country. So there is always going to be a variance on cost. And there has always been cross-subsidization.

The Board of Governors has exercised their judgment in terms of how much of that cross-subsidization they would allow, and their filing last May in 2006 reflected their judgment regarding that

cross-subsidization that they would allow to happen. They knew that some mailers weren't covering their costs, while others were more than covering their costs. So there was a balance there that led to what would be an average price increase for periodicals.

In the case of what just happened, the Board of Governors' judgment was overridden by the Rate Commission's or Regulatory Commission's view of the prices that were proposed in light of their interpretation of the law and how they should apply those economic principles.

Mr. JORDAN. Thank you, Mr. Chairman.

Mr. DAVIS OF ILLINOIS. Thank you, Mr. Jordan.

Mr. Cummings.

Mr. CUMMINGS. Good morning.

Let me see if I can get a handle on some of this.

This basically is a done deal, isn't it? I am just trying to figure out whether we are here wasting our time, because time is short. I am just curious. It sounds like you are basically saying this is a done deal. Somebody answer me, please.

Mr. POTTER. Well, by law the case that was proposed last year is a done deal, but I think the value of this discussion will help shape us and our thinking for future rate cases.

Mr. CUMMINGS. Well, I am glad you said that, Mr. Potter, because the new law basically gives mailers even less input, is that right?

Mr. POTTER. Not in my opinion.

Mr. CUMMINGS. No? I see you shaking your head, Mr. Miller. Why are you shaking your head?

Mr. MILLER. Well, they can have a lot of input, and my understanding is the new law—and I may be incorrect in this. I am not a lawyer, but I am advised by lawyers that the new law gives the Board in its rate changes the discretion to include other things, things in addition to attributable cost.

Mr. CUMMINGS. Mr. Potter, did you have something that you wanted to say?

Mr. POTTER. I just wanted to agree with them.

Mr. CUMMINGS. I guess where I am going with this is I am trying to figure out, we have, say, for example, in my District the African American newspaper. This is a newspaper that basically has been around for over 100 years. A lot of the people that they mail to don't have the Internet, and so I am sitting here and I am thinking I would hate to see a business like that go out of business. I understand this balance thing you are all talking about, making sure that folks carry their weight, smaller mailers. But we also have another issue here, and that is, I guess, I wonder about Government and what part Government should play in making sure that free speech is out there, that speech is out there.

I am just wondering, when you talk about this transition and the effects it is going to have on the smaller folks. I understand you have given a 4-month window to try to work some things out. What is it that you plan to work out in that 4 months?

Mr. MILLER. Well, Mr. Chairman, we gave a delay of several months before the rates went into effect.

Mr. CUMMINGS. Right.

Mr. MILLER. We want to have continual discussions with all of our customers and to work ways of making it a win/win proposition for them as well as us. I do not anticipate a rollback in the rates that the Postal Regulatory Commission has approved but——

Mr. CUMMINGS. So if these folks go out of business is that a win/win?

Mr. MILLER. Well, it would be——

Mr. CUMMINGS. If these small publications go out of business, is it a win/win?

Mr. MILLER. But that is a hypothetical.

Mr. CUMMINGS. No, no. No, no. I am asking you a question. Is it a win/win if they go out of business?

Let me tell you why I am asking you that. I think that is pretty much largely why we are here today. You have a lot of businesses that put out publications that are saying that this is going to affect them in a negative way. I am not going to ask the people out there in the audience to stand up who feel that way. I am not going to do that. But I can tell you that we get the complaints in our office about people who have been in business going out of business. I am just asking you a simple question: if they go out of business, is it a win/win situation? That is all.

Mr. MILLER. I would say if they cannot cover their cost it is a win/win situation. Let me tell you why I think that: because other classes of mail would be covering their cost. Talking about first amendment, if you write a letter right now to your Congressman expressing your opinion about something, or you write a letter to your local paper to have it published, or you write your friend and encourage them to work with you in achieving certain policy goals, you are paying 200 percent of attributable cost.

Again, under the package that the Postal Rate Commission approved—and it was more complicated, and that part was different than what the Postal Governors had recommended—under that proposal, under that new system, though, publications are covering 0 percent of overhead. The markup for them is zero. So if they were given some preferential treatment, it would mean that others, such as people who write letters expressing their first amendment rights, or using their first amendment rights, would have to pay the difference.

Mr. CUMMINGS. And so your answer is it is a win/win for everybody but the people who go out of business?

Mr. MILLER. Yes, but it is an empirical question, Mr. Cummings, of whether they would go out of business. Again, in the testimony that I have read and the things that have been printed, editorials, etc., they don't talk about raising their prices or being more efficient to comply with the opportunities this new rate system gives them to commingle and to co-palletize and so forth. It is not that I am heartless. it is not that we are heartless.

Mr. CUMMINGS. I didn't say you were. I just asked the question.

Mr. MILLER. Yes. But, I mean, we have to consider all sides, and I think the fairest thing is for each class of mail to at least cover the cost directly attributable to carrying their mail.

Mr. CUMMINGS. Let me ask you this: you all do projections, right? You project we are going to go through this again fairly soon, this rate increase situation, this rate adjustment? And just one thing,

because I want to interject this into your answer. I want you to consider this. I noticed that with all businesses when we are talking about retiree payments and things like that go to benefits, we have the Baby Boomers retiring and all that kind of thing. How do you see that affecting what will happen in the future with regard to any kind of rate adjustments?

Mr. MILLER. That is an excellent question, sir.

Mr. CUMMINGS. Thank you.

Mr. MILLER. I am sure that maybe Jack, as well, but some of the analysts at the USPS have probably looked into that. Let me answer your first question. We do anticipate having another rate case. Whether we file under the old rules or the new rules, I assure you that it will not be more than the CPI; that is, for every class of service the increase would not be more than the increase in the CPI. That is the law now. That would be the case into the future, so you wouldn't have another situation like the one that we have just gone through, just to answer your question.

The other thing, though, is how would readership change with the Baby Boomers and their retiring and so forth. How would that mix of things change? I mean, on the one hand people have more time to read things; on the other hand, maybe they would have other interests. I don't know. But that is a very good question.

Jack maybe has a thought.

Mr. POTTER. First let me address the issue of benefits. Postal Service pension programs are fully funded. We are fully funded. As far as health benefits for retirees——

Mr. CUMMINGS. That is what I was aiming at, the health benefits.

Mr. POTTER. We have been on a pay-as-you-go basis, but the new law requires us to build a health benefit fund for retirees. As a result of the new law, we already have some $20 billion in that fund. We are on track within 10 years to have a nearly fully funded retiree health benefit program. I think we will probably be the only agency in the Federal Government that can make that claim, that the moneys are there now.

In having us pay that almost fully funded within 10 years, which the new law did, it has put a burden on all mailers because, in effect, we are paying into a fund the equivalent of what we would have overpaid our pension program for, and so we could have been provided some relief by, rather than having that paid off in 10 years if we would amortize it over 40.

But, be that as it may, we built a plan and we are working hard to build a plan that will go beyond the next couple of years that will allow us to live within the law which says basically that we will keep our rates below the rate of inflation for each class of mail. It is going to require us to work with the mailers to make sure that we are moving mail as efficiently as we possibly can, work with our unions to help us deal with the challenges of the law.

So going forward I wouldn't consider it a win if we lost mailers because of price, because I think there are alternatives for small publications that we need to do a better job of working with to help them make their product more efficient. The industry I think is ready to help, as well. I am talking about the printers.

And it is going to require change. People are going to be hurt at the end of the day, but if they want to stay in the mail we want to try and work and help them to do that.

Mr. CUMMINGS. I will finish, Mr. Chairman. You have to wonder whether, as a society, Congress needed to do more to subsidize some of this more than what we need to do. The reason why I say that is because I think that, just like with NPR and the kinds of things that we do as a society to provide people with information, it seems to me that this is the kind of thing with these small periodicals that we need to find ways to try to help them. That is on us. I got that.

But it certainly concerns me, and I do not consider it a win/win when a business has to go out of business. I have been in business before, and it is not a good feeling for people—and I have represented people who have gone out of business—when they have given their blood, their sweat, their tears, and then next thing you know they have to close their doors. It is a very, very, very, very painful thing.

Thank you all for your testimony.

Mr. DAVIS OF ILLINOIS. Gentlemen, thank you very much. We have a vote on. We have only got two votes, so if you could stay until we return I would appreciate that.

[Recess.]

Mr. DAVIS OF ILLINOIS. The subcommittee will resume.

Let me thank you gentlemen so much for waiting for us and being available.

Let me go right to you, Mr. Blair. We have talked a great deal about rate increases and how much it is and who is paying and why, but let me just ask why are the costs so high for periodicals in the first place?

Mr. BLAIR. That is a real good question. I think that, to the extent that you have to have any kind of hand processing that is not machinable or automatable, that drives up the process. I think the Postmaster General's statement reference the fact of the flat sequencing sorter, the new machine that will be coming online the end of this year or next year, and that holds promise to keeping costs down, if not driving some costs down.

But one of the questions is: to whom will those cost savings and benefits be available? If you don't have machinable mail, will that work in something like that?

But I think that you did hit the nail on the head on this: why are the costs so high in the first place? That is the fundamental question, and what can be done to drive down these costs.

Mr. DAVIS OF ILLINOIS. You know, I was just remembering when I used to work in the Post Office and we used to have fun throwing the flats. We would pretend that we were playing basketball, and we would have the racks, and we would kind of toss them over and it was a lot of fun. It was good, clean, hard work.

Let me ask you also, What is the difference between the percent increase for big mailers as opposed to those that we would call small mailers?

Mr. BLAIR. I don't know if we have a percent increase. I would be happy to try to supply that for you for the record. I will tell you that for the group called small periodicals, those at 15,000 or

under, they received overall the smallest percentage increase due to the fact that pass-through discounts were, in fact, tempered; the low institutional cost contribution for the class overall; and the fact that the editorial discount was increased, and that benefited those smallest of periodicals, as well.

Mr. DAVIS OF ILLINOIS. Thank you.

I know that we are going to hear testimony from the National Newspaper Association that in the most recent rate case the PRC essentially gave the Postal Service a pass on providing data within respectable ranges of reliability for their in-county mail cost, yet the PRC had, in the past, gone so far as to point out the unreliability of this data to the GAO. Can you explain to us why the PRC did not zero in on this problem in this past case?

Mr. BLAIR. I don't remember that being highlighted as a problem in this past case. I can tell you for within county the PRC's recommended decision substantially cut the proposed increased by the Postal Service. As I recall, that was in the 24 percent range and we knocked it down to 18 or 19 percent, and so the within counties benefited by the Commission's recommendations.

Mr. DAVIS OF ILLINOIS. Let me ask, Is it a continuing concern to your economic experts that the Postal Service seemed to see large cost increases in small mailing classes, where perhaps what there really are are wide margins of error that, in terms of what is being assessed and determined? Are you comfortable that the data that you are using is not error-free but does not contain enough error to maybe skew the decision in a way that is obviously not favorable toward the small mailers?

Mr. BLAIR. Data has always been a fundamental question. We worked consistently with the Postal Service over the years to improve the quality of the data. I remember in 1995, then PRC Chairman Ed Glassman complaining about the quality of the Postal Service's data in that rate case. In response, the subcommittee at that time authorized a study. It was a joint study of the Postal Service and Rate Commission study with the help of GAO in looking into that.

Improvements in the data have been forthcoming over the years; however, it is a continuing problem. But I think that the new tools that you provided to the Regulatory Commission will help us in that area, as well.

It is important that we get the good data. We want to work closely with the Postal Service to improve that quality, and that is something we will be doing over the course of my tenure at the Commission.

Mr. DAVIS OF ILLINOIS. Thank you very much.

Let me ask you what perhaps will be my last question. Mr. Potter, of course we get continuous complaints from our fellow colleagues relative to a continuous flow of complaints that they receive relative to time-sensitive mail like newspapers and weekly magazines and, of course, sometimes their newsletters where they expect to convey certain information to their constituents, and it is sometimes not in a timely enough manner.

Why is the slow processing of periodicals such a problem?

Mr. POTTER. Well, let me address periodicals, in general. Earlier you asked about the cost of periodicals. Well, periodicals as a class,

in data that I have reviewed over the years, have the worst addresses of any class of mail. You start with a bad address, you are going to get a bad delivery. You also have with periodicals a situation where we have tried to move them from preparing mail in the old-fashioned way, I will call it, in sacks, to getting it on pallets. In fact, we have upped the amount of flats that you had to put, or periodicals you had to put into a sack, from 6 to 24, just to bring them in line with the way other mails are being processed.

So there is a whole host of reasons to why periodicals cost more than what would be catalogs in terms of comparability, so we have to address that going forward.

From a service standpoint, this is a situation that needs to be addressed long-term. It starts with understanding the whole supply chain. From the time that mail is printed, the logistics companies that bring it to the Postal Service just to take advantage of discounts I periodicals, you have to use them, and then our handling of the mail. We are preparing and moving ahead on a plan that would have every piece of mail have a bar code on it such that we can get at some of the costing issues that you asked Chairman Blair about, because we would be able to measure each piece of mail and where it was processed and how much it cost us to process that mail.

It would also enable us to track, from a service standpoint, where, first of all, the mail was deposited, when it was printed, when it was deposited with us, and then how we handled it through the system. That will give greater transparency to where problems lie. And I would be the first to tell you that we are going to have problems in our system, but our goal is to fix those problems and to improve service going forward.

I welcome what Chairman Blair talked about earlier, the fact that we are going to publish and we have right now in the Federal Register standards for all the market-dominant products, as required by law. We are going to seek the input of the public to determine whether or not those are appropriate, and we look forward to their input. And then we are going to establish goals and track ourselves against that.

The key, in my mind, is the big step, which is to put intelligent mail barcodes on each and every piece of mail that comes into the system, enabling us to track mail and, in the long run, deal with the issue that you have just described so we can deal with it from a point of data, as opposed to, at times, what turns out to be some rhetoric. So we would like to pinpoint the problems and fix them, and our goal is to do that.

Mr. DAVIS OF ILLINOIS. Well, I do have one additional question that comes to mind for you and Chairman Miller. During the exchange between yourself and Mr. Sarbanes, both of you talked about the tremendous infrastructure that the Postal Service provides for certain kinds of services that could be provided to the Federal Government, especially in the area of disaster relief or disaster assessment. He ended by suggesting that the Service could also get paid or could get paid or should get paid for those services. How would you respond to that as a kind of possibility?

Mr. POTTER. Well, let me just speak to some of the services that we provide. When it comes to passport services, the Postal Service

charges those who use us for passports the same fees that the State Department would allow others to charge for that service, so there is a mechanism for us to get compensated.

When it comes to disaster relief, we do get some funds transferred from HHS, the Health and Human Services Department, when we conduct these tests.

What I am saying is I would like to look beyond those to determine where are other opportunities for us to generate revenue on behalf of the Federal Government by representing the Federal Government.

In addition to that, again, the reconnaissance, if there is money to be had that is great. I do want the revenue, but when I spoke I was talking about just using the system to better the well-being of the American public in those places that might be hit by a hurricane or other natural disaster. Certainly, I think there could be a value placed on the information that we could provide to others and to generate a source of additional revenue for the Postal Service.

Mr. DAVIS OF ILLINOIS. Mr. Chairman, let me ask if you have any comments that you want to make.

Mr. MILLER. Well, Mr. Chairman, I agree with what Jack just said. We already asked Congress to appropriate moneys for the foregone opportunities, the services that we already provide for free, and Congress, the appropriators, don't ante up fully on that. I would be hopeful, but not real optimistic on something like that.

Mr. DAVIS OF ILLINOIS. Well, let me just say I raise it because I think that revenue generation and enhancement is going to be an ongoing discussion that we will be having relative to postal matters for some time to come.

Mr. MILLER. Right.

Mr. DAVIS OF ILLINOIS. And, like you, I share the recognition of need, understanding that you can't get blood out of a turnip, as we discussed earlier as we talked about efficiencies and improving systems and all of those things. Eventually you get down to the point where the only thing that supplies the need is some resources. You can be as efficient, as effective, and we want to make sure that all of that happens, but I don't think that there is anything that takes the place of money.

So let me thank you gentlemen very much. We appreciate your being here, and you are excused.

Mr. MILLER. Thank you, Mr. Chairman.

Mr. POTTER. Thank you, Mr. Chairman.

Mr. BLAIR. Thank you.

Mr. DAVIS OF ILLINOIS. Let me go ahead and introduce the witnesses for panel two as they are being seated.

We have Mr. Andy Zipser. He is the Editor of the Guild Reporter and is a Past President of the International Labor Communications Association [ILCA]. The ILCA works to strengthen and expand labor publications, Web sites, and radio, television, and film productions by providing resources, expertise, and networking opportunities for labor communicators.

We have Mr. Victor Navasky, who is Publisher Emeritus of the Nation, and the Columbia Journalism Review. The Nation is Amer-

ica's oldest and most widely read weekly journal of progressive political and cultural news, opinion, and analysis.

We have Mr. Jeff Hollingsworth, who is vice president of Eagle Publishing and Assistant Secretary of the Phillips Foundation. He has monitored legislative and regulatory activities at the local, State, and national levels.

Mr. Max Heath is vice president of Postal Acquisitions for Landmark Community Newspapers, Inc., in Shelbyville, KY, where he is responsible for postal issues.

Mr. Hamilton Davison has been the executive director of the American Catalog Mailers Association [ACMA], since its founding in April 2007. Mr. Davison's involvement in postal affairs started in 1992 with his service as part of the Greeting Card Association's Postal Affairs Committee, which has been an intervener in virtually every rate case since the PRC was committed.

Gentlemen, we thank you very much for being here. It is our custom of this committee, we always swear in our witnesses. If you would stand and raise your right hands.

[Witnesses sworn.]

Mr. DAVIS OF ILLINOIS. The record will show that each witness answered in the affirmative.

Of course, your entire statement is in the record. The green light indicates that you have 5 minutes to summarize your statement. The yellow light means that your time is running down and you have 1 minute remaining to complete your statement, and the red light means that your time is expired.

Thank you all again for appearing, and we will begin with Mr. Zipser.

STATEMENTS OF ANDY ZIPSER, FORMER PRESIDENT, INTERNATIONAL LABOR COMMUNICATIONS ASSOCIATION; VICTOR NAVASKY, PUBLISHER EMERITUS, THE NATION, AND CHAIRMAN, THE COLUMBIA JOURNALISM REVIEW; JEFF HOLLINGSWORTH, VICE PRESIDENT, EAGLE PUBLISHING; MAX HEATH, VICE PRESIDENT OF POSTAL/ACQUISITIONS, LANDMARK COMMUNITY NEWSPAPERS; HAMILTON DAVISON, EXECUTIVE DIRECTOR, AMERICAN CATALOG MAILERS ASSOCIATION; AND DAVID R. STRAUS, COUNSEL, AMERICAN BUSINESS MEDIA

STATEMENT OF ANDY ZIPSER

Mr. ZIPSER. Thank you, Mr. Chairman. Good morning. My name is Andy Zipser, and I am the editor of the Guild Reporter, but you have given me a promotion. I was a past vice president of the ILCA, not a past president. I appreciate it.

Founded in 1955, the ILCA is an AFL–CIO and Change to Win affiliated professional organization of labor journalists and communicators in North America. Our several hundred members produce newspapers, magazines, newsletters, and other media with a total circulation in the tens of millions.

Robert McChesney, the journalist and media critic, has said, "It was Postal policy that converted the free press clause in the first amendment from an abstract principle into a living, breathing reality for Americans." Although he wasn't thinking specifically of us

when he made that statement, Mr. McChesney may as well have been describing what we do. We are the communications lifeblood of the union movement.

The Postal Service that delivers our publications from one end of the country to the other is the primary medium through which our union leaders speak to their members and the members to them. If this link is broken, that exchange is silenced.

The recent postal increase, an increase that has hit our publications with disproportionate harshness, is threatening to do just that. While benefiting large publishers who can exploit economies of scale to take advantage of various discounts, the new rate structure is slamming smaller publications with increases of up to 30 percent. These crippling increases are even more onerous when one recognizes that relatively few union publications carry paid advertising.

Moreover, as in-house organs that are published specifically for our members, union publications do not have subscriber bases. That means any postal increases come directly from dues-sustained union treasuries, without the possibility of offsetting increases in advertising or subscription rates.

Mr. Chairman, let me give you some examples of how the increased mailing costs affect us.

The paper I edit, the Guild Reporter, was slapped with a 27 percent hike. It now costs more to mail the Guild Reporter than it does to print it. The Communicator, a glossy magazine of about 70,000 circulation produced by a New York based affiliate of the American Federation of Teachers, estimates its increased cost at about 21 percent. For the Labor Paper, a tabloid with 80 percent of its circulation within just two counties in southern Wisconsin, the increase was approximately 15 percent.

As a result, many of our publications are being forced to reduce page counts or publication frequency, and there is a very real possibility that some may cease publishing altogether.

The International Musician, a 36 to 40 page magazine with circulation of about 100,000 produced by the American Federation of Musicians, saw its mailing costs jump approximately 25 percent and is looking at changing its publication frequency from once a month to once every 2 months.

The American Federation of Government Employees has chopped its publication size in half in order to qualify for cheaper non-profit mailing permit.

Some defenders of the new postal rates point to the Internet as a cheap distribution alternative for publishers. While the Internet holds great promise for democratizing media, union surveys consistently show members still prefer paper publications delivered to their mailboxes. Moreover, not all union members have personal computers, nor do they all have Internet access. Many who do are still using dial-up modems, which are less than optimum for distributing publications.

Mr. Chairman, in the labor movement, as with all of the advocacy press, the consequences of this dramatic run-up in postal rates are predictable: fewer voices, less discourse, withering democracy. This is the legacy you leave if you don't change policy direction now. That is why we respectfully but urgently request this sub-

committee to do whatever is in your power to restore the more progressive postal rate structures of the past.

Thank you for giving me the opportunity to testify today on behalf of the ILCA and small labor publications across the Nation. I will be happy to answer any questions you may have.

Mr. DAVIS OF ILLINOIS. Thank you very much.

Mr. Navasky.

STATEMENT OF VICTOR NAVASKY

Mr. NAVASKY. Thank you. I am grateful for the opportunity to testify before this subcommittee, but let me make it clear that I hope to speak today not only on behalf of the Columbia Journalism Review, which I chair, and the Nation, but also on behalf of independent, small-circulation, political journals, in particular, and on behalf of the readers of these journals, and all of those engaged in and informed by the public discourse that these magazines exemplify.

Before I present my formal testimony, I want to make a confession about my personal bafflement and bias. Of all the services Government provides, only the mails are required to break even or make a profit. The founders, who saw the mails as a circulatory system of our democracy, made no such presumption. George Washington, himself, was in favor of the free delivery of newspapers—which, by the way, in those days were often weekly, usually partisan, and as such the equivalent of today's journals and political opinion.

These journals, whose core franchise is public discourse about public affairs, are a public good, like education and defense. Yet, as a result of the new periodical postal rates in place as of July 15th of this year, precisely those magazines that can least afford it and devote the most space to public affairs bear the heaviest burden.

In the case of the Nation, the cost of mailing the magazine is already more than three times the cost of the paper on which it is printed. Its new rate increase will be 20 percent and will cost the magazine an additional $500,000 a year. The Nation, by the way, which has the highest circulation among the opinion weeklies and bi-weeklies, is in better shape than many small-circulation periodicals, some of which will undoubtedly expire in the months ahead.

The bi-monthly Columbia Journalism Review estimates that its postal rate increase could be as high as 30 percent. The American Journalism Review, the only other impartial media monitoring journal in this country, has announced that it may have to go out of business by year's end.

We hear stories on a weekly basis of magazines contemplating cuts to their frequency of publication or going out of business entirely.

On the other hand, under the new rate structure, more opulent mass-market magazines with heavy advertising content enjoy a lower rate increase or, as we understand it, some magazines are seeing actual rate decreases.

How did this happen? From the outside, it appears as if Time Warner lobbyists carried the day. We can't say for sure, because lobbyists are a luxury small journals can't afford. The big publish-

ers have spent millions of dollars over the years arguing for a reversal of public interest postal policy that supports a diversity of voices in the periodical class. It is important to point out that the Postal Rate Commission has repeatedly rejected this kind of argument for many years, supporting instead the postal policies of the founding fathers.

It is for Congress to decide if the PRC was correct in finally acceding to Time Warner and abandoning this public service principle. This begs the question, did the Commission know precisely what would happen in the marketplace, not to mention the marketplace of ideas, if this decision was implemented?

According to the rate case, the data base that the PRC used to make its recommendation turned out to be deeply flawed. In fact, the Commission had no real data to project how the rate changes would impact the periodical industry. The result, not matter how well intentioned—and I am sure it was well intentioned—was a disaster.

The Commission's hope was to increase efficiency, as we heard this morning, by creating a set of rewards and penalties for different mailing practices. In practice, this resulted in giving large-volume periodicals big discounts for what they already do, and it hit huge rate penalties. It hit on weekly periodicals that cannot take advantage of efficient mailing practices which are dependent on economies of scale and have no sensitivity to timely delivery. My definition of small, by the way, is anything under 250,000.

Further, there was no attempt at all to weigh the public interest in the circulation of information and opinion against this so-called efficiency standard. Had they done so, they might have considered the option of re-allocating costs within the periodicals class, itself, to benefit the public interest, as has been postal policy for over 200 years.

In my written testimony I suggest 10 ideas on what is to be done. Here let me mention only four. Congress should: One, instruct the USPS that the rate-setting system should be based on a public interest standard first and foremost, favoring diversity over so-called efficiency in the periodical class.

Two, Congress should change the law so that in the future either the requirement that each class pay its own way be struck and/or that social mission be emphasized in the allocation of charges within each class. For example. charge dramatically less to publications with a higher percentage of editorial content and more to periodicals with a higher percentage of advertising content.

Three, the Congress should issue its own fact-finding report, including a history of postal policy on small-circulation magazines, but also impact studies using an enlarged and open data base.

Four, why not revive the proposal put forward by Congressman Morris Mo Udall and supported by Barry Goldwater and others many years ago, that the first 250,000 copies of all publications be mailed at reduced rates? Or the legislation proposed as recently as 2002 by Bernie Saunders that would place a moratorium on postal increases for magazines with a low percentage of advertising content, low circulation, or non-profit status?

Alternative, if you and we do nothing, the impact of the new postal rate increase on the flow of ideas and opinions in America

is likely to be significant and devastating. The periodicals that have been hurt the worst by this rate increase are the seed bed of American journalism, the life blood of democracy in our society. I urge you to take immediate action to reverse course.

Thanks for your time. I look forward to your questions.

[The prepared statement of Mr. Navasky follows:]

PREPARED STATEMENT OF
VICTOR S. NAVASKY
ON BEHALF OF *THE NATION,*
AND *THE COLUMBIA JOURNALISM REVIEW,* AND OTHERS,
BEFORE THE
FEDERAL WORKFORCE, POSTAL SERVICE AND DISTRICT OF COLUMBIA
SUBCOMMITTEE OF THE
HOUSE COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM
110TH CONGRESS, 1ST SESSION
(October 3, 2007)

My name is Victor Navasky. I have served as editor, then publisher and now publisher emeritus of *The Nation*, America's oldest weekly magazine, from 1978 until the present. As publisher I testified before the Postal Rate Commission as a rebuttal witness for the American Business Press in 1995. I am presently Chairman of the *Columbia Journalism Review* (CJR), Director of the Delacorte Center for Magazines and Delacorte Professor of Magazine Journalism at the Graduate School of Journalism, Columbia University, New York. I am the author of A MATTER OF OPINION, which won a George Polk award in 2006 and deals with, among other subjects, the relationship between postal rates and our democratic heritage. I have published articles about postal policy and democracy in *The Nation* and CJR, but also in *The Washington Post* and *The Washington Monthly,* and I have written a chapter in the forthcoming Public Affairs Press book WHAT GEORGE ORWELL DIDN'T KNOW (November, 2007), on Time Warner's role in the recent round of rate increases and how high postal rates can result in de facto censorship to the detriment of the public sphere. (It's title: "Neither Snow Nor Rain Nor Dark of Night Shall Keep Our Couriers From the Swift Completion of Their Appointed Rounds, But What About Big Media?")

I am grateful for the opportunity to testify before this subcommittee, but let me make it clear that I hope to speak today not only on behalf of CJR and *The Nation*, and on behalf of small-circulation political journals, but also on behalf of the highly influential readers of these periodicals – journals in general, editorial writers, legislators and their staffs, non-profit executives, corporate public affairs officers, the academic community, students and teachers, among others. In other words, all of those engaged in, and informed by, the public discourse these magazines exemplify.

A PERSONAL STATEMENT

Before I present my formal testimony, let me confess my personal bafflement and bias. I know all about the Postal Reorganization Act of 1970 and its ostensible requirement that each class of mail pay its own way, but I have never understood why of all the services government provides – defense, education, environmental protection, health, housing, highways and the rest – only the mails are required to break even or make a profit.

The founders, who saw the mails as the circulatory system of our democracy, made no such presumption. George Washington himself was in favor of the free delivery of newspapers (which, by the way, in those days were often weekly and usually partisan, and as such the equivalent of today's journals of political opinion). These journals, whose core franchise is public discourse about public affairs, are, like water, national defense, public highways and public education, a public good and as such it would seem to me ought to be paid for out of public funds (i.e. general tax revenues).

But I know this view is generally regarded as quaint and unrealistic – utopian, as it were – and so the rest of what I have to say does not depend on it, but I thought in the interests of full disclosure, and the hope that it might set some of you to thinking, that I ought to share it.

Also, before I talk about the postal situation, I want to say a word about the Internet, but for what it's worth, my view is that whatever its virtues – and with its low-cost high-speed interactivity, they are considerable – it is not and will never be a substitute for old-fashioned hard-copy, portable journals such as *The Nation*, CJR, *National Review* and others which speak with an authority that reflects the editorial

vetting, fact-checking and deliberative characteristic of journals of opinion, which are after all in the business of setting the standard for political discourse. The authority and legitimizing function these journals enjoy is in my opinion unavailable to the speeded-up, un-fact-checked blogosphere, where shorter attention spans don't allow articles of much more than 1,000 words in length. Moreover, the Internet, where most content is provided free of charge, has yet to come up with a viable business model (and advertisers have historically resisted supporting the kind of content found in journals of opinion of the left or right).

THE PROBLEM

As you know and as David Straus has appropriately put it, we meet to lock the barn door after the horse has gotten out. As a result of the new periodical postal rates in place as of July 15 of this year, precisely those magazines that devote the most space to public affairs – to covering in depth events like the hearings before this very subcommittee – are put in serious jeopardy. In the case of *The Nation*, the cost of mailing the magazine is already more than three times the cost of the paper on which it is printed. Its president, Teresa Stack, after consulting its printer, has concluded that the new rate increase will be 18% and will cost the magazine an additional $500,000 a year. Last year, the magazine lost circa $348,000 as reflected on its federal income tax form, and *The Nation*, which has the highest circulation among the opinion weeklies and biweeklies, is in better shape than many small-circulation periodicals, some of which will undoubtedly expire in the months ahead.

CJR estimates that unless it is able to co-mail (see below), its postal rate increase could be as high as 30%. As with almost all such journals, publishing CJR is not a money-making proposition. Although CJR had a good year in fiscal 2006 and raised substantial support from philanthropic sources, had the new rates been in effect its budget would have been broken. *The American Journalism Review*, the only other impartial media-monitoring journal in the country, has announced that it may have to go out of business by year's end.

Here is the best estimates other journals of opinion have made of how the new rates will affect them:

The American Conservative: +58%

The National Review: +17% (see attached memorandum)

The New Republic: +15.5%

In These Times: +23%

New York Review of Books: +15%

The Washington Monthly: +15%

Commonweal: +15%

UU World: +21.5%

Commentary: +16%

As a class, small-circulation magazines and journals of our sort face a financial crisis, dramatically exacerbated by the recent action of the postal authorities. These small-circulation journals, whose influence far exceeds their numbers (because of the quality of their readers and the seriousness of their content), are mostly underfunded, yet they bear the brunt of the recent periodical rate increase, whereas more opulent mass-

market magazines with a high percentage of advertising content enjoy a lower rate increase or, as we understand it, in some cases actual rate decreases.

WHY DIDN'T WE INTERVENE SOONER?

I am not interested today in playing the blame game, and I want to move quickly to what is to be done. But before I do, there is one misunderstanding that requires clarification. It is said that since the Postal Regulatory Commission held public hearings for more than ten months, including the opportunity for public commentary and interpretation, prior to making its recommendations to the USPS Board of Governors, small-circulation magazines had the same opportunity as Big Media to have their voices heard, to make their views known; and that failure to do so should disqualify them from complaining after the fact. (The assumption here is that had small-circulation journals of our sort intervened, it would have made a difference in the PRC's recommendations. Perhaps.)

Why didn't journals of opinion intervene? On the surface it's a good question. Clearly in retrospect they should have done so. But here let it be said that the cost of intervention – lawyers and lobbyists – is more than journals of opinion as a class can bear. When I asked lawyers and lobbyists who have monitored and intervened in past PRC hearings on behalf of corporate clients about their fees, cost estimates ranged from $250,000 to more than $1 million per rate case. (If I were a member of this Committee I would ask Time Warner precisely how much it has spent trying to influence the rate-setting process.) A few years ago the sole trade organization representing small-circulation political and cultural journals, the San Francisco-based Independent Press

Association (IPA), with a membership of more than 400 independent journals, managed to hire a top-notch Washington lawyer-lobbyist at rock-bottom pro bono prices, to represent their interests. Both *The Nation* and CJR were members. Let me tell you what happened. IPA did get to present its case, but subsequently it went out of business for lack of funds, and its lawyer-lobbyist, after decades in DC, decided to quit being a lawyer-lobbyist and now teaches high school.

A second reason journals like ours didn't intervene was that the information we thought we had about what the PRC's recommendation would be (based on what the USPS had recommended for the 2006 rate case) turned out to be unreliable on two counts: One, the rate of increase – at least for small-circulation periodicals – was not the anticipated 11% but for some small journals two or three times as much. Two, the formula by which the rate was determined turned out – unlike the last dozen rate cases, which treated large and small magazines more or less equally – to work in favor of large corporations and to the great disadvantage of small, stand-alone publishers. In the past the formula for the rate increase now adopted by the USPS had been put on the table by Time Warner, the largest magazine publisher in the world, and been rejected by the PRC, presumably as inequitable and unwise. In fact, when I testified before the PRC in October 1995 (as a rebuttal witness for the American Business Press), others pointed out at great length the problems the Time Warner proposal posed, and I addressed the harsh burden this proposal would visit on small political magazines (and had a fascinating colloquy with the PRC, which is reflected in 158 pages of testimony); it never occurred to me that having turned such a problematic proposal down time and again that the PRC would recommend and the Board of Governors would adopt it now. (By the way, IPA

went out of business not primarily as a result of its lobby's activities. It also served as a newsstand distributor for small magazines, and its distribution subsidiary went bankrupt. But of course one of the reasons it went into the newsstand distribution business in the first place was the high cost of mailing subscriber copies, and another had to do with the difficulty of securing retail display space, otherwise occupied by large-circulation titles.)

HOW DID IT HAPPEN?

How it happened is a mystery to me. Officially it happened as a result of a public process that is documented in however many hundreds of thousands of pages of PRC documents and testimony, as a result of which the PRC in its wisdom made a recommendation that the Board of Governors accepted. Unofficially, to those outside the process unable to afford to participate (or too naive to devote energy and resources before now) it appears as if Time Warner lobbyists carried the day. How precisely they persuaded the PRC to override the recommendation of the USPS and accept that of Time Warner I cannot tell you. From the perspective of those of us outside the process, all we know is that we were given just eight working days to prepare a response to a 758-page rate plan. (It included rate formulas so complex that to this day some magazine computer models are still struggling to catch up with the PRC's recommendations.) One result is that while some magazines are actually enjoying rate decreases, hundreds of smaller titles face rate increases of more than 30%.

Earlier I said I do not want to play the blame game, and I don't. If this Committee through its hearings can tell the behind-the-scenes story, I think that would be a considerable public service. But even lacking that story, if one takes the PRC and the

USPS at their word, we know that however the PRC and the Governors made up their minds it was based on inadequate data.

According to the rate case, the database that the PRC used to make its recommendation turned out to be deeply flawed. As its own report acknowledged, "The database is not a completely representative sample..."

That the database the PRC relied upon to assess the impact of its rates was not representative is an awful admission. The PRC had a sample of only 251 publications' rates to assess the impact on 30,000 publications of every size and distribution pattern imaginable. The USPS furnished the sample, but it was not a representative sample. The technical term is projectable. If a sample is not projectable to the universe it is representing, valid statistical inference can't be made. There are standard procedures for obtaining projectable random samples. These were not followed by the USPS. Nonetheless, the PRC used the sample because that is all that it had. Consequently the PRC could not make reliable inferences from the sample.

The scandal is that the PRC went ahead and radically changed the rate structure for what it knew was a fragile group of publications even though it did not know the impact of the new structure. The PRC should have ordered the USPS to provide a projectable sample of the 30,000 odd publications or deferred taking such action until a reliable impact assessment could be made.

Nevertheless, in the name of "efficiency" the PRC recommended and the USPS accepted a formula whereby corporations that could pre-sort, drop ship, palletize and all the rest would be charged less than those that could not afford such economies of scale. On the surface the plan has certain logic. In effect Time Warner and large mailers like

Hearst and Condé Nast were saying, We will do the work that the Post Office used to do – we will in effect sort and deliver the mail, and you should pay us for it – in the form of reduced postal rates. In the non-postal world this is called outsourcing, or privatization. Take your pick. (But the PRC neglected to include a provision requiring that the rate-break for periodicals be spread evenly over the entire class, and as a result, small-circulation periodicals are bearing a grotesquely disproportionate share of the postal rate increase.)

CO-MAILING: AN ILLUSORY SOLUTION

To magazines that couldn't afford to drop ship and other economies of scale, the PRC said, Well, you can solve your cost problems in other ways. For example by co-mailing. That may work for some non-weeklies. But it just doesn't work for time-sensitive periodicals or non-standard-sized magazines. The Commission thought that it addressed the problem of co-mailing for small-circulation publications with time-sensitivities (news values) when it proposed removing time-sensitive editorial content (an unacceptable condition for most weeklies). This past summer *The Nation* tried to co-mail, and here's what we found:

Our plan called for testing four issues during the late summer months of this year, when our frequency temporarily drops to every other week. Our sense was that this was the optimum time to test, given the unknowns regarding co-mailing and how it would affect timely delivery. The results of our test at least in our case made clear that co-mailing caused more problems than it solved. The first issue tested, immediately following the July 15 rate increase, did not even enter the mail stream until five to six

days AFTER we would have normally mailed, due to the problems our printer experienced with that week's now extremely complex co-mail pool. Delivery of the issue, which featured one of our most important investigative stories of the year, did not reach our readers until on average NINE DAYS after our normal non-co-mailed delivery would have occurred (and as long as 17-22 days later to the West Coast). While this first issue's results were due in part to problems on our printer's end, they speak to the complications of actually implementing the new rate structure, the pressures on our printer caused by the increased demand for co-mailing services and the vagaries of organizing a large number of titles in a co-mailing pool that changes every week. Any of these variables can and do cause substantial delivery delays, intolerable to a weekly title.

The second and fourth test issues co-mailed as designed, on time and without incident. But, as the third issue approached, our printer informed us that it was experiencing problems similar to the early ones, and we decided to pull the issue from the co-mailing pool at the last minute, lest we experience the same unacceptable delivery delays as we did with the first issue. But for the second and fourth issue, which mailed properly, in the 17 cities we tracked across the country, delivery was delayed on average by SEVEN days, ranging from a four-day delay into Detroit to an 11-day delay into Raleigh, NC, and Washington, DC. And while the postage savings was substantial, around $3,500 per issue, an additional week to deliver a weekly magazine is simply unacceptable. The value of our content is dramatically reduced, if not erased, if we cannot reach our readers in a timely manner, which we have done consistently for over 140 years via the well-run and publicly minded operation that was the United States Postal Service.

Some will tell us to change printers. Like most periodicals, *The Nation* has a long-term printing contract, not easily cancellable even if we wanted to (which we don't). Our printer, Fry Communications in Mechanicsburg, Pa., has printed *The Nation* magazine for the last 10+ years. Our current contract began in June 2006 and runs through 2010. At the time the last contract expired, we undertook a thorough search for other printers that might successfully print and deliver our weekly publication. Obviously we looked at who could handle our volume, our paper stock, our weekly schedule and our mechanical specifications, and most important, ensure good delivery of our timely content. We sent out RFPs to many printers and evaluated our options in great detail. While several dozen printers nationally could handle our printing-specific needs, mailing capabilities became the leverage point in our final decision. Given the postal requirements at the time, and what we anticipated for the future, we made what we believe was the correct decision to stay with Fry, which offered us both excellent pricing and strong mailing capacity. The finalists in the RFP process all spent many hours looking at ways that we might improve delivery and lower costs, including co-mailing, co-binding, co-palletizing, shared drop-shipping arrangements and even utilizing satellite printing plants in geographically dispersed areas closer to in-home delivery centers. After much research, it became clear that as a weekly with a very tight operating budget (a magazine that has in fact lost money for almost all of its 140+ years), our options to deliver in a timely and affordable manner were extremely limited, even at the most state-of-the-art facilities provided by printers such as Donnelly or Quebecor. Fry has been co-mailing since 2002, and has one of the largest co-mailing machines in the industry.

The postal consultants at our fulfillment house, Kable, and our printer, Fry, assure us that as a single title, we mail as efficiently as possible, fully presorting our mail and using the most efficient containers available given our volume and geographic concentrations. We continue to look at other options, such as co-binding, which may offer some smaller savings and perhaps fewer delivery delays vs. co-mailing. Yet our potential co-binding partner (the religious weekly magazine *World*) has been so devastated by the rate increases that it plans to cut its frequency in half in January, making it an unsuitable candidate for co-binding. Other experts we spoke to at the Magazine Publishers Association, while expressing sympathy for our predicament, offered small comfort: we might as well co-mail, they tell us, since rumor has it that the USPS plans to downgrade the service to single-title weeklies anyway. The alleged plan: delivery will get slower and slower, till such time as it matches the current co-mailing delivery schedule.

If this venerable institution, the USPS, goes forward with plans to further decrease its service levels, it will indeed be a sad state of affairs. (I am old enough to remember when mail was delivered twice a day.) Shifting work and costs onto the private sector may sound good in theory, but in fact what it will mean is that the largest and most profitable players (with their lobbying clout) will increase their profits while the USPS ignores the postal principle deemed by the founders to be essential to the enlightenment of the Republic. Namely, preferred treatment for the press, which in their day was largely radical, revolutionary and partisan.

WHAT THE POST OFFICE DID AND DIDN'T DO

In the name of "efficiency," what the USPS did do (based on a moderated version of Time Warner's proposal) was adopt a formula whereby each magazine would pay its own way (instead of averaging costs within the class, as used to be the case). What the USPS didn't do was weigh the public interest against the so-called "efficiency" interest; the social interests of readers and the democratic public sphere in the circulation of information and opinion against the economic interests of the powers that be in so-called "efficiency" (so defined as to be available only to mega-magazine publishers in a position to achieve economies of scale). It's important to remember that the magazine class has always been subsidized (as per the founding fathers' mandate); currently it does not contribute to USPS overhead, unlike other classes of mail. Over the years, these big magazines have received far more actual dollars of support than all the magazines like *The Nation* combined. And with this rate decision, they will receive even more.

A little history may be in order.

As I suggested above in my personal statement, the founding fathers of this country believed that the circulation of information, opinion and what they called intelligence was a pre-condition to self-governance. They saw the postal service as the circulatory system of democracy. Also, they thought it would help bind the country together. As one contemporary put it, the postal system helped transform the country from a confederation of separate states into "one great neighborhood."

That is why among other reasons, Benjamin Franklin agreed to serve as Postmaster General. That is why Thomas Jefferson sought to persuade Washington, who believed that all newspapers should be delivered free of charge, to name the great pamphleteer Tom Paine as Postmaster General. In defense of the view that periodicals

should be mailed free, Rep. Elisworth Gerry of Massachusetts declared, "wherever information is freely circulated, there slavery doesn't exist, or if it does, it will vanish as soon as information has been generally diffused."

For the next two hundred years we proceeded on this assumption that the mail, especially periodicals including information and opinion relating to public affairs, was a public good. Had the postal authorities properly factored this into their deliberations and weighed it against their narrow definition of efficiency, it is difficult to see how they could have ended up with the invidious formula they ultimately adopted.

Had they done so, they might have considered the option of reallocating costs within the periodicals class itself to benefit the public interest, i.e. for example, charge even less to publications with a higher percentage of editorial content and more to periodicals with a higher percentage of advertising content; less to publications that devote more space to public affairs and more to publications that ignore public affairs. None of these ideas is easy to implement. Each of these proposed acts comes with delicate and nuanced First Amendment and other issues to be worked out, but in the interests of a robust democratic public sphere the exercise may be more than worth the trouble.

WHAT IS TO BE DONE

The members of this Committee know better than I what CAN be done by way of legislation, and on what sort of timetable, but I know better than you what could happen if nothing is done, the damage to be inflicted on the very same periodicals – left, right, center, libertarian and communitarian, Democrat and Republican, secular and religious –

whose core mission is to cover the public sphere, to set the standard for reasoned argument and public discourse.

Over the years any number of people involved with magazines such as *The Nation* and *The New Republic,* but also *Harper's* and the late *Saturday Review*, have given much thought to matters postal. Here are some of the ideas it seemed to me worth bringing to your attention.

(1) Change the law so that in the future either the requirement that each class pay its own way be struck and/or that social mission be emphasized in the allocation of charges within each class; in other words that the rate-setters better balance the post office's historic mission against so-called prudent business practices only available to large mailers.

(2) Congress should take back the rate-setting prerogative it gave away in 1970. What appeared then to be delegation turns out now to have been abdication in favor of Big Media.

(3) Congress should pass a resolution condemning the new rate structure and urging the Board of Governors to reverse itself.

(4) The Commission should issue its own fact-finding report including a history of postal policy (see Kelibowitz and Joseph) but also impact studies, using an enlarged and open database, on small-circulation magazines.

(5) Dumb Question: If it is true that the postal service has been losing volume at least in part due to increased fees, isn't the alternative to lower rates and thereby increase volume?

(6) First Class mail consists of mail that private citizens want and pay to send. Second Class (now called periodicals class) mail consists of mail that private citizens want and pay to receive. First and Periodical Class mail is a service to the public. Third Class mail – direct or junk-mail – is said to be doing well when it realizes a return of 2%.[1] But that means that 98% of the people who receive direct mail don't want it. It's an advertising medium. Why not raise the price class of mail that nobody wants anyway and use it to subsidize the periodical class mail, which 100% of its receivers have paid good money for and which performs a public service?

(7) If one thinks of the mails as a communication channel and one thinks of our other communication channels a question arises: Unlike most other nations the US has turned over certain channels of communications (television first and foremost among them) to profit-making corporations. Unlike the post office, which oversees the mails, the television channels are not required to break even. Fair enough. But if every TV station were asked to pay a reasonable rental fee for the use of its channels, then resulting revenue would erase the postal debt overnight. Think about it.

(8) In the future, when setting periodical class rates, why doesn't Congress take into account the size of circulation, profitability, as well as some of the other variables outlined above? In other words, why doesn't Congress take a holistic approach and charge less for publications that are published in the public rather than for-profit interest? (To a degree this already happens for non-profits, but in the political periodical business publications that might otherwise be non-profit retain their for-profit status because they

[1] (I know because both *The Nation* and CJR depend on direct mail.)

want to be free to endorse candidates and push for legislation – something non-profits are not allowed to do under the law.)

As *The New Republic* has pointed out, "to subsidize the mail is not to underwrite a political view of one special interest over another. It is to underwrite a diversity that invigorates democracy."

(9) Why not revive the proposal put forward by Congressman Morris "Moe" Udall and supported by Barry Goldwater and others many years ago: That the first 250,000 copies of all publications be mailed at reduced rates? Or the legislation proposed as recently as 2002 by Bernie Sanders that would place a moratorium on postal increases for magazines with a low percentage of advertising content, low circulation or non-profit status?

(10) Finally, and immediately, under the new postal bill the USPS has the flexibility, working in tandem with Congress, to roll back and/or redistribute rates now – before the end of the year. I propose that Congress ask the USPS to extend non-profit rates to small-circulation political magazines (without imposing upon them the restrictions that bar the endorsement of candidates or attempt to influence legislation).

To recapitulate: I do not pretend to have the simple solution to solve the crisis that confronts us. But if you/we do nothing, the impact of the new postal rate increase on the flow of ideas and opinions in America is likely to be significant. It is no accident that the President of *The Nation* and the Publisher of *National Review,* two periodicals on the opposite sides of the political spectrum, recently teamed up to write an Op Ed essay sounding the alarm (see attached page). Such small political journals – which, by the way, carry the most discourse – bear the heaviest rate increases. The unpopular ideas and

opinions that these journals propagate and circulate today often turn out to be tomorrow's wisdom. They act as intellectual and political gadflies, they prod their larger and staider colleagues, they question conformity and complacency.

By helping them recover from the grievous wound inflicted upon by the recent rate increase, this Committee will have deepened and strengthened our democracy.

Los Angeles Times opinion, May 28, 2007

Magazines feeling postal pinch: High-circulation periodicals enjoy discounted rates, while smaller publications get hit with steep rate hikes.

By Teresa Stack and Jack Fowler
TERESA STACK is president of *The Nation*. JACK FOWLER is publisher of the *National Review*.

The cost of getting magazines into your mailbox will shoot up July 15. How much? It depends.

Magazine publishers are facing a radical postage rate restructuring that favors those with large circulations and transfers costs to small- and mid-circulation publications.

Past increases to periodical postage were applied fairly equally across all publications. But this time, things are drastically different—and potentially damaging to the diversity of voices that our founders strove to foster when they created the national postal system.

Our respective magazines—*The Nation* and the *National Review*—sit on opposite ends of the political spectrum and disagree on nearly every issue. But we concur on this: These proposed postal rate hikes are deeply unfair.

It is not simply that we want to avoid a massive increase in our mailing costs, though that is a factor. More important to us is that we believe in a vibrant marketplace of ideas (where we each think our ideas will prevail). We are not afraid of intellectual competition; we welcome it.

For this latest round of rate hikes, the U.S. Postal Service proposed a 12% increase that would have affected magazines more or less equitably. Then, in an unprecedented move, that plan was rejected by the Postal Regulatory Commission, the body responsible for setting rates. Instead, it approved a complicated pricing system based on a proposal by Time Warner Inc., the largest magazine publisher in the country. Rather than base rates on total weight and total number of pieces mailed, the new, complex formula is full of incentives that take into account packaging, shape, distance traveled and more.

It adds up to this: discounts for some periodicals; as far as we can see, mostly the huge-circulation titles associated with firms like Time Warner. At smaller magazines like ours, rates will go up 15% to 25%. Research by McGraw-Hill Cos. concludes that the rate increases for some small-circulation publications could hit 30%.

Time Warner and the Postal Regulatory Commission say this scheme rewards efficiency. But the rates appear to have been adopted with little research into their effect on publishers and with no meaningful public input.

How will small magazines that operate on the economic margins—yet have an outsized effect on public discourse—accommodate $500,000 (in the case of *The Nation* and the *National Review*) in additional postage expense? Will we be forced to cut back on reporting, raise our prices, reduce our staffs or our number of pages to stay afloat? For some titles, the change may prove fatal. It certainly will make it more difficult to start a new magazine, and publishing will be less competitive as a result.

Time Warner and the postal commission seem to have little understanding of the crucial role the Postal Service has played in establishing an open marketplace of ideas. It has always been a central policy of the Postal Service to use its pricing mechanism to encourage smaller publications and competition.

Since the time of James Madison and the founders in the 1790s, it has been understood that low rates for small publications make it possible to have the rich, open and diverse media that a self-governing people require. This is what is at stake today. And because so much of the material online originates in print magazines, these postal rates could have the unintended effect of shrinking the digital marketplace of ideas as well.

We urge the relevant congressional committees to hold a hearing to investigate this coming crisis before it is too late. The last 215 years of postal policy were instrumental in the creation of the extraordinary free press we have in the U.S. today. We should not begin to overturn this magnificent tradition.

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Appendix

Attached to this testimony are the written statements of a number of other magazines that have been similarly impacted by the rate increases. They are included here for the record.

NATIONAL REVIEW

215 Lexington Avenue
New York, NY 10016
212-679-7330

www.nationalreview.com

Statement by Jack Fowler, Publisher, concerning the Periodical Postal Rate Increase of July 15, 2007
Submitted September 28, 2007

To the Honorable Danny Davis, Chairman, the Honorable Kenny Marchant, Ranking Member, and all Esteemed Members of the Federal Workforce, Postal Service and District of Columbia Subcommittee

National Review is a conservative journal of news and opinion. Founded in 1955 by William F. Buckley Jr., the magazine has enjoyed 52 years of full, vigorous, and influential participation in America's ongoing important public debate of ideas.

We contend that America benefits from the existence of opinion magazines, which in addition to *National Review* include *The Nation*, *The American Conservative*, *Human Events*, *The New Republic*, *The American Spectator*, *The Progressive*, *The Weekly Standard*, and others. Despite our conflicting ideologies and frequencies and formats, our magazines share one thing: we receive little advertising support, particularly when compared to popular mass circulation publications which discuss celebrity, gossip, sports, and other topics far afield from political speech and debate, the form of speech most central to protection by the First Amendment.

This is the life we have chosen. But we have chosen it knowing that, while advertisers may be wary of associating with the opinions published in our collective pages, at least the United States Post Office and Postal Service historically recognized the vital role our journals played in the life of our Republic. That special recognition seems to have ended on July 15th, with the imposition of new rates that particularly impact opinion magazines.

On June 7, 2007, *National Review* mailed 161,443 copies of the June 25th issue, which totaled 60 pages and weighed 0.26 pounds per copy. On August 9, 2007, three weeks after the new rates commenced, we mailed 161,321 copies of the August 27th issue. This smaller issue totaled 52 pages and weighed 0.23 pounds per copy. Our postage bill for the June 25th issue was $41,779.59, or $0.2587 per copy. The postage bill for the smaller August 27th issue was $48,823.80, or $0.3026 per copy. That represents a 17% increase. That is huge.

The new rates place a higher increase in postal costs on opinion journals than on popular magazines on the rationale that such should incentivize opinion journals to find new efficiencies. This assumes that 1) proposed efficiencies which are enjoyed by large-circulation publications may also be enjoyed by *National Review* (they cannot, or, when they can, they risk severely impacting the delivery of our time-sensitive publication), and 2) we are not constantly seeking ways to save costs (we are).

In response to previous postal rate increases, *National Review* has been forced to do a number of things, including the following: 1) reduce our paper stock and quality to the bare minimum which we believe will acceptable for advertising, 2) reduce the number of editorial pages in each issue, and 3) lessen our frequency from 25 times annually to 24 times.

In response to this latest large and disproportionate increase, we now ask that this Committee and this Congress take appropriate action to reduce the new periodical rates imposed on opinion magazines, at least to the level enjoyed by those magazines which utilize the services of the United States Postal Service in order to inform America about drunken heiresses and the latest doings of former Heisman Trophy winners.

Thank you for considering this important appeal.

September 27, 2007

Statement of Allen Chin on behalf of THE NEW REPUBLIC for the Federal Workforce, Postal Service, and District of Columbia Subcommittee of the House Committee on Oversight and Government Reform, 110th Congress, 1st Session (October 3, 2007):

I am writing to inform you of the financial impact of the postage-rate increase that took effect on July 15, 2007. Since that time, THE NEW REPUBLIC has seen a 15.5 percent increase in postage costs. Annualized, this represents an additional $40,000 in postage, a significant amount for a magazine with a small subscriber base.

Due to our small subscriber base, we are unable to take advantage of the discounts that reward efficiencies in mail preparation and entry. And that's a real loss to the nation: For more than 90 years, THE NEW REPUBLIC has been a significant part of America's institutional memory. With unconventional takes on major political changes, cultural shifts, and the issues of the day, THE NEW REPUBLIC does not just catalogue, but shapes the policies that affect the country. In short, THE NEW REPUBLIC has an important role to play both in journalism and in the history of the nation, delivering intelligence to the nation's most intelligent and creating a discussion that is about changing American discourse—not about popularity.

1331 H STREET NW SUITE 700 WASHINGTON, D.C. 20005 202-508-4444 F 202-628-9380

The New York Review of Books
1755 Broadway, 5th Floor, New York, NY 10019 Tel: 212-757-8070 FAX: 212-333-5374

September 24, 2007

Subcommittee on the Federal Workforce, Postal Service and The District of Columbia
Danny Davis, Chairman

Re: Periodical Postal Rate Increase effective July 15, 2007.

Dear Chairman Davis,

I am writing in support of the testimony of Victor Navasky, Publisher Emeritus, *The Nation*, regarding the recent periodical postage rate increases.

The New York Review of Books is a journal of ideas published twenty times per year since 1963. The *Review* has served as a forum for writers and thinkers to discuss not only current books but also the complex issues of American culture, society, economics, politics, and the arts. The *Review* is not a mass-market, advertising-driven magazine. It has a modest but devoted subscriber base that is its primary source of financial support.

As a small, independent publisher we are disproportionately affected by any substantial increase in our postal expense. We have taken steps in order to minimize this postal increase as much as possible. We have reduced the weight of the *Review's* paper stock to the minimum that can be handled by the postal equipment. We also are paying our printer to drop ship copies to postal BMCs, rather than paying the USPS for these shipments, whenever we can recognize net savings. Unfortunately, as a tabloid publication, we are unable to take advantage of other potential savings such as co-mailing and co-palletization, which our printer does not offer for publications of our dimensions.

After taking all these steps *The New York Review of Books* has seen a 15% increase in postage costs. Annualized, this represents an additional $100,000 in postage, a substantial increase in expense for a small, single-title publisher.

Please consider the undo burden that this rate increase has placed on small publishers who are least able to absorb substantial cost increases. Thank you for providing a hearing for these concerns.

Sincerely,

Rea S. Hederman
Publisher

The American
Conservative

"Statement of Scott McConnell on behalf of The American Conservative *for the Federal Workforce, Postal Service and District of Columbia Subcommittee of the House Committee on Oversight and Government Reform, 110th Congress, 1st Session (October 3, 2007)"*

I regret to report that the postage increases we are facing under the new provisions are little less than catastrophic. Magazines like ours operate on a very tight margin. We are right now just beginning a push to expand beyond our initial subscription base. But suddenly we are faced with an increase of postage costs of 58 percent, a rise in postage per copy from $0.198 to $0.315. This will raise our annual postage rates to more than $60,000, whereas they used to be under $40,000 a year. Before the increase, postage represented a 15 percent of our cost of goods sold. It now rises to 23.7 percent. It is my understanding that these increases are higher even than they are for larger publications, because there are fewer opportunities for us to take advantage of discounts.

This increase forces a publication like ours to confront some very painful choices. We could try to absorb the cutbacks by cutting editorial expenses--what we pay writers, what we pay editors, what we pay artists. These sums are hardly grand--like most little magazines, our contributors make a large sacrifice when they write for us. But to cut them further risks a kind of dilution of editorial quality that could obviate the reason for our existence. Perhaps we could change our format, and publish the magazine less frequently, but that would put us in an entirely different market category, and would also be harmful to our editorial influence.

Short of such measures, I am really at a loss as to what we might do. I earnestly hope the rate increase is reconsidered.

1300 Wilson Blvd., Suite 120, Arlington, Virginia 22209 Phone (703) 875-7600 Fax (703) 875-3350 www.amconmag.com

Mother Jones

www.motherjones.com
222 Sutter Street Suite 600
San Francisco, California 94108
T 415 321 1700
F 415 321 1701

October 1, 2007

To: Subcommittee on the Federal Workforce, Postal Service and the District of Columbia. Danny Davis, Chairman

Re: Periodical Postal Rate Increase effective July 15, 2007.

Dear Chairman Davis,

Thank you for inviting testimony on the matter of the 2007 revisions to the postal rate structure.

As pedestrian as the topic may sound, these new rates touch virtually every citizen who feeds her interest in public issues by reading thought-centered periodicals. Radically increased postal costs – non-profit *Mother Jones'* postal expenses have now increased more than 25% in the last two years – have the effect of *punishing* political discourse at a time when our country is wrestling with some of the most difficult issues it has ever faced. Is this a time to push engaged citizens -- people with the willingness to educate themselves and engage in the search for solutions – away from idea-centered print journalism?

Mother Jones is a bi-monthly magazine of independent investigative reporting, published by the non-profit foundation for National Progress. Our circulation is approximately 230,000, making us relatively large within the ranks of independent publications but still small for an enterprise dedicated to the (time-intensive and thus expensive) work of reporting. Our advertising base is very modest – ad sales account for less than 15% of our total revenue. The change in the postal rate structure hurts publications such as *Mother Jones* disproportionately.

The Postal Rate Commission introduced the new structure, one that followed in significant respects a proposal made by Time-Warner, after only a very brief

window of public comment. In adopting the plan, the PRC consistently asserted the goal of increased efficiency, certainly a desirable trait in the system. But in implementing a structure which gives such clear financial preference to publications with large subscriber lists and lots of advertising, the new system shifts significant costs *onto* publications whose volumes are smaller, whose "postal sorts" yield smaller bundles, and who carry modest number of ad pages. And while it is true that smaller publications can, in theory, achieve greater volume and increased postal discounts by "co-mailing" with other publications, that practice can itself be difficult and costly. The net effect of these changes is thus to selectively harm the set of periodicals that are in the business of ideas at a time when we are also dealing with other dramatic changes in the media world. Trying to compete with *Time* on the one hand and Google on the other may make for a David v. Goliath story line – but the odds aren't good for political discourse.

I urge the committee to consider the impact of the new postal rate structure on independent magazines of ideas and to re-introduce into the mandate of the PRC the notion, core to the founding ideals of the country, that the nourishment of thought in our democracy has a value that trumps "cost efficiency."

Sincerely,

Jay Harris
President & Publisher

IN THESE TIMES

INSTITUTE FOR PUBLIC AFFAIRS
2040 North Milwaukee Avenue
Chicago, Illinois · 60647
PHONE (773) 772-0100
FAX (773) 772-4180
WEB www.inthesetimes.com

Statement of Joel Bleifuss on behalf of *In These Times* for the Federal Workforce, Postal Service and District of Columbia Subcommittee of the House Committee on Oversight and Government Reform, 110th Congress, 1st Session (October 3, 2007).

In August 2007, *In These Times*, an independent magazine based in Chicago, was hit hard by a 23% postal rate increase. This complex new rate structure, designed by and for the benefit of the largest publishing companies, has severely impacted our small magazine's ability to do business. We face an immediate threat to our financial health. These reckless postal rate increases are aimed at the heart of our nation's independent press. I urge you to ask the spokespeople of the media conglomerates whether they would support these increases if their mailing costs had risen 23%.

This is a democracy issue. The founding fathers, in their infinite wisdom, created a system that made it cheaper for smaller publications, irrespective of viewpoint, to launch and survive. In 1792 the United States Congress converted the free press clause in the First Amendment from an abstract principle into a living reality for Americans by providing newspapers with low postal rates. These low rates were crucial for the growth and spread of the abolitionist movement, the progressive movement and, later, the civil rights movement. More broadly, they have been central to the development of participatory democracy in general. Today, low postal rates remain crucial to the survival of independent American publications like *In These Times*.

A national monthly magazine with a circulation of 20,000 people, *In These Times* is committed to providing a forum for discussing the politics that shape our lives, and to producing a magazine that is read by the broadest and most diverse audience possible. Throughout its 31-year history, *In These Times* has published the writings of such invaluable American authors and political figures as Kurt Vonnegut, Studs Terkel, Alice Walker, George McGovern and the late Sen. Paul Wellstone, who was one of our first subscribers.

Three decades after its founding, *In These Times* remains committed to covering the controversial issues of our time. Through five presidential administrations, *In These Times* has adhered to the belief that in order to thrive, our nation's citizens need independent media to inform, educate and orient themselves. Our nation's founding fathers believed this, too. The postal rate policy they enacted has served free thought in America for more than 200 years. We ask Congress to provide some rate relief and reverse this substantial attack on the viability of our nation's independent press.

UUWORLD

THE MAGAZINE OF THE UNITARIAN UNIVERSALIST ASSOCIATION OF CONGREGATIONS

September 25, 2007

House Subcommittee on Federal Workforce,
Postal Service, and the District of Columbia
The Hon. Danny K. Davis, chair
U.S. House of Representatives
110th Congress
Washington DC 20515

TESTIMONY CONCERNING THE PERIODICALS POSTAGE RATE INCREASE

UU World is the nonprofit religious magazine published four times a year for 125,000 member households affiliated with the Unitarian Universalist Association of Congregations. The magazine is the primary way the Association serves all members of its 1,000+ congregations in the United States. (We also mail several hundred copies to our religious partners internationally.)

Changes in the periodicals postage rate, effective July 15, 2007, increased *UU World*'s postage expenses by 21.5 percent. Like many magazines, we had expected an increase of between 11 and 12 percent. Although consumer magazines might find it relatively easy to absorb a $20,000 annual increase in postage costs, for a nonprofit membership organization's quarterly magazine, the amount is significant.

It is disturbing to learn that the new rates abandon the long-standing American tradition of supporting a diverse marketplace of ideas with a fair and uniform postage rate for periodicals. Historically, the periodicals rate allowed small journals of opinion to reach a national audience. But the new rates reward high-circulation periodicals with discounts that smaller-circulation periodicals simply cannot qualify for. Instead, we face a steep and unfair increase in mailing costs.

UU World already takes advantage of the cost-cutting measures offered by our printer, one of the country's largest. We allow delays in delivery to put as many magazines as possible on pallets for shipping to regional distribution centers, rather than mailing them from a central location. But the simple truth is that a national magazine with only 125,000 subscribers cannot take advantage of the discounted rates the new periodicals scheme makes available to the largest magazines.

I urge you to consider the role of smaller periodicals in America's civic life and to look for ways to restore fairness to periodicals postage.

Gratefully yours,

Christopher L. Walton
Editor

25 Beacon Street, Boston, Massachusetts 02108 • www.uuworld.org • 617-742-2100 • Fax 617-742-7025

The Progressive

Statement of Matthew Rothschild,
Editor and Publisher, The Progressive Magazine
for the Federal Workforce, Postal Service and District of Columbia
Subcommittee of the House Committee on Oversight and Government Reform, 110th Congress,
1st Session (October 3, 2007)

Chairman Waxman and Members of the Committee,

The Progressive magazine was founded in 1909 by Republican Senator Robert M. La Follette—"Fighting Bob," as we call him even today.

One of the things he fought for was a fair playing field in the media arena.

He knew, as we know, that big media corporations have a huge influence over the electorate.

He knew, as we know, that they have resources well beyond the wildest fantasies of struggling little magazines like ours.

And he would be outraged, as we are outraged, that the government is allowing the Postal Rate Commission to engineer a rate hike that favors the already favored media giants and makes life even more precarious for small, underfunded political magazines.

These magazines, from the left and from the right, offer the lively political give and take that our founders understood was so crucial to our democracy.

At *The Progressive*, we need to watch every penny. We budget carefully, and we have no owners or philanthropists who bail us out with five-figure or six-figure donations when times get tough.

And so, when postal rates jump beyond our budgeted figures, we suffer. The postal hike is costing us at least $20,000 more than we bargained for. Unlike most businesses, magazine publishing is particularly sensitive to postal hikes. Because our customers subscribe and pay for our service in advance, we cannot simply print and deliver less of our product and remain in business.

We generally expect and plan for modest postal rate increases. Significant hikes like this one, however, threaten to obliterate the most conservative budget projections and increase the likelihood of layoffs and bankruptcy.

The Progressive has published the words of many fine members of the U.S. Congress, from La Follette himself to Senators Gaylord Nelson, Hubert Humphrey, Paul Wellstone, and John F. Kennedy. We've also published articles by, or interviews with, Representatives David Obey and Tammy Baldwin, as well as Sherrod Brown and Bernie Sanders before they became Senators.

This is just one of the public services we provide.

But by raising the postal rates on *The Progressive* we'll be hard-pressed to continue to provide this or any of the other services we offer in our attempt to enrich our democracy.

Fighting Bob La Follette, were he in this Congress today, would urge you, as I urge you, to overturn the decision by the Postal Rate Commission and reestablish that level playing field that is so crucial to the free exchange of ideas.

Washington MONTHLY

1319 F Street NW, Suite 710
Washington, DC 20004

Tel 202 393-5155
Fax 202 393-2444

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October 1, 2007

Statement of Claire Iseli, Vice President of Circulation and Business, on behalf of the *Washington Monthly,* for the Federal Workforce, Postal Service and District of Columbia Subcommittee of the House Committee on Oversight and Government Reform, 110th Congress, 1st Session (October 3, 2007):

Re: Periodical Postal Rate Increase effective July 15, 2007

We support the testimony of Victor Navasky, Publisher Emeritus, *The Nation*, regarding the recent periodical postage rate increases.

As a small-circulation nonprofit magazine published ten times a year since 1969, we serve as an important independent source of reporting on government and politics in the Nation's Capital, presenting thoughtful and thought-provoking articles on what needs to be done to move the country forward. We are also a training ground for some of the country's best journalists, many of whom got their start at the *Washington Monthly*. Under the best of circumstances, the economics of publishing a single title are difficult. That is why the steep increase in periodicals postal rates – an unavoidable cost of doing business – has hit us so hard. We have taken every possible step to minimize the impact, including co-mailing and co-palletization, yet we are facing a 15% increase that will cost us additional thousands of dollars each year to get our magazine to our subscribers.

More and more, it seems as if the national conversation is being controlled by the large media corporations. We hope that this Subcommittee will help to preserve a network of independent voices by reversing the postal rate increases that have placed an unfair burden on small publishers.

Thank you for providing us the opportunity to express our concerns.

Commentary

165 East 56 Street
New York, New York 10022
(212) 891-1400
Fax (212) 891-6700

Statement of Sarah Stern on behalf of Commentary for the Federal Workforce, Postal Service and District of Columbia Subcommittee of the House Committee on Oversight and Government Reform, 110th Congress, 1st Session (October 3, 2007)

Commentary prides itself on being America's most distinguished monthly journal of ideas. Although the magazine has a relatively modest circulation, it is widely considered to be the most influential opinion magazine in the country.

Commentary is published by Commentary, Inc., a registered not-for-profit. Its primary goal is to be an important voice in public debate and to promote reasoned discussion of the pressing issues of the day. Although it has always striven to keep costs to a minimum, like other small-circulation opinion magazines it runs at a deficit, and indeed has lost money every year since its founding in 1945.

Given these ongoing losses, the magazine has been compelled to keep its personnel costs--its single largest expense--low. It has also continually worked hard to reduce its second highest expense--printing and production--while still publishing a handsome and high-quality product. The third biggest budget item is postage, something over which the magazine has had no control.

This most recent postal increase has hit the magazine's bottom line very hard. Costs have risen by over 16 percent for the two issues that have been mailed since the new rates went into effect. Why? Commentary's circulation rate base is now 27,000, most of which consists of individual subscribers. Although the discount offered by the postal service goes to publications that are able to "bundle," only 2 percent of Commentary's mail is shipped in bundles; the rest, 98 percent, is sent piece-rate to subscribers who are dispersed widely throughout the nation. Many of Commentary's readers, although they are remarkably loyal to the magazine, are likely to reject a subscription price increase of the magnitude now becoming necessary to make up for the shortfall caused by the new rate structure.

In sum, this latest rate increase could have a severe impact on the future of a 62-year old publication that continues to make a significant contribution to American culture and to inform and enlighten public discourse on the most urgent issues of the day.

Mr. DAVIS OF ILLINOIS. Thank you very much, Mr. Navasky.

Mr. NAVASKY. Thank you.

Mr. DAVIS OF ILLINOIS. We will go to Mr. Hollingsworth.

STATEMENT OF JEFF HOLLINGSWORTH

Mr. HOLLINGSWORTH. Thank you, Mr. Chairman.

I am Jeff Hollingsworth, vice president of Eagle Publishing. We are the leading publisher of materials on public policy that appeal to a politically conservative readership. Our products include Human Events, the national conservative weekly, which has been published continuously since 1944 and which will be the focus of my comments today; Regnery Books; the Conservative Book Club; the Evans-Novak political Report; a stable of highly regarded financial and investment newsletters; and RedState.com, one of the country's top conservative blogs.

Today the survival of Eagle's products is in jeopardy. Human Events, in particular. This isn't due to a lack of demand or declining interest in what we market; rather, it is because of the caprice of Government. Regrettably, it seems that when you are dealing with Government it is not what it can do for you, it is what it can do to you. Such is the case with the latest in a dizzying round of postal rate increases.

The July increase has had the effect of punishing publishers of periodicals high in editorial content, such as scholarly publications, newsletters, non-profit organization bulletins, and journals of culture and opinion, such as Human Events. More precisely, the July rate increase socked Human Events with a staggering 17 percent increase in postal costs.

While we are paying more, we are getting less. This is because the USPS expects mailers to do more preparatory work than ever before. Chronic slow delivery of Human Events ultimately forced us to go to a split print with facilities on both coasts. Unfortunately, while this arrangement has improved the timeliness of delivery, it is not amenable to co-mailing or other efficiencies the PRC incorporated in the rate case.

Maintaining profitability in the publishing industry has always been challenging. For small- and medium-sized publishers, the postal rate increase is making an already difficult job even more so.

When established more than 200 years ago, the Postal Service was intended to be the means to bind the Nation together. Its purpose was to improve communication; aid commerce; allow news, ideas, opinion, learning, and culture to reach all Americans. It was and has been a key facilitator in the exercise of our first amendment rights to free expression. For generations, small journals of opinion and culture mailed to subscribers have enriched the lives of countless Americans and contributed substantially to our national identity and the body politic.

But this hallowed legacy is on the verge of being crippled, not by virtue of the ebb and flow of market forces, nor by consumers deciding for themselves what they wish to read or not read, but by the actions of a single Government agency. By imposing unreasonable rate increases without analyzing adequately and thoroughly the potential consequences to small- and medium-sized publishers,

the Postal Regulatory Commission may be responsible for wiping out Americans' access to various journals of opinion and culture. It may be responsible for diminishing the marketplace of ideas. It may be responsible for making the exercise and enjoyment of our first amendment rights to free speech and expression more difficult.

If Congress fails to take notice of what is happening and what is at stake and fails to act, it, too, will deserve its fair share of responsibility for the deleterious impact of this rate increase.

Since the Postal Service is a monopoly protected by statute, publishers in financial distress, thanks to the rate hikes, have almost nowhere else to go. Many have turned to the Internet, and Internet content by newspapers, magazines, journals, and other periodicals is growing at light speed.

In another example of the law of unintended consequences, the more the Postal Service balloons its rates, the more customers it either puts out of business or drives away to the electronic media.

Ultimately, in my opinion, the answers to these problems are two-fold. No. 1, the Postal Service must be privatized. As Former Postmaster General William Henderson wrote in a Washington Post essay shortly after stepping down, "The time is now for privatization." Suggestions on how to do this include selling it to its employees, making it a public stock company, or breaking it up into regional companies.

No. 2, modify or repeal the private express statutes. Users of most classes of mail services currently have nowhere else to turn. They deserve alternatives. And because the Postal Service has no competition in those areas, it has no incentive to be customer friendly, efficient, or truly business-like in its operations.

With competition, when our mailboxes are finally liberated, the results will be good for the Postal Service, entrepreneurs, and postal stakeholders.

As for the here and now, we urge the Congress to act promptly in order to make it crystal clear to the PRC and the Board of Governors that it never intended any of its statutes on postal policies to be construed such that rate hikes can be imposed with the effect of stifling free expression, driving publishers out of business, and unfairly imposing onerous financial burdens on entities least able to afford them.

We urge Congress to work with the Postal Service to revisit the July rate increase before even more damage is done to the publishing industry.

Thank you, Mr. Chairman.

[The prepared statement of Mr. Hollingsworth follows:]

STATEMENT OF D. JEFFREY HOLLINGSWORTH, VICE PRESIDENT, EAGLE PUBLISHING CHAIRMAN'S OFFICE, BEFORE THE COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM SUBCOMMITTEE ON FEDERAL WORKFORCE-POSTAL SERVICE-DISTRICT OF COLUMBIA, U.S. HOUSE OF REPRESENTATIVES OCTOBER 3, 2007

Thank you, Mr. Chairman, Mr. Marchant, and members of the Subcommittee for the opportunity to appear before you today. I am Jeff Hollingsworth, Vice President at the Chairman's Office of Eagle Publishing, Inc.

Established in 1993, Eagle is America's leading source of books, periodicals, and Web sites with a conservative, free-enterprise focus. Many of our products are familiar to most of you, I'm sure, both Democrats and Republicans alike. They include:

- *Human Events,* the national conservative weekly which has been published continuously since 1944,
- Regnery Publishing, Inc., marking its 60th anniversary this year, the country's leading publisher of hard-hitting books on current affairs, public policy, and political philosophy. More than 30 Regnery titles have appeared on *The New York Times* Best-Seller list, the most recent being Laura Ingraham's *Power to the People,* which debuted this week at #1.
- The Conservative Book Club, which was launched in 1964,
- *The Evans-Novak Political Report*, for 40 years one of America's most highly respected newsletters on campaigns and elections, politics, and "inside" news on the presidency and Congress,
- A stable of highly regarded financial and investment advisory newsletters, including *Mark Skousen's Forecasts & Strategies,* Fabian's *Successful Investing,* Vardy's *Global Stock Investor,* and others,
- RedState.com, one of the country's top conservative blog sites.

Today, the survival of Eagle's products is in jeopardy, *Human Events* in particular. This is not due to a lack of demand or declining interest in what we market. Rather, it's because of the caprice of government.

Regrettably, all too often when it comes to dealings with government, it's not about what it can do *for* you, but what it can do *to* you. Such is the case with the latest in a dizzying round of postal rate increases. The increase that took effect in July has had the effect of punishing publishers of periodicals high in editorial content, such as scholarly publications, newsletters, non-profit organization bulletins, and journals of culture and opinion such as *Human Events.* More precisely, the July rate increase socked *Human Events* with a staggering 17% increase in postage costs.

In order to keep publishing, *Human Events* recently took the unprecedented step of making a direct appeal to subscribers asking for their help in offsetting the increased expense. They have responded generously and well beyond expectations. However, *Human Events,* or any other journal of opinion and culture, regardless of viewpoint, cannot use the hat-in-hand approach indefinitely. Instead, we submit that Congress must take remedial action or the Postal Service Board of Governors needs to re-visit promptly this rate case.

By contrast, periodicals with less editorial content but high in advertising, with circulations in the millions, have felt the effects hardly at all. That should come as no surprise – it was certain leaders in the mass-market magazine industry who crafted the rate increase proposal ultimately adopted by the U.S. Postal Service Board of Governors.

Eagle Publishing spends nearly $2.5 million each year for postage and mailing. Overall, our postage costs have shot up by $211,000 this year, and the average company-wide increase for postage is nearly nine per cent as a result of the July jump in rates. While we are paying more, we are getting less. This is because the USPS expects mailers to do more preparatory work than ever before, and at times the concept of good customer service is completely alien to postal personnel. Chronic slow delivery of *Human Events* ultimately forced us to go to a "split print" from facilities on both the East Coast and West Coast. Unfortunately, while this arrangement has improved the timeliness of delivery, it is not amenable to co-mailing or other "efficiencies" the Postal Regulatory Commission incorporated in the rate case.

Human Events not only must cope with increased postal rates, it also must pay a USPS "container fee." Mass-market periodicals are able to be placed in large quantities on pallets but are charged a per-pallet, single-container fee no matter how many bundles or copies are on it. *Human Events* must go into standard canvas mail sacks because we do not have the volume to qualify for pallets, and as far as the USPS is concerned, each sack is a separate "container" subject to its own individual charge. Meanwhile, the USPS has offered no alternative to the canvas sacks, which it would prefer to discontinue. Any such alternative is subject to labor union approval before it can be adopted, a process which can be lengthy and sometimes contentious.

Maintaining profitability in the publishing industry has always been challenging. Meeting the new postal rate hikes is not being handled with money our company just has lying around, but through hard work to increase sales and more aggressive programs to raise advertising revenue. For small and medium-sized publishers, the postal rate increase is making an already difficult job even more so. In some cases, the increase is proving to be the straw that broke the camel's back. It is the death knell for some publishers, who are being driven out of business.

When established more than 200 years ago, the postal service was intended to be a means to bind the nation together. Its purpose was to improve communication, aid commerce, and allow news, ideas, opinion, learning, and culture to reach all Americans. It was and has been a key facilitator in the exercise of our First Amendment rights to free expression. For generations, small journals of opinion and culture mailed to subscribers have enriched the

lives of countless Americans and contributed substantially to our national identity and the body politic.

This hallowed legacy is on the verge of being crippled not by virtue of the ebb and flow of market forces, nor by consumers deciding for themselves what they wish to read or not read, but by the actions of a single government agency.

By imposing an unreasonable rate increase without analyzing adequately and thoroughly the potential consequences to small and medium-sized publishers, the Postal Regulatory Commission (with the concurrence of the Postal Service Board of Governors) will be responsible for wiping out Americans' access to various journals of opinion and culture.

The Postal Regulatory Commission will be responsible for diminishing the marketplace of ideas.

The Postal Regulatory Commission will be responsible for making the exercise of our First Amendment rights to free speech and expression more difficult.

If Congress fails to take notice of what is happening and what is at stake, and consequently fails to act, it, too, will deserve its fair share of responsibility for the deleterious impact of this rate increase.

Since the Postal Service is a monopoly protected by statute, publishers in financial distress thanks to the rate hikes have nowhere else to go. They have no alternative. Many have turned to the Internet, and Internet content by newspapers, magazines, journals and other periodicals is growing almost at light speed. In another example of the law of unintended consequences, the more the Postal Service balloons its rates, the more customers it either puts out of business or drives away to electronic media.

The U.S. Postal Service likes to refer to itself as a business employing business-like methods, but in fact, it is neither fish nor fowl. It's not a true, independent corporate entity but isn't an authentic government agency, either. Besides its statutory monopoly, it enjoys other special protections and privileges real businesses can only dream about. On the other hand, it is subject to Congressional oversight and sometimes Congressional micro-management, especially when attempting to close, consolidate, or merge unprofitable post offices and facilities.

The biggest single expense of the Postal Service is personnel: salaries and benefits, health insurance, and pensions. To avoid further rate increases, it is imperative that the Postal Service get these costs under control. The Postal service also needs to implement aggressively the changes and reforms contained in last year's landmark postal reform bill. In other words, the Postal Service simply cannot continue to pick its stakeholders' pockets through rate hike after rate hike, but must demonstrate that it is serious about change, improvements, and meaningful cost control.

Ultimately, the answers to these problems are two-fold:

1. **The Postal Service must be privatized.** As former Postmaster General William Henderson wrote in a *Washington Post* essay shortly after stepping down, the time is now for privatization. Suggestions on how to do this include selling it to its employees, making it a public stock company, or breaking it up into regional companies.

2. **Modify or repeal the Private Express Statute.** Users of most classes of mail services currently have nowhere else to turn. They deserve alternatives. And because the Postal Service has no competition in those areas, it has no incentive to be customer-friendly, efficient, or truly business-like in its operations. With competition –when our mailboxes are liberated at last – the result will be good for the Postal Service, good for entrepreneurs, and good for stakeholders.

As for the here-and-now, we urge the Congress to act promptly in order make it crystal clear to the Postal Regulatory Commission and the Board of Governors that it never intended any of its statutes on postal policies to be construed such that rate hikes can be imposed with the effect of stifling free expression, driving publishers out of business, and unfairly imposing onerous financial burdens on entities least able to afford them. We urge Congress to work with the Postal Service to re-visit the July rate increase before even more damage is done to the publishing industry.

Eagle Publishing 2007 Postal Increase Analysis

Product Description	Mail Class	Annual Mail Qty	Cost/piece pre-increase	Cost/piece post-increase	% Increase	Annual Cost Before Hike	Annual Cost After Hike	Annual Cost Increase
Hedge DM	presort standard letter	480,000	$0.2226	$0.2361	6.06%	$106,848.00	$113,328.0000	$6,480.00
Succesfful Investing DM	presort standard letter	600,000	$0.2205	$0.2330	5.67%	$132,300.00	$139,800.0000	$7,500.00
High Monthly Income DM	presort standard letter	640,000	$0.2205	$0.2330	5.67%	$141,120.00	$149,120.0000	$8,000.00
Forecast & Strategies DM	presort standard letter	750,000	$0.2205	$0.2347	6.44%	$165,375.00	$176,025.0000	$10,650.00
GSI DM	presort standard letter	200,000	$0.2204	$0.2330	5.72%	$44,080.00	$46,600.0000	$2,520.00
Human Events DM	presort standard letter	1,000,000	$0.2138	$0.2330	8.98%	$213,800.00	$233,000.0000	$19,200.00
CBC DM	presort standard letter	300,000	$0.2226	$0.2360	6.02%	$66,780.00	$70,800.0000	$4,020.00
Human Events - Courtesy Bills & Renewals	presort first class	1,398,000	$0.3267	$0.3600	10.19%	$456,726.60	$503,280.0000	$46,553.40
Successful Investing Courtesy Bills	presort first class	32,000	$0.3267	$0.3600	10.19%	$10,454.40	$11,520.0000	$1,065.60
Forecast & Strategies Courtesy Bills	presort first class	60,000	$0.3267	$0.3600	10.19%	$19,602.00	$21,600.0000	$1,998.00
CBC Bulletins	presort standard letter	1,300,000	$0.2303	$0.2470	7.25%	$299,390.00	$321,100.0000	$21,710.00
Human Events Issues	periodical flat	690,000	$0.2550	$0.2980	16.86%	$175,950.00	$205,620.0000	$29,670.00
Forecast & Strategies Issues	periodical letter	180,000	$0.2668	$0.2960	10.94%	$48,024.00	$53,280.0000	$5,256.00
Successful Investing Issues	periodical letter	96,000	$0.2668	$0.2960	10.94%	$25,612.80	$28,416.0000	$2,803.20
High Monthly Income Issues	first class letter	18,000	$0.3900	$0.4100	5.13%	$7,020.00	$7,380.0000	$360.00
Book Club and Human Events premiums	bound printed matter	288,000	$1.1500	$1.3000	13.04%	$331,200.00	$374,400.0000	$43,200.00
								$210,986.20

Mr. DAVIS OF ILLINOIS. Thank you very much.

We will go to Mr. Heath.

STATEMENT OF MAX HEATH

Mr. HEATH. Thank you, Mr. Chairman and members of the subcommittee. I am Max Heath, Chairman of the National Newspaper Association's Postal Committee since 1984, and am a senior rep on the Mailers Technical Advisory Committee at the Postal Service since 1989.

I would like to reassure the subcommittee that rumors of small papers' demise from Internet news is vastly exaggerate. Though our industry faces many challenges, the Internet thus far has shown little ability to provide truly local news and information, which are the trademarks of community newspapers. That is not to say that the 2,500 community newspapers which are mostly family owned and serving smaller communities across America have smooth sailing ahead. Our postal problems are real and troubling, and that is why your work here today is so important.

I will be speaking both about the in-county periodical subclass, which is highly pre-sorted and locally entered, and the outside county regular rate subclass which we use to mail to readers farther away.

You asked us, are newspapers being put out of business by the 2007 rate cases? The short answer is, not yet. But the rates hit us very hard and will affect our ability to cover the news because the only way to survive increases in the 20 to 30 percent range and more for lightweight titles is to cut costs or sharply increase subscription prices, which will cause a drop in subscribers for us and the U.S. Postal Service.

But the deeper answer is more complex than that. I have provided in our written testimony a sad farewell column by one of our most loyal members, half of a husband and wife team in Vandalia, MO. Gary Sosniecki lays out in poignant detail how hard it is to do this work in the 21st century. He lays a portion of his terminal exhaustion at the door of the Postal Service. It isn't just about steep rate hikes, it is worrisome service problems that cost us subscribers and cut the artery that keeps us alive.

I am going to quickly summarize the points that I made in our testimony.

First, NNA believes that the root of the recent steep increase in our in-county postage rates was flawed data, trouble capturing accurate data. The Postal Service has had trouble capturing accurate data on in-county mail, since it is such a small segment of the volume. In the past, the PRC applied pressure to improve the data or the Postal Service smoothed out bumps created by small data samples. That did not happen last year.

The Postal Service asked for a 20 to 30 percent increase, and the PRC gave the Postal Service a pass on the poor data. We are now stuck with the rate base that we believe is inaccurate.

Second, our regular rate periodicals mail was hit hard by the new container and bundle prices that were suggested by Time Warner and put into place by the Commission. NNA has fought since 1996 to keep the larger magazine publishers from de-averaging the periodicals class. We understand their goals. It enables them to

take advantage of the privileges that periodicals receive without bearing the cost of smaller mailers.

Regardless of the costing data that swayed the Commission, we believe it is bad policy to allow this degree of de-averaging in a mail class whose very purpose is to disseminate a wide range of information.

While most newspaper mail is local and extremely efficient, our longer-distance mail comes in small, diffuse volumes. The so-called price signals that were intended to force mailers into co-mailing and palletizing and other efficiencies are signals to which most small-volume newspapers are unable, by their very nature, to respond. So the signal to us is: go away, you are bothering us.

Finally, we are troubled by misunderstandings of the in-county prices community newspapers pay. We have heard more than once that our 20 to 30 percent increase has amounted to only a few cents, and that our mail price is about $0.10 a piece. Our mail is highly pre-sorted, more than three quarters of it carrier route mail, and almost all entered at the delivery office, and most of that walk sequence.

I would like to point out that our in-county mail is probably the first or second most efficient subclass within the Postal Service, the other one being enhanced carrier route standard mail, which our papers also heavily use to serve non-subscribers with advertising information.

We have many worries ahead. First, the new postal reform law has made our in-county subclass vulnerable to steep increases, despite the price cap. That is because the cap was set at the class level. We hope the Postal Service will observe the spirit of the law and keep our increases within the CPI levels.

Second, our service problems are agonizing. Delays to mail that must go through processing plants have increased. Even local mail has new service problems with the advent of the 24 piece container minimums in May 2006. But generally, since postal reclassification in 1996, and flats automation in 1998, outside county delivery has worsened both in time and consistency.

Finally, with the new flat sequencing system [FSS], coming next year, we have fears for our primary mail entered at delivery offices, and now given timely service. If we cannot keep local delivery unit entry for our periodicals and standard mail products, I fear it will really be the end of us. It has been heavily involved in consultation on the mailing standards for this new machine, but we must have the ability to drop our mail at the local office and keep the drop-ship and carrier route walk signals discount for doing so.

FSS is simply not going to be able to provide us workable deadlines with the assurance of same day or next day delivery of the mail often dropped from the press to the dock at midnight to be in the mail the following day. Without that assurance, Mr. Chairman, we are toast.

We have been trying for nearly 3 years to get the Postal Service to provide that we will keep our privileges, and we cannot get that assurance. We hope the committee might inquire on behalf of community newspapers on this topic.

To summarize then, the newspaper mail was hit hard. We are surviving it so far, but we fear it is the first of many such blows.

We think the increase was unfair and wrong headed and we vigorously oppose the de-averaging of periodicals and mail.

We need stable rates, better service, and we need to keep our local delivery unit entry in the FSS environment.

We appreciate your interest in our problems and would be happy to supply any other information that you need. Thank you.

[The prepared statement of Mr. Heath follows:]

National Newspaper Association
Washington Office
PO Box 5737
Arlington, VA 22205
703.465.8808
Fax: 703.812.4555
Web Site: www.nna.org

Testimony of Max Heath
Vice President, Circulation/Postal/Acquisitions
Landmark Community Newspapers, Inc.
And Chairman of the National Newspaper Association Postal Committee

Before

The Subcommittee on
The Federal Work Force, Postal Service and District of Columbia

October 30, 2007

Thank you, Mr. Chairman and members of the subcommittee, for the opportunity to comment on the situation facing periodicals in the mailstream.

My name is Max Heath. I am vice president of postal/acquisitions for Landmark Community Newspapers, Inc., Shelbyville, KY. Our company owns 7 nationwide periodical publications and 57 community newspapers, including the weekly Vandalia Leader-Union in your home state, Mr. Chairman. I am also the chairman of National Newspaper Association's Postal Committee and its senior industry representative on the Mailers Technical Advisory Committee.

I represent National Newspaper Association here today. NNA was founded in 1885 to represent community newspapers. It is presently headquartered in Columbia, MO, and maintains a government relations headquarters in Arlington, VA. NNA's membership comprises about 2,500 newspapers, of which most are weekly, twice-weekly or 3 times weekly newspapers. The typical circulations would be under 5,000 copies.

While we do not collect financial data from our members, I can tell you from personal observation that many of our privately-owned member papers have gross sales of less than $500,000 per year, and profits that are in the low to middle single-digits. These are not the newspapers of the 20-30% profit margins that you may have read about in the go-go days of the 1990s. Also, it is important to note that the Internet competition that has now cut into the larger newspapers' margins has affected community newspapers to a much smaller degree. Possibly because they are accustomed to operating on very thin

profit margins, these newspapers continue to be a critical link between readers, businesses, public officials and governmental bodies in their communities. It would be a mistake to assume that the encroachment of the Internet, therefore, is inevitable and that the mails will cease to be critical for the foreseeable future.

I should add, Mr. Chairman, that my own company is somewhat atypical of NNA membership. We are a bit larger in a corporate sense than most community newspaper companies, which are generally family-owned small businesses with one, two or three papers. Fortunately for me, and for NNA, my company (which is still family-owned) is large enough to permit me to actively engage in postal policy discussions at the national level—something few of our papers could do without NNA.

I appear here today to make three critical comments about newspapers' future in the mail.

First, the most recent rate increase has threatened the ability of most of our newspapers to reach readers, especially in distant areas. Increases in Outside-County mail ran from $3-5 up to $30-35 per subscriber per year, and percentages, while mostly in the 20-25% range, can hit as high as 30-40% for very light-weight papers—and of course those are the ones with the least advertising, and therefore the most vulnerable. Some publishers are attempting to pass some of that increase along in higher subscriber rates (which is never a good thing, but cannot be avoided here). In January (six months after we began paying the higher postage ourselves), we will institute increases for Outside-County subscriptions by the amounts listed above. We expect to lose many outside-area subscribers hit with cost increases that large. But for the postage expense, we would not have to drive up our own prices. We will lose subscribers, and USPS will lose this mail.

There are no winners, only losers, among small publications in this Periodicals rate case. High gasoline prices have sharply reduced spendable income, and subscription price increases for In-County mail are difficult to make without loss of subscribers. In most cases, our company is absorbing the cost of the 15-23% hike in In-County postage. But for those that can't, and must pass along $1-3 more in postage costs per subscriber per year, loss of volume is a real harm to their business.

Second, future aggressive increases will assuredly drive smaller newspapers out of business, and further reduce volume of other small publications in the mails, as subscriptions become less affordable. I am attaching here a poignant column from our friend Gary Sosniecki of Missouri, who testified before the PRC in the 2006 rate case about his fears of the impact of rising prices and poor service, lamenting that he and his wife are worn out, and are giving up. They have sold their paper to a larger company. Gary, who has personally wrestled the Postal Service for the past couple of years, cites the time drains and frustration from poor service as the single greatest factor in his decision.

This is a particularly sad development for NNA, because the Sosnieckis are people who regularly give up their Friday nights to personally cover the high school football games, and who will stay up all night making sure the voters' guide is completely correct

before going to press prior to an election. When newspapering loses people like this, we all lose, including the voters in Missouri.

Third, even without double-digit increases, the deteriorated service of recent years has severed the connection between many readers and their hometown newspaper, and we fear, for that reason, the coming of the new Flats Sequencing System machines, or FSS, which will force many community newspapers to lose carrier-route rates, haul mail to distant cities on backed-up deadlines for news and advertising, and live in fear the Postal Service will not be able to deliver on time. This mail, when removed from the delivery offices where most of our In-County mail is deposited and delivered efficiently now, and is the mail that drives our cash flows and lets us serve readers and advertisers, is in jeopardy of leaving USPS for private delivery. Its loss will be the nail that causes the shoe to be lost, as the proverb goes.

1. **The damage created by the 2007 increase was palpable and deeply felt.**

NNA appeared before the Postal Rate Commission (now the Postal Regulatory Commission) in 2006 to address the proposed periodicals rates. NNA has appeared since 1970 in virtually every rate or classification matter that even tangentially affects newspapers. There is ample reason for this tenacity, though every new litigation seemed to pose the possibility of such serious financial outlays for lawyers and economists that the existence of the association itself is called into question. Our newspapers rely upon the Postal Service as their primary circulation avenue. This has been true since the beginning of the Republic. As the Postmaster General will readily acknowledge, the first postmaster general, Benjamin Franklin, was a newspaper publisher.

Our primary mailing to readers is through the Within-County (or In-County) subclass of periodicals; for readers just outside our core areas, as well as those further away, we use Outside-County subclass; and for nonsubscribers, we are heavy users of high density Enhanced Carrier Route (the former third class) mail. Many weekly newspapers also provide saturation ECR mail coverage on another day of the week as a full-coverage option for advertisers. My company, for instance, spends over $4 million annually on Standard Mail and over $2 million for Periodicals mail, showing how widely used Standard Class is by community newspapers. Free newspapers and shoppers use Standard.

In rate cases, NNA focuses most heavily upon Within-County mail for two reasons. First, that is the core mailing rate for our in-market subscribers. Second, NNA is the only organization that consistently tends this important mailing rate. We have increasingly had to pay more attention to Outside-County rates, however, because of new problems with that mail.

In the 2006 case, we made several key points. Among them were these:

- The appearance that In-County mail was failing to cover USPS costs, we believe, may have been rooted in deep flaws with USPS cost measurements. To state the problem simply, the statistical samples taken are inadequate to be accurate.

- The proposals that our friends from Time-Warner had put forth for charges of bundles and containers were unfair to newspaper publishers. These proposals have been clothed in the misleading assumption that publishers have options to use different containers and to create higher density mail. That may be true for some large-volume magazines, but it is untrue for community newspapers. The so-called "price signals" sent by the PRC were simply not applicable to our business, so we are stuck with paying higher rates forever.

Quite frankly, if we were surprised by the 20-28% USPS rate proposals for In-County, we were devastated that the PRC trimmed the proposal only slightly, and failed to make any useful recommendations for repairing the statistical problems. We were doubly surprised by this because the PRC chairman had previously highlighted our problem in letters to Congress and to the Government Accountability Office.

And we were completely floored that the Commission swallowed the concept of Time-Warner's complex rates almost completely.

Why these two occurrences happened would be for the Commission to explain. However, we attributed the outcome to these elements:

- On the data quality, while the PRC knows there is a problem, no one seems quite sure what to do about it. NNA's proposals to average certain aspects of the data were found wanting and rejected.

- On the bundle and container rates, the PRC was tired of watching Periodicals rates struggle to cover costs. It recognized that the appearance of "subsidized" periodicals was an outflow of the Postal Service's inability to control mail processing costs (and in spite of expensive flat-sorting automation that may have inadvertently raised costs, rather than fulfilled its promise to reduce them). After nearly a decade of trying to hold down prices, it decided to make the mail fit the system instead of continuing to urge the system to handle the mail. So those of us that cannot adapt are considered dispensable, apparently.

- With the onset of the price cap, the fear that the problems in the rates would be frozen into the rate system forever made both USPS and the Commission bolder about taking big steps, regardless of the risks to the Periodicals mailstream.

- Finally, with respect to In-County, there seemed to be a whispering campaign that newspapers were paying only about 10 cents per delivery. In fact, in some cases that is true—but this particular mail is so highly presorted to the carrier route, walk-sequenced, and transported to delivery offices, that all USPS has to do is walk or drive down the street and drop off the copies. The price is roughly comparable to, or higher than, what private delivery systems with appropriate volumes need to cover their costs. It may sound low, but the price provided meets the service.

The result of the case was a range of double digit increases in postage. Our members report that In-County mail costs went up 15-20% and Outside-County mail as much as 25% in many cases, largely because of the container and bundle costs. The new "shape-based" rate concept and container charges led to higher percentage increases on the small, lighter-weight papers Outside-County, with revenues that make them least able to afford the sharp increase that has reached as high as 50-60%. One hit 61.6%, and had a $5 subscription price serving volunteer fire-fighters in multiple states.

In addition to the postage increase, many members had to invest in new software that would enable them to meet the new mail sorting requirements, such as providing counts of bundles at their various sortation levels and containers at their various sortation levels. This is not a mean feat, as other witnesses I'm sure will attest. Where periodicals previously had to measure their weight, advertising content, sortation and travel distance, now they must also take a variety of measurements of their bundles and sacks.

Although NNA has long encouraged all of its members to purchase PAVE-certified software so they can take advantage of the available discounts, we have also long realized that coming up with $2,000-$10,000 purchase costs for this software is not an easy task for the smallest papers. It has always been a worry to us that many felt they simply could not do it—and so they have prepared mail with a mélange of cheaper tools, ranging from index cards to Microsoft Access® or Filemaker Pro® software, and then filled out the required mailing forms by downloading blank forms from the Internet and hand-writing them.

With the 2007 rates, this expediency is just about impossible. The software must now be purchased, and staff trained to use it.

So for the smaller papers—let's use a 2,000 circulation country weekly as an example—that might have spent $15,000 last year to use periodicals mail, the 2007 bite was $3,000 more plus an additional $2,500 for the least expensive software. That could amount to increases of about 35% in a single year. I'm not even counting the business opportunities lost as staff have to be distracted from core duties while they are trained to handle the software.

Now the Postal Service might counter: the postage for In-County went up from maybe 9.5 cents to 11 cents. That is only a penny and a half. *Quit-cher-whining*. In fact, we have heard that informally from some officials. But I would say back: 35% is 35%. No business can sustain those types of increases in their key costs. It is as simple as that.

We have not seen the Postal Service's volume reports from this most recent quarter to see what real impact this has had. But we did look at the mailings for the 3rd fiscal quarter. In-County mail volumes fell 2.6%. This may have been from mailers trying to get out before the rates hit. Or it may have been from the usual problems in getting accurate data. We do not know.

The Committee asked us whether the increases were putting newspapers out of business.

So we tried to find out.

It should be said that NNA has no resources available for exhaustive surveys and studies. This limitation has been our Achilles heel in rate cases, because the economists nonetheless want to hold us to the same data quality requirements it creates for multi-million dollar corporations. But we do maintain regular contact with opinion leaders in the industry, including our boards and state chairmen, as well as those who actively participate in our Congressional outreach. Though they are busy publishers and beset by surveys of all sorts all the time, we can usually get at least some feedback when we ask them to help us.

So we asked: were you surprised by the amount of the increase? How much was it for you? Have you coped with it by cutting costs, increasing subscription rates, trimming profit margins or possibly going out of business or selling the paper to a larger company?

The responses were fairly consistent. Here is what we learned.

The increases were indeed a nasty surprise. Publishers knew from reading NNA's various publications that an increase was coming, but the magnitude of this one was in no one's budget.

So far, publishers seem to be handling it by cutting other costs and trimming already thin profit margins. With the Internet breathing down our necks, we are all fearful of the risk of trying to pass much of this cost onto customers, especially local ones In-County and adjoining counties. So, we are mostly making do with less. A few are considering leaving the mail and trying private delivery. Many are assuming their long distance subscribers are going to drop off as they raise those rates by $3-30 per year. A few papers offer their whole issue online, but most don't. Those readers will simply be gone.

Finally, when we asked what would happen if another increase of this magnitude in 2008 came our way?

And there we drew blood. Most said they would have to seriously consider either leaving the mail or getting rid of the newspaper somehow—selling or shutting down.

2. <u>What happens next.</u>

This concern leads me to my second point—one that carries some urgency for us.

I will precede this discussion by making it clear that NNA was a supporter of the decade-long postal reform effort that lead to the Postal Accountability and Enhancement Act (PAEA). We were not grudging supporters, but active lobbyists here with your committee and before the Senate. Though we knew the risks that might come from passage, and we were fully conscious that the devil is in the details, we also knew the Postal Service was going to need some help to survive the Internet onslaught. We put our trust in the bill sponsors, and both the Postal Service and the Commission.

The bill emerged with mostly good, and for us only two big evils. The first of those was the requirement for pre-funding retiree health benefits. We had hoped that the overpayment of postage that we funded through 2003 would be returned to mailers.

The other prong on the devil's fork for us was the decision to take the Senate version of the price cap, which sets the cap at the class level, rather than the subclass. We understand the Postal Service felt strongly that it needed that pricing flexibility.

But for In-County mail, this was a terrifying outcome, particularly since the Postal Service seems to think raising our rates 25% is ok so long as it is only a few pennies per piece.

You see, because In-County volumes are less than 10% of the total for the mailing class, the cap could miss our heads entirely. If the total cap were, say, 3% increase, USPS could trim that impact to 2% for the larger magazine class and hit us with a 25% increase again. Or it could make us pay the entire increase, and leave the Outside-County prices as they are. It has that flexibility and you, the Congress, gave it to them.

I am thought to be the incurable optimist in our industry about the Postal Service. I've worked with the institution for many years, and I know it to be run by sincere and well-intentioned public servants. I also have a real appreciation for the challenges they face in keeping the nation's most valued institution afloat with the decline of first-class mail we all face.

But I am very worried. I fear that at the top of the service—possibly among the governors even—the notion that a 25% increase isn't so bad so long as it only means a few pennies really doesn't count. I believe the Postal Service will be wiser than that. But then I believed it before the 2006 case, and they let me down.

So I say to this subcommittee, if we should find ourselves faced with another double-digit increase, you will most likely be losing many of the small newspapers that reach the communities that you represent. They will not be able to sustain this one.

3. **<u>If the rate monster doesn't get us, the service monster might.</u>**

It goes without saying that news isn't news when it arrives late.

Despite this age of 24/7 blogs and news feeds, our newspapers are still pretty much the sole source of a lot of information. That may be the school board news, the zoning hearing, the high school sports scores or the sidewalk SALE coupons—and believe me, when we are late with the discount coupons, we hear it from all sides.

We have had long-standing problems with reliable service over great distances. But now the outbreak has been reported within our core markets. Newspapers all over the country report serious problems with mail that has to move through a Sectional Center Facility, or an Area Distribution Center.

Our board member, Dave Berry of Bolivar, MO, explained this problem before the PRC last summer. He explained that he serves a lake resort area, and many of his readers subscribe to the paper so they can see it before they pack for the weekend. They are within a 1-2 day service area, according to existing USPS service standards. But

they simply do not get the paper in time. He spends a lot of his time answering complaints.

I can attest that all of us spend a great deal of time answering complaints. Besides my own publications at Landmark, I probably get a dozen requests a week for help with service problems.

To its credit, USPS provides me with access to senior operations people to troubleshoot these problems. We usually find a solution—sometimes it is a different mail preparation by the mailer, a change in routing, or sometimes a little pushing of the operational managers. But of course we get only the tip of the iceberg. Our survey indicated that problems are pervasive—both deep and wide.

I believe the primary cause is the work-hour cuts that USPS has passed along as part of its cost controls. It also may be a combination of other concerns. USPS, of course, always points first to the mailer's own failures—and sometimes that does happen. But it also is about the way newspapers are handled, the inability of USPS to know where mail is at any given time while it is in its facilities. I was recently shocked to learn that the daily mail condition reports, that plants have to submit to show what mail remains unworked, do not have to include mailings under 1,000 pieces. So it is easy to see how a small newspaper could lie around for several days. Unacceptable, but easy to understand.

We try to help our members learn how to sort their mail so it can travel on first-class ground transportation where possible—a fairly costless privilege that USPS created for us. They can sort mail in flats tubs instead of sacks, though they have to pay the container charge—and that sometimes helps. They can file an ePubWatch report, which NNA and others fought to keep off the budget cuts floor recently. Or they can do what more and more are doing: try to get that reader to read the newspaper online.

Now, the .pdf online, or the more common short summary version, is clearly a growing part of our futures. I suppose in time most of our long-distance subscribers will move in that direction if delivery remains poor and costs continue to skyrocket.

But hoping our core local readers—those that shop in our markets—will prefer the paper online is like Caesar wishing Brutus had a sharper knife.

We all have to figure out our relationship with the Internet. We are all working at it.

The fact remains right now, and for the foreseeable future, that no newspaper website can produce the revenue required to support a legitimate news-gathering operation. That is true from the top to the bottom of our industry, and even more true in rural areas, where nearly 40% of readers are on dial-up services or not online at all.

The equation from rising costs and poorer service does not add up to an electronic future. It adds up to no future at all for local news and information.

If we believe civic life, and important things like voter turnout, and parent/school partnerships, kids sports and a host of other important community values are threatened now, I invite you to contemplate it without the local newspaper. For myself, it is a future

that makes me hope for imminent retirement on a desert island, where I won't have to see what comes next.

Mr. Chairman, we are second to none in our belief in the importance of the Postal Service. We rely upon it, and we hope to continue to be able to do so. We appreciate the opportunity to explain our situation to you.

To answer your question: will the rate increases put newspapers out of business, then, let me respond simply. Not yet, thankfully, but it has weakened them. Without your continued vigilance and the support of the Postal Service and the Postal Regulatory Commission, the next time you ask the question, we may not be here to answer it.

-30-

THE VANDALIA LEADER
Queen of the Prairie — Vandalia's newspaper since 1874

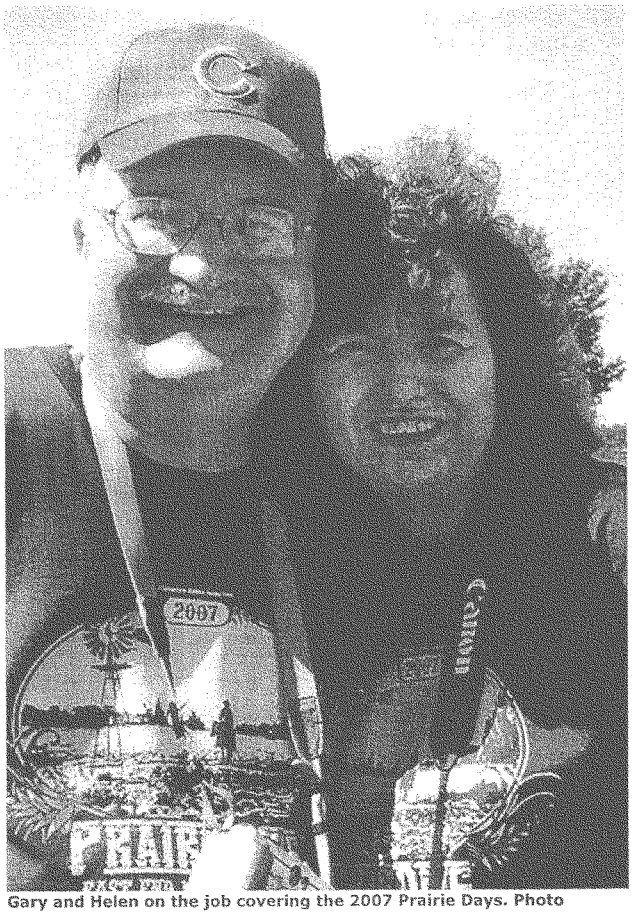
SOZ SEZ: 10 steps to a better Vandalia

SOZ SEZ: Sometimes, loving your job, town aren't enough

SOZ SOZ: Why we need dispatching here

'Soz Sez' columns named state's best

LEADER INTERN: 'Farm girl' felt at home here



Gary and Helen on the job covering the 2007 Prairie Days. Photo

GUEST COLUMN: Bye-bye, Lady Bird, from Bobby Moore

GUEST COLUMN: I'll take the rap for Paris Hilton

Sosniecki's editorial judged one of 12 best

SOZ SEZ: New Wal-Mart in Bowling Green means trouble ahead for Vandalia

SOZ SEZ: Two Vandalias, both smiling

MAYOR: WERDCC has been good for Vandalia

WERDCC SUPERINTENDENT: Employees 'show' us much on a daily basis

Former White House correspondent Bob Moore of Vandalia remembers 'nice guy' Jerry Ford

GUEST COLUMN: Playing post office for a day

GUEST COLUMN: Picking up Vandalia's trash is educational

GUEST COLUMN: Blame Bob for lack of weather

GUEST EDITORIAL: The original Curryville cop

SOZ SEZ: Taking your delivery

courtesy of Clarence and Doris Ray

SOZ SEZ: Sometimes, loving your job, town aren't enough

By Gary Sosniecki

Let's make this clear from the beginning:

I love my job.

I love The Vandalia Leader.

I love the people of Vandalia and Farber.

And, being childless, I especially love the kids of Van-Far.

But, sometimes, love isn't enough.

Sometimes, your body tells you that you aren't as young as you used to be, that, as you approach your 57th birthday, you're pushing your body too hard, that 90 hours a week on the job, week after week after week, is too much for it to handle no matter how much you love what you're doing or the community you're doing it for.

So Helen and I are going to take a break. A good, hard-working and honest family, nationally respected in the community-newspaper industry, is going to buy The Leader on Nov. 1, and it is going to build on what J. Linn Ladd, Frank and Lily Frost, Fred DeTienne, Pete and Lora Steiner and Gary and Helen Sosniecki have built before it.

Under the ownership of the Jack Fishman family, The Vandalia Leader will continue to grow and prosper and, most importantly, will continue to serve the people of Vandalia and Farber for generations to come.

Five-year plan became four

We hadn't expected to sell The Leader this soon.

We came to Vandalia in the summer of 2003 with a five-year plan, which meant we intended to publish The Leader at least five years before even talking about moving on to, as Helen likes to say, one last newspaper on a beach.

But in April we received a phone call from a nearby publisher who had heard a rumor that The Leader was for sale and, if it was, he was interested in buying it. We told him it wasn't that was the truth but we also told him that if he wanted to talk about it, we would be glad to listen. As I've heard many times, the only business that can't be bought for the right price has a fool for its owner.

complaints to the top

'Didn't you used to be Bob Moore?'

Check out our advertisers' Web sites, too

SOZ SEZ: President to co-publisher: 'Hello, Helen'

What Deep Throat didn't know about Watergate

An alumnus answers the question: 'What's a Van-Far?'

Rappin' Robert Holden and other great cartoons

We want to hear from you!

We never heard back from that publisher, but we thought about his call a lot in the months that followed.

It has not been the best of years for small-town weekly-newspaper editors. In March, Brian Mazza, editor of the Rocky Mountain House Mountaineer in Alberta, Canada, a friend of ours from the International Society of Weekly Newspaper Editors, died unexpectedly of coronary artery disease at age 45. He was found dead in his house after he didn't show up to take a photo on a Sunday.

Then in April, Steve Oldfield, publisher of The Adrian Journal and last year's Missouri Press Association president, suffered a massive stroke the day after his daughters wedding. Steve nearly died and faces a long recovery.

In May, Rusty Hartwell, 47-year-old publisher of The Holden Image died of an apparent heart attack.

Three months, three tragedies involving younger people who do the same work you do, two of them friends.

Then came June, the month when Helen and I normally recharge our batteries after a long school year and our biggest annual printing job, the Vandalia Area Fair book.

Both of our elderly mothers wound up in the hospital in June, mine from a fall that led to several weeks in rehab followed by three weeks of 24-hour home-health care, Helen's mom also from a fall, then a continuing series of ailments that have sent her to the emergency room several times in recent months and culminated in gallbladder surgery last Friday.

Being tied down to a seven-day-a-week job, we have dealt with our moms' health issues mostly long distance. Helen was able to get away twice to check on her mom, including Friday for her surgery, but I still haven't been able to check on my mom in Florida other than through daily phone calls.

On July 4, which has been our only full day off this year, we talked about our options. We had tried twice this year to hire more part-time help but didn't have much luck. (And I can't even remember the last time a high-school student even those who have gone on to college to study journalism-related fields asked for a job here.) And though The Leader has grown each year we've been here, we haven't grown enough to hire a full-time reporter, which would ease our workload more than anything else.

We decided to take a trip to Branson to see a show and to have coffee with Ed Anderson, a friend for about 15 years. Some of you who visit Branson a lot may remember Ed as the former publisher of Branson's Country Review magazine. We met him when we owned the Seymour

newspaper; he was dating a teacher from Seymour, and they took us to dinner and a show, where Ed introduced us to the very funny Jim Stafford.

Ed is a newspaper broker now. He advised us when we sold our Seymour newspaper almost nine years ago, and we sought his advice before we bought The Leader in 2003. Once again, we asked Ed for his opinion.

Ed thought the time was right for us to put The Leader on the market and look for a newspaper a little bigger, with more staff, so we didn't have to do so much of the work ourselves. Maybe near that beach Helen keeps talking about.

So we did, and that led us to the announcement on Page 1 today.

New owners not strangers to us

What about the new owners?

We know that they have been interested in The Leader a long time, that they were talking to the Steiners at the same time we were when the Steiners accepted our offer four years ago.

We first met Jack Fishman seven years ago at a National Newspaper Association convention he is a past NNA president and we've met him several times since, including when he dropped by The Leader office a couple of months ago while visiting some of his Missouri newspapers and also last month at the NNA convention in Norfolk, Va.

Jack is a native of Jackson, Tenn., and we have joked that the three of us -- Jack, Helen and myself -- all began our newspaper careers at The Jackson Sun.

Jack is an impressive man. It would take a full column to list all his professional accomplishments: he received NNA's highest honor in 2002, the James O. Amos Award and his community-service work at the local, state --he served many years on the Tennessee Board of Regents-- and national levels, and it probably would embarrass him to do so.

Jack can tell stories with the best of anyone who hangs around a Vandalia coffee shop. When he dropped by The Leader office, he told us about how a young local singer named Elvis Presley had trouble drawing a crowd when Jack was a student at what now is the University of Memphis.

When Jack was nominated for the NNA's Amos Award, Morristown Mayor John R. Johnson wrote: "Jack is one of those rare individuals who has a deep commitment to items of public interest and is willing to throw himself into the fray without regard to his own personal or financial reward."

ETSU connection

One of the many awards Jack has received came in 2001 when — pay attention now Van-Far basketball fans — he was named an honorary alumnus of East Tennessee State University, the same ETSU where Van-Far's Mike Smith plays basketball. Jack's sons, both of whom are involved in the family newspaper business, are ETSU grads. In fact, Jeff (ETSU Class of 1986) and I talked about Mike and Bucs basketball at the NNA convention last month.

Jack's management team in Missouri includes Walt Gilbert of Louisiana, a longtime weekly-newspaper publisher in northeast Missouri and a former newspaper owner himself. And how lucky Jack and Walt are to have hired someone with Vandalia ties, Ron Schott, to run The Leader.

Jack's company, Lakeway Publishers, has so many resources to help The Leader to continue to be successful in the years ahead. When one of The Leader's Macintosh computers acts up, Lakeway will have someone who can fix it rather than Gary or Helen having to drive to Quincy, Ill., to find a repairman. The newspaper business always has been challenging, but it especially has become challenging in the digital age. Mom-and-pop newspaper owners like Helen and me are forced to become experts in so many things, from computer software to the Internet to rapidly changing postal regulations, that it's tough to keep up. It will be great for The Leader to have a support network that it doesn't have now.

It also will be great for our advertisers to have Lakeway's resources at their disposal. Now, if Leader advertisers also want to reach the Bowling Green, Louisiana, Troy or Centralia markets, they'll be able to place their ad with the Leader staff and be done with it.

Please be patient

We ask you to be patient and understanding as Ron and the staff make the adjustments that always come with new ownership. Lakeway will do things differently than we do, just as we did things differently from the Steiners.

If you don't like what they do, don't tell us; we won't want to hear it. We support whatever they do to keep The Leader successful.

Please don't complain to them, either. Every new business owner deserves a honeymoon while new ideas are tested.

But if you like what they do, please tell them. Your compliments have done much to keep us going even when the hours got long.

Helen and I are proud of what we've done here the past 50 months. Thanks to new technology, you have been reading the best newspaper that Helen and I are capable of producing without any other full-time help. We're awfully proud of the newspapers we've produced here, though it's humbling, as Bill Steiner once told us, that the best-selling

newspaper of the year always is the one with the all-town garage-sale ads, not the one with some "great" news story that you've worked on for days.

We're proud that some of our editorials seemed to have impact in the community, such as our endorsement of the Van-Far school-bond issue, which passed by five votes in 2006 after failing badly the year before. We were successful in getting the school to stop spending $25,000 with Wal-Mart every year for gift cards to reward summer-school attendance; that money now stays at home. And we convinced 253 people to show up at a community meeting in an effort to save local 911 dispatching. Unfortunately, that battle appears lost, a real tragedy for Vandalia.

We're also terribly proud of our Web site, which has gained a national reputation among small newspapers for its profitability as well as its content. Just last week, I faxed information on how to set up a Web site like ours to three different newspapers that asked for it, one in New York and two in Missouri. I will miss publishing The Leader, of course, but I think I'll miss working on www.vandalialeader.com even more.

Unfortunately, our work at The Leader kept us from doing as much community service as we did in our other communities. Even so, I'm proud that the Vandalia Area History Book was my idea and that I suggested the publisher for it, I'm proud to have designed the "We are... Van-Far" logo worn on so many T-shirts and sweatshirts around town, and I'm proud of my behind-the-scenes work with Nancy Stafford and June Rackers in creating (and naming) "A Vandalia Hometown Christmas." I'm disappointed that our vision of a wonderful holiday evening in downtown Vandalia didn't survive.

But we have few other regrets. Vandalia, for the most part, has been good to us. People have been friendlier to me here than anywhere I've ever worked, and the business community has been very supportive with its advertising. I will miss so many people, especially all my friends on my Wednesday-morning "paper route." I'll miss critiquing "The Price Is Right" with the guys in the back room at 54 General Store in Farber, I'll miss my baseball discussions with Postmaster Chris Hull, Razor Hull, David Crow, Calvin Hull and whoever else happens to be hanging around the Farber Post Office, I'll miss my long, weekly chats about the perils of small business with Bill and Nancy Stafford in the office of The Rose, I'll miss the regular visits (and Lyndon Johnson stories) from "Ol' Bob" Moore and I'll especially miss pouring my second cup of coffee every morning at Vandalia Firestone after I've picked up the mail. I won't miss cleaning up after I spill that coffee opening up our back door with my hands full.

It's unlikely that we'll ever have more fun than we did when the Van-Far Indians won the state basketball championship in 2004. What a thrill that was. Never have we seen a community come together the way Vandalia and Farber did that wonderful winter and spring. We'll never forget those kids: Mike Smith, Garon Suddarth, Chad Reading, Tanner Fennewald, Joe Basinger, Chris Nation, Shane Brookshier, Chris Bahr,

Jeff Johnson, Tyler Hawkins, Richie Schlueter and Ryan Schuckenbrock. Most of those kids probably have forgotten Gary and Helen already, as kids are prone to do, but we sure hope that in 2029, when the 25th anniversary of that great team is celebrated, somebody will think about inviting us to the party.

We burn no bridges

Has life been perfect here? No. Besides working too much, we've had our share of ugly experiences, as you have in any job in any town. Nothing would be accomplished by mentioning them. We burn no bridges in leaving Vandalia.

(But I don't mind burning bridges with the U.S. Postal Service and the incompetence that permeates it above the level of our customer-friendly local post offices. If you want to point a finger at any single thing that has caused us to grow tired of publishing The Vandalia Leader, you can point to the four years of lousy service we have received in trying to mail newspapers to subscribers in towns near and far. We are tired of phone calls from angry subscribers asking, "Didn't you publish a newspaper this week?" *Of course* we published a newspaper. The post office just lost it again.)

But we're not leaving quite yet. Helen and I will publish the next two issues of The Leader — you'll have two more "Soz Sez" columns to read — and we may be around a little longer moving our stuff out of the office.

Vandalia will continue to be our home while we figure out what we're going to do next. First, we plan to take a few months off to sleep and travel. Weather permitting, we hope to play some golf. Ironically, we came to Vandalia planning to play golf and enjoy Mark Twain Lake. But the only time I've been to Vandalia Country Club is to take pictures of the Van-Far golf team. And we've been to Mark Twain Lake twice, once for a Sunday hike our first year here and once as guests of Bob and Sue Giltner, who, thankfully, once a year dragged us out of the office for some fun activity.

As we travel, we'll start looking for our next challenge. Maybe we'll own one last weekly newspaper before retirement with a little bigger staff than we've had here, maybe we'll manage a newspaper for someone else, which we've also done before, or maybe we'll do something different, like teach journalism or help small newspapers develop Web sites. Chances are, as Helen reminds me, it won't be far from a beach.

And chances are that it will be for fewer than 90 hours a week. Right now, a 60-hour work week would sound like a vacation.

"You'll find that we work hard and we're honest," I wrote in my first column in the Sept. 3, 2003, Leader, an issue that was only 10 pages.

We hope we've lived up to that billing.

Gary Sosniecki is co-publisher of The Vandalia Leader. Until Oct. 31, he may be reached at (573) 594-2222 or by e-mail at vandalialeader@vandaliamo.net. After Nov. 1, he may be reached at sozsez@aol.com.

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Mr. DAVIS OF ILLINOIS. Thank you very much, Mr. Heath.

We will go to Mr. Davison.

STATEMENT OF HAMILTON DAVISON

Mr. DAVISON. Mr. Chairman and distinguished members of the subcommittee, I am Hamilton Davison, the executive director of ACMA, the American Catalog Mailers Association.

Thank you for having me. I would like to address three topics, and I go into greater detail in my written testimony.

First, catalog mail is valuable. Second, the rate increase had a serious impact on our industry. Third, we have some concrete suggestions that we feel the Postal Service can work with us on this crisis to their own financial self-interest.

Catalogs play a critical role in both the economy and in the U.S. mail. Half of all consumers buy through catalogs. There are some 20,000 catalog companies nationwide. In recent years, our industry has been vibrant and growing.

Rather than be pushed out by Internet commerce, we have thrived online. Studies show that some 80 percent of all online orders have a catalog somewhere along involved in the process. Whether through the mail or online, we deliver revenues of $270 billion a year, or roughly $1 million every 2 minutes.

All of that catalog-driven commerce benefits the U.S. mail. In addition to invoices and letters to customers and shipment advisories and tons of parcels, catalog mailers send between 20 and 30 billion catalogs a year. I would note that we have always covered our attributable costs and we paid billions of dollars in institutional costs.

Catalog companies are not occasional mailers. They mail every day of every year and spend billions in postage annually.

And catalogs have a strong multiplier effect that provides recurring revenue to the Postal Service. Each time a catalog prospect becomes an ordering customer, it generates 30 to 40 new pieces of mail in the form of future catalogs, invoices, and packages. But more importantly, catalogs help keep the mail relevant, because people like catalogs.

Postal Service surveys show that, unlike some kinds of mail, people look forward to receiving catalogs. They read, save, and order from them. They like catalogs for the same reason they like magazines: they offer products and ideas and information about their specific interests.

How has the rate increase affected our industry? It has been brutal. We expected 9 to 12 percent increases; we got 20 to 40 percent increases. Postage represents one of the largest cost centers for our members. This put enormous pressure on the entire catalog industry. Nor can we turn on a dime, given our carefully calibrated and integrated marketing plans.

So, as a result, nearly all of our members have been forced to make some hard decisions. Some are looking at layoffs. Some are limiting future hires. Others are actively reducing their reliance on mail. And, of course, some, in fact, many, are cutting circulation. But the response that should alarm the Postal Service most is that catalogers are cutting prospect mailings. Prospect mailings are a vital source of new business and a key to the industry's future

growth. When a potential customer responds to a prospect catalog, the Postal Service gets dozens of new pieces of mail as a result, so cutting prospect mailing today limits the Postal Service's revenues tomorrow.

Let me offer some ways that the Postal Service, using its new authority to set rates, can work with us to grow both of our businesses and ensure that the mail remains a vibrant channel of communication.

First, the Postal Service should price catalogs separately. Catalog mail represents a unique product different from other forms of standard mail. We have a different business model, and we make different mailing decisions. In addition, we add value to the mail stream.

Second, the Postal Service should work with our industry to adopt creative pricing arrangements, including pricing to encourage prospect mailing.

Third, the Postal Service should ensure that negotiated service agreements are accessible not only to the largest mailers, but also to smaller and medium-sized mailers or catalogers that were particularly hard hit in this last increase.

Fourth, we would like, as an association collectively and individually as companies, to work directly with the Postal Service on the operational and pricing details of its new FSS equipment and how declining flats volumes might affect the FSS roll-out.

I believe we can make a strong business case that growing catalog volume is in the short- and long-term best interest of the entire mail stream and the Postal Service.

That concludes my testimony. Thank you.

[The prepared statement of Mr. Davison follows:]

Testimony of Hamilton Davison
Executive Director of the
American Catalog Mailers Association

Before the Subcommittee on Federal Workforce,
Postal Service, and the District of Columbia
October 30, 2007

Good morning, Chairman Davis and distinguished members of the Subcommittee. My name is Hamilton Davison, and I am the Executive Director of the American Catalog Mailers Association, or ACMA. Thank you for inviting ACMA to testify today.

I would like to address three topics:

1. Why catalog mail is unique, valuable, and critical to the U.S. economy and, in particular, to the future of the Postal Service.

2. How the unexpectedly large postage increases—on the order of 20 to 40%—will harm the catalog industry and the Postal Service if no remedial steps are taken.

3. Why the Postal Service's ability to respond to its customers in a business-like manner is essential to both the survival of the catalog industry and the commercial success of the Postal Service. In this respect, I will suggest specific steps the Postal Service should take to respond to the crisis in our industry created by the recent postage increases.

I. Catalogs are Critical to the U.S. Economy and the Postal Service.

A. Catalog Companies Play a Key Role in U.S. Commerce.

ACMA represents a growing list of the estimated 20,000 business-to-business and business-to-consumer catalogers nation-wide, from household names like Crate & Barrel to smaller companies unrecognized outside of their niche markets. Catalogs

have a deep and wide reach into the U.S. economy. An estimated 49% of consumers buy from catalogs. (*Source:* MediaMark 2006.) Virtually every major catalog company today has a significant web presence to provide details of its products and accept online orders. The combination of catalog and online sales drive revenues of more than $270 billion a year—or roughly a million dollars every two minutes.

Catalogers boost the U.S. economy in a number of other ways as well. Directly and indirectly, we employ an estimated three million Americans in relatively high paying white collar and blue collar jobs. We pay hundreds of millions of dollars in state, local, and federal taxes. We also provide a way for smaller, mom-and-pop companies to connect with consumers in a market increasingly dominated by large, consolidated retail stores.

Despite the growth of online business, the mailed catalog remains the primary driver for new customers and product sales. In fact, studies show that catalogs play a role in 80% of online sales. (*Source:* Interactiveretail.com.) Moreover, even those companies that derive most of their sales from other channels still view the catalog as a vital communications tool. As a result, the U.S. Mail remains critically important to catalog companies.

Unfortunately, the Postal Service is only now beginning to realize the potential contribution catalogs make to its long-term success. For example, the Postal Service does not yet calculate catalog-specific demand elasticities (i.e., how much an increase in postage price will affect catalog volumes), nor does it track the total number of catalogs mailed, even though industry estimates put the annual number of catalogs at 20-30 billion pieces—which means that catalogs constitute a significant percentage of the Postal Service's total business.

B. Catalogs Add Value to the Mail as a Form of Communication.

In addition to billions of dollars in revenue and contribution derived from postage, catalogs make the entire mail stream a more viable distribution channel because ***people like catalogs***. A glance in any mailbox will show that advertisements make up more and more of today's mail, but unlike other advertising mail that is often pitched unopened, consumers welcome catalogs. Postal Service surveys show that people look forward to receiving catalogs; they read, save, and order from them. People like catalogs for the same reasons they like magazines: they offer products, ideas, and information relevant to their specific interests like home decorating, fly fishing, camping, cooking, or other activities. Moreover, catalogers do their best to send their relatively costly mail pieces only to those who enjoy a specific hobby or need their products. For businesses, catalogs offer essential products that cannot be bought at a

retail store, such as workplace safety equipment or employee training materials. In short, catalogs help keep the mail relevant.

For these reasons, internet commerce has not sounded a death knell for catalogs. To the contrary, synergies between the two have grown. Even for those who have internet access, catalogs offer something the internet cannot: an exciting, hard copy presentation to thumb through and products to plan for and dream about. For those in isolated areas without specialty retail stores or high-speed internet access, catalogs open the door to almost any kind of product one may need: from swimsuits to swimming pools, linguini to lingerie. This service is particularly important for the millions of Americans who, on account of advanced age or disability, cannot easily drive or walk through enormous retail stores or shopping malls.

Catalog companies are not "occasional mailers." They mail *every* month *every* year and spend billions in postage annually as a result. Catalogs also have a "multiplier effect" that provides recurring revenue for the Postal Service. Every time a catalog company receives a response to a prospect catalog, it generates 30 to 40 new pieces of mail in the form of future catalogs, invoices, and packages. Thus, if the Postal Service wants to increase its volume, it needs look no further than the catalog industry. For its part, the catalog industry remains intimately tied to the Postal Service because postage makes up so much of its overall marketing costs. A better partnership between the Postal Service and catalogers will only benefit both.

II. The Unexpectedly Large Postage Increases Have Hurt the Catalog Industry and its Potential for Growth, and Will Harm the Postal Service Unless Immediate Action is Taken.

How has the R2006-1 rate increase affected our industry? I wish I could say that the catalog industry has simply taken the rate hike in stride and moved on, but I cannot. To the contrary, the unexpectedly large 20-40% increases (in contrast to the 9-12% increases widely expected) hit us hard. Catalogers are particularly sensitive to such rate increases for several reasons:

- Postage makes up from 8% to over 20% of overall costs, the largest component aside from the cost of the product itself. Any increase in postage—particularly a large and unexpected increase—is keenly felt.
- The catalog business is a comparatively high volume, low profit undertaking. A well-run catalog company typically has a 5% profit margin. But if you take such a company and apply a 35% increase to a cost center that represents 8% of sales (and for catalogers postage generally represents 8% or more), it will

reduce that 5% profit company to a 2% profit company, and the business can no longer fund growth. If it has any bank debt or outside investment at all, it may not be able to earn its cost of capital, and over time will cease to exist.

- Of necessity, catalogers face long planning cycles. A successful catalog business requires careful planning and experimentation. We test and carefully measure everything extensively—different covers, sizes, and layouts, different sources for prospects, different offers—and we tweak that formula gradually over time based on success. Catalogers are also locked into long-term print and paper contracts and make forward commitments to merchandise and build inventories to be able to ship orders promptly.

These industry characteristics make it hard to "turn on a dime" and respond to unexpected—and unexpectedly large—rate increases. At ACMA, we have interviewed many catalogers who have seen much of their profit and cash flow for this year wiped out overnight by the postage rate increase. As you might expect, this has caused many catalogers to rethink not only their marketing plans but also their entire business plan. Such heavy reliance on the vagaries of postage rates now seems a major vulnerability to their business.

How have our members responded to the rate increases in the short term? Some are actively pursuing substitutes to mail to reduce their reliance on mail, which ultimately hurts the Postal Service. Once a company leaves the mail stream and makes the investment necessary to support other advertising channels, it will be much harder to get them back.

Others are reducing the volume of catalogs they mail. As the cost of a mailing increases, the number of customers who generate enough business to justify a catalog decreases, forcing the cataloger to trim circulation.[1]

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[1] Catalogers have also tried to mitigate the effects of the rate increases by changing their mailing practices. Nevertheless, most of our members cannot, for example, easily fold a catalog in half—turning it into a letter—because their catalogs are often far too thick. But even if they could, doing so would likely devastate the response rate. Covers of catalogs—the most carefully designed part of all—play a key role in converting prospects to customers and inducing regular customers to open the catalog, browse through it, and place an order. Repeat customers have also come to expect a particular look and feel. Mail pieces define a brand, and simply changing formats—without extensive testing and validation—poses a huge risk. Similarly, co-mailing, whereby mailers group their mail together to qualify for a lower postage rate, does not offer a practical solution for most of us. First, printers must get a return on their investment on expensive co-mailing equipment and take a not insignificant portion of potential savings. Second, most printers currently lack the capacity required and, in any event, often give

The response that should alarm the Postal Service most is that catalogers are deciding to ***cut prospect mailings—a vital source for new business and the key to the industry's continued growth.*** In prospect mailings, a cataloger sends handpicked consumers a sample catalog. As I mentioned earlier, every successful conversion of a "prospect" to an active "customer" results in several dozen additional pieces of mail per year for two to three years. Through prospecting, catalog companies expand their list of customers. But prospecting can be a risky and expensive proposition, and postage remains the biggest component of this expense.

Cuts in prospect mailings should concern the Postal Service because, if the trend is not reversed, it will be hard to check a downward spiral in volumes.[2] A vibrant, thriving catalog industry offers huge benefits for the Postal Service, not only by increasing mail volumes but also by keeping mail a relevant and welcome form of communication. This past year's drastic rate increases endanger the goose that laid the golden egg, and we would like to work with the Postal Service to reverse that trend.

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preference to magazines. Lastly, co-mailing requires a cataloger to time production with other catalogers—something that sounds fine in theory, but proves extremely difficult in practice.

[2] Consider the real-life effects of the R2006-1 rate increase on one of our members: Positive Promotions, headquartered in Hauppauge, NY. The company sells ribbons, certificates, lapel pins, bookmarks, coloring books, pencils, pens, and other products that educate and inform people on public interest topics ranging from breast cancer and drug abuse to fire safety and Black History month. Its customers are schools, non-profit organizations, fire departments, and small businesses. Companies like Positive Promotions reflect the face of America. They are a union shop, and employ nearly 600 people, including a wide range of white collar and blue collar workers, like graphic designers, photographers, writers, layout experts, database managers, IT staff, accountants, buyers, sales and customer service representatives, managers, and factory and warehouse workers of all kinds. Over half of their employees are minorities. Others are immigrants, and they offer an ESL (English as a Second Language) class on the factory floor.

Like most catalogers, Positive Promotions expected postal rates to increase in the R2006-1 rate case. They expected, however, a worst-case increase of about 9%. As a result, the company was stunned to discover that its annual postage costs would increase by 35%--nearly four times more than their worst-case scenario. That translates into a $2.2 million hit—a huge hit for a company that size—and one that they anticipate will cut pre-tax profits by 40%. Positive Promotion has seen postage take a large bite out of cash flow they need to fund growth. Growing companies need additional working capital to fund inventory expansion, additional accounts receivable, additional mailings (catalogs and postage), and other expenses.

Positive Promotions operates on tight margins, which means that it has to make up the postage increase money somewhere else: by cutting staff, cutting capital investment, and/or cutting circulation. Beyond that, the unexpected rate increase puts the company on an entirely different trajectory, changing it—almost overnight—from a vibrant, growing company into one forced to tread water. Put differently, it means that, in the future, the company may not be able to do prospect mailings to generate new

III. Setting Catalog Rates in a More Business-Like Manner Will Help Both the Catalog Industry and the Postal Service Succeed.

We believe that the new Postal Accountability and Enhancement Act (the "PAEA") provides the Postal Service with the tools it needs to address the crisis in the catalog industry created by the R2006-1 rate increases. We support the Postal Regulatory Commission's proposed regulations that implement the PAEA and give the Postal Service greater flexibility to set prices in a businesslike manner. And we applaud Chairman Dan Blair's leadership in getting the first set of regulations out well ahead of schedule. With the ability to consider not just costs but market characteristics as well, the Postal Service can now respond quickly to shore up the catalog industry, a move that would benefit the Postal Service itself in both the short term and the long term. We have a shared goal with the Postal Service: to ensure that mail remains an important and vibrant channel of communication for many years to come.

The Postal Service can use its new authority to help our industry in the following ways:

1. First and foremost, we want the Postal Service to get to know us as an industry and as individual customers. In the past, the Postal Service may have thought of us as just another mailer of Standard Mail flats, but we are a unique industry and an eager customer. ACMA was created to provide an identity and voice for catalogers separate from other mailers. The Postal Service has thus far welcomed our contribution.

2. Catalog mail represents a unique product, different from other forms of Standard Mail. We have a different business model and a different approach to mailing decisions. Catalogs benefit other forms of Standard Mail and the entire mail stream by adding value and keeping mail relevant and interesting. As a result, catalog mail should be priced differently.

3. Creative pricing arrangements are essential during this crisis period and for the future of the industry. In particular, we need to explore together innovative rates to encourage prospect mailings. Given their high multiplier effects, prospect mailings can translate into significantly more mail pieces—and therefore significantly more revenue—for the Postal Service.

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business, to increase circulation, to hire new employees, or to provide new or greater benefits to existing ones.

4. Many of our members want to pursue Negotiated Service Agreements (or "NSAs") with the Postal Service. Volume incentive discounts not only encourage catalogers to send more mail, they also offer the Postal Service an opportunity to get to know us and our business needs better. But many of our smaller members—the very companies hit hardest by the rate increase—may be considered "too small" to justify the significant commitment of time that it takes for Postal Service executives to complete an NSA negotiation. The Postal Regulatory Commission has done its part to streamline the regulatory approval process, but we need the Postal Service to respond with an NSA program that is accessible to mailers of all sizes.

5. We also need the Postal Service to work with catalogers directly in regard to both the operational and pricing details of its new Flats Sequencing System (FSS) machines. Already reeling from the postage increases, our industry faces additional disruption as the Postal Service rolls out FSS over the next few years, and we want to be prepared for it and have a say in the decision making process. ACMA has recently been invited to participate in the Mailers Technical Advisory Committee (MTAC), and we look forward to participating in that group.

Chairman Davis and members of the Subcommittee: We greatly appreciate the role that Congressional oversight plays in safeguarding our national postal system and in supporting U.S. industry. The recent PAEA, which you were so instrumental in passing, provides the Postal Service with critical new tools to move forward in a more business-like manner. We realize that Congress is not in a position to address many of the specific issues we have raised today, but there is one thing you can do: Since no innovation takes place without support from the top, we urge you to endorse the Postal Service to embrace innovation and rational experimentation in its efforts to become a more business-like entity.

In this new world of the PAEA, we will do our part to work with the Postal Service to craft creative solutions and to make the best business case why encouraging catalog mail is in the best interests of the Postal Service itself.

Again, thank you for the opportunity to testify this morning, and thank you for taking the time to understand these issues that are so crucial to our industry and to the future of the Postal Service.

Mr. DAVIS OF ILLINOIS. Thank you very much, Mr. Davison.

We will go to Mr. Straus.

STATEMENT OF DAVID R. STRAUS

Mr. STRAUS. Thank you. As a 37 year veteran of postal wars, I am here representing American Business Media, whose members produce about 2,000 high-quality business-to-business publications a year and spend about $400 million a year on periodicals postage.

I am going to have to divert from what I was proposing to say today because there is so much confusion that was left, I believe, on the record this morning about the relationship between the requirement that the periodicals class cover its attributable costs and the 20 and 30 and even 40 percent rate increases that some of our members have experienced.

The problem has nothing to do with attributable cost coverage for the class. The Postal Service proposed rates in this case would have had an average increase of about 12 percent on periodicals, and periodicals would have covered attributable costs. The Postal Regulatory Commission's recommendation produced exactly the same dollars, the same cost coverage, but it chose to broaden the band of increases and decreases such that, instead of having no increases very much smaller than or larger than the average, there were some decreases and some increases in 30 to 40 percent. Again, it has nothing to do with the requirement that the class cover attributable cost; it has only to do with how the Postal Regulatory Commission decided it would be best to accumulate those dollars.

American Business Media, in fact, supported the Postal Service's proposal in R2006–1. The Postal Service opposed the Postal Regulatory Commission's approach because it opposed the Time Warner proposal. American Business Media urged the Governors of the Postal Service to ask the Regulatory Commission to reconsider its decision that was opposed by most parties in the case, and it didn't do so, so our grip was with the Regulatory Commission for recommending those rates, and with the Postal Service for accepting that recommendation without question.

Now, American Business Media member publications average about 65,000 circulation. Some of them are a lot smaller, some of them are somewhat bigger, but rarely do they exceed 100,000 copies. Compare that with the mass consumer publications like Time, Newsweek, Sports Illustrated, and the like, with multi-million circulations.

Because of this difference, American Business Media, for its 100 year existence, has basically taken to position that it is there to represent the little guy, but I recognize, as Mr. Sarbanes suggested this morning, that this case is over. The rates have been implemented. There is no more judicial review. As he said, this sounds like a done deal, and I feel a little bit like Vice Admiral Stockdale at the 1992 Vice Presidential Debates where he famously asked, "What am I doing here?"

I ask myself that. What am I doing here? Why am I testifying in this hearing? I guess the reason that I am is that if the 11.4 percent increase for periodicals had been spread relatively equally across the class, I wouldn't be here and you wouldn't be here. The

problem was that it wasn't spread equally across the class, and somebody has to let the Postal Service and the Postal Regulatory Commission know and let Congress know that it has an oversight obligation not to let this happen again, certainly not to let it happen again, but also to take a look at the rates the next time they are changed to see whether something could be done.

The rates that are in effect now are not going to be in effect as of June of next year, it looks like, so there is really nothing that can be done about these rates. It is the next rates we are concerned with.

Where the Postal Regulatory Commission went wrong in this case is it looked at periodicals as a test tube for experimenting with price signals, with efficient component pricing, with matching precisely cost with rates. Interesting, periodicals are a content-based class, yet the Regulatory Commission decided it should be the most cost-based rate. Catalogs did get hit hard, but catalogs don't have bundle charges and pallet charges and sack charges. Only periodicals, the content-based class, has to pay rates that are strictly based on cost. That wasn't necessary. It didn't have to happen that way.

We heard today that periodicals haven't even covered attributable costs. From the perspective of periodical mailers I guess that is a good thing, but it is not going to continue indefinitely.

The point is that periodicals as a class get a subsidy. They pay no institutional cost. All other mailers pay the institutional costs that periodicals might otherwise be responsible for. That is, in a sense, a subsidy paid by other mailers into the periodicals class.

The problem that Time Warner identified and that the Commission bought was that Time Warner's subsidy isn't as big as it ought to be because small circulation publications, journals of opinion, get a little bit bigger subsidy to keep them in existence. So it is not that the big guys are subsidizing the little guys; it is that the subsidy provided by the first class mailers and the standard mailers goes more to some periodicals and less to other periodicals. That is the issue, and that is what the Postal Rate Commission decided it would not allow to continue.

If you don't believe that, ask Time Warner what its periodicals would pay if they paid catalog rates, and you will see that if they paid catalog rates those rates would be much higher than they pay today, than they paid last year under the old rates, because they were enjoying a subsidy. They just wanted more of that subsidy.

This desire of the Regulatory Commission to closely match cost and revenues is something that even Time Warner has admitted can be very harmful.

In the rulemaking that was just concluded by the Regulatory Commission, Time Warner was in opposition to a proposal to bring together costs and revenues, not when the big subsidy for all periodicals was put in jeopardy. This is its word. It called totalitarian any proposal that "subordinates every other possible consideration to a single, narrow principle." That dastardly principle was that cost and revenues must converge. In fact, in Time Warner's own words, the rate increases that would result from that principle might result in "driving some thousands of magazines out of the mails and out of business." To that we can say, exactly.

The PRC guessed that this wouldn't happen because people would co-mail. I won't go into the detail, but in our written statement we explain why co-mailing simply isn't available for most of the small circulation publications, for weeklies, for tabloids, and for others.

In conclusion, I would like to say that ABM has not opposed changes in rate design. We have been accused of being the Ludites of the periodicals class. It isn't true. We have supported pallet discounts, bar code discounts, pre-sort discounts, drop ship discounts. What we don't support is discounts that are not imposed in an incremental fashion but are imposed all at once to the detriment of small circulation periodicals.

We have already seen publications closing their doors or trying to survive by going digital, and more will soon follow.

Thank you.

[The prepared statement of Mr. Straus follows:]

PREPARED STATEMENT OF
DAVID R. STRAUS
ON BEHALF OF AMERICAN BUSINESS MEDIA
BEFORE THE
FFEDERAL WORKFORCE, POSTAL SERVICE AND DISTRICT OF COLUMBIA
SUBCOMMITTEE OF THE
HOUSE COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM
110TH CONGRESS, 1ST SESSION
(October 30, 2007)

American Business Media celebrated its 100th anniversary in 2006, and for most of those 100 years American Business Media has been an active participant in postal matters on behalf of its business-to-business media members. The reason for this participation is obvious: collectively they spend roughly $400,000,000 annually on postage. American Business Media has assumed leadership roles in the creation of both the Kappell Commission and the President's Commission on the United States Postal Service, which led, respectively, to the passage in 1970 of the Postal Reorganization Act and in 2006 of the Postal Accountability and Enhancement Act. Throughout its existence, American Business Media has fought in Congress and before the Postal Rate Commission to ensure continuation of the privileges and protections provided by law and custom to Second Class/Periodicals mailers.

Although as Washington Counsel for American Business Media and someone who has been involved professionally with postal rates since 1970, I appreciate the opportunity to testify before this Subcommittee, testifying here today is a lot like trying to explain how to close the barn door after the horse is long gone. The rates for Periodicals were raised an average of 11.4% on July 15, after a fully litigated case before the Postal Regulatory Commission. If that large average increase had been relatively flat among the many types of Periodicals, the impact would have been bad enough. But as you probably know by now, there was a very wide range of results around that average. In fact, as I understand it, the existence of staggeringly high increases on some mailers is the reason for the hearing today.

Due to the complexity of the new, allegedly cost-based Periodicals rates—by far the most indecipherable rate schedule for the one class of mail that's supposed to be based on content, not cost—most American Business Media members still have not been able to determine exactly how large their increases have been, although some have reported postal cost hikes of more than 20% and even more than 30%. American Business Media opposed the so-called "rate grid" approach to determining postal rates for Periodicals during the proceeding before the Postal Regulatory Commission, predicting that, even as moderated by the PRC, it would create severe hardships for many publications already reeling from the loss of advertising revenue. American Business Media also argued, accurately but to no avail, that the changes in "behavior" that would supposedly result from the "price signals" in the new rates would be more limited than forecast, because the printing industry simply does not now and will not soon, if ever, be able to co-mail the thousands of Periodicals that, in theory, could be protected from the worst of the increases by co-mailing.

Yet, as I stated earlier, it seems that there is little that can be done at this point to reverse the new rate structure that has emerged from Docket No. R2006-1. After all, that rate case, which inflicted this damage, is over, and at this time it is uncertain, at least mailers are uncertain, whether there will ever be another litigated rate case. The Postal Accountability and Enhancement Act of 2006 (PAEA) profoundly changed the way that postal rates will be set in the future, with the possibility of one vestigial rate case under the superseded law should the Postal Service choose to ignore the pleas from Congress, the PRC and mailers that it close the books on the ten-months-of-horror approach to rate setting.

The PAEA, which gave the Postal Service a great deal of additional ratemaking autonomy, was Congress's second venture into fundamental postal reform. The first, in 1970, shifted rate setting from the legislative branch to a combination of the Postal Rate Commission and Postal Service. Unless Congress is willing to insert itself again into the ratemaking process and somehow reverse the decision reached in the latest case, it seems that American Business Media members have little recourse but to try

and absorb these high postal costs (or in some cases to avoid them by shutting down publication). Indeed, I should point out that the rates proposed by the Postal Service in the most recent case were reluctantly supported by American Business Media. It was the Postal Regulatory Commission that decided to substitute economic theory, price signals, matrices and formulae for common sense. Our primary concern with the Postal Service is that, having the opportunity to seek reconsideration of the PRC decision on these rates, as it had on others, it failed to do so.

Yet, if nothing else, this hearing is an opportunity to remind Congress, and along with it the Postal Service and the PRC, that the Postal Service is indeed a service provided to the American people by our government. It is not and I hope never will be either a private service or a service that prices its products as would a for-profit, private-sector company. While it's easy—too easy, apparently, based on the outcome of this case—to get wrapped up in the fine-tuning of cost segments, efficient component pricing, price signals and economic efficiency, such myopia is not what the American people deserve. How else can one explain the unchallenged propriety of a postage charge of 41 cents to send a letter from Washington, D.C., either to Alexandria, Virginia or to Chugach, Alaska? How else can one explain why it's fair to other mailers that Periodicals as a whole receive a substantial rate break not at all justified by cost differentials but nevertheless appropriate because of their "educational, cultural and scientific, informational" value? Yet, why do the proponents of the great rate disparities created by the new rates find it perfectly acceptable to benefit from non-cost factors vis-à-vis, say, catalogs when the relative rate burdens between classes are being assessed, but bemoan any remnants of non-cost factors once safely inside the Periodical class?

What the PRC lost sight of in its desire to assure that every type of publication pays "its" costs is that there is no requirement that the reduced rate for Periodicals be spread evenly over the entire class. Even under the rates complained of by the mass-circulation magazines, they paid far less than they would have if mailed at the unsubsidized, Standard rate that would apply to a catalog that looked exactly like the

Periodical and that obtained worse service. The PRC should not have so readily cast aside 200 years of history in which the Periodicals "benefit" was applied in a way that assured a Periodicals class rich with diversity of both circulation size and content and that did not overburden smaller-circulation Periodicals with rates that make it much less likely they will be able to continue informing diverse audiences.

As I expect Victor Navasky will explain in detail and with passion, the basis for the protected Periodical status is the promotion of a wide range of ideas from publishers with a wide range of net asset value. The benefits of non-cost based Periodicals rates were not intended only for the wealthy or the popular.

American Business Media does not wish this testimony to be viewed as casting aspersions on either the PRC or the Postal Service as a result of the outcome of what we hope was the last litigated rate case. Perhaps we could have done more than to engage in active discovery, cross-examine many witnesses and present the testimony of three people with vast experience in the Periodicals business. Perhaps we underestimated the extent to which the PRC would be persuaded by those with outstanding economic credentials but no hands-on experience as publisher or a mailer. As American Business Media stated in its Initial Brief to the PRC (footnotes omitted):

> American Business Media has presented the expert testimony of three publishing professionals, each with decades of hands on experience dealing with printers, arranging for transportation, deciding how to best prepare the mail and reacting to the impact of increases in postal costs. They have been on the front line of the constant battle to weigh postage costs, speed of delivery, editorial closing times, the demands of editors and art directors and a host of issues the combination of which is crucial to an understanding of how, in practice not in theory, postage rate design and level changes affect publishers.
>
> In sharp contrast, it appears from their testimony and cross-examination that not one of the four witnesses for Time Warner and MPA/ANM has ever spent a single day, or a single minute, in the employ of a periodical publisher, or a printer. Rather, they are, by education, a mathematician, a physicist, and two economists who, to be sure, have a world of insight into the unique economics of postal costs, but their view is

> gained from the lofty plane of theory rather than the more useful planes of the publishing office and the printing plant. American Business Media does not for a minute question their skill or their numerical, economic or theoretical premises or conclusions, lacking the resources even to make an attempt. But American Business Media does question in meaningful ways the application of their elegant yet sterile theories and conclusions to the real world of periodicals publishing and distribution.

In deciding to adopt the Time Warner-sponsored Periodicals rate matrix so complicated that the software still has not caught up with the rate design, and in accepting the proposition that mailers of small circulation publications can respond to the "price signals" in the rate by co-mailing, the PRC either ignored or gave insufficient weight to the evidence presented by American Business Media's witnesses. Its apparent belief that smaller circulation Periodicals can be incentivised by high rates to co-mail with other publications was refuted on the record, which shows that there was unsatisfied demand even before the rate increase. For example, American Business Media witness Bradfield described (1) the unsuccessful efforts of the publishing company for which he works to persuade its major printers to co-mail volumes below 5,000 (Tr. 12,064)[1], (2) a different, major printer's announcement on its web site that it will not co-mail any publication with a version below 5,000 or more than two between 5,000 and 10,000 (Tr, 12,065), and (3) his company's unsuccessful efforts to find a printer that would co-mail its tabloids and weeklies (Tr. 12,108). American Business Media witness McGarvy described Crain Communications' inability to obtain co-mailing service for its weeklies or tabloids (Tr. 12,177; 12,179). American Business Media member Hanley Wood is able to obtain co-mailing service for only 2 of its 15 monthly publications (Tr. 12,178). Multiply the unsatisfied demands of these three companies by the hundreds of publishers with thousands of publications they seek to have co-mailed, and it is clear that the customers have been demanding service that the mail service industry is unable to provide.[2]

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[1] These "Tr." references are to the official transcript of the proceeding before the PRC. The transcripts are available on the PRC web site, www.prc.gov.

[2] Those seeking to minimize this problem pointed to the fact that printer Quebecor World had recently announced that it is increasing its co-mailing capacity by 50% (see Tr. 12,104-06). Yet that increase will permit, at most, only an additional 225 publications to commence co-mailing, out of the thousands that could benefit from co-mailing (see Exhibits MPA-X-1 and LB-5). When an expansion of this size justifies

The Commission's consideration of this important issue was as brief as it was unpersuasive. It found (¶ 5725):

> The Commission's assessment is that the record in this case indicates that there is no reason that the state of the mailing services industry should stand as an automatic bar to adoption of proposals tied directly or indirectly to such services, assuming all applicable statutory considerations are met. Instead, theory and reality should converge in the rate structure, thereby sending price signals that provide the Postal Service, mailers and others with the information they need to achieve lowest combined cost.

As American Business Media proved on the record, there were price signals in the previous rate design that led publishers to seek co-mailing services that the mailing services industry is unable to provide. Enlarging those price signals, which simply is a nice way to say raising rates for the smaller circulation Periodicals, we showed, would inflict pain from which there is no escape until those services might become available – years from now, at best.

The second major error committed by the PRC in its haste to provide "price signals" for Periodicals found nowhere else in the Postal Service's rate schedules was the Commission's dismissal, as casual choice, of the business models underlying the very existence of certain publications, primarily those focused on presenting time-sensitive news) and those that must be prepared in several demographic or geographic versions in order to meet the demands of readers and advertisers. Neither business model is unusual among Periodicals publishers, yet neither practically allows for co-mailing because of the very nature of that business model.

Speaking of the news-oriented, weekly publications published by Crain Communications, witness McGarvy testified (Tr. 12,186-87) that the core of these publications' business model is to close editorial on Friday night and be in readers'

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a three-page press release, just imagine how long it will take for the expansion that is needed to satisfy the demand.

hands by Monday. If they cannot do that, she noted, they might as well not exist, and the Periodicals class would as a result be less broad and less diverse. As she said (Tr. 12,194), if Crain Communications is unable to get its editorial content into the hands of its readers while it is fresh, "we don't have readers." Similarly, publishers do not undertake lightly the costly task of separating a single, short-run publication into multiple versions, which as a practical matter limits or eliminates the possibility of co-mailing. Rather, witness Bradfield testified (Tr. 12,064) that "a publication to survive must make available to its advertisers editions broken down geographically and/or demographically."

The Recommended Decision of the Postal Regulatory Commission (at ¶ 5719), which the Postal Service Governors accepted over American Business Media's objections, characterizes these situations as those in which "some mailers may choose not to avail themselves of those opportunities [e.g., co-mailing], even if made available, for business reasons and therefore would still need to rely on sacks."[3] It later added (¶5724) in response to contentions that weeklies simply do not have co-mailing services available that "[m]oreover, the record makes clear that some mailers may choose not to avail themselves of these services—even if widely available—for business reasons, such as maintaining editorial freshness."[4]

What is even more puzzling about the results of this last rate case is that only 16 months earlier, in Docket No. C2004-1,[5] the Commission determined that the "vibrant" and "diverse" Periodicals class was a necessity and rejected a proposed rate structure very similar to the one approved in Docket No. R2006-1.

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[3] The Commission did not address the plight of the thousands of publications with total circulation below 5,000 for which co-mailing is unavailable. For them, there has never been any "choice."

[4] This reference is akin to telling a catalog mailer that if he wants lower rates, he should abandon his "business decision" not to include editorial content and call it a magazine.

[5] Rec. Dec. C2004-1, App. B ¶36; App A ¶¶322-28; App. B ¶9.

Yet, those longstanding goals will now be sacrificed because in the cases of all but a few large weeklies, of versioned publications, and of others that cannot escape the severe impact of the recommended rates, the Commission showed a willingness to discard the baby with the bathwater. It stated (¶ 5756) that delaying adoption of rates that will punish those that seek but cannot obtain co-mailing service "makes little sense because they apparently will never be able to take advantage of co-mailing service." Moreover, it found (id.) that moving less far or more slowly is not an option merely because some mailers would have to change their essence to co-mail (e.g., weeklies). In other words, abandon the very reasons that the Periodicals class was created and full steam ahead, notwithstanding that most publications cannot board the train.

In conclusion, Mr. Chairman, American Business Media is not opposed to change. It has supported measured changes to the Periodicals rate design, such as the introduction of presort, bar code and pallet discounts, and it has urged its members to do whatever is feasible to lower the Postal Service's costs by moving out of sacks through co-mailing or co-palletizing. That effort, combined with the incentives that already existed in the Periodicals rate schedule prior to Docket No. R2006-1, have had a dramatic effect. The record before the PRC showed, for example, that the percentage of American Business Media member publication pieces on pallets has grown from about 57% to about 74% in just the past five years (Tr. 12,062).

The drastic measures recommended by the Commission and adopted by the Governors to improve "price signals" and thus efficiency were not needed to foster a continuation of that trend. It serves no laudable purpose to create a demand for co-mailing services well in excess of the ability of the industry to provide them. Thus, there was no justification for Periodicals rate increases that for many if not most smaller publications will turn out to be nearly three times the average rate increase for all mail.

As stated at the outset, however, we hold out little hope that the present rates will be modified prior to the advent of cap-based ratemaking under Postal Accountability and Enhancement Act, which, it appears, will occur as early as next spring. If this

hearing can accomplish anything, it can be used as a basis for revisiting that rate design the next time rates are changed, with an eye toward easing the burden on those most severely damaged by the present rates and to assuring that American readers still have available to them a rich and diverse variety of publications to inform them. At the very least, the record of this hearing ought to convince the Postal Service and, if necessary, the PRC, that any further movement toward allegedly "efficient" rates must be approached with much greater caution than in Docket No. R2006-1.

Respectfully submitted,

/s/ David R. Straus

David R. Straus
Attorney for American Business Media

Law Offices of:

Thompson Coburn LLP
1909 K Street, NW
Suite 600
Washington, DC 20006-1167
(202) 585-6900
dstraus@thompsoncoburn.com

Mr. DAVIS OF ILLINOIS. Thank you very much. I want to thank each one of you gentlemen for your testimony.

I believe I heard you, Mr. Navasky, suggest that each class maybe ought not have to pay its own attributable way. Is that right?

Mr. NAVASKY. I said two things, Mr. Chairman. No. 1, yes, maybe the law ought to be changed, because to speak only of journals of political opinion, but across the political board they are a public good. This country was founded on the idea that free speech and robust public discourse is a good thing.

Like education and defense and the environment, the Government, in my view, ought to subsidize that. But short of that, within the existing system, if you are going to keep the class and require each class to pay its own way, then it seems to me the way to make it work and to make democracy work is to reallocate the cost within the class.

The panel this morning recognized that, but they seemed unwilling to take the next step. It seems to me that there is nothing wrong with saying that the huge mega-corporate magazines that are crammed full of advertising ought to pay a little more, and these marginal publications that are dealing in ideas and that didn't go into business in the first place to make money ought to make a little less.

This is where they are technically non-profit or not. One of the reasons that political journals like National Review and the Nation and the New Republic are not non-profit is that, under the law, if you are non-profit you can't endorse candidates for political office and you can't devote more than a certain percentage of what you do to try and influence legislation. That is what we are in business to do, but we are not in business particularly to make money, and we just want to survive.

Mr. DAVIS OF ILLINOIS. Let me ask you, Mr. Straus, how would you respond to Mr. Navasky's comments?

Mr. STRAUS. I think it is exactly right. It is a little bit artificial to divide mail into classes and say each class has to cover attributable cost, but within each class some mail has to and some mail doesn't.

You in Congress were faced with a real dilemma with the price cap system, whether applied at the class level, the subclass level, or the rate element level.

I am very troubled by something that Chairman Dan Blair said this morning, which is exactly the same thing they said in their rulemaking order issued yesterday, which is the price cap will prevent future rate shock. Well, no, it won't. If there were an 11.4 percent price cap in effect in 2006, the periodicals rate would have gone up 11.4 percent, but they still could have raised some 40 percent and reduced some, but the price cap will not prevent rate shock. Only the Postal Service reviewed by a Postal Regulatory Commission that cares about avoiding rate shock will avoid rate shock.

The notion that every piece of mail has to cover its attributable cost is wrong for two reasons. First of all, there is no logical foundation for that. Second, how do you know what the costs are of each individual piece of mail? Do you want to charge me more if

I hand-write a greeting card to my brother, charge me even more than that if my handwriting is messy and hard to read? I don't think so. What you have to do is set fair rates that in large groups are cost effective.

Mr. DAVIS OF ILLINOIS. Mr. Zipser, let me ask you, How was your organization notified of the July rate increase?

Mr. ZIPSER. I'm not sure our organization was notified. Our individual publications were through our mailing houses. But when I talked to our mailing house back in May trying to get a handle on what to expect in terms of an increase, just for the Guild Reporter now I am speaking, I was told, I don't know yet. It looks like maybe 10 percent. So when it was 27 percent, that came as a bit of a shock.

Mr. DAVIS OF ILLINOIS. So you did experience some shock?

Mr. ZIPSER. Yes, enormous shock, and we are in the process right now of discussing whether or not to go entirely online, whether we should cut our publication schedule in half and have alternating issues online and in print. We are looking at changing the physical size of our publication so it can be folded down to a size that qualifies for a non-profit rate. Then that brings up other considerations the they have heard regarding political advocacy.

There are all kinds of things we are looking at because we can't continue going on the way we are right now.

Mr. NAVASKY. Can I add to that, Mr. Chairman?

Mr. DAVIS OF ILLINOIS. Yes.

Mr. NAVASKY. You know, this morning we were told that there was a year in which to comment on these rate increases. Aside from the fact that we were led to believe it was only going to be an 11 percent increase, the only way you can take advantage of that year is to have yourself a representative technically known or popularly known as a lobbyist. We went and asked what it would cost us to have someone to monitor this process and got rates that ranged from a quarter of a million dollars to a million dollars. We as a class cannot afford that. So effectively we are denied the opportunity to participate in the rate-setting process.

Mr. DAVIS OF ILLINOIS. Let me ask this question, and perhaps each of you do agree that mail delivery should be a function of the Federal Government, with the exception of Mr. Hollingsworth.

Mr. ZIPSER. Yes. I view it as a public utility.

Mr. DAVIS OF ILLINOIS. Mr. Heath.

Mr. HEATH. Yes. I think I do.

Mr. DAVIS OF ILLINOIS. Mr. Davison.

Mr. DAVISON. I'm sorry, Mr. Chairman. I missed the question.

Mr. DAVIS OF ILLINOIS. You do believe that mail delivery should be a function of the Federal Government?

Mr. DAVISON. Mail delivery should be a function of the Federal Government? Yes, I think I do.

Mr. STRAUS. I absolutely agree. I think people would be shocked at what periodicals rates would look like if all of the first class mail were skimmed off by private industry.

Mr. DAVIS OF ILLINOIS. Mr. Hollingsworth, let me ask you, How would privatization perhaps balance more equitably the notion that there is fairness in the process of determining the rates?

Mr. HOLLINGSWORTH. Normally I would caution against international comparisons, such as comparing the United States to some other country in terms of it being an equivalent comparison, and I would subscribe to that in what I am about to say to an extent. However, I do believe that we can learn from what is being done in some other countries, such as Japan, maybe particularly Japan, certain parts of Europe, New Zealand, and elsewhere where their postal services are on an inevitable and no-looking-back pathway to privatization and it is working.

What privatization offers is competition and choice. We see that with the one aspect of mail that is not as tightly regulated by the monopoly statutes, and that is with regard to parcel post, where we have thriving competition amongst the Postal Service, United Parcel Service, DHL, FedEx, and others.

It is also a question of whether or not we will ever see the liberation of our mailboxes. It is also against the law to put anything that you might want other than regulated mail into a mailbox.

So I think with competition you have better options, better choices, better pricing, and I think in the long run it is going to be beneficial for the stakeholders, for the mailers, and for the customers.

This is not a process, I would add, that is going to happen overnight, but I think we can look at what is going on elsewhere in the world and take those necessary steps that former Postmaster General Henderson said we need to do.

Mr. DAVIS OF ILLINOIS. Do you believe that small mailers or smaller mailers would be at a serious disadvantage under such a system?

Mr. HOLLINGSWORTH. Not necessarily, because they will have wider choices and better prices from which to choose. As of now they are captive. They have nowhere else to turn. So who is to say that a monopoly system is going to treat them any better?

Mr. DAVIS OF ILLINOIS. Thank you.

Mr. HEATH. Mr. Chairman, in regard to our feeling about that, we would just like to say that the community newspaper industry is primarily more rural oriented, and our concern with privatization would be that it would kill rural delivery and, in fact, kill the small newspapers.

Mr. STRAUS. I think we can look to the electric utility industry for an example of where theorists suggested that competition would lead to lower prices when, in fact, competition, in those States that have opened up their systems to competition, electric utility prices have soared because there is no real competition. The same thing would happen with the Postal Service. There will be no competition to carry a 30,000 or 40,000 circulation publication to 30,000 or 40,000 addresses dispersed across the entire country.

It was suggested to look at the parcel industry. OK. If I want to mail one parcel from my house, I have to drive. There are two United Parcel Service deposit points, I think, in the Washington metropolitan area. Now, a big company with thousands of parcels, they come and pick them up. They will come to pick it up for me if I pay an extra charge. But competition in parcel service is great for the mass parcel mailer, not so good for the individual parcel

mailer who has to go stand in line at a post office or drive 30 miles to Springfield to put it into their system.

Mr. DAVIS OF ILLINOIS. Thank you, gentlemen, very much.

I am going to go to Mr. McHugh.

Mr. MCHUGH. Mr. Chairman, thank you very much.

I don't have a lot of questions. I wanted most of all to be here because of the enormous respect I have for people on the panel who are known to me personally and, where I don't know them personally, I know of the work that they do. I don't always agree with it, but I always admire it. I thought their comments were important, and I would hope instructive.

I would say to Mr. Navasky, because I don't think you heard Mr. Straus when you were quoting the quotes you received on lobbying. He said you should have come to him. Apparently he is willing to save you money next time. I am just trying to create a business deal here. But your point was taken in the broader context.

I was going to pursue the issue of the privatization question, Mr. Chairman. I appreciated your doing that. I think there is always some fundamental questions as to how we best provide the mail in this country. I happen to believe with the majority of this panel that, for all its flaws, that the Government is certainly in the main—not always, but in the main—the appropriate source of that service. As we have seen here, it is a very difficult challenge to make sure we balance all of the various interests.

I would note with the upcoming regime the change from the task that, as I commented to the first panel, we do have a mechanism in place in this bill that will provide the opportunity for periodicals to be re-examined, and I would hope provide the opportunity for individuals and organizations such as these good folks to have a more direct influence and, in their minds, I am sure, more appropriate outcome as to rate determinations under the new regime as ahead in the future.

I am curious, though, there was the opportunity under this rate case to take the grievance to the Federal courts that have certainly been an avenue of relief that has been accessed by many in the past under past rate cases. Did any of you consider that? If so, why didn't you pursue it? And if not, why was it not considered?

Mr. STRAUS. We probably thought about it for all of about 3 seconds and rejected the notion. A couple of reasons why it would not be a good idea to do it. First of all, there has to be legal error. Merely a different judgment is not going to get a court of appeals to reverse a Federal agency. They give a lot of discretion to the judgment, and here the judgment of the Postal Regulatory Commission was different from that of American Business Media, different from that of magazine publishers of America, different from that of the Postal Service, pretty much in line with that of Time Warner, but not so unreasonable that we thought that a court would reverse it.

But, more importantly, a court of appeals cannot enjoin rates; it can only find them unlawful. By the time a court would have acted, this rate would have been long since over and the law under which it was devised would have been long since over, and so we could have spent $50,000 or $100,000 on an appeal. Even if we won, we would have won absolutely nothing because if the court found that

those rates were unlawful they would no longer have been in existence. That just would have been a silly thing to do.

Mr. NAVASKY. Mr. McHugh, I would add that it would never occur to us to do that because lawyers are, for most small journals—again, that may publish 20,000 or 25,000—if they are weekly, they don't have time to do anything except get their magazine out, no less money to pay a lawyer, so it is way outside of what the reality of the business of putting out one of these journals is.

One of the problems with the suggestions of the postal authorities that we heard this morning, co-mailing, is we did try that, and we found that one of the consequences of it was it delayed delivery to the District, for example, for up to 11 days late. This is for a weekly magazine. It is from another planet to make that suggestion to this class of magazine.

So the idea of going to court to stop it, the idea of co-mailing to overcome it, they really are off the point of what is the equation that Congress ought to consider when it deals with this mailing question, and what our big suggestion is that you ought to go beyond efficiency, go beyond the market, and consider the public interest and the social mission of these publications when you set the rules.

Mr. MCHUGH. Mr. Heath.

Mr. HEATH. Mr. McHugh, we considered that primarily on the grounds of the tub charge, flat trays or tubs. The container charge, which is the most harmful thing to small newspapers in this rate case, was applied, we believe, illegally to flats trays. We are trying to move toward those. We have worked with the Postal Service very favorably to move toward those. The PRC did give the opinion that charge for containers should not apply to the flats tubs because there was no cost basis, no cost studies that would indicate that they should apply.

They were applied anyway. However, our association, small as it is, and made up of rural members like the community newspapers that you are very familiar with in your rural District, and the chairman I believe is originally from Arkansas where there are many small, rural papers where he grew up. Those papers don't have the revenue base to support the dues to file the kind of lawsuits that would require to be successful, so we are not able to do so.

Mr. MCHUGH. I thank you all for saying that. I think it is important to get that on the record, because I have already heard, and I am sure as this process goes forward we will continue to hear, from those who don't share your positions, as I am sure you might gather, that was an avenue and somehow you are not pursuing it would suggest you understood you were in the wrong.

I thought it was important to get your side of that on to the record.

With that, Mr. Chairman, again, as I opened up 5 minutes ago saying I had nothing to say, no questions to ask, I shall now be happy to yield back with my thanks to this panel for being here.

Mr. DAVIS OF ILLINOIS. Thank you very much, Mr. McHugh. I have no further questions. Gentlemen, I want to thank you very much. We appreciate your being here.

While the third panel is being seated, I will go ahead with the introduction of the panelists.

We will have first Mr. James O'Brien for Time Warner. He is vice president of Distribution and Postal Affairs. Mr. O'Brien has been involved with the printing, publishing, and distribution of magazines for more than 35 years.

Then we will have Mr. Mark White, who is vice president of manufacturing at U.S. News and World Report LP. In that role he has responsibility for production and distribution of the company's weekly news magazine, U.S. News and World Report, which last year mailed more than 95 million copies using periodicals class postage.

Mr. Joseph Schick is director of postal affairs for Quad/Graphics. He is the primary liaison with the U.S. Postal Service on all matters affecting Quad/Graphics and their customers. Mr. Schick joined Quad/Graphics in 1981 and was named to his current position in 1990.

Ms. Anita Pursley is vice president, postal affairs, for Quebecor World Logistics, a division of Quebecor World, Inc. In her capacity, she is responsible for establishing corporate postal policy and is the primary liaison with the Postal Service on all matters affecting Quebecor World and its customers.

And last but certainly not least, Mr. Jerry Cerasale joined the Direct Marketing Association [DMA], in January 1995 as senior vice president, Government Affairs. His primary functions are working with Congress, Federal agencies, and State and local governments.

Thank you all very much.

It is the custom of this committee to swear in all witnesses, so if you would stand and raise your right hands.

[Witnesses sworn.]

Mr. DAVIS OF ILLINOIS. The record will show that each of the witnesses answered in the affirmative.

We will then proceed. Of course, the green light means that you have 5 minutes. The yellow light means that you have 1 minute left. And the red light means that your time is up.

We will begin with Mr. O'Brien. Thank you very much.

STATEMENTS OF JAMES R. O'BRIEN, VICE PRESIDENT, DISTRIBUTION AND POSTAL AFFAIRS, TIME, INC., TIME WARNER; MARK W. WHITE, VICE PRESIDENT, MANUFACTURING, U.S. NEWS & WORLD REPORT; JOSEPH SCHICK, DIRECTOR, POSTAL AFFAIRS, QUAD/GRAPHICS INC.; ANITA PURSLEY, VICE PRESIDENT, POSTAL AFFAIRS, QUEBECOR WORLD LOGISTICS; AND JERRY CERASALE, SENIOR VICE PRESIDENT, GOVERNMENT AFFAIRS, DIRECT MARKETING ASSOCIATION

STATEMENT OF JAMES R. O'BRIEN

Mr. O'BRIEN. Thank you. I would like to begin by thanking Chairman Davis and the committee for inviting me to testify at this hearing.

My testimony will focus on how the current periodicals rate structure was adopted and why that structure is critically needed.

The issues involved are not new. They have been discussed widely in the postal community for at least a decade. This chart shows the rise in what it costs the Postal Service to process a periodical from 1986 through 2006. The red line is periodicals cost, the black line is CPI.

As you can see, these costs have outpaced inflation by over 60 percent. In 1998, the magazine publishing industry and the Postal Service formed the Mail Processing Task Force in order to determine why periodicals' costs were rising so rapidly. I was a member of that task force, as were representatives from the Magazine Publishers of America, American Business Media, other publishing companies, and printers. We visited 17 postal facilities and identified a number of contributing factors.

One of the most prominent was the fact that the periodicals' rates were misaligned with Postal Service's cost. I can best explain this by giving an example.

This is a periodicals mail sack. Depending upon where it is entered into the mail stream, it costs the Postal Service between $1.58 to $6.23 to process this sack, not counting the cost of transporting, sorting, or delivering the magazines inside. Until last year, this sack could be placed in the mail containing as few as six copies of a magazine, which might collectively pay postage as low as $1.50. In short, the total postage would be less than the handling costs for the sack, alone. In other words, the rates were not aligned with the costs.

Because of this, the unanimous report of the task force that included large and small periodicals mailers issued 9 years ago concluded that "periodicals rate structure should be reviewed to ensure that it is consistent with the overall periodicals processing strategy and induces appropriate mailer behavior."

Because the postal rates for periodicals did not reflect the Postal Service's cost and gave mailers little reasons to choose more efficient mailing practices, periodicals' costs continued to escalate. Something had to be done to break this pattern. For this reason, in January 2004 Time Warner, Conde Nast, Newsweek, Reader's Digest, and TV Guide filed a complaint with the Postal Rate Commission requesting that it recommend to the Postal Service a rate structure that reflected the cost of processing periodicals mail. In other words, pay for what you use.

We proposed that if the Postal Service incurred $1 in cost to process a sack, the mailer would pay a sack charge of $1.

The Commission conducted a 22 month proceeding in the full regulatory limelight, including hearings on the record, with the opportunity for all interested parties to present testimony, conduct discovery on other parties, and cross examine their witnesses, and file briefs. In its 235 page final order, the Commission expressed concern over the potential impact upon some smaller mailers and declined to act at that time. But it also stated, "Progress toward a more cost-based rate structure is both possible and necessary."

In 2006, the Postal Service filed for a general rate increase, and once again Time Warner submitted a cost based rates proposal. However, at this time we substantially modified our previous proposal to reduce the impact upon smaller or less efficiently prepared publications. The key adjustment was that we proposed passing

through on rates only 60 percent of the cost associated with bundles and containers. In other words, if a sack costs the Postal Service $5 to process, the rates would only reflect $3.

After 10 months of on-the-record hearings, testimony, and cross-examination, the Commission recommended to the Postal Service a rate structure that was more cost-based than the existing structure, but that reduced the potential impact on smaller mailers even further by passing through only 40 percent of the actual bundle and container costs.

As a result of this decision, 60 percent of those costs continue to be covered by the periodicals class as a whole, rather than the mailers who cause them.

I would also like to say a word about subsidies. Many people are unaware of the fact that, other than free mail for the blind and overseas voting, the Postal Service receives no taxpayer subsidies from Congress. As a result, periodicals rates must cover their cost, and each mailer should pay for the services that they consume.

The rate structure proposed by Time Warner is based upon the premise of paying for what you use. If mailers are given the proper price signals by being held responsible for the costs they impose on the system, they will find ways to become more efficient.

In the absence of cost-based rates, periodicals class costs will continue to out-pace inflation, and that is something that our industry cannot afford.

Thank you.

[The prepared statement of Mr. O'Brien follows:]

TESTIMONY OF
JAMES R. O'BRIEN

ON BEHALF OF
TIME WARNER INC.

BEFORE THE
U.S. HOUSE OF REPRESENTATIVES

COMMITTEE ON OVERSIGHT
AND GOVERNMENT REFORM

SUBCOMMITTEE ON FEDERAL WORKFORCE,
POSTAL SERVICE, AND THE DISTRICT OF COLUMBIA

OCTOBER 3, 2007

Thank you Chairman Davis and members of the Federal Workforce, Postal Service, and the District of Columbia Subcommittee for taking the time to explore this issue that is so vital to the future of the publishing industry.

My name is Jim O'Brien and I have been involved with the printing, publishing, and distribution of magazines for more than 35 years. Prior to joining Time Incorporated in 1978, I held positions with R.R. Donnelley & Sons Company, United Parcel Service, and U.S. News & World Report.

During my tenure with Time Inc. I have held a variety of positions in the areas of magazine production, printing plant management, and distribution. I am currently responsible for the delivery of many of the nation's leading magazines including Time, Sports Illustrated, People, Entertainment Weekly, Fortune, and Money.

I am also the former CEO of Publishers Express, an alternative delivery that competed with the Postal Service in the delivery of magazines and catalogs. Under my leadership, Publishers Express grew from a two zip code test in Atlanta to a nationwide network serving 1,000 zip codes in 32 cities.

I am the Chairman of the Association for Postal Commerce (Postcom), former Chairman of the Magazine Publishers of America (MPA) Postal Committee, serves on the Mailers Council Board of Directors, and the MPA Government Affairs Committee.

I have testified before the President's Commission on the Postal Service and been a witness before the Postal Rate Commission in two separate proceedings.

I'm a graduate of the University of Illinois and the Harvard Business School Program for Management Development.

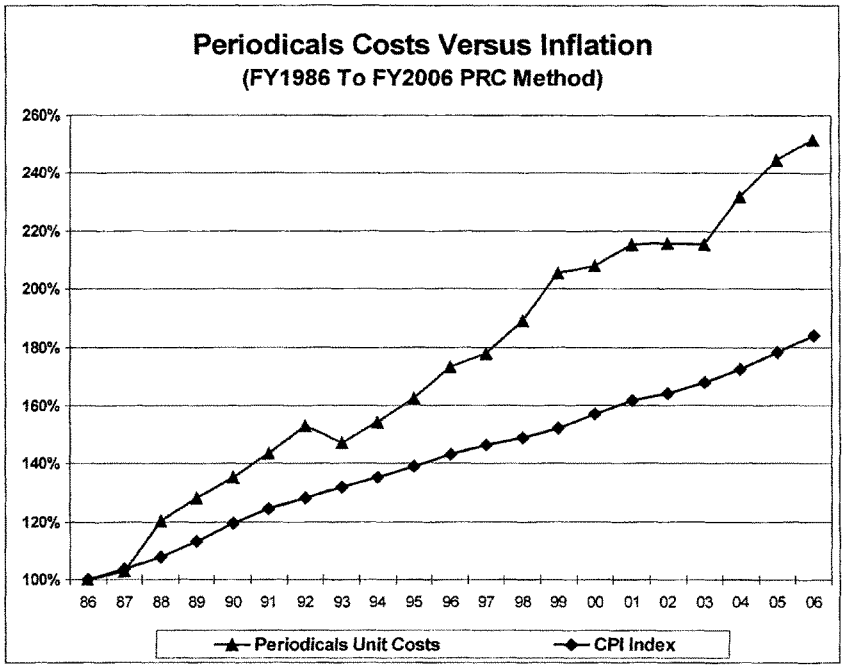
Background

A commonly held misconception throughout the United States is the assumption that the Postal Service is funded by taxpayer dollars. Today, the entire cost of the Postal Service, with the exception of free mail for the blind and overseas voting, is funded by the postage that is paid by mailers. In addition, the law dictates that each class of mail must cover its attributable costs and make a contribution to the institutional costs (overhead) of the Postal Service. In other words, if costs rise for a given class of mail, those costs are borne solely by the mailers within that class.

Traditionally, Periodicals Class mail has received the benefit of providing a small contribution to institutional costs because the law also requires that the rates reflect the "educational, cultural, scientific, and informational (ECSI)" value provided by magazines. Adjusting the contribution to institutional costs was a primary tool for the Rate Commission to recognize the ECSI value of magazines to the American public. As a result, Periodicals Class mail currently contributes approximately 1% to the Postal Service's institutional costs while other classes contribute 50% or more. Historically,

Periodicals contributed as much as 16% to institutional costs but this figure was reduced over the years by the Postal Rate Commission in an effort to offset rapidly rising mail processing costs and the corresponding rate increases. The Periodicals industry has applauded the Rate Commission for their efforts in recognizing ECSI value and protecting magazines from punishing rate increases.

This graph illustrates why the Commission elected to reduce Periodicals' contribution to institutional costs.



As you can see, Periodicals Class costs have outpaced inflation by more than 60% since 1986. The rate of increase became quite severe in 1997 and the Periodicals industry asked the Postal Service to form a joint task force to investigate the causes of the rapidly increasing costs.

In 1998, the USPS Joint Periodicals Operations Review Team was formed. Representatives on the team included the Magazine Publishers of America, American Business Media, publishing companies, printing companies, and the Postal Service. This review team visited a total of seventeen Postal facilities in the fall of 1998. At the conclusion of the process, the team presented a report containing fifteen recommendations (report attached). Recommendation #15 stated that the "Periodicals rate structure should be reviewed to ensure that it is consistent with the overall periodicals processing strategy, and induces appropriate mailer behavior."

Following this report, the industry expected the Postal Service to make progress on this recommendation but no significant changes were made to the rate structure. In 2000, the Postal Service filed a rate case, R2000-1, with the Postal Rate Commission. I provided testimony in this case on behalf of The Alliance of Nonprofit Mailers, American Business Media, The Coalition of Religious Press Associations, Dow Jones & Company, The Magazine Publishers of America, The McGraw Hill Companies, the National Newspaper Association, and Time Warner Inc (testimony attached). In this testimony I discussed the results of the Periodicals Operations Review Team and the need for mailers to "Pay for what they use" (Page 23, line 11). In addition, this testimony contained a rate structure that contains many of the elements adopted by the Postal Rate Commission in R2006-1. It is ironic that some of the very mailers who requested a Congressional hearing in 2007 were the sponsors of my testimony in 2000.

The best way to understand the problems uncovered by the Periodicals Operations Review Team and included in my R2000-1 testimony is by example. Periodicals mail is required to be put into bundles prior to delivery of the mail to the Postal Service. The most efficient bundle is called a carrier route bundle. This type of bundle contains copies that are all going to be delivered by the same letter carrier, and it's designed to travel unopened through the entire postal system until it is finally opened by the letter carrier in a local zip code, such as 60624. If this carrier route bundle is on a 5-digit pallet that enters the Postal system in Chicago, the entire pallet gets transferred to the outbound truck for the 60624 branch. The pallet never leaves the dock area and the only person to touch that pallet is a single fork lift driver.

If the same bundle happens to be on a pallet that contains other bundles for zip codes throughout Chicago, the pallet arrives at the dock and must be taken into the facility where the bundles are sorted on the Automated Package Processing System into containers according to their individual zip code. This machine costs between $3 - 5 million and is staffed by six to twenty people. Once the bundles have been sorted, a postal employee delivers the container to the outbound truck for zip code 60624.

It's hard to believe, but the old rate structure charged the exact same price for these bundles, even though the amount of processing required and the associated costs are dramatically different. It's clear that the rates did not reflect the actual costs of providing the service. No real business could operate this way, and neither should the Postal Service.

Another example pertains to mail sacks. Depending upon where a sack is entered into the mailstream, it costs the Postal Service between $1.58 and $6.23 to process the sack, not counting the costs of transporting, sorting, and delivering the magazines inside. Until last year, sacks could be placed in the mail containing as few as 6 copies of a magazine, which might collectively pay postage as low as $1.50. In short, the total postage would be less than the handling costs for the sack alone. In other words, the rates were not aligned with the costs. Because the postage rates for Periodicals did not reflect the Postal

Service's costs, and gave mailers little reason to choose more efficient mailing practices, Periodicals costs continued to escalate. Something had to be done to break this pattern.

For this reason, in 2004, Time Warner, Conde Nast, Newsweek, Readers Digest, and TV Guide filed a complaint with the Postal Rate Commission, requesting that it recommend to the Postal Service a rate structure that reflected the costs of processing Periodicals mail. In other words, "Pay for what you use." We proposed that, if the USPS incurred $1 in cost to process a sack or pallet, the mailer would pay $1. The Commission elected to hear this case, and from January, 2004 to November, 2005 it conducted proceedings in the full regulatory limelight, including a hearing on the record with the opportunity for all interested parties to present testimony, conduct discovery on other parties and cross-examine their witnesses, and file briefs. After receiving testimony and hearing arguments from all sides, the Commission issued a 235-page Final Order that contained two main conclusions. The first of these was: "progress toward a more cost based rate structure is both possible and necessary."[1] The Commission explained:

> It is clear that there is room for improvement in the Periodicals rate structure, especially in light of the new insights that the Complainants provide into the costs of bundles, sacks and pallets. At a minimum, the Time Warner et al. proposal is a more cost-based rate structure than the current structure. If it were fully implemented, it would provide financial incentives to mailers to engage in lower cost mailing practices by encouraging mailers to use more efficient bundling, containerize more efficiently, change to a more efficient zone distribution, and increase the proportion of machinable pieces. . . . The Commission does not view these changes as radical, as some participants contend, because they reflect existing mail preparation practices and mail flows and constitute only partial de-averaging.[2]

The Commission's second main conclusion was that it was not prepared to recommend adoption of the rate structure that the Complainants had proposed, because the potential rate impact upon some smaller publications was too great. The Commission nonetheless made it unequivocally clear that it expected progress towards the kind of rate structure that we had proposed, and that it expected it in the next general rate proceeding. The Commission's final order stated:

> While the Commission is not adopting Complainants' proposal in this proceeding, this result should not be read as a ringing endorsement of the *status quo*. . . . The

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[1] Postal Rate Commission, Docket No. C2004-1, Order Addressing Complaint of Time Warner Et Al. (Order No. 1446), issued Oct. 21, 2005, ¶ 1013.
[2] Order No. 1446, ¶¶ 5003-04.

> Commission urges the Postal Service to proceed forthwith to develop a rate design for Periodicals that better serves the needs of all interested stakeholders and thereafter file a request for a recommended decision with the Commission. It is hoped that this Order will further inform the Postal Service and spark prompt action.[3]

In 2006, the Postal Service filed for a general rate increase, and once again, Time Warner submitted a "cost based rates" proposal. However, in this filing, we substantially modified our previous proposal in an effort to reduce the impact upon smaller, less efficiently prepared publications. We withdrew our earlier proposal's introduction of zoning in the editorial pound rate, and we reduced the portion of costs associated with bundles and containers that we proposed passing through in rates from 100% to only 60%. Once again, the opportunity for a full hearing on the record was afforded to, and fully taken advantage of, by parties who opposed our proposal, and once again the issue that was most extensively litigated was the alleged potential impact of our proposed rate structure on some smaller publications which had become accustomed to paying rates that were far exceeded by what it cost the Postal Service to deliver them. After ten months of hearings, the Commission recommended to the Postal Service a rate structure that was more cost based than the existing structure but that further reduced the potential impact on smaller publications by passing through only 40% of the actual bundle and container costs. As a result of this decision, 60% of these costs continue to be covered by Periodicals Class as a whole and not individual mailers.[4]

Current Status

As a result of the new rate structure, a sea change is taking place within the printing and publishing industry. Publishers who formerly didn't care about how many sacks they were using suddenly have a reason to reduce their sacks and are actively pursuing new mail preparation methods. These changes are being sought by both weekly and monthly publishers with varying levels of circulation. Within Time Incorporated, we are investigating the mailing practices for each of our titles and making changes. We're expanding the number of titles that co-mail, co-palletize, and drop ship. One of our competitors, U.S. News & World Report is co-binding with Info Week to improve their presort levels and create more cost effective mail for the Postal Service.

The changes also affect the printers and logistics companies that produce and distribute Periodicals publications. Large printers like Quebecor World, R.R. Donnelley & Sons, Quad Graphics, and Brown Printing are expanding their co-mail and co-palletization capabilities. The September, 2007 issue of FOLIO magazine contains ads offering co-mailing from smaller printers Ovid Bell Press, Inc. and Sheridan Magazine Services. Would these printers have offered co-mail without a change in the rate structure? Change

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[3] Order No. 1446, App. B, ¶¶ 28, 13.

[4] Relevant portions of the Commission's decisions in theR2005-1 and R2006-1 omnibus postal rate cases appended to this testimony.

is taking place very quickly and the reason is that people now have a rate incentive to change their mailing behavior. As we saw during the period from 1998 until 2006, very little change occurs without a rate incentive. If mailers are given the proper price signals, by being held responsible for the costs they impose on the system, they will find ways to become more efficient.

Future

Going forward, I anticipate continued growth in co-mailing, co-palletization, and drop shipping as more printers and publishers respond to the new rates. As a result, I'm hopeful that Periodicals mail processing costs will come back into alignment with the rate of inflation and possibly drop below inflation. This will allow the Periodicals industry and the Postal Service to take full advantage of the Postal Accountability and Enhancement Act and operate within a period of predictable price increases capped by the Consumer Price Index.

In closing, I once again thank the Chairman and Committee Members for providing this opportunity to inform the Committee on the history of Periodicals Class rates and why the current rate structure is critically important to the future of Periodicals Class Mail.

APPENDIX TO TESTIMONY OF JAMES R. O'BRIEN

EXCERPTS FROM POSTAL RATE COMMISSION DECISION IN THE R2005-1 AND R2006-1 OMNIBUS POSTAL RATE CASES

Docket No. R2005-1, PRC Opinion & Recommended Decision

[The following passages from the Commission's R2005-1 decision show that it is absurd to claim that the Commission's adjustment of the Periodicals rate structure in Docket No. R2006-1 was any kind of reversal of policy or sudden and unforeseeable development.]

[Page ii] The Commission's preference is to develop rates that accurately reward mailers' worksharing. It is concerned that the delay in recognizing the impact of recent innovations and improvements in postal operations, coupled with the passage of time, will probably result in unusually disproportionate increases and decreases in different rates in the next case. The Postal Service and mailers seem prepared for that possibility as they too recognize that proper cost-based rates foster efficiency and promote a healthy postal system.

[On Standard rates]

[5030] On brief, Valpak argues that adoption of the proposed rates may have an unsettling effect in the next rate case since they "would likely exacerbate future instances of rate shock." Valpak Brief at II-13. Apart from the fact that the comment is necessarily speculative, it does highlight a risk that settling parties run, one presumably considered and deemed acceptable. The implicit message appears to be that rate shock should have less weight as a mitigating factor in the next case if it is the result of rate increases *not* adopted in this case.

[5032] Rate shock arguments are often raised in rate proceedings. They are likely to be raised in the next proceeding as well, in which case the Commission will assess their merits based on the record developed in that proceeding. Parties should be aware that the Commission will seek to obtain economically efficient cost-based rates and appropriate allocation of institutional burdens. The discussion of rate design in the following chapter highlights several problematic areas deserving of closer examination in the next proceeding.

[On Periodicals rates]

[6103] *Participants' positions*. Participants in this case representing senders of Periodicals mail include ANM, ABM, CRPA, Dow Jones, The Hearst Corporation, MPA, McGraw-Hill, NNA, NAA, PPA, and Time Warner. Each has signed the Stipulation and Agreement. ANM, Time Warner, and jointly, ABM and McGraw-Hill, filed separate comments or briefs in this case, and Time Warner, along with ABM, Dow Jones, MPA and McGraw-Hill, filed a joint brief as the Periodicals Coalition.

[6104] The Commission recommends, without change, the set of Periodicals Outside County rates and fees identified in the settlement proposal. The recommended rates represent an across-the-board increase; they do not reflect application of traditional rate design methodology. Pound charges, for example, do not reflect the actual distribution of pound miles in the base year. This result carries forward into the test year; thus, in the future, some rate elements may require larger than expected increases to realign rates with costs. Consequently, mailers must stand forewarned that some may face "rate shock" in subsequent proceedings. The Commission recommendations do not include any classification changes consistent with the settlement.

[6122] The Commission notes that the proposed sacking and other changes in Periodicals preparation practices have not emerged in a vacuum; to the contrary, they occur in the much broader context of Docket No. C2004-1, a formal complaint filed by five senders of Periodicals mail prior to the current rate request. The Complaint, in turn, is an outgrowth of concern over escalating cost trends discussed in earlier cases, dissatisfaction with the Postal Service's progress on promised classification reform, and new insights on cost causation as it relates to the continued efficacy of the longstanding Periodicals rate structure.

Docket No. R2006-1, PRC Opinion & Recommended Decision

[The following passages from the Commission's R2006-1 decision show that it carefully weighed extensive evidence and argument on all the issues raise by FreePress et al., and that it largely rejected their views on the basis of a careful assessment of the factual evidence in that docket, factual evidence that had been accumulating over a series of previous cases, and policy judgments that it has been developing and weighing over a series of cases.]

[5607] Outside County. The record on Outside County reveals virtually unanimous support for structural reform; unchallenged cost studies showing that bundles, sacks and pallets impose costs on the system, independent of those associated with pieces and pounds; the expectation that many lightly-filled sacks will have been eliminated by the test year, given a recent rule change; and more potential for co-mailing and co-palletizing. The Commission recommends adoption of the framework underlying the Time Warner Inc. (Time Warner) proposal in this case and its related costing support, but with significant moderation of passthroughs.

[5608] The proposal in this case differs in significant respects from the proposal Time Warner sponsored, along with others, in Docket No. C2004-1. These differences, especially the elimination of a fully-zoned editorial pound rate, result in substantial moderation of the rate impacts associated with the previous proposal. The Commission recommendation further moderates the Time Warner proposal in this case. Time Warner, while maintaining full support for its proposal as filed, acknowledges that the Commission might find some moderation (or tempering) in order. U.S. News & World Report, Inc. affirmatively suggests that the Commission pursue that approach. U.S. News

Brief at 13.

[5614] The proponents of the three main alternatives are the Postal Service, Time Warner and, acting jointly, the Magazine Publishers of America and the Alliance of Nonprofit Mailers (MPA-ANM). Their proposals differ in direction and degree, but reflect agreement that a more cost-based structure is needed. Other participants voicing opinions on substantive aspects of structural reform concur.

[5615] This consensus is the welcome result of the close scrutiny the Outside County Periodicals structure received in the recent Complaint of Time Warner Inc., et al. and in the ensuing Commission Order. Docket No. C2004-1, Order No. 1446. Indeed, each proponent characterizes its proposal as a response to the Commission's call for measured, but meaningful reform. Other participants addressing the proposals also do so in that context. At the same time, the Commission is pleased that participants have not restricted discussion to the state of Periodicals as of the issuance of Order No. 1446 in October 2005, but have evaluated developments since then and offered considered assessments of the future.

[5712] The Commission finds itself faced with credible, consistent and cumulative testimony that both the container charge and the entire Postal Service package do not send the intended signals to major segments of the class. The Service has not been able to show that the examples provided on this record are isolated or unique instances. Regrettably, the key features of the Service's proposal provide incentives that are so modest that they are, in many instances, outweighed by the elimination of the pallet discounts. In other cases, they are so contradictory that mailers that already engage in efficient practices would not receive appropriate recognition for their efforts. This is clearly contrary to the Service's stated objective of not only incenting new, more efficient behavior, but also recognizing — and continuing to encourage — other mailers' ongoing efficient practices. The Commission concludes that these features of the proposed structure impair the stated objective of proving better price signals and preclude a favorable recommendation.

[5713] Given the conclusion that there are fundamental problems with execution of the Service's objective, the impact arguments ABM and McGraw-Hill offer lose much of their currency. The comparisons flow from a faulty premise; namely, that the structure, in general, is oriented toward providing better price signals.

[5745] The Time Warner proposal uses essentially the same rate design framework as the Complaint case proposal, but incorporates several adjustments intended to moderate impact. This leads most participants to address the proposal in terms of whether those adjustments, considered in light of this evidentiary record, sufficiently mitigate concerns the Commission raised in the Complaint case, including the rate impact on mailers.[241] US News, a supporter of the Time Warner proposal, contends that they do. It asserts: The

Commission's only criticism of the original Mitchell model in C2004-1 is that it would lead to inordinately high rate increases for some small mailers. Mitchell's current proposal incorporates those concerns, following the same logic as before but softening the impact on certain mailers (and necessarily balancing that by making worksharing incentives less than they were in the C2004-1 proposal. These efforts ... are reasonable .... U.S. News Brief at 13.

[5746] Opponents generally counter with claims that the proposal is still too much, too soon and still has unacceptable rate impacts. See, for example, ABM-RT-2 at 7. [5747] Assessment in light of an updated record. For all participants except McGraw-Hill, witness Mitchell's decision not to propose a fully zoned editorial pound rate appears to moot the two concerns the Commission expressed in the rate case (undue rate impact on certain small mailers and abridgement of public policy). The Commission has noted its approval of the inclusion of editorial pound rate dropship discounts in its preliminary comments, so that aspect of the Time Warner proposal does not pose a difficulty.[242] Mitchell also proposes an editorial discount that is equivalent to the Service's proposed rate and higher than both the existing rate and the rate proposed by MPA-ANM. Therefore, there is continued recognition of the presence of editorial content.

[5748] McGraw-Hill nevertheless contends that the Time Warner proposal undermines the unzoned editorial pound charge because ... non-transportation costs that are nevertheless distance-related would be recovered from 100% editorial publications (as from all other publications) through container charges that (like the zoned advertising pound charges) increase with the distance that a container travels through the postal system. McGraw-Hill Brief at 25-26.

[241] McGraw-Hill asserts that the Time Warner proposal is at odds with the guidance in Order 1446. McGraw-Hill Brief at 21. The Commission finds this assertion unfounded.

[242] McGraw-Hill points out that Time Warner proposes increasing the flat editorial pound charge to a level that is 83 percent of Zones 1 and 2 advertising pound charge. It notes that the traditional level is 75 percent. McGraw-Hill Brief at 25, n.24.

[5749] It notes that origin-entered containers would pay much higher container charges than destination-entered containers under the Time Warner proposal, and concludes that a 100 percent editorial publication would pay substantially more than the unzoned editorial pound charge "for the privilege of making a greater use of Postal Service transportation." Id. at 26. To that extent, McGraw-Hill finds that the purpose of the unzoned editorial pound charge is defeated. Id., McGraw-Hill Reply Brief at 15-17.

[5750] The policy of promoting editorial diversity and widespread dissemination of editorial matter is one of many that must be weighed and balanced. Some of those considerations include recognizing costs and promoting worksharing. The Commission finds that cost-based container charge differentials reflecting dropshipping alternatives can not reasonably be said to defeat the public policy purpose underlying the flat editorial pound charge. It therefore rejects the suggestion that the Time Warner proposal should not be adopted on this ground.

Mr. DAVIS OF ILLINOIS. Thank you very much.

We will go to Mr. White.

STATEMENT OF MARK W. WHITE

Mr. WHITE. Thank you for providing me this opportunity to clear up several misconceptions regarding periodicals' postal rates. There is no question, as you have already heard, that many publications have large increases in their postage this year, but it is not a small versus large issue. Many large circulation publications, including our own, had higher increases than average. We mail nearly 2 million copies of every issue, mailed extremely efficiently, yet our postage rates went up about 15 percent, much higher than average.

The issue comes down to lightweight publications, light, nationally distributed publications. Virtually all of us had large increases, whether large circulation or small circulation.

Another misconception is that the new rates are cost based. They are a move in the right direction, but they are not truly cost based. One problem or one flaw is that they still undercharge for bundles and containers. That means for the periodicals class to break even there must be overcharges in other areas. For U.S. News, that means that, though we are an efficient mailer, we still are overcharged. We are still subsidizing other magazines, including those published by much larger publicly traded corporations, because they are mailing their magazines less efficiently.

I would also like to point out that, contrary to some of what you have heard, time-sensitive publications can take advantage of incentives in the new rates. Weekly publications can join freight pools to gain drop-ship discounts in a way that is efficient. We have been doing it for more than a decade, despite the fact that many people told us it couldn't be done.

Weeklies can engage in co-mail and similar activities to reduce postage. We mail nearly all of our copies with another weekly, binding on the same binding line, despite our high volume which makes the incentives not as attractive for us as it is for smaller mailers to join such co-mail pools.

Many people claim that these programs will delay delivery. Our experience is that drop-shipping or pool-shipping, co-binding, co-mail actually improve delivery. We are able to create more-efficient bundles, more finely sorted pallets, drop-shipped further into the postal system.

Let me also point out that true cost-based rates would not automatically hurt small circulation publications. Many local newspapers and regional magazines are inherently efficient mailers. Many small publications have joined co-mail pools and have taken other tactics to become efficient mailers. As an aside, I will point out that I worked with two other publications the last couple of years, one a small publication typically mailing about 20,000 copies, did it very efficiently. Another one, when I started working with them, was mailing 500,000 to 600,000 copies, doing it very inefficiently. It is not a strictly small or large issue; it is efficient versus inefficient.

The problem we had is the old rate structure that we inherited. Mailers were subsidized for mailing inefficiently because periodicals rates did not send the right signals to mailers. The disconnect

between what we publishers paid and the Postal Service's cost caused inefficient mailing behavior. That led to rapid rate increases for all of us.

The new rate structure is the beginning of a cure, though admittedly one with bitter medicine that treats some symptoms while largely ignoring others. But this partial cure is already having the intended effect, causing publishers to mail more efficiently, which is minimizing costs for the entire periodicals class. Such moves toward greater efficiency are our best hope for reigning in future increases in periodicals rates.

Thank you.

[The prepared statement of Mr. White follows:]

STATEMENT OF MARK W. WHITE
VICE PRESIDENT, MANUFACTURING
U.S. NEWS & WORLD REPORT, L.P.

SUBCOMMITTEE
ON FEDERAL WORKFORCE, POSTAL SERVICE
AND THE DISTRICT OF COLUMBIA
COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM
U.S. HOUSE OF REPRESENTATIVES

OCTOBER 3, 2007

Good afternoon, Mr. Chairman and members of the Subcommittee. My name is Mark W. White, and I am Vice President of Manufacturing for U.S. News & World Report, L.P., publisher of *U.S. News & World Report*. In that role, I am ultimately responsible for the production and distribution of our weekly newsmagazine, which is commonly referred to as *U.S. News*. We are a privately held company that for the most part competes with much larger publicly traded corporations. Last year, we mailed more than 95 million magazines, making the United States Postal Service our largest vendor. More information about our company and about me is available in the attached biography.

Thank you for providing me this opportunity to testify on behalf of U.S. News and to clear up misconceptions about Periodicals postal rates. I would like to make eight points to help clear up these misconceptions:

1) *Not all small-circulation publications had disproportionately large increases in Periodicals rates this year, nor did all large-circulation publications have small increases.* In fact, all relatively light publications were hit with a large increase because the new rates rebalanced the piece/pound revenue split. Despite mailing more than 1.9 million copies at a time, co-binding with another publication, and dropshipping extensively, our postage increase amounted to more than 15 percent – well above the

average increase for Periodicals. (We have shaved more than a percentage point off the increase by changing the way we mail to take advantage of incentives in the new rate structure.) By contrast, some small-circulation publications apparently had rate decreases.

2) *There is nothing inherently unfair about some mailers getting larger rate increases than others in the same class.* Moving toward greater recognition of the Postal Service's costs in postal rates requires that some rate increases be larger than others. For U.S. News, the problem with the most recent rate case is not that our rates rose more than did those of many other mailers. The problem is that the rates did not go far enough in reflecting cost differences. That means U.S. News continues to pay more postage than warranted by the Postal Service's costs of handling our magazines so that other Periodicals publishers can pay less than the Postal Service spends to handle their mail.

3) *The current Periodicals rates are certainly not the result of a secret plot by Time Warner Inc.* The PRC did not even approve Time Warner's proposal. Time Warner has been openly advocating cost-based Periodicals rates for years, making its research on the Postal Service's costs and a corresponding rate structure available to all. The PRC made no secret in 2005 of its desire to implement cost-based rates in general and of its acceptance of most of Time Warner's logic in particular. The PRC conducted the rate case out in the open over the course of many months, with a variety of participants representing all aspects of the publishing industry. Time Warner's proposal – a somewhat watered-down version of what it had been advocating for years – was no secret. In the end, no one else, including the Postal Service itself, presented a rate structure that was so directly linked to the Postal Service's costs. To have cost-based Periodicals rates, the PRC therefore had no choice but to use Time Warner's proposal as a starting point. It

significantly altered that proposal, however, watering it down even further to lessen the impact on small publications.

4) *The old Periodicals rate structure was neither reasonable nor fair.* In reality, the old rate structure got us into this mess by enabling Periodicals to be mailed in ways that were expensive for the Postal Service. The structure did not charge mailers sufficiently for doing things that caused the handling of Periodicals to be labor intensive for the Postal Service, such as mailing publications in sacks. That contributed to rapid increases in the Postal Service's costs for handling Periodicals, which in turn led to large rate hikes for all publications. And because the Postal Service must break even financially on the Periodicals class, efficient mailers were in effect subsidizing inefficient mailers.

5) *The Postal Service presented a proposal in the last rate case that was neither reasonable nor fair.* The original Postal Service proposal was well intentioned but based on flawed analyses and assumptions. It would have discouraged some forms of work sharing, which would have caused the Periodicals class to become even more inefficient for the Postal Service and therefore would have led to large rate increases in the future. It also would have done little to correct the relative subsidization of inefficient mailers by efficient mailers. Fortunately, the PRC recognized these flaws, as did the Postal Service's own Board of Governors.

6) *Those of us who advocate cost-based Periodicals rates are not completely satisfied with the outcome of the most recent postal rate case.* The new rate structure was a move in the right direction but by no means fixes all that is wrong with Periodicals postal rates. By passing through only a portion of the Postal Service's costs related to bundles and containers, the new rates still tend to overcharge mailers like U.S. News that have

efficient bundles and containers. We are still, in effect, subsidizing companies – some of them major corporations – that mail their publications in ways that are less efficient for the Postal Service.

7) *Contrary to popular opinion, weekly magazines and other time-sensitive publications can engage in various activities to enhance their worksharing discounts.* We have been pool shipping most mailed copies of our weekly magazine to achieve dropshipping discounts for more than 10 years. Virtually all of our mailed copies are shipped with other products – including other weekly magazines – to postal facilities. And virtually all of our mailed magazines are co-bound with another weekly magazine, which means the two publications are collated on the same binding lines and together have more efficient bundles and containers than could be achieved if they were bound separately. Some publishers worry that such efforts will delay delivery, but we have found that they improve delivery by enabling us to create more finely sorted bundles and pallets that can be dropshipped deeper into the postal system.

8) *True cost-based rates do not automatically hurt small-circulation publishers or help large-circulation ones.* Many small publications mail efficiently and therefore would benefit from true cost-based rates. Local newspapers and regional magazines tend to have a relatively small number of mailed copies but often mail quite efficiently. Many small, nationally distributed publications mail efficiently by participating in offline co-mailing – which, by the way, is not practical for *U.S. News* because of our magazine's multiple editions – and poolshipping. Meanwhile, some magazines that mail hundreds of thousands of copies per issue mail inefficiently because they have managed their multiple versions poorly.

Before the current rate structure was implemented this year, Periodicals rates did not send the right signals to mailers. The disconnect between what publishers paid and the Postal Service's costs caused inefficient mailing behavior, which led to rapid rate increases for all publishers. The new rate structure is the beginning of a cure – though admittedly one with bitter medicine that treats some symptoms while largely ignoring others. This partial cure is already having the intended effect: causing publishers to mail more efficiently, which is minimizing costs for the entire Periodicals class. And the marketplace is still in the process of responding to the incentives in the new rates. Such moves toward greater efficiency are our best hope for reining in future increases in Periodicals rates.

Mr. DAVIS OF ILLINOIS. Thank you very much.

We will go to Mr. Schick.

STATEMENT OF JOSEPH SCHICK

Mr. SCHICK. Mr. Chairman and members of the subcommittee, thank you for providing me with this opportunity to testify on behalf of Quad/Graphics. Quad is the largest privately held printer and third largest commercial printer, public or private, in the United States. Last year we distributed more than 9 billion magazines, catalogs, and direct mail pieces through the Postal Service, equating to about $2 billion in postage paid by our clients. We are headquartered in Sussex, WI, and have other printing plants across the Nation.

While it is true we don't pay postage for the books that we print, postal rates do have a major impact on the printing industry. Every time the Postal Service increases rates, our clients react in a way that is detrimental to printers. They reduce circulation. In worst-case scenarios, they may discontinue a publication. They cut back on the number of pages. They reduce their frequency. In some cases, they may move to the Web. The result is a reduction in total print volume, and therefore our business.

Because of the volume of mail we and our colleagues in the printing industry produce, it is a necessity that we work very closely with the Postal Service to create an end-to-end process that results in the lowest combined cost for our mutual clients. It is a term we have coined over the years with the Postal Service, basically stating that we don't want costs pushed to one side or the other, because at the end of the day our customers still end up paying for it.

We are business partners with the Postal Service. Think of the Postal Service as the next department in a printing operation. We hand off the product to the Postal Service for final delivery, and our clients expect that to be a seamless process. That requires us to continue to find ways to be able to prepare mail in its most efficient way so that the Postal Service will incur the least amount of cost in carrying out their part of the process.

As a large mailer, it is obvious that the long-term viability of the Postal Service is critical to our success and that of our clients. Over the last 25 years, through technological advances and process changes resulting in productivity gains of more than 4 percent annually, the printing industry has been able to actually reduce the price for printing adjusted for inflation. On the other hand, the Postal Service has seen their overall cost continue to rise, which has resulted in higher postage rates for mailers. So it becomes even more imperative that we try to do as much as possible in preparing and distributing the mail before we present it to the Postal Service.

Over the years the printing industry has worked with the Postal Service and others to develop drop-shipping for transportation efficiencies, bar coding for automation, mail dock for distribution planning, Postal One for postage payment, and numerous other products and services. And many years ago carrier-out pre-sort was established as the finest level of pre-sort, which eliminated a great deal of work in postal processing and delivery, and therefore costs for the Postal Service.

There was a time when only large circulation or local city regional publications could realize carrier route savings. Thankfully, that changed with the advent of co-mailing. I am proud to say that Quad/Graphics pioneered co-mailing in 1986 when we were a much smaller printer. In fact, we were about a $260 million printing company with 2,100 employees. We knew it was the right thing to do at the time to help our clients reduce the heir postal costs, but at the end of the day we also have a business to run, and we knew that we needed to provide a unique service that would help us grow our business, as well. Thankfully, that happened.

Today we offer four different co-mail processes, both in-line and off-line, with options for virtually every one of our clients, regardless of circulation or trim size.

Over the years, many other companies, printers large and small, and third-party logistics providers have made investments in co-mail equipment and technology. One size does not fit all, and that is apparent by the different co-mail processes that have been developed.

As with any other investments, there has to be a return on that investment. We are in this to make money. In this case, that would equate to work share discounts provided because of a savings realized by the Postal Service. Over time, we have to drive behavior through those work share incentives for the continual process improvement of the technologies that prove successful, as well as using them to help Postal Service reduce their cost. Co-mailing is that successful technology. The new rate structure is the driver that will provide the incentives to continue to grow co-mail and make it even more viable for a larger audience of users.

We don't like to see postal increases any more than the next guy. We suffer, as do our clients who have to deal directly with the postage increases. We are sympathetic to all mailers, big and small. Our clients run the gamut from niche publications with print orders of 60,000 copies, of which only 10,000 are distributed through the mail, to some of the largest general interest publications and catalogs with circulation in the millions.

Regardless of the quantities mailed, each publication is challenged to find ways to reduce the impact of a rate increase. If our clients are challenged, that means we are challenged to provide them with the opportunity to reduce those costs. That is our business.

There is no debating the fact that we have just experienced the most challenging rate increase in recent history. Many mailers experienced higher increases than had been originally proposed. Periodicals question the rationale of the complexity of the new rate structure.

As a printer, we were faced with having to explain to our clients what happened and what we were going to do for them to help them survive. While this was a challenge, it was not unlike what has happened after every rate case that I have ever been involved with over the last 20 years. A main reason for that is the rate-making process under the old law. Everything about it created a situation where we all had to react to something that was usually unexpected. In this case, that was taken to the nth degree.

We are encouraged by the signing of PAEA in 2006 because it limits rate increases to CPI, takes a 10-month rate-setting process out of play, and gives the Postal Service an opportunity to use market pressures on different classes of mail as a guide for setting rates. It should allow us the opportunity to better plan and manage our businesses.

I fully expect that going forward we will continue to work with the Postal Service as business partners to do whatever it takes to maintain the concept of lowest combined cost. Because of PAEA, there should be more opportunities than ever to accomplish that goal. The viability of the printing industry and the Postal Service is at stake.

Thank you for allowing me to make those views known.

[The prepared statement of Mr. Schick follows:]

STATEMENT OF JOSEPH SCHICK
DIRECTOR, POSTAL AFFAIRS
QUAD/GRAPHICS, INC.

SUBCOMMITTEE
ON FEDERAL WORKFORCE, POSTAL SERVICE
AND THE DISTRICT OF COLUMBIA
COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM
U.S. HOUSE OF REPRESENTATIVES

OCTOBER 3, 2007

Mr. Chairman and members of the Subcommittee, thank you for providing me with this opportunity to testify on behalf of Quad/Graphics. My name is Joseph Schick and I am the Director of Postal Affairs for Quad/Graphics, Inc. I have been employed by Quad for 26 years, the last 17 in my current position. I have served as Chairman of the Postmaster General's Mailers' Technical Advisory Committee (MTAC) and continue to participate in MTAC-related working groups. Quad/Graphics has participated in recent rate case proceedings, and I have been a witness at the Postal Regulatory Commission on several occasions.

Quad/Graphics is the largest privately held printer of magazines, catalogs, retail inserts, direct mail and other commercial products in the Western Hemisphere and third largest commercial printer – public or private – in the United States. Annual sales total $2 billion. Among our more than 1,000 clients are magazine publishers Time, Inc., Conde Nast Publications, American Express Publishing and National Geographic Society; catalogers Victoria's Secret Direct, Williams-Sonoma, Potpourri Group and Lands' End; and retailers Macy's, Target and ShopKo. Our manufacturing mix is 51% catalogs / direct mail; 37% magazines; 11% retail inserts; and 1% books.

We provide full production services from design and photography through printing, data services, finishing and distribution, using some of the most modern equipment and service approaches in the industry. Our R&D division, QuadTech, has been designing and manufacturing computerized controls for press and finishing equipment for more than 25 years and has products installed in more than 80 countries.

Quad/Graphics is headquartered in Sussex, Wisconsin. We have 12 domestic printing plants, located in Milwaukee, West Allis, Pewaukee, Sussex, Lomira and Hartford, Wisconsin; Saratoga Springs, New York; Martinsburg, West Virginia; Fredericksburg, Virginia; The Rock, Georgia; Oklahoma City, Oklahoma; and Reno, Nevada. In addition, we have 21 imaging service centers, which are located near our clients or on-site at their facilities. We have partnerships with printers in three international locations: Poland, Brazil and Argentina. Worldwide, Quad/Graphics' employment totals 12,000 people.

While we don't pay postage for the books that we print, postal rates do have a major impact on the printing industry. Every time the USPS increases rates, our clients react in a way that is detrimental to printers. They reduce circulation and in the worse-case scenario, they may discontinue a publication. They cut back on the number of pages and reduce their frequency. They move their business to the web. The result is a reduction in the total print volume.

We suffer as do our clients who have to deal directly with the postage increases. We're sympathetic to all mailers, big and small. Our clients run the gamut, from niche publications with print orders of 60,000 copies of which only 10,000 are distributed through the mail, to some of the largest general interest publications with circulation in the millions. Regardless of the quantities mailed, each publication is challenged to find ways to reduce the impact of a rate increase. And if our clients are challenged, that means we are challenged to provide them with the opportunity to reduce those costs. Because of that, in the last 10-15 years providing postal and distribution services to publishers and catalogers has become one of the most important and competitive aspects of the printing industry.

As a large mailer of periodicals, catalogs, and direct mail, the long-term viability of the United States Postal Service is critical to our success as well as the success of our clients. In the production, distribution and delivery of a publication, there are 3 general cost components for our clients; paper, printing and postal. Only one of those components is directly controllable by the printer and that is obviously the printing costs. Over the last 25 years, through technological advances and process changes resulting in productivity gains of more than 4% annually, the printing industry has been able to actually reduce the price for printing (adjusted for inflation).

Paper prices have fluctuated during that same time, rising and falling based on supply and demand. At the present time we are in an upward cycle for paper prices. To ensure that we are providing our clients with the lowest possible cost and highest quality product, we have dedicated staff continually working with the paper manufacturers. We are also coordinating with transportation companies, rail and over-the-road, to ensure the most cost-effective and timely delivery of paper from the mills to our plants. Through industry initiatives we have developed standards for managing inventories and waste. So despite the fact that we aren't in control of paper prices, industry efforts have resulted in the management of paper prices.

Unfortunately, postal rates have continued to rise during the same time and continue to put pressure on our clients and the viability of hard-copy distribution through the mail. As we do with paper companies, the printing industry works together with the Postal Service to try and maintain the "lowest combined costs". That phrase relates to the entire process cost for our (USPS' and printers') mutual clients, from mailpiece design to mailbox delivery. It makes no sense for the Postal Service to reduce their costs by shifting them back to the printer, because at the end of the day the client will still pay a higher price. Our goal in working with the Postal Service is to help to reduce their cost by providing them with more efficiently prepared mail while not increasing our cost of

production. Without these efforts, postal rates would have increased at a much higher rate.

Over the years, Quad and our colleagues in the printing industry have worked with the Postal Service and others to develop drop shipping, barcoding for automation, Mail.Dat for distribution planning, PostalOne® for postage payment, and numerous other products and services.

The most basic of all that we do is preparing mail in the finest of presort levels with carrier route being the finest sortation. There was a time when only "large" circulation or local/city regional publications could realize carrier route. Thankfully that changed with the advent of comailing. (Comailing is the process of combining/presorting two or more titles, magazines and/or catalogs, into a single mail-stream. This process lowers the per-piece postage rates due to the improved level of presort for each title. It also creates deeper penetration into the postal system, facilitates more consistent and timely delivery, and allows magazines and catalogs to arrive in better condition with less handling by the United States Postal Service.)

Quad/Graphics pioneered comailing in 1986 when we were a much smaller printer, a $260 million company employing 2,197 employees. We knew it was the right thing to do at the time to help our clients reduce their postal costs, and we knew that we needed to provide a unique service that would help us grow our business as well. Using a QuadTech built "Multi-Mailer," we merged together the mailing lists of several different pre-bound magazines to create one large mailstream. Today, we offer four different comail processes, inline and offline, with options for virtually every one of our clients regardless of circulation or trim size.

Some of the publications and publishers who participate in our comailing process are Aspire Publications, *Outdoor Life, American Girl, Audubon,* National Trust for Historic Preservation, *American Iron, Road Biker*, Rodale, *Working Mother, National Geographic Traveler and National Geographic Kids.*

To illustrate the growth of comailing, today we have more than 110 publications and more than 100 catalogs that currently participate in our comail processes. The circulation ranges from 1,500 copies to 5,000,000 copies (with nearly half being less than 100,000 copies). The extents to which our clients participate vary from title to title. For some, we comail their entire mailing list. While other publications may only comail specific versions or back issue and/or supplemental copies.

We also offer the same comail processes to our catalog customers. As a result of the recent rate case, we have seen a dramatic increase in the number of catalogers who are participating. In 2006, our total comail volume between periodicals and catalogs was about 1 billion copies. With about 890 million copies comailed to date in 2007, we have almost reached that volume through August of this year. The following represents the four comail processes that we offer and their total volumes for the last three years.

	2004	2005	2006
Multi-MAIL	217,000,000	244,600,000	257,000,000
Multi-WRAP	38,300,000	66,000,000	104,000,000
Multi-BIND	26,900,000	259,200,000	602,600,000
Multi-BLEND	0	0	15,200,000

- **Multi-MAIL** is our offline process that merges the mailstreams of several different pre-bound magazine or catalog titles into one large mailstream.
- **Multi-WRAP** combines different pre-bound, polybagged magazine or catalog titles offline and presorts them together into a single mailstream. Onserts and enclosures can be polybagged with each title.
- **Multi-BIND** is our inline binding process that combines different magazine or catalog titles and presorts them together into a single mailstream. Each book maintains its unique, individual attributes.
- **Multi-BLEND** incorporates pre-bound magazines or catalogs with other titles being produced inline. The Multi-Blend process involves an automated portable pocket feeder that rolls up next to the saddle stitcher. Finished books — perfect bound or stitched — are fed after the trimmer and before ink jetting.

It should be noted that a particular type of comailing may not work in every situation or for every publication. There can be challenges related to the size and shape of the publication. Timing of the comail process could create problems for time-sensitive publications. Publications that are individually poly wrapped with multiple inserts could find it difficult to "fit in" a comail process.

Fit is the key word. There may be trade-offs for publishers who want to comail. Sometimes that might involve changing trim sizes and/or production schedules. The publisher has to determine if the savings potential is worth making changes. Our goal has always been to try and create comail processes that will minimize the amount of change required by our clients. In doing so, we have opened up comail opportunities for a larger audience. As comailing has evolved we have been able to overcome many of the aforementioned obstacles. In fact, one of our comail processes involves poly wrapped publications with inserts. That is now one of the fastest growing comail segments. Another one of our processes involves two weekly publications who have been

successfully comailing for almost one year without jeopardizing the timely delivery of their publications.

The ways in which postal costs can be reduced is not limited to comailing. In addition to comailing, we also offer our clients drop shipping. Drop shipping is a service whereby we transport magazines and catalogs as close to their final destination as possible to take advantage of USPS discounts. We have been drop shipping since 1991 when work share discounts were first created for Standard Mail. Prior to that, we had been pool shipping periodical publications to zone skip and deliver closer to their final destination.

100% of our clients participate in our drop ship program. Efficiencies in transportation management and delivery planning allow our clients to reduce their postage costs and better manage their business while ensuring that their catalogs and magazines are handed off to the USPS in time to meet their in-home delivery dates. Drop shipping has become one of the most successful and valuable workshare initiatives for mailers and the Postal Service and we expect that the introduction of editorial pound dropship discounts in the new rate structure will ultimately allow us to expand our dropshipping efforts for high-editorial publications.

There is no debating the fact that we have just experienced the most challenging rate increase in recent history. Many mailers experienced higher increases than had been originally proposed. Periodicals questioned the rationale of the complexity of the new rate structure. As a printer, we were faced with having to explain to our clients what happened and what we were going to do to help them survive. While this was a challenge, it was not unlike what has happened after every rate case that I have been involved with over the last 20+ years. A main reason for that is the rate-making process under the old law. Everything about it created a situation where we all had to react to something that was usually unexpected. In this case, that was taken to the nth degree.

Happily, with the signing of the PAEA we should not have to deal with this unmanageable process in the future. Under the PAEA, rates will increase on a regular, predictable schedule and by smaller amounts than under the old system (e.g., an average CPI-based rate increase for Periodicals, as opposed to the recently-implemented 12 percent increase for Periodicals). And unlike under the old system, the postage rates that the Postal Service files at the PRC will be those that are implemented unless they don't comply with the cap.

We responded to our clients by providing them with as much information as possible on why the Postal Service and Postal Regulatory Commission did what they did. We then proceeded to recommend how they could reduce their postal costs through regional day-long postal seminars. At the same time we were explaining how to reduce postal costs, we were also providing ideas on how they could add value to their catalogs and magazines in order to drive a higher response rate. Then we gave our clients time to digest the information, assess their budgets, and determine if they would adjust their business and mailing strategy for the balance of the year. We then listened to what they intended to do and what they wanted us to do. It became very apparent that more and

more clients wanted to utilize comail as the means to lower costs. The new rate structure in Standard Mail and Periodicals creates even more incentives for comailing. As mentioned earlier, our volumes have substantially increased from 2006. Because of that, we have invested in more comail technology and equipment to meet the capacity needs of our print clients.

It has become apparent to those of us who are immersed in postal affairs that the Postal Service must continue to provide incentives for mailers to prepare the most efficient mail as possible (highly presorted – carrier route; palletized; drop shipped as close to final destination as possible). Since the enactment of postal reform legislation in 2006 requiring the USPS to operate under CPI-based pricing, they need all the help they can get in managing their operational costs. And we need the USPS to continue to provide the incentives to help us recoup our investments in technology, equipment and buildings associated with providing work share discounts to our clients.
I fully expect that going forward we will continue to work with the Postal Service as business partners to do whatever it takes to maintain the concept of "lowest combined costs". Because of PAEA there should be more opportunities than ever before to accomplish that goal. The viability of the printing industry and the USPS is at stake.

Thank you for the opportunity to express our views on this important issue.

Mr. DAVIS OF ILLINOIS. Thank you very much.

We will go to Ms. Pursley.

STATEMENT OF ANITA PURSLEY

Ms. PURSLEY. Good afternoon, Chairman Davis, Congressman McHugh. Thank you very much for this opportunity to testify today.

Quebecor World is the second-largest commercial printing company. We offer products and services to numerous market segments, magazines, catalogs, retail mailings, and within those market segments to small, medium, and large customers. Quebecor World strives continuously to bring high value and lower cost solution sets to the customers we serve in these markets. With that said, I am pleased to present to the subcommittee information about Quebecor World's logistics express collation mailing system [ECMS].

The ECMS system is our version of what is commonly referred to in the mailing industry as a co-mailing system. As you have heard today, co-mailing is one of the few options that short-run publications have that provide them the opportunity to qualify for the same types of postage discounts as larger circulation publications.

As with all successful work sharing programs, we recognize that co-mailing will help many but not all, at least in the short term, publishers mitigate the impact of the most recent postage rate increase.

Additionally, due to the reduction in postal handlings, co-mailing allows magazines to arrive to their subscribers in better condition and in a narrow, more predictable time window.

Although we have been co-mailing longer-run publications since 1998, our ECMS, we began that system program in May 2005 in the Chicago area. In that year, we co-mailed a total of 30 million magazines. The program grew to slightly over 100 million co-mailed magazines in 2006, and we expect to exceed 150 million this year. Today, almost 900 titles participate in our program.

As a result of the new rate structure and increased demand, we recently opened the program to publications that are printed elsewhere, and already 50 publications printed by other companies participate in our program. We expect to see this number grow significantly.

The core of this program, as I said, is the short-run publication market, because these type of publications have the most to gain. For example, co-mailing gets mail out of sacks and onto pallets, while larger publications generally can palletize on their own.

Given this focus, the average size of publications in our program is approximately 30,000 copies, and has actually dropped each year as our program has expanded.

In response to this demand, and in order to meet the needs of even smaller publishers, we recently reduced the minimum to as few as 5,000 copies per issue, and we have also tailored the program to be extremely user friendly.

Two key aspects of the program are timeliness and flexibility. To ensure timely delivery, we typically run four co-mail pools for magazines each week, with one always beginning on a Monday. This

ensures that magazines do not sit at the plant waiting for the next pool.

Our experience has shown that for most publications the time required to co-mail a publication is more than offset by the delivery improvements that result from entry of co-mail publications deeper into the postal network.

To allow publishers scheduling flexibility, we allow them to move publications in and out of the program from one issue to the next without penalty and with only 72 hours of notice. Similarly, they can move from one pool to another with only 36 hours notice.

Publishers simply need to provide us with their mailing lists 3 days prior to the start of a co-mail pool, and the actual magazines 1 day prior to the startup.

Quebecor World Logistics recently announced plans to significantly expand our co-mail operations to meet this increased demand. To better service the non-Quebecor World print marketplace, we are moving into a new and larger consolidation facility in the northeast in 2008. This expansion will allow us to serve a broader spectrum of publications. And, unlike some previous co-mailers, the new generation of equipment that we would begin deploying in 2008 can process poly wrapped and tabloid-sized publications.

The first two machines will be deployed into this facility, and we have agreements in place to purchase an additional four machines. This added capacity in the northeast will allow us to serve additional customers and plants in this region.

In closing, I would like to add that Quebecor World does not support rate increases of this overall magnitude for any class of mail, but supports a rate structure that promotes efficiently prepared mail and reduces overall USPS processing costs.

Moving forward, we fully expect that PAEA's rate indexing system will prevent such large rate increases in the future, while allowing the Postal Service to encourage efficient preparation. We also recognize that no single solution will satisfy all market segments or customer sizes. But we are committed to invest as appropriate to allow our customers to take advantage of whatever rate structure is in place.

Thank you very much. I would be happy to answer any questions.

[The prepared statement of Ms. Pursley follows:]

STATEMENT OF ANITA PURSLEY
VICE PRESIDENT, POSTAL AFFAIRS
QUEBECOR WORLD LOGISTICS

SUBCOMMITTEE
ON FEDERAL WORKFORCE, POSTAL SERVICE
AND THE DISTRICT OF COLUMBIA
COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM
U.S. HOUSE OF REPRESENTATIVES

OCTOBER 3, 2007

Good afternoon, Mr. Chairman and members of the Subcommittee. My name is Anita Pursley. I am Vice President of Postal Affairs for Quebecor World Logistics. In this capacity, I am responsible for establishing corporate postal policy and am the primary liaison with the Postal Service on all matters affecting Quebecor World and its customers. I am also the Vice Chair-Elect of the Postmaster General's Mailers' Technical Advisory Committee (MTAC), which provides a venue for the Postal Service to share technical information with mailers and to receive advice and recommendations from the mailing industry.

Quebecor World Inc. is a large printing solutions provider offering products and services to numerous market segments (magazines, catalogs, retail mailings) and within those market segments to small, medium and large customers. Quebecor World strives continuously to bring high value and lower cost solution sets to the customers we serve in these markets. With that said, I am pleased to present to this Subcommittee information about Quebecor World Logistics' Express Collation Mailing System (referred to as ECMS), which we make available not only to our own print customers, but also to publications and Standard Mail flats that are printed elsewhere. I will start by providing some background on our program. Then, I will discuss some recently-announced enhancements that will allow additional publishers to participate.

The Express Collation Mailing System is our version of what is commonly referred to in the mailing industry as a "co-mailing" system. Co-mailing is a process that merges multiple publications into a single, efficient mailing that is highly presorted; prepared on pallets; and enables entry deep into the postal network. Co-mailing is one of the few options that short-run publications have that provides them the opportunity to qualify for the same types of postage discounts as larger-circulation publications.

As with all successful worksharing programs, we recognize that co-mailing will help many, but not all (at least in the short term), publishers mitigate the impact of the most recent postage rate increase. Additionally, due to the reduction in postal handlings, co-mailing allows magazines to arrive to their subscribers in better condition and in a narrower and more predictable time window.

Quebecor World initiated the Express Collation Mailing System in May 2005 in Bolingbrook, IL, near Chicago. In that year, we co-mailed a total of 30 million magazines. The program grew to slightly over 100 million co-mailed magazines in 2006 and we expect to exceed 150 million this year. Today, almost 900 titles participate in our ECMS program. As a result of the new rate structure and increased demand, we recently opened the program to publications printed elsewhere and already fifty publications printed by other companies participate in our program. We expect this number to increase significantly.

The core of our program is short-run publications because these types of publications have the most to gain. For example, co-mailing gets their mail out of sacks and onto pallets while larger publications generally can be palletized on their own. Given this focus, the average size of publications in our program is approximately 30,000 copies and has actually dropped each year as our program has expanded. In response to the demand and in order to meet the needs of even smaller publishers, we recently reduced our minimum to as few as 5,000 copies per issue and have tailored the program to be extremely user-friendly.

Two key aspects of our program are timeliness and flexibility. To ensure timely delivery, we typically run four co-mail pools for magazines each week with one always beginning on a Monday. This ensures that magazines do not sit at our plant waiting for the next pool. Our experience has shown that, for most publications, the time required to co-mail a publication is more than offset by the delivery improvements that result from Quebecor World's entry of co-mailed publications deep into the postal network.

To allow publishers scheduling flexibility, we allow them to move publications in and out of our program from one issue to the next with no penalty and with only 72 hours of notice. Similarly, they can move from one pool to another with only 36 hours notice. Publishers simply need to provide us with their mailing lists three days prior to the start of the comail pool and their magazines one day prior to the start of the pool.

Quebecor World Logistics recently announced plans to significantly expand our co-mailing operations to meet the increased demand for these services and to bring optimized solution sets to our customers. To better service the non-Quebecor World print marketplace, we are moving into a new and larger consolidation facility and co-mail center in the Northeast by early 2008. This expansion will allow us to serve a broader spectrum of publications. Unlike some previous co-mailers, the new generation of equipment that we will begin deploying in early 2008 can process polywrapped and tabloid-sized magazines. The first two machines will be deployed into this new facility and we have agreements in place to purchase an additional 4 machines. This added capacity in the Northeast will allow us to serve additional customers and plants in this region as well as more publications that are printed elsewhere.

Finally, while I believe that the recently introduced Periodicals rates will encourage more efficient mail preparation throughout the mailing industry, I'd be remiss if I didn't point out one problematic, and likely unintended, aspect of the new rates. In an attempt to mitigate the impact of its rate recommendation, the Commission set the new container charges at much less than the Postal Service costs for handling these containers. This had the effect of reducing the incentive to dropship Periodicals deep into the postal network. This will reduce the amount of Periodicals

that is dropshipped and ultimately increase Postal Service costs. I strongly encourage the Postal Service to address this problem the next time that it adjusts Periodical rates.

In closing, I would like to add that Quebecor World does not support rate increases of this overall magnitude for any class of mail but supports a rate structure that promotes efficiently prepared mail and reduces overall USPS processing costs. Moving forward, we fully expect that the PAEA's rate indexing system will prevent such large rate increases in the future while allowing the Postal Service to encourage efficient preparation. We also recognize that no single solution will satisfy all market segments and customer sizes. We are committed to invest as appropriate to allow our customers to take advantage of whatever rate structure is in place.

Thank you for your time and your interest. I would be happy to answer any questions you may have.

Mr. DAVIS OF ILLINOIS. Thank you very much.

We will go to Mr. Cerasale.

STATEMENT OF JERRY CERASALE

Mr. CERASALE. Mr. Chairman, Mr. McHugh, it is a pleasure to have the opportunity to testify before you on this important subject.

I want to first take a minute to personally from the DMA thank the chairman for taking time out of his busy schedule to attend our conference and meet DMA members in the beautiful facility in the wonderful city of Chicago located in your District, Mr. Chairman. Thank you.

The DMA is a premier association of direct marketers using all channels of communications, but the mail is still a very, very important channel to our members.

I want to look at just four categories of mail today, not a periodicals—that has already been taken—but looking at standard mail flats, first class mail flats, standard mail parcels, and standard mail not flat machinables.

All of them received rate increases, which will have affect on volumes and affect decisions of those mailers who mail in those classes and subclasses of mail.

Looking at standard mail, since 1990 the Postal Service began moving rates in standard mail to reflect the cost differences between handling letter-shaped mail and flat-shaped mail. They started to do that gradually, little step at a time, to avoid rate shock, to eventually reach that goal.

In this last rate decision, the Postal Regulatory Commission [PRC]—and I really have to thank all of you for changing the name from the Postal Rate Commission to the Postal Regulatory Commission, keeping the abbreviation PRC the same for old guys like me. But the PRC jumped immediately to full recognition of the cost differential between handling letters and flat-shaped mail.

It is too early to tell right now what the full impact is of that on volume to the Postal Service. We do not know the impact of how much more volume there will be in letter-shaped mail than that proposed by the Postal Service, nor are we fully aware of the full impact of a 20 to 40 percent increase in flat-shaped mail, including most of the catalogs.

The DMA believes that the PRC over-estimated the conversion of flat-shaped mail to letter-shaped mail to try and avoid that huge rate increase. As in my written testimony, for catalogers it takes a great deal of lead time to produce a catalog. You have to determine what you will order. You have to order those products. The products have to be created, delivered to the cataloger, put in the warehouse, and then sold through the catalog. So by the time the rate increases went into effect in May, the holiday season ordering was already in effect, and the size of the catalogs was likely already locked into place, since they had the products that they were going to try to sell already on order.

So what is happening? What is this causing these flat-shaped mailers to do? They are looking at co-mailing, commingling, and, more importantly, they are looking to a more rapid change to the

Internet. I attended a conference of catalogers, and over half of the programming was on Internet marketing.

That is what is happening a little bit in standard mail.

Looking at first class mail flats, we see a greater conversion of first class mail. First class mailers are able to fold their flat-shaped mail and put it in letter-shaped pieces, so we are seeing less of an impact of the 20 percent increase on first class flats because they can convert more easily.

Looking at standard parcels, a very small part of the standard mail stream, we see the 40 percent increase, far below the increase that was requested by the Postal Service. I think that the fear going forward is for standard parcels, Will the Postal Service go forward and really raise the rates here? We want to work hard with them to try and not have that happen to destroy standard parcels.

Finally, not flat machinables. What are those? A good example are non-profits sending out premiums such as pens or pins. They had a rate increase of 200 plus percent, some of them. They have virtually been priced out of existence, to the detriment of some of our non-profit mailers who have those pins and pens on inventory. They are just no longer there. This is a type of mail that is gone due to the rate increases.

So what do you do? What is the solution here to try and take a look at these disparate things? I think you created that solution with the postal reform. We have to let it work. We have to give the Postal Service the opportunity to look at the market impact of rate increases and take into account volume changes caused by the PRC recommendation, take into account the cost of paper that is dramatically rising, especially coated paper. Take a look at the new machines, the new equipment for sorting letters and flats. And, finally, hopefully, some changes allowing mailers to commingle and co-mail different classes of mail, so periodicals and catalogs can go together.

Fortunately, yesterday the PRC promulgated rules to implement the reform, and we hope with that act that the old rate system is now gone forever.

Thank you.

[The prepared statement of Mr. Cerasale follows:]

BEFORE THE

COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM
SUBCOMMITTEE ON FEDERAL WORKFORCE, POSTAL SERVICE, AND THE DISTRICT OF COLUMBIA
UNITED STATES HOUSE OF REPRESENTATIVES

HEARING ON

EFFECTS OF THE 2007 POSTAGE CHANGES ON MAILERS

OCTOBER 3, 2007

TESTIMONY OF

JERRY CERASALE
SENIOR VICE PRESIDENT, GOVERNMENT AFFAIRS

DIRECT MARKETING ASSOCIATION, INC.

Jerry Cerasale
Senior Vice President, Government Affairs
Direct Marketing Association, Inc.
1615 L Street, NW Suite 1100
Washington, DC 20036
202/861-2423

Good afternoon Mr. Chairman and members of the Subcommittee. I am Jerry Cerasale, Senior Vice President for Government Affairs of the Direct Marketing Association, and I thank you for the opportunity to appear before you as you examine the effects of the most recent postage changes on mailers.

The Direct Marketing Association, Inc. (DMA) is the leading global trade association of businesses and nonprofit organizations using and supporting multichannel direct marketing tools and techniques. DMA advocates industry standards for responsible marketing, promotes relevance as the key to reaching consumers with desirable offers, and provides cutting-edge research, education, and networking opportunities to improve results throughout the end-to-end direct marketing process. Founded in 1917, DMA today represents more than 3,600 companies from dozens of vertical industries in the U.S. and 50 other nations, including a majority of the Fortune 100 companies, as well as nonprofit organizations. Included are catalogers, financial services, book and magazine publishers, retail stores, industrial manufacturers, Internet-based businesses, and a host of other segments, as well as the service industries that support them.

DMA and our members appreciate this Subcommittee's continued outreach to the business community on important issues involving the Postal Service. Mailers depend upon reliable and affordable postal services, and it is important for this Subcommittee to examine the effects of the most recent postage increases on mailers.

Every postal rate change affects the mailers' decisions—how much mail—what mix of mail—what mix of communication channels. The Postal Service's shift to shape-based rates coupled with the greater than requested and anticipated postage increases for flat-shaped mail created an almost untenable situation for many businesses in the mailing community. I would like to discuss four specific postage changes:

- Standard Mail flats
- First-Class Mail flats
- Standard Mail parcels
- Standard Mail not flat machinables

Flat-shaped mail

In 1990 the Postal Service began implementation of a postal rate design to reflect differences in handling, transporting and delivering between letter-shaped and flat-shaped mail in First- Class and Standard Mail.[1] As required by the Postal Reorganization Act, both the Postal Service and the Postal Rate Commission designed rates to mitigate the impact of rate increases on flat-shaped mail—they began a gradual shift in rates that would eventually fully reflect the handling differences. In the last rate case, the Postal Service's proposed increases continued that gradual shift. However, the Postal Regulatory Commission (PRC) abandoned the mitigation approach and recommended rates that reflected the full differential.[2] Those increases were implemented on May 14, 2007. This resulted in rate increases double or more than those proposed by the Service—approximately 20% for First-Class flats and 20% to 40% for Standard Mail flats. Certain nonprofit members of DMA faced greater than 50% increases in postage with the May 14 rates. Increases of that magnitude have significant impact on mailers.

Standard Mail

The PRC recommended letter-shaped mail postage rates lower than those proposed by the Postal Service. We do not have data on the expected positive volume effect due to the lower than proposed postage increases for letter mail. It is important to note that letter-shaped mail accounts for approximately 75% of Standard Mail volume and 67% of Standard Mail revenue. We should demand more up-to-date data from the Postal Service to understand the effects on letter-shaped mail volume. We do know, however, that since 1999 immediately following postage increases, Standard Mail

[1] Standard Mail is bulk identical pieces of mail weighing less than 1 pound. It receives no free forwarding, is not sealed against inspection, is not transported by air, must be presorted and have postage paid that does not require cancelling. First-Class Mail is sealed against inspection, transported by air, receives free forwarding, may have postage paid by stamps requiring cancellation, need not be presorted, and need not be part of a bulk mailing. Flat-shaped mail is mail greater than 6.25 inches by 11.5 inches with a thickness no greater than 1.25 inches.

[2] Both the rates that the Postal Service proposed and the rates that the Postal Regulatory Commission recommended had flat-shaped mail and letter-shaped mail in First- and Standard Mail covering their costs.

volume continued to rise albeit less than it would have without the increase. Sadly, that is NOT the case after this postage increase. Standard Mail volume is down almost 1%. This is problematic for the Postal Service since Standard Mail has been its growth generator.

DMA members have written to the Governors of the Postal Service showing their planned adjustments in mailings due to fixed budgets and greater than expected flat-shaped postage. Our catalog members are compelled to reduce volume an additional 10% to 15% reduction in the number of pieces mailed based on the additional increases over the Postal Service's proposed rates. The loss of that catalog mail will result in a loss of orders and a resulting loss of additional mail. It has been estimated that every order generates an additional 21 pieces of mail. All that will be lost.

As a result, DMA members are examining all avenues to reduce postage costs. There is far greater interest in co-mailing and commingling catalog mail. Those efforts will help mitigate the huge rate increase catalogers face. But catalogers are looking elsewhere as well. I recently attended the Fall Conference of the New England Mail Order Association. Over one-half of the conference programming was focused on the Internet and Web site development. The rate increase has accelerated the shift away from paper communications—not a good omen for the Postal Service's only significantly growing class of mail.[3]

Catalogers are not the only mailers of Standard flats. A DMA member that publishes a weekly newsletter, mailed First-Class, has used a Standard Mail flat for its promotion. Anticipating greater increases on flat-shaped mail than letter-shaped mail, the publication changed its promotion piece to letter-shaped. The response was SIGNIFICANTLY lower than the historic flat-shaped promotion. For each newsletter subscription lost there was a loss to the Postal Service of 52 First-Class Mail pieces—the law of unintended consequences at work.

The PRC assumed in its recommendation that many flat-shaped mailers would change the shape of their mail pieces to letter-shaped (6 inches by 11 inches by ¼ inch is still a letter). That has not occurred in Standard Mail to any significant extent. The shape

[3] In the latest budget for the Postal Service, Standard Mail is the only class for which the Service estimates a growth in mail volume.

of a mail piece is determined by many factors—not simply postage. Response of customers is a major factor as shown in the newsletter example above. ¼ inch may not allow enough pages to show all the product offered. Letter-shaped catalogs must be tabbed to allow them to be processed on letter sorting equipment—an additional expense and historically a barrier to customer response. Furthermore, DMA and mailers have heard that the 6 by 11 letters, "slim jims" may not be as compatible with letter sorting equipment as thought. There are expectations that slim jims may be considered flat-shaped mail next time around. This is causing mailers to wait and see before making any change. As DMA explained to both the PRC and the Governors of the Postal Service, the PRC assumed migration to letters will not materialize as estimated; rather, volume will be lost and along with it much needed revenue. As explained in filings, DMA believes that the revenues for Standard Mail estimated by the PRC will not be realized.

In addition, a catalog company has a significant lead time before a catalog is produced and mailed. Product to be sold *via* the catalog must be chosen, then purchased, then produced, then shipped to the cataloger in time for sales generated by the catalog. Once the products to be offered in the catalog are ordered, the size of that catalog, for all practical purposes, is set. Purchase decisions for the holiday season were well underway by May 14, when these rates became effective. Thus, the full effect of the rate increase on catalog volume has yet to be felt. The Subcommittee should continue its examination beyond today.

The effect of the rate increase on the nonprofit community, particularly on one veteran group, was devastating. Donations from their flat-shaped promotions have fallen because the charity could not afford to mail as many pieces as planned. At a time of war this rate increase has not helped the veteran beneficiaries.

Finally, some collateral effects of the Standard flat increase are being felt. Non profit mailers indicate that the number of prospect donors on lists is declining since there are fewer catalogs being mailed and thus there are fewer catalog customers. This phenomenon will only increase as the full effect of the increase is felt after the holiday mailing season.

First-Class flats

Unlike our observations for Standard Mail, it appears that many flat-shaped First-Class mailers are converting their pieces to letter-shaped. Sales for 9 by 11 envelops is down significantly, but sales for 6 by 9 envelops have grown. This suggests that mailers may be folding flat-shaped pieces to fit into a 6 by 9 envelop. From our information the effects of the flat-shaped postage increases on First-Class Mail are less severe than for Standard Mail.

Standard Mail parcels

Standard Mail parcels, bulk parcels weighing less than 1 pound, had postage increases of 40%.[4] DMA members had to pass these increases to their customers and are seeing a reduction in orders. This, in turn, reduces the number of promotional pieces of mail sent as mailing lists of customers shrink. Parcel shippers are examining different packaging to try to shift from parcels to flats. DMA expects to see significant long-term reductions in this mail as customers decline to pay higher shipping costs for products ordered—the items are removed from the shopping cart.

Not flat machinables

The postage for not flat machinables for non profit members of DMA increased 100% to 200% and more. The inclusion of a small premium (a pen or pin, for example) in a donation request mail solicitation has virtually ended. DMA nonprofit members were left with significant inventory of premiums that are now too costly to mail.[5] One charitable organization planned to mail almost 8 million donation solicitations with premiums enclosed in 2008. The current plan is to mail 100,000 such pieces. The ancillary effect again will be a reduction in the number of prospective donors on mailing

[4] The 40% increase recommended by the PRC was significantly less than the increase proposed by the Postal Service.
[5] DMA and its DMA Non Profit Federation asked the Board of Governors to delay until December 31, 2007 the increase for not flat machinables to allow non profits to draw down their premium inventory. Sadly, that request was rejected.

lists. It appears to DMA that the Postal Service wanted to end this type of mail, and the PRC agreed.

Solution

The solution available is to avoid an "old law" rate case that produced the current rates. Do not allow that to happen. Any future rate change should be under the provisions of the Postal Accountability and Enhancement Act which gives the Postal Service flexibility to establish postal rates as the market demands. The Service must balance the effects of increases on all shapes of mail and must protect the growth of Standard Mail which will generate mail volume in all other classes. Under that Act, the Service should consider the volume disruptions, if any, caused by the May 14th rates. Hopefully, the Service will account for the pending spike in coated paper prices that will dramatically affect catalogs and magazines when establishing rates under the new law. The new investment into sorting equipment for letters, flats and parcels and any expected productivity improvements should be an integral part of any future rate changes. Strict adherence to short-term cost of service pricing is not in the best interest of mailers, Postal Service and the American public. We need the new law to work, and DMA asks this Subcommittee use all available tools at its disposal to insure that the next postal rate changes are accomplished under the provisions of the Postal Accountability and Enhancement Act.

DMA thanks the Subcommittee for allowing it to present its views at this hearing. I will be happy to answer any questions you may have for me.

Mr. DAVIS OF ILLINOIS. Thank you all very much. We have just two votes. We are about 5 minutes away from the first one, and the next one is a 5-minute vote. That means that we have to be gone about 10 minutes, 12 at the most. I do have some questions I would like to ask, so if you could remain I would really appreciate it.

Thank you very much.

[Recess.]

Mr. DAVIS OF ILLINOIS. Thank you all so much. We will resume.

Why don't I begin, Mr. O'Brien, what would you say to those mailers who blamed Time Warner for the rate increase? I mean, they say Time Warner gave us this rate increase.

Mr. O'BRIEN. Well, I think, Mr. Chairman, they should first take a look at that graph. It is not Time Warner, it is the industry that for many, many years we as an industry allowed inefficiency to come into the process and we drove up the costs. That example that I gave you earlier about a sack costing $5 or $6 and only containing $1.50 worth of revenue really happens.

So we were driving up the cost. It costs the Postal Service a lot of money to process these things, and we turned a blind eye to it.

I think the other thing that has happened is, to be honest, we magazine publishers are junkies and we got hooked on a number of bad practices, one of which was a discount for bar-coded copies at the five-digit level. The discount was 899 percent above what the Postal Service's cost savings were. So you are giving away much more money than you are actually saving by the value of that discount.

So what is wrong with this picture? We are all junkies. We all got hooked on that discount. It was reduced in this case back to only giving away 100 percent of what the Postal Service saves instead of 899 percent. That is one thing that was out there.

Time Warner had nothing to do with that discount getting put back to where it should have been all along.

Another thing that happened in this case was that the Postal Service recommended a shift from pounds to pieces, moving cost away from pounds to pieces, so, as you heard some of the earlier witnesses say, I have a lightweight publication and we got hit harder. That wasn't Time Warner's doing; that was a result of a proposal by the Postal Service to shift from pounds to pieces. All lightweight pieces got hit, including our publications.

The whole idea behind these rates, Mr. Chairman, was not to put publishers out of business. We are as strong a proponent of the first amendment rights as anyone. We own CNN. We own Time Magazine. We want news. We want information to get put out to the public. But I think at the same time we want mailers to change their behavior to try and become more efficient.

I thought it was kind of interesting earlier that Mr. Zipser said we are doing all kinds of things to try and offset this increase. That is exactly what was supposed to happen as a result of this proposal. Mailers were supposed to change their mailing behavior, not go out of business.

So for everyone that comes up and tells you I am getting hit with a 20 percent or 30 percent or 40 percent increase, you have to take that with a little bit of a grain of salt because they haven't tried

to do what Mr. White is doing with his weekly publication or what Mr. Schick and Ms. Pursley are doing for their customers in trying to make them become more efficient.

See what their rate increases are after they change their behavior, and I think you will get a completely different picture.

Mr. DAVIS OF ILLINOIS. So you are saying that it is a matter that the industry took a good look and decided, in a sense, to propose what you consider to be in the best interest of the industry, as well as the best interest of the Postal Service?

Mr. O'BRIEN. Yes, Mr. Chairman. You know, this task force that we were on took place in 1998, 9 years ago. Big mailers, small mailers. Mr. Straus, one of your earlier witnesses, was on that task force right alongside me at every one of those postal facilities. We all looked at everything that was out there, and we came to the conclusion that there were 15 things that the Postal Service needed to change, and one of them was to have the rate structure get more closely aligned with the costs.

We as an industry said that 9 years ago. The Postal Service didn't take action. It was incumbent upon the industry to take action. And yes, we had the courage to step forward and take that fight on on behalf of the industry, but I think it is for the long-term survival of the industry. Yes, there is short-term pain until people change their mailing behavior, but once that is done I think in the long term you are going to see an effect on that curve, on that red curve, because if we don't change that, the Postal Service will never be able to meet the requirements of the new law to keep periodicals class cost below the rate of inflation. It won't happen.

Mr. DAVIS OF ILLINOIS. Thank you very much.

Mr. O'BRIEN. Thank you.

Mr. DAVIS OF ILLINOIS. At this point let me ask you, have you noticed any changes, new trends with your publication, since the new rates have gone into effect?

Mr. WHITE. You mean in our own mailing behavior?

Mr. DAVIS OF ILLINOIS. Yes.

Mr. WHITE. Yes. We are doing many of the things, but I think it helped us to be able to co-bind all of our magazines. Before we were only co-binding most of them. It clearly increased the incentives for potential co-binding partners. We have changed some of the rules that we used for pre-sorting to try to avoid sacks and to create more efficient pallets.

I think more broadly, industry-wide, certainly there are a lot of people looking at things like co-mail again, and our message to printers has been co-mail or no mail. Either figure out how to help your customers minimize their postal cost or get out of the business of printing stuff that is mailed. That is a necessary part of the business, as these folks have pointed out.

Mr. DAVIS OF ILLINOIS. Ms. Pursley, let me ask you, have you noticed any change, trends, since the new rates were implemented?

Ms. PURSLEY. Well, it is very, very obvious in our operation. Our co-mail facility has just exploded, the demand. The customers are knocking down the doors. We are, as I mentioned in my testimony, expanding the program to not only offer our northeast customers co-mail operations or co-mail offerings, but also to non-Quebecor World print customers. Many of our customers now are other print-

ing companies that may not be able to invest in co-mail equipment and make the return on the investment necessary in order to make it successful as a small printing company. So we are working in tandem.

It is very, very impressive how our program has grown significantly just in the last 2 to 3 years.

Mr. DAVIS OF ILLINOIS. Would you suggest that efforts to educate the members has had that kind of impact to be more efficient or to find more efficient ways of mailing?

Ms. PURSLEY. Educating those customers? Definitely. I mean, it is an education process, because co-mailing doesn't work for everybody and a customer may have to make a few changes in their existing practices, but you can make it work. I mean, there are a lot of options. As with every rate case, we have customers who come to us and say, What is it that we can do to lower our postage costs? Many times it is suggestions such as lowering paper weights or reducing trim size. It is no different in a co-mail environment where we may be suggesting slight operational changes for them to be able to participate. But overall it is working very successfully.

Mr. DAVIS OF ILLINOIS. Thank you.

Mr. Schick, what efforts have you made to help your customers take advantage of more of the discounts in standard mail?

Mr. SCHICK. Well, Mr. Chairman, I think I will concur with Anita's comments on trying to get more of our catalog customers to look at co-mailing. I can tell you that this year over last we have already seen about a 75 percent increase in the volume just in standard mail catalogs that are currently taking the opportunities to do some kind of co-mailing.

But we actually went back to our customers when we saw what the rates were going to be and said, Let's start from the beginning. Let's focus first of all on your mailing list. Let's ensure that you are mailing to the right people. Let's ensure that you have good addresses, because there are opportunities to save some money on that side of the business, and then that savings just kind of compounds going forward because you are able to do so many more things without adding some cost.

Likewise, if you don't do those things up front to ensure that you are mailing good addresses, you are just adding cost as it gets piled on through the process.

So we took that approach, then we also said let's look at our transportation planning and distribution to see where we can take better advantage of some of the transportation efficiencies and opportunities for additional drop shipping.

Then, while we were doing that, we were also focusing on helping them with their response rates, and looking at the technology that we have available to them to help them target their customers better so that they can raise the rate of response. By the time you raise the response rates and get more sales and reduce your costs a little bit, at the end of the day you are able to manage those overall costs pretty well. I think we have seen a lot more customers with open eyes taking advantage of all those different processes.

Mr. DAVIS OF ILLINOIS. Thank you.

Mr. Cerasale, as you know, the PAE makes it considerably easier for the Postal Service to engage in pricing experiments. Can you

describe for the committee one or two experiments that you would like to see the Postal Service try?

Mr. CERASALE. I think the first one is the one I mentioned, could happen relatively quickly, is to allow commingling of more than one class of mail. As Mr. Schick talked about, catalog mailers going in and commingling, we can take the smaller publications and put them on those pallets as well and kind of reduce those costs. So I think that is one that can go fairly quickly and one that would have a great impact on helping especially the smaller mailers and the lighter weight mailers, the ones who were hit most hard in this past rate case, both in periodical class and in standard mail.

I think the push toward having mail, it started with the NSA from Bank of America, which is still a question as to whether or not that will be approved, but the idea of moving forward to try and get what the Postmaster General explained, the intelligent bar code forward, to try and really cut costs out of the system.

One of the things that has been delayed is when everyone will be required to use the intelligent bar code. It may be time to, through the NSA, through maybe experiments, to try and push more and more mailers to start using the intelligent bar code and see what savings we can have here, what other offerings can come off of it, including potential of being able to help mailers target mail better and get a better rate of return. So I think that is an area where the Postal Service should probably look at quickly, as well.

Mr. DAVIS OF ILLINOIS. Well, thank you very much. Let me ask one last question that any of you might answer. In our last panel we had some discussion of privatization. Would any of you characterize privatization as perhaps a better way to deal with the issues and problems that we have discussed?

Mr. O'BRIEN. Mr. Chairman, I have some experience in this area. I used to be CEO of a company called Publishers Express that competed with the U.S. Postal Service for delivery of magazines and catalogs, and we were in business from 1989 until 1996. During that period of time, we took the business from two zip codes in Atlanta to 1,000 zip codes in 36 cities throughout the United States.

The way that we did the business was we licensed our business to local newspapers, and when they were delivering their saturation products that would go to every household in a zip code, those carriers would deliver magazines and catalogs along with them.

What we found, we were in business for that period of time. We made money exactly 1 month. We were in business 6 years and made money 1 month, so it is a tough business. The quality of delivery is suspect. I know it was kind of funny because I was running this company and yet Time, Inc.'s magazines were some of the customers. What we found was that our level of quality for the private delivery was 10 times worse. We received 10 times more complaints in the zip codes where Publishers Express existed.

So it was very, very difficult because we were using part-timers. We were not allowed mailbox access, so we had to hang magazines and catalogs in a little plastic bag on a door knob. Because people were part time, sometimes they delivered, sometimes they didn't. We had problems with consumers saying I don't want this, I want

the product in my mailbox, put me back the other way, put me back in the Postal Service. We had to honor those requests.

So privatization may be held out as a panacea here. I can tell you from personal experience it is a very, very difficult business.

Mr. DAVIS OF ILLINOIS. Thank you very much.

Anyone else care to comment?

Mr. CERASALE. Yes. The mail represents $900 billion a year in economic impact. Unlike some of the experiments that are going on in Europe where privacy laws really diminish the amount of advertising mail that can be put into the system, the United States, with its economic model, mail volume, mail advertising is thriving. It is growing faster than the growth of the economy, as a whole, so it is continually growing in that kind of a view, even in the face of the Internet.

I think it is a little bit premature to take a look at privatization now. You really have to look at the postal reform legislation and see how this works. We have to give it an opportunity to work, and if it fails for some reason then we might start to look at it.

Also, I think we are seeing in Europe just there still is a vestige of part of a monopoly in the European systems, and they are moving now to get rid of that. It is probably time to take a look and see. If you want to look at Europe, you have to wait and see what happens when it is really, truly privatized, understanding that they are not as mail centric as the United States is, with the type of the economy that we have.

Mr. O'BRIEN. Mr. Chairman, just one followup to that. I second what Jerry says. The thing that killed Publishers Express was mailbox access, that we could not deliver to the mailbox. The other thing that you ought to think about is the fact that the new law just went into effect in 2006, and I think we need to let that play out.

But I do say that if you ever elect to look at this, private delivery will not survive without mailbox access. There is a tradeoff there with the American public. A lot of people say, I get my retirement checks in the mail. I don't want anyone else's hands going into that mailbox. There are very, very difficult issues that need to be wrestled with.

So I would say let the new law play out, and if it doesn't play out in a number of years down the road, then maybe we would consider that, but it has to go hand-in-hand with the mailbox.

Mr. DAVIS OF ILLINOIS. All right.

Mr. SCHICK. I would just make one other comment, and that is, from a business perspective, when you look at the environment the Postal Service works in today where they deliver to every address 6 days a week, with diminishing revenues in each of those delivery points, there isn't a business out there that would ever want to do that. So without changes to the requirements of how many days you deliver and how many times you have to go to each household, or without the opportunity to surcharge, as the competitors of the Postal Service do, I really don't see that being a viable thing at this time.

I also believe that the Postal Service's last mile delivery is their bread and butter, and it is what is really of value. As long as we as an industry can continue to work with the Postal Service to de-

velop work sharing opportunities so that we can cut some of the costs out of the Postal Service's processing network, their delivery still is the best delivery and I wouldn't want to see that go away any time soon.

Mr. DAVIS OF ILLINOIS. Well, thank you all so very much. It has been a pleasure. We certainly appreciate your patience and endurance.

Jerry, let me just say it was good to see you and other members of the Direct Marketing Association in Chicago. If you ever want to come back, the city is yours.

Mr. CERASALE. Thank you.

[Whereupon, at 2:30 p.m., the subcommittee was adjourned.]

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