

Testimony of Don Hall, Jr.

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**Before a Joint Hearing of the Senate Subcommittee on Federal Financial Management,
Government Information, Federal Services and International Security and the House,
Postal Service and the District of Columbia**

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Good afternoon. Chairman Carper, Chairman Lynch, Ranking Members McCain and Chaffetz and other distinguished members of the Committees. My name is Don Hall, Jr. and I am President and CEO of Hallmark Cards, Inc. Thank you for the opportunity to speak to you today about the future of the United States Postal Service.

2010 marks the one hundredth anniversary of Hallmark Cards, Inc. For more than a century we have helped our consumers connect with friends, relatives and loved ones and to give voice to their feelings. In January, 1910 my grandfather, Joyce Hall started a business with two shoeboxes of greeting cards. That business has grown into a \$4 billion corporation offering products to consumers in one hundred countries around the world and in 40,000 stores in the United States. We offer employment to more than 27,500 people in the United States and work closely with thousands of small business entrepreneurs in every state through our 3,200 independently owned Gold Crown stores.

Our slogan “when you care enough to send the very best.” has been more than an advertising phrase – it’s been a promise to our consumers.

We at Hallmark care a great deal about postal issues. I care because for much of our history, the Postal Service has been a vital partner to us. We participate with others in our industry through the Greeting Card Association, and I am a member of the CEO Council of the Mailing Industry Task Force. We all share the common goal of a robust and stable Postal Service – a goal that I believe is vitally important to the people of this country.

Hallmark has been working with the Postal Service to develop new products and services to increase mail volume. We have undertaken a major product and marketing initiative to use the USPS's Intelligent Mail Barcode technology to offer prepaid postage to our consumers and generate additional First Class mail volume.

Along with the GCA, we have helped promote two new and popular innovative products. They are the popular "Forever Stamp" and the new "Butterfly Stamp" for square greeting cards.

USPS Sustainability – A Crisis

The issue of sustainability is what compels me to be here today. Clearly, the Postal Service is facing its most severe crisis. The country's economic downturn, competition from newer technologies made possible by the Internet and Broadband in particular, and the Service's continuing challenges of the new realities of shrinking demand, have come together to create the "perfect storm" for the Postal Service. By 2020, it is forecasting losses of as much as \$238 billion. I compliment the Postmaster General for actions to date to bring postal costs in line, but it is not enough if we are to sustain this institution.

Over the past 30 years it has never been easy to manage the Postal Budget. Often shortfalls have been solved by raising postal rates, which consumers have accepted. Given this economic contraction, significant changes in consumers' willingness to accept price increases in

all aspects of their lives, and the number of alternatives available to users of the mail system today, solving budget shortfalls through price increases and reduction of service not only won't work, it will make matters worse. We are at a tipping point.

We must find a sustainable solution now. No one knows better than you that it will not be easy. But we can no longer avoid this reality.

The Problem – A Two-Legged Stool

Many of you are all too familiar with the ten-year effort to pass postal reform legislation. During that long period of debate, a bi-partisan Commission issued a report in 2003 calling for changes in three key areas: 1) Rate Setting, 2) Regulatory Oversight and 3) Cost and Capacity Controls. The legislation that ultimately passed in 2006 addressed only the first two of these areas.

Although the price cap rate-setting scheme was intended to help management control costs, few specific provisions were included for the Postal Service or its regulator to do so. I think of it as having constructed a stool with only two legs and expecting it to stand. As I have monitored the debate over how to solve the current crisis, it is imperative now to address the third leg of the stool – costs and capacity controls.

Simply put, the Postal Service cannot survive without a sustainable cost structure, and that means one that is considerably lower than what it is today. The 2006 postal reform law imposed an enormous financial burden for fully funding future retiree healthcare costs, an imposition that hasn't been applied to any other government organization. While the Postmaster General has made great strides removing costs and increasing productivity through workforce attrition, those savings have not come close to matching the declines in volume and revenue.

The loss of mail to the Internet, compounded by the severe recession that began in 2008, has made this burden untenable.

Reducing Services and Increasing Prices

As you know, the Postal Service has proposed a dual strategy of reducing services and further raising rates. I would argue that there is no other business in America that would pursue such a strategy to achieve its long-term viability. In the past, pricing increases could make up this shortfall. In this environment whether it is for greeting cards, magazines, advertising, catalogs or bill paying, all segments will tell you that the Postal Service cannot price its way to solvency by raising rates. Rate increases at this time will only serve to drive more volume away, increasing costs for mail remaining in the system. This, in turn, will lead to more volume losses creating a vicious cycle that some have described as a “death spiral.”

Similarly, eliminating Saturday mail service will further drive volume away, and ultimately result in less volume and revenue. I am concerned that going down this path does not address the critical issues and we will soon be talking about 4-day or 3-day delivery. Such a Postal Service would no longer “bind the nation together” as required by law -- of rich and poor, city and country. Rather, it will add to the cynical feelings the general public has about government, and it will further erode the value consumers ascribe to the mail as it becomes less timely and less relevant.

What Congress Can Do

So if not rate increases or service cuts, then how should the Postal Service proceed? I submit that Congress should – as a matter of great urgency – make those changes within its power to provide a sustainable business environment in which the Postal Service can stabilize its finances and reduce its costs of operations to protect jobs now and into the future. First, the retiree healthcare pre-payment obligation discussed earlier should be restructured to provide a longer period of time in which to satisfy the responsibility. This would serve to mitigate the year-to-year impact to the USPS operating deficit. No other federal agency is funding these obligations at the rate the Postal Service is required to do and no private company could – and still survive.

Also it should be determined immediately whether the Civic Service Retirement System obligation has been overfunded. If so, this \$75 billion could be applied toward funding the retiree healthcare obligation.

I also support the language, now pending in the Senate, which would allow the arbitrator to consider the financial health of the Service. This is a practical provision that offers the ability to achieve contracts appropriate to the prevailing economic conditions.

Finally, I believe that Congress should provide the Postal Service with the means to manage its facilities in light of volume and capacities. The Presidential Commission on the United States Postal Service recommended the adoption of the military base closing model for a postal commission to make such decisions without undue political interference. The Postal Service has proposed removing language barring the closure of Post Offices for economic reasons. While it is important to protect the public interest by ensuring adequate access to a full

range of postal services, this can be accomplished while allowing the Postal Service to reshape its network for maximum efficiency.

Excess Capacity – A Hidden Opportunity

One area where the USPS can cut costs substantially is mail processing capacity. Unlike delivery service cuts, rate increases, or closing retail post offices, eliminating excess plant capacity is largely invisible to the general public and the customer base of the Postal Service. Yet, despite this advantage, the USPS has gone through three plans since 2005 with little tangible cost savings.

The GAO (General Accountability Office) estimates there is 50 percent excess capacity in mail processing. No business could be sustained with this kind of cost overhang. In addition, the Office of the Inspector General (OIG) has cited data that is quite telling:

- There were 270 mail processing and distribution facilities (P&DCs) in 2005. Only 1% was eliminated by the end of 2009.
- Twenty-one Bulk Mail Centers (BMCs) were determined to be obsolete yet their budgets were reduced by only 2%.
- In 2005 there were 195 customer service centers and by 2009 not a single one had been cut.
- Incredibly, the number of mail processing logistics and distribution centers increased from 11 to 14 between 2005 and 2009.

Clearly no business can be sustained if a 50% over capacity is not acted on.

Key to Sustainability

None of the actions I have mentioned alone is sufficient to solve the projected losses. With more than 80 percent of Postal costs allocated to wages and benefits, Postal management, Union leaders and stakeholders must work together to find solutions that reflect the current financial situation. Over the next two years Labor and Management will be renegotiating contracts. Both parties will raise legitimate issues. The only way to preserve the institution and maximize the number of quality jobs, will be to take actions consistent with a long-term view.

During much of the Postal Service's history continually growing volumes and revenues mitigated the need to become highly efficient. With declining volumes and resources, it will be imperative to become more efficient. Raising prices or cutting service will only work to drive more volume of mail out of the system and put even greater pressure on costs in the future.

Conclusion

The Postal Service's future depends on affordable rates and the ability to provide high levels of service. Current volume and revenue projections make it essential that the Postal Service achieve a sustainable cost structure. Congress has the authority to adjust the obligation for future retiree healthcare costs, grant authority to develop new products and establish greater control over its facility network creating an environment in which the Postal Service can thrive. It should be encouraged to work towards a set of contracts that recognize the current economic realities facing the Service in order to ensure their mutual long term benefit.

And it's not just postal jobs that I'm worried about. The mailing industry has lost 1.5 million jobs since 2006. The remaining 7.5 million jobs rely on a robust Postal Service. Those jobs must be considered as well.

You have an opportunity to take bold action on behalf of the citizens and postal stakeholders. You can make changes that will allow the Postal Service to address undue financial burdens, manage its facility network, continue to provide service and competitive pricing, and retain people in the mail stream.

I am here because we are a partner with the U.S. Postal Service and care deeply about its future. We value the people who work at the Postal Service, the people whose businesses depend on the mail and the American public that is connected by it. Absent a long-term view, prices will continue to increase greater than inflation, more mail will be driven out of the system, and more jobs will be lost.

The future of the Postal Service hangs in the balance.