

MINUTES

Time: 8:30 am PST

Date: April 4, 2003

Location: Westin Hotel at Los Angeles Airport
Los Angeles, California

Members in Attendance: Co-Chairs James A. Johnson and Harry J. Pearce, Commissioners Dionel Aviles, Carolyn Gallagher, Richard Levin, and Joseph Wright.

Staff in Attendance: Executive Director Dennis Shea, Randall Lewis, James Cox, and Jana Sinclair White.

Agency Employees in Attendance: Designated Federal Official Roger Kodat.

Members of the Public Providing Oral or Written Statements: Patrick R. Donahoe, Chief Operating Officer and Executive Vice President, USPS; Anita J. Bizzotto, Chief Marketing Officer and Senior Vice President, USPS; A. Keith Strange, Vice President, Supply Management, USPS; David Rebholz, Executive Vice President, Operations and Systems Support, FedEx Express; Richard Corrado, Senior Vice President of Marketing, Airborne Express; Robert Matheson, President, National Star Route Contractors Association; John Campanelli, President, RR Donnelley Logistics; Sudhir Aggarwal, Chief Executive Officer of Ancora Capital, on behalf of the National Association of Presort Mailers; Steve D. LeNoir, National President, National League of Postmasters; Ken McBride, President, Stamps.com; Gary B. Pruitt, Chairman and Chief Executive Officer, The McClatchy Company, on behalf of the Newspaper Association of America; Brian Spindel, Vice President, PostNet Postal and Business Centers, on behalf of the Mail and Parcel Industry; Ken McEldowney, Executive Director, Consumer Action.

Matters Discussed:

Co-Chair Harry J. Pearce called the meeting to order at 8:30 am. Mr. Pearce noted that the focus of the meeting was the role of the private sector in the mail processing and delivery system. He thanked the witnesses for testifying before the Commission. He noted that this was the Commission's second "field" hearing and that the Commission chose to have three meetings outside of Washington in order to hear from concerned citizens and constituents who have an interest in the Postal Service. The meeting continued with remarks by Co-Chair James A. Johnson.

Mr. Johnson discussed the agenda for the meeting and reviewed each panel of witnesses. He also announced that members of the audience would have an opportunity to share their views with the Commission at the end of the meeting. The meeting continued with remarks by Commissioner Joseph Wright, Chair of the Private-Sector Partnership Subcommittee.

Remarks by Commissioner Joseph Wright

Mr. Wright provided a brief description of the Private-Sector Partnership Subcommittee's activities to date, noting that it had convened twice by conference call, had reviewed materials, had been briefed by the Postal Service, and had met individually with private parties. He also noted that the Commission had requested and received a paper prepared by RR Donnelley that details its analysis of the potential savings that would be available to the Postal Service if it were to outsource much of its "upstream" activities. He emphasized that the subcommittee had not reached any conclusions thus far. Mr. Wright stated that the subcommittee has been exploring how private-sector partnerships impact the Postal Service's bottom line and whether the use of such partnerships should be expanded or reduced. He also stated that the subcommittee is examining existing partnerships with the private sector and considering what lessons the Commission can draw from these alliances.

Panel One: The Postal Service Perspective - Overview of Outsourcing, Purchasing, and Worksharing

Testifying on this panel were Patrick R. Donahoe, Anita J. Bizzotto, and A. Keith Strange. Please see attachments A, B, and C for the text of their prepared written comments.

Questions for Mr. Donahoe: When asked to define universal service, Mr. Donahoe stated that he would define universal service as service six days a week to every location in the country. He elaborated that his definition would apply to all classes of mail, including parcels. He noted that dropping one day of service would save the Postal Service between \$1.7 billion and \$1.9 billion annually. He also noted that the Postal Service, as the service provider, should not suggest limits on universal service, but rather the scope of service is a public policy issue for Congress to decide. Regarding consumer access to postal services, Mr. Donahoe stated that the Postal Service defines access as the ability to obtain postage and postal services, but does not believe that it necessarily requires a Postal Service facility with an employee in the facility. When asked about the economics of postal facilities, Mr. Donahoe stated that the most expensive method of selling stamps is over the counter and the least expensive method is through the Internet. Mr. Donahoe noted the Postal Service sells approximately 80% of stamps through Postal Service facilities and approximately 14% through Contract Postal Units (CPUs). He said that it is much more economically feasible to expand access through less costly methods, such as ATM machines than to do so through contracting with the private sector. He further stated that it was the Postal Service's goal to increase the number of access points, but that it did not have a goal to sell a certain amount of stamps through alternative vendors. When questioned as to why the Postal Service sells stamps and provides other services at 5,000 CPUs, instead of 50,000 or 500,000, Mr. Donahoe stated that the Postal Service is working to increase the number of CPUs. He also noted that 2,500 automated postal centers will be introduced into Postal Service lobbies and other places, such as grocery stores and malls, in FY 2003. In response to questions concerning the Postal Service's workers' compensation program, Mr. Donahoe noted that the Postal Service spent \$1.5 billion in FY 2002 on workers' compensation costs and asserted that the Postal Service

would welcome the opportunity to outsource its workers' compensation claim handling program.

Questions for Ms. Bizzotto: In response to a question concerning limitations on the expansion of CPUs, Ms. Bizzotto stated that there is nothing that limits the continued expansion of CPUs. She also noted that there are currently 44,000 consignment locations that sell stamps. When asked about the discounts given for worksharing activities, Ms. Bizzotto stated that in setting worksharing discounts the Postal Service considers not only the costs it avoids through worksharing programs, but also the impact of the discounted rates on customers and competitors. When questioned as to whether the Postal Service actually "captures" the savings attributable to worksharing, Ms. Bizzotto stated that she did not have a precise accounting, but that Robert H. Cohen, the Director of the Office of Rates, Analysis and Planning at the Postal Rate Commission, has written that it would require 187,000 additional Postal Service employees to perform the functions currently completed through worksharing. In response to questions concerning the pricing of postal services, Ms. Bizzotto stated that the only uniform rate the Postal Service offers today is the 37-cent rate for letters. She stated that virtually every other rate includes a distance or preparation component. She noted that each package is priced according to its weight and the distance shipped. She further stated that currently there are approximately 4,000 different rates. She further asserted that any future definition of universal service should include pricing flexibility for the Postal Service.

Questions for Mr. Strange: In response to questions concerning the uniform purchasing process, Mr. Strange said that the process did not work because the Union of Needletrades, Industrial and Textile Employees (UNITE) and a number of small suppliers jointly lobbied Congress to stop the program. He noted that the Postal Service chose to stop the program because of political pressure. When asked about supply management, Mr. Strange stated that the total value of goods and services purchased by the Postal Service is \$13 billion. He noted that the Postal Reorganization Act does not provide clarity about purchasing guidelines. He stated that certain federal statutes apply to the Postal Service, but not others, such as Buy America. He further stated that there is real uncertainty among stakeholders as to what "business-like" means.

Panel Two: Outsourcing - Transportation

Testifying on this panel were David F. Rebholz, Richard Corrado, and Robert Matheson. Please see attachments C, D, and E for their prepared written comments.

Questions for Mr. Rebholz: When asked whether he believes the Postal Service cross-subsidizes its non-monopoly products with funds from monopoly products, Mr. Rebholz stated that he was not in a position to question the Postal Service's allocation of costs. In response to a question concerning the universal service obligation, Mr. Rebholz stated that the formula under the Private Express Statutes, which allow carriers to carry urgent letters for a fee of two times the postal rate for that letter, is too restrictive. When asked whether there are additional services he would like to see the Postal Service outsource, Mr. Rebholz replied that he believes the services outsourced by the Postal Service are

adequate. He also noted that he believes the Postal Service enjoys an advantage in terms of consumer convenience with respect to the number of facilities it operates. When asked whether the processing of mail should be privatized and the Postal Service's activities limited to the "first mile" and the "last mile," Mr. Rebholz stated that he believes this level of privatization would cut the process back too far. He elaborated that some of the sorting requirements are part of a "backbone" that could not be dismantled. He also noted, however, that the Postal Service's greatest advantage is in the last mile.

Questions for Mr. Corrado: When asked whether Airborne was at a disadvantage to the Postal Service because of the latter's monopoly status, Mr. Corrado stated that Airborne was not at a disadvantage because it could offer volume discounts. He elaborated that the Postal Service does not offer discounts on Express Mail or Priority Mail and stated that Airborne would be at a disadvantage if the Postal Service offered discounts for these products. In response to questions concerning the flexibility of the Postal Service to partner with the private sector, Mr. Corrado stated the Postal Service operates efficiently where it has established rules, but noted that it has problems with the creation and development of new ideas. He also asserted that the rate setting process should be more flexible. When asked about additional services he would like to see the Postal Service outsource, Mr. Corrado opined that there is an opportunity to create additional worksharing agreements for First-Class mail.

Questions for Mr. Matheson: When asked whether there are any situations in which it would be appropriate for the Postal Service to conduct "reverse auctions" to solicit bids for transportation services, Mr. Matheson stated that it could be appropriate for spot loads and unscheduled trips. In response to questions concerning the Postal Service's flexibility to partner with the private sector, Mr. Matheson stated that the National Star Route Contractors Association has had a good working relationship with the Postal Service, but that the Postal Service employees' labor unions restrict the Postal Service's flexibility to partner with the private sector. Mr. Matheson also noted that the Postal Service's current practice of requiring all contractors to obtain fuel from a single supplier chosen by the Postal Service has the potential to harm the relationship between the Postal Service and the highway contracting industry. When asked to elaborate on his statement that services provided by members of the National Star Route Contractors Association are important to homeland security, Mr. Matheson stated that all drivers are subject to complete background checks and FBI fingerprinting. He noted that these activities may not occur when the Postal Service conducts a "reverse auction."

Panel Three: Worksharing

Testifying on this panel were John Campanelli and Sudhir Aggarwal. Please see attachment G and H for their prepared written comments.

Questions for Mr. Campanelli: In response to a question concerning the role the Postal Service should play in products that replace First-Class mail, Mr. Campanelli stated that the role of the Postal Service should remain the delivery of hard-copy mail. He further stated that the Postal Service should use new technology to improve the delivery and

processing of mail and to relay information about its services, but that it should not enter into new product markets. When asked how the Postal Service could create a system of incentives to operate in a more “business-like” manner, Mr. Campanelli stated that the Postal Service should examine its strategy, structure, and culture. He elaborated that the break-even mandate and employee compensation ceilings should be removed. When asked about standardizing the mail piece, Mr. Campanelli stated that businesses do not want to be limited to a standardized mail piece design. He further asserted that the Postal Service should encourage standardization, but should allow for non-standardized pieces at increased rates. Mr. Campanelli noted that RR Donnelley has not been successful in convincing businesses to standardize products and stated that it offers non-standardized pricing for non-standardized pieces.

Questions for Mr. Aggarwal: In response to questions concerning the appropriate roles of the private sector and the Postal Service in the pick-up, processing, and delivery of mail, Mr. Aggarwal stated that the private sector could not provide the same delivery services as the Postal Service without a government subsidy. He also stated that pick-up and delivery services should remain with the Postal Service, but that the processing and transportation of mail should be handled by the private sector. When asked whether the private sector should process all mail, Mr. Aggarwal stated that the private sector could process all mail, including “blue-box” mail, provided the Postal Service picked up the mail and delivered it to a processing center. He asserted that the private sector may be able to automate the processing of “blue-box” mail. When asked about standardizing the mail piece, Mr. Aggarwal stated that the business community could adapt more quickly to standardization requirements than “Aunt Minnie” mailers.

Panel Four: Retail - Existing Relationships and Potential Opportunities

Testifying on this panel were Steve D. LeNoir and Ken McBride. Please see attachments I and J for their prepared written comments.

Questions for Mr. LeNoir: In his prepared written comments, Mr. LeNoir recommended that the Postal Service expand non-postal and social services at Postal Service facilities. When asked about his thoughts on the argument that the Postal Service should not offer non-postal services because it would constitute an abuse of the Postal Service’s monopoly, he stated that many of the services he recommended are not offered by the private sector in rural areas. In response to the contention that certain social services do not make money, but rather cost money to operate, Mr. LeNoir stated that each postal facility does not have to break-even, but that the Postal Service only has to break-even on an aggregate basis. When questioned about the Postal Service’s deficit, Mr. Lenoir encouraged the Commission not to forget that the Postal Service was created as a service to the people.

Questions for Mr. McBride: Mr. McBride received no questions.

Panel Five: The Postal Service as a Competitor with the Private Sector

Testifying on this panel were Gary Pruitt, Brian Spindel, and Ken McEldowney. Please see attachments K, L, and M for their prepared written comments.

Questions for Mr. Pruitt: In response to questions concerning the Postal Service as a competitor with the private sector, Mr. Pruitt stated that the Postal Service should only operate where there has been a market failure. He stated that the delivery of mail is a natural monopoly and that the Postal Service should continue this function, but that the Postal Service should not participate in the advertising business as there is no market failure. Mr. Pruitt further stated that the Postal Rate Commission should have the authority to evaluate any extension of services beyond the Postal Service's core functions. When asked how the Postal Service can remain viable, Mr. Pruitt stated that the Postal Service should have more freedom to manage its costs. He elaborated that Congress should not be involved in Postal Service activities. In response to questions concerning the appropriate mission of the Postal Service, Mr. Pruitt stated that the Postal Service should focus on its core mission of providing universal service at a fair rate. Mr. Pruitt defined universal service as the delivery of all letters and packages to all addresses in the country at non-discriminatory rates. Mr. Pruitt also stated that rates should not favor one class of mail over another class. When asked whether the Postal Service could break-even through facility optimization and cost-cutting alone under Mr. Pruitt's definition of universal service, Mr. Pruitt stated that although the cost savings would be substantial, it is impossible to know what precisely they would be.

Questions for Mr. Spindel: When asked about the 10,000 stores that are a part of the Mail and Parcel Industry, Mr. Spindel stated that he did not know the number of stores that operate in rural areas, but noted that some stores operate in towns with populations as few as 5,000.

Questions for Mr. McEldowney: In response to questions concerning financial reporting by the Postal Service, Mr. McEldowney stated that applying existing SEC reporting requirements to the Postal Service would be a good start. When asked to define universal service, he stated that universal service is the delivery of mail and parcels to all addresses in the country at affordable rates, and ideally would include delivery six days a week and the retention of collection boxes. Mr. McEldowney also stated that the Commission should consider whether first class mail or packages should be subsidized.

Testimony from the audience

Larry Brown, President of the Los Angeles National Association of Letter Carriers: Mr. Brown asserted that the universal service obligation should not be changed. He further stated that collective bargaining should not be eliminated.

Peter Casserly, President of Walz Postal Solutions: Mr. Casserly stated that if the Commission is considering allowing the Postal Service to expand into competitive markets, then there should be rules and firm oversight established to ensure that

competition is not artificially restricted by the Postal Service. Mr. Casserly gave the Commission a more detailed document that outlines his comments in further detail.

Phillip Warlick, Legislative Director for APWU in Los Angeles, California: Mr. Warlick stated that the Postal Service is many things to many people. He noted that many activities of Postal Service employees are not measurable and are not reflected in the Postal Service's "bottom-line."

Jesse Scroggins, President of the Long Beach Chapter of the APWU: Mr. Scroggins stated that the discounts given to presort mailers in 1985 were a necessity because the Postal Service did not have the automation equipment necessary to process all of the mail, but that today the Postal Service has the equipment. He asserted that the Postal Service should not offer the current nine-cent discount to mailers, but rather should offer a four-cent discount to mailers that drop their mail off at the processing center by 10 am. He asserted that this would allow the Postal Service employees the time to process the mail. He further stated that the Postal Service does not need any new employees to accommodate this change. He noted that the Postal Service needs to optimize its equipment and asserted that the automation equipment is currently not used for large parts of the day.

Bob Fredman, an inventor: Mr. Fredman stated that he has an invention he tried to introduce to the Postal Service. He stated that he has had problems dealing with the Postal Service and that he has found the Postal Service to be less than entrepreneurial.

Eugene Woynoski, EW Consulting: Mr. Woynoski recommended that the Postal Service consider the implementation of selling agent commissions for independent third-parties to market postage stamps through major U.S. retailers. This recommendation was made in response to the Commission's question on why retail access had not grown more.

Yoggi Riley, Secretary and Treasurer for San Fernando Valley Area APWU: Ms. Riley stated that the American public wants to keep the universal service obligation. She also noted the importance of the sanctity and security of the mail.

John Cryder, Postal Affairs for Sprint: Mr. Cryder stated that his company and others are prepared to help the Commission in any way possible.

Commission Business

Co-Chair Johnson announced that the Commission's next public meeting will take place in Chicago, Illinois, on April 29.

The meeting adjourned at approximately 12:30 pm PST.