

POSTAL ISSUES UPDATE

SUMMER 2007

Mailers Adjust to New Postage Rates

New postage rates were implemented on May 14. The biggest changes for Standard Mail® users include:

- Substantially increased destination entry discounts. These worksharing discounts are now \$42/M for SCF entry and \$33/M for BMC entry.
- Elimination of the Automation Basic ECR rate (AutoCR). Mail that previously qualified for this rate will mostly migrate to the automation 5-digit rate.
- Flats rates have increased significantly. Rates for these larger pieces (exceeding 6-1/8" x 11-1/2") have gone up 20–40%.
- The Postal Service Board of Governors (BOG) asked the Postal Regulatory Commission (PRC) to reconsider its recommendations for these flats rates. The PRC recommended a temporary reduction in flats rates of 3¢/piece (2¢/piece for nonprofit mail) that would last until September 29. As of this writing, the BOG has not acted on this recommendation. The PRC did not recommend any changes to letter rates to balance the temporary reduction for flats.

Notable changes for First-Class Mail® users include:

- Separate rate structures for letters and flats. This eliminates the non-machinable surcharge on flats weighing less than an ounce.
- Elimination of the Automation Basic ECR rate (AutoCR). Mail that previously qualified for this rate will mostly migrate to the automation 5-digit rate.
- The "additional ounce" rate has been reduced to 12.5¢ for automation letters and 17¢ for nonautomation letters and flats.
- Postcard rates are still lower than Standard Mail letter rates.

What's in store for the next rate case? Although the Postal Service is allowed to file one more cost of service rate case before December 20, both the mailing industry and PRC Chairman Dan Blair have encouraged them to forego this "one last bite of the apple" and to focus instead on working within the price cap system. Both the BOG and Postmaster General John Potter have said that a final decision on whether or not to file a final rate case under the old rules has not yet been taken. However, recent indications from the Postal Service are that it would be open to filing the next case under the price cap system if it were able to structure the increase to cover one time costs it is facing in the transition to the new rate making system. Informal conversations continue between industry, the Postal Service, and the PRC regarding how this might be accomplished

Implementing Postal Reform

After more than ten years of effort by the mailing community, the Postal Accountability and Enhancement Act (PAEA) was passed and signed into law this past December. Highlights of the law include:

- The law requiring the USPS to pay \$3 billion annually into an escrow fund is repealed. The money will now be used to cover retiree healthcare liabilities, putting the USPS on firm financial footing for the future.
- Pension costs associated to military service will be returned to the Treasury department, where they rightfully belong and where they will be funded by all Americans, not just postage rate payers.
- The Postal Rate Commission becomes the Postal Regulatory Commission with stronger oversight powers over more postal issues, not just rates.
- One of the first acts of the new PRC is to establish a new process for setting postage rates. This new process is expected to be more flexible than the current highly-litigious and drawn-out process of filing for rate increases. Although the law gives the PRC 18 months to establish new rate setting procedures, Chairman Dan Blair has said he wants to accelerate the process and have the procedures in place by this fall. The PRC has been gathering a wide range of input from postal community stakeholders on what the process should include. As well as gathering formal comments on the subject, the PRC also co-sponsored (with the USPS) a "regulatory summit" in March that received broad postal community participation to further discussion about how the PAEA should be implemented. IWCO Direct was among the postal stakeholders attending the summit.
- In addition, rate increases for market-dominant products (mail classes for which the USPS has a monopoly) will be capped using the Consumer

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Mail Moves America Coalition Formed to Combat Do-Not-Mail Legislation

Since the beginning of the year, legislation calling for the creation of do-not-mail registries have been introduced in more than 15 states. The registries would be similar to the national do-not-call list. To date, none of the bills has passed, and many have been withdrawn after meeting local opposition from industry, labor and other groups. Both the USPS and several of its unions have also been vocal in opposing this type of legislation.

In response to this trend, several direct marketing and mailing associations have formed the Mail Moves America (MMA) Coalition to monitor the progress of these bills in the various state legislatures as well as to educate legislators and the public regarding the value of mail. The MMA Communications Committee, of which IWCO Direct is an active participant, is developing materials that can be used to educate policymakers on the role of mail in the economy. The materials are expected to be available this summer.

Among the themes that will be highlighted in this educational material are:

- Mail is non-intrusive. You can open it now, read it later, or not at all. And with advertising mail, there are no bells to answer, program interruptions, or other distractions. You can choose to buy or not buy a product or service. You can choose in the comfort of your home or the convenience of your office, and you can choose without having to endure high-pressure sales tactics. Mail lets you do business on your terms and on your schedule. Not someone else's.
- Consumers prefer mail. According to a recent New York Times article "Marketers are finding that a lot of people . . . prefer [advertising] mail to [email] and phone solicitations." A recent US Postal Service study found that 56% of respondents say receiving mail is a "real pleasure" and 55% of respondents "look forward" to the mail they receive.
- Consumers already have a choice. There is already a simple, reliable way for consumers to remove their name from marketing lists: the Direct Marketing Association's Mail Preference Service. The vast majority of legitimate marketers already subscribe to this service.
- Advertising mail keeps postage rates low. Advertising mail supports our universal mail delivery system by lowering the cost of postal services. The Postal Service has fixed costs for people and facilities. Advertising mail represents about 55% of all mail volume. Take away advertising mail and to keep universal postal deliveries nationwide, six days a week, you still need most of the postal facilities and people now on the payroll. Fewer users sharing largely the same fixed costs means only one thing -- vastly higher rates for the postal patrons who remain. Without advertising mail, the price of a first-class letter would soar.
- Mail provides jobs. The jobs of more than nine million Americans depend on the mail. Direct mail is a growing industry, but the industry's ability to create and sustain jobs is dependent on the continued viability of mail as an advertising and communication medium.

Direct Mail Coalition Works to Prevent Tax on Postage and Mailing

The Direct Mail Coalition continues to work with the Governing Board of the Streamlined Sales Tax Agreement (SSTA)[†] to address issues related to taxation of postage and mailing services. The coalition is also representing mailing industry interests in talks regarding specific regulations in New Jersey and Nebraska, as well as before the U.S. Senate Commerce Committee as they consider federal SSTA legislation.

The coalition is urging the SSTA Governing Board to conform its regulations to the following principles:

- Stop the imposition of sales tax on postage:
 - Postage is not part of the sales price of printed materials or mailing services.
 - Postage purchased through a mailing agent is not part of the sales price.
 - Postage is not a "delivery charge."
- Separately priced mailing services are not part of the sales price of printed materials:
 - The direct mail sourcing rules do not convert a sale of printed materials at the loading dock to a sale of printed materials at the mailbox.
 - Use tax on distribution may be imposed at the mailbox on promotional materials if the sender has nexus.
- Simplify sales and use tax collection and reporting for direct mail with goal of one rate per state.

The SSTA Governing Board began discussions of direct mail issues at its March meeting in Charlotte, NC, but deferred action until its June meeting in Detroit, MI so the board could continue to study the issue.

[†] SSTA was designed to create simpler and more uniform sales tax regulations among the states, with the hope that Congress would allow states adopting this simplified system to collect sales and use taxes from entities not having a presence in the state. Several states participating in SSTA have adopted the standard definition of "delivery charges" which includes postage payments made through printing and lettershop vendors.

USPS Continues Push for Improved Address Quality

Delivery Point Validation (DPV): Beginning August 1, DPV becomes a required part of certifying addresses for automation processing. The traditional CASS certification process compares the primary house number in each address to ranges of valid house numbers in order to assign/verify the +4 portion of the ZIP code. This system allows some house numbers that are within range, but that don't actually exist, to be assigned a +4 and therefore to be eligible for automation discounts. DPV compares the house number to a table of the actual "delivery points" on that street. If there is not an exact match, a +4 cannot be assigned and the address is not eligible for automation discounts.

Testing shows that most mail files will see an increase in nonautomation rate mail of 0.5 – 2.0%. Mailers will need to decide if they want to continue mailing these records at nonautomation rates or drop them from their mail files.

Move Update (NCOA^{LINK}): The Postal Service has announced expanded move update requirements for First-Class and Standard Mail. Currently move update processing (typically accomplished via NCOA^{LINK}) is required for First-Class Mail and must be run within the 185 days (six months) prior to mailing.

The USPS announcement stated that the move update requirement is being extended to Standard Mail as well as First-Class Mail. It also stated that the window for move update processing is being shortened from 185 days to 95 days (three months). The USPS will allow a minimum 18-month implementation period to allow mailers to adjust to the new regulations. This will result in implementation no earlier than November 2008.

USPS Agrees to Contracts with Clerks and Mail Handlers – Negotiations with Carriers Stall

The Postal Service has signed new contracts with two of its four largest unions, the American Postal Workers Union (APWU) and the National Postal Mail Handlers Union (NPMHU). No agreements have been reached with the National Association of Letter Carriers (NALC) or the National Rural Letter Carriers Association (NRLCA).

Negotiations with NALC have ended in an impasse and have gone to binding arbitration. Arbitration begins in September and is expected to conclude in November. NRLCA rejected a contract offer in February. Negotiations are continuing, but if agreement is not reached by early June this dispute could also go to arbitration. The fear in the mailing industry is that arbitration awards are often larger than negotiated settlements, which could push up the Postal Service's cost structure as about 80% of USPS spending goes toward labor costs.

Among the disagreements the two carrier unions have with the USPS is their opposition to the USPS's move to use more contractors for mail delivery and other functions. These differences were aired at a recent hearing of the Federal Workforce Subcommittee of the House Committee on Oversight and Government Reform.

Most labor leaders appearing before the committee spoke against "contracting out" mail delivery and other functions. The one dissenting voice was APWU President William Burrus who cautioned against unions seeking congressional intervention in matters that should be left to collective bargaining.

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Price Index (CPI). This should mean less "rate shock" for mailers and the opportunity for smaller, more predictable rate increases that mailers can more easily build into their annual budgets.

- The USPS is required to develop performance standards for market-dominant products and measure their performance against the standards, reporting the results publicly. The USPS has formed a Mailers Technical Advisory Committee (MTAC) Workgroup to gather mailing industry input on development of the performance standards as well as service performance measurement. IWCO Direct is an active participant in the workgroup.
- The Government Accountability Office (GAO) has removed the USPS from its high-risk list for government organizations. The GAO cited major management progress since 2003 as well as the passage of the Postal Accountability and Enhancement Act as reasons for the move. The GAO did caution that the USPS faces on-going challenges regarding employee retirement and network consolidation.

Accounting Shifts, Volume Decline Affect USPS Financial Performance

Postal Service CFO Glen Walker has reported that the Postal Service ended the second quarter of FY2007 with a \$3.7 billion net loss. Although much of the loss is a result of accounting shifts mandated by the Postal Accountability and Enhancement Act (PAEA), it was compounded by declining mail volumes in the second quarter.

Passage of PAEA changed certain pension and health benefit payments and how the USPS is required to reflect those payments in its financial statements. While PAEA relieves the USPS of having to make additional Civil Service Retirement System (CSRS) pension contributions, it requires the USPS to contribute to a newly established Retiree Health Benefit Fund (RHBF). In addition, PAEA also required the USPS to transfer the \$3 billion it had placed in escrow at the end of FY2006 to the RHBF, which required the USPS to show that amount as an expense on this year's books.

Year-to-date mail volumes were buoyed by strong first quarter growth, while second quarter volumes were off 0.6% from the same period last year. First-Class Mail was down 2.5% in Q2. Standard Mail showed an anemic 1.2% growth in Q2, but year-to-date its volume growth was a more robust 3.2%.

Rising expenses were also a factor in the loss, with salaries and benefits increasing by \$909 million and transportation by \$333 million over plan year-to-date.

	FY 2007 Oct – Mar	Change from FY 2006
Financials		
Total revenue	\$38.2 billion	2.8%
Total expense	\$37.1 billion	4.1%
Income from operations	\$1.1 billion	(26.4%)
Escrow/pension adjustments	(\$4.8 billion)	
Net loss	(\$3.7 billion)	
Volume		
Total mail volume	110.1 billion	0.9%
First-Class mail volume	49.8 billion	(1.3%)
Standard mail volume	53.7 billion	3.2%

Intelligent Mail Program Moves Forward

The USPS has begun roll-out of its "intelligent mail" program that will rely on one standardized intelligent barcode used on each piece or container of mail.

The barcode for letters and flats, termed the Intelligent Mail Barcode or IMB, uses four different "states" of bars to encode information. The IMB can encode much more information than the current Postnet barcodes. The IMB can include mailer identification, delivery information, tracking information and Address Change Service participant information, all in about the same amount of space needed for a Postnet barcode.

Use of the IMB is currently optional, but will become required by early 2009. Currently the IMB can be used for automation processing of letters and flats and OneCode CONFIRM service. It can also be used for OneCode ACS service, but only for First-Class Mail. OneCode ACS for Standard Mail is expected to be available in the fall.

New barcodes on containers of mail (trays, pallets, etc.) will allow the USPS better visibility to where each container is within their processing network at any given time. Once the system is fully operational, mailers will also have improved abilities to track mail throughout the postal network.

The USPS is already pilot testing a process they are calling "Seamless Acceptance." With Seamless Acceptance mail can be inducted and verified by the USPS by comparing barcode scans as mail processes through their network to documentation provided by mailers. This would reduce the amount of manual verification that needs to be conducted at vendor plants before mail enters the mailstream.



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