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Incorporating Postal World

Monitoring the Postal Service, Private Carriers and Suppliers

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Many Products Not Covering Costs

In a clear signal of just how tough 2009 turned out to be, USPS's Annual Compliance Report (ACR) shows a number of mail categories aren't generating enough revenue to cover the cost of handling them.

For FY 2009, market dominant products in general that were flat shaped or parcel shaped did not cover their attributable costs.

By law each product is supposed to cover its own costs and make a reasonable contribution to overhead so that it isn't subsidized by other products.

In FY 2009, products that have historically had a difficult time staying above water were hit hard. For example Periodicals, which covered 84% of costs in FY 2008, covered just 76% of those costs in FY 2009, due to a $643 million loss. Standard Mail flats covered about 82% of their costs – compared with 94.1% cost coverage in FY 2008 – while Standard Regular parcels and Not-Flat Machinables raised enough to cover just 75% of their attributable costs. That's down from 79.6% in FY 2008.

The Package Service class saw a $53 million loss in FY 2009. Within that class Bound Printed Matter flats and Inbound Surface Parcel Post were the only products to cover their attributable costs. In the Special Services category, Confirm, Registered Mail, Stamped Cards and International Ancillary Services did not meet their obligation to cover costs. And International Inbound Single-Piece First Class Mail covered just 60% of its costs.

Within Competitive Products, the class as a whole covered incremental costs but seven international products feel short, including competitive international business reply service negotiated service agreement contracts.

The Postal Accountability and Enhancement Act requires USPS to provide to the Postal Regulatory Commission, within 90 days of the close of the fiscal year, data on costs, revenues, rates and quality of service.

This year's ACR creates a dilemma for the Postal Service and the PRC – one that Congress may have to address as well. The law requires that each product cover costs and contribute to overhead but the CPI-based cap on annual rate increases limits their ability to do so. Negative inflation in the later part of 2009 meant that the Postal Service would not be able to raise rates in February. Postmaster General Jack Potter, recognizing mailers' need for certainty, announced back in October 2009 that USPS would not raise rates in 2010 regardless of the inflation rate. This decision suggests USPS sees the need to hold down costs as much as possible to slow the migration out of the mailstream. But the competing demands continue and may only get worse.

Comments on the ACR are due Feb. 1 with reply comments due Feb. 16.

Reporting Request Considered Too Onerous

Meanwhile, the PRC rejected the effort of the commission's public representative (PR) to force USPS to provide certain estimated rate level adjustments for every market dominant rate. The PR, who essentially plays the role of consumer advocate within the commission, is looking for estimates that would equate overall postal revenue with USPS estimated costs in a way that would ensure financial stability by the end of FY 2011.

The PR argued this is required by the postal reform law. A number of business groups and large mailers disagreed with the motion and supported USPS's opposition. USPS said it found it "patently unreasonable" to use its resources to address the PR's request.

The PRC agreed, saying that it is not warranted to make USPS go through the time and complexity required to develop sets of estimated rates for all market dominant products. The commission said the ACR, periodic reporting rules and other requirements provide a strong starting point for parties trying to evaluate whether USPS rates and fees comply with the law.

Capitol Hill Group Looks at Health Payment Issue

The Congressional Research Service (CRS), a division of the Library of Congress that provides information for lawmakers, is the latest organization to suggest Congress may want to take a look at its pre-payment schedule demands for USPS retiree health benefits.

In an update on implementation of the 2006 Postal Accountability and Enhancement Act, CRS noted that the Postal Regulatory Commission as well as the Postal Service Office of Inspec-

Short Takes

The idea of a pricing incentive that rewards increased mail use with discounts on future mailings – something along the lines of a frequent flier program – isn't likely to happen until 2011 or so when the intelligent mail barcode is more fully integrated into the postal system. A top USPS official said that the agency looked at that idea for one of its next sales – in the spring or in the summer – but rejected it for the time being because it is too complicated and the technology isn't there to do it. When the IMB is in place it will be easier to do, he said (*see 11/30/09, p. 6*). USPS is keen to go forward with more of these incentive programs but needs to come up with a way to prevent gaming of the program by mailers. The more notice mailers have of these sales, the official reasoned, the easier it will be for them to game the system, meaning they will have the time to plan their mailing programs so that volume increases in the period when costs are lower in the sales months. USPS wants these sales to encourage more mailings, rather than provide lower rates for mail that would have been sent without the discounts. The sales so far have been set up so that discounts are available for the increased volume in that period under a formula that takes into account uncharacteristically low volume in the month after the sale.

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Postmaster General Jack Potter has ordered an end to gifts of new commemorative stamps to members of the House and Senate committees that oversee USPS. Potter's order became public in mid December after Sen. John McCain, R-Ariz., complained about the "presentation albums" he had been getting embossed with his name in gold. "I find it irresponsible for the Postal Service to provide members of Congress such personally engraved albums when the Postal Service reported last month a net loss of $3.8 billion for the most recent fiscal year following losses totaling $7.9 billion in 2007 and 2008," McCain told Potter in a Dec. 16 letter. McCain asked the postmaster general not to send him any more albums. A USPS spokesperson said he won't be getting any more because Potter had ordered an end to the practice, effective this year. The senator was highly critical of Potter at a Senate hearing this year. He accused him of moving slowly to address the financial crisis that has plunged USPS into debt. In his letter to Potter, McCain noted that taxpayers have had to loan the Postal Service $10.2 billion to cover losses it has encountered during the past three years. "Until the Postal Service no longer owes American taxpayers billions of dollars, I request that you refrain from spending limited Postal Service resources on unnecessary items such as engraved albums showcasing commemoratives stamps for members of Congress and instead focus on moving the Postal Service to fiscal solvency," he told Potter.

tor General have publicly proposed revisions to the schedule that reflect not just changing financial circumstances but also the declining postal workforce. The OIG, for example, says USPS only needs to pay $1.6 billion annually through 2016 to fund its obligations. That's because there will be fewer retirees in need of health benefits going forward. Under these circumstances, CRS said, Congress may want to reassess the payment schedule. By law USPS's obligation is as follows:

Fiscal year	Payment (billions)
2007	$5.4
2008	$5.6
2009	$5.4
2010	$5.5
2011	$5.5
2012	$5.6
2013	$5.6
2014	$5.7
2015	$5.7
2016	$5.8

Notably, Congress relieved USPS of $4 billion of its obligation for 2009, so the agency paid $1.4 billion into the trust fund.

The additional $4 billion is scheduled to be paid after 2016. USPS is not allowed to lobby Congress, but it will be educating members on its financial situation and hopes for a revised payment schedule it can plan for.

Postal officials continue to make the point that their prepayment schedule is far more aggressive than that of other federal agencies or the private sector.

So far federal lawmakers have been more interested in addressing the situation one year at a time and continue to press for more evidence of cost-cutting and innovations in products and services.

CRS also proposed that in view of the difficulty USPS has making these payments, Congress may want to consider building in a mechanism for missed or incomplete payments.

Report author Kevin Kosar proposed a legislative fix with an automatic rollover of a shortfall into a subsequent fiscal year's scheduled payments.

The report, "The Postal Accountability and Enhancement Act: Overview and Issues for Congress," is available at http://opencrs.com.

OIG

Report Shows Work Ahead for Mail Entry

A recent audit of USPS business mail entry and payment technologies can't be good news for the agency, which is trying to shore up its acceptance process to meet tougher accounting requirements.

The Office of Inspector General (OIG) found that internal controls were generally in place and effective at business mail entry units (BMEUs), but "a significant deficiency continues to exist related to the acceptance of mail" in fiscal year 2009. This is the third straight year the OIG has found significant deficiencies.

The finding is a concern, but probably not shocking news to USPS. Officials there have been increasingly vocal about the need to get processes in place to be compliant with the Sarbanes-Oxley (SOX) corporate accounting law. Under the 2006 postal reform act USPS must be SOX compliant this year and previous audits show it is deficient in revenue assurance – specifically it is lacking systems in place to document that it is getting paid for the mail it is receiving.

USPS is implementing a Lean Mail Acceptance Process (LMAP) to set specific, efficient procedures for accepting and documenting mail.

LMAP is designed to optimize the configuration at acceptance, including staging of mail that has not yet been verified, use of placards for mail arriving on site and when it enters the mailstream, a "first-in-first-out" approach, and a team/triage approach rather than using a single person for all steps in the process.

The LMAP effort has a lot of mailers worried because it disrupts long-standing arrangements that have eased the process. And there is word of resistance by the acceptance personnel charged with implementing the procedures because of relationships they have built up with customers and informal procedures that have been in place for a long time.

But headquarters says informal procedures won't work in the SOX world where it must be documented that volume and receipts are in line.

OIG's audit of detached mail units (DMUs) found mail personnel didn't' always follow required acceptance, verification and clearance procedures. The biggest deviations were relating to lack of verification for Periodicals, particularly the practice of allowing Periodicals to enter the mailstream in non-business hours without verification. This arrangement has been critical for Periodicals mailers due to the time-sensitive nature of the product. OIG noted that the Business Mail Acceptance (BMA) unit is changing its policy for time-sensitive Periodicals that are low-risk so that they can continue to be accepted in off hours.

The review of 96 BMEUs found personnel did not always complete and process postage statements in a timely manner, test and calibrate scales, close inactive accounts and run MERLIN (Mail Evaluation Readability Lookup Instrument) verifications at the proper frequencies. Also, in five locations it was found that major controls were not effective.

USPS has been working to identify and address compliance problems at acceptance for some time. OIG noted that its audits of 88 units in the first three quarters of the fiscal year didn't show signs of improvement. But the last eight units it tested did show compliance improvements.

Litigation

Nonpostal Dispute Coming to a Head

What may be the largest disagreement between the Postal Service and the Postal Regulatory Commission (PRC) since enactment of postal reform legislation is now in the hands of the federal courts as the D.C. Circuit takes on the dispute over nonpostal products.

Oral arguments begin Feb. 8 in the D.C. Circuit Court of Appeals. Somewhat ironically, the case, which responds to a congressional directive that USPS should not be in the nonpostal business, is coming to a head just as USPS is gearing up to seek a change in the law so it can use its postal network – and help pay for that network – with sales of other goods and services.

The case goes back to December 2007, when the PRC began a review, based on its understanding of its obligations under the Postal Accountability and Enhancement Act PAEA, of USPS services to determine which nonpostal services should continue. USPS provided three groups of services: postal, nonpostal and services that are not postal services but are authorized through special means, such as real property leases and licensing philatelic services. It said the PRC had no authority to make a determination of whether the third category of services should continue. After ongoing proceedings in the commission, the PRC said it would hold an additional proceeding to see how it should exercise its regulatory authority over nonpostal services and how it should classify and regulate services such as licensing and leasing. At that point, the Postal Service went to the courts for a review.

In its brief before the court, the PRC says the plain language of the statute defines a nonpostal service as "any service that is not a postal service."

Licensing and leasing activities should be included because they are "services" within the law, the commission said. A service is "'any activity performed in whole or in part for the purpose of financial gain, [including] any sale, rental, leasing or licensing for use.'"

Aside from being contrary to the statute, the PRC said, the USPS interpretation is contrary to the purpose of that law, namely, to keep the Postal Service from offering commercial services beyond its core business.

The USPS brief argues that the PRC is overreaching itself with a review of nonpostal services that extends further than the law's restriction of them.

USPS says the law only intended to cover certain nonpostal services under earlier law that were part of the new definition of postal services under the PAEA. This was not authorizing the PRC to review and possibly terminate other series that are authorized elsewhere in the statute. Furthermore, USPS said, Congress' concern was about new business ventures USPS might get into.

There is no evidence that Congress was worried about USPS's ability to manage its property or run its philatelic services, USPS said.

DMM Updates for January Announced

January is a busy month for updates in the *Domestic Mail Manual*. Some highlights are provided below:

New prices and mailing standards for Shipping Services. Revisions support the Jan. 4 changes in shipping services prices and mailing standards. The increase in prices averages 3.3% and covers Express Mail, Priority Mail, Parcel Select and Parcel Return Service.

Permit imprint with extra services. Revisions to 604.5.3.7 and 604.5.3.8 clarify the permit imprint class markings for Standard Mail and Package Services and allow for abbreviated phrasing when permit imprint postage is used with extra services.

Nonprofit Standard Mail pricing. Revisions to 703.1.6.11 bring standards in line with the Internal Revenue Code restrictions on products mailed at Nonprofit Standard Mail prices that meet one of three exceptions.

Hardcopy and electronic return receipt rules. A combined purchase of hardcopy and electronic return receipt services is now authorized with revisions noted at 503.6.2.1.

Expansion of Priority Mail commercial base and commercial plus prices. Revisions to 402.2.1a., 423.1.0, 424.1.1, 425.2.2, and 507.11.1.5 allow Priority Mail commercial base and commercial plus prices for permit holders who use Priority Mail services for Merchandise Return Service mailpieces.

Presentation of stamped mail over 13 ounces. Revisions to 116.1.0, 126.1.0, 156.1.0, 176.1.0, 186.1.0, 426.1.0, 507.6.0, 601.11.0, and 703.2.0 require all mailpieces weighing over 13 ounces bearing only postage stamps to be presented to a USPS employee at a retail service counter in a post office.

Permit imprint postage payment extension. Revisions to 413.1.0 and 414.1.0 clarify that Express Mail commercial base and commercial plus prices apply to permit imprint customers using the Electronic Verification System (eVS) program to pay and document postage.

Consolidation

Closing Case Still Pending at Commission

More than a month after the Postal Service said it no longer wants the Postal Regulatory Commission's opinion on plans to close several hundred stations and branches, the proceeding is continuing.

In early December the Postal Service said that it no longer considered a PRC advisory opinion necessary for the plan to consolidate the retail network by closing postal stations and branches.

USPS said at that time that when it made the request early in its planning it wasn't certain what the situation would be. Since then the number of facilities being considered for closure has declined significantly from the initial 700 or so.

USPS is required to seek an advisory opinion from the PRC when it is considering a change that would have national service implications. Although a PRC response is "advisory," the Postal Service would undoubtedly feel a lot of pressure to follow that advice.

Meanwhile the number of facilities under review continues to be whittled down with 170 offices candidates for consolidation as of mid-December. So far none of the facilities under review has actually been closed.

A USPS official said that "as a part of the proceeding we had agreed to update the PRC each month with the list of offices that are under review and as the case is still open we will honor our agreement. If the case remains open in January there would be an update on that list. But that's a question that really remains with the PRC."

Although the PRC is mum on its intentions, the commission's public representative, who has been extremely critical of USPS's consolidation filing, thinks the proceeding should continue. The public representative argued that under PRC precedent the question is not whether the changes proposed would generally affect service on a nationwide or substantially nationwide basis but whether they would impact "representative" customers.

Alternatively, the public representative suggested that the PRC issue a "conditional" advisory opinion. It would be more efficient, the public representative reasoned, because if the plan is later found to have a national service impact the views of the PRC already would be available.

Finances

FedEx Sees 10% Revenue Decline

The global economic recession continued to hit the package industry hard in recent months with FedEx Corp. seeing a 30% decline in net income to $345 million in its second quarter ending Nov. 30, 2009, compared with last year's $493 million.

The company saw revenue of $8.60 billion, a 10% decline from the same period last year (SPLY).

Operating income was down 27%, at $571 million, and the operating margin was 6.6%, compared with last year's 8.2%.

FedEx largely attributed the drop in revenue and earnings (which were $1.10 per diluted share, compared with $1.58 SPLY) to a substantial decline in the fuel surcharge.

Looking domestically, FedEx Express domestic average daily package volume increased 4% but revenue per package dropped 19%. The decline came from the fact that consumers were using less costly options and mailing lighter weights, as well as the impact of falling fuel prices on the fuel surcharge.

This led to a 13% decline in revenue for the sector in quarter two, compared with SPLY. Operating income was down 36% and the operating margin was 6.5%, compared with 8.9% SPLY.

FedEx Ground picked up 4% in average daily package volume. That, along with 63% growth in FedEx SmartPost average daily volume, meant revenue was up 3%.

FedEx Ground and FedEx Home Delivery rates went up an average 4.9%, effective Jan. 4. The company is somewhat optimistic for the third quarter, planning for modest economic improvement and announcing that it will resume merit salary increases in 2010 along with a 50% match of 401(k) plans for most employees.

Alan Graf, FedEx Corp. executive vice president and CFO, said in a statement that there is some uncertainty about where demand trends will go after the peak holiday shipping season. But "our balance sheet is strong [and] volumes are growing," he said.

Shipping Revenue Up

In a very welcome spot of good news, the Postal Service registered a 1% increase in mail and services revenue combined for November 2009, when compared with the same period a year earlier, and significant gains in shipping services.

For November, shipping services' volume was up 3.1%, with revenue up 6.7% compared with the same period last year (SPLY). For the fiscal year so far, shipping services' revenue is up 2.2% although volume is down 1.2%.

The other bright spots for November in terms of volume were First Class Mail, which saw a 3.3% increase in volume and 1.3% increase in revenue, and Periodicals, which saw a 6.3% increase in volume although revenue was down 10.5% compared with SPLY.

Despite these encouraging signs that the economic recession may be slowing down, USPS had a loss of $255 million for the month, although that was better than the $507 million loss SPLY. Year to date the loss is $476 million.

USPS is still trying to get control of costs, with operating expenses down 3.4% for November and 3.4% year-to-date compared with SPLY.

As the postal workforce continues to shrink, personnel compensation and benefits are also declining, with a 4.6% reduction overall. Looking at the workforce by category, compared with SPLY, customer service and retail expenses were down 9.9%; mail processing was down 6.9%; city delivery declined 2.3%; and rural delivery dropped 1.7%. Also, the general "other" category, which includes plant and vehicle maintenance as well as operational support, postmasters and administration, was down 3.7%.

November 2009 Volume/Revenue

(in thousands)

	Actual	SPLY	%SPLY Var
Mailing Services			
First Class			
Volume	6.273,868	6,487,908	3.3%
Revenue	$2,784,325	$2,749,712	1.3%
Periodicals			
Volume	571,461	609,935	6.3%
Revenue	$150,057	$167,592	-10.5%
Standard Mail			
Volume	7,483,506	7,848,049	-4.6%
Revenue	$1,582,832	$1,633,974	-3.1%
Package Services			
Volume	48,233	57,590	-16.2%
Revenue	$115,745	$129,958	-10.9%
Total Mailing Services			
Volume	14,439,876	15,049,419	-4.1%
Revenue	$4,951,964	$4,942,450	2.0%
Total Shipping Services			
Volume	121,036	117,386	3.1%
Revenue	$689,095	$645,773	6.7%
Postal Service Totals			
Volume	14,560,912	15,166,805	-4.0%
Revenue	$5,641,059	$5,588,223	0.9%

Source: US Postal Service

Briefs

At its closed door meeting this month the Postal Service Board of Governors is likely to take a hard look at reports prepared to outline the longer term future of mail and how to make USPS viable in the face of a declining tool for nationwide communication. As those heady issues are considered, the Postal Service will continue to hammer away at its current core proposals for addressing volume decline, including the retiree health benefits trust fund and use of the ubiquitous postal network to sell things other than postal products. These issues are starting to get the attention of the House and Senate, with lawmakers also weighing the idea of five-day delivery. There was some question on Capitol Hill whether the Postal Service was going to stick with its desire for a change in delivery days but key staffers are now getting the message that this is very much a keeper on USPS's agenda.

Alan Kessler has been reappointed to the Postal Service Board of Governors for a second term that expires Dec. 8, 2015. Kessler was first appointed by President Bill Clinton in 2000 and served as chairman of the Board from January 2008 to January 2009. He is now serving as co-chair of the Board's Governance and Strategic Planning Committee. Kessler is an attorney and partner in the Philadelphia-based firm of Duane Morris LLP.

It's that time again! The National Postal Forum will return to Nashville in 2010. Registration is now open for the premiere postal event, which will be held April 11-14. To register and get additional information, visit the forum website at www.npf.org.

Legislation to promote electric vehicles within the huge USPS fleet was introduced last month. The American Electric Vehicle Manufacturing Act (H.R. 4399) directs the Energy Dept., in consultation with USPS, to set up a two-phase program to award funds for the manufacture, testing and delivery of 20,000 electric drive long life delivery vehicles. The bill also outlines steps to develop a grid service. Funds for the program would have to be separately authorized. Sponsored by Rep. Jose Serrano, NY-16, the bill has five cosponsors and was reported to the Oversight and Government Reform, Energy and Commerce, Transportation and Infrastructure and Science and Technology committees.

Direct marketing research firm Mintel Comperemedia is reporting that rewards for bank purchases are the latest trend in financial marketing. It said for the first three quarters of 2009 .31% of checking direct mail offers promoted rewards for everyday banking, up from 13% of offers in 2007. by

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