



February 24, 2005

Honorable Susan M. Collins
Chairman
Committee on Homeland Security
and Governmental Affairs
United States Senate
Washington, DC 20510-6250

Dear Chairman Collins:

As Congress and the Administration turn to further consideration of postal reform this year, we, the Governors of the United States Postal Service (USPS), wish to communicate our views. We believe that the years of study and hard work devoted to this endeavor will be rewarded only upon enactment of comprehensive legislation that promises substantial improvements in the postal system over the long run.

During the past five years, the Postal Service has made great strides in improving service and controlling costs. In fiscal year 2004, on-time delivery of overnight First-Class Mail reached a record 95 percent. The Service achieved a record fifth straight year of increased total factor productivity, with staffing that is down to pre-1985 levels. USPS debt is now at the lowest level in 20 years.

On the other hand, the Service faces significant challenges. Its decades-old business model, in which a continually-growing First-Class Mail volume with its large per-piece contribution defrays the major portion of infrastructure costs, is no longer valid. First-Class Mail volume has declined three straight years, and this trend is expected to accelerate. Moreover, USPS faces significant liabilities and pressures on costs. At the same time, the Service must maintain a delivery network to serve 142 million homes and expand it to accommodate 1.8 million additional addresses annually.

Thus, we take our position on pending legislation with full awareness of the difficulties as well as opportunities facing the Postal Service and our responsibility to insure the Postal Service continues to meet its universal service commitments with the level of service the American public has come to expect, while providing competitive products and services at reasonable prices.

In the Board meetings of January 11, 2005, and February 16-17, 2005, we reviewed with Postmaster General Potter the Service's operations, the need for remedial action, and the current state of the legislative process. We believe strongly that to be successful the reform package must incorporate the following elements.

First, the escrow requirement for the so-called savings in payments to the Civil Service Retirement System (CSRS) should be removed. The misnamed "savings" is actually a correction of a statutorily-mandated (over)payment into the retirement system. To continue to require the Postal Service to hold these funds in an escrow or other account would simply continue the overpayment and unfairly burden postal ratepayers.

Second, the portion of the costs of CSRS benefits for USPS employees attributable to their military service should not be borne by USPS. The requirement that military service count toward USPS retirement is a Federal policy and a national obligation. Moreover, the Postal Service is required by law to give preference to veterans when hiring new employees. It is unfair effectively to penalize USPS for hiring those with military service, and it is neither equitable nor efficient for this cost to be assessed effectively as a Postal tax upon the use of the mail by millions of Americans. If this were allowed to continue, the Postal Service would be the only agency with CSRS employees that is required to fund these benefits. And we know of no private-sector company that is required to credit military service toward retirement.

Nevertheless, we understand the concerns of Congress and the Administration over the current fiscal situation and also over the long-run cost obligations for USPS retiree health care. Accordingly, we have proposed an approach that we believe would address both concerns while mitigating customer uncertainties regarding future postage rates in the near- and mid-term. We hope you will give serious consideration to our proposal.

Third, the legislation should incorporate improvements in the labor area—which accounts for nearly 80 percent of USPS costs. Current law charges USPS management and labor with addressing wage issues through collective bargaining, but also imposes major federal benefit programs by statutory requirement or restriction. We believe that important employee benefit features that are part of total compensation strongly influence the USPS's future costs and thus should be subject to negotiation at the same table with wages. Also, when management and labor fail to reach a bargaining agreement, the law requires mandatory arbitration. We believe that an arbitrator should be required by statute to factor into the decision the economic history of the employer, present financial health and ability to pay, as well as anticipated future growth, productivity, and total labor costs.

Fourth, the USPS should be granted more rate flexibility and authority to introduce new postal services. At present, the ratemaking process is very costly and time-consuming. General rate cases take at least 18 months to conclude, by which time the market may have changed significantly. As we have seen in the recent past, USPS finances can be impacted dramatically by events outside its control, such as increases in the cost of fuel. We feel that it is imperative that an exigent rate case be provided for, to ensure the continued delivery of services in the face of serious adverse events. And while there are provisions for special new services ("Negotiated Service Agreements"), in such cases as well the impediments are costly and overdrawn. Consequently, we believe that the USPS should be granted authority to change rates and introduce appropriate new postal services (both with Board approval) within a range (determined by the Postal regulator) without prior approval.

Historically, postage rates have stayed within increases in the Consumer Price Index (CPI). We believe that CPI would be an acceptable, albeit very challenging, price cap on rates (that is, the top of the range). We also believe that the bottom of the range should be established sufficiently low to allow price competition while covering reasonable estimates of attributable costs. The cap should be applied at the aggregate level, and certainly no lower than each class, to allow the Board the requisite pricing flexibility.

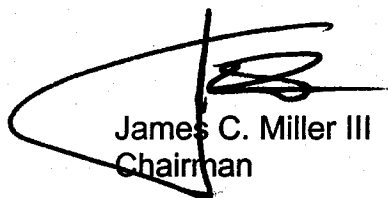
Fifth, any future changes in the scope of the postal monopoly should be considered within the context of the Postal Service's universal service mission and other social policy obligations. We believe that Congress and the Administration, not the regulator, are best positioned to set national policy striking a balance among these dimensions.

Sixth, we believe that we should be held fully accountable for the governance of the USPS, but also that we should be granted requisite authority. We ask to be empowered to establish, without external review, levels of compensation, based on performance, for the chief officers of the organization rather than being limited to caps on federal pay. We should also continue to be responsible for the retention of auditors, as well as the organization's Inspector General. Moreover, we should continue to be responsible for pursuing the efficiencies and cost control available from continuously rationalizing postal networks. We would welcome inclusion of a provision in the reform legislation recognizing the ongoing need for network changes and the Board's responsibility to assure execution of an effective program. We should be responsible for establishing appropriate levels of service and making sure they are maintained. Finally, we (rather than Congress) should continue to approve USPS budgets and requests for appropriations.

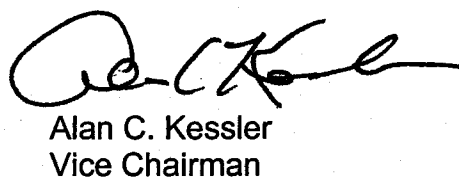
We realize that in some areas we are requesting more authority, but we are perfectly willing to accept the added responsibility, including oversight by Congress and the Administration. Our objective is to make the USPS perform as efficiently and effectively as possible, and in a way that is increasingly competitive and customer-friendly. We believe that legislative reform is needed to make this possible.

We have discussed these issues extensively with the Postmaster General, and we are in agreement as to the necessary elements of reform. We have directed the Postmaster General to pursue these initiatives aggressively, in order to ensure that reform legislation enables USPS to continue to provide its service to the nation for many years to come. We, along with the Postmaster General, look forward to working with Congress and the Administration to fashion appropriate language.

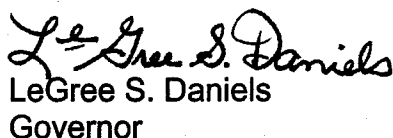
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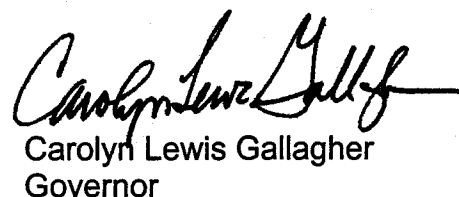
James C. Miller III
Chairman



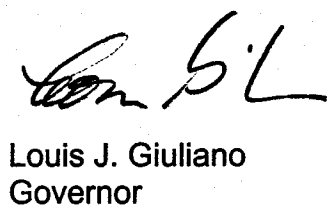
Alan C. Kessler
Vice Chairman



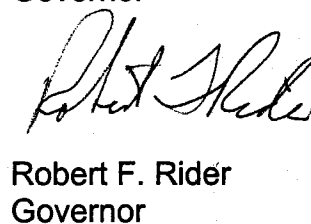
LeGree S. Daniels
Governor



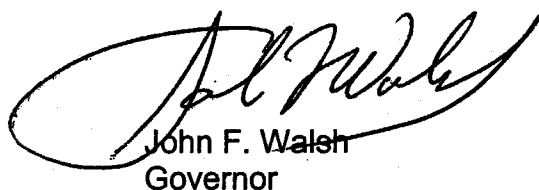
Carolyn Lewis Gallagher
Governor



Louis J. Giuliano
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cc: Senator Frist
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