

# EMBRACING THE FUTURE



**MAKING THE TOUGH CHOICES TO PRESERVE UNIVERSAL MAIL SERVICE**

Report of the President's Commission on the United States Postal Service



President's Commission on the United States Postal Service  
1120 Vermont Avenue, suite 971  
Washington, DC 20005

July 31, 2003

The President  
The White House  
1600 Pennsylvania Avenue, NW  
Washington, DC 20500-0001

Dear Mr. President:

It is our honor to submit to you the final report of the President's Commission on the United States Postal Service. Much has changed since the nation last revisited its mail system in 1970, most notably the rise of the Internet as a faster and more affordable communications alternative. We appreciate the opportunity to work with the Postal Service and the entire postal community to strengthen this vital institution at a pivotal moment in its history.

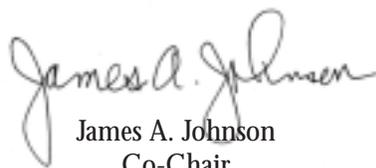
In appointing this Commission, you recognized that the Postal Service faces significant challenges to its fiscal health due largely to an outdated and inflexible business model amid a rapidly changing postal landscape. Having explored in detail the many challenges and opportunities before the Postal Service, the Commission wholeheartedly shares your concerns. However, we are decidedly optimistic about the future of this unique and venerable American institution.

We believe that the Postal Service has an extraordinary opportunity to usher in an exciting new era of greater efficiency and rising value to the mailing public. As a result, while the sustainability of the Postal Service's current business model is in serious doubt, with bold leadership today, the future of universal postal service can most certainly be secured.

Our recommendations aim to tailor the Postal Service to the modern mail needs of the country and focus the institution on "best execution" in all aspects of its operations. It is our hope that a revitalized 21<sup>st</sup> century Postal Service—one that makes best use of every resource it has and takes full advantage of private-sector partnerships and new technologies—can serve as a prime example of how to enhance the quality and cost-effectiveness of operations throughout the Federal government.

Finally, Mr. President, we are not only proud of this report for the scope and ambition of its recommendations, but also for the process that produced it. Numerous public meetings were held across the country. The Commission heard and read statements from hundreds of postal employees, customers, partners, and experts. At every turn, we encouraged and received an open and frank exchange of ideas and opinions. This report was substantially enriched for this broad participation. If the widespread public commitment to making this a constructive process is any indication, then the future of the Postal Service and the mail will indeed be bright.

Sincerely,

  
James A. Johnson  
Co-Chair

  
Harry J. Pearce  
Co-Chair

Attachment



# Embracing the Future

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Report of the President's Commission on the United States Postal Service



## The President's Commission on the United States Postal Service

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# Foreword

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The Commission is honored to have been asked by President George W. Bush to gather the opinions of postal experts, customers, partners, competitors, and employees and craft a vision “to ensure the efficient operation of the United States Postal Service while minimizing the financial exposure of the American taxpayers.” While the challenges before the Postal Service are substantial, so are the abundant opportunities that exist today to enhance both the value of the mail and the institution that delivers it. If the nation embraces an ambitious modernization, then the Commission is very confident that the Postal Service can continue its 225-year tradition of innovation and adaptation to remain a valued and relevant enterprise to the nation it exists to serve.

In making these recommendations, however, the Commission wishes to note that, particularly in today’s technology-driven world, the future has a way of surprising us all. In 1968, the last Presidential Commission on the U.S. Postal Service made important strides in the delivery of the nation’s mail. While it urged greater use of technology to automate the largely manual processes of the Postal Service at the time, that Commission could not have foreseen the coming Internet revolution and its dramatic impact on traditional mail volumes, which so profoundly make the case for ambitious new reforms today.

Similar breakthroughs certainly could change the fundamentals underlying the assumptions made in this report. For this reason, the Commission did not set out to define a Postal Service for the new millennium. Rather, it set a more modest 15-20 year horizon. Additionally, many of the recommendations included in this report aim to build more flexibility into the Postal Service, so key aspects of the institution—from the scope of the postal monopoly to the size of the postal network itself—are not set in stone, but rather are managed in a dynamic way that is more capable of successfully adapting to change in a timely fashion.

The long-term fate of the Postal Service and hard copy correspondence in the Information Age is impossible to see clearly from today’s vantage point. Projecting future mail volumes is an inexact science at best, particularly in the modern context where technologies change rapidly. The Commission believes, however, that Internet use is likely to divert increasingly larger portions of the mail stream to the electronic format. The chart

below illustrates the unprecedented near- and mid-term threat posed by technology to the Postal Service's bottom line under one possible scenario:

<b>A Costly Status Quo: Projected Mail Volumes &amp; Fiscal Health</b>					
<i>(in millions)</i>					
Year	2002	2003	2007	2012	2017
<b>Mail Volume</b>	202,822	202,200	208,900	201,500	181,700
<b>Operating Revenue</b>	\$66,463	\$68,868	\$75,000	\$81,000	\$83,000
<b>Operating Expenses</b>	\$67,139	\$64,368	\$74,000	\$85,500	\$91,500
<b>Net Income (Loss)</b>	(\$676)	\$4,500	\$1,000	(\$4,500)	(\$8,500)
<b>Cumulative Net Income (Loss)</b>	(\$6,036)	(\$1,536)	\$4,250	(\$6,700)	(\$47,500)

Source: Mail volume and financial projections are based on the "Gradual Displacement Scenario," contained in "Two Scenarios for Future Mail Volumes, 2003-2017," Greg Schmid, Institute for the Future, May 2003 (prepared for the Commission). Assumptions reflected in the projections include the following: operating revenues are based on rates adjusted annually at CPI (2.5%); labor-related costs are increased annually by 3.5%; non-labor costs are increased annually by 2%; and operating expenses have been adjusted to reflect volume variances.

These projections reflect independent analysis performed for the Commission. They incorporate the projected savings anticipated by the Postal Service's own reforms already underway. This forecast also assumes that postage rates will continue to adjust with inflation, as they have for the past 30 years. Even with these revenue-positive factors, the 15-year outlook for the Postal Service remains grim and makes a powerful case for a far more ambitious overhaul of the nation's postal system.

The specific numbers cited above are, of course, speculative. But the trends they foresee are sobering and credible: The traditional mail stream will likely continue to migrate to cheaper Internet-based alternatives. Largely as a result, the Postal Service will increasingly find it difficult to meet its "break-even" mandate (i.e. charging just enough for postage and other services to cover expenses). And, even if postage rates continue to adjust for inflation, the Postal Service, over the next 15 years, is likely to run substantial deficits. Equally discouraging, these obligations would pile on top of the Postal Service's \$92 billion in current debt and other unfunded obligations.

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Without significant modernization, the Postal Service will have three choices: dramatically roll back service, seek a rate increase of unprecedented scale, or fall even further into debt, potentially requiring a significant taxpayer bailout. Clearly, the public interest is better served by a strategy that aims instead to root out the substantial inefficiencies and other unnecessary costs apparent throughout the institution today in order to produce a far more efficient and capable 21<sup>st</sup> century Postal Service.

Toward this end, it is the Commission's emphatic view that an incremental approach to Postal Service reform will yield too little too late given the enterprise's bleak fiscal outlook, the depth of current debt and unfunded obligations, the downward trend in First-Class Mail volumes and the limited potential of its legacy postal network that was built for a bygone era.

The American people deserve the most capable and efficient Postal Service that modern techniques and "best execution" strategies can make possible. With strong management and employee performance, sound partnerships and sophisticated technologies, the Commission is confident that the Postal Service can dramatically reduce its costs and stabilize its bottom line. The Commission also firmly believes that e-mail, despite its significant inroads, does *not* spell the end of the traditional mail system—at least on the horizon of our report. Thus, the biggest threat today is being too timid in the area of postal modernization and gambling with the future of affordable, universal mail service, in the process.

Already, important progress has been made by Congress and by the Postal Service itself. This report aims to accelerate and elevate the pace and direction of these changes. In doing so, it is the Commission's hope that these recommendations can ensure a strong future for universal postal service and, perhaps by doing so, encourage other Federal agencies to refocus on their core value, rethink how they do business, and reshape public service in the process.



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# Executive Summary

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Universal postal service remains vital to the nation and its economy at the dawn of the 21<sup>st</sup> century. Unfortunately, the institution that delivers it is in significant jeopardy. Buffeted by the mounting costs of an inefficient delivery network and the popularity of electronic mail, the Postal Service has more than \$90 billion in debts and unfunded obligations and an unstable financial outlook. Absent fundamental reforms, the risk of a significant taxpayer bailout or dramatic postage rate increases looms large.

As a result, the nation must make a defining choice about the future of its Postal Service: It can prepare to pay—either on tax day or at the post office—for increasingly dated and costly mail service. Or, it can permit an ambitious modernization that embraces proven business strategies, private-sector partnerships and new technologies to rein in costs aggressively and improve service.

To continue the nation's commitment to affordable universal postal service, President Bush last year formed the President's Commission on the U.S. Postal Service "to ensure the efficient operation of the United States Postal Service while minimizing the financial exposure of the American taxpayers." It is no small task considering the size and unique nature of the institution. The Postal Service is a \$67-billion organization, the 11<sup>th</sup> largest U.S. enterprise by revenue, the second biggest employer in the nation, and the hub of a thriving domestic mailing industry. It also has a rare charter for a Federal institution—to operate like a business, financing its operations through "break-even" sales rather than Congressional appropriations.

The laws governing the Postal Service have not been substantially revised in more than 30 years. These rules were written well before the Internet offered a cheaper, faster form of correspondence and far in advance of the Information Revolution's profound leaps in technology-driven opportunities to reduce costs. Now is the time to revisit these rules and modernize the Postal Service to not only preserve its future, but also to enhance its service to all Americans.

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## Universal Postal Service Is at Risk

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First-Class Mail volumes appear to be on the brink of long-term decline as more Americans take advantage of cheaper electronic alternatives. The rates of growth for First-Class Mail and Standard Mail, that together generate more than 75% of all postal revenues, have been in long-term decline since the 1980s. Electronic diversion threatens to accelerate this trend significantly. Unless Postal Service expenses can be similarly reduced, it is questionable whether affordable universal mail service via a self-financing public institution is sustainable.

With its debt reaching destabilizing levels and its traditional revenue streams in retreat, the Postal Service's transformational efforts and long-term outlook were placed on the U.S. General Accounting Office's "high-risk list" in 2001. At the request of Congress, the Postal Service began developing its Transformation Plan to adapt to the future. Since the Plan's release in April of 2002, the Postal Service has reduced its workforce by more than 40,000 career positions and will deliver \$2.5 billion in annual cost savings by September 30, 2003. However, even with this substantial progress, it is quite possible that the Postal Service will experience significant (and rapidly ballooning) deficits within just a few years' time, even if stamp prices continue to rise with inflation. This prospect points to the urgent need for a far more sweeping set of reforms.

Even if the Postal Service were not in financial jeopardy, however, the inefficiency of its operations and legacy network today causes billions of dollars in unnecessary costs that should be eliminated rather than passed on to ratepayers. Far more emphasis must be placed on restoring fiscal stability not by ratcheting up rates or scaling back service, but by aggressively rooting out inefficiencies throughout the Postal Service.

Unfortunately, a cumbersome regulatory and rate-setting model, the entrenched cost of an aging infrastructure, inflexible work arrangements, and other significant obstacles clutter the path to a fundamental overhaul of the Postal Service. As a result, the institution urgently requires broader flexibility to adjust to increasingly dynamic markets and to pursue new strategies to bring revenues and expenditures into balance without sacrificing quality of service and the ability to meet the nation's evolving postal needs. In short, the Postal Service needs a new business model for the modern world and the changing postal needs of the nation.



Source: USPS.

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## The Postal Service Should Remain a Public Institution

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The Commission believes that the Postal Service should remain an independent entity within the executive branch of the Federal government with a unique charter to operate as a self-sustaining commercial enterprise. Some have suggested that for the Postal Service to best act like a business, perhaps it should *become* a business. The Commission believes an abrupt privatization of the Postal Service is far too risky and would unnecessarily destabilize universal mail service.

The Postal Service delivers more than 200 *billion* pieces of mail per year across the vast geographic expanse of the United States. Privatization of a commercial entity the size of the Postal Service could seriously disrupt both mail service and the private postal marketplace. It is highly unlikely that the private sector, acting alone, could provide the *universal* mail services we have come to expect from the Postal Service. For the Postal Service itself, privatization would likely involve a decade or more of wrenching organizational changes that could undercut the stability and continuity that are the hallmark of public postal service. Thus, the Commission believes that the preferred strategy is a more *evolutionary* approach, under which the Postal Service is maintained as a public entity, but refocused and reorganized to enhance its efficiency and adaptability in the face of an uncertain, and ultimately more competitive, future.



Source: USPS.

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## Postal Monopoly Should be Clarified and Narrowed Over Time

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Once the conclusion has been reached that the Postal Service should remain a public institution, an urgent need arises to modernize and clarify the mechanism that finances its operations—the postal monopoly.

A great deal of confusion exists today, even at the Postal Service, about the true extent of its scope. This confusion is understandable considering much of the nation's postal monopoly law dates back to 17<sup>th</sup> century England and is virtually untranslatable in the modern environment.

The Commission recommends that an independent Postal Regulatory Board be established to provide broad public-policy oversight of the Postal Service. Among its tasks should be translating the monopoly's musty definition into straightforward, modern language that reflects the postal monopoly as the nation relies on it today. Specifically, the Commission proposes that the boundary lines be clearly and narrowly drawn by weight and by price (to permit private express carriers to handle mail of less than 12 ounces, so long as they charge at least six times the price of a First-Class stamp).

While a postal monopoly remains essential to the reliable, affordable provision of universal postal service today, the Commission acknowledges that this may not always be the case. As such, it recommends authorizing the independent Postal Regulatory Board to periodically review the scope of the monopoly with an eye toward narrowing it over time, so long as a greater reliance on a thriving private postal marketplace can occur without sacrificing universal, affordable access to essential postal services.

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## The Postal Service Should Focus on its Core Value: Universal Mail Service

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Delivering high-quality service in an era of stagnant mail volumes will require the Postal Service to recognize that as demand for its services contracts, so, too, should the institution. To do so without sacrificing essential services, however, will require the Postal Service to focus on its core value: the reliable, affordable delivery of the mail to every American home and business.

While the Postal Service in recent years has explored an array of new revenue streams far afield of what most Americans consider “postal services,” the Commission recommends that the Postal Service be restricted to products and services related to the delivery of letters, newspapers, magazines, advertising mail, and parcels. More broadly, the Commission recommends that the mission of the Postal Service be “to provide high-quality, essential postal services to all persons and communities by the most cost-effective and efficient means possible at affordable and, where appropriate, uniform rates.” This definition focuses the organization on universal service. It makes cost-effectiveness an explicit obligation. It asserts that affordable rates do not come at the expense of service, and it opens the door to greater involvement of the private sector in the delivery of the nation’s mail.

The Commission strongly endorses the basic features of universal mail service today—affordable rates, six-day delivery, and convenient community access to retail postal services. However, in such a rapidly changing mail environment, the Commission cautions against building rigidities into the system. Instead it proposes that a mechanism be put in place to permit some flexibility over the scope of the universal service obligation in the future. This can be achieved by authorizing the independent Postal Regulatory Board to periodically review the universal service obligation as the nation’s reliance on its mail system continues to evolve.

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## The Postal Service Should be Guided by Best Business Leaders, Practices

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If the Postal Service were a private endeavor, it would rank eleventh on the Fortune 500 list of the largest corporations in the United States based on revenues. It is the second largest employer of Americans today. Through its vast national delivery network, it connects virtually every American home and business. Given its importance to the country and its businesslike mandate, the Postal Service should have the best corporate leadership available today and an unwavering commitment to best execution in every aspect of its operations.

Both the Postal Service and its customers would benefit greatly from the creation of a strong, independent, and experienced Board of Directors of a stature that truly reflects the size and significance of the Postal Service's work. This Board would apply the best practices of the business world and would attract members with the talent and skills necessary to transform the Postal Service into a world-class service business. The Board's overriding mission would be guiding the Postal Service to a standard of excellence that consistently rivals the private sector in both productivity and quality of service. The Board also would be responsible for holding management accountable for performance and for ensuring that Congress and the American people are fully informed of the institution's fiscal health.

To ensure that the Board is most capable of fulfilling its duties, the Commission recommends a new structure and scope of responsibilities, modeled after the most successful corporate boards in America (detailed in Chapter 3). This would help ensure that the Board operates in the most efficient and productive manner possible, is safely distanced from undue political influence and has the depth and diversity of skills necessary to guide the Postal Service to a higher level of operations and a more stable long-term fiscal outlook.

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## The Postal Service Requires Broader, Constructive Oversight

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The Commission proposes transforming the narrowly focused Postal Rate Commission (“PRC”) into an independent Postal Regulatory Board with broad authority to safeguard the public interest without micromanaging day-to-day postal operations.

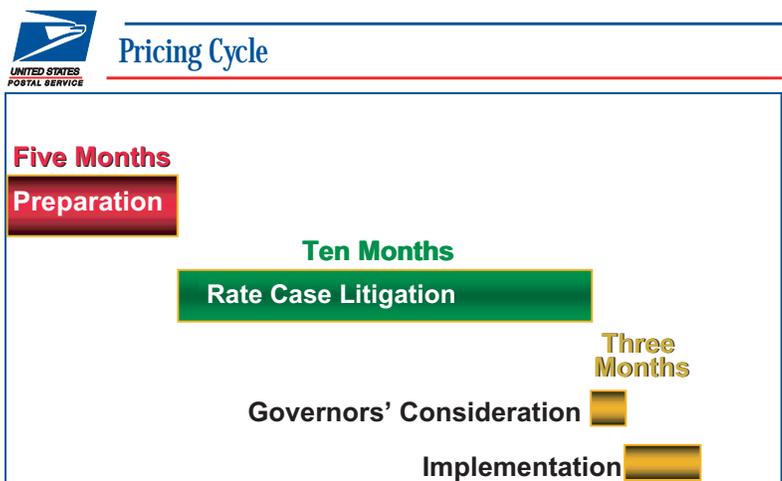
Rather than a sole focus on rate-setting and mail classifications, the Postal Regulatory Board would be tasked with broad public-policy oversight, including: ensuring financial transparency; guarding against the cross-subsidization of competitive products; reviewing the scope of the postal monopoly; limiting the prices charged for non-competitive products; overseeing the scope of the universal service obligation; reviewing worksharing and other discounts; reviewing changes to service standards that may have a substantial and negative national impact; and ensuring the Postal Service meets its statutory obligation to compensate its employees at a level comparable to (but not exceeding) the private sector.

The Commission envisions a Postal Regulatory Board that is an independent establishment of the executive branch of the U.S. government and is composed of three individuals of significant stature, appointed by the President of the United States and confirmed by the Senate.

Once assembled, the Postal Regulatory Board should move quickly to improve the rate-setting process for both postal customers and managers. The current process is far too cumbersome and time-consuming, with rate changes taking as long as 18 months, an impossible situation for an institution charged with the responsibility of acting in a businesslike manner.

As an alternative to the current process, the Commission proposes the establishment of a rate-ceiling mechanism that would allow prices for non-competitive products to be adjusted upward within strict limits, subject to an after-the-fact review by the Postal Regulatory Board. Specifically, the Commission proposes setting the ceilings below inflation, thereby restricting revenue growth to motivate the Postal Service to pursue a far higher standard of efficiency.

A well-designed rate ceiling could produce a Postal Service much more aligned with the interests of ratepayers, who would prefer that the Postal Service aggressively tackle unnecessary costs before asking them to pay more for stamps. However, designing this mechanism is an intricate undertaking. Fortunately, recent legislation signed into law by President Bush strongly discourages the Postal Service from increasing rates before 2006, providing ample time for the Postal Regulatory Board to fine-tune a workable rate-ceiling mechanism.



Source: USPS.

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## The Nation Should Overhaul Its 1950s Era Postal Network

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Few dispute the fact that the postal network as it exists today is far too sprawling and cumbersome for the nation's needs. Fortunately, through the strategic deployment of new technologies, partnerships with the private sector and appropriate cost-reduction strategies, the Postal Service has significant opportunities to grow smaller *and* stronger—upholding and advancing the nation's commitment to universal service without overburdening ratepayers. Achieving this vision will take flexibility on the part of all who have an interest in the Postal Service's success—customers and employees, partners and politicians.

The Postal Service deserves praise for its recent efforts to create a sound analytical basis for redesigning the postal network. Accelerating these efforts, as the Commission recommends, involves permitting a whole-scale realignment with full public participation but also free from undue external intervention.

Toward that end, the Commission envisions an independent process, much like that governing military base closures in the 1990s, for consolidating and closing back-end processing and distribution facilities. Additionally, the Postal Service should carefully study and contemplate end-to-end standardization of the postal network to reduce the uneven nature of many postal processes and facilities that combine to create wide variances in productivity levels among facilities, adding up to billions of dollars in unnecessary costs.

The Commission has also examined the Postal Service's network of 38,000 post offices. In the Commission's view, "low-activity" post offices that continue to be necessary for the fulfillment of the Postal Service's universal service obligation should *not* be closed, even if they operate at a substantial economic loss. In circumstances where universal service is protected, the Postal Service should have the flexibility to dispose of "low-activity" post offices with appropriate community involvement.

In addition, the Commission strongly recommends that the private sector become more involved in the delivery of the nation's mail. Most Americans are unaware of the extent to which private companies already play key roles throughout the postal network—handling, for example, most long-haul air transport and performing certain processing, distribution, and shipping functions. The Postal Service is also a global pioneer in innovative worksharing partnerships with some of its most active customers. Where additional partnerships advance service and reduce costs, the Postal Service should embrace them and recognize their ultimate value to the customers it serves.

This report also identifies a number of additional areas where the adoption of innovative private-sector strategies could likely deliver significant additional savings, particularly in the areas of procurement reform and more active management of the Postal Service's substantial real estate portfolio. In virtually every aspect of its operations today, the Postal Service has ample opportunities to adopt innovative approaches, learn from the successes of the business world, and deliver significant cost savings to the American people. As a public institution, the Postal Service is duty-bound to aggressively pursue them all.

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## Encouraging a Culture of Excellence in the Postal Workforce

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Few of the reforms outlined in this report are possible without the support and contributions of the Postal Service's most mission-critical asset: its workforce.

The Postal Service employs approximately 843,000 people, making it the second largest workforce in the U.S. Its jobs are highly coveted. As of July 2001, the Postal Service had a backlog of some 400,000 job applicants and virtually no turnover. Contributing to the Postal Service's ability to recruit and retain employees is the special status within the Federal government of postal workers, who enjoy the right to collectively bargain. The Postal Service is also required by statute to compensate employees at a level comparable to the private sector. In addition, postal employees have among the most attractive benefits packages in the nation.

The Commission strongly supports the right of postal workers to collectively bargain and to be compensated at a level comparable to that of the private sector. For an institution tasked with operating like a business, both of these tools are essential to maintaining a world-class workforce capable of delivering the 21<sup>st</sup> century Postal Service envisioned by this report.

Critical to this effort, however, is the ability of management and labor to work constructively together to determine the right *size* of the postal workforce and to ensure appropriate flexibilities in its deployment. Both are significant issues. More than \$3 out of every \$4 in Postal Service revenues go to cover the costs of current and retired postal employees. Of the approximately \$92 billion in debt and unfunded obligations the Postal Service is struggling with today, more than \$48 billion is due to the costs of retiree health benefits alone.



Source: USPS.

Far more than individual benefits, the *size* of the workforce determines the *costs* of the workforce. Therefore, getting the right size workforce is *the* critical issue when it comes to controlling the costs of the workforce and upholding the Postal Service's ability to compensate its employees in a manner competitive with the private sector. Fortunately, there is a significant attrition opportunity, with some 47% of current career employees eligible for regular retirement by 2010 that can help guide the rightsizing of the workforce in the least disruptive manner possible.

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Beyond the size of the workforce, the ability to deploy workers in the most efficient manner possible and create a culture of excellence are essential. Achieving a more positive and productive climate will require a number of steps.

First, Postal Service management must repair its strained relationship with employees, manifested in the high number of grievances filed and appealed and the frequency of contract negotiations proceeding to protracted arbitration.

Second, management and employee unions must have a more constructive collective bargaining mechanism to work together to bring expenses and revenues into alignment (detailed in Chapter 6). This includes being able to negotiate wages *and* benefits. It also entails authorizing the Postal Regulatory Board to develop a fair and impartial mechanism for ensuring total compensation is comparable to the private sector, but does not exceed that generous standard.

Third, the Postal Service must build an incentive-based culture that encourages excellence by developing a pay-for-performance program that rewards all employees for contributing to the success of Postal Service reform.

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## Information Technology Can Deliver the Future of Mail Today

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While many of the challenges before the Postal Service are technological in nature, these same technologies also present substantial *opportunities* to deliver the nation's mail more efficiently and in a way that markedly increases its value.

By placing a unique barcode on every piece of mail and investing in technologies throughout the postal network that can put that information to use to enhance customer service and reduce costs, the Postal Service can begin building a truly digital network that links postal facilities, vehicles, partners and employees not only to each other, but also via the Internet to customers and to the mail itself.

By applying the sophistication of the electronic world to the physical mail, the Postal Service can develop a new postal proposition for the 21<sup>st</sup> century, known as Intelligent Mail, and make its advantages available to *all* customers. Intelligent Mail could allow the Postal Service to permit mail-tracking and other in-demand services via a robust website that ultimately becomes the equivalent of an always open, full service post office. Intelligent mail also can significantly improve mail security through enhanced traceability, and could lead to substantial savings through sophisticated, real-time logistics management. Adopting this system will lead to the development of “personalized” stamps that digitally embed basic information (such as the sender, the class of mail, and the destination) to enable a highly automated and efficient journey. This advance also could allow customers to design their own stamps, perhaps adding a family photo or small business logo.

While the technology needed to make this vision a reality will require significant investment, the Commission is confident that the resulting efficiency and revenue gains, as well as service improvements, will deliver the necessary returns to the Postal Service and its customers, if successfully executed.



A next generation barcode (wavy lines) encodes data in a color field that includes postage value, date, and serial number (shown underneath as text), and is spread throughout the color field.

Source: Escher Group

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## The Postal Service Customer Experience Will Advance Significantly

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The reforms included in this report aim not only to stabilize the Postal Service, but to revolutionize its customer service. While *how* the Postal Service conducts its business will change dramatically (and for the better), from the customer's perspective, service will be significantly enhanced. From mail tracking to personalized stamps to more consistently cost-efficient and high-quality operations, the focus on customer service is apparent throughout this report.

While an independent survey performed for the Commission found that most Americans are generally happy with their postal service, complaints typically revolved around actually *visiting* a post office. To address the issue of inconvenient hours and waiting in line, the Commission recommends expanding and accelerating efforts already underway at the Postal Service to bring a wider array of services to customers in convenient locations *throughout* their community—from grocery stores, to pharmacies, to cash machines, and even into homes and businesses via a more robust and user friendly Postal Service website.

This revolution in retail access would allow postal customers to avoid the greatest inconvenience of a post office—having to make a special trip there. These alternative venues would feature expanded hours of service, including around the clock access at sophisticated self-service kiosks that can perform all the most popular functions of a post office. This enhanced customer convenience is also a plus for the Postal Service's bottom line, since these more convenient customer points of access are generally more cost-effective than service delivered at the post office itself.



Source: USPS.

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## Conclusion

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The Postal Service must be freed from unnecessary and outdated statutory constraints. In turn, by cutting costs and better managing its assets, by increasing organizational effectiveness and streamlining production and distribution facilities, by shaping more effective private-sector partnerships, by offering greater financial transparency, and by rightsizing and rewarding the workforce for superior performance, the Postal Service can enhance the value of the mail in the modern context and deliver a capable, sophisticated and leading-edge 21<sup>st</sup> century national postal endeavor.

Ensuring a bright future for universal postal service will require bold choices and broad national support. With it, the Postal Service can deliver the mail as never before and offer an example to other Federal institutions about reducing costs while enhancing their service to the nation.



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# Chapter 1: Adapting to a New World: Universal Mail Service at Risk

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## Introduction

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For more than 225 years, the national post office has bound the country together and advanced commerce by enabling the exchange of goods, ideas and information. From the humble beginnings of 30 post offices spread across the American colonies, today's Postal Service has roughly \$67 billion in annual revenues,<sup>1</sup> making it the 11<sup>th</sup> largest enterprise by revenue<sup>2</sup> in the nation and the hub of a thriving domestic mailing industry.

Without question, the Postal Service has made an extraordinary contribution to the economic health and unity of the nation. But tough choices are required now in order to overcome significant challenges to the institution's continued ability to ensure universal mail service at affordable rates. Like some private-sector delivery services, the Postal Service today is suffering from weak mail volumes and rising labor and infrastructure-related costs. In the third quarter of 2003, the Postal Service had a revenue shortfall of nearly half of a billion dollars.<sup>3</sup> In addition to these pressures, significant debt loads, network inefficiencies and rigid statutes governing the institution's management are preventing the Postal Service from adequately adapting to the fundamental market and technology changes underway, placing at risk its ability to deliver the nation's mail at affordable rates.

While many of these trends are exacerbated by a weak economy and other cyclical factors, the most significant threat is not. To the contrary, it appears that the nation is at the beginning of a long-term decline in First-Class Mail volumes as more and more Americans take greater advantage of cheaper electronic communications alternatives. In this new environment, unless Postal Service operating expenses can be reduced correspondingly, it is questionable whether affordable universal mail service via a self-financing public institution is sustainable.

Fortunately, the Commission and many others, including the Postal Service itself, have identified dozens of organizational and policy changes which can ensure continued high-quality and efficient delivery of the nation's mail at affordable rates. Taken together, they will produce nothing short of a fundamental transformation of the United States Postal Service.



Source: USPS.

## Postal Service Has Begun the Reform Process

The Bush Administration, the United States Congress, and the Postal Service are to be commended for recognizing the need for and beginning the process of fundamental change. In its 2002 Transformation Plan, the Postal Service calls for the evolution of the institution into a “Commercial Government Enterprise,” a more agile government entity that maintains its universal service duties, but also enjoys greater flexibility to operate in a more businesslike manner. This Plan was produced at the request of the United States Senate, which grew concerned about the Postal Service’s long-term ability to fulfill its universal service obligation in the wake of a report by the U.S. General Accounting Office (“GAO”) placing the Postal Service on its “high-risk list.”<sup>4</sup> GAO’s April 2001 report was, in turn, developed as a result of extensive hearings in the U.S. House of Representatives on the need for postal modernization.

### Spotlight

*The Transformation Plan appropriately identifies the core institutional challenge facing the Postal Service: “a modern, self-sufficient postal system...requires new flexibility to adjust networks and services to modern conditions and to minimize entrenched governmental rules and expectations that carry with them costs and inefficiencies.”*

The Transformation Plan recognizes that revisiting the core elements of the institution—from the postal monopoly, to governance and regulatory structures, to workforce and infrastructure costs—is essential to the Postal Service’s continued ability to deliver universal postal service. The Plan also appropriately identifies the core institutional challenge: “a modern, self-sufficient postal system...requires new flexibility to adjust networks and services to modern conditions and to minimize entrenched governmental rules and expectations that carry with them costs and inefficiencies.”

Since the Transformation Plan’s release in April of 2002, the Postal Service’s substantial workforce has been reduced by more than 40,000 career positions. By the end of September 2003, the Postal Service expects to have captured \$2.5 billion of the \$5 billion in annual cost savings it aims to attain by 2006. Despite this laudable progress, overall growth in operating expenses outpaced growth in operating revenues in fiscal years 2000 to 2002.<sup>5</sup> So while these efforts are a critical down payment on the enhanced productivity and fiscal discipline necessary, the Postal Service requires reform on a far grander scale.

## Presidential Commission Tasked with Accelerating the Transformation

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In recent years, Congress has debated several proposals to make a modern, self-sufficient Postal Service a reality. But given the inevitable political pressures surrounding an agency with such a strong local presence and large employee base, no comprehensive legislation reforming the Postal Service's business model has been enacted since 1970. To overcome these hurdles and restore the Postal Service to a solid, stable footing, President Bush appointed this Commission to craft a vision "to ensure the efficient operation of the United States Postal Service while minimizing the financial exposure of the American taxpayers."<sup>6</sup>

The Executive Order's comprehensive mandate instructs the Commission to explore the key questions that will determine the Postal Service's role in the 21<sup>st</sup> century, including:

- What flexibility should the Postal Service have to change prices, control costs, and adjust service in response to financial, competitive or market pressures?
- Do rigidities in cost or service limit the efficiency of the postal system?
- How can universal mail delivery at affordable rates be sustained over the long term in a way that will allow the Postal Service to cover its significant liabilities with minimum exposure to the American taxpayer?
- Do postal monopoly restrictions continue to advance the public interest today or do they now permit the Postal Service to compete unfairly with the private sector?
- And, what is the most appropriate governance and oversight structure for the Postal Service?

## The Case for Change

A number of trends are driving the need for such a sweeping exploration of the Postal Service's role and operations in the 21<sup>st</sup> century. Chief among them is the fact that the rising cost of operating the Postal Service is on a collision course with declining mail volumes. The *rates of growth* for First-Class Mail and Standard Mail, the twin engines of Postal Service cash flow that together generate more than 75% of all postal revenues,<sup>7</sup> have been in long-term decline since the 1980s.<sup>8</sup> Looking ahead, electronic diversion of First-Class Mail threatens to accelerate this decline significantly. At the same time, a cumbersome regulatory and rate-setting model, the entrenched cost of an aging infrastructure and inflexible work arrangements make difficult the ambitious overhaul of the Postal Service that is needed today.

There are three ways the Postal Service can adapt to declining mail volumes: by 1) aggressively reducing costs, 2) expanding revenues, or 3) undertaking a combination of both strategies. While some potential exists to increase revenues, particularly in the area of Intelligent Mail (see Chapter 7), a significant portion of the Postal Service's fiscal stabilization must come from reduced costs through the modernization of every element of its operations, service delivery and asset management. This reality is magnified by the Postal Service's sizable debts and ongoing obligations.

Despite numerous rate increases and efforts to reduce costs through attrition-led downsizing and investment in automation, the expense of the Postal Service's legacy networks and large employee base are expected to outpace the growth in its operating revenue. This trend threatens to increase the debt load being carried by the Postal Service and provides no cushion to address a retiree health benefit obligation of

**Exhibit 1-1.**

Liabilities and Obligations (in Millions)			
	2001	2002	May 16, 2003
Debt to U.S. Treasury	\$11,315	\$11,115	\$7,275
CSRS Deferred Pension Liability	\$32,023	\$32,231	\$5,824
Other Liabilities (e.g., workers' compensation, accrued leave)	\$18,079	\$18,671	\$19,934
<b>Total Liabilities per USPS Financial Statements</b>	<b>\$61,417</b>	<b>\$62,017</b>	<b>\$33,988</b>
Obligation for Retiree Health Care Benefits	Est. \$46,400	Est. \$48,000	Est. \$48,800
Minimum Payments on Non-Cancelable Operating Leases	\$9,383	\$9,604	Est. \$9,750
<b>Total Liabilities and Other Obligations</b>	<b>Est. \$117,200</b>	<b>Est. \$119,621</b>	<b>Est. \$92,538</b>

approximately \$48 billion, an unfunded workers' compensation liability of approximately \$6.5 billion, an unfunded pension liability of \$5.8 billion, and more than \$7 billion owed the U.S. Treasury. Each of these factors presents an enormous challenge to the Postal Service. Together, they add up to a pressing need for an ambitious modernization (see Exhibit 1-1).

Source: Debt to Treasury, CSRS Deferred Pension Liability and Other Liabilities obtained from USPS annual and quarterly reports. Obligation for Retiree Health Care Benefits derived from Congressional Budget Office letter to the Honorable Jim Nussle, dated January 27, 2003. Minimum Payments on Non-Cancelable Operating Leases obtained or derived from USPS Annual Reports.

While it is true that the Postal Service anticipates ending Fiscal Year 2003 with a significant surplus, this outcome is primarily the result of the most recent rate increase and the effect of legislation, passed in April 2003, lowering the Postal Service's annual pension contribution to the Civil Service Retirement System. Neither of these developments, however, is adequate to address the long-term outlook of the Postal Service. According to independent, in-depth financial analyses performed for the Commission, even factoring in these developments, the Postal Service is projected to run significant deficits within five years, adding to its already destabilizing debt load. Fundamental change is the only option that will deliver a high-quality, financially stable Postal Service.

While the Postal Service is not in crisis today, it is under extraordinary pressure to perform at a higher level. Rapidly changing economic, business and technological realities are rendering its legacy business model and structure counterproductive to the Postal Service's ability to perform its most vital function: ensuring the universal availability of reliable, affordable postal services. The institution today needs broader flexibility to adjust to increasingly dynamic markets and to pursue new strategies to bring revenues and expenditures into balance without sacrificing quality of service and the ability to meet the nation's evolving postal needs. In short, the Postal Service needs a new business model for the modern world and the changing postal needs of the nation.

**Exhibit 1-2.**

### Gradual Displacement of Mail Volume (billions)

	2002	2007	2012	2017
First Class	102.4	98.7	90.5	81.0
Priority	1.0	1.1	1.2	1.3
Periodicals	9.7	9.5	9.1	8.7
Standard Mail	87.2	97.1	98.2	88.1
Package Service	1.1	1.1	1.1	1.2
International	0.9	0.9	0.9	0.9
Other government	0.5	0.5	0.5	0.5
Total	202.8	208.9	201.5	181.7

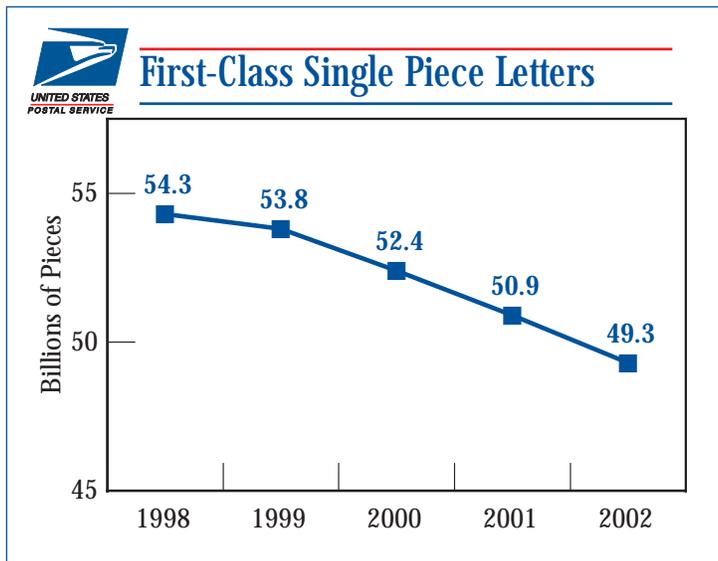
Source: "Two Scenarios of Future Mail Volumes, 2003-2017," Greg Schmid, Institute for the Future, May 2003 (prepared for the Commission).

### *Challenge #1: Electronic Diversion of Mail Changes Everything*

In 2002, the volume of First-Class Mail (single-piece letters and bulk mail)—which accounts for more than half of all Postal Service revenues—declined for the first time in more than a quarter century.<sup>9</sup> The next most lucrative category of mail—Standard Mail—has experienced only anemic revenue growth in recent years.<sup>10</sup> Detailed projections produced for this Commission indicate that these trends likely mark the beginning of a permanent shift of key correspondence to electronic format.

This trend alters the most basic assumptions of the Postal Service business model. It poses a significant financial risk to ratepayers and taxpayers alike, should the Postal Service prove unable to adapt to a sustained period of declining or stagnant mail volumes. While the Commission, of course, cannot predict the pace or scope of this decline, any discussion of the future of the Postal Service must take into account its potential implications.

**Exhibit 1-3.**



Source: USPS.

Electronic substitution is the primary reason long-term First-Class Mail volumes are threatened. The initial rise of the Internet, e-mail, instant messaging and other communications trends siphoned away a large share of personal, one-to-one correspondence. As a result, First-Class single-piece letters began to decline a full five years ago—dropping steadily from 54.3 billion pieces in 1998 to 49.3 billion in 2002 (Exhibit 1-3).

As Americans become increasingly comfortable doing more complex correspondence on-line, the subcategory of First-Class Mail now most vulnerable to erosion is bill payment. Businesses have a strong incentive to encourage this trend: processing a digital payment over the Internet costs between one-third and one-half less than a check sent through the mail.<sup>11</sup>

Customers are drawn to the convenience of on-line bill payment. With many Americans growing more comfortable performing secure financial transactions on-line, over the last five years, businesses and consumers have steadily transitioned to electronic payments. Today, 1 in 4 consumers pay at least *some* bills on-line. Interestingly, consumers are more reluctant when it comes to electronic bill *presentment*, with nearly half of those queried stating firmly that they are “not at all” comfortable with receiving electronic bill statements.<sup>12</sup>

Nevertheless, over the next eight years, as much as 20% of bill payment and some presentment could occur electronically rather than through the mail.<sup>13</sup> This poses a significant threat to Postal Service revenue since more than half of all First-Class Mail is composed of communications from businesses and other organizations to households, primarily the invoices and payments now shifting on-line.<sup>14</sup>

Financial institutions, telecommunications services and credit card companies are aggressively seeking to accelerate this trend. Rather than charging for the convenience of on-line bill paying, as they did a few years ago, banks now offer incentives to customers who pay bills through their website—everything from cash to Caribbean cruise raffles.<sup>15</sup> These marketing campaigns, along with the technology’s cost savings and convenience, are combining to make paying bills on-line the fastest-growing use of the Internet today, eclipsing catching up on the news, looking up movie times and downloading music.<sup>16</sup> However, there are some signs that this trend may now be maturing. In fact, a recent poll indicates that 42% of Americans remain flatly uninterested in paying their bills on-line over the next five years, underscoring the continued need for a strong, reliable national postal system.<sup>17</sup>

### Personal Letters a Smaller Portion of the Mail Mix

*In the digital era, mail use is changing dramatically. Unlike 30 years ago, letter correspondence is no longer the most affordable way to keep in touch with friends and loved ones. From the popularity of cell phone plans with “free evening and weekend minutes” to the explosion in e-mail and instant messaging, personal correspondence now is a relative rarity for many Americans at times other than major holidays. Indeed, mail emanating from households accounts for only 22% of overall volume,<sup>18</sup> and this household-generated mail is overwhelmingly aimed at businesses, the government and non-profit organizations. In other words, individual Americans primarily rely on the Postal Service to deliver their bills, taxes and charitable giving.*

*As individual households rely more and more on the Internet for a wider array of their communications, the nation’s Postal Service—by default—is becoming primarily a medium for the transmission of business correspondence. All tallied, bill presentment and payment, commercial correspondence and advertising combine to generate 93% of total U.S. First-Class Mail volume today.<sup>19</sup>*

While electronic correspondence undoubtedly enhances convenience and offers new cost-saving options for individual consumers and businesses alike, its rising popularity calls basic assumptions underlying the Postal Service's current business model into question and, with it, the Postal Service's continued ability to meet the nation's postal needs while minimizing the cost to ratepayers and the risk to taxpayers.

### Spotlight

*The General Accounting Office notes that the Postal Service's financial challenges "are not a cyclical phenomenon that will fade as the economy recovers."*

For these reasons, the GAO notes that the Postal Service's financial challenges "are not a cyclical phenomenon that will fade as the economy recovers."<sup>20</sup> The risk posed by electronic substitution over the long term is undeniable. The Postal Service could lose a major fraction of financial transactions, correspondence and heavy advertising pieces. It would be foolhardy to bet the future of the Postal Service on a slow introduction of electronic alternatives. Instead, the Postal Service must adapt both its size and way of doing business to the nation's changing postal habits and to take advantage of the significant opportunities that exist today to improve productivity, enhance service and dramatically reduce the excessive costs and inefficiencies throughout the postal network.

### *Challenge #2: Postal Law Predates the Internet*

As apparent as the electronic diversion trend may be in the daily communications habits of most Americans, it is nowhere reflected in the current legislation governing the operations of the Postal Service. Why? Because the laws on the books have not been substantially changed since before the Internet—the most powerful global communications tool ever invented—existed.

With electronic diversion and other trends likely to alter permanently the ways the nation communicates, the commercial environment for the Postal Service in the next several decades will likely be radically different from that premised in the Postal Reorganization Act of 1970 ("the 1970 Act"). Further complicating matters, with the benefit of three decades of hindsight, it is also clear that this legislation includes obvious flaws that ill serve the nation and its mail service today.

The 1970 Act, for example, assumes perpetuation of a voluminous and archaic postal monopoly law that dates back to 1845 and is all but inscrutable in the modern context. As a result, there exists no clear boundary between the end of the postal monopoly and the beginning of the competitive postal marketplace.

While the 1970 Act charged the Postal Service with operating in an independent, businesslike manner, it created a Board of Governors almost entirely made up of political appointees and with no requirement that they have the level of business acumen a private corporation with \$67 billion in revenues would insist upon to ensure proper oversight and accountability.

The 1970 Act granted the Postal Service broad authority to engage in more entrepreneurial activities. With the advent of the Internet and the blurring of the lines of what constitutes “mail,” this led to some dubious new business ventures for the Postal Service that most Americans would consider far afield of its basic function—delivering the mail to everyone. These efforts had a potentially market-distorting effect, since the Postal Service entered into competitive markets with the backing of its monopoly and its access to borrowed funds through the U.S. Treasury.

The 1970 Act also created an independent postal regulatory entity, but narrowly focused it on oversight of ratemaking and classifications through a process that embodies the worst of public-sector pacing and bureaucracy. This process, taking as many as 18 months to navigate, has hampered the Postal Service’s ability to adjust its revenues to changing market circumstances in a timely manner and to engage in innovative partnerships with customers that could help control costs and stabilize mail volumes.

While the 1970 Act appropriately upholds the nation’s commitment to universal service, it created no mechanism for an external review and refinement of the various components of that obligation. As the postal needs of the nation change, this omission leaves unanswered many important questions, chief among them: Does the universal service obligation require that the Postal Service *itself* carry out the core postal services expected by every American and business? Or does it merely *ensure* that essential postal services are available to everyone, perhaps in partnership with the private sector?

Constructively answering these questions and freeing the Postal Service from the most severe public-sector requirements hindering its business operations are essential to the continued health of the institution and quality of its service to the nation.

### *Challenge #3: Entrenched Inefficiency and Resistance to Modernization*

As the Postal Service struggles under a dated law, it faces rising pressure to answer successfully a fundamental question: How can it maintain high-quality universal postal services when its primary revenue streams are in retreat? The solution clearly lies with focusing the Postal Service on its core value to the nation—delivering the mail—and recognizing that, as demand for that service contracts, perhaps the Postal Service should contract, as well. By any account, that is a tall order, requiring significant cultural, organizational, regulatory and philosophical change.

#### Spotlight

*As the Postal Service struggles under a dated law, it faces rising pressure to successfully answer a fundamental question: How can it maintain high-quality universal postal services when its primary revenue streams are in retreat?*

**Spotlight**

*Despite the need for fundamental change, no comprehensive reform legislation has been enacted in the past three decades.*

While opportunities for significant cost reductions through automation, standardization, procurement reform and a host of other initiatives are relatively obvious, there is intense pressure whenever the sensitive issues of closing a post office, consolidating distribution centers, or reducing the size of the workforce are raised. The result, too often, is stalemate. In the past decade alone, Congress has debated the entire gamut of postal issues, such as pricing flexibility, binding arbitration with labor, revisiting the Postal Service's monopoly, and altering the number of post offices across the country. Yet despite the need for fundamental change, no comprehensive reform legislation has been enacted in the past three decades.

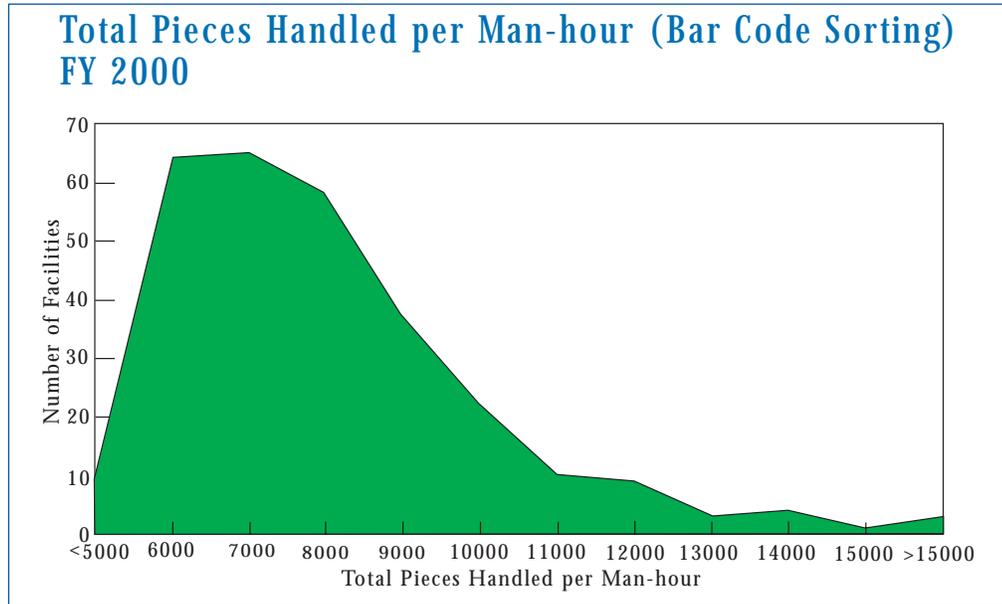
If current economic and market trends continue and the Postal Service does not reach higher levels of efficiency, it will be unable to meet its "break-even" mandate, potentially shifting substantial obligations to the taxpayer. Making up these potential losses by increasing revenue from other categories of mail is highly unlikely. As a result, stabilizing the Postal Service's financial situation requires significant cost reductions. Fortunately, in this arena, the Postal Service has ample opportunity—if given the appropriate flexibility and support.

With the rapid growth of the nation's postal needs over the last century, the Postal Service has developed a vast network of local offices, processing and distribution facilities, Bulk Mail Centers, and related transportation systems. This network includes some 300,000 collection boxes, almost 38,000 retail postal outlets, 446 mail processing facilities (Exhibit 5.1), along with one of the world's largest transportation networks, featuring some 215,000 vehicles and more than \$5 billion in annual contracts for highway, air, rail and water transport.

Few, if any, believe that if the Postal Service were established today, such a sprawling logistics network would be necessary to deliver the nation's mail. The GAO has noted that the number and location of postal facilities is based on "operating strategies that are now outdated, as the [Postal] Service has moved from a manually oriented processing and delivery environment to a highly automated environment."<sup>21</sup> The facilities it does have are not designed or put to use in the most efficient manner. As a result, productivity varies from facility to facility, due to either lack of use or lack of efficient processes (Exhibits 1-4, 1-5, and 1-6). With significant liabilities and a bleak outlook for its traditional core revenue stream, the Postal Service can ill afford its legacy network.

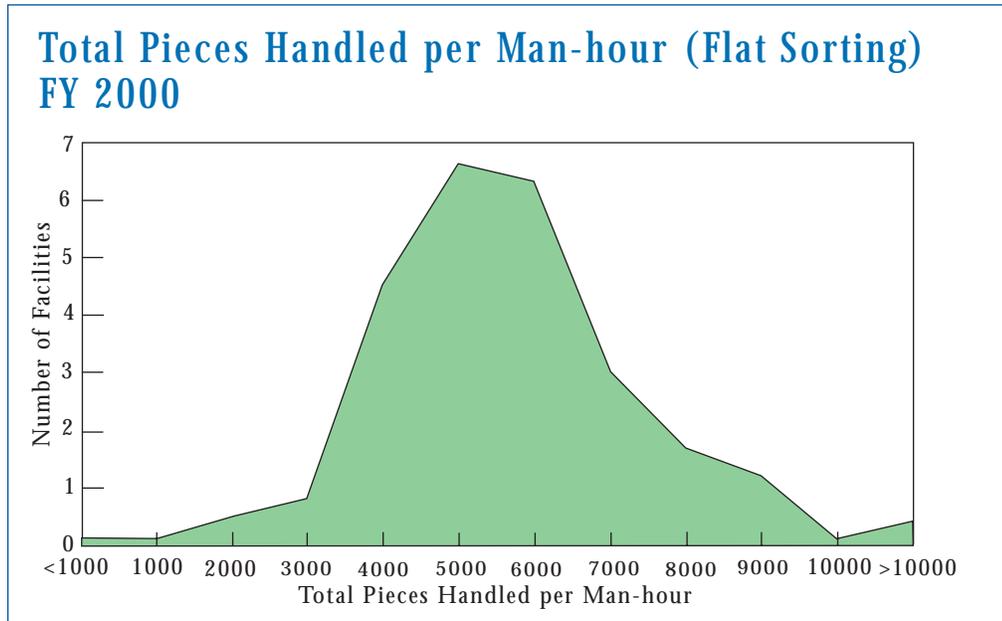
## Productivity Varies Greatly by Facility

**Exhibit 1-4.**



Source: Postal Rate Commission.

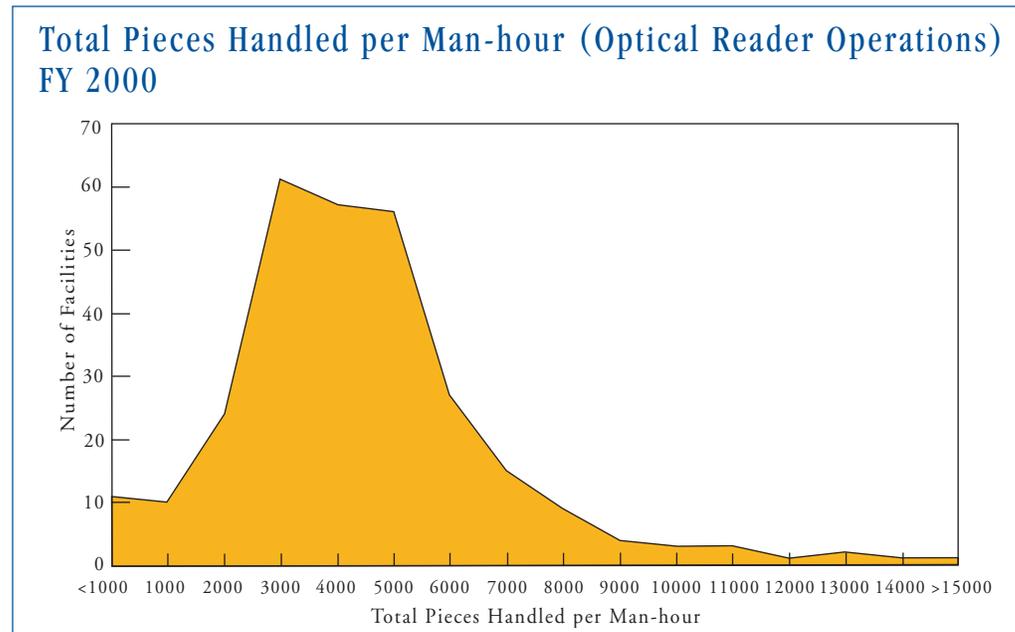
**Exhibit 1-5.**



Source: Postal Rate Commission.

### Spotlight

*Productivity varies from facility to facility, due to either lack of use or lack of efficient processes.*

*Exhibit 1-6.*

Source: Postal Rate Commission.

Fortunately, the Postal Service recognizes the hindrances posed by its legacy network and has undertaken an important network rationalization initiative (see Chapter 5) to bring its processing and distribution system into the 21<sup>st</sup> century. The Commission applauds this effort. It is the Commission's view that, with aggressive business strategies, much of the Postal Service's legacy network could be retired. Many facilities could be consolidated or closed. Those that remain could be standardized, modernized and given a common footprint. Opportunities also abound to engage the private sector more fully in the delivery of universal service. But many of these critical advances cannot occur unless interested parties from Congress to customers, private-sector partners to postal competitors, recognize the opportunity and the necessity to realign and redeploy the nation's Postal Service with the most sophisticated technology, the most experienced and capable leadership, the most skilled workforce, and the most aggressive productivity and cost-saving strategies it can muster. Without these efficiencies, even if rates remain "affordable," ratepayers aren't getting what they deserve: the most capable, efficient, high-quality network at the lowest cost.

If the public interest lies with achieving an ambitious, nationwide public service at reasonable cost, rather than merely perpetuating the status quo means of *delivering* that service, then the Postal Service must have the nation's support in aggressively adopting private-sector productivity and cost-saving strategies and applying them to the public mission of delivering the mail.

## Conclusion: Toward A New Business Model

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The Postal Service faces a defining moment: It can continue to carry out its universal service obligation via a costly and outmoded infrastructure, at extraordinary and perhaps unsustainable expense, or it can embrace new technologies, partners and private-sector strategies to ensure a bright future for the nation's mail. Without a new approach, universal service is in peril. But by making the tough choices and embracing new strategies, ample opportunities exist for the Postal Service to enhance its service to the nation and simultaneously reduce the cost of that service.

It is evident to this Commission that the nation and its postal needs have been fundamentally transformed. What is not yet clear is the Postal Service's place in this new environment. How the institution is permitted to address the formidable and diverse challenges before it will determine its future role and the fate of its most valuable contribution to the nation—uniting the American people and economy through the mail.

A successful modernization, however, must begin more fundamentally. As an essential starting point to the successful realignment of such a vast and vital national network, the Postal Service must clearly identify its *forward*-looking purpose and core value to the nation. It must carefully weigh the transforming technological and economic changes that have swept the globe in the 30 years since it was last overhauled and answer three critical questions: Who are we? What do we do? And, how can we do it better?

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## Endnotes

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## Chapter 2: Delivering the Mail: The Constant Mission of an Evolving Institution

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### Introduction

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While many assume that the mission of the national post office has remained static throughout history, this is far from the case. The institution was founded in the 18<sup>th</sup> century as an inter-city post office to post office pouch service. In the second half of the 19<sup>th</sup> century, it assumed the functions of a big city “penny post,” as well. In the early 20<sup>th</sup> century, national postal service reached out to the vast rural areas where most Americans still lived and worked. Most recently, in 1970, the national post office was relaunched as a more efficient, businesslike service. Throughout its 225 years, the core mission of the Postal Service and its predecessors has undergone significant changes at pivotal moments. Yet, the national post office has remained a vital and valuable institution precisely because of these timely adaptations.



Source: USPS.

Today, the Postal Service once more must evolve alongside the changing postal needs of the country. But whereas the challenge in the past has largely been to keep pace with the nation’s *expanding* need to exchange goods and information, the challenge before the institution today is to advance its core modern purpose—delivering high-quality universal postal service to the nation—in an era when demand for traditional postal services may well be *contracting*.

Continuing to keep the country, its economy and its people connected through the mail will be a challenge in this modern environment. However, if the Postal Service has a clear legal framework, the capacity to innovate, and the charge to make greater use of private-sector partnerships, then the institution could well clear the hurdles currently in its path and rise to a new standard of excellence. Its success, however, requires a sharply focused institution with a clearly defined purpose.

#### Meeting Modern-Day Mail Needs

*The Postal Service should have a focused, clear mission that reflects the modern-day mail needs of the country. That mission should be “to provide high-quality, essential postal services to all persons and communities by the most cost-effective and efficient means possible at affordable and, where appropriate, uniform rates.”*

The Commission recommends that the mission of the Postal Service be “to provide high-quality, essential postal services to all persons and communities by the most cost-effective and efficient means possible at affordable and, where appropriate, uniform rates.” This definition focuses the organization on its core value—delivering high-quality universal postal service at affordable rates; it makes efficiency and cost-effectiveness explicit obligations the Postal Service owes its customers; it emphasizes that affordable rates must not come at the expense of service quality; and it further opens the door—appropriately—to greater involvement of the private sector in the delivery of the nation’s mail.

By modernizing postal laws that have not been revisited in more than 30 years, by enhancing universal service through more flexible delivery standards, by clarifying the postal monopoly and potentially narrowing it over time, and by advancing the businesslike perspective and operations of the Postal Service, we may well change the *institution* dramatically. Yet, with a newly focused mission, the Postal Service’s primary *function*—ensuring universal service—will be preserved and advanced.



*“As we look to the past, a very proud past, I think that... [the] hundreds of thousands of people in the Post Office Department can look to a better future...”* President Nixon’s Remarks, August 12, 1970 (signing of the Postal Reorganization Act).

Source: National Archives.

## After 30 Years, Postal Laws Must be Modernized

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As mentioned above, legislation creating the Postal Service has not been updated since 1970. At that time, the Postal Service was not self-supporting. Like other government agencies, it was dependent on Congressional appropriations. The institution also was plagued by complaints about the reliability and quality of its service as well as the often politicized nature of its operations. In response, the 1970 Act delineated a broad mission “to bind the nation together through the personal, educational, literary, and business correspondence of the people.” The 1970 Act also separated the nation’s politics from its postal service and instructed the Postal Service to operate in a more businesslike manner: improving customer service, being more entrepreneurial, and operating without the benefit of taxpayer subsidies.

The 1970 Act defined the purpose of the Postal Service as:

- binding the nation together through the personal, educational, literary, and business correspondence of the people;
- providing prompt, reliable, and efficient services to all persons in all communities;
- charging fair and reasonable rates and fees; and
- showing no undue or unreasonable preference to any user.

While these remain appropriate guiding principles for the institution today, a focused mission of delivering the mail to everyone in the most cost-effective and efficient manner possible highlights the fiscal discipline and strong business orientation the Postal Service needs today to ensure the future of universal service at affordable rates. As many corporations have learned, an important element of success is staying focused on your core business.



Source: USPS.

## Should the Postal Service be Privatized?

Given how dramatically the postal environment has changed in the past 30 years, some have suggested that perhaps the Postal Service can best *act* like a business, if it is permitted to *become* a business. While privatization has been a reform strategy adopted by some leading postal systems around the globe, the Commission believes that such a precipitous step for the Postal Service would unnecessarily jeopardize universal service at affordable prices. The Postal Service handles more than 200 billion pieces of mail per year. It delivers over 40% of the world's mail, across the vast geographic expanse of the United States.<sup>1</sup> The nation's mail remains essential to the American people and economy. It is highly unlikely that the private sector, acting alone, could provide the *universal* mail services we have come to expect from the Postal Service. All of these factors merit a "first-do-no-harm" approach.

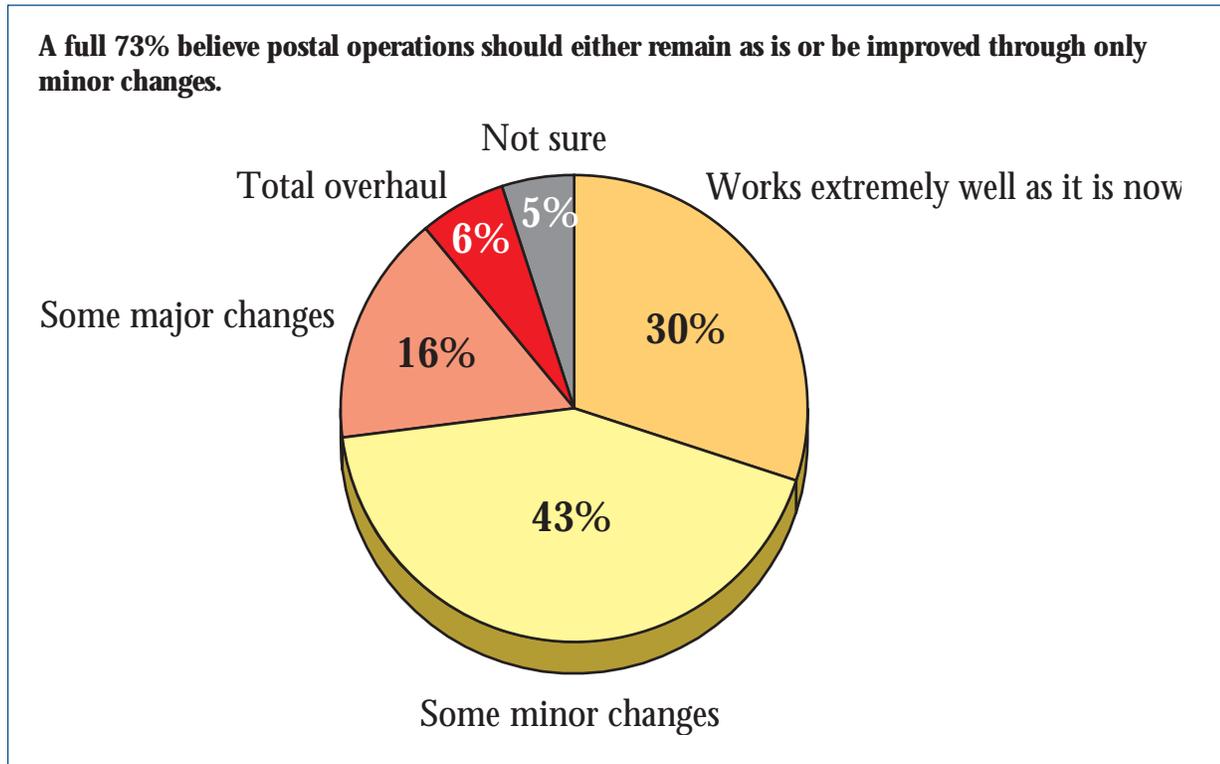
In the judgment of the Commission, privatization of the Postal Service would today pose a substantial risk of doing great harm. Privatization of a commercial entity the size of the Postal Service could seriously disrupt the highly successful private delivery service markets. For the Postal Service itself, privatization could imply a decade or more of wrenching organizational changes. Most importantly, while the end result of privatization could be a dynamic and efficient private postal sector, the privatization process could undercut the stability and continuity that are the hallmark of a public service. Given the essential nature of universal postal service for the foreseeable future, the Commission believes that the least risky strategy is a more evolutionary approach. The Postal Service should be maintained as a public entity, but refocused and reorganized to enhance its efficiency and adaptability in the face of an uncertain, and ultimately more competitive, future.

That certainly is the feedback the Commission has received from consumers in its survey of their perspectives on the Postal Service. More than two-thirds of respondents indicate they are generally satisfied with the service and value they receive from the Postal Service. A full 73% believe postal operations should either remain as is or be improved through only minor changes. They support the notion of a self-financing institution, but flatly oppose near-term privatization. Interestingly enough, the survey results suggest that a majority would rather pay more for postage than see the nation go into debt to maintain universal postal service.<sup>2</sup>

### The Postal Service: A Self-Sustaining Commercial Enterprise

*The Postal Service should continue as an independent establishment within the executive branch with a unique charter to operate as a self-sustaining commercial enterprise. However, it should take full advantage of the flexibility afforded it under this construct to aggressively adopt best business practices throughout the organization to maximize the quality of universal service and minimize the cost and risk to ratepayers and taxpayers.*

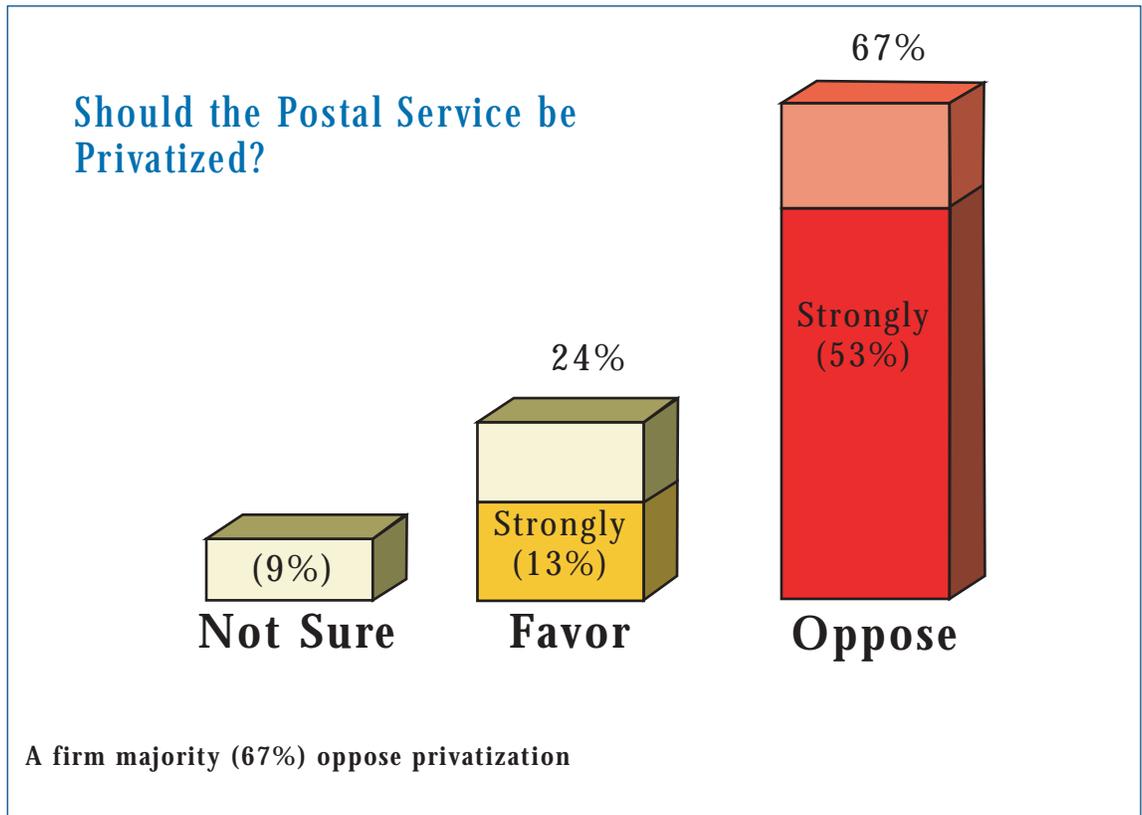
Exhibit 2-1.



Source: Black & Veatch (Hart Research and American Viewpoint) consumer survey conducted for the Commission.

These strong customer opinions support the Commission’s conclusion that the Postal Service needs to improve the *way* it does business, but not fundamentally alter its mission or structure in the near term.

*Exhibit 2-2.*



Source: Black & Veatch (Hart Research and American Viewpoint) consumer survey conducted for the Commission.

*Postal Monopoly Should be a Bridge to a Competitive Marketplace*

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While a postal monopoly will likely be necessary for many years, the Commission strongly recommends new mechanisms that will permit incremental steps toward the ultimate desired destination: a thriving, competitive postal marketplace capable of delivering stable, high-quality, affordable and universal postal service. This conclusion is consistent with regulatory reforms adopted in other sectors of the U.S. economy over the past quarter century, where government-sanctioned monopoly markets have been opened up to private-sector competition. Those examples demonstrate that rarely is it in the public interest for a monopoly to be a permanent construct. Rather, monopolies are most beneficial when they serve as a bridge—albeit, often a long one—to the rise of a healthy, competitive, and reliable marketplace.

We see strong evidence that the practical impact of the postal monopoly is diminishing in the United States. Today, a vibrant U.S. private-sector postal industry is extending its reach and service capabilities. At the same time, new technologies are shifting transmission of large amounts of national correspondence from the postal monopoly to competitive telecommunications carriers. Indeed, even the Postal Service is facilitating more private-sector involvement—for example, by offering discounts to high-volume mailers that do the processing and transportation of their own mail. In the United States, the private sector is far more involved in the mail delivery stream than in most other industrialized countries.

This report could accelerate these trends. In doing so, it asks the nation to answer a fundamental question: Should the country's mail *forever* be delivered by the government? While this report does not pursue privatization as a near-term goal nor seek to have the private sector replace the government in performing vital government functions, it does aim to pave the way for introduction of best business practices throughout the Postal Service. As a result of the aggressive strategies we propose, it is our hope that Postal Service customers will increasingly reap the benefits of a more businesslike institution.

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*Archaic Postal Monopoly Law Needs Clarity, Modernity*

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Once the conclusion is reached that the public interest is best served by the continuation of the Postal Service monopoly in the near-term, an urgent need arises to revisit and recast the country's arcane postal monopoly law. The lack of a straightforward and circumscribed definition of the postal monopoly was a common complaint heard by the Commission. Legislation governing the postal monopoly has gone largely unchanged for more than a century. As a result, regulatory interpretations of the monopoly have grown increasingly muddled.

### Postal Monopoly Law Predates Light Bulbs, Let Alone E-mail

*Many of the provisions of the current postal monopoly law date back to the postal laws of 17<sup>th</sup>-Century England and have remained virtually unchanged, often offering no point of reference to the modern world and producing a dense thicket of vague and contradictory regulations.<sup>3</sup>*

*Put another way, the nation's postal monopoly law predates not only the computer, e-mail and the fax machine, but also the radio, the telephone and the electric light bulb. America's postal monopoly law was crafted at the dawn of the Industrial Revolution to serve the social and commercial needs of an America that overwhelmingly lived on the farm, worked in the family business, and traveled by stagecoach. Several years into the nation's Information Revolution, it is clear that these archaic laws should be clarified and modernized.*

In light of this confusion, the nation would be best served by a modern, straightforward definition that reflects the postal monopoly as the nation knows it and relies on it today. The Commission feels that this issue would best be addressed by placing the postal monopoly's forward-looking oversight and scope in the hands of an independent Postal Regulatory Board (whose structure and responsibilities are explained in chapter 4).

With the on-line world blurring the meaning of "correspondence," the Commission proposes clarifying that the postal monopoly applies only to hard-copy communications. The Commission also strongly recommends that a bright line be drawn between the postal monopoly and the competitive mail market. In its Transformation Plan, the Postal Service itself acknowledges the absence of a clear border, noting that "there is no precise line that distinguishes protected volumes from unprotected volumes."

The basic uncertainty in the scope of the postal monopoly derives from the way it is defined. In the nineteenth century, the postal monopoly was declared to include the carriage of "letters," but not other types of postal items.<sup>4</sup> While this standard may have been clear enough in simpler times when there were only a few types of mail, it

is extremely difficult to apply to the variety of items posted today. In some other industrialized countries, postal reform laws have abandoned efforts to define the postal monopoly by the content of what is transmitted and have instead extended the monopoly to all envelopes falling within certain weight and price limits.<sup>5</sup> The Commission recommends a similar approach, defining the postal monopoly to cover:

*Any hard copy communication that is to be conveyed and delivered to a specific address in the United States indicated by the sender, provided its weight is less than 12 ounces and the delivery price is less than the basic stamp price times six.*

The *weight limit* in the proposed definition is 12 ounces. Under this approach, the Postal Service would have a monopoly over the carriage of all envelopes weighing less than 12 ounces; that is, private carriers would not be permitted to carry envelopes weighing less than 12 ounces unless they charge more than the price limit described below. While the precise level of a weight limit is necessarily somewhat arbitrary, the Commission believes that 12 ounces is a simple and convenient standard that includes virtually all of what people ordinarily think of as “letters” reserved for the Postal Service. Twelve ounces is slightly less than the weight limit adopted in the European Union in 1997 (350 grams or 12.5 ounces) but considerably more than the EU-wide weight limit placed in effect earlier this year (100 grams or 3.5 ounces).<sup>6</sup> On the other hand, a 12-ounce limit will allow competition for items now carried by Priority Mail, mostly very large envelopes and small parcels. The Commission doubts that most people today think of such items as “letters” within the postal monopoly.

The *price limit* in the proposed definition is six times the price of a First-Class stamp. The purpose of the price limit is to reserve for the Postal Service the carriage of letter-sized envelopes by ordinary postal services while allowing private carriage by more rapid or value-added services. In 1979, the Postal Service initiated the practice of using a price limit on the postal monopoly to allow private carriage of urgent letters.<sup>7</sup> This concept has been copied in postal reform legislation around the world and is now almost invariably expressed as a simple multiple of the basic stamp price. By linking the price limit to the First-Class stamp, price protection of the postal monopoly will be maintained even if stamp prices increase. The price limit proposed by the Commission is the same as that proposed in the recent postal modernization bill developed by the House of Representatives. It is more protective of the Postal Service than the price limit adopted in the European Union (set at five times the stamp price in 1997 and reduced to three times the stamp price in 2003).

The recast postal monopoly should retain traditional statutory exceptions for carriage of a letter enclosed with cargo, a letter carried by its owner, a



Source: USPS.

letter carried by special messenger, and a letter carried free of charge. In addition, the statute should continue the major regulatory exceptions to the postal monopoly recognized today. These include exceptions for the carriage of newspapers, checks and other financial instruments, advertisements included with merchandise, intra-university mail, and carriage to or from a post office. Specific details of the rule and the task of fashioning new exceptions should be left to the discretion of the Postal Regulatory Board.

### Defining the Postal Monopoly in Clear and Understandable Terms

*Astute readers will note this report's reference to codifying the postal monopoly "as the nation knows it today." This caveat is necessary because the reality of the postal monopoly is far from that envisioned more than a century ago. The nation's postal monopoly statute, last revised substantially in 1872, was originally crafted to cover only letters. Today, it is generally believed to cover all First-Class Mail and Standard Mail (mostly advertising)—in other words, virtually all letters and documents of both a personal and business nature.*

*Over time, exceptions to the monopoly were created by "suspensions" issued by the Postal Service, such as intra-university mail and "urgent" mail (i.e. private express delivery).<sup>8</sup> While these suspensions serve the nation's modern mail needs, some question whether the Postal Service has the authority to define and alter the scope of its own monopoly.*

*This leads the Commission to two conclusions: (1) the postal monopoly should be defined in clear and understandable terms; and (2) the monopolist (i.e. the Postal Service) should not regulate the scope of its own monopoly. Thus, the Commission recommends that this responsibility should reside with an independent Postal Regulatory Board (more fully described in chapter 4).*

### *Toward a More Efficient and Performance-Oriented Monopoly*

The Commission readily acknowledges that a monopoly is often an inherently inefficient device with a natural propensity for stagnation and mediocrity. By recommending a wide array of aggressive strategies to improve the efficiency and business practices of the Postal Service, this report aims to make the U.S. postal monopoly far more performance-oriented. To encourage those results, the Commission recommends several mechanisms that will impose on the Postal Service the same bottom-line risks and rewards that motivate private-sector companies and their employees.

These mechanisms include the adoption of an incentive-based compensation program that rewards *all* employees who contribute to the improved performance of the Postal Service, from mail carriers and postal clerks to the most senior executives (discussed in detail in Chapter 6). The second noteworthy mechanism is rate ceilings (discussed in detail in Chapter 4), which eliminate any notion that rising costs can simply be funded by rising rates. Instead, this mechanism caps the growth in revenues the Postal Service can expect from ratepayers at a level below inflation. It is our hope that through the use of these tools, an institution that once could be lulled by the luxury of monopoly revenues can be transformed into a more businesslike institution that aggressively roots out the inefficiencies and excessive costs that exist throughout the nation's postal network.

The postal monopoly as it exists today has a second element as well: Only the Postal Service is permitted to have access to the nation's mailboxes. A recent survey conducted for the Commission is consistent with a 1997 GAO study that concluded that the vast majority of adults oppose allowing just anyone to put mail into their mailboxes.<sup>9</sup> However, the Commission notes that the GAO survey also indicated that the level of opposition reduces by *half* when access is limited to familiar delivery brands.<sup>10</sup> This mixed message appears to indicate that the *status quo* blanket mailbox monopoly may be overriding the individual preferences of a sizeable minority of Postal Service customers. Therefore, at an appropriate time in the future, the new Postal Regulatory Board may wish to take a closer look at the mailbox monopoly with the aim of easing its boundaries to permit greater individual consumer choice. If customers want to give certain carriers access to their mailbox, the Commission feels the Postal Regulatory Board should bless that practice, so long as it occurs with the customer's consent.



Source: USPS.

#### **The Mailbox Monopoly: Current Law**

*“Whoever knowingly and willfully deposits any mailable matter such as statements of accounts, circulars, sale bills, or other like matter, on which no postage has been paid, in any letter box established, approved, or accepted by the Postal Service for the receipt or delivery of mail matter on any mail route with intent to avoid payment of lawful postage thereon, shall for each such offense be fined under this title” (18 U.S.C. § 1725).*

As this monopoly asset is slowly opened to private businesses, the Commission also encourages the Postal Regulatory Board and the Postal Service to contemplate any revenue opportunities that may be associated with this step. Without access to mailboxes, private carriers must deliver to a customer's doorstep or office, hindering the efficiency of their routes. As such, mailbox access could have significant worth that might make it in the public interest for the Postal Service to levy a fee on private carriers that desire this more efficient means of doing business. As it reconsiders the postal monopoly "as the nation knows it," it is only appropriate for the Postal Regulatory Board and the Postal Service to explore all possibilities for maximizing the public benefit in the process.

### Regulating Access to the Mailbox

*The Postal Regulatory Board should be authorized to permit mailbox access by private carriers in future regulations, so long as it does not impair universal service or open homeowners' mailboxes against their will.*

That point made, however, the Commission firmly believes that individual customers should have the final say over access to their mailbox, and that such access should be granted only with their express consent and only if it in no way jeopardizes universal service. The solution could be as simple as authorizing private carriers to produce and distribute stickers that their customers can place on their mailboxes to indicate their consent on a per carrier basis. But the idea merits thoughtful exploration in the spirit of enhancing customer service and consumer choice.

## Revolutionizing the Delivery of Universal Postal Service



Mail delivery in the Grand Canyon.

Deep in the heart of the Grand Canyon lies the nation's most remote active mail route. Nestled a treacherous 8 miles down from the canyon's south rim, the 515-member Havasupai Indian Reservation is inaccessible by land vehicle or helicopter. Yet five days a week, the Postal Service makes the grueling three-to-five hour journey, each voyager carrying on average 200 pounds of mail, food, and more.<sup>11</sup> How is this possible? The Postal Service connects the Havasupai tribe to the world via its last active mule train. While the vast majority of the nation is far more accessible than the Havasupai, the "above and beyond" nature of this delivery route offers a powerful demonstration of just how seriously the Postal Service and, through it, the nation takes its commitment to *universal* mail service.



Snowmobile mail delivery in Alaska.  
Source: USPS.

Throughout this report, the point is made that the Postal Service must be far more aggressive in enhancing its performance and reducing its costs. Yet with each recommendation, the same caveat is made: First and foremost the nation's commitment to affordable universal postal service must be upheld. From the office buildings of Manhattan to the bush country of Alaska, the near daily appearance of the Postal Service at virtually every U.S. home and business remains essential to American commerce and society. As a result, the Commission strongly endorses not only universal service as a principle but

as the guiding mission of the Postal Service, reflected in the proposed charge “to provide high-quality essential postal services to all persons and communities by the most cost-effective and efficient means possible.” The Commission further strongly endorses the basic features of universal service—affordable rates, frequent delivery, and convenient community access to retail postal services.

Where the Commission sees ample room for improvement, however, is in *how* universal service is delivered to the nation. In this regard, the Commission recommends that the Postal Service be instructed to:

- focus on core products and services;
- continue six-day delivery;
- maintain uniform rates...with review;
- dramatically enhance retail access to postal services; and
- involve the private sector more in universal postal service.

### Is E-mail a Postal Service?

*The world has greatly benefited from the revolution in correspondence precipitated by the rapid rise of electronic mail. Nevertheless, a Postal Service governed by a law written before the Internet as we know it even existed has led to some...confusion. The 1970 Act may be read to provide broad authority to the Postal Service to be entrepreneurial in pursuing its self-financing mandate. However, the on-line revolution dramatically blurred the lines of what constitutes a “postal service,” producing some dubious forays.*

*Many Americans have no idea that their Postal Service:*

- Sells Postal Service-branded electronic bill presentment and payment services;
- Explored offering Internet-based tax services and money transfers;
- Offers certified electronic mail and on-line greeting cards; and
- Contemplated offering e-mail and other data transmission services.

*These ventures have produced largely disappointing results. Also of concern, each of these markets is served by private companies who do not have the backing of the U.S. government and a national postal monopoly. These efforts also have drained time and resources that could have been spent improving traditional postal services. For this reason, the Commission recommends focusing the Postal Service on traditional mail, leaving electronic products and services to a well-served and innovative private marketplace.*

### *Focus on Core Postal Products and Services*

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The 1970 Act may be read to provide broad authority for the Postal Service to pursue an undefined array of new revenue streams—regardless of whether or not they are related to traditional postal markets or their potential market-distorting affects.

The Commission recommends focusing the Postal Service more exclusively on what the country and its economy rely on it most to do—provide products and services directly relating to the delivery of letters, newspapers, magazines, advertising mail, and parcels on a universal basis. Under this approach, the institution's time and resources can be focused on the quality of its most vital services and how they can be delivered most efficiently, rather than diverting limited resources to new product development and marketing, which may or may not be within the core mission of the Postal Service.

#### **Sticking to the Core Mission**

*The 1970 Act should be revised to specifically instruct the Postal Service to offer only products and services directly related to the delivery of letters, newspapers, magazines, advertising mail, and parcels. Other governmental services offered for the customers' convenience should be permitted, so long as the full cost of providing them is recovered.*

Achieving this focus will require clarifying the broad authority granted in the 1970 Act, which permits the Postal Service to “provide, establish, change or abolish special **non-postal** or similar services (emphasis added).” To enhance customer convenience, however, the Postal Service should be permitted to provide additional governmental services (such as passports) when in the public interest and when the Postal Service is able to recover the full costs of providing such services.

### *Continue Six-Day Delivery*

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The Commission firmly recommends continuing the Postal Service's current Monday through Saturday delivery regimen. While the Postal Service could save as much as \$1.9 billion (less than 3% of its annual budget) by reducing its delivery schedule by one day a week,<sup>12</sup> its value to the nation's economy would suffer. Beyond the universal reach of the nation's postal network, the regularity of pick-up and delivery is an essential element of its worth in the current climate. Elimination of Saturday delivery, for example, could make the mail less attractive to business mailers and advertisers who depend upon reaching their target audience on that day. In addition, given the volume of mail the nation sends each day, scaling back to a five-day delivery regimen could create difficult logistics, mail flow, and storage problems.

While the Commission firmly rejects the idea of reducing the frequency of universal postal delivery in circumstances substantially similar to today, it would be imprudent to be arbitrarily inflexible on this point. Postal Service leaders have indicated that the rising popularity and sophistication of e-mail correspondence may ultimately lead to a reduction in the demand for mail services and may allow for the relaxation of the *six*-day delivery requirement.<sup>13</sup> If that time does arrive, the Commission believes that the Postal Service should have flexibility to adapt with the changing postal needs of the nation.

### *Maintain Uniform Rates... With Review*

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Currently, there are three categories of mail that are required to have uniform rates: (1) First-Class Mail weighing less than 13 ounces; (2) Media Mail (including books, compact discs, cassettes and videos); and (3) library rate mail shipped primarily to or from a library. The Commission proposes to maintain this list, but to create a mechanism for its independent and periodic review.

### *Dramatically Enhance Retail Access to Postal Services*

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Beyond universal service at the mailbox, every individual and business has the right to ready access to retail postal products and services. The Commission strongly recommends accelerating efforts underway to expand access to retail postal services at venues *other* than the post office. These efforts focus on bringing more services *to* the customer—at banks, grocery stores, ATMs, and other convenient locations across the country. This recommendation is one example of the opportunities available to the Postal Service to control costs and enhance customer convenience by delivering core postal services in innovative ways. (Specific strategies are discussed in Chapter 5.)

### **Maintain Six-Day Delivery**

*The Postal Service should retain its six-day delivery regimen, with its existing flexibility for exceptional circumstances. The Postal Regulatory Board should also have the authority to refine future delivery frequency requirements as changing circumstances may warrant.*

### **Uphold Uniform Rates**

*The Postal Regulatory Board (see Chapter 4) should have the authority to periodically review the list of postal services for which uniform rates are required by law. The Board should have the authority to refine the list as appropriate and necessary to advance this important aspect of affordable universal service.*

### **Bring Postal Services to the Consumer**

*The Postal Service should more aggressively pursue private-sector retail partnerships that can dramatically enhance access to the most popular postal services at more convenient times and locations for customers in communities across the country.*

### *Involve the Private Sector More in Universal Postal Service*

Where private-sector companies can perform aspects of the nation's postal service better and at less cost, the Postal Service best serves the nation by involving them in the provision of universal postal service. The Commission recommends that the Postal Service have maximum flexibility in delivering universal service by the most cost-effective, quality means available to it, including outsourcing a particular function to the private sector.

#### Who Moved My Mail?

*The national postal network is an interwoven fabric of public and private endeavors. For more than two centuries, public and private postal ventures have led a relatively symbiotic existence, each driving the growth and development of the other to the benefit of the nation. From the days of Mark Twain, when enterprising individuals grabbed satchels of business correspondence and hopped on riverboats to conduct the first "express mail" to today's state-of-the-art global networks, private carriers have contributed significantly to the diversity and sophistication of the nation's shipping services. Many don't understand the lengths to which the private sector already is involved in the delivery of their mail. For example, the Postal Service does not own airplanes. Instead, it outsources air transport of the nation's correspondence. In addition to its logistical integration, the public-private postal network also together forms a powerful economic force.*



Source: USPS.

The Commission notes that this evolution already is underway at the Postal Service, through its many retail postal partnerships and role as the global pioneer in worksharing. The Commission supports these efforts and encourages the Postal Service to aggressively expand its efforts in this area. (Proposed strategies are discussed in detail in Chapter 5).

#### Seek Out the Lowest-Cost, Most Effective Provider

*The Postal Service should aggressively expand the number and diversity of its private-sector partnerships. Where private companies can advance affordable, universal postal service at an equivalent or better price and service level than the Postal Service, the organization should select the option that least burdens ratepayers.*

*Exhibit 2-3.***Universal Postal Service in the 21<sup>st</sup> Century**

## The Mission

*“To provide high-quality, essential postal services to all persons and communities by the most cost-effective and efficient means possible at affordable and, where appropriate, uniform rates.”*

## Components

**Product Coverage:** Products and services must be directly related to the delivery of letters, newspapers, magazines, advertising mail, and parcels. Other government services (e.g. passports) are permitted, so long as the Postal Service can recover the full cost of providing those services.

**Delivery Frequency:** The Postal Service should retain its six-day delivery regimen, with its existing flexibility for exceptional circumstances. The Postal Regulatory Board should also have the authority to refine future delivery frequency requirements as changing circumstances may warrant.

**Uniform Rates:** The Postal Service should continue uniform rates for First-Class Mail, Media Mail and library package mail; however, the Postal Regulatory Board should have authority to refine the list, as appropriate.

**Retail Access:** The Postal Service should aggressively step up efforts to deliver more convenient low-cost access to retail postal services.

**Private-Sector Partners:** The Postal Service should out-source functions that can be performed better and at lower cost by the private sector.

**Conclusion**

The Postal Service sorely lacks a clearly defined mission and bright-line boundaries around the scope of its postal monopoly. An explicit definition of the Postal Service’s mission and universal service obligation—set in the modern context of new technological and competitive realities—is necessary to focusing the institution on its essential forward-looking contributions to the nation.

By clearly defining the Postal Service’s mission, its universal service duties, and the scope of the postal monopoly and by freeing the institution to fulfill its core obligations in innovative ways, the Postal Service will be able to elevate its service to the nation. At the same time, a sharp focus on traditional postal products and services and an aggressive strategy to pursue more in-depth partnerships with the private sector will help ensure the Postal Service’s future viability. So long as this evolution not only protects, but advances universal postal service, it will be a positive transformation for ratepayers and taxpayers alike.

With the establishment of a clear vision of the modern role and relevance of the Postal Service, responsibility for its success will rest in the hands of those who would shepherd this important evolution of a vital national institution, making it even more important to establish a governance structure that aligns the Postal Service's resources with its forward-looking duty and purpose.

### Chapter 2 Recommendations\*

- B-1 **Basic Structure.** *The Postal Service should continue to operate as an independent establishment within the executive branch with a unique mandate to operate as a self-sustaining commercial enterprise.*
- B-2 **Mission.** *The 1970 Act should be amended to clarify that the mission of the Postal Service is to provide high-quality, essential postal services to all persons and communities by the most cost-effective and efficient means possible at affordable and, where appropriate, uniform rates. In doing so, the activities of the Postal Service should be limited to: 1) accepting, collecting, sorting, transporting, and delivering letters, newspapers, magazines, advertising mail, and parcels; and 2) providing other governmental services when in the public interest and where the Postal Service is able to recover the appropriately allocated costs of providing such services.*
- B-3 **Monopoly.** *The Postal Service should maintain its current mail monopoly, and also retain its sole access to customer mailboxes. However, the 1970 Act should be amended to: 1) authorize the Postal Regulatory Board (see Chapter 4) to clarify and periodically review the scope of the mail monopoly; and 2) clarify that the Postal Service does not have the authority to alter the scope of the mail monopoly or to determine the extent of access to customer mailboxes.*

\* See Appendix C for a complete list of Commission recommendations.

## Endnotes

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2. Peter D. Hart Research Associates, Inc., Study #7006, May 2003, p. 4.
3. Campbell Jr., James I., Testimony Before President's Commission on the United States Postal Service, Feb. 20, 2003, p. 18.
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13. Potter, John E., Postmaster General, United States Postal Service, Testimony Before President's Commission on the United States Postal Service, May 29, 2003, p. 5.

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## Chapter 3: Building a World-Class Business: Best Execution, Corporate Leadership at the Postal Service

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### Introduction

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If the Postal Service were a private endeavor, it would rank eleventh on the Fortune 500 list of the largest corporations in the United States based on revenue (Exhibit 3-1). It is the second largest employer of Americans today, behind only Wal-Mart (Exhibit 6-2).

**Exhibit 3-1.**

Fortune Top 20 Companies in 2003		
Rank	Company	2002 Revenues (\$ millions)
1	Wal-Mart Stores	246,525.0
2	General Motors	186,763.0
3	Exxon Mobil	182,466.0
4	Ford Motor	163,630.0
5	General Electric	131,698.0
6	Citigroup	100,789.0
7	ChevronTexaco	92,043.0
8	Intl. Business Machines	83,132.0
9	American Intl. Group	67,722.8
10	Verizon Communications	67,625.0
	<b>11 United States Postal Service</b>	<b>66,500.0</b>
12	Altria Group	62,182.0
13	ConocoPhillips	58,394.0
14	Home Depot	58,247.0
15	Hewlett-Packard	56,588.0
16	Boeing	54,069.0
17	Fannie Mae	52,901.1
18	Merck	51,790.3
19	Kroger	51,759.5
20	Cardinal Health	51,135.7

Source: *Fortune Magazine*, April 14, 2003.

Through its vast national delivery network, the Postal Service connects virtually every American home and business and is responsible for carrying out one of the most essential services the nation provides to its citizens. Given its importance to the country and the challenges to its future, the Postal Service should meet the highest standard of corporate leadership and should have a powerful, defining commitment to best execution in every aspect of its operations.

If the Postal Service is to adapt successfully to a changing postal market, overcome its significant fiscal challenges, and emerge an efficient and more businesslike institution, then it must be guided by a nimble and results-oriented management and corporate governance structure charged with applying the best business practices of the private sector to the public-spirited mission of delivering the nation's mail.

### Spotlight

*The Commission strongly recommends that the Postal Service voluntarily comply with applicable SEC financial reporting requirements for public corporations.*

Toward that end, the Commission envisions a strong, independent, and experienced Board of Directors that reflects the size, scope, and significance of the Postal Service's work. While the proposed structure grants senior executives more latitude in their management of the day-to-day endeavors of the institution (within the context of a focused Postal Service mission), by establishing a truly effective Board, management will be held accountable for performance.

By extracting itself from the micromanagement of postal operations, a corporate-style Board could fully dedicate itself, like its private-sector peers, to the big picture and to critical fiduciary responsibilities. In this capacity, the Board could focus its attention and experience on mission-critical oversight, exploring key issues like: strategies to increase productivity and reduce costs; holding management accountable for achieving stated performance and service quality goals; leading risk management efforts—particularly with regard to restoring the Service's fiscal health; and, ensuring strategies are developed to address future challenges and opportunities.

Of course, a private corporate governance structure has one more check and balance: the intense public scrutiny demanded by shareholders and oversight by the Securities and Exchange Commission (SEC). To ensure that a management structure with greater latitude has appropriate oversight, the Commission strongly recommends that the Postal Service voluntarily comply with applicable SEC financial reporting requirements for public corporations and that the existing Postal Rate Commission be transformed into an independent Postal Regulatory Board with broad oversight authority (both proposals are discussed in detail in Chapter 4).

This combination of empowered, accountable managers; a strong, strategic Board of Directors; and enhanced oversight and financial transparency has the greatest capacity to deliver to the American people a healthy and efficient Postal Service that consistently operates at a high standard of excellence and delivers service quality, productivity and performance on a par with the nation's leading corporations.



## Good Corporate Governance Starts at the Top

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The first essential ingredient of a strong corporate governance structure is a well-designed Board with outstanding and experienced directors of the highest integrity. Given the institution's size and importance to the nation, the Board of Directors of the Postal Service should be one of the most capable and experienced Boards in the world.

Taking the Board to this level of excellence is about far more than the Postal Service attaining its rightful status. As is the case with corporate entities, the expectations, capabilities, and achievements of the Board in no small part determine the goals, strategies, and successes (or failures) of the institution it governs. Simply put, a world-class, business-oriented Postal Service requires a world-class, business-oriented Board.

Through a Board structured to ensure independence, attract the most qualified candidates, and discharge the same core responsibilities vested in leading private-sector boards, the Postal Service can bring substantial private-sector experience and capabilities to its leadership and, through it, the institution as a whole.

### It Is Time to Revisit the Governance Structure

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Like the Postal Service's mission, its governance structure has not been substantially revised in more than 30 years. The structure established by the 1970 Act was appropriately responsive to the times. While many of the principles guiding the 1970 Act—ensuring the institution is self-financing, depoliticizing the Postal Service—remain important today, the legacy governance structure is increasingly at odds with the Service's mission in the modern environment.

This structure consists of a Board of Governors with broad authority over the day-to-day operations of the Postal Service. While the 1970 Act vests ultimate mail rate and classification determinations with the Board of Governors, it strives to check this authority by requiring the Board to seek recommendations from the Postal Rate Commission that require lengthy public processes. This cumbersome procedure sometimes lasts up to 18 months and flatly undercuts Postal Service efforts to be more businesslike and responsive to changing economic conditions and mail trends.

For these reasons, the Commission strongly recommends that the design, composition, and responsibilities of the Board be changed. At its heart, the legacy structure in place today is a distinctly public-sector leadership hierarchy and web of authorities, producing results that—intended or not—too often slow down needed adaptations and overemphasize micromanagement of day-to-day postal operations.

The new fiscal realities of the Postal Service require aggressive leadership that identifies and pursues new strategies to control costs and boost productivity and efficiency in what many analysts believe will be an era of declining First-Class Mail volumes. Overcoming these challenges to ensure that universal service can continue without imposing an excessive new burden on ratepayers or taxpayers will require the focus and commitment of the nation's leading business minds, something the Commission's recommended structure would make possible.

### Core Responsibilities of a Corporate-Style Board of Directors

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Both the Postal Service and its customers would benefit greatly from a corporate-style Board of Directors. This Board would reflect the best practices of the business world and would attract members with the talent and skills necessary to transform it into a leading-edge institution. Under this approach, the Board would be less engaged in the Postal Service's day-to-day business and more focused on actively monitoring the overall effectiveness of management policies and decisions.

In terms of the specific challenges facing the Postal Service today, this broad vision translates into a laser-like focus on two pivotal areas: cost reduction/quality of service and financial viability/protection of taxpayer interests.

#### A Corporate-Style Board of Directors

*Postal Service leadership would be enhanced by the establishment of a corporate-style Board of Directors. Under such an approach, the Board would replace micromanagement of the day-to-day operations of the Postal Service with a high-level strategic focus on cost reduction and service quality, as well as minimizing the financial risk to taxpayers and restoring the fiscal health of the institution as a whole.*

#### *Cost Reduction and Quality of Service*

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The Board would be responsible for ensuring best execution throughout the Postal Service's operations. Its overriding mission would be the transformation of the Postal Service into an enterprise that consistently rivals the private sector in terms of the key benchmarks of cost reduction and quality of service. To achieve this ambitious goal, the Board would limit its involvement in the

daily management of the Postal Service in order to devote its attention to ensuring management remains on track in meeting its cost reduction and quality of service targets and other established business goals (such as human resource development and management).

### *Financial Viability and Protection of the Taxpayer*

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The Board would also be responsible for ensuring that Congress and the American people are advised promptly of any significant adverse financial developments (such as expanding liabilities or lack of capacity to borrow sums adequate to cover short-falls) that might make rate increases or taxpayer subsidies necessary to sustain postal services. These warnings should be accompanied by an adequate level of explanation, so all interested parties understand the trends that threaten the Service's ability to perform its vital functions. Specifically, the Board should continually monitor the Postal Service's pension and health care obligations and its ability to repay its debt. Here, especially, ratepayers should have a fundamental "right to know."

### **Applying Corporate Best Practices to the Postal Service**

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In order to pursue these two guiding priorities most effectively, the Commission recommends sweeping changes to the Board's structure, as well as to the scope of both its general responsibilities and specific duties, in order to apply the high standards and practices of the world's most successful companies to this unique public venture. With its vast reach, large employee base, and service-oriented nature, the Postal Service can benefit greatly from a strong institution-wide commitment to corporate best practices. In the post-Enron world, this business discipline has rightly garnered a great deal of attention. The following recommendations reflect the Commission's attempt to apply corporate best practices to this unique public institution.

### *General Board Responsibilities*

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In a prominent survey of best-practice standards for Boards of Directors, seven key areas were identified as either vital to success or worthy of greater effort to ensure future success.<sup>1</sup> The Commission recommends that the Postal Service's Board of Directors assume the same general responsibilities as leading private-sector boards:

- Determining the institution's vision and mission (within the boundaries set by statute and the Postal Regulatory Board) to guide and set the pace of operations and future development;
- Considering the legitimate interests of customers, partners, and other interested parties who have the capacity to affect the Postal Service's attainment of its objectives;
- Reviewing and evaluating present and future opportunities, threats, and risks in the external environment;
- Determining corporate and financial strategic direction and identifying resources, contingency plans, and the means to support them;
- Communicating senior management's successes and failures to them, and ensuring appropriate rewards, sanctions, and training are provided;
- Ensuring that internal control procedures provide valid and reliable information for monitoring operations and performance; and
- Ensuring that the Postal Service's organizational structure and capability are appropriate for implementing its chosen strategies.

### *Specific Board Duties*

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The following tasks were identified by the Commission as essential to the successful direction of the Postal Service. Some are already part of the Board of Governors' scope of work. Others steer the Board away from micromanagement. Still other duties are newly assigned and are consistent with the duties of a corporate board.

The specific tasks identified by the Commission as appropriate to the forward-looking efforts of a modern, corporate-styled Postal Service Board of Directors are as follows:

- Hiring, monitoring, compensating and, when necessary, replacing the Postmaster General;
- Ensuring that an adequate succession plan is in place at all times for top management positions;
- Approving an annual report on the Postal Service's financial viability;
- Approving rate adjustments within the limits imposed by the new Postal Regulatory Board (see Chapter 4) and, if necessary, requesting that the regulatory board increase these limits;
- Ensuring Postal Service compliance with informational requests of the Postal Regulatory Board;
- Approving new products and services within the core mission;
- Approving the disposition of post offices (while ensuring that "low-activity" post offices are maintained if necessary to universal service);
- Approving the Postal Service's recommendations to the Postal Network Optimization Commission (see Chapter 5);
- Approving policies and procedures on the management of Postal Service real estate holdings;
- Approving Postal Service annual budgets and required strategic plans;
- Approving capital projects of a truly substantial nature;
- Approving risk management plans;
- Hiring, monitoring, compensating, and replacing, when necessary, internal auditors and an independent public accounting firm;
- Setting compensation and evaluating Postal Service executives and officers against clearly defined benchmarks; and
- Evaluating Board performance and nominating new members, as necessary.

With a firm commitment to emulate the best practices of the world's leading corporations, the Postal Service can become what it should be today: the model for applying the best practices of the private sector to the public-spirited mission of a government agency.

### Applying the Best Practices of Leading Corporate Boards

*With the Postal Service's vast infrastructure, large employee base, and service orientation, the Board of Directors could maximize its impact on the institution by applying the best practices of leading boards to its leadership of the Postal Service.*

## Board Structure, Make-Up and Governance

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To ensure the Board is capable of fulfilling its general responsibilities and specific duties, the Commission recommends a new structure, modeled after the most successful corporate boards in America. This design would ensure the Board operates in the most efficient and productive manner possible, is more removed from undue political influence, and has the depth and diversity of skills necessary to guide the Postal Service to a higher level of operations and a stronger long-term outlook.

### *Composition*

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More and more, corporate boards in America are placing a premium on independence. It has become quite common, in fact, for the Chief Executive Officer (in the case of the Postal Service, the Postmaster General) to be the only management representative on the Board. Generally, leading Boards feature a substantial majority comprised of outside, independent directors, who lack family, business and other material relationships to the institution or its senior managers.

The Commission recommends that the Board be comprised of 12 individuals—eight independent members, three Presidential appointees, and the Postmaster General (who is selected by the other 11 members). Consistent with corporate best practices, this composition is small enough to allow each member to participate fully, yet large enough to ensure that the varied expertise of its membership can combine to deliver the necessary breadth of experience and skills.

As mentioned earlier, this model would be a significant shift away from the politically charged nature of the Board nomination process today. Currently, all nine Governors who serve (with the Postmaster General and the Deputy Postmaster General) on the 11-member Board of Governors are appointed by the President and confirmed by the United States Senate. Under this model, the Commission proposes that a super-majority be independent, one of the most essential ingredients of a successful Board.

*Exhibit 3-2.*

<b>RECOMMENDED COMPOSITION OF NEW BOARD OF DIRECTORS</b>		
<b>8 Independent Members</b>	<b>3 Appointed Members</b>	<b>Postmaster General</b>
<ul style="list-style-type: none"> <li>Initially selected by appointed members, then by majority Board vote</li> <li>Selection dependent upon concurrence of the Secretary of the Treasury</li> <li>Can only be removed by the Secretary of the Treasury</li> <li>Can serve on any committee</li> </ul>	<ul style="list-style-type: none"> <li>Appointed by the President</li> <li>Select initial independent members</li> <li>Can only be removed by the President</li> <li>Can serve on any committee</li> </ul>	<ul style="list-style-type: none"> <li>Selected by the other 11 members</li> <li>Can be removed by majority vote of the other 11 members for any reason</li> <li>Cannot be a member of the Compensation, Audit and Finance, or Nominating and Corporate Governance committees</li> <li>Cannot serve as Chair</li> </ul>

### *Appointments and Nominations*

As Exhibit 3-2 indicates, the Commission recommends that the President appoint three members of the Board. Initially, these three appointees would select the first eight independent Board members whose selection would be dependent on the concurrence of the Secretary of the Treasury. Thereafter, independent members would be selected by the Board as a whole, based on recommendations made by a newly created Nominating and Corporate Governance Committee (discussed below) and with the concurrence of the Secretary of the Treasury.

In developing this proposal, the Commission has been mindful of the fact that the Constitution strictly regulates the appointment of officials exercising significant governmental power under the laws of the United States. The proposed appointment process, including the requirement of ultimate concurrence by the President or the Secretary of the Treasury, is intended to achieve a Postal Service Board of Directors that enjoys the maximum level of political independence consistent with the Constitution. The Commission feels strongly that an independent, depoliticized Board is crucial to the future success of the Postal Service.

Like the board of a public corporation, the essential responsibility of the new corporate-style Postal Service Board will be to manage as efficiently as possible the assets entrusted to it by the owners of the enterprise—in this case, the American people.

Under the Commission's proposal, the Postal Regulatory Board (see chapter 4) will assume responsibility for defining and refining most of the critical governmental policies associated with the postal system including the extent of the postal monopoly, limits on rates for non-competitive products, the particulars of the universal service obligation, the scope of the Postal Service's charter, and the comparability of wages with the private sector. It should be noted, however, that today top officials of the Postal Service also perform several other secondary but distinctly governmental functions—such as law enforcement, adjudication of mailability issues, and oversight of Postal Service operations through the inspector general's office. In order to achieve the independent Board envisioned by the Commission, it may be necessary to adjust the manner in which the offices and tasks of these officials are legally defined. The Commission therefore recommends a careful review of the appropriate provisions of the 1970 Act in order to ensure the objective sought: a new independent, corporate-style Board that can, without any trace of constitutional doubt, provide the Postal Service the highest standard of managerial leadership.

### *Qualifications*

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The Commission recommends a structure that ultimately delivers a well-rounded Board with a diversity of backgrounds and skills that can have a positive impact on the Postal Service. Members should have significant financial and business expertise and experience managing major corporate enterprises and other large organizations. While certain criteria should *disqualify* a Board candidate (such as equity ownership or employment with a competitor, a significant user, or major supplier of the Postal Service), selection criteria should remain sufficiently flexible and dynamic as to ensure that each new member enhances the overall complement of Board skills.

With regard to appointing independent Board members, a new Nominating and Corporate Governance Committee would have significant responsibility (see p. 47). Attributes the committee should consider include: unquestioned integrity, expertise relating to Board activities (corporate governance, corporate finance, performance management, audit and accounting), and experience specifically relevant to the Postal Service (management of a labor-intensive service business, automated processing and distribution systems, vehicle fleet management, network integration and facility consolidation, real estate management, and technology applications).

To give the committee adequate flexibility, the Commission recommends that these criteria be incorporated in the Board's bylaws or governance guidelines, rather than into statute. This approach would grant the Board adequate flexibility should changes to its qualifications criteria prove necessary over time.

### *Board Member Independence*

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The Commission recommends that no individual (other than the Postmaster General) should qualify as a Board member if he or she has a material relationship to the Postal Service or its management team, whether directly or as a partner, shareholder or officer of a related entity. Specifically, the Commission recommends that the following persons should not qualify as a member of the Board:

- Officers or employees of the Postal Service (other than the Postmaster General);
- Officers, employees, or affiliates of the Postal Service's independent public accounting firm;
- Officers, employees, or affiliates of substantial suppliers of the Postal Service (for example, a supplier who derives more than 2% or \$1 million of gross revenue from the Postal Service, whichever is greater);
- Officers, employees, or affiliates of a company that depends on the Postal Service to distribute a substantial portion of its products or to carry out a significant amount of its business; and
- Immediate family members of any person who would not qualify as a Board member.

### *Selection and Role of the Chair*

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The Commission recommends that the Chair be selected by the entire Board and have responsibility to:

- Provide Board leadership;
- Convene and chair Board meetings;
- Establish Board meeting agendas;
- Ensure Board members receive sufficient information to carry out their duties;
- Facilitate the contribution of all Board members; and
- Serve as the primary link between management and the Board.

### *Term Limits*

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The current nine-year terms are far too long, particularly as many corporate boards restructure to achieve shorter terms and allow for a more dynamic Board composition that is responsive to the changing needs of the venture. A careful balance must be

struck between terms that are so long that members lose interest and terms that are so short they restrict members' ability to learn the business and offer meaningful oversight. For Presidential nominees, the potential difficulty of the appointment process is a further burden for consideration. Given these factors, the Commission recommends three-year terms for all Presidential appointees and independent Board members, subject to the staggering mechanism described below. The Commission further recommends that the Board of Directors establish a maximum number of terms that a Board member may serve and that members be required to retire at age 70.

### *Staggered Terms*

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In order to mitigate potential conflicts of interest in the nomination process, the Commission recommends that the terms of independent Board members should be divided and staggered into three classes. Initially, two members should be appointed to one-year terms; three members should be appointed to two-year terms; and the remaining three members to a full three-year term.

### *Removal of Board Members*

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The Commission recommends that the Board continue to have authority to remove the Postmaster General for any reason. The Commission also recommends that the President have the authority to remove any Presidentially-appointed Board member and that the Secretary of the Treasury have the authority to remove any independent Board member. These powers are intended to mirror most corporate models, which permit shareholders to vote on the removal of Board members for any reason. In the past, Board members could only be removed "for cause," a term of art that narrowly covers only the most severe conflicts of interest and criminal behavior. Somewhat broader latitude is granted in this design in order to ensure a corrective mechanism exists, should this largely self-perpetuating Board begin building a tradition of mediocrity rather than excellence.

### *Committee Structure and Procedures*

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The Board should continue to utilize a committee structure that enables individual members to fulfill clearly defined responsibilities that are more efficiently and effectively carried out by a component group rather than the Board as a whole. Today, the Board has three standing committees: Audit and Finance, Capital Projects, and Strategic Planning. The Commission recommends that the Board eliminate the Capital Projects committee and have the Board as a whole approve only the most substantial capital investments. The current \$10 million threshold for Board consideration of capital projects is far too low.

The Commission also recommends the elimination of the Strategic Planning committee and instead suggests that the entire Board address issues, such as the Postal Service's product and service offerings, that have traditionally fallen within this committee's purview. In addition, the Commission recommends that the Board establish two new standing committees as it assumes a more corporate fiduciary role:

- **Nominating and Corporate Governance Committee:** Because the Commission recommends that the Board be largely self-perpetuating, selecting 8 of its 11 members, a Nominating and Corporate Governance committee is necessary. This committee should have primary responsibility for ensuring the Board includes at all times a healthy mix of leaders and skill sets that combine to form one of the world's most capable and experienced Boards. The Postmaster General should not be permitted to serve on this committee, which also should be charged with on-going evaluation of the Board's performance and needs and ensuring all Board members receive the information and training necessary to fulfill their duties.
- **Compensation Committee:** One of the most important roles of a corporate board is to ensure that management performance is aligned with clearly defined institutional objectives. One of the most powerful tools at the Board's disposal is compensation. Because the Commission recommends that the Postal Service have greater flexibility over the compensation of its senior executives (for example, pay-for-performance incentives), this committee is necessary to develop expertise in this area, including tools for evaluating executive performance. It will assume responsibilities relating to executive compensation that are currently discharged by the Strategic Planning committee. To avoid a conflict of interest, the Postmaster General should not be allowed to serve on the Compensation committee or vote on its recommendations. This committee should be free to determine the factors contributing to executive compensation decisions and have complete authority to set compensation levels to attract and retain the very best managers. (Specific recommendations relating to this authority are discussed in detail in Chapter 6.)

While the Board would have the authority to create additional committees, this configuration anticipates that work relating to postal rates, new products and services, facility closures, and real estate management would continue to be handled by the pre-existing committees or the Board as a whole. The Audit and Finance committee would also continue to play an increasingly vital role in ensuring the Postal Service's fiscal health, risk management, and financial transparency.

As is the case under current practice, each committee would operate under a charter adopted by the full Board. These charters should outline the purpose, authority and duties of each committee. They should also be available to the public and posted on the Postal Service's website.

Initially, the Board as a whole should select the members and chair of the Nominating and Corporate Governance committee. Once in place, that committee should be responsible for recommending the chairs of the other committees for approval by the Board.

### *Meetings*

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The Commission believes that the current monthly meeting schedule of the Board of Governors is excessive and invites micromanagement rather than high-level oversight and governance. For these reasons, the Commission recommends that the Board convene six regular meetings each year. In addition to the regular meetings, the Board should have the flexibility to call additional meetings when deemed necessary by the Chair or by established process.

### *Compensation*

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In order to attract the caliber of candidates equal in capability and stature to those serving on comparable corporate boards, the Commission recommends that compensation be made competitive with that of Board members of large publicly traded companies.

### *Voting Procedures*

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Under current law, most Board decisions require a simple majority, with six members present for quorum (proxies are not allowed). However, there are exceptions. For example, an absolute majority of Governors is required to appoint or remove the Postmaster General. With regard to rate-setting, the following exceptions also apply:

- *Approval, allowance under protest, or rejection of a PRC recommended rate or classification decision:* The Board may act on a majority vote of the Governors present, but five of the six members required for quorum must be Governors; and
- *Modification of a PRC recommended rate or classification decision:* The Board may act only on the unanimous written vote of all Governors.

The Commission recommends that similar voting rules continue, until the Postal Regulatory Board has established the new rate ceiling mechanism (discussed in detail in Chapter 4). Once the new mechanism is in place, rates can be adjusted *within* the limitations set by the Postal Regulatory Board on a majority vote of those Board members present (with quorum). However, a super-majority should be required to request that the Postal Regulatory Board consider approving rates in excess of the established limits.

### *Limitations on Outside Activities and Ethics*

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Currently, Board members may hold any other office or employment not inconsistent or in conflict with their Postal Service duties, responsibilities, and powers. In order to ensure an adequate level of commitment, the Commission recommends Board members be subject to the limitations on outside activities generally applied to directors of corporate boards. Consistent with corporate best practices, Board members should promptly inform the Chairman if an actual or potential conflict of interest occurs and should resign if a significant conflict cannot be resolved. Additionally, if a Board member's position or responsibilities substantially change from the time of his or her appointment, a letter of resignation should be automatically submitted to be acted on by the full Board.

#### **Setting High Standards**

*The Postal Service should be guided by an independent, self-perpetuating Board of Directors with significant financial and business expertise. Board members should have no material relationship to the Postal Service. Terms should be staggered. Regular meetings should take place six times per year. Standing committees for audit and finance, executive compensation and nomination/corporate governance should exist. Compensation of Board members should be comparable to that of similarly sized, publicly traded companies. Standard quorum and majority rules decision-making processes should apply, with the following exception: a decision to request rate increases that exceed the rate ceilings imposed by the Postal Regulatory Board should require a super-majority. Board members also should follow general corporate guidelines limiting service on other Boards to reasonable levels and should adhere to the highest ethical standards.*

## Conclusion

Given the challenges before the Postal Service and the essential role this large and complex institution plays at the center of American commerce and society, the Postal Service both needs and deserves one of the most capable boards in America. Such a Board could provide the Postal Service leadership with a wealth of sophisticated skills and experience that, appropriately applied, can reinvigorate this vital 225-year-old institution.

Supported by a governance structure that emphasizes corporate best practices, ensures a truly independent spirit, seeks out only the most qualified candidates, and focuses the Board on oversight, management accountability and “big-ticket items,” such as cost reduction, quality of service and restored fiscal health, this Board would be capable of driving the changes most needed at the Postal Service today. These advances include greater efficiency, more strategic focus, strong financial leadership, greater accountability and transparency, service and capabilities on a par with leading private-sector entities and, overall, a more businesslike approach to the delivery of the nation’s mail.

In partnership with a newly empowered Postal Service leadership, this Board would shape and define the fundamental change needed at the Postal Service. However, if the Board and postal managers are to be granted more responsibility and latitude to “steer a ship” that has monopoly powers, then appropriate oversight and accountability mechanisms must be in place, not to impede the journey, but to ensure it is appropriately undertaken.

### Chapter 3 Recommendations\*

*B-4. **Financial Transparency.** The Postal Service should voluntarily comply with applicable Securities and Exchange Commission reporting requirements. In addition, the Postal Service should periodically report on the allocation of costs among mail products and services in accordance with form, content, and timing requirements determined by the Postal Regulatory Board.*

*C-1. **Governance.** In order to establish a governance structure that exemplifies the best practices of similarly-sized private sector corporations, the current Postal Service Board of Governors should be transformed into a corporate-style Board of Directors with broad authority to oversee Postal Service operations. Further, the Board of Directors should consist of three Directors appointed by the President, the Postmaster General, and eight independent Directors initially selected by the three Presidentially-appointed Directors with the concurrence of the Secretary of the Treasury. Thereafter, the eight independent Directors would be selected by the full Board of Directors with the concurrence of the Secretary of the Treasury. All Directors should be selected based on business acumen and other experience necessary to manage an enterprise of the Postal Service’s size and significance. Terms for all Directors should be three years with a mandatory retirement age of 70.*

\* See Appendix C for a complete list of Commission recommendations.

## Endnotes

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1. The Conference Board, "Determining Board Effectiveness: A Handbook for Directors and Officers," Special Report 99-1, Nov. 4, 1998, p. 13.



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# *Chapter 4:* Protecting the Public Interest: Enhanced Accountability and Public-Policy Oversight

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## Introduction

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For the Postal Service to operate in a more businesslike fashion, its managers must have greater flexibility to manage and innovate. With this latitude, however, comes the need for enhanced managerial accountability and public-policy oversight. Managerial accountability comes from a corporate-style Board of Directors tasked with holding Postal Service officers responsible for performance. Public-policy oversight must come from an independent regulator endowed with broad authority, adequate resources, and clear direction to protect the public interest and ensure the Postal Service fulfills its duties appropriately and continues to meet the evolving postal needs of the country.

Toward this end, the Commission recommends transforming the Postal Rate Commission (“PRC”) into a new Postal Regulatory Board with broad authority to set the public-policy parameters within which the Postal Service is allowed to operate. Rather than a narrow focus on rate setting and mail classifications, this new regulatory entity would:

- Ensure the financial transparency of the Postal Service;
- Establish rate ceilings for Postal Service non-competitive products and pre-approve rate increases that exceed the rate ceilings;
- Ensure the Postal Service remains focused on traditional products and services;
- Ensure that competitive products are not cross-subsidized by revenues from non-competitive products;
- Guarantee that the Postal Service is meeting its universal service obligation and refine, as necessary, the specific elements of that obligation;
- Review proposed changes to service standards when such changes are expected to have a substantial and negative national impact;
- Review the postal monopoly for its public benefit and, if circumstances warrant, narrow it over time;
- Review worksharing discounts, negotiated service agreements, and other non-competitive rates for undue or unreasonable discrimination; and
- Ensure that the Postal Service upholds its statutory obligation to compensate its employees at a level comparable to the private sector.

It is imperative that the Postal Service (in part, a monopoly) have clear, independent regulatory oversight. Placing the oversight function in a strong, independent Postal Regulatory Board will allow greater operational latitude to Postal Service managers, while assuring the nation that the quality, reliability and affordability of the nation’s postal services will continue. As such, an improved regulatory structure can deliver both dividends and disciplines to the Postal Service of tomorrow.

## Transform the Postal Rate Commission

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Like the Postal Service, the current regulatory framework was established by the 1970 Act with the creation of the independent, five-member Postal Rate Commission. The PRC's current narrow regulatory oversight of the Postal Service has a very uneven impact. At one extreme, the Postal Service's competitive products are burdened by ratemaking procedures far in excess of anything required of private competitors or current best practices in regulated industries. At the other, the *quality* of services entrusted to the Postal Service on a monopoly basis largely escapes scrutiny altogether.

A key feature of the present rate process is the fact that new domestic rates and classifications are subject to lengthy review by the PRC *prior* to taking effect. The PRC must give all interested parties a chance to challenge the Postal Service on the need for the change. This administrative procedure, involving dozens of participants, can become extremely costly, time consuming and litigious. This makes it very difficult for the Postal Service to operate in a businesslike fashion—for example, by offering discounted products to leading customers or adjusting to unanticipated changes in costs. Every significant change demands a major administrative proceeding. This unfortunate construct places the Postal Service in an adversarial relationship with its major customers and at a distinct competitive disadvantage.

The Commission believes that independent regulation of the Postal Service must continue but that a major revamping of the regulatory review *process* is in order. In light of lessons learned under the current regime and the changing nature of postal markets, the Commission believes that the laudable goals of the current regime can be achieved more efficiently and effectively. Protecting postal customers against undue discrimination can be continued while minimizing the regulatory costs imposed on the Postal Service. Restrictions against cross-subsidy from non-competitive to competitive products can be maintained and enhanced without hamstringing the ability of the Postal Service to participate in competitive markets.

In addition, the *scope* of regulatory review should be extended. The Postal Service should not be able to pass on the costs of substantial inefficiencies to mailers captured by the postal monopoly, and the quality of services provided in monopoly markets should be held to a strict accounting. As suggested in Chapter 2, the mission of the Postal Service should be clarified and subject to outside review. Viewed against the backdrop of the Postal Service's challenges today, enhanced regulatory oversight—appropriately structured—will not be an added burden but will aid in the renewal of the Postal Service.

### A Postal Regulatory Board Founded on Public-Policy Oversight

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The Postal Service's need for oversight today is as broad as the PRC's authority is narrow. The Postal Service urgently needs a vigilant, broadly empowered and independent Postal Regulatory Board to focus on its ability to fulfill its core duties in an appropriate and effective manner. Given the significant responsibilities vested in this regulatory body, the Commission envisions three individuals of significant stature, appointed by the President of the United States for five-year terms and subject to Senate confirmation. The Commission believes that the Postal Regulatory Board members should have backgrounds in areas relevant to the regulation of large, complex business entities and that they should be selected solely on the basis of demonstrated expertise and professional standing. In selecting new members, care should be taken to ensure the broadest possible representation of skills among Board members. Additionally, no more than two of the members should belong to the same political party.

It is imperative that the Postal Regulatory Board be a truly independent institution. Like the PRC, the Postal Regulatory Board should be an independent establishment within the executive branch of the Federal government. Unlike the PRC, its budget—while supported by ratepayers—should be subject to Office of Management and Budget review but not Postal Service approval.

### What are Non-Competitive Products?

*The Commission believes that the term “non-competitive products” should include products covered by the postal monopoly as well as products over which the Postal Service has a market-dominant position. The Commission suggests that the following products should fall within the “non-competitive” category: First-Class Mail, Periodical Mail, Standard Mail, media mail, library mail, and bound printed matter. The Postal Regulatory Board should review and refine this list over time, as circumstances warrant.*

Exhibit 4-1.

Comparison of the Postal Rate Commission to the Postal Regulatory Board		
	Postal Rate Commission (PRC)	Postal Regulatory Board (PRB)
Independence	An independent establishment of the Executive Branch.	
Budget Approval	Budget subject to Postal Service approval.	Budget subject to Office of Management and Budget review.
Composition	Five Commissioners, including one Chairman, only three of whom may be of the same political party.	Three members, including one Chairman, only two of whom may be of the same political party.
Appointment	Appointed by the President and confirmed by the Senate.	
Qualifications	Members chosen based on their professional qualifications.	Members chosen solely on the basis of their technical qualifications and professional experience.
Terms	Six years.	Five years.
Authority	<p>Narrow authority:</p> <ol style="list-style-type: none"> <li><b>1. Rates:</b> Issues recommended decisions on mail rates and classifications, and fees for postal services.</li> <li><b>2. Service Standards:</b> Reviews changes in postal services that will generally affect service on a nationwide or substantially nationwide basis and offers advisory opinions.</li> </ol>	<p>Broad public-policy oversight regarding:</p> <ol style="list-style-type: none"> <li><b>1. Rates:</b> Engages in after-the-fact reviews of rate increases for non-competitive products and services.</li> <li><b>2. Cross-subsidy:</b> Ensures that revenues from non-competitive products are not cross-subsidizing competitive products.</li> <li><b>3. Postal Monopoly:</b> Clarifies and refines the scope of the monopoly.</li> <li><b>4. Cost Allocation:</b> Ensures that the Postal Service is appropriately allocating its costs across its competitive and non-competitive products and services.</li> <li><b>5. Transparency:</b> Ensures financial transparency, and obtains information from the Postal Service, if need be, through the use of subpoena power.</li> <li><b>6. Products and Services:</b> Monitors the types of products and services offered to ensure that the Postal Service does not exceed its core mission.</li> <li><b>7. Universal Service:</b> Issues standards defining the scope of this obligation.</li> <li><b>8. Service Standards:</b> Reviews proposed changes to service standards that may have a substantial and negative national impact and issues binding opinions under certain circumstances.</li> <li><b>9. Compensation:</b> Ensures that Postal Service employees receive total compensation comparable to the private sector.</li> <li><b>10. Retained Earnings:</b> Ensures that retained earnings are accumulated at an appropriate level, and consistent with the public interest.</li> </ol>

### Streamline the Rate-Setting Process

Once the Postal Regulatory Board is in place, it should move quickly to improve the rate-setting process, allowing greater flexibility to Postal Service managers while imposing firm price and spending discipline on the institution, so that rate increases are the *last* line of defense against rising costs rather than the *first*.

Unfortunately, the current rate-setting process achieves precisely the opposite effect. It is simultaneously inflexible and undisciplined. Today, when the Board of Governors anticipates that rising costs will exceed revenues, it proposes a new schedule of rates and classes and asks the PRC for a formal opinion. It can take as many as 18 months before the Postal Service sees the revenues it needs. What takes so long? The Postal Service is required to prove (and opponents spend millions of dollars seeking to disprove) that the proposed rates are “fair and equitable.” In the course of public hearings, it is not uncommon for the PRC to hear from dozens of witnesses and sift through tens of thousands of pages of supporting documents. Even after the PRC has submitted its formal opinion, the Postal Service remains tightly constricted. The Board of Governors can accept, reject, implement under protest, seek reconsideration or challenge in court the PRC’s recommendations. What management cannot do is rapidly adjust rates to changing circumstances, based on its expert opinion of the needs of the operation. What the PRC *cannot* do is tell the Postal Service that the

**Exhibit 4-2.**

<b>Reforming the Rate-Setting Process</b>	
<b>Postal Rate Commission <i>A Lengthy, Litigious Process</i></b>	<b>Postal Regulatory Board <i>A More Streamlined Process</i></b>
<p>Responsible for responding to Board of Governors requests for rate increases, or changes in the classification of mail.</p> <ul style="list-style-type: none"> <li>• Bases its judgment on a host of statutory requirements.</li> <li>• Required to hold a hearing to include representatives of the Postal Service and the mailing public.</li> <li>• Required to transmit its recommended decision to the Board of Governors within 10 months, which under certain circumstances, may be extended.</li> <li>• The Board of Governors may approve, allow under protest, reject or modify a PRC recommended decision.</li> <li>• Board allowance under protest may lead to judicial review or return to PRC for reconsideration.</li> <li>• Board rejection of a PRC recommended decision leads to a resubmission of the Board’s request.</li> <li>• Board modification of a PRC recommended decision can only take place under certain circumstances and requires unanimous Board approval.</li> <li>• May hold hearings based on complaints; issues either recommended decisions or public reports based on hearing.</li> </ul>	<p>Responsible for establishing incentive-based rate-setting methodology.</p> <ul style="list-style-type: none"> <li>• Establish baseline rates and rate ceilings for non-competitive products and services (below which the Postal Service is largely free to set rates as it wishes).</li> <li>• Upon written complaint, would conduct after-the-fact review of rate increases for non-competitive products and services. Would require adjustments if rate increases are found to be inconsistent with established rate ceilings.</li> <li>• Review, in advance, rate requests for non-competitive products and services that <i>exceed</i> established rate ceilings and rate requests for new products and services.</li> <li>• Ensure that rates for competitive products and services are not cross-subsidized by revenues generated by non-competitive products and services. Would be authorized to take appropriate remedial action.</li> <li>• Make all final determinations within 60 days.</li> </ul>

overall level of rates is too high. If the current rate-making process teaches us anything, it is how *not* to motivate a large government entity to act in a more nimble, businesslike, and disciplined fashion.

As Exhibit 4-2 illustrates, the Commission firmly believes that the current rate-setting process should be abolished and replaced with a more streamlined structure that continues to impose rigorous standards on rate setting, but does so without impeding the ability of Postal Service officials to manage and lead. In addition, this new process should proactively encourage the Postal Service to improve productivity and efficiency and not rely solely on rate increases to secure its fiscal health.

### *A Powerful New Tool to Encourage Productivity, Cost Savings*

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While increases in postage rates over the past 30 years have been kept more or less within the bounds of inflation, it is important to keep this achievement in perspective. During this same period, the prices of many other goods and services have fallen dramatically in real terms. And, compared to earlier times, the pace of postage rate increases has accelerated dramatically. Since 1970, there have been 12 increases in the price of a First-Class stamp. In the last 30 years, rate increases have become the first cure for the fiscal woes of the Postal Service, not the last.

Not surprisingly, inefficiencies and excessive costs—often structural in origin—are apparent throughout the Postal Service. This begs an important question: If the Postal Service can deliver “affordable rates” without rooting out what many believe to be billions of dollars in inefficiencies and unnecessary costs, *is* the Postal Service providing the best service it can to the nation? Clearly, the answer is “no.” But in a public-sector monopoly environment, with none of the flexibilities or bottom-line disciplines of private-sector competition, the question becomes how can the institution be sufficiently enabled and motivated to rise to a higher standard of service? Addressing this challenge head-on is implicit in the Commission’s proposed mission for the Postal Service “to provide high-quality, essential postal services by the most cost-effective and efficient means possible at affordable and, where appropriate, uniform rates.”

One of the most important tools to press the institution in this more businesslike direction is the adoption of an incentive-based regulation called “rate ceilings.” Appropriately designed, this new mechanism would greatly assist Postal Service management in its drive toward controlling costs and realizing new efficiencies. Successfully deployed, it also could deliver a wide array of corporate-style flexibilities and results:

- ***Simplicity:*** Instead of a litigious, costly and lengthy ratemaking process that can delay needed new revenues by more than a year, adjustments would be at the discretion of the Board of Directors, so long as rates remain under the ceiling. If additional revenues are needed, prices could only be increased with the prior approval of the Postal Regulatory Board.

- ***Certainty:*** Of almost equal concern to frequent mailers as the *cost* of postal services is the *predictability* of prices. Rate ceilings would permit mailers to factor rate increases into their business plans with greater predictability. They also would benefit Postal Service managers by giving the Postal Service a ceiling under which management knows they need to control costs.
- ***Timeliness:*** Rather than having to estimate two or three years out what the revenue needs of the Postal Service will be, managers will be able to adjust rates and make other operational decisions based on the realities of the current climate.
- ***Alignment:*** By building in appropriate incentives, such as the ability to retain earnings that result from keeping costs beneath set limits and allowing the Postal Service to use those earnings, in part, to finance incentive-based compensation (see Chapter 6), the motivations of Postal Service managers will be more closely aligned with the interest of customers who value controlling costs over higher postage rates.

For these reasons, the Commission recommends that the existing rate-setting procedures be replaced with an incentive-based process.

### *Incentive-Based Regulation: How It Could Work at the Postal Service*

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Rate ceilings are not merely a tool to deliver greater management flexibility. They are a powerful incentive for achieving what is largely lacking at the Postal Service today: the alignment of the interests of postal managers and employees with the interests of ratepayers. Specifically, rate ceilings allow prices to be adjusted upward within limits established by a regulator based on an “escalator” that incorporates factors for both inflation and productivity.

The organization will benefit from enhanced flexibility to adjust rates, so long as it does not exceed the ceilings established by the Postal Regulatory Board. This efficient approach would end the days of lengthy and litigious ratemaking proceedings and free the Postal Service to adapt to changing economic circumstances in a more businesslike timeframe. But if the rate ceiling is appropriately constructed, the Postal Service will also feel intense pressure to rein in spending and improve efficiency and productivity.

It should be noted that some doubt exists as to whether a public-sector institution (without, for example, employee stock options) can successfully use these tools. Leading experts, however, believe that a combination of *negative* incentives (such as holding managers accountable for performance) and *positive* incentives (such as performance bonuses) can take full advantage of this innovative mechanism to the ultimate benefit of ratepayers.<sup>1</sup>

Incentive-based regulatory schemes are designed to allow prices to be adjusted regularly and modestly upward within strict limits typically set below the rate of inflation to encourage aggressive cost reduction and productivity efforts. The specific mechanism, established by a regulator, is built around two levers: (1) the *inflation factor* allows rates to increase within limits to reflect rising costs, while (2) the *productivity factor* exerts downward pressure on rates, creating the “incentive” to reduce costs.

Such a construct forces an organization to prioritize productivity and cost savings. For the Postal Service, it abruptly ends the temptation to seek rate increases every time expenses increase. A well-designed rate ceiling can mimic the bottom-line pressures facing private companies and produce a 21<sup>st</sup> century Postal Service much more aligned with the interests of ratepayers.

Building the right rate-ceiling design is an intricate endeavor that the Commission recommends assigning to the Postal Regulatory Board. However, the Commission does have some thoughts on how such a mechanism could work:

***Selecting an appropriate inflator.*** Numerous indexes have been suggested, most notably the Gross Domestic Product Implicit Price Deflator (“GDP-PI”), which focuses solely on the domestic economy; the Gross National Product Implicit Price Deflator (“GNP-PI”), which incorporates foreign investment flows; the Consumer Price Index (“CPI”), which focuses on consumer prices rather than prices of investment goods; and, because of the labor-intensive nature of the Postal Service, the Employment Cost Index (“ECI”), developed by the Bureau of Labor Statistics. Some economists suggest a hybrid approach—perhaps 80% ECI and 20% GDP-PI—would best suit the unique nature of the Postal Service.<sup>2</sup>

***Selecting an appropriate productivity factor.*** As an offset to the inflator, the productivity factor is the pressure placed on inflation-adjusted prices to encourage Postal Service managers to reach a target performance level. It has been suggested by one economist that the Bureau of Labor Statistics’ private non-farm business total factor productivity could be a useful target for the Postal Service.<sup>3</sup>

***Application of the escalator.*** Once identified, inflation and productivity factors combine to produce an “escalator,” the adjusted formula for rate ceilings to which the organization must adhere in the pricing of non-competitive products. The regulator must then determine how to apply the mechanism to the products offered. It is not likely that one rate ceiling for all Postal Service products and services would be appropriate. To accommodate varying costs and other concerns, regulators typically rely on “baskets” and “bands.” Baskets are broad groups of products and services subject to their own price cap. At the Postal Service, this mechanism could help guard against cross-subsidization (i.e. shifting costs among “baskets”). “Bands” work similarly, but within a given basket. With regard to the Postal Service, one economist

suggests three baskets—single-piece First-Class Mail, periodicals, and other mail (excluding international)—with additional bands within each basket to limit price increases for specific products and services. That economist also recommended that prices of all products and services be required to cover incremental costs as a means of protecting against cross-subsidization, making more important the Postal Service’s cost-allocation efforts.<sup>4</sup>

**Setting Rates.** Implementation of the new incentive-based rate-setting process provides the opportunity to discard the current system involving a time-consuming and expensive comprehensive rate case every two to three years. In its place, there will be an *initial* rate case used to set rates and rate ceilings for products and services. The Commission envisions that the process for this *initial* rate case would be similar to the current rate-setting process, but with one significant difference: It would be limited to the establishment of rates and rate ceilings for *non-competitive* products and services. The Postal Regulatory Board would not determine prices for *competitive* products; it would only ensure that the initial prices set by the Postal Service are not being cross-subsidized by revenues generated by non-competitive products.

The true benefits of the new process would become apparent after this initial rate case has been completed. Once the rate-ceiling regime is in place, the Postal Service would be free to change rates without prior review by the Postal Regulatory Board, as long as rates remain within established rate ceilings and other limits established by the Postal Regulatory Board.

The Commission recognizes, however, that questions may arise as to whether the Postal Service’s rates for non-competitive products are, in fact, within established rate ceilings or whether rates for competitive products and services are covering the cost of providing the product or service. As a consequence, the Commission recommends that the Postal Regulatory Board be authorized to conduct expedited after-the-fact reviews of rate changes when a written complaint is filed. If the Postal Regulatory Board determines that the rate of a non-competitive product or service is not within an established rate ceiling or the rate of a competitive product or service is being cross-subsidized, it would be authorized to require the Postal Service to adjust the rate. Only Postal Service requests for rates in *excess* of established rate ceilings (for example, in the case of a precipitous decline in mail volumes), as well as rates for new products and services, should be subject to a similar expedited *advance* review.

Procedures established by the Postal Regulatory Board should ensure that all affected parties have an opportunity to participate through written submissions. As envisioned by the Commission, the process should be limited to the review of written submissions and should be completed in no more than 60 days.

### Simplify the Rate-Setting Process

*Replacing the existing rate-setting process with an incentive-based regulatory system will dramatically simplify the rate-setting process and allow the Postal Service to react in a timelier manner to changes in the mailing industry. The Commission therefore recommends that the current rate-setting process be repealed, and that the Postal Regulatory Board be authorized to design a new incentive-based regulatory scheme for Postal Service rates.*

The proper development of this rate mechanism is an intricate and sensitive undertaking. Fortunately, the Postal Service has a window of opportunity to implement this important change. Recent legislation signed into law by President Bush to reduce the Postal Service's pension liability (discussed in detail in Chapter 6) also includes a passage strongly discouraging a rate increase before 2006.<sup>5</sup> This provides ample time for the Postal Regulatory Board to develop and fine-tune a workable rate ceiling mechanism. The Commission recommends that the Postal Regulatory Board, over the next two years, undertake an extensive process to design the most appropriate, workable and beneficial mechanism. While the Commission believes the Postal Regulatory Board should have broad latitude in doing so, it should generally strive to develop a mechanism that promotes: reduced costs and increased efficiency, rate predictability and stability, reasonable pricing flexibility, adequate revenues and a reduced administrative burden for the rate-setting process.

### Defining the Appropriate Scope of Postal Service Operations

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Beyond designing and implementing an unobtrusive rate ceiling that both ensures affordable rates and places greater institutional emphasis on cost controls and productivity gains, other essential roles of the Postal Regulatory Board are defining the scope of the postal monopoly, refining the appropriate components of the universal service obligation, and establishing the bright-line boundaries between the postal monopoly and competitive markets.

In discharging these responsibilities, the Postal Regulatory Board would factor in changing market circumstances, hear the concerns of interested parties, weigh the arguments of the Postal Service, and make a final determination consistent with the more focused mission of the institution.

### *Upholding Universal Service*

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The Commission believes the Postal Regulatory Board is the most appropriate body to charge with regularly reviewing the components of universal service to ensure they meet the modern mail needs of a nation whose correspondence habits are changing dramatically. In Chapter 2, the Commission expressed its support for all aspects of the universal service obligation, but tasked the Postal Regulatory Board with refining key aspects of universal service as circumstances require and/or permit. These important decisions should rest with an independent entity charged with providing thoughtful, careful review and an outcome that best serves the public interest. For example, the Commission endorses maintaining the current list of products and services that are required to be offered at uniform rates, but empowering the Postal Regulatory Board to revise the list as appropriate in the future. These steps will ensure that the universal service obligation is a dynamic responsibility, one capable of changing as the country's postal needs evolve and remaining in step with the country's mail needs.



Source: USPS.

### *Service Standards*

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The 1970 Act currently requires the Postal Service to seek *non-binding* advisory opinions from the PRC whenever a “change in the nature of postal services . . . will generally affect service on a nationwide or substantially nationwide basis.” Before such a change may take effect, the Postal Service must first submit a proposal to the PRC for the purpose of obtaining an advisory opinion. In the years following the enactment of the 1970 Act, Federal courts interpreted this language in a manner that limited the necessity for the Postal Service to seek such advisory opinions to instances where three factors *coexist*: 1) the change must have a meaningful, quantitative impact on service; 2) the change must be in the “nature” of the postal service being altered; and 3) the change must affect service on a nationwide or substantially nationwide basis.<sup>6</sup> In one instance, a Court determined that the advisory opinion requirement did not apply to the consolidation of district offices because there was little evidence that consolidation would affect the nature of postal service;<sup>7</sup> in another, a Court concluded that a policy denying door-to-door delivery service to certain residents of Harris County, Texas, also did not require an advisory opinion because there was no nationwide impact.<sup>8</sup> As a consequence, the Postal Service has referred proposed changes to the PRC for advisory opinions only four times since July 1, 1971.<sup>9</sup>

Regardless of how often the advisory opinion requirement has been invoked, its practical impact is negligible. As one Court explained, Congress's intent was for the advisory opinion requirement to be a safeguard applicable only in situations where Postal Service management contemplated significant changes.<sup>10</sup> The question for this Commission is whether a new approach is necessary.

The Commission is reluctant to recommend that the Postal Service continue to have unlimited ability to change service standards. Given the economic pressures facing the Postal Service, the temptation for management at some future time to turn *first* to lower service standards as a means of reducing costs, rather than as a *last* resort, might prove irresistible. The balance lies with creating a clearer standard for *when* the Postal Service must turn to the new Postal Regulatory Board for advice, and in making such advice *binding* on the Postal Service when it will have a substantial and negative impact on national service standards. The Commission recommends the following approach:

*When the Postal Service determines that there should be a change in the nature of postal services which will negatively affect service on a nationwide or substantially nationwide basis, it shall first submit a proposal, within a reasonable time prior to the effective date of such proposal, to the Postal Regulatory Board requesting an opinion on the change. Proposals for opinions must be accompanied by an analysis of the impact of the proposed change indicating the percentage impact on: 1) aggregate volume for each class and subclass of mail affected by the proposed change; or 2) delivery points. Requests for opinions must be made by the Postal Service whenever a proposed change will result in a negative impact on more than 10% of aggregate volume at the class or sub-class level, or on more than 10% of delivery points. If the proposed change will impact more than 25% of aggregate mail volume for a class or subclass of mail or 25% of delivery points, the opinion of the Postal Regulatory Board shall be binding on the Postal Service; otherwise, the opinion is advisory.*

The Commission believes that such an approach provides the Postal Service with an appropriate amount of latitude to manage postal operations, while setting a clear standard for when it must seek external input. It also makes clear that the Postal Service may not independently lower service standards on a nationwide basis if doing so is determined by the Postal Regulatory Board not to be in the public interest. In addition, the Commission recommends that the Postal Regulatory Board be required to prepare a comprehensive annual report assessing the Postal Service's performance in meeting established service standards.

### *Oversight of Postal Monopoly*

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The Commission also recommends that the Postal Regulatory Board be tasked with clarifying and administering the scope of the postal monopoly. Given the Postal Service's status both as a monopoly and a competitor, administrative authority over the monopoly should reside outside the institution. It is inappropriate for a commercial organization to decide the scope of a law that restrains its competitors. To the contrary, it is a fundamental premise of American justice that the law should be administered by persons without a financial interest in the outcome.

The Commission also believes that there must be a reasoned and impartial administrative procedure for reviewing and updating the scope of the postal monopoly. The Postal Service has itself adopted a number of administrative exceptions to the postal monopoly.<sup>11</sup> This process of continual review of the costs and benefits of the postal monopoly is important, but is best carried out by an independent entity. The Postal Regulatory Board should therefore be vested with authority to modernize the law by narrowing the postal monopoly if and when the evidence shows that suppression of competition is not necessary to the protection of universal service without undue risk to the taxpayer.

### *Settling the "Boundary Wars"*

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To ensure that the Postal Service adheres to its core mission—delivery of letters, newspapers, magazines, advertising mail, and parcels—the Commission further recommends that the Postal Regulatory Board be authorized to monitor services and products offered by the Postal Service and to hear complaints from those who believe the institution has exceeded its authority and entered markets outside its core mission.

This opens up a complex web of questions commonly referred to as the “boundary wars.” Most would agree that every American should be able to send a letter or parcel to every other American at reasonable cost through the local post office. But should the Postal Service provide on-line bill payment? Or is that a service for which consumers should turn to a private vendor? By setting clear boundaries, the Postal Regulatory Board can deliver greater clarity and certainty for those who may find themselves in competition with the Postal Service.



Source: USPS.

## Financial Transparency

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The Commission believes that the Postal Service has a responsibility to the public to be transparent in its financial reporting. Given its important public mission and central role in the nation's economy, changes in Postal Service economic health should not come as a surprise to those responsible for or impacted by its performance.

By engaging in more businesslike financial reporting and more aggressively allocating costs by product and service, the Postal Service will gain essential insight into all aspects of its operations. Equally important, as a prominent public institution, all Americans will have a better understanding of the financial challenges and opportunities facing their Postal Service.

### *Voluntarily Comply with Applicable SEC Reporting Requirements*

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As a public entity, the Postal Service is wholly owned by the American people. They are the shareholders of the Postal Service, and they are due a regular and full accounting of the fiscal health and/or challenges facing this vital national institution.

Unfortunately, the Postal Service today is far from this goal. Since September 2000, GAO has issued numerous reports urging greater financial transparency and expressing mounting concern that fiscal pressures were putting at risk the Postal Service's ability to fulfill its mission.<sup>12</sup> The apparent catalyst for concern was the period from November 2000 through February 2001, during which Postal Service estimates of operating results for FY2001 started at a \$480 million loss, and ended up, just three months later, as an estimated loss of \$2 billion to \$3 billion, with too little explanation for the sharp decline.<sup>13</sup>

As a unifying force in American commerce and society, and as a customer-financed government endeavor, the Postal Service should be setting *the* standard for financial transparency by which all other Federal entities are judged. While the Postal Service does, in many respects, conduct financial reporting over and above what is required today of Federal agencies, it remains behind the level of disclosure offered by its corporate peers. The Commission strongly recommends that the Postal Service be required to close the gap by voluntarily complying with applicable provisions of the major SEC reporting requirements (quarterly (10-Q), annual (10-K), and "significant event" (SK-8) reports).

### *Improve Cost-Allocation Safeguards Against Cross-Subsidization*

Where the Postal Service participates in markets also served by private industry, effective oversight is essential to ensure that monopoly revenues are not manipulated to the benefit of the Postal Service's competitive offerings. For this reason, the Commission recommends that the Postal Service periodically report on the allocation of costs among all products and services in accordance with form, content and timing requirements determined by the Postal Regulatory Board.

While the Postal Service should become more businesslike, it remains a government entity. Private carriers have no U.S. Treasury to borrow from at favorable rates, no monopoly markets to reliably generate more than 75% of operating revenues and no government exemption from most taxes and laws imposed on private enterprises. Given that distinction and the Postal Service's presence in contested markets, it has a special duty to ensure it does not wield its monopoly and government privileges unfairly against companies that have no such advantages. To guard appropriately against cross-subsidization, the Commission recommends that the Postal Service significantly improve its cost-allocation system. Beyond addressing the legitimate concerns of private carriers, aggressive reforms in this area would greatly support the shift to a more streamlined ratemaking process. This approach would also enhance public confidence that postage rates reflect actual processing costs and do not unfairly shift burdens among the various classes of mail and, thus, categories of customers.

Included in the Postal Service's break-even requirement today is a specific mandate that each class of mail essentially pay for itself—covering both its direct and indirect costs and an appropriate percentage of overall institutional costs (costs that are not attributed to any one category of mail). This requirement has resulted in a two-tiered cost-allocation process whereby direct and indirect attributable costs are tallied for each category of mail and institutional costs are divided among the various categories based on eight determining factors. Historic preferences for certain categories of mail, such as periodicals and non-profit correspondence, are also provided. The system is not without controversy, due primarily to the fact that more than 40% of costs fall into this general category of institutional costs. Testimony presented to the Commission on this topic was contradictory. While the Postal Service claims that significant improvements are not feasible, one leading private-sector carrier noted it had a procedure for achieving 100% cost allocation.<sup>14</sup> The Commission feels that the appropriate target for the Postal Service lies somewhere in between. While the Commission hesitates to prescribe a percentage, there is a strong consensus that an attribution level of less than 60% is far too low, and would not be considered acceptable in similar private-sector ventures.

The Commission strongly encourages the Board to make this issue a top priority in order to ensure the system is fair, adequately protects the postal market from the distorting effects of cross-subsidization, and ensures the Postal Service has real insight into the success and failure of its various products and services. The Commission also believes that existing preferences for favorable rates for the mailing of periodicals and non-profit correspondence should be maintained.

#### Spotlight

*Private carriers have no U.S. Treasury to borrow from at favorable rates, no monopoly markets to reliably generate more than 75% of operating revenues and no government exemption from most taxes and laws imposed on private enterprises.*

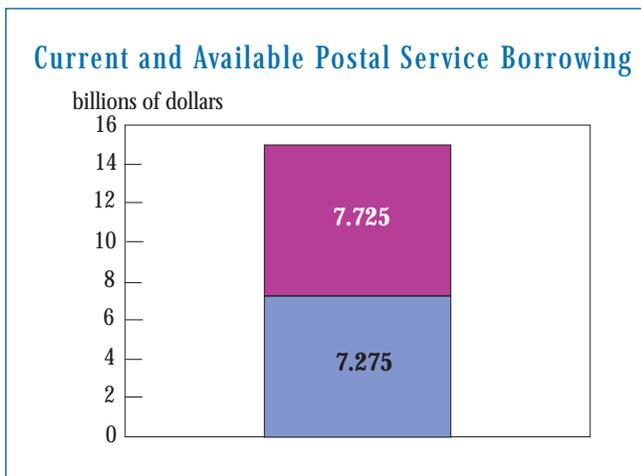
### *Procedures*

In its recommendations, the Commission has vested much authority in the Postal Regulatory Board. In order to exercise these authorities, the Postal Regulatory Board should also be authorized to establish appropriate procedures. In carrying out its regulatory functions, such as reviewing the scope of the Postal Service's universal service obligation and monopoly, the Postal Regulatory Board should employ an appropriate regulatory-style process that ensures input from those affected by its determinations. When reviewing complaints, such as whether the Postal Service has entered a market outside the scope of its mission, the Postal Regulatory Board should employ a process similar to that recommended for conducting complaint-based reviews of postal rates: the procedures should be limited to the review of written submissions and should be completed promptly, perhaps in as few as 60 days.

### *Postal Service Viability and Risk to the Taxpayer*

In addition to SEC-like reporting, the Commission recommends that the Board of Directors be required to submit annually a detailed report to the Postal Regulatory Board on the financial viability of the institution, providing both significant financial insights as well as adequate explanation of related trends. The report should adhere to the "no surprises" rule, ensuring that any major changes to the fiscal health of the institution are widely understood in advance, so appropriate responses can be anticipated and generated. The Commission further recommends that this report be made available to the public.

**Exhibit 4-3.**



Source: USPS un-audited FY 2003 Third Quarter Report on Financial Condition and Results. As of May 16, 2003, the Postal Service had outstanding debt of \$7.275 billion; the Postal Service can borrow an additional \$7.725 billion before reaching its statutory borrowing cap.

### *Debt Ceiling*

The Commission recommends continuing the current debt ceiling of \$15 billion, so the Postal Service continues to have ample latitude to cushion itself in down-cycle years and cope with the volatility and uncertainty created by electronic diversion. The Commission also recommends repealing the sub-limits on annual borrowing for capital and operating needs within the existing \$3 billion annual limit on borrowing.

### *Regulator Should Have Subpoena Power*

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For the Postal Regulatory Board to ensure financial transparency and make fully informed determinations on issues ranging from rate ceilings to cross-subsidies, it must have access to the most reliable and current information possible. For this reason, the Commission recommends that the Postal Regulatory Board have the authority to request accurate and complete financial information from the Postal Service, including through the use of subpoena powers, if necessary, to obtain a thorough and reliable snapshot of Postal Service operations.

### Ensuring Pay Comparability

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The Postal Service is required by law to provide compensation to its employees comparable to that offered by the private sector. As discussed in detail in Chapter 6, the Commission received a great deal of testimony claiming the existence of a compensation premium. Rather than take a firm position in this debate, the Commission recommends that the Postal Regulatory Board be tasked with making an impartial determination as to whether there exists a compensation premium over the private sector. If the Postal Regulatory Board determines that a premium exists, then it should be authorized to take immediate binding and corrective action for prospective new hires, once the comparability analysis is complete. The Postal Regulatory Board also should establish a reasonable timeline for corrective action for existing employees, which management and the postal unions would be required to achieve over time in their collective bargaining and arbitration proceedings. On the other hand, if the Postal Regulatory Board determines there is *not* a compensation premium, then it should say so and effectively end the debate.

#### **Upholding Compensation Comparability**

*The Postal Regulatory Board should be responsible for determining that the Postal Service is in compliance with statutory provisions requiring comparable pay to the private sector. The Regulatory Board should identify an appropriate point of comparison, and—if a premium exists—take reasonable corrective action (see Chapter 6).*

## Conclusion

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For the Postal Service to operate in a more businesslike fashion, its managers must have greater freedom and accountability for the daily operations and management of the institution. For that to happen in an appropriate way, the Postal Service needs a strong, independent Postal Regulatory Board with broad authority over matters ranging from appropriate ceilings on rates, to the scope of the postal monopoly, to the level of detail required in rigorous new financial reporting requirements. In doing so, this entity will play an important role in ensuring the financial viability of the Postal Service, protecting the health of the nation's public-private postal network, and preserving the quality and sustainability of the services upon which the American people and the U.S. economy rely.

Once an independent regulatory entity is in place, Postal Service managers must have broader latitude to modernize a vast and outdated postal network to produce substantial gains in service quality and costs. Maximizing the benefits of this endeavor will require a fundamental transformation of how the Postal Service does business: elevating the performance of the nation's postal network, taking full advantage of new partnerships and aggressively pursuing leading-edge cost-savings and productivity strategies. If pursued in tandem and as part of a comprehensive effort, such an endeavor could utterly transform the value, service and operations of the Postal Service to the benefit of its customers and the U.S. economy as a whole. Its time has come.

### Chapter 4 Recommendations\*

- B-3. **Monopoly.** The Postal Service should maintain its current mail monopoly, and also retain its sole access to customer mailboxes. However, the 1970 Act should be amended to: 1) authorize the Postal Regulatory Board to clarify and periodically review the scope of the mail monopoly; and 2) clarify that the Postal Service does not have the authority to alter the scope of the mail monopoly or to determine the extent of access to customer mailboxes.*
- B-4. **Financial Transparency.** The Postal Service should voluntarily comply with applicable Securities and Exchange Commission reporting requirements. In addition, the Postal Service should periodically report on the allocation of costs among mail products and services in accordance with form, content, and timing requirements determined by the Postal Regulatory Board.*
- C-2. **Management Flexibility.** The Board of Directors and senior Postal Service management should be given greater flexibility to manage without the limitations imposed by statutory constraints. More specifically: 1) Postal Service management should be given the flexibility to take advantage of corporate best practices; 2) the Postal Service should be allowed to set rates within limits established by a new Postal Regulatory Board without obtaining prior approval; 3) the sub-limits placed on annual borrowing for capital and operating needs within the existing \$3 billion annual limit on borrowing should be repealed; and 4) the Postal Service should be allowed to retain earnings subject to limits established by the Postal Regulatory Board.*
- C-3. **Accountability and Public-Policy Oversight.** In order to ensure that a Postal Service management with greater latitude has appropriate oversight, the Postal Rate Commission should be transformed into a new Postal Regulatory Board with the responsibility to protect the public interest and promote public confidence in the fairness and transparency of postal operations. The new Postal Regulatory Board should have authority to: review and refine the scope of the Postal Service's universal service obligation; clarify and refine the scope of the postal monopoly; regulate rates for non-competitive products and services; establish limits on the accumulation of retained earnings by the Postal Service; ensure financial transparency; obtain information from the Postal Service, if need be, through the use of new subpoena power; and review and act on complaints filed by those who believe the Postal Service has exceeded its authority. The new Postal Regulatory Board should be comprised of three members who are appointed by the President and confirmed by the Senate, and no more than two should be members of the same political party. Members of the Postal Regulatory Board should be selected solely on the basis of their demonstrated experience and professional standing.*

*C-4. **Rate-Setting Procedures.** The existing rate-setting process should be replaced with an incentive-based rate-setting methodology in which the Postal Regulatory Board: 1) establishes baseline rates and rate ceilings for non-competitive products and services; 2) reviews, in advance, rate requests for non-competitive products and services that exceed established rate ceilings; and 3) ensures that rates for competitive products and services are not cross-subsidized by revenues generated by non-competitive products and services. The Postal Regulatory Board, upon written complaint, should be authorized to conduct after-the-fact reviews of rate increases for non-competitive products and services, and, if necessary, to require adjustments to these rates when they are inconsistent with established rate ceilings. The Postal Regulatory Board should also be authorized to review, upon written complaint, whether a rate for a competitive product or service is being cross-subsidized by revenue generated by non-competitive products or services and to take appropriate remedial action. In conducting after-the-fact reviews, the Postal Regulatory Board should ensure that affected parties have an opportunity to participate, but should also ensure that the timeframe for the review is dramatically reduced from that permitted under the existing rate-setting process. Participation by interested parties should be limited to written submissions, and all procedures should require a final determination within 60 days.*

\* See Appendix C for a complete list of Commission recommendations.

## Endnotes

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12. For example, "U.S. Postal Service: Enhancements Needed in Performance Planning and Reporting," GGD-00-207, Sep. 19, 2000; "U.S. Postal Service: Transformation Challenges Present Significant Risks," GAO-01-598T, Apr. 4, 2001; "U.S. Postal Service: Financial Outlook and Transformation Challenges," GAO-01-733T, May 15, 2001; "U.S. Postal Service: Deteriorating Financial Outlook Increases Need for Transformation," GAO-02-355, Feb. 2002; "U.S. Postal Service: Moving Forward on Financial and Transformation Challenges," GAO-02-694T, May 13, 2002; "U.S. Postal Service Actions to Improve its Financial Reporting," GAO-03-26R, Nov. 13, 2002; and "Major Management Challenges and Program Risks: U.S. Postal Service," GAO-03-118, Jan. 2003.
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# Chapter 5: Pushing the Envelope: Designing a Smaller, Stronger, New Postal Network

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## Introduction

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The proper configuration of a 21<sup>st</sup> century postal network is at the heart of a successful transformation of the Postal Service. The network of processing and distribution facilities combined with technology is where the vision of a high-performing modern institution capable of continuing its enduring mission of delivering the mail to everyone at affordable rates meets the sobering reality of the Postal Service's significant fiscal challenges. With revenues stagnant and the number of delivery points increasing each year, the Postal Service today is asked to do what many in the private sector have been asked to do: bring down costs while elevating service. If truly freed to operate in a businesslike manner, the Postal Service has a real opportunity to succeed in this make-or-break endeavor.

In facing its fiscal dilemma, the Postal Service can “push the envelope” in one of two ways. It can aggressively explore new products and services in pursuit of new revenue streams, something it has done with dubious success in the past. Or, it can push the envelope of innovation, daring to acknowledge that the postal network as it exists today is far too sprawling and cumbersome for the nation's needs and that through the strategic deployment of new technologies, partnerships with the private sector and appropriate cost-reduction strategies, it can grow smaller *and* stronger—keeping the Postal Service's commitment to universal service without overburdening ratepayers.

Stagnant mail volumes place intense pressure on the Postal Service to eliminate costs and inefficiencies and modernize systems and processes throughout its network. Yet even if a changing fiscal outlook did not demand these changes, it is important to note that ratepayers deserve them nonetheless. Regardless of the economic climate, the nation is due the most cost-effective, efficient, high-quality Postal Service that strong leadership, innovative technology, pioneering partnerships, and a capable, dedicated workforce can provide.

Fortunately, given its process orientation, the Postal Service is well-positioned to gain substantial savings from new efficiency and productivity gains, *if* it is free to engage in true corporate-style realignment. In the Commission's view, many of the Postal Service's challenges can be overcome with tools and strategies readily available today. The defining challenge, however, remains significant—the willingness of all interested parties (employees, customers, partners, regulators and members of Congress) to support a strategic realignment that will dramatically alter not *what* the Postal Service does, but *how* it provides its vital services to the nation.

The Postal Service deserves praise for developing and testing its network rationalization initiative, which strives to create a sound analytical basis for redesigning the



Source: USPS.

postal network. The strategy acknowledges the need to control high fixed infrastructure costs, which have little room to fluctuate with changes in mail volumes and revenues. It also aims to reduce costs, consolidate plants, improve consistency of service and standardize processes—all providing a strong start to efforts to rein in costs while improving overall efficiency and service.

Accelerating these efforts, as the Commission recommends, involves permitting this realignment to proceed free from undue external intervention. This will be a significant challenge. The Postal Service employs hundreds of thousands of Americans in communities across the country. Its facilities, trucks, and letter carriers are—to most people—

the most visible and familiar face of the Federal government in their daily lives. Changes to the numbers of people and facilities that comprise the Postal Service affect the makeup of virtually every community. This process must be viewed and supported as advancing the nation's Postal Service, rather than undercutting it.

Toward that end, the Commission envisions a comprehensive postal network realignment that is facilitated by an independent process, much like that governing military base closures in the mid-1990s, for consolidating and closing unnecessary processing and other back-end postal facilities; asking communities to play a more prominent role in the disposition of post offices that are unnecessary for the fulfillment of universal service; promoting greater use of private partnerships to ease the Postal Service's fixed infrastructure burden; and pursuing end-to-end standardization of the postal network to reduce the uneven nature of many postal processes that combine to add billions of dollars in unnecessary costs into the system each year.

At the same time, to ensure service is enhanced, the Commission recommends revolutionizing retail access—bringing a wider range of postal services to consumers in grocery stores, pharmacies, and other convenient locations. The Commission also endorses a more aggressive approach to outsourcing that allows many postal functions to be provided by private-sector companies that demonstrate an ability to provide a higher quality service at less cost. The Commission also has specific recommendations for management of the Postal Service's substantial real estate assets, and the appropriate funding of the Postal Inspection Service and the Office of the Inspector General.

Given the opportunities to perform the nation's postal business better, the Postal Service—despite its challenges today—can have a bright future and continue to play a central role in American commerce and society. But it will take flexibility on the part of all who have an interest in the Postal Service's success—customers and employees, partners and politicians. The institution must be permitted to take full advantage of the many efficiency opportunities it should have today by virtue of its unique businesslike mandate and the strong national desire to see its vital service to the country continue at affordable prices and minimal expense to taxpayers. The Postal Service has ample opportunity today to successfully achieve these goals. Whether it is permitted to do so is largely a question for those who rely on, work in, and govern its operations.

## Rightsizing the Nation's Postal Network

There are two basic elements to the successful realignment of the nation's postal network: structure and strategies. Rightsizing addresses the *structural* component—identifying and configuring the ideal *physical* network of facilities for the most cost-effective and quality delivery of the nation's mail in the modern environment.

Few dispute that the legacy postal network relied on today is not what would be built from scratch if the Postal Service were created in the 21<sup>st</sup> century. Without question, the Postal Service has far more facilities than it needs and those facilities it does require often are not used in the most efficient manner. It should be noted that these infrastructure modernization challenges are common throughout the Federal government today. According to the GAO, the physical infrastructure of most Federal agencies is “based on the business model and technological environment of the 1950s. Many of the assets are no longer effectively aligned with, or responsive to, agencies’ changing missions and are therefore no longer needed.”<sup>1</sup> While a statement on Federal infrastructure generally, it is an apt description of the postal network today.

Corporate America, too, is feeling the pressure to take a close look at its processes, assets and strategies to ensure an optimization that minimizes costs and inefficiencies. Unfortunately, while the Postal Service has many

### Rightsizing is Reshaping Corporate America, Too

*You're a large national enterprise with a bottom line that's seen better days. While robust growth and strong revenue streams once easily financed vast operations, new fiscal realities have changed the picture dramatically. As a result, your entity's success hinges on wringing inefficiencies, redundancies and other excess costs out of the system.*

*Sound like the Postal Service? Well, yes. But it also is the story of many leading private companies. Just ask the executives at Cisco Systems. It was not long ago that the Internet giant was growing rapidly through an aggressive strategy of acquisition and new hires. Today, the Fortune 100 company is sharply focused on tackling duplication and waste. It is consolidating and downsizing its organization and standardizing technologies to boost productivity and rein in costs. In no small part as a result of these aggressive measures, Cisco's net income rose 35% during the fiscal third quarter of 2003.<sup>2</sup>*

*Rather than having myriad teams working on overlapping and sometimes competing projects, the company now stresses both standardization and versatility. For example, it now uses a single chip to power two of its most popular products when it once used different chips. This and other changes allowed Cisco to keep larger quantities of fewer parts and save \$23 million annually.<sup>3</sup>*

*As a similar process-oriented institution, the Postal Service's opportunities to benefit from greater standardization and a sharp focus on doing business in new, better and cheaper ways are significant. While they require a substantial overhaul of the legacy network, this ambitious reform is in step with current trends among leading U.S. corporations. Those that want to not only stick around but succeed tomorrow are focusing hard today on doing their work better and at lower cost.*

of the same opportunities as leading corporations to find new efficiencies, it also faces unique political and statutory hurdles. In reality, the Postal Service does not have the latitude to manage its infrastructure based on the needs of the postal network. Instead, the network remains largely unchanged and increasingly inefficient due to the inertia that results from restrictive statutory requirements as well as political resistance to closing or consolidating postal facilities.

The Postal Service must be freed from these debilitating political restraints that ill serve all who rely on the institution. It should be free to pursue its network rationalization initiative to modernize the design of the nation's postal network; it should be encouraged to work with local communities to determine the fate of low-activity post offices that are no longer necessary to the fulfillment of universal service; and it should be encouraged to fundamentally enhance all Americans' access to the most popular retail postal services—all in pursuit of greater efficiency, greater customer convenience and service, and a 21<sup>st</sup> century Postal Service that delivers like never before.

### *Rationalizing the Network*

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Many leading companies are consolidating facilities, often doing the same amount of work, simply at fewer locations, thanks to the advances of new technology, standardization and other innovative strategies in boosting corporate efficiency and productivity. The Commission fully supports the Postal Service's ambitious efforts to realize similarly positive results for the delivery of the nation's mail.



Source: USPS.

The Postal Service's network rationalization initiative is the most tangible and important deliverable of its 2002 Transformation Plan. This effort addresses the back-end distribution, processing, and bulk mail centers dispersed across the country today. While not the front-line retail post offices most familiar to the American people, the efficiency of these facilities' operations is essential to the quality of postal service that all Americans receive.

Exhibit 5-1.

Overview of Logistics Network	
Facility Type	Number of Facilities
Processing and Distribution Plant	290
Air Mail Center	90
Bulk Mail Center	21
Remote Encoding Center	20
Priority Mail Processing Center	11
International Service Center	7
Independent Mail Transfer Center	7
<b>Total</b>	<b>446</b>

Source: USPS.

Through extensive and sophisticated analysis, the Postal Service is developing a network design based on distribution concepts that allow it to simplify and standardize mail flows in order to enhance the efficiency of every aspect of postal operations. This approach shifts the focus from the performance of a particular product line or geographic area to that of the *entire* logistics network. In other words, rather than focusing solely on the efficiency of each *step* of the mail process, this strategy also maximizes the efficiency with which all the pieces *fit together*. By streamlining the distribution network, the Postal Service can pave the way for the potential consolidation of sorting facilities and the elimination of other excess costs. The ultimate deliverable of this data-driven endeavor is a robust yet flexible logistics network that reduces costs, increases operational effectiveness and improves consistency of service.

The network rationalization initiative is at the heart of the Postal Service's efforts to take \$15 billion in cumulative costs out of the institution over a five-year period. So far, the initiative has successfully designed a model that mirrors the size, scope and purpose of the challenge at hand. Now, the analysts are feeding the model with ideas from postal experts and the mailing industry, as well as various "what if" scenarios. These efforts ultimately will identify a "network consolidation point," a distribution concept that results in a more standardized and simplified mail processing environment and greater opportunities for transportation consolidation. This operational testing phase is expected to continue through the end of the year, at which time the Postal Service hopes to begin putting the new strategy to work for the nation.



Source: USPS.

To do that, Postal Service leadership will need the latitude to proceed. This will be a challenge. The centers that may be consolidated or closed employ a significant number of Americans. Understandably, political leaders become concerned when general plans to consolidate or close unneeded facilities become specific and involve people, jobs and facilities in the communities they represent. In addressing these concerns appropriately, the Commission feels there are lessons to be learned from the realignment and closures of military bases in the mid-1990s,<sup>4</sup> when the end of the

Cold War altered in significant ways the size, structure and deployment strategies of the nation's armed forces.

A widely respected independent process was put in place. The Commission recommends a similar entity be established not only for the *purpose* of closing and consolidating unneeded processing, bulk-mail and distribution facilities, but also to ensure an appropriate *process* in which the legitimate concerns of local communities and all interested parties are heard and, once decisions are made, the needs of affected communities and individuals are adequately addressed.

### Postal Network Optimization Commission (P-NOC)

*To ensure an independent and strategic realignment of the Postal Service's processing, distribution and bulk mail centers, the Commission recommends the following process be authorized through legislation to occur in two rounds, with the option for the Postal Service to ask Congress for future rounds should further alignment be required:*

**Criteria for Decision-Making:** *The Postal Service should make public the criteria it proposes to use in recommending the closure and realignment of facilities and should invite public comment. In addition, the information used in decision-making should be certified as accurate and complete by the Postal Service.*

**Commission Formation:** *The President should appoint eight commissioners with the advice and consent of the Senate, and designate a Chairman. The House Speaker, the Senate Majority Leader, the Senate Minority Leader, and the House Minority Leader should each recommend one member to the President. One member also should be selected by unions to represent bargaining-unit employees.*

**Public Hearings:** *After receiving the Postal Service's recommendations, the Commission should have four months to issue a final recommendation. During this time, it should be required to conduct open meetings on the Postal Service's proposal, receiving testimony from those who would be affected, including postal employees and customers, as well as community and government leaders.*

**Presidential Approval:** *Within 15 days, the President can accept the Commission's recommendations or reject them in whole or in part. If rejected, the President should return the list to the Commission with an explanation, and the Commission should be asked to send a revised list.*

**Congressional Approval:** *Once the President approves the plan, it should be sent to Congress with the stipulation that the plan is final unless Congress passes a joint resolution disapproving the plan in its entirety within 45 days.*

**Implementation:** *The Postal Service should begin closures and consolidations within 12 months.*

**Transition Assistance:** *Assistance should be provided through the appropriate Federal agencies, including assisting communities in determining how they can best develop the surplus property and training grants to provide the workforce with new skills.*

With mail volumes stagnant, with opportunities to outsource and provide better service at less cost (see “Leveraging the Private Sector,” p. 84), and with less fixed infrastructure to maintain, the Postal Service has significant opportunities to rein in the costs of its logistics network. To do so, however, it must be adequately shielded from external pressure to maintain an expensive and inefficient *status quo*. The process proposed above allows for broad public participation and input, but it also ensures that the unfair burden placed on *all* ratepayers today by an inefficient and outdated network can be significantly lifted.

The Commission wishes to emphasize, however, that the procedure it proposes should not be used as an excuse for delay. The Postal Service must continue its network rationalization effort without interruption and aggressively pursue opportunities to reduce costs throughout its processing and distribution system.

### *Allowing Communities to Determine the Fate of Low-Activity Post Offices*

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While a substantial portion of the savings and streamlining of the nation’s postal network will occur on the back-end logistics side of postal operations, the Postal Service today also needs to constructively address the fact that many of the nation’s post offices are no longer necessary to the fulfillment of its universal service obligation, given with the proliferation of alternate retail access points in grocery stores, drug stores, ATMs and other more convenient locales in communities across the country.

The Postal Service’s ability to tackle this issue head on is strictly limited by Congress, which regularly includes language in annual appropriations bills forbidding the closure or consolidation of rural post offices.<sup>5</sup> This protective approach to local post offices has been a mainstay of postal legislation going back to the 1970 Act, which flatly orders that “no small post office shall be closed solely for operating at a deficit.” The intent, quite clearly, is a good one—to protect universal access to postal services. This aim is reinforced in the 1970 Act, which also includes language making plain the “specific intent of the Congress that effective postal services be insured to residents of both urban and rural communities.”

Fortunately, the Postal Service has a unique opportunity to address both the intent of Congress to uphold universal access to postal services and the legitimate concerns of a self-financing institution to rein in unnecessary expenses. The first opportunity—a dramatic expansion of the availability of the most common postal services (from stamp purchases, to Express Mail, to parcels) in grocery stores, pharmacies, banks, and other convenient locations—has profound positive implications for the convenience and accessibility of postal services to all Americans. (These efforts are discussed in detail in the next section, “Freeing Postal Service From the Post Office.”)



Source: USPS.

As postal services become more available at alternative venues, the Postal Service will be in a position to assess whether maintaining a particular “low-activity” post office is necessary for the fulfillment of the Postal Service’s universal service obligation in the geographic area served by that facility. If the answer is in the affirmative, then the “low-activity” post office should remain open and continue to serve its community, even if it is operating at a significant economic loss. If, on the other hand, the Postal

Service determines that a post office is no longer necessary for the fulfillment of its universal service obligation (presumably because postal services are adequately available at other convenient locations), then the Postal Service should have the flexibility to dispose of that facility as it sees fit, including through the facility’s sale.

The Postal Service may find there is no adequate market demand for the purchase of a “low-activity” post office. Under these circumstances, the Commission encourages the Postal Service to work with state and local governments, as well as not-for-profit organizations, to determine the means of disposition most beneficial to the local community. Such disposition could include transfer to a state or local government or not-for-profit organization, with or without reimbursement, as best serves the public interest.

### Maximize the Potential of “Low-Activity” Post Offices

*“Low-activity” post offices that continue to be necessary for the fulfillment of the Postal Service’s universal service obligation should **not** be closed, even if they operate at a substantial economic loss. In circumstances where universal service is protected, the Postal Service must have the flexibility to dispose of “low-activity” post offices with appropriate local community involvement. Existing statutes limiting the Postal Service’s flexibility with respect to the disposition of post offices should be repealed and similar provisions in annual appropriations should be avoided.*

Particularly at a time of significant budget crunches, access to surplus Postal Service infrastructure could be very beneficial to local and state governments. This approach would reflect the local nature of the postal network and ensure these facilities continue to serve the communities in which they have been a valued presence. (Further discussion of best management of the Postal Service’s substantial real estate portfolio is found in the section on “New Efficiencies,” p. 94.)

### *Freeing Postal Service From the Post Office: Revolutionizing Retail Access*

The approach outlined above for addressing “low-activity” post offices would not be possible today, if it were not for the exciting revolution underway in how the nation receives its postal services. In recent years, the Postal Service has taken significant steps in expanding retail access.

Today, Americans can perform basic Postal Service activities at 5,000 grocery stores, Wal-Mart stores, and banks. They can buy stamps at some 17,000 ATM locations, approximately 20,000 consignment locations (typically, grocery stores), through the mail, and over the Internet. Also, the Postal Service has developed next generation self-service kiosks, called Automated Postal Centers, which provide about 80 percent of postal products and services, including First-Class Mail, Priority Mail, Express Mail, Parcel Post, Delivery Confirmation, Certified return receipt, and international postage. The Service plans to begin deployment of 2,500 of these kiosks in communities across the country in 2004. These alternatives offer an equivalent standard of service as a post office at substantially less cost. They also enhance customer service by eliminating the greatest inconvenience of a post office—having to make a special trip there.

*Exhibit 5-2.*

<b>The Cost to the Postal Service of Selling Stamps</b>		
<b>Location of Stamp Purchase</b>	<b>Share of Sales</b>	<b>Cost to Postal Service per Dollar</b>
Post Office counters	80%	\$0.07
Supermarkets, drug stores and other large retailers	7%	\$0.016
ATMs	1%	\$0.016

Source: USPS.

This new approach offers a win-win proposition to the Postal Service and its customers—far more convenient, often 24x7, access to basic postal services at significantly less cost to ratepayers. It does so by questioning one of the most basic assumptions of how postal services have traditionally been delivered, asking if customers should *have* to go to a post office to get these services. The answer in many communities today is “no.” In fact, the day may not be too far off when the answer is also “no” for an even more far-reaching question: Do most Americans *ever* have to set foot in a post office again? Special trips and afternoon lines all could become a thing of the past.

In pursuit of enhanced customer service and convenience, as well as substantially reduced overhead costs, the Commission recommends that the Postal Service dramatically escalate its efforts to forge partnerships to expand access to postal products and services beyond traditional post offices and bring these services *to* customers—at home, at work, and where they shop. Specifically, the Postal Service should aggressively explore new partnerships with grocery stores, pharmacies, banks, convenience

stores, and small businesses to sell stamps and other postal products at their facilities and to place automated postal centers in convenient locations. To speed these endeavors, the Commission believes that the Postal Service should set clear annual targets for moving a greater percentage of postal transactions out of the post office to less expensive and more accessible retail outlets and should make achieving these targets a management priority.

### Set Annual Targets for Bringing Postal Services to Consumers

*The Postal Service should aggressively expand and market retail access to postal services in venues other than post offices to enhance convenience for customers and dramatically reduce facilities and overhead costs. The Postal Service should set clear annual targets for this expansion and make it a management priority to meet these goals.*

By making Americans more aware of convenient alternatives, a collateral benefit is easing the burden on post offices by diverting many simple tasks. Postal surveys indicate, for example, that about one in three people visiting a post office make the trip solely to buy stamps.<sup>6</sup> The Postal Service should be more aggressive with its marketing to help people understand the growing number of alternatives available and just how many different postal services are covered by these options.

### Leveraging the Private Sector

With a process in place to appropriately identify and realize a streamlined, effective structure for the nation's postal network, the next step is to identify strategies to allow for its successful deployment. Here, the private sector can and should play a much more prominent role. Most Americans are relatively unaware of the fact that private carriers already play key roles throughout the postal network in ensuring universal mail delivery and access to postal services. FedEx and other private air carriers, for example, are responsible for almost all of the long-haul air transport of the nation's correspondence. The Postal Service also is the global pioneer in worksharing—offering discounts to high-volume mailers who do a portion of the processing, distribution, and shipping themselves, in order to ease the demand for the Postal Service to grow its own infrastructure.



Source: FedEx.

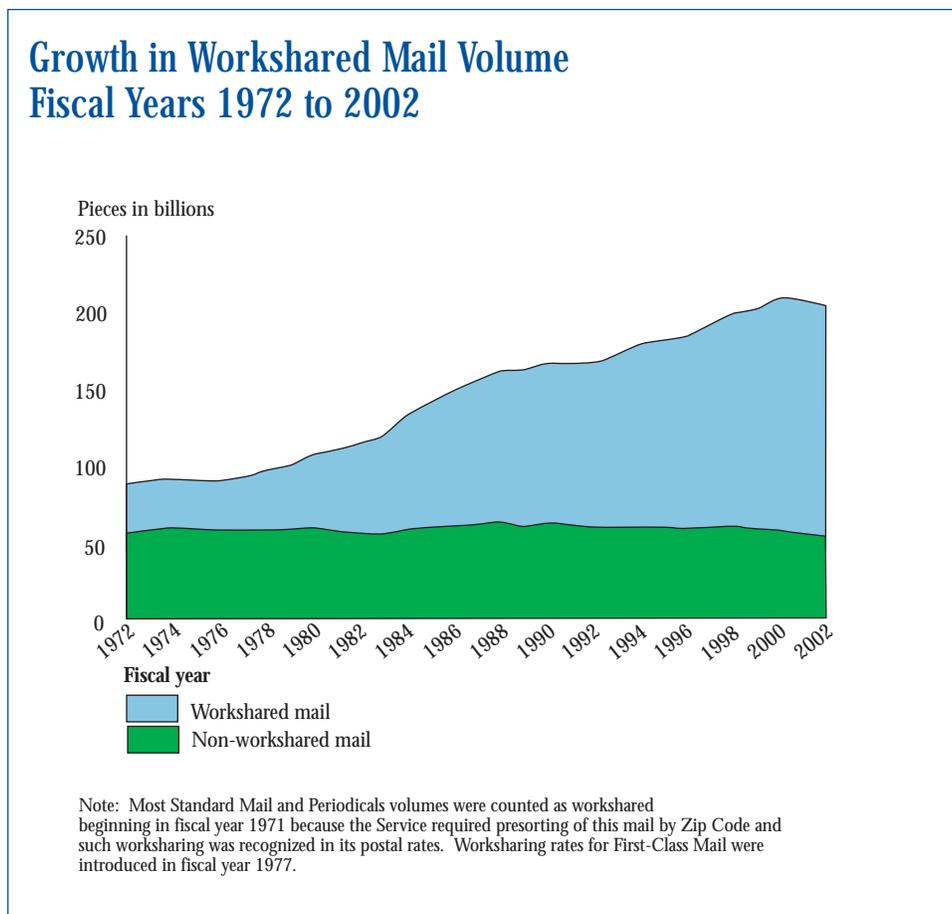
Far more can be done with the private sector today to improve the nation's mail service, reduce costs, and gain new efficiencies. All of it can and should be done according to a core philosophy: Those who can do it best and for the best price should have the job, regardless of whether the "best execution" provider is the Postal Service and its existing workforce or a private-sector company. This greater integration of the public and private postal networks will add value to both. It also holds the possibility of allowing the Postal Service to focus on its true core competency: delivery of the mail, the first and last mile reach that makes the Postal Service unique.

*Worksharing: Involving Customers as Partners*

The U.S. Postal Service is an international pioneer in the field of worksharing arrangements that offer mailers discounts in exchange for performing more of their own mail preparation, including presorting, bar coding, standardization, and dropshipping. These efforts substantially ease the burden on the Postal Service’s infrastructure, and represent a trail-blazing strategy in which mail processing in the U.S. has been opened up to the private sector in a way not imagined in foreign posts.

In 2002, worksharing discounts totaled \$15.2 billion.<sup>7</sup> According to one estimate, the Postal Service would have to employ an additional 187,000 people to perform the tasks being handled by its worksharing partners.<sup>8</sup> As a result, worksharing is an attractive concept both for the Postal Service and for mailers because it enables the Postal Service to employ fewer people, reduce expenses, and control the costs ultimately passed on to ratepayers.

**Exhibit 5-3.**



Source: GAO (GAO-03-812T).

Because it is mutually beneficial to the Postal Service and its customers, the Commission recommends that the Postal Service continue to explore opportunities to develop additional worksharred products, particularly as new technologies are developed, that reflect lowest combined public-private sector costs. The Commission also recommends that the Postal Service work closely with smaller mailers to develop ways for them to participate in these mutually beneficial arrangements.

### Worksharing: Get the Customer More Involved

*Worksharing discounts are a valuable strategy for controlling the fixed infrastructure costs of the Postal Service and should be more aggressively pursued. To assist that effort, Congress should eliminate the time-consuming ratemaking process governing the approval of a work-sharing discount for a non-competitive product. In its place, the new Postal Regulatory Board should be authorized to perform an expedited, after-the-fact review, upon written complaint, to ensure discounts do not exceed savings to the Postal Service.*

The Postal Service needs greater flexibility to pursue these partnerships. This will require transitioning from the cumbersome ratemaking process imposed on the discounts today. The Commission believes such a move could occur while *enhancing* oversight by specifically requiring that no new worksharing discount for a non-competitive product should exceed costs saved (including the present value of projected future costs saved) and that the Postal Regulatory Board should have the authority to conduct an expedited, after-the-fact review upon written complaint that such a discount is excessive. This approach would ensure costs and other burdens are not shifted onto postal employees or ratepayers generally, while producing breathing room for the Postal Service in avoided infrastructure costs. This alignment of costs with discounts can become even more precise when combined with the cost-allocation recommendations of the previous chapter.

### Passing the Envelope: Outsourcing What Others Can Do Better, at Lower Cost

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For the Postal Service to make the most productive use of its assets and focus on the delivery of mail, it should be not only free but encouraged to outsource functions that the private sector can do better and more cost-effectively.

Already today the Postal Service outsources several key functions of the nation's postal network, including its long-distance air transportation and most of its technology research and development.<sup>9</sup> The Postal Service is correct in its assessment that many other functions could be outsourced successfully, as well. In fact, this is a positive trend being encouraged throughout the Federal government today. A recent update to the President's Management Agenda encourages public-private competition for tasks currently performed by Federal employees that are readily available in the commercial marketplace, where the private sector can perform them cheaper or better.

In pursuing this strategy, the Commission believes that decisions regarding which functions to outsource are best left to Postal Service management. In doing so, the Commission suggests that the Board of Directors be especially mindful of decisions requiring expenditures for automation technology. The Postal Service increasingly relies on automation to improve efficiency and reduce costs; in many cases, new technologies used by the Postal Service have resulted from partnerships with the private sector.<sup>10</sup> In that respect, the Commission acknowledges the steps taken by the Postal Service to automate its system for processing single-piece letter mail and welcomes the progress made in the automation of the processing of flats and packages. The Commission, in fact, recommends that the Postal Service continue the development of an effective merging system that is responsive to customer needs and culminates in one bundle of mixed letters and flats for each delivery point.

However, the Commission also believes there needs to be a balance between continued capital investment in technology and appropriate outsourcing of parts of the processing network. When faced with future decisions relating to the investment in new automation technology, the Board of Directors should consider whether the Postal Service is contemplating the purchase of the appropriate amount of a new technology, and whether the technology relates to a function that can be performed better and at less cost by the private sector. The Postal Service should be encouraged to continue this type of collaboration with the goal of balancing its desire to be at the forefront of mail piece processing technology with the need to contain costs.

The Commission also encourages the Postal Service to consider contracting out several “big-ticket” functions that go beyond the institution’s core competency. These include: real-estate management, vehicle maintenance, management of information technology systems, and other services incidental to the delivery of mail. Outsourcing peripheral but important functions would ensure these significant areas are managed by dedicated teams of experts who could apply their experience to the successful management of these assets and functions.

By hiring experienced professionals in these areas, who are wholly focused on a particular operation, the Postal Service is free to focus on its own core competency—delivering the mail. This outsourcing of non-core functions, particularly real estate asset management, is also a popular trend among corporations today because it permits them to focus on doing what they do best while leaving the rest to outside experts. In at least the case of transportation, costs are rising disproportionately faster than the overall cost of the postal network. Thus, applying focused expertise on these areas could deliver substantial value. The Commission believes that outsourcing these functions to experts in these fields wholly dedicated to their successful and effective management could potentially save the Postal Service hundreds of millions of dollars annually.

### Seek Out the “Best Execution” Provider

*The Postal Service should focus on its core competency—delivering the mail. Where private companies can deliver portions of the nation’s postal service or specific related functions better and at lower cost, those tasks should be outsourced.*

### *Focusing on the First and the Last Mile: New Private-Sector Partnerships*

The real strength and unique value of the Postal Service is its daily connection to virtually every American. No other service delivers to as many addresses as the Postal Service—approximately 140 million homes, businesses, and post office boxes. The Commission recommends that the Postal Service continue to explore opportunities to leverage its “first” and “last” mile reach through the development of mutually beneficial partnerships with the private sector.

#### **Leverage the Postal Service’s Core Strength**

*The Postal Service should explore new partnerships with the private sector that leverage its first and last mile capabilities and connect them with private sector efforts to deliver new consumer propositions to the U.S. postal and shipping market.*

Partnerships that leverage the first and last mile are still in their relative infancy. But the Postal Service should pursue wherever possible opportunities to leverage its extensive delivery network while benefiting from the complementary strengths of the private sector. One example of successful public-private cooperation is Airborne@home, a residential delivery service of Airborne Express whereby Airborne picks up large volumes of parcels from shippers and dropships them to the local post office closest to the recipient. The Postal Service then delivers the parcels the “last mile.”<sup>11</sup> Where the Postal Service can work with private companies to deliver innovative new consumer propositions that leverage its first- and last-mile reach, it should fully explore these opportunities.



Source: Airborne Express.

### *Pumping Up the Volume: Negotiated Service Agreements*

With more personal correspondence taking place online, a greater percentage of Postal Service volume is generated by businesses, oftentimes communicating with their customers.<sup>12</sup> Whether it is marketing or billing, Americans continue to indicate their strong preference that these communications take place through the mail.<sup>13</sup> For this reason, substantial opportunities exist to maintain and even grow this category of mail, particularly if the Postal Service continues to be a global pioneer in innovative partnerships with other postal companies and its most active customers.

Perhaps the most promising new area for exploration is Negotiated Service Agreements (“NSAs”). The Postal Rate Commission recently approved the first such agreement with Capital One Services, the single largest producer of First-Class Mail today.<sup>14</sup> Under the agreement, Capital One will be eligible for volume discounts if its annual First-Class bulk mail volume exceeds 1.225 billion pieces. The agreement offers discounts ranging from three to six cents per piece of mail, increasing as Capital One’s mail volumes increase.<sup>15</sup>

In addition to the stability and possible growth of this mail stream, the agreement permits the Postal Service to avoid the costs of returning undeliverable Capital One solicitations—for a three-year savings in excess of \$40 million. To assure that other mailers are not disadvantaged by these terms, the PRC imposed a three-year cap of \$40.6 million on the discount, which equals 95% of the Postal Service's savings over that same period. In approving the agreement, the PRC stated that it would be premature to adopt rules governing NSAs generally. It did stipulate, however, that once an agreement is approved, comparable terms must be made available to similarly situated customers, a decision this Commission supports.<sup>16</sup>

While this landmark agreement certainly is a positive step, the cumbersome eight-month process required for its approval is a cause for concern. Perhaps it was justifiable to proceed carefully for the first agreement. However, the fact that every NSA will be subject to this same ratemaking proceeding before it can commence is a hurdle that many potential private partners—used to the faster pace of corporate transactions—will deem too high. Such a lengthy regulatory review process runs contrary to the speed and decisiveness of successful private sector endeavors. As a result, those who could be valuable partners and stabilizing forces on mail volumes may not be willing to submit to such a time-consuming and tedious process. This cumbersome approach also undercuts the spirit of the agreement: The Postal Service is offering to be more responsive to the needs of its highest volume mailers to stabilize and possibly grow mail volumes. Yet, under the *status quo* procedures, its ability to respond to customer needs could take close to a year to commence.

NSAs could benefit the Postal Service by fostering overall cost efficiency and revenue growth. As such, the Commission believes these agreements are entirely appropriate given the Postal Service's businesslike mandate. However, the current process for evaluating these agreements discourages their use by delaying and increasing the cost of negotiating customer-specific rates. Thus, the Commission recommends that the Postal Service be given greater flexibility to enter into these agreements in a more timely fashion, so long as it abides by general criteria established by the new Postal Regulatory Board. Rather than “presuming guilt” and putting off the benefits of the partnership to both parties, the Postal Regulator should have the authority to conduct an expedited, after-the-fact review of an agreement, if a written complaint is filed.

### NSAs Must be Available to Similarly Situated Customers

*The Postal Service should be permitted to enter into NSAs with individual customers based on general criteria established by the Postal Regulatory Board. Rather than requiring a protracted rate proceeding, the Postal Regulatory Board should be authorized to conduct an expedited, after-the-fact review of a specific agreement, if a written complaint is made challenging its compliance with the Postal Regulatory Board's established criteria. Once terms are agreed upon, they must also be made available to similarly situated customers.*

## Rethinking the Entire Mail Processing System

With the process begun by the Postal Service's own network rationalization initiative and the aggressive expansion of the Postal Service's private-sector partnerships, a far broader universe of possibilities opens up to the Postal Service in terms of the performance levels the institution is capable of achieving. To take maximum advantage of these opportunities, the Postal Service must look far beyond how best to get the most out of its *existing* infrastructure, and begin to contemplate all the different ways it can harness the possibilities of new technologies and leading-edge corporate strategies to maximize productivity and capacity in order to propel the Postal Service to a higher standard of excellence.

Given the aging nature of the Postal Service network and the fact that it was designed for a different era, such a fundamental redesign should begin with a fresh and thorough examination of every legacy system within the mail processing chain to reassess its forward-looking value, purpose, and necessity. This review would be just the beginning of a wide-ranging examination of the total overhaul of the mail

processing endeavor with an eye toward redesigning it as a single integrated system. In conducting this study, the Postal Service should employ a rigorous and disciplined methodology that incorporates data and statistical analysis to measure and improve operational performance by identifying and eliminating inefficiencies at every stage of postal processing, including: mail preparation, rationalization of the processing network, introduction of new automation to the delivery function and other key areas where small variations in how tasks are performed combine to create costly impediments to productivity and efficiency.

Such a system also should integrate *quality* control mechanisms, enabling deep, real-time visibility into performance, maintenance requirements, and productivity levels throughout the mail processing system.

### Think Big: Redesign the Entire Mail System

*The Postal Service should study the problem of mail processing within the broader goal of redesigning the entire mail system, using the most sophisticated technologies available. As a part of this process, the Postal Service should examine every legacy system and reassess its modern-day value and necessity. Given the ambition of this planning effort, the Postal Service should begin immediately.*

*Building a Common Postal Service Footprint*

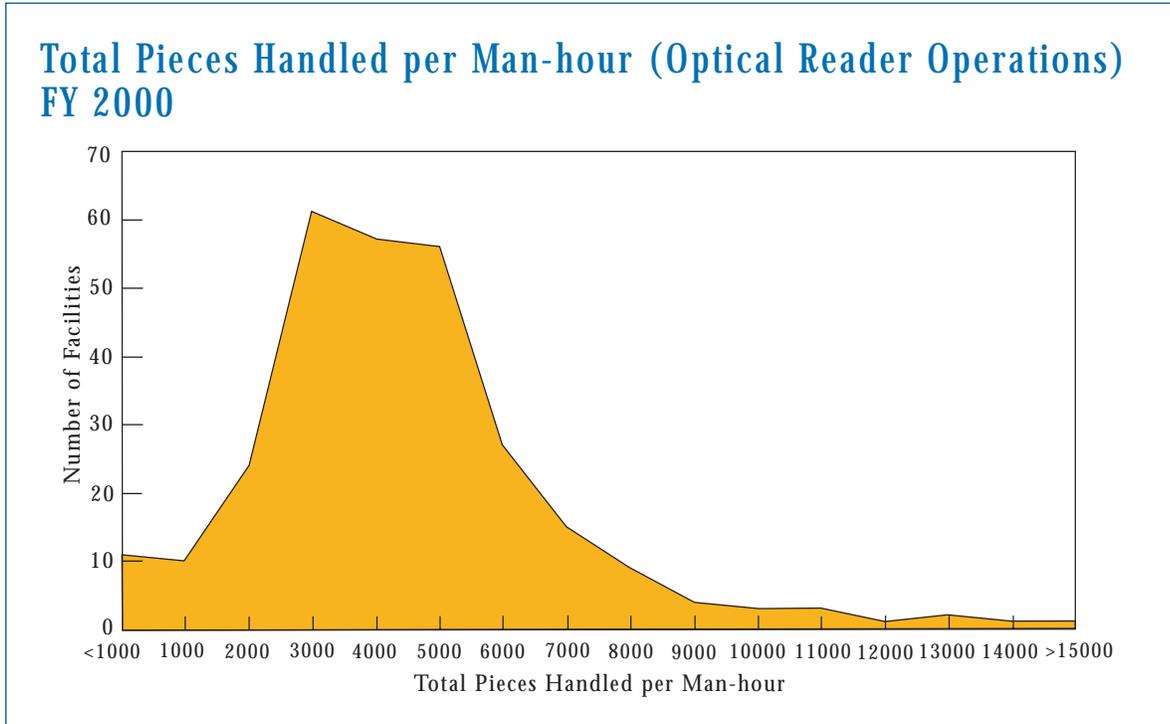
Many leading corporations, particularly those with process-oriented operations, are seeking to reduce friction in their operations in order to enhance productivity and efficiency. The ability for a line worker to move from a plant in Dallas, Texas, to a plant in Dearborn, Michigan, for example, is highly valued as companies seek to make basic tasks, facility design, and operations nearly identical throughout their operations.

The Postal Service should strive for a similar standardization of its facilities as a part of any redesign of the mail processing chain. The facilities of the Postal Service today are far too different in architecture and machinery to allow an integrated and flexible system. From facility to facility, the differences run from general floor plan design, to the type and age of the machines used, and even to new technologies installed. The Commission believes the mark of a good mail system is the ability to place employees at any facility and have them start work immediately without retraining. Building a common facility footprint is essential to attaining such a high degree of efficiency.

**Standardize Facilities, Tasks to Produce Substantial Savings**

*Any overhaul of mail processing systems should seek to establish a standard footprint for every processing facility and an identical level of technology and machinery. This would allow for seamless shifting of personnel to manage mail flow more efficiently and the elimination of costly and obsolete postal facilities.*

**Exhibit 5-4.**  
**Productivity Varies Widely by Facility**



Source: Postal Rate Commission.

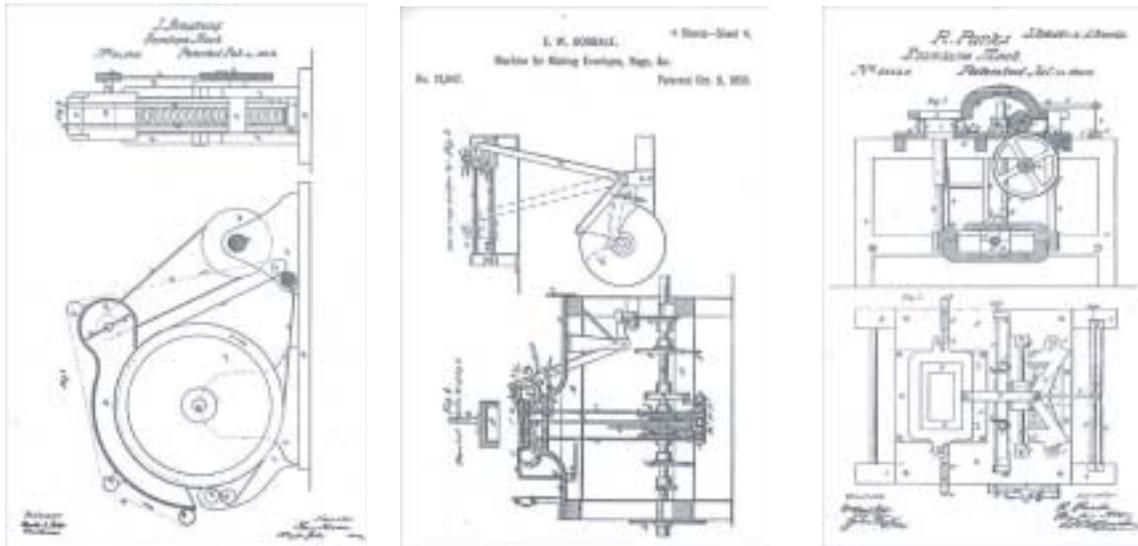
This graph demonstrates the widely varying productivity rates of the Postal Service's Optical Character Recognition (OCR) technology, indicating different productivity rates on various types of machines across Postal Service facilities.

*Changing the Shape of the Mail*

While many opportunities exist to standardize virtually every aspect of the postal network, one of the most controversial measures revolves around “outliers”—mail of unique size and shape that requires manual handling to process. Individual Americans may have encountered this issue upon realizing their oddly sized holiday cards required additional postage. For the most part, however, this is hallowed ground for large mailers, particularly advertisers, who argue that their creative efforts to catch the eyes of consumers (and, thus, the value of advertising through the mail) would be reined in significantly if the Postal Service were to require that all mail be the same size.

**Exhibit 5-5.**

**19<sup>th</sup> Century Envelope Manufacturing Machines**



*Crucial to the everyday conduct of business and daily life for most Americans was the ready-made envelope, an innovation that helped make possible the inexpensive and reliable delivery of mail to every part of the country. Between 1840 and 1900, the manufacture of envelopes was a catalyst for continued commercial expansion and diversification.*

Source: National Postal Museum.

On the other side of the fence, size standardization can produce substantial savings, allowing near total automation of letter handling. As a result, it is an attribute of some foreign posts, such as Post Denmark.<sup>17</sup> The Commission views skeptically the costs associated with accommodating non-standard sized mail, particularly the burden imposed on all ratepayers by the fact that current premium pricing is widely believed to fall short of the true cost of accommodating much of this mail. As a result, the Commission recommends “outliers” either come back into the fold or pay the full price of their unique journey.



### Non-Standard Mail Should Cover All Costs

*In consultation with its customers, the Postal Service should develop uniform design requirements that deliver processing efficiencies and savings to ratepayers generally. Mailers wishing to continue sending odd-size letters should be permitted to do so, but the premium rates charged should cover all related costs.*

Source: Envelope Manufacturers Association.

### *Involving Interested Parties in the Future of the Mail*

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Modernizing the nation's mail system will require overcoming another series of potential obstacles—the often parochial concerns of postal customers, partners, and employees. Employees, understandably, are worried about new productivity and performance targets and what greater automation means for their jobs. The business community, as noted above, has concerns about the potential effect on *how* they reach out to customers through the mail. Finally, members of Congress, while generally supportive of postal modernization, worry about the impact on employment and facilities in their districts. The Commission firmly believes that an ambitious standardization initiative should be viewed from the exact opposite point of view: By squeezing billions of dollars in inefficiencies out of the legacy network, the Postal Service is in a much better position to compensate its employees well and build state-of-the-art facilities to advance service quality and efficiency for all Americans.

Historically, collaboration among postal employees, customers and private-sector partners has been uneven, particularly when affected parties are asked to do business in new ways. Hopefully, that can change through the broad recognition of the ultimate value of the endeavor to everyone. Success in end-to-end standardization would generate significant cost savings to the Postal Service and allow postal operations to advance to a level of performance and productivity not thought possible until very recently. By asking relatively small sacrifices of all parties that work for and rely on the Postal Service, the institution can be made far stronger for the country as a whole.

### Public Support Is Essential

*The Postal Service should work closely with its customers, employees, partners, and Congress to structure an integrated 21<sup>st</sup> century mail processing system that advances the Postal Service's efficiency, productivity and service to the nation.*

## New Efficiencies

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In addition to the substantial savings and productivity gains that can be secured by a strategic realignment and modernization of the nation's postal network and a greater range and number of partnerships with the private sector, additional initiatives can further enhance the institution's efficiency and cost savings. These efforts include: reforming the Postal Service's procurement rules to more closely mirror corporate best practices, strategically managing the Postal Service's vast real estate holdings, and revisiting how law enforcement and key oversight functions are financed within the Postal Service.

### Procurement Reform

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#### Spotlight

*The Postal Service spent nearly \$12.4 billion in 2002, purchasing everything from supplies and equipment, to rent and fuel, to construction and mail transport services. It owes ratepayers one of the most efficient and sophisticated procurement efforts in the country today.*

Companies in the private sector have been able to lower costs substantially through sophisticated breakthroughs in materials purchasing techniques in recent years. While the Postal Service has adopted some private-sector best practices pertaining to procurement, potentially hundreds of millions of dollars can be gained by a more aggressive approach. The Postal Service spent nearly \$12.4 billion in 2002, purchasing everything from supplies and equipment, to rent and fuel, to construction and mail transport services. It owes ratepayers one of the most efficient and sophisticated procurement efforts in the country today.

Getting there, however, means overcoming significant barriers that are simply unparalleled in the private sector. The 1970 Act appropriately grants the Postal Service latitude to conduct its procurement with fewer substantial regulations and statutes than those governing Federal purchasing generally. However, the Postal Service has consistently elected not to take advantage of the flexibility. Official explanations revolve around claims of intense public pressure to abide by the more rigorous and costly standards imposed on other Federal agencies. It is the view of this Commission that it is inappropriate to apply regulations and statutes aimed at traditional agencies to a Federal entity required to finance its own multi-billion-dollar operations. The Commission therefore recommends that the Postal Service take full advantage of the flexibility it is granted under current law and that Congress strongly support its aggressive procurement reforms in acknowledgement of its substantial benefits to all ratepayers.

The importance of this support will only grow as more vital postal functions become candidates for outsourcing. The ability to select the most capable contractor, with an attractive cost and a high quality of service, should be the paramount concern of all parties. The Commission is encouraged to note that the Postal Service is currently working to revise its purchasing regulations to maximize the flexibility provided to it under current law and to reflect commercial best practices. The Commission strongly supports these efforts and urges Congress to do the same.

### Flexing Their Buying Power

*With nearly \$12.4 billion in purchases last year, the Postal Service and its customers would benefit greatly if the Service joined the purchasing revolution sweeping leading corporate enterprises today.*

*Leading the trend is Wal-Mart. Last year, the company created its own internal Global Procurement Division, which is stripping away costs so successfully (saving 25% on zippers alone) that the division is expected to be a key earnings driver for Wal-Mart over the next five years.<sup>18</sup> Retail chain Kroger also cut costs by \$306 million last year through procurement reform.<sup>19</sup>*

*When the U.S. economy faltered, procurement reform was among the first places corporate leaders looked to root out excess costs. The Postal Service could potentially achieve similar savings, if it aggressively followed the example of its private-sector retail counterparts.*

### Get More Bang for the Buck through Procurement Reform

*The Postal Service should revise its purchasing regulations to take full advantage of the flexibility given to it under current law. The Commission also encourages Congress to support these efforts in acknowledgement of the substantial savings they will produce for all ratepayers.*

### *Best Management of the Postal Service's Significant Real Estate Assets*

The Postal Service is one of the largest property owners and renters in the Federal government today.<sup>20</sup> It pays more than \$840 million per year in rent. It owns more than 222 million square feet of office, warehouse and other internal space and more than 900 million square feet of land. Its more than 35,000 facilities range in size from less than 100 square feet to more than 1 million square feet; in age, from more than 100 years old to brand new; in location, from inner cities to remote rural areas; and, in function, from highly automated processing facilities to one-person retail outposts (Exhibit 5-6).

While the Postal Service's substantial real estate portfolio has a current book value of approximately \$15 billion, its current *market* value is believed to be a multiple of that figure.<sup>21</sup> Needless to say, effectively managing this portfolio is a major undertaking with significant implications for the Postal Service's ability to fulfill its mission of delivering universal service at affordable rates.

#### **Exhibit 5-6.**

<b>Postal Service Facilities</b>	
<b>Inventory</b>	
Total owned facilities	8,313
Total leased facilities	26,319
Total GSA/other government facilities	431
<b>Total facilities</b>	<b>35,063</b>
Total owned interior square feet	222,068,232
Total leased interior square feet	102,039,015
Total GSA/other government interior square feet	4,067,574
<b>Total interior square feet</b>	<b>328,174,821</b>
<b>Total owned land in square feet</b>	<b>900,302,842</b>
<b>Rent Paid (in millions)</b>	
<b>Annual Rent paid to lessors</b>	<b>\$ 841.1</b>
<b>Income Received - FY 2002 (in millions)</b>	
Leasing to private tenants	\$ 9.2
Leasing to government tenants	\$ 31.2
Sale of excess property	\$ 25.5
Rent from developmental property	\$ 20.7
<b>Total</b>	<b>\$ 86.6</b>

Source: USPS Comprehensive Statement of Postal Services, FY 2002.

Like most Federal entities with a strong community presence throughout the country, the Postal Service has a real estate portfolio that includes not only leading-edge facilities, but a growing number of older properties, often in a state of severe disrepair. In fact, the Postal Service reports that, as of October 2002, it had 115 facilities or land parcels that were vacant or underutilized.<sup>22</sup> These facilities have little, if any, value to the modern-day delivery of the nation's mail.

The Postal Service's challenges with real property are not unique. In January 2003, GAO placed the Federal government's real estate holdings on its "high-risk" list and reported that restoring and repairing deteriorating Federal buildings will cost tens of billions of dollars.<sup>23</sup>

As indicated earlier in this chapter, the Commission strongly believes that local communities should be given every opportunity to assume local ownership and control of excess properties, whether through their purchase or donation. This would ensure these facilities, even if deemed excess for *postal* purposes, continue to play a vital role in the communities they served for many years.

Currently, the Postal Service is permitted to "trade" excess real property with other *Federal* entities, through the U.S. government's purchasing and property management agency, the General Services Administration ("GSA"). Under this mechanism, the Postal Service notifies GSA when a property becomes surplus. While funds are not exchanged in these "transactions," when the Postal Service goes property hunting, it can acquire the unneeded facilities of other Federal agencies using the "credits" it received for its own donations to the surplus property pool.

Just as the Postal Service has taken advantage of its authority to transfer surplus property to other Federal agencies, it should now do the same with state, county, and local governments, as well as local not-for-profit organizations. The transactions should be encouraged when such a transfer can deliver a net public benefit.

Beyond the important issue of managing an aging real estate portfolio and retaining the community value of these facilities long after their value to the Postal Service has subsided, effective management of the institution's real estate portfolio remains a daunting task. Many other factors are due substantial consideration—for example,

### Determine the Best Use for Surplus Post Offices

*Where there is inadequate market demand for an excess post office, the Postal Service should be encouraged to transfer the facility—with or without reimbursement, as best serves the public interest—to state and local governments, as well as not-for-profit organizations.*

the appropriate balance of leased versus owned property. With the Postal Service's preferred borrowing costs through the U.S. Treasury and the fact that its real estate holdings are exempt from property taxes, the benefits of property ownership are often greater than standard analyses indicate. These and other complex, high-stakes

decisions regarding the maintenance, rehabilitation, disposition and acquisition of properties in local real estate markets across the country all combine to make management of the Postal Service's real estate portfolio a possible candidate for the Commission's recommendations to outsource critical support functions to expert, outside professionals who are 100% focused on that vital task.

Regardless of how the portfolio is managed, however, the Commission is encouraged to note that the Postal Service has recognized that effective real estate management is a prerequisite to operating a large, successful enterprise. As the single biggest asset category at the Postal Service, the Commission encourages the Board of Directors to take a more active role in ensuring its effective, strategic management in support of the institution's mission and goals. As an essential first step, the Commission recommends that the Postal Service obtain an independent appraisal of the current market value of its major real estate holdings.

### How Much Is It All Worth?

*The Postal Service should set as a priority obtaining an accurate current market value for its real estate assets and doing a detailed analysis of the appropriate balance between real estate it should **own** and properties it should **lease**. The Board also should be encouraged to include objectives relating to the active management of Postal Service real estate in future strategic plans, and should be authorized to outsource management of Postal Service real estate, if such an approach is most capable of maximizing the benefits and minimizing the costs of the institution's substantial real estate holdings.*

## Appropriate Financing of Security, Oversight Functions

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As the Postal Service engages in an end-to-end effort to reduce costs and improve efficiency and productivity, no aspect of the institution's operations should be above scrutiny. In reviewing the security and oversight functions of the Postal Service, the Commission has two recommendations consistent with the overall goal of this report to ensure the continued delivery of high-quality universal service at affordable rates.

*Taxpayers, Not Ratepayers, Should Finance Law Enforcement*

The United States Postal Inspection Service performs an essential role safeguarding the nation's mail and ensuring the postal system is not used for illegal purposes. In combating everything from drug trafficking to child pornography to credit card fraud, the Postal Inspection Service has a broad and important law enforcement function. It is the Commission's view that the fact that these crimes are committed through the mail should not make them the financial responsibility of ratepayers. The cost of most law enforcement functions are shared by all taxpayers. The vital law enforcement work of the Postal Inspection Service should be no different.

As one of the nation's oldest law enforcement entities, the Postal Inspection Service has provided safety, security and integrity to the mail system for more than two centuries. Since its establishment by Benjamin Franklin, Postal Inspectors have played a vital role in conducting investigations on fraud, waste, and abuse relating to the nation's postal services. The Postal Inspection Service enforces more than 200 Federal laws, ranging in purpose from protecting employees against workplace violence to cracking down on drug trafficking to exposing workers' compensation fraud to tracking down the culprits who steal people's mail.<sup>24</sup>

**'The Silent Service'**

*U.S. Postal Inspectors are a colorful part of the nation's law enforcement history. From trailing 19<sup>th</sup> century outlaw William Bonney (aka "Billy the Kid") to playing a key role in the joint task force that brought Ted Kaczynski (aka the "Unabomber") to justice, Postal Inspectors have long embodied the best of American law enforcement. Long before the FBI's "10 Most Wanted List," Inspectors tacked up posters of prominent mail robbers in post offices across the country with the famous phrase "wanted dead or alive."*

*Postal Inspectors' tenacity is well-known to criminals. In the late 1960s, a country store that also housed the community post office was robbed. When local police arrived, they noticed a chalk line separating the commercial and postal areas of the store. It was drawn by the robbers who left a note: "Inspectors, we did not cross this line." True to their word, not a single item of post office equipment was disturbed. Today, the Inspection Service makes about 12,000 arrests each year, including hundreds charged with exploiting children and 1,500 suspected drug traffickers and money launderers.<sup>25</sup>*



Source: USPS FY 2000 Annual Report.

In addition, the Postal Inspection Service has a number of investigatory responsibilities. Externally, they are responsible for looking into possibly fraudulent activity relating to mailings, postage, and meters; fraud against consumers, business, and government; crime prevention and security; mail theft; prohibited mailings (child exploitation, bombs and drugs); robberies and burglaries; assaults and threats; money orders, financial instruments, and postal property crimes. Within the Postal

Service, they also are charged with rooting out embezzlers of postal cash and money orders, workers' compensation fraud, health care fraud, drugs in the workplace, and mail theft.<sup>26</sup>

While the Postal Inspection Service used to provide an audit function, with the transfer of that responsibility to the Office of the Inspector General (discussed below), the Postal Inspection Service today is overwhelmingly a law enforcement entity. It employs some 3,875 professionals, including approximately 1,900 postal inspectors, who enjoy full Federal law enforcement authority, including the right to carry firearms, make arrests, execute search warrants and serve subpoenas.<sup>27</sup> The Postal Inspection Service also employs some 1,400 uniformed guards and 800 professional and technical employees.<sup>28</sup> Its annual budget is approximately \$464 million.

### Who Should Bear The Cost?

*The Commission recognizes that the Postal Inspection Service plays a vital law enforcement function. Only those activities of the Postal Inspection Service that directly support the safety and security of the nation's mail and postal systems should be assumed by the ratepayers. The cost of law enforcement operations that track broader crimes committed through the mail should be borne by taxpayers, generally.*

### *Taking a Closer Look at the Office of the Inspector General*

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In 1996, with an amendment to the Inspector General Act, Congress transferred the auditing and related investigative duties of the Postal Inspection Service to a newly created Office of the Inspector General (OIG). The Inspector General is currently appointed by the Board of Governors for a term of seven years. The Office has increased dramatically in size since its inception, growing from 223 employees in 1998 to 722 employees in 2002. Today, its annual budget is approximately \$111 million.

According to a 2002 GAO report, the Postal Service's OIG has the 5<sup>th</sup> largest budget of all inspectors general operating in the Federal Government, behind that of the Department of Health and Human Services, the Department of Defense, the Department of the Treasury's OIG for Tax Administration, and the Department of Housing and Urban Development.<sup>29</sup> The Postal Service's Office of Inspector General enjoys a budget larger than that of the inspector general for the Department of Agriculture, with its \$77 billion annual budget and \$100 billion loan and loan guarantee portfolio. Within this context of other leading Federal agencies, the Commission encourages the Board of Directors to carefully review the size and funding levels of the Postal Service's OIG, particularly in light of its explosive growth in recent years.

### **Taking a Closer Look at the Office of Inspector General**

*The Board of Directors should look closely at the appropriateness of the OIG's size and funding levels in comparison to other Federal agencies.*

## Conclusion

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The realignment and modernization of the Postal Service's network represents the single greatest opportunity the institution has today to take its service to the nation to a higher standard of excellence. Fortunately, the Postal Service has an extraordinary array of options in this arena, if it is supported in its efforts to take full advantage of them.

If the Postal Service is willing to reduce its size to reflect declining mail volumes, and do so strategically, it can emerge from this realignment a stronger institution and a better day-to-day servant of the nation's modern postal needs. By 1) utilizing the rightsizing and standardization strategies being deployed throughout corporate America; 2) pursuing its network rationalization initiative; 3) exploring new private-sector partnerships to do business better, stabilize and even grow key mail volumes and ease demands on its infrastructure; and 4) effectively managing its substantial real estate portfolio and procurement efforts, the Postal Service can craft an ambitious overhaul that truly has the potential to transform not only its operations, but the delivery of the nation's mail.

The Commission's recommendations in this regard aim to ensure this evolution takes place the right way: free from undue political interference, with maximum community involvement and with the end goal of high-quality universal service at affordable rates propelling every effort.

With this strategy in place, the support of the Postal Service's many constituencies will in no small part determine its success or failure. But among this group, one set will be absolutely pivotal to the success of the Postal Service's modernization and realignment—the men and women who make the daily delivery of the mail to virtually every American home and business possible—the more than 840,000 employees of the U.S. Postal Service (Exhibit 6-1).

## Chapter 5 Recommendations\*

- B-5. **Processing Facilities.** *A Postal Network Optimization Commission (P-NOC), modeled in part after the Defense Base Closure and Realignment Commission, should be created to make recommendations relating to the consolidation and rationalization of the Postal Service mail processing and distribution infrastructure. The P-NOC should be comprised of eight members appointed by the President with advice and consent of the Senate. Recommendations of the P-NOC, once submitted to Congress by the President, should become final, unless Congress disapproves them in their entirety within 45 days.*
- B-6. **Post Offices.** *Efforts already underway by the Postal Service to expand access to retail postal services at venues other than post offices, such as banks, grocery stores, and other convenient locations, should be supported. When the Postal Service determines that a “low-activity” post office is no longer necessary for the fulfillment of its universal service obligation, the Postal Service should make every effort to maximize the proceeds from the sale of that facility. If the Postal Service determines that there is no adequate market demand for the purchase of a “low-activity” post office, the Postal Service should be encouraged to work with state and local governments, as well as not-for-profit organizations, to determine the means of disposition most beneficial to the local community. Such disposition could include transfer to a state or local government or not-for-profit organization, with or without reimbursement, as best serves the public interest. Existing statutes limiting the Postal Service’s flexibility with regard to the closing and disposition of post offices should be repealed and similar provisions in annual appropriation acts should be avoided.*
- B-7. **Real Estate Asset Management.** *The Postal Service should be encouraged to include policy goals and objectives relating to the active management of Postal Service real estate in future strategic plans. As a first step, the Postal Service should obtain an independent appraisal of the current market values of its major real estate holdings. Further, the Postal Service should use its current statutory flexibility to dispose of real estate assets to strengthen its long-term financial position and provide benefits to the public in the form of moderated rate increases and improved products and services.*
- P-1. **Maximizing the Use of the Private Sector.** *Those Postal Service functions that can be performed better and at lower cost by the private sector should be outsourced to the private sector.*
- P-2. **Utilizing the Postal Service’s Core Strength: “The First Mile” and “The Last Mile.”** *The Postal Service should continue to explore opportunities to utilize its core strengths in the “first” and “last” mile of the mail delivery stream through the development of mutually beneficial partnerships with the private sector.*
- P-3. **Expanding Retail Access to Postal Products and Services.** *The Postal Service should develop additional private-sector partnerships to better serve the consumer and expand access to postal products and services beyond the traditional post office.*

- P-4. **Worksharing Discounts for Non-Competitive Products.** *The Postal Service should continue to look for opportunities to offer discounts for additional workshared products and to expand opportunities for small mailers to participate in them, particularly as new technologies are developed, that reflect lowest combined public-private sector costs. The new Postal Regulatory Board should be required to conduct an expedited, after-the-fact review of a new worksharing discount upon written complaint by a party that the discount exceeds the costs avoided by the Postal Service. A discount that exceeds the costs avoided by the Postal Service should not be permitted. In addition, the Postal Service should ensure that the expected savings from worksharing discounts are actually captured in the form of reduced costs.*
- P-5. **Negotiated Service Agreements for Non-Competitive Products.** *The Postal Service should be given greater flexibility to enter into negotiated service agreements for non-competitive products. Specifically, the Postal Service should be allowed to enter into agreements based on general criteria established by the new Postal Regulatory Board. The Postal Regulatory Board should conduct expedited, after-the-fact reviews of such agreements when a written complaint is filed.*
- P-6 **Procurement Reform.** *There is a significant opportunity to improve the Postal Service's "bottom-line" through revision of its procurement regulations and the adoption of commercial best practices. Therefore, the Postal Service should revise its purchasing regulations to maximize the flexibility given to it under current law and to reflect commercial best practices. Congress should strongly support Postal Service procurement reform in acknowledgment of its substantial benefit to all ratepayers.*
- T-1. **Automation Technology.** *The Postal Service should balance capital expenditures on new automation technology with consideration of outsourcing elements of the processing network. The Postal Service should neither acquire excess capacity that would only be used during peak periods nor undertake functions that the private sector could perform more effectively and at less cost than the Postal Service itself. Nonetheless, the Commission acknowledges the steps the Postal Service has taken to automate its system for processing single-piece letter mail and welcomes the progress made in the automation of the processing of flats and packages. The Postal Service should continue to develop an effective merging system that is responsive to customer needs and culminates in one bundle of mixed letters and flats for each delivery point.*
- T-2. **Processing Standardization.** *The Postal Service should study the problem of mail processing with the possible goal of redesign of the whole mail system, using the latest in 21<sup>st</sup> century technology systems. The Postal Service should examine every one of its "legacy systems" and question its purpose and whether it is needed. In addition, the mail processing redesign should include a standard or common footprint for each processing facility, with an identical level of technology and machinery in each. This would allow easy shifting of personnel to manage the mail flow more efficiently. This redesign study should be viewed as complementary to the Postal Service's current network rationalization initiative.*

\*See Appendix C for a complete list of Commission recommendations.

## Endnotes

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## Chapter 6: Aligning People with Progress: Building a 21<sup>st</sup> Century Postal Service Workforce

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### Introduction

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No matter how well-laid the plans for modernizing the nation's postal network, for these efforts to succeed in elevating postal operations to a new standard of excellence, they must more effectively utilize the Postal Service's most valuable assets—its employees. The ambitious plans outlined in this report provide the basis for sweeping changes in the way that the Postal Service meets its mission and pursues additional “break-through” improvements in productivity.

These changes will have a profound impact on the Postal Service as an institution. The level of success achieved by the Postal Service will hinge on its ability to successfully deploy and motivate a talented, capable, nimble workforce of a size appropriate to the future postal needs of the nation and to give its employees a personal stake in the success of the institution's ambitious goals.

The new Board of Directors and Postal Service management must assume responsibility for building and maintaining a world-class workforce in terms of service standards and efficiencies. Essential to this process is the ability of management and labor to work constructively together to determine the right size of the postal workforce and to ensure appropriate flexibilities in its deployment. This is *the* critical issue when it comes to controlling the future costs and capabilities of the workforce. Far more than individual benefits, the *size* of the workforce determines the *costs* of the workforce.



Source: USPS.

## Background

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The last major overhaul of the Postal Service in 1970 was caused, in part, by the demands of postal workers for adequate pay and the needs of management to have the cooperation of employees as the Postal Service embarked on a significant modernization to meet the country's changing postal needs. Today, the Postal Service again must significantly overhaul its operations to reflect changes in technology as well as shifts in how the nation uses the mail. Once more, successful adaptation hinges on the cooperation and support of the workforce that makes the regular, reliable and universal delivery of the nation's mail possible.

The challenge today, however, is far more complex. Postal workers enjoy special status within the Federal workforce. They are granted the right to negotiate wages, hours, and workplace conditions through collective bargaining. The 1970 Act was debated and enacted against the dramatic backdrop of the first major strike of Federal workers in U.S. history, involving approximately 152,000 postal employees in 671 locations. The strike was particularly paralyzing to business in New York City, the country's financial center. The strike was over shortly after it began, and in 1971, the U.S. government signed the first comprehensive Federal labor contract ever achieved through collective bargaining. The ongoing right to collective bargaining (absent the option to strike) was a key outcome, in addition to language in the 1970 Act requiring the Postal Service to offer compensation to employees that is comparable to the private sector.<sup>1</sup>

**Exhibit 6-1.**

	<b>Career</b>	<b>Non-Career</b>	<b>Totals</b>
American Postal Workers Union (APWU)	307,000	23,000	330,000
National Association of Letter Carriers (NALC)	231,000	5,000	236,000
National Rural Letter Carriers' Association (NRLCA)	61,000	56,000	117,000
National Postal Mail Handlers Union (NPMHU)	58,000	5,000	63,000
<b>subtotal</b>	<b>657,000</b>	<b>89,000</b>	<b>746,000</b>
Non-Bargaining	81,000	13,000	94,000
<b>subtotal</b>	<b>738,000</b>	<b>102,000</b>	<b>840,000</b>
Other Bargaining	3,000		3,000
<b>Total</b>	<b>741,000</b>	<b>102,000</b>	<b>843,000</b>

Information as of February 2003

Source: USPS.

Thirty years later, the overall result has been positive for the workforce. Postal clerks and city letter carriers, for example, have an average annual wage of more than \$42,500. Postal workers also enjoy the job security and ample benefits packages that make Federal employment attractive. According to the Postal Service, average annual *total* compensation, including both wages and benefits, for postal clerks and for city letter carriers is nearly \$60,000.

Given this “best of both worlds” package, it is entirely understandable why so many would be attracted to Postal Service employment. As of July 2001, the Postal Service had a backlog of some 400,000 job applicants and virtually no turnover.<sup>2</sup> In 2002, less than 1.5% of bargaining unit employees resigned before they retired, a “quit rate” that is lower than the rate for most private firms in America.



Source: USPS.

*The Postal Service Pays More than 76% of its Revenues to Employees*

The Postal Service employs approximately 843,000 people in both career and non-career positions (Exhibit 6-1), making its workforce more than twice the size of the United Parcel Service and more than four times the size of FedEx. All tallied, the Postal Service’s workforce as of 2002 was second in size only to Wal-Mart in the United States and was the fourth largest civilian workforce in the world (Exhibit 6-2). Approximately, one out of every three civilian employees of the U.S. government works for the Postal Service.<sup>3</sup> Given these facts, it comes as little surprise that more than \$3 out of every \$4 earned by the institution in Fiscal Year 2002—some \$51.5 billion of \$66.5 billion—went to pay the wages and benefits of its employees.<sup>4</sup>

Unlike their private-sector counterparts, however, total compensation costs are largely outside management’s control. Benefits are effectively set by statute. Costs for retiree health care and pension plans are skyrocketing for all employers, and the Postal Service has unfunded obligations for retiree health benefits of approximately \$48 billion.<sup>5</sup> Yet retiree health care and pension benefits are effectively “off the table” of collective bargaining.

**Exhibit 6-2.**

Among the Global 500			Among US Companies		
Rank	Company	Employees as of 2002	Rank	Company	Employees as of 2002
1	Wal-Mart Stores	1,300,000	1	Wal-Mart Stores	1,300,000
2	China National Petroleum	1,146,194	<b>2</b>	<b>US Postal Service</b>	<b>854,376</b>
3	Sinopec	917,000	3	McDonald’s	413,000
<b>4</b>	<b>US Postal Service</b>	<b>854,376</b>	4	United Parcel Service	360,000
5	Agricultural Bank of China	490,999	5	Ford Motor	350,321
6	Siemens	426,000	6	General Motors	350,000
7	McDonald’s	413,000	7	Intl. Business Machines	315,889
8	Ind. & Comm. Bank of China	405,000	8	General Electric	315,000
9	Carrefour	396,662	9	Target	306,000
10	Compass Group	392,352	10	Home Depot	300,000
11	China Telecomm	365,778	11	Kroger	289,000
12	DaimlerChrysler	365,571	12	Sears Roebuck	289,000
13	United Parcel Service	360,000	13	Tyco International	267,000
14	Ford Motor	350,321	14	Citigroup	252,500
15	General Motors	350,000	15	Verizon Communications	229,497

Source: Number of employees rankings by *Fortune Magazine*, April 14, 2003.

In addition, rigid work rules make it difficult to redeploy employees to new functions aligned with a changing network. To meet the needs of an optimized and efficient new postal network, substantial realignments of the workforce are necessary. Some employee crafts, such as last-mile mail carriers, should continue to grow with the nation. Other positions, most notably in processing and in middle management, are likely to decline as the Postal Service pursues new partnerships with the private sector and achieves greater productivity gains.

Most parties generally acknowledge the imperative to rightsize the Postal Service around the forward-looking needs and design of the nation's postal network. Fortunately, there is a potentially significant attrition opportunity on the horizon, with some 47% of current career employees eligible for regular retirement by 2010 (Exhibit 6-3). Already, the Postal Service has begun capitalizing on this opportunity to reduce its size. This trend could accelerate now that the Office of Personnel Management has granted the Postal Service permission to offer voluntary early retirement to large numbers of its bargaining-unit employees. The Postal Service must take full advantage of this attrition opportunity and exercise maximum discipline in its hiring practices in order to realign its workforce with minimal displacement of current workers.

**Exhibit 6-3.**

Employee Type	Current Number of Career Employees	2006		2010		2010 Cumulative	
		# Eligible	%	# Eligible	%	# Eligible	%
APWU	307,000	90,000	29.3%	60,000	19.5%	150,000	48.9%
NALC	231,000	52,000	22.5%	39,000	16.9%	91,000	39.4%
NRLCA	61,000	18,000	29.5%	14,000	23.0%	32,000	52.5%
NPMHU	58,000	16,000	27.6%	10,000	17.2%	26,000	44.8%
Non-Bargaining	81,000	29,000	35.8%	19,000	23.5%	48,000	59.3%
<b>Total</b>	<b>738,000</b>	<b>205,000</b>	<b>27.8%</b>	<b>142,000</b>	<b>19.2%</b>	<b>347,000</b>	<b>47.0%</b>

Source: USPS.

*Improve, Rather than Overhaul, Tools Available to Manage Workforce*

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The Commission firmly believes that postal workers should continue to have access to collective bargaining and total compensation comparable to, but not exceeding, the private sector. Both are consistent with an enterprise that operates in a business-like fashion and is charged with being self-financing. However, the Commission proposes several reforms aimed at achieving the following goals: delivering much-needed clarity to the definition of “comparability;” adjusting the collective bargaining model to encourage more timely resolution and greater fiscal restraint; reforming a broken system for dealing with employee-management disputes; and granting the Postal Service latitude to deal with the mounting costs of its workforce in innovative ways that neither add to the burden on ratepayers nor sacrifice the Postal Service’s commitment to compensating its employees at a level comparable to that of the private sector.

First and foremost, Postal Service management must repair its strained relationship with its employees, most prominently evidenced by the unusually high number of workforce grievances filed and appealed and the relatively frequent occurrence of contract negotiations being settled through protracted arbitration.

Second, management and employee unions must have a constructive mechanism to work together to bring expenses and revenues of the Postal Service into alignment. This includes allowing management greater flexibility in the deployment of the workforce as the nation’s postal network is realigned and redesigned over time. It also entails establishing an impartial mechanism for resolving deeply divisive debates about the possible existence of a total compensation premium for postal workers.

Third, the Commission believes that successful management of the workforce requires far more than fixing problems and controlling costs. Building an incentive-based culture up and down the ranks is key to elevating the Postal Service to a new standard of performance. To align personal and institutional goals, the Commission recommends the development of an objective, understandable pay-for-performance program that grants all employees, not just management, a meaningful stake in the success of the Postal Service.

Simply put, the Postal Service cannot deliver the service the nation needs and deserves if its managers and employees are not working together effectively. As such, the Postal Service must be given an array of tools to manage its workforce constructively in a period of fundamental change.

### Toward More Constructive Collective Bargaining

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As mentioned previously, postal workers enjoy a special status within the Federal government in light of their right to negotiate compensation and other basic working rights and conditions through collective bargaining. The Commission favors retaining this important tradition, but recommends several constructive reforms aimed at strengthening this vital process to improve the often adversarial relationship between management and employees.

In making its recommendations, however, the Commission wishes to clearly note that its collective bargaining proposals are *prospective*. They would not affect existing negotiated agreements. Nor would they impact the status of current Postal Service retirees. The Commission endorses the collective bargaining process. Its recommendations simply aim to make possible in the future a more effective and constructive engagement between Postal Service management and the men and women who handle, process, and deliver the nation's mail.

The unique status of the Postal Service—a government entity required to act in a businesslike manner—is readily apparent in the design of its collective bargaining process. On the one hand, if the Postal Service were a standard Federal agency, its wages and benefits would not be subject to negotiation. On the other hand, if it were a private corporation, it would operate under a collective bargaining model that would arm each side with the ultimate “big stick”—for employees, the right to strike; for the Postal Service, the right to lockout workers without a contract.

Given the essential nature of the service provided by postal workers, Congress expressly forbade these traditional bargaining weapons in the 1970 Act. Instead, the existing collective bargaining provisions provide two avenues for the parties to use in reaching an agreement—they can jointly agree on alternative negotiation procedures before an existing agreement expires, or follow the procedures outlined in statute. The statutory process allows a minimum of 225 days of negotiation, fact finding and arbitration. In recent years, the parties have consistently agreed to forego that process in favor of alternative procedures. The alternative process used by the parties typically involves a three-person arbitration board consisting of one arbitrator selected by management, one selected by the union, and a third “neutral” arbitrator selected by the other two. Because the parties often agree to go directly to arbitration, the fact-finding process is rarely used. One seasoned participant aptly likened this segment of the process to a “dead letter.”<sup>6</sup>

Under the alternative process generally used by the parties, the arbitration board is not limited to selecting a proposal submitted by one of the parties. Instead, the board has the freedom to fashion a compromise or to come up with a wholly new, binding approach. Further, because the alternative procedures generally do not include strict time requirements, the length of the proceedings are often extended far beyond the timeframes contemplated in the 1970 Act's collective bargaining provisions. In fact, the last three proceedings took between 13 months and 17 months to conclude.

Not only has the current process resulted in lengthy proceedings, the Postal Service also lags behind the private sector in its ability to negotiate contract settlements without resorting to arbitration. With respect to the Postal Service's largest union, nearly 1 in 3 contract agreements have required arbitration.<sup>7</sup> However, the testimonies of numerous collective bargaining experts persuasively make the case that the fault lies not with the parties, but with a process ill-suited to the unique context of the Postal Service.

At the heart of the problem is the inherently circular nature of the current collective bargaining model. Parties enter into negotiations, identify issues that can be agreed upon, and then work toward each other on the issues that divide them. At a certain point, absent the “big sticks,” parties sometimes conclude they have nothing to lose by going to arbitration. At that point, both sides revert to their original position and prepare to begin their arguments all over again for the arbitrators. In short, the current system provides few incentives for the parties to reach a negotiated settlement. Instead, it appears to leave difficult decisions to arbitrators, rather than the parties who have to live with the arbitrators' decisions.



Source: USPS.

At a time when the Postal Service needs to significantly control costs and realign its workforce, a process that fosters management-employee discord and deters timely and reasonable compromises is especially counterproductive. It produces a “chilling effect” not only on the collective bargaining process,

but also on the relationship between management and employees, and ultimately the service both are capable of delivering to customers.

The solution initially advocated by the Postal Service in its Transformation Plan would grant the Postal Service and its employees the same right to lockout and to strike, respectively, enjoyed by their private-sector counterparts. While adding the risk of such extreme actions into the mix certainly could stimulate dispute resolutions, the Postal Service has since, appropriately, reconsidered this recommendation recognizing its high price. Without question, a strike of potentially hundreds of thousands of postal workers would be unprecedented in scope and devastating in its impact on the economy. The nation simply cannot accept such a risk.

The Commission recommends a more constructive, middle-ground approach. In fact, in the primary weakness of the current model—its drawn-out pacing, litigious nature and multiple redundancies—lie the core ingredients of a better approach called “mediation and arbitration.” “Med-arb,” as it is known, is far better suited to ensure each stage of the labor-management dialogue *builds* on the progress to date, rather than permitting the parties to retrench to the hard-line positions from which they began their negotiations.

### Spotlight

*“Med-arb,” as it is known, is far better suited to ensure each stage of the labor-management dialogue builds on the progress to date, rather than permitting the parties to retrench to the hard-line positions from which they began their negotiations.*

Under a med-arb approach, the rarely used “fact-finding” phase would be replaced with an intensive and mandatory mediation stage that the Commission proposes to begin *immediately* after a contract expires without a new agreement in place. In this phase, a respected and experienced mediator—jointly selected by the parties from a list provided by the Director of the Federal Mediation and Conciliation Service (“FMCS”)—works with the parties to navigate any stalemates and forge an agreement, if possible. If not, the list of outstanding issues is narrowed, so the arbitration can focus on the key differences rather than reopen every debate. Also to keep the process advancing toward resolution, the Commission proposes that this mandatory mediation phase last no more than 30 days.

### *A New, Time-Sensitive Approach to Arbitration*

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If the process moves to arbitration, once again the progress to date is maintained. This is due to a core med-arb requirement—that the *mediator* serve on the *arbitration* panel, along with two other neutral arbitrators (each of whom would be selected by one of the parties from a list provided by the Director of FMCS). By carrying over the mediator, the progress gained in the negotiation and mediation phases is not lost, as it often is under the current model. All parties are focused *solely* on the outstanding issues identified in the mediation phase. The arbitrators also are aware of what tentative concessions both sides have offered in seeking to reach agreement. Therefore, there is little opportunity for either side to revert to original bargaining positions, open up old debates and force the entire process to start from scratch.

To further strengthen the momentum toward resolution, the Commission proposes that the arbitration stage last no more than 60 days and be broken up into several distinct phases. For the first 40 days, both sides should present their arguments to the arbitration panel and continue negotiating with each other. At the end of that period, each side should be required to produce *two* good-faith offers, share them with the other side, and try once more to negotiate a resolution.

If there still is no agreement, then the Commission proposes to escalate the stakes, asking each side to produce *one* “last best final offer” (“LBFO”). To further nudge the parties together, the Commission proposes that the arbitration panel be required to select one of the two *packages* and be permitted to fashion its own award only if *both* packages fail to honor the comparability standard set by the Postal Regulatory Board (discussed in the next section). The LBFO strategy is a technique used in negotiations with essential employees, such as police officers and firefighters, in numerous states.<sup>8</sup> It places extraordinary pressure on both sides to produce a reasonable, workable compromise that incorporates the core interests of both parties. It also places a high risk on insisting on one-sided demands (i.e. the likelihood the arbitrators will simply select the other negotiating party’s package).

#### Spotlight

*The LBFO strategy is a technique used in negotiations with essential employees, such as police officers and firefighters, in numerous states. It places extraordinary pressure on both sides to produce a reasonable, workable compromise that incorporates the core interests of both parties.*

The Commission proposes that the arbitration panel have only three days to settle on a tentative award. At that time, the Commission proposes a 10-day period, which offers the two parties one last chance to fashion their own final agreement. This reflects a central theme of the new model crafted by this Commission: At *every* stage, parties have the opportunity to forge their own agreement and preempt the arbitrators' award. The resulting cycle—repeatedly going back to the negotiating table with a more refined set of choices and pressed on by a strict timeline and the prospect of an LBFO award—keeps the pressure on the parties that have to *live* with the final outcome of the process to take care of business *themselves* and do so in a timely and mutually agreeable manner, rather than a lengthy and confrontational one.

***Making the Collective Bargaining Process Work Better***

*The 1970 Act should be amended to transition the Postal Service to a three-stage “mediation-arbitration” approach to collective bargaining that encourages both management and unions to work together toward reasonable, timely and good-faith resolutions.*

***Stage 1: Negotiated Settlement (90 days)***

*The current requirement that parties begin negotiations 90 days prior to the expiration of an existing agreement should be retained.*

***Stage 2: Mandatory Mediation (30 days)***

*In the absence of an agreement at the end of a contract period, parties move immediately to a 30-day mandatory mediation. This stage would replace the current fact-finding period. At this stage, parties can either forge a final resolution or narrow the range of issues to be addressed in arbitration.*

***Stage 3: Interest Arbitration (60 days)***

*If an impasse persists, a 60-day arbitration is conducted by a three-person panel of neutral arbitrators selected from a list provided by the Federal Mediation and Conciliation Service. To avoid “starting from scratch,” one arbitrator is the mediator. This stage would proceed as follows:*

**Hearing:** *Immediately after mediation, parties have 40 days to present arguments.*

**Last Best Final Offer:** *After the hearings, each party must submit two final offer packages. The parties then have seven days to continue negotiations. If an impasse remains, each party would submit a final offer, and the panel would have three days to select one or the other as its tentative award. Arbitrators cannot fashion their own award (unless both final offers fail to honor the Postal Regulatory Board’s comparability standard).*

**Final Negotiations:** *Following the tentative award, parties would have a 10-day period to negotiate a substitute agreement that would preempt the panel’s award.*

**Final Award:** *If no substitute settlement is reached, the panel’s tentative award becomes final.*

### *Comparability Must Cover Total Compensation*

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The most thorny issue in collective bargaining today is pay and benefit comparability. As mentioned earlier, Postal Service workers currently enjoy the best of both the public- and private-sector worlds—salaries akin to those offered by leading corporations, plus the substantial job security and benefits associated with Federal employment.

This notion of matching private-sector compensation is clearly endorsed in the 1970 Act, which directs compensation for Postal Service employees and officers to be “comparable to the rates and types of compensation paid in the private sector of the economy of the United States.” Yet the statute contradicts itself by excluding pensions from collective bargaining and effectively taking retiree health benefits off the table, as well, by requiring that they be maintained at the generous levels in place when the 1970 Act became law.

By demanding pay comparability yet effectively excluding sizable pension and health benefits from collective bargaining, the 1970 Act forces negotiators and arbitrators alike to focus almost exclusively on wages. The consequence has been a heated 30-year debate over the meaning of pay comparability, one that regularly antagonizes the collective bargaining process.

It is the Commission’s view that the benefits of comparability are undermined for all parties when significant segments of total compensation are rendered non-negotiable. For bargaining-unit employees, this places disproportionate downward pressure on wages, rather than across wages and benefits. For ratepayers, it is unfair to ask that they finance postal compensation above the generous provisions of the law (i.e. comparability to the private sector).

### Spotlight

*It is the Commission’s view that the benefits of comparability are undermined for all parties when significant segments of total compensation are rendered non-negotiable.*



Source: USPS.

*Compensation Premium Debate Requires Independent Resolution*

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While the Commission strongly supports total compensation comparability, it recommends that this commitment be appropriately and clearly measured by an *independent* entity—the Postal Regulatory Board—and used as a ceiling in collective bargaining. While the clear intent of the comparability standard is to ensure wages do not lag behind the private sector, expert witnesses made the case to the Commission that a *premium* may exist today.<sup>9</sup> Appearing to support these claims is the low turnover rate and the fact that new hires, on average, receive a 28.4% pay increase when they join the Postal Service.<sup>10</sup>

In the arena of benefits, the contrast is even more pronounced. While health care benefits are part of the collective bargaining process, employees have access to the full range of generous plans available to Federal employees. They also contribute only slightly more than half (16.5% of the total premium) of what private-sector workers contribute (about 31.5% of the total premium)<sup>11</sup> and of what other Federal workers pay (about 28% of the total premium) for health care coverage.

Retirement benefits are even more generous, rising with inflation (a rare provision among private plans). The Postal Service, like the Federal government overall, permits employees to retire as early as age 55 (under the Civil Service Retirement System, CSRS) and as early as age 57 (under the Federal Employee Retirement System, FERS) with a full pension. And, while fewer private companies today offer retiree health care benefits (and many more are shifting a greater percentage of the costs to recipients),<sup>12</sup> these benefits remain a mainstay at the Postal Service.

In sum, these benefits accounted for just under \$20 billion of the \$51.5 billion the Postal Service spent on its employees in Fiscal Year 2002—almost \$1 out of every \$3 the Postal Service spent in that fiscal year.<sup>13</sup> A lack of negotiating authority with respect to these costs would be intolerable to most private-sector companies. They should be brought within the collective bargaining process at the business-oriented Postal Service, as well.

**An Unambiguous Definition**

*The 1970 Act should be amended to include an unambiguous definition of “comparable pay” that clearly defines compensation as all wages and benefits. Specifically, the legislation should be amended to make clear that comparability should be achieved on a total compensation basis, including all fringe benefits.*

While the Commission received persuasive testimony supporting the existence of a compensation premium (and notes that a number of respected neutral arbitrators have acknowledged it),<sup>14</sup> the Commission also received information challenging the existence of such a premium.<sup>15</sup> As a result, the Commission believes it is inappropriate for itself, Congress or any interested party to settle this debate. Rather, the overriding public interest lies with entrusting this determination to an independent entity, the Postal Regulatory Board, to fairly settle the issue.

To assist the Postal Regulatory Board, the Commission recommends clarifying the meaning of the term “comparability” by revising 39 U.S.C. § 101(c). The Commission suggests a definition substantially similar to the following:

*As an employer, the Postal Service shall achieve and maintain compensation for its officers and employees comparable to the total rates and types of compensation paid in the private sector of the economy of the United States. The term “total rates and types of compensation” shall include wages, holidays, leave, insurance, pensions, medical and hospital benefits, the continuity and stability of employment and all other benefits received.*

This change would clarify that the Postal Service’s commitment to pay comparability with the private sector applies to an employee’s *total* compensation package.

In addition, the Commission recommends that the 1970 Act be amended to authorize the Postal Regulatory Board to determine the appropriate sector(s) in the private workforce to be used in calculating comparable compensation and to clarify the factors to be considered by the Board in making this calculation.

As envisioned by the Commission, 39 U.S.C. § 1003(a) would be revised to read as follows:

*It shall be the policy of the Postal Service to maintain total compensation and benefits for all officers and employees on a standard of comparability to the total compensation and benefits paid for comparable levels of work in the private sector of the economy as determined by the Postal Regulatory Board. Factors to be considered by the Postal Regulatory Board should include the economic history of the employer, present financial health and ability to pay, as well as anticipated future growth, productivity, and total labor costs.*

In making the determination of whether a compensation premium exists, the Postal Regulatory Board should be authorized to consult with the Secretary of Labor, the Secretary of the Treasury, the Director of the Office of Personnel Management, the Comptroller General of the United States, and other individuals and organizations that the Postal Regulatory Board deems necessary.

### Defining the Appropriate Private-Sector Comparison

*The 1970 Act should be further revised to direct the Postal Regulatory Board to define the appropriate private-sector comparison for employee compensation, factoring in the similarities between the Postal Service’s financial health and ability to pay, anticipated future growth, productivity and total labor costs and that of the other business(es) and/or sector(s), with which it is deemed comparable.*

The Commission believes that all individual components of total compensation should be subject to the collective bargaining process, as is the case in the private sector. This approach could require granting the Postal Service and its unions the flexibility to develop new plans separate and apart from existing Federal pension and health care programs. The Commission, however, is concerned about the potential impact of such a step on other Federal employees. Therefore, it recommends that the Postal Service work with the Department of the Treasury, the Office of Personnel Management, and others to determine the impact that creating separate Postal Service pension and health care plans would have on existing Federal systems and workers.

As a first step, the Commission recommends: (1) authorizing the Postal Service to negotiate FERS eligibility requirements and employee contributions; (2) authorizing the Postal Service to negotiate the eligibility and retiree contributions under the post-retirement health care component of the Federal Employee Health Benefit Program for future Postal Service retirees; and (3) repealing language in the 1970 Act that effectively freezes fringe benefits at levels in place when the Postal Reorganization Act became law on July 1, 1971.

### Spotlight

*By amending the 1970 Act to include a broader range of benefits in the collective bargaining process, negotiators and arbitrators will be better able to ensure private-sector comparability across most wage and benefits components.*

By excluding significant benefits from the collective bargaining process, the 1970 Act denies negotiators and arbitrators alike the ability to factor the entire wage/benefit package into the agreement. By amending the 1970 Act to include a broader range of benefits in the collective bargaining process, negotiators and arbitrators will be better able to ensure private-sector comparability across most wage and benefits components.

### ***Addressing the Protected Status of Represented Employees in the Comparability Analysis***

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The Commission's proposed definition of comparability includes the phrase "continuity and stability of employment" as a benefit to be considered in the computation of comparable total compensation. This language refers to protection against layoff, a benefit currently enjoyed by more than 580,000 Postal Service employees (Exhibit 6-4). Layoff protection is not guaranteed by the 1970 Act, but instead is negotiated by the Postal Service and its major unions as part of the collective bargaining process.

The "no layoffs or reduction in force" provisions (Article 6) in the current collective bargaining agreements date back almost 25 years and have been included in successive agreements. For three of the Postal Service unions, layoff protection covers all career employees who have been part of the Postal Service workforce on a full-time basis for at least six years. For the fourth union, layoff protection extends to every career employee regardless of his or her term of service.

**Exhibit 6-4.**

<b>Career Union Employees Protected by No-Layoff Guarantees</b>				
	<b>Total Members</b>	<b>Protected</b>	<b>Unprotected</b>	<b>% Protected</b>
APWU (Clerks)	304,334	293,797	10,537	<b>96%</b>
NPMU (Mail Handlers)	57,621	54,133	3,488	<b>94%</b>
NALC (City Carriers)	230,171	175,329	54,842	<b>76%</b>
NRLCA (Rural Carriers)	60,718	60,718	0	<b>100%</b>
<b>Total</b>	<b>652,844</b>	<b>583,977</b>	<b>68,867</b>	<b>89%</b>

*Information as of February 2003*

The Commission believes that existing protections against layoff will *not* impair the ability of the Postal Service to “rightsize” its workforce *in the near term*. The Commission also believes it is critical for Postal Service management to ensure that future collective bargaining agreements provide the necessary flexibility to manage the size and deployment of the Postal Service workforce.

The Commission, however, was divided on the appropriateness of no-layoff provisions in future agreements between the Postal Service and its represented workforce. In light of the potential of declining mail volumes, a majority of commissioners (6) believe that future Postal Service managers should have the flexibility to make necessary adjustments in the size of the workforce without the constraints imposed by these provisions. These commissioners note that protection against layoff is a benefit not available to other Federal employees, who are subject to Federal reduction-in-force requirements in the event there is no longer any work for them to perform. They also note that layoff protection is rare in the private sector today, as companies demand the flexibility to rightsize their workforces as market conditions warrant.

A majority of commissioners would therefore recommend that the 1970 Act be amended to require that *future* Postal Service employees (*i.e.*, employees hired by the Postal Service after a change in the law) be covered by the same reduction-in-force rules as other Federal employees and to specify that this requirement may not be varied through the collective bargaining process. Under this approach, Postal Service workers hired before the change in the law could continue to enjoy layoff protection negotiated on their behalf through the collective bargaining process.

A minority of commissioners (3) believe that a statutory prohibition against the negotiation of no-layoff provisions protecting future Postal Service workers would undermine the authority of the new Board of Directors and would unnecessarily intrude into the collective bargaining process. The minority notes that Postal Service management has the ability today, and will continue to have the ability, to seek the removal of these provisions in future negotiations with the major Postal Service unions.

The minority also believes that job security is a legitimate subject of collective bargaining. In their view, specific circumstances may arise in which offering job security or no-layoff arrangements would demonstrably be in the best interests of the Postal Service. In addition, the minority notes that taking layoff protection off the negotiating table through an overriding statutory prohibition is inconsistent with the Commission's approach to governance and its desire to expand the range of issues subject to collective bargaining between the Postal Service and its represented workforce.

### *Comparability Analysis Should Bind Labor Negotiations*

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Finally, the Commission believes that the 1970 Act should be amended to establish that the comparability standard determined by the Postal Regulatory Board creates a ceiling over the negotiation and arbitration process. This limitation should be imposed *immediately* on the compensation of employees hired after the comparability analysis is completed, and *gradually* for existing employees, in the event that the Postal Regulatory Board determines a total compensation premium exists. Specifically, the Commission suggests that 39 U.S.C. § 1207(c)(2) be revised to read:

*The arbitration board shall give the parties a full and fair hearing, including an opportunity to present evidence in support of their claims, and an opportunity to present their case in person, by counsel, or by other representative as they may elect. For existing employees, the arbitration board must consider the Postal Regulatory Board's calculation of the total compensation premium and consider the Postal Regulatory Board's deadline for eliminating the total compensation premium. For new employees, the arbitration board must apply the Postal Regulatory Board's calculation of total compensation as a cap on total compensation. Decisions of the arbitration board shall be conclusive and binding upon the parties. The arbitration board shall render its decision within 60 days after its appointment.*

In effect, this recommendation would create a two-tiered system aimed at applying the discipline of a comparability standard to the collective bargaining process without unduly disrupting the relationship between management and current employees. For new workers hired after the comparability determination is made, its findings will immediately serve as a ceiling on total compensation. However, for existing employees, *if* the Postal Regulatory Board determines a compensation premium exists, then it will calculate the extent of the premium and set a reasonable timeframe for the Postal Service and unions to eliminate the disparity.

Because it is not the Commission's intent to lower the real wages of existing employees, this timeframe should be long enough to permit achieving comparability over a period of years. However, to keep the process advancing, arbitrators should be required to consider the extent to which each proposal advances comparability in determining their award. In addition, the Postal Regulatory Board should be tasked with periodically reviewing both its initial determination and the Postal Service's progress in eliminating any premium. Beyond that, how the Postal Service and the unions meet this goal within the Postal Regulatory Board's timeframe shall remain flexible and be determined within the context of the collective bargaining process.

One inherent flaw in the current process, as it applies to the Postal Service, is the common knowledge among all parties that ratepayers can be asked to make up any deficit. This is hardly the case in the private sector, where management ultimately could plead for the parties' mutual interest in the enterprise's financial viability. Having the Postal Regulatory Board's comparability standard limit total compensation seeks to replicate this private-sector discipline.

### **Addressing Significant Retiree Benefit Obligations**

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Nearly half a million Americans today are retired postal workers. As a result, pension and retiree health benefits alone comprise \$6 billion of the annual \$12 billion the Postal Service pays out in fringe benefits.<sup>16</sup> As pension and health care costs skyrocket for all employers, the Postal Service is not alone in its need to manage this large liability effectively. Postal Service employees, too, have a stake in this effort. Particularly given the fact that more than 45% of the Postal Service's career workforce is within a decade of the minimum retirement age (Exhibit 6-3), involving these benefits in the collective bargaining process will ensure that the health care needs of future postal retirees are adequately addressed as the Postal Service works to control and manage this large category of expense.

*Postal Service Owes the Public Complete Transparency*

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The Postal Service must also address the substantial benefits obligations its legacy systems have already accrued. In this arena, the Postal Service has a “good news, bad news” situation. The good news is that recently enacted legislation reduced the Postal Service’s unfunded liability for CSRS pension benefits (those covering employees hired before 1984) from \$32.3 billion to \$5.8 billion.<sup>17</sup> The bad news, however, is that the Postal Service today continues to have an unfunded retiree health benefit obligation of about \$48 billion.<sup>18</sup>

**Accounting for Unfunded Retiree Health Care Obligations**

*The new Board of Directors should work with the Postal Service’s independent auditor to determine the most appropriate accounting treatment of the Postal Service’s unfunded retiree health benefit obligation in accordance with applicable accounting standards. In making this determination, the Board of Directors should consider the Postal Service’s role as a valued public institution. The Commission also recommends that the Board consider funding a reserve account to address these obligations to the extent that Postal Service finances permit.*

The difference in the fate of the two benefit funds is due to the fact that the pension obligation is funded as benefits are earned and recovered through rates, while the retiree health care obligation is funded on a “pay-as-you-go” basis that focuses on obligations *due* today rather than the larger figure of obligations *earned* by and owed to employees today. The Commission wishes to make clear that the Postal Service’s independent auditor has indicated that such an approach is in compliance with current applicable accounting standards governing the reporting of retiree health care costs. Putting aside these standards, however, the Commission believes that the Postal Service should strive for complete transparency. As a result, it strongly encourages the new Board of Directors to revisit this issue in terms of the

public’s “right to know” the fiscal health of its public institutions and to formally acknowledge the full extent of this sizable obligation in its financial statements. The Commission further suggests that, if the financial condition of the Postal Service improves, the Board of Directors consider funding a reserve account to begin paying down this obligation, so future ratepayers are not forced to pay for postal services delivered to the nation today.

### *Taxpayers, Not Ratepayers, Should Finance Military Pensions*

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With regard to the CSRS pension fund surplus, President Bush in April signed into law the Postal Civil Service Retirement System Funding Reform Act (Public Law 108-18), which lowered the Postal Service's annual contribution to fund its remaining liability. Because the old statutory funding formula required higher payments that would have eventually resulted in the Postal Service *overfunding* its CSRS obligations, the new formula will translate into about \$3 billion in available revenues in 2003, which are being used to pay down a sizable portion of the Postal Service's debt owed to the Department of the Treasury.

This legislation was a positive step. However, included in the law permitting the Postal Service to adjust its pension contributions was language requiring the Postal Service to fund the CSRS retirement benefits of its employees that were earned while serving in the U.S. military. The cumulative cost to the Postal Service of funding the military service component of its CSRS retirees' pension payments has been estimated by the GAO to be \$27.9 billion.<sup>19</sup>

As explained by the Office of Personnel Management ("OPM") during Congressional hearings on this legislation, it has been standard practice for all Federal agencies to cover the total actual pension costs of their retirees under FERS since its inception in 1984. OPM noted that contributions made by Federal agencies for their retirees under CSRS have always been handled differently, with many agency contributions (such as those made by the Postal Service) being calculated based on legislative mandates that are not linked to actual costs. OPM viewed the bill that was later enacted as P.L. 108-18 as an opportunity to make future Postal Service CSRS contributions incorporate all retirement liabilities associated with Postal Service retirees, as well as all payments and earnings. In OPM's view, this approach simply made Postal Service contributions for CSRS costs consistent with those it makes for costs under FERS.

The Commission understands the OPM position, but does not agree with the application of this approach to the Postal Service. While the approach may be standard practice for all Federal agencies under FERS, the Commission notes that P.L. 108-18 only applies this standard to the Postal Service. No other Federal agency is required to pay such costs for its retirees under CSRS. In the Commission's view, it is inappropriate to require the Postal Service, as a self-financing entity that is charged with

#### **Financing Military Pension Benefits: Whose Responsibility?**

*The portion of CSRS retirement benefits accrued by postal workers through service in the U.S. military should be financed by taxpayers, not ratepayers. Congress should return responsibility for these benefits to the Department of the Treasury which, until recently, paid these obligations through appropriations.*

operating as business, to fund costs that would not be borne by any private-sector corporation (costs associated with benefits earned while the retiree was employed by another employer). In addition, requiring Federal agencies financed through Congressional appropriations to cover the military retirement benefits of its employees still ultimately taps resources from the same appropriate revenue source—taxpayers. Requiring a self-financing Federal entity to follow suit is wholly different. It asks those who use the nation's postal system to subsidize the U.S. military every time they use the mail.

The Commission recommends repeal of this requirement. Fortunately, by directing the Postal Service, the Department of the Treasury, and OPM to submit proposals regarding the funding of military benefits of postal employees, P.L. 108-18 provides the basis for Congress to revisit the issue.

The Commission supports returning responsibility for this portion of retiree benefits to the Department of the Treasury, where it resided before the recent legislation, and where this liability can be financed through funds generated by taxpayers.

### **Building an Incentive-Based Culture of Excellence**

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With a stronger collective bargaining process in place that permits the Postal Service to address the entire compensation equation, it is equally important that Postal Service management acknowledge that employee morale is vital to the success of any service-oriented enterprise. This is especially true at such a defining moment for the Postal Service, when substantial productivity gains and significant realignment of the workforce are needed to ensure the institution's continued ability to fulfill its mission of universal service at affordable rates.

To address employee job satisfaction and motivate the workforce behind broad institutional goals, the Postal Service has some significant repair work to do in order to strengthen the management-employee relationship. Central to this effort is substantially reducing the backlog of employee grievances pending arbitration and getting at the root cause of the unusually high volume of complaints. After the repair work is done, the Postal Service needs to build a well-designed incentive compensation program that goes beyond the upper ranks of management and makes *all* employees meaningful participants in the Postal Service's success.

Last but not least, in light of its businesslike orientation, the Postal Service should be permitted to offer attractive and competitive salaries that can assist in recruiting and retaining top-level business leadership that is necessary to guide the Postal Service to a higher standard of excellence and value to the nation.

### *Reducing Grievances*

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Employee morale is an essential element of an incentive-based culture. It is undermined when employee-management relations are acrimonious. Unfortunately, the high number of “second step” grievances and the large backlog of grievances pending arbitration at the Postal Service today clearly indicate that the relationship between Postal Service management and workers is strained—to the detriment of employee morale, productivity and, ultimately, service to ratepayers. As cost containment and employee efficiency become pivotal to profitability, numerous service industries have worked with their unions to make dispute resolution more efficient and less contentious. The time has come to make this same progress in the Postal Service grievance process.

There is much ground to be gained. In 2002, 184,329 grievances filed by members of the Postal Service’s four major unions reached a “second step” appeal, and 106,834 were pending arbitration (Exhibit 6-4). Clearly something is wrong when a unionized workforce of 746,000 employees generates more than 184,000 “second step” grievances in a year’s time.

By comparison, with a workforce of nearly 102,000 employees, American Airlines launched a major Alternative Dispute Resolution initiative when its backlog of employee complaints reached a mere 800.<sup>20</sup> The Commission is confident in its assessment that not only does the current grievance dispute resolution process at the Postal Service lag behind the best practices of the business world; it likely brings up the rear.

While the Postal Service has separate dispute resolution agreements with each of its four major unions, the process starts generally with an employee, possibly accompanied by a union steward, discussing the dispute with the supervisor.<sup>21</sup> If a successful

process were in place, most grievances would be resolved at this stage, by the primary parties. More often than not, however, the grievance escalates through numerous time-consuming steps, ultimately ending with arbitration. Here, the adversarial relationship is quite apparent in both the significant number of grievances appealed and the significant backlog of complaints awaiting arbitration. In Fiscal Year 2002, 115,065 grievances advanced to “second step” appeal and 89,784 were “pending arbitration” at just one union, the American Postal Workers Union, adding up to two grievances for every three of their represented employees (Exhibit 6-5).

**Exhibit 6-5.**

**A Strained Relationship: “Second Step” Appeals and Pending Arbitration**

<b><i>APWU (American Postal Workers Union)</i></b>		
<b>Fiscal Year</b>	<b>2nd Step Grievance Appeal</b>	<b>Pending Arbitration</b>
FY1999	137,504	91,561
FY2000	116,247	65,035
FY2001	134,178	78,209
FY2002	115,065	89,784
FY2003*	56,839	83,745
<b><i>NALC (National Association of Letter Carriers)</i></b>		
<b>Fiscal Year</b>	<b>2nd Step Grievance Appeal</b>	<b>Pending Arbitration</b>
FY1999	46,372	17,734
FY2000	51,037	19,350
FY2001	48,659	15,513
FY2002	29,164	9,906
FY2003*	16,500	8,846
<b><i>NPMHU (National Postal Mail Handlers Union)</i></b>		
<b>Fiscal Year</b>	<b>2nd Step Grievance Appeal</b>	<b>Pending Arbitration</b>
FY1999	28,281	4,729
FY2000	30,109	5,528
FY2001	31,607	6,135
FY2002	33,533	7,122
FY2003*	17,288	7,602
<b><i>NRLCA (National Rural Letter Carriers' Association)</i></b>		
<b>Fiscal Year</b>	<b>2nd Step Grievance Appeal</b>	<b>Pending Arbitration</b>
FY1999	2,483	44
FY2000	3,412	56
FY2001	3,504	73
FY2002	6,567	22
FY2003*	2,855	155

Source: ADR Associates, LLC, Report to Commission (June 2003).

\*Data through April 7, 2003

The Commission notes the encouraging progress being made by the National Association of Letter Carriers. The union and the Postal Service recently completed the first totally restructured and streamlined grievance procedures for any postal union in 23 years. After only one year, its pilot phase resulted in 78% of grievances being resolved locally and a 65% decline in appeals. And, as of July 2003, the backlog of pending grievances was down 74% since 1998. The Commission believes that Postal Service managers should work aggressively to establish similar productive agreements and relationships with the other employee unions.

By resolving more disputes at the local level, reducing the number of steps involved before a case goes to arbitration and establishing a common understanding between the Postal Service and the union with regard to key contract provisions, the NALC process aims both to resolve individual grievances quickly and locally and also to foster awareness among all parties of what, precisely, the work rules and other contract stipulations are in order to prevent future disputes.

Given the success of these reforms, the Commission believes that a concerted effort to establish similar agreements with the other major postal unions should be a primary objective. The Commission suggests that the Postal Service establish pilot programs with the following attributes:

- Mandatory mediation at the local level;
- Use of neutral third parties as mediators; and
- Jointly developed training for both union and management representatives.

For such programs to be successful, it is imperative that the Postal Service give clear direction that settlement of problems and cooperative labor-management relations are a priority. Additionally, it must hold managers accountable for behavior that results in poor labor-management relations.

Any long-term reform of the dispute resolution process will require cooperation between the Postal Service and its unions. It will take time and effort, but the results, both in financial terms and in employee morale, will pay huge dividends to the institution and its ability to serve the nation. Satisfied employees are of far more value to the nation's postal endeavor than those in a contentious relationship with their employers. Addressing an unworkable grievance system and the climate that has created it is the first necessary step to establishing an incentive-based culture of excellence.

### **A Model Approach to Grievance Reform**

*Using the recent progress between the Postal Service and the NALC as a model, the Postal Service should work diligently with its other employee unions to institute similar procedures aimed at reducing both the time needed to process grievances and the number of grievances appealed to arbitration.*

*Pay-for-Performance Incentives*

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Performance-based compensation programs, designed correctly, are a valuable tool for aligning the goals of employees with an institution's mission-critical performance targets. With its large employee base, as well as its service and business orientations, the Postal Service is ideally positioned to reap the benefits of a well-designed and well-executed incentive compensation program. Toward that end, the Commission recommends that the Postal Service undertake a careful study of performance-based compensation, for both management *and* represented employees, and that it work with the unions and management associations to design and implement a pay-for-performance initiative that is meaningful to employees and capable of taking the Postal Service to a higher level of operational efficiency, productivity and quality.

While the Postal Service has attempted to implement performance-based compensation programs in the past, these efforts have often run into challenges. Two years ago, the Economic Value Added Variable Pay Program and related Merit Pay Program were terminated amid political criticism. On the merits, the six-year effort appears to have been effective in focusing management on preventing workplace injuries, increasing productivity, improving on-time delivery and even reducing by 5% compensation costs as a percentage of Postal Service operating expenses. The effort eliminated cost-of-living and other standard pay increases for its top 83,000 employees, requiring instead that each manager earn any pay increase through performance. While the program was attacked for handing out more than \$1 billion to Postal Service managers, it is worth noting that canceling automatic pay increases *saved* \$2.4 billion.

The initiative's shortcoming? It failed to involve the workforce as a whole. In fairness to the Postal Service, however, the notion of variable pay based on performance is frequently opposed by some union leaders. Earlier this year, the Postal Service began the National Performance Assessment, which relies on a balanced scorecard approach that links objective measures such as customer service, employee productivity and business productivity with compensation. While the focus again is on top managers, the Postal Service has plans to expand the program in 2004. The Commission urges union leadership to reconsider such initiatives and their ability to enhance the compensation of the represented workforce.

In a large organization in need of significant realignment, productivity gains and high-quality service, performance-based compensation can offer meaningful incentives to align the interests of workers with the specific performance goals of the institution as a whole. The Commission believes that developing and properly designing such a plan can serve as a powerful communications and motivational tool, helping employees understand how they can contribute to the organization's financial health and success—and be rewarded for their effort.

In crafting its program, the Commission recommends that the Postal Service emphasize the following “best practice” features: 1) effective alignment of strategic priorities with desired employee behavior; 2) a simple plan design; 3) clear communication of the plan to employees; 4) a credible and reliable measurement process; 5) proper integration of the plan with workplace processes and systems; and 6) reasonable assurances that the plan will pay for itself through improved productivity.<sup>22</sup>

The Commission also encourages the Postal Service and its unions to think broadly in terms of incentives. For example, employees represented by the National Rural Letter Carriers' Association today enjoy a very effective non-monetary incentive—an evaluated route process in which rural carriers are compensated for completing a set route, no matter how quickly and efficiently they get the job done.<sup>23</sup> This approach benefits both parties. It limits overtime costs to the Postal Service (the root cause of many carrier-related grievances), and it rewards productive workers, compensating them equally for performing their route in five hours, for example, as they would have been paid for eight hours of work. In other words, if they beat the “evaluated time” for their route, they are not penalized financially for doing so. The Postal Service should consider similar approaches with employees represented by its other unions.

If the Postal Service is to have the businesslike capacity to nimbly adapt to change, then the entire postal workforce should be eligible for some form of incentive compensation that gives them an additional financial stake in the success of the enterprise. The use of incentive compensation has proven a very effective tool in aligning workers with an institution's productivity, efficiency and service goals. With respect to the Postal Service, a positive, constructive, motivating compensation structure is critical to building a less confrontational and more cooperative employee-management culture, one that consistently strives for excellence. In short, by giving every employee a personal stake in the success of the Postal Service, that success becomes far more attainable.

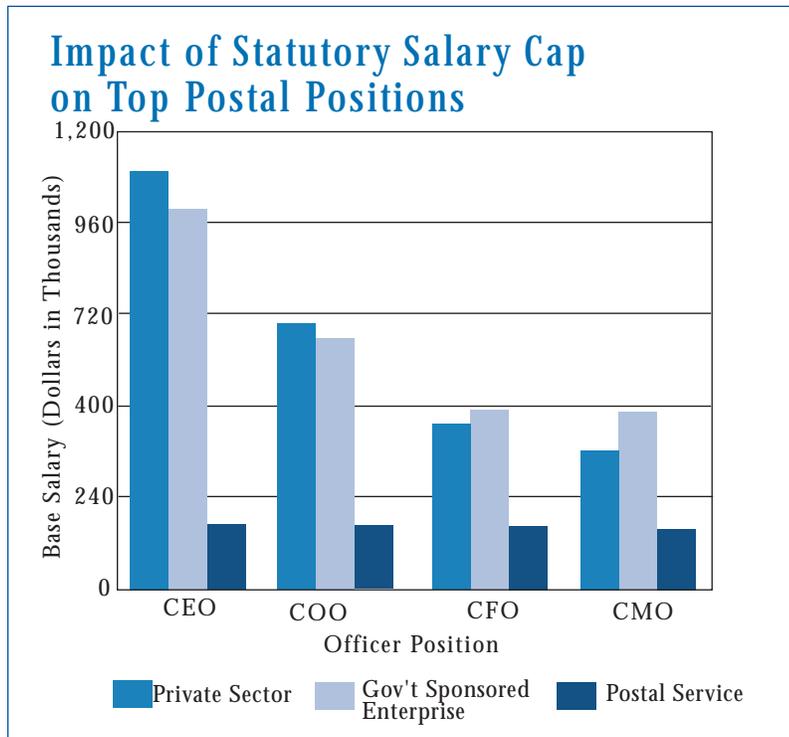
### Develop a Meaningful Pay-for-Performance System

*The Postal Service should carefully study and design a pay-for-performance compensation program that provides meaningful incentives to employees—both management and labor—to personally advance the productivity, efficiency and service quality goals of the Postal Service. The plan should be simply constructed, clearly communicated and able to self-finance through the delivery of significant efficiency and productivity gains.*

*Executive Compensation*

While the 1970 Act calls for pay comparability for both managers and represented employees, it also includes a salary cap. As a consequence, executive compensation is nowhere near that of corporate leaders running comparably large enterprises. While it is not feasible that Postal Service executive compensation rival its private-sector counter-

**Exhibit 6-6.**



Source: USPS Transformation Plan.

parts, it is the Commission's view that top managers' pay should move significantly in that direction, with the caveat that it be closely tied to key performance measures for the Postal Service overall.

As a consequence, the Commission recommends repeal of the Federal salary cap as it applies to the Postal Service (currently \$171,900) and that the Board of Directors be authorized to establish rates of pay for top Postal Service officers and employees that are competitive with the private sector. Many Federal entities requiring a capable, experienced CEO and other top officers to ensure the quality and continuity of operations already have such authority. These entities include the Tennessee Valley Authority, the Federal Reserve Board, the Public Company Accounting Oversight Board and the Federal Home Loan Banks.<sup>24</sup>

Without such a move, the result is a compression of salaries at the top, leaving little financial incentive for top employees to take on new levels of responsibility or to perform

at "break-through" levels. This cap also presents a significant recruiting and retention challenge for the top leadership posts.

When compared to wages paid for similar private-sector positions, and even other self-financing government enterprises, the Postal Service simply cannot compete in attracting and retaining key managers who are capable of lifting the enterprise to new levels of performance and service. The cap should be lifted and the Board should have the discretion to set compensation to attract and retain qualified individuals in key leadership posts.

As noted in Chapter 3, the Commission believes that executive pay must be tied directly to performance, and has recommended that the new Board establish a Compensation Committee that would develop a compensation system that delivers that result.

### Finding Private-Sector Efficiencies

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In addition to improving its unique collective bargaining process and building a more constructive management-employee climate, the Postal Service has a number of opportunities today to control labor costs and gain new efficiencies from its workforce through greater application of standard business practices. By making slight but meaningful adjustments in the Federal Employees' Compensation Act (FECA) to reflect the Postal Service's unique businesslike and self-financing role, the Postal Service can advance its goal of a leaner, more productive and less costly workforce, and emerge a stronger and more stable organization fully capable of continuing to play a vital role at the center of U.S. commerce and society.

### Attracting and Retaining Top Talent

*The Postal Service should be granted a Title 5 salary-cap exemption, permitting it to compensate top employees at a level that is competitive with the private sector. Total compensation, however, should be tied to performance and left to the discretion of the Board.*

### Rein in Workers' Compensation Liabilities

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The 1970 Act requires Postal Service employees—like all Federal employees—to be covered by FECA, which authorizes the Federal workers' compensation program. Under FECA, the Postal Service has maintained a broad and effective workers' compensation program and recent efforts have lowered injury rates considerably. Since Fiscal Year 2000, the Postal Service has linked management compensation to improved worker safety. During this period, the Postal Service has seen annual improvements in safety, as measured by the Occupational Safety and Health Administration's Injury Illness Frequency Rates. The Postal Service has also recently initiated an Ergonomic Strategic Partnership with OSHA, the American Postal Workers Union, and the National Postal Mail Handlers Union to reduce the number of musculoskeletal disorders, which account for more than 40% of workplace injuries and illnesses. The Commission applauds these efforts at making the Postal Service a safer workplace and urges the Postal Service to continue to make worker safety a top priority.

Unfortunately, the application of FECA to the Postal Service has led to some costly and unintended consequences, most notably a \$6.5 billion unfunded liability.<sup>25</sup> Unlike most workers' compensation plans governing the private sector, FECA imposes no waiting period before benefits begin. Employees with dependents are eligible for 75% of their pay, rather than the standard 66 2/3%. There is also no maximum dollar cap on FECA payments. As a result, particularly when employees are receiving the 75% benefit, they often do not opt to retire, staying permanently on the more generous workers' compensation rolls. Exhibit 6-7 illustrates the difference in take-home pay for an employee receiving a CSRS-based pension benefit versus the same employee receiving workers' compensation benefits.

**Exhibit 6-7.**

<b>Projected: Comparison of FECA Workers' Compensation Benefits and EAS-13 Employee Post-Tax "Take-Home" Pay</b>		
Year	CSRS Retirement Net Pay (56% of High 3+ taxable)	Workers' Compensation (75% of pre-injury salary plus COLAs - non-taxable)
2003	\$21,949	\$37,847
2004	\$22,547	\$38,982
2005	\$23,162	\$40,152
2006	\$23,796	\$41,356
2007	\$24,449	\$42,597
2008	\$25,112	\$43,875
2009	\$25,814	\$45,191
2010	\$26,528	\$46,547
2011	\$27,263	\$47,943
2012	\$28,020	\$49,381
<b>Total</b>	<b>\$248,640</b>	<b>\$433,871</b>

Source: USPS Transformation Plan.

The Commission believes that the Postal Service, given its unique businesslike charter, should be provided relief from those provisions of FECA that are creating costly unintended consequences. Specifically, the Commission recommends that the Postal Service be permitted to:

- Impose a three-day waiting period before benefits begin;
- Limit benefits to two-thirds of an employee's pay; and
- Transition workers' compensation recipients to the appropriate retirement program when they become eligible for retirement.

### **Reforming Workers' Compensation**

*Consistent with its self-financing mandate, the Postal Service should be permitted to provide workers' compensation benefits on a par with the private sector, most notably by limiting its FECA benefits to 66 2/3% of salary, imposing a three-day waiting period, and requiring beneficiaries to transition to the appropriate retirement program when they qualify for retirement.*

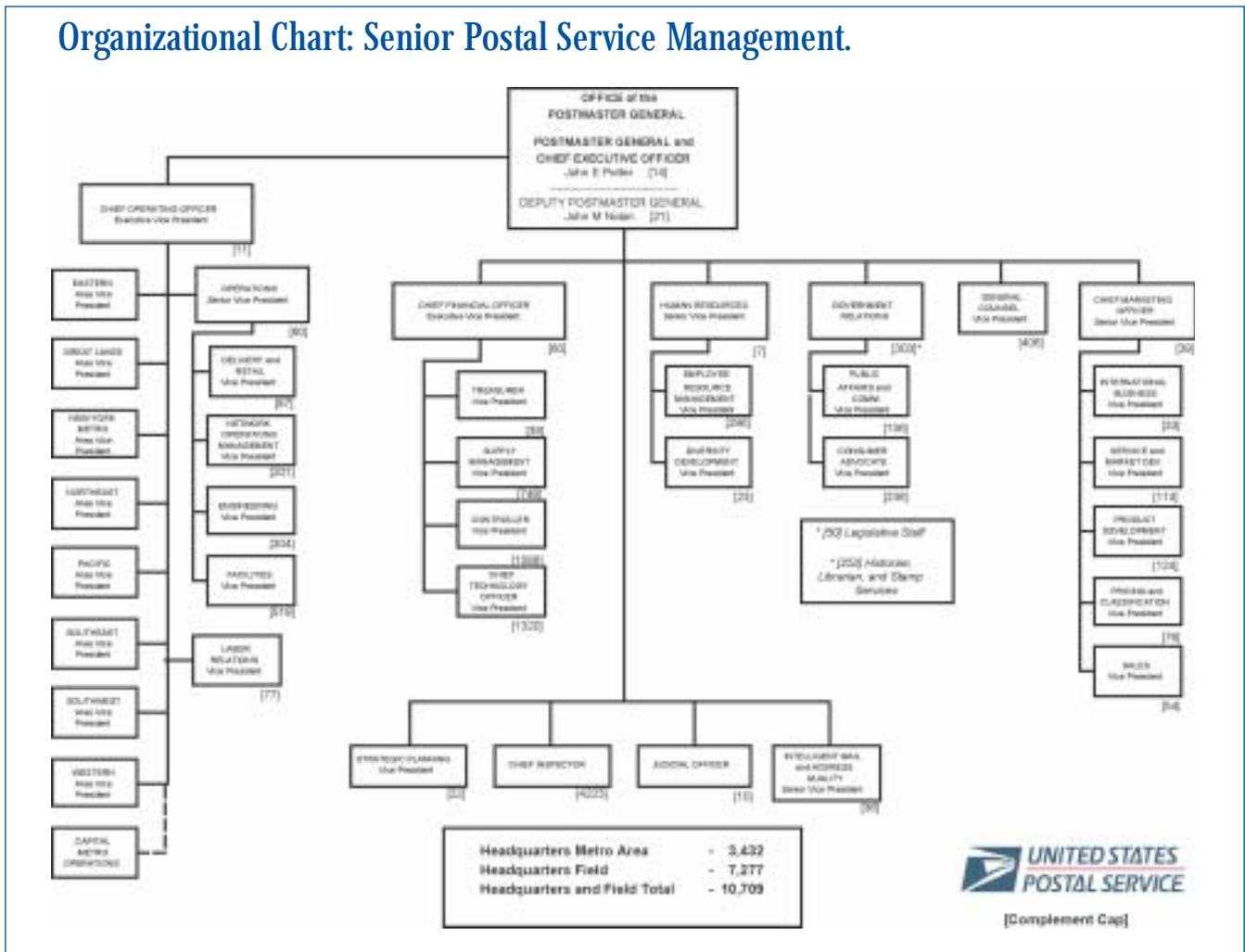
Similar measures are fairly standard practice in the private sector. They are aimed at controlling costs while providing adequate coverage to employees. Given the Postal Service's current \$6.5 billion unfunded workers' compensation liability and its businesslike, break-even mandate, taking actions similar to those that would be taken in the private sector seems appropriate.

*Management Ranks Need to be Thinned, Too*

Today, the Postal Service management follows a “command-and-control” approach with significant policy and operational decisions made at Headquarters, under the offices of the Postmaster General and the Chief Operating Officer. These decisions are then disseminated throughout the managerial hierarchy, including Area Vice Presidents, District Managers, Managers of Post Office Operations, and Postmasters (Exhibit 6-8).

While the Postal Service’s management structure is generally sound, there is always room for substantial improvement in an organization of the Postal Service’s size and nationwide reach. It is critical, for example, that communication of strategy and goals *not* get lost along the way from senior managers to represented employees. The Postal Service must also continually focus on removing layers of managerial bureau-

**Exhibit 6-8.**



Source: USPS Transformation Plan.

cracy with an eye toward simplicity and downward delegation. Removing layers of management and resting authority in lower level managers will free senior executives to focus on higher level strategy and goal-setting.

The Commission believes that the Postal Service's network rationalization effort, already underway, provides a unique opportunity for the Postal Service to examine and realign its management structure at the same time it is working to realign its physical infrastructure and represented workforce. The Commission encourages the Postal Service to use this opportunity to examine every management position and managerial layer to determine how it fits into the larger organization and whether it aids in the fulfillment of the Postal Service's overall mission. As part of the effort, the Postal Service should conduct a review of the entire management structure, size, and cost to determine whether each component is necessary and consistent with the best practices of the private sector and to require managers to justify their functions and the size of their respective staffs.

The Postal Service, for example, recently announced the consolidation of the administrative functions in five of its 85 districts, thereby reducing the total number of districts to 80.<sup>26</sup> Is further consolidation possible? Does every district need to be headed by a single executive? Does the Postal Service have the appropriate number of areas and districts? These are the questions that Postal Service management must continually ask itself as it seeks to remove bureaucratic redundancies.

The Commission also believes that the Postal Service would benefit from greater consistency and standardization throughout its management ranks. To optimize efficiency, promote transparency, and improve communication across the organization, it is important that each managerial role be clearly articulated and standardized. While flexibility is important to foster a healthy work environment, it is vital that functions and roles be identical regardless of geography. Much like represented employees moving between plants, a Manager of Post Office Operations in Boston, for instance, should be able to replace seamlessly a Manager of Post Office Operations in San Francisco.

Finally, as with its workforce in general, the Postal Service will see large numbers of its managerial employees become eligible for retirement within the next few years—fully 55% of officers and executives will be eligible in 2006 compared with 26% in 2002. While this provides an opportunity for the Postal Service to simplify its management structure and remove redundant positions and unnecessary layers, it also presents the risk that the Postal Service may lose key personnel. The Commission believes the development of a succession plan for key management positions throughout the organization must be an ongoing priority of the Board of Directors.

## Conclusion

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As valuable as the Postal Service is to the nation, its ability to deliver that value is only as great as the capability, motivation and satisfaction of the people who make the daily delivery of the mail to virtually every American home and business possible. Their desire to make the modernization of the nation's postal network a success, along with their willingness to make possible the Postal Service's ambitious goals to rein in costs while improving productivity and service, will in no small part determine the success or failure of the entire transformation endeavor and, ultimately, the fate of universal service at affordable rates.

A new collective bargaining process that brings management and employees together and places a premium on constructive and timely resolutions, more businesslike flexibility that permits the Postal Service to address mounting benefits liabilities, and a new commitment to making *all* employees vested in the enterprise—all these steps can help bring under control the extraordinary costs of the Postal Service's national employee base. This result can be achieved without turning to ratepayers or sacrificing the Postal Service's commitment to compensating its employees comparably to the private sector.

If the Postal Service proves capable of focusing its mission and purpose, its workforce must be no larger than necessary and committed to facing the realities of declining mail volumes and revenues. In this area, its strategy must be two-fold: minimizing the risk to taxpayers and ratepayers, and realigning the workforce to the realities of a leaner Postal Service without sacrificing service. A lean, motivated and strategically deployed workforce is essential to this equation.

Equally important is the potential of technology, even amid such a challenging transition, to propel the Postal Service to a new standard of excellence.

## Chapter 6 Recommendations\*

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*W-1. **Developing an Appropriately-Sized Workforce.** As the Postal Service works to meet the challenges of the 21<sup>st</sup> century, it must develop a world-class workforce appropriate to fulfilling its universal service obligation. Fortunately, the Postal Service will soon be presented with a unique attrition opportunity with some 47% of current career employees eligible for retirement by 2010. The Postal Service is urged to take full advantage of this attrition opportunity and to exercise maximum discipline in its hiring practices in order to rightsize and realign its workforce with minimal displacement.*

*W-2. **Collective Bargaining: Process Improvements.** The collective bargaining process should be retained. However, the collective bargaining process should be improved to create additional incentives for the parties to reach negotiated settlements, and, when the parties fail to reach a negotiated settlement, to ensure that arbitration awards are made within a reasonable period of time. In particular, the collective bargaining process should be as follows:*

- ***Basic process.** A negotiation process, beginning 90 days prior to the expiration of an existing agreement, followed by a 30-day mandatory mediation process and, if mediation fails, an immediate 60-day interest arbitration process.*
- ***Mandatory mediation and “Med-Arb.”** The 30-day mandatory mediation process would be conducted by a mediator who would become a member of the arbitration panel should mediation fail. The purpose of the mediation process would be to either reach a negotiated settlement or to narrow the range of issues to be submitted to interest arbitration.*
- ***Interest arbitration.** The 60-day interest arbitration process would be conducted by a three-person arbitration panel comprised of three neutral arbitrators, one having served as the mediator. The interest arbitration process would incorporate the Last Best Final Offer mechanism and a 10-day period during which the parties would have a final opportunity to reach a negotiated settlement prior to the arbitration panel’s final award.*

*W-3. **Collective Bargaining: New Subjects.** The Postal Service’s pension and post-retirement health care plans should be subject to collective bargaining – meaning that the Postal Service and its unions should have the flexibility to develop new plans that are separate and apart from existing Federal pension and retiree health care plans. However, because of concern about the uncertain impact such a change would have on the Federal system as a whole and on other Federal employees in*

*particular, the Postal Service should work with the Department of the Treasury, the Office of Personnel Management, and any other persons or entities deemed necessary to determine the impact separate Postal Service pension and retiree health care programs would have on the existing Federal systems. As a first step:*

- *The Postal Service should be authorized to negotiate Federal Employee Retirement System eligibility requirements and employee contributions;*
- *The Postal Service should be authorized to negotiate the eligibility and retiree contribution requirements for the post-retirement health care component of the Federal Employee Health Benefit Program, specifically for future Postal Service retirees; and*
- *The current statutory requirement that “[n]o variation, addition, or substitution with respect to fringe benefits shall result in a program of fringe benefits which on the whole is less favorable to the officers and employees than fringe benefits in effect on [July 1, 1971]” should be repealed.*

**W-4. Pay Comparability.** *The 1970 Act should be amended to clarify the meaning of the term comparability, and the new Postal Regulatory Board should be authorized to determine comparable total compensation for all Postal Service employees. In determining comparable total compensation, the Postal Regulatory Board should be authorized to determine the appropriate sector(s) of the private-sector workforce to be used as the basis of comparison. The comparability determination of the Postal Regulatory Board should be enforced as a cap on the total compensation of new employees. In addition, if the Postal Regulatory Board determines that a total compensation premium exists for current employees, it should be authorized to determine the appropriate period of time during which the premium must be eliminated, and to review periodically its initial determination and the Postal Service’s progress in eliminating the premium.*

**W-5. Pay-for-Performance.** *Performance-based compensation programs are effective tools that, when designed correctly, can be used to align the goals of management and labor and result in improved efficiency and service quality. The Postal Service should undertake a careful study of performance-based compensation programs for both management and represented employees, and it should work with the unions and management associations to design and implement a performance-based compensation program that is meaningful to Postal Service employees and assists the Postal Service in meeting its productivity and service quality goals.*

**W-6. Grievances.** *The current dispute resolution process must be revised if the Postal Service is to operate in accordance with the best practices of private-sector companies with highly unionized workforces. As a first step, the Postal Service should work diligently with its unions to implement best practice grievance procedures, including those recently implemented by the Postal Service and the National Association of Letter Carriers.*

*W-7. **Workers' Compensation Claims.** The Postal Service should be provided relief from the requirements of the Federal Employees' Compensation Act as follows:*

- The Postal Service should not be required to pay benefits until after the expiration of a three-day waiting period;*
- The Postal Service should be allowed to limit benefits to 2/3 of the maximum weekly rate; and*
- The Postal Service should be allowed to transition individuals receiving workers' compensation to the Postal Service's retirement plan at such time as the employee would have become eligible for retirement notwithstanding the injury giving rise to the workers' compensation benefits.*

*W-8. **Executive Compensation.** The current statutory salary cap should be repealed. Further, the Postal Service should be authorized to establish rates of pay for officers and employees at levels competitive with the private sector. Performance should be considered as a key component of senior executive pay.*

*W-9. **Management Structure.** The Postal Service should restructure its management to eliminate redundant positions and geographical divisions and to standardize and clarify job functions. The Postal Service should conduct a review of the entire management structure, size, and cost to determine whether each component is necessary and consistent with the best practices of the private sector, and it should require managers to justify their functions and the size of their staffs.*

*W-10. **Accounting for Retiree Health Care Obligations.** The Postal Service should review its current policy relating to the accounting treatment of retiree health care benefits, and work with its independent auditor to determine the most appropriate treatment of such costs in accordance with applicable accounting standards and in consideration of the Postal Service's need for complete transparency in the reporting of future liabilities. The Postal Service should consider funding a reserve account for unfunded retiree health care obligations to the extent that the its financial condition allows.*

*W-11. **Funding Military Service.** Responsibility for funding Civil Service Retirement System pension benefits relating to the military service of Postal Service retirees should be returned to the Department of the Treasury.*

\* See Appendix C for a complete list of Commission recommendations.

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# Chapter 7: Creating the Digital Postal Network: Linking Customers, Carriers, and Correspondence to the Future of the Mail

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## Introduction

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Although a more efficient and capable physical network and workforce will be critical for the Postal Service in the years ahead, these steps will not suffice to ensure the future of traditional mail services. The future of the mail will depend upon the ability of the Postal Service to develop a new fusion of traditional services and advanced information technologies, “a digital postal network.” Successfully realized, a digital postal network will enhance the value of the mail as a 21<sup>st</sup> century communications mode and improve virtually every aspect of the nation’s postal service, from efficiency and security to the range and quality of customer choices.

Technology can therefore give back some of what it takes away. While many of the challenges before the Postal Service are technological in nature, the net financial risks posed by technology can be significantly ameliorated if the Postal Service is able to take advantage of the *opportunities* that technology offers. Although the Commission firmly believes that the Postal Service should remain focused on delivery of physical mail, it also believes that the Postal Service should take full advantage of the Internet and other technological advances to perfect value-added services that will better serve the needs of its customers.

A central feature of the digital postal network of the future will be “Intelligent Mail.” Each piece of Intelligent Mail will carry a unique, machine-readable barcode (or other indicia) that will identify, at a minimum, the sender, the destination, and the class of mail. If successfully deployed, Intelligent Mail will allow the real-time tracking of individual mail pieces.

Ultimately, Intelligent Mail can serve a far broader purpose, functioning as the foundation of a truly digital network that links postal facilities, vehicles, partners and employees not only to each other, but also via the Internet to customers and to the individual mail pieces themselves. Through the deployment of a “universal language,” Intelligent Mail may also allow dynamic real-time routing and other sophisticated applications.

### Spotlight

*Ultimately, Intelligent Mail can serve a far broader purpose, functioning as the foundation of a truly digital network that links postal facilities, vehicles, partners and employees not only to each other, but also via the Internet to customers and to the individual mail pieces themselves.*



Source: USPS.

### How ‘Smart’ Can Hard Copy Get?

*...A customer checks what was delivered to her mailbox from her computer at work.*

*...A letter and a mail processing machine collaborate to correct an inaccurate address.*

*...Midway through its cross-country journey, a piece of mail “learns” that the recipient is on vacation and the mail piece is re-routed to a different vacation address.*

*...Parents send announcements of a child’s birth featuring stamps with the baby’s picture.*

*...The routes of postal workers and vehicles are organized without a single phone call—and reorganized in real-time when a vehicle breaks down.*

*...Whether a birthday card or a mission-critical business document, every sender and recipient of mail can check where the correspondence they care about is on its journey.*

*The technology to make possible each of these capabilities exists today. Experts predict that within five years, all kinds of everyday physical objects will grow “smarter,” capable of communicating key information about their whereabouts and disposition via wireless networks.<sup>1</sup> The Postal Service could lead this trend and deliver advances from security to efficiency to customer service that increase the value and, thus, the viability of the mail as a modern communications medium.*

Deploying such a system will require significant investment and a strategic focus that must be sustained over time. But if successfully executed, the Postal Service will reap the rewards of its most significant opportunity today to increase the value and security of the mail while reducing costs and improving overall performance.

## Background

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The postal business has always been one of information transportation. As such, throughout history, it has been challenged to adapt to new technologies, from the telegraph, to the telephone, to the fax machine, to the rise of private overnight delivery services and, now, the Internet. However, no prior advance has offered so much opportunity to improve the value of the mail, to root out excess capacity and costs and—increasingly important—to enhance the security of the nation’s postal system.

The Postal Service is well aware that technology presents many opportunities. Beginning in the 1980’s, the Service began automating what was, at the time, an almost entirely manual and mechanized postal undertaking. Given that the Postal Service spends more than 75 cents of every dollar it earns on personnel-related costs, automation continues to hold significant cost-saving potential.

Technology that enhances coordination among the workforce also can play a key role. However, fundamental gaps exist in the infrastructure available in the field today, most notably the fact that most mail carriers have no means of communicating with one another or with their local post offices while out on their routes.

Customers, too, feel the lack of a leading edge in information services. While some advanced capabilities are available on a limited basis, such as mail tracking, they tend to be either focused exclusively on larger mailers or they are costly and rudimentary. Current barcode technology is limited in its reach and is not completely standardized, inhibiting the efficiency gains of a uniform approach. Current on-line postage printing options are cumbersome, expensive, and confusing to many individual users. True mail tracking is only available to larger mailers. So even where progress is occurring, too often the full benefits do not reach smaller businesses and individual customers. Making this truth even more troublesome is the fact that many of these same services are standard for all customers of private postal carriers, placing the Postal Service significantly behind the curve of not only technology adoption, but also of consumer expectations.

Much of this can be attributed to a rather piecemeal approach the Postal Service has taken in the past to the acquisition and deployment of technology. Over the years, the Postal Service has incorporated technology

### Spotlight

*While some advanced capabilities are available on a limited basis, such as mail tracking, they tend to be either focused exclusively on larger mailers or they are costly and rudimentary. Without a sustained focus, the Postal Service will not keep pace with emerging customer requirements.*



Source: USPS.

into its processes as it becomes available and affordable. However, these steps often lacked an over-arching strategy designed to maximize the benefits of these investments and enable rapid response to shifting market demands, mail volumes, and other current events. To begin addressing these issues in a more coordinated fashion, the Postal Service recently established the Mailing Technology Strategy Council to rationalize the Postal Service's approach to its technology acquisitions and deployment.

### Intelligent Mail: Thinking Outside the Envelope

Traditional mail has little chance of competing directly with e-mail and its virtually free and instantaneous delivery. Rather than take a stand for traditional mail, the Postal Service should apply new technologies to make it smarter.

What *are* the advantages of physical mail? The nation is comfortable and familiar with it. Unlike e-mail, the internal contents of each piece can be readily categorized (e.g. bills, advertising, and personal letters are easy to differentiate). Because of its physical nature, it can be conveniently moved around. For example, magazines can go into the living room and mortgage bills can go to a home office for payment, then be transferred to a tax file. Why do people like e-mail? It's free. It's fast. It's versatile. And, it is the mirror opposite of the physical mail stream: Large documents, photographs, bills, and correspondence all can fly back and forth without a single piece of paper changing hands.

Physical mail and e-mail each has its own separate and distinct value. However, by not viewing them as an "either/or" choice, but by applying the sophistication of the electronic world to the physical mail, the Postal Service can develop a new postal proposition for the 21<sup>st</sup> century. Once it does, it should work aggressively to make its advantages readily available to all customers.

Intelligent Mail, at its heart, is a powerful hybrid, applying leading-edge information technology to the delivery of paper correspondence. Mail has long carried information inside, but by encoding basic information *outside* the envelope, a whole new range of

services can be made available to make mail a more attractive and valuable option to consumers. By thinking “outside the envelope,” the Postal Service will be able to:

- Enhance the services it makes available to consumers;
- Improve mail security by enhancing traceability;
- Transform its website into a valued destination far more convenient to customers (and less costly to the Postal Service) than a post office visit; and
- Potentially save billions of dollars annually through enhanced logistics management.

Information such as sender identification, geographic origin, and mail class can be applied at the initial stage of the mail process and can be encoded by “smart” stamp vending machines or postage meters at the time of purchase. Then, once specific outgoing mail pieces enter the postal network, additional data (chiefly the destination and the date of processing the “postmark”) could be added to the barcode by smart processing technology, making Intelligent Mail not only feasible, but highly unobtrusive, even for individual customers.

### *Intelligent Mail’s Security Applications Should be Aggressively Pursued*

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The information-rich barcode that is the foundation of Intelligent Mail also has the potential to improve significantly the security of the nation’s mail stream, particularly if the Postal Service fully explores whether it is feasible to require every piece of mail to include sender identification, in order to better assure its traceability in the event of foul play. The events of September 11, 2001, and the subsequent anthrax attacks that exploited the nation’s mail system have raised significant concerns relating to the vulnerability of the nation’s relatively open postal network. In the weeks following the attacks, delivery of the mail slowed substantially, affecting all aspects of American life—from commerce to Congress. In addition to the many steps already taken by the Postal Service, the Commission believes that sender identification on all mail could further enhance the security and speed of the nation’s mail service.

Requiring all mail to identify its sender would likely have a negligible impact on most users of the Postal Service who readily identify themselves when they send mail and would consider such a requirement a relatively modest concession to ensure their safety

and that of the men and women who deliver the nation’s mail. The greatest inconvenience, most certainly, would be to those who use the mail system for unlawful purposes, since such a move would hand law enforcement a powerful new tool to identify and prevent such abuse.

The Commission recommends that the Postal Service, in coordination with the Department of Homeland Security, study the development of sender-identification requirements for all mail. Issues of privacy should, of course, be noted and balanced with the value of enhanced safety. As a part of the study, the Postal Service should additionally explore the potential of technology to transition stamp purchasing equipment (e.g. vending machines, cash machines, self-service kiosks, post office counter sales, the Postal Service website, and postage meters) from the provision of general stamps to “personalized stamps” that automatically embed sender identification.

**All Customers Should Be Able To Track Their Mail**

Of course, the barcodes that can easily contain basic sender identification also have numerous commercial applications, as well, pointing to the possibility of new revenue streams for the Postal Service and an enhanced ability to meet and even exceed rising customer expectations.

One of the most telling conclusions reached by the independent customer survey performed for the Commission was the fact that the top demand was not cheaper stamps or shorter lines at the post office, but the ability to know where specific mail items are in their journey.<sup>2</sup>

Tracking is a standard service delivered by private carriers. While the Postal Service does currently offer some tracking services, it lags far behind consumer expectations and the capabilities of technology. Currently, for example, the Postal Service will estimate, but not guarantee, a delivery date for any type of mail.

**Exhibit 7-1. – What the Future Could Look Like**

 <b>Track Shipments - Detailed Results</b>				
Tracking number:	XXXXXXXXXX		Delivered to:	Recipient
Signed for by:	J. Waite		Delivery location:	Pawtucket RI
Ship date:	Jun 24		Service type:	First-Class letter
Delivery date:	Jun 25			
Time:	10:00 am			
	Jun 24, 2015	10:00 am	Accepted at Origin	Brockton, MA
		4:30 pm	In-Processing	Boston, MA
		7:00 pm	Originating Processing Completed	Boston, MA
	Jun 25, 2015	1:00 am	Destination Processing Begun	Providence, RI
		4:00 am	Sorted to local Post Office	Providence, RI
		11:00 am	Delivered and Signed by J. Waite	Pawtucket, RI

Should individual customers require more complete information about their mail, tracking is available only at a very rudimentary level and only when customers pay for premium services, such as Priority Mail. As a result, if customers want to track a standard letter, rather than paying the current 37-cent price of a First-Class stamp, they must pay more than 10 times that amount to send the letter via Priority Mail, *and* they must pay an additional 45 cents for delivery confirmation. Even then, customers are notified only when the letter is placed in a recipient's mailbox. There is no option to track its journey.

More conventional tracking services are available to a limited class of large users through systems designed for commercial vendors. The Postal Service, however, considers these systems too expensive for broader use. The Commission believes that mail tracking is essential to enhancing the modern-day value of the mail. It also believes that, by embracing intelligent mail and smarter postal processing technologies, mail tracking can be made feasible for all postal customers. The Commission thus recommends that the Postal Service deploy mail tracking technology in a timely and comprehensive manner, making it available to all users at an affordable price. If it deems such an approach infeasible, then the Postal Service should be directed to explore partnerships with private postal carriers for developing tracking services and an "intelligent" postal environment.



*Automated Package Processing System*

Source: USPS.

## Toward a 21<sup>st</sup> Century Postal Network



*Delivery Bar Code Sorter*

Source: USPS.

Once individual mail pieces are made intelligent and communicative, they require a means of conveying their information to relevant machines, information systems and people. This is why the creation of one overarching Postal Service technology acquisition and deployment strategy is so essential. By settling on a standard barcode, by adopting smart technologies that allow this code to convey its information throughout the postal network, and by securely linking these communications to customers via the Internet, the Postal Service can build a truly digital 21<sup>st</sup> century network with many attractive new features and others we are only beginning to imagine.

### *Speaking the Same Language*

The first step in building a robust, interconnected and information-rich network is to adopt one official “language” that all the related pieces, machines and people can “speak.” To accomplish this task, the Commission recommends that the Postal Service continue to study the development of a single universal barcode designed for *all* mail pieces. This code could contain, at a minimum, sender identification, class of service,

meter ID (i.e. where the stamp was printed) and delivery destination (added to the barcode during initial processing by the Postal Service). The Commission also recommends that the Postal Service study upgrading its stamp vending and printing equipment to make possible a national requirement that all postage carry this universal barcode—laying the groundwork for a truly intelligent mail system that can fulfill the many security, efficiency, and commercial functions described in this chapter.



*Automated Flat Sorting Machine*

Source: USPS.

Such a requirement would render each piece of mail unique and able to communicate basic information about itself. Increasing the intelligence of each mail piece and adopting a universal barcode will enable many capabilities beyond mail tracking. Encouraging private partners to adopt the same system, for example, could create seamless public-private partnerships, enabling a far more efficient “hand off”

of mail from worksharing partners to the Postal Service. Also, the more widely Intelligent Mail is capable of communicating its information to other elements of the postal network, the less likely it is to get lost or wind up at an outdated address—no small matter considering such mail costs the Postal Service \$2 *billion* a year to try and resolve.<sup>3</sup>

In addition to making each mail piece unique, the Commission recommends the Postal Service accelerate its efforts at marking and ensuring an information-based link between individual mail pieces and the *containers* they move in—whether a tray, palette, or transport vehicle. Allowing a “smart” container to know what it is carrying further allows for the real-time pinpointing of individual mail pieces, despite the extraordinary volumes the Postal Service handles on a daily basis. The intelligent container will also make a dynamic network possible.

### *Encouraging “Dialogue:” Dynamic Mail Routing*

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Once mail and postal processes are communicating effectively with one another, the potential to produce significant efficiency gains is extraordinary. Regional ebbs and flows in mail volume can be adjusted by re-routing mail to less busy facilities to ensure its more rapid processing. Weather conditions or vehicle breakdowns can be adjusted for in real time to keep the mail moving.

Beyond improvements to the physical networks (discussed in Chapter 5), a robust information technology network can link these fixed facilities with the vast mobile transportation network of the Postal Service, producing efficiency not merely on a facility-by-facility basis but *throughout* the postal network.



Source: USPS.

In its Transformation Plan, the Postal Service outlined strategies to achieve this result through its Surface Air Management System (SAMS), which would provide transportation assignments to specific surface and air mail routes. SAMS also would make possible the allocation of capacity by various mail classes and the on-line tracking of manifests. The Commission commends the Postal Service for this effort and urges the rapid deployment of SAMS.

However, the Commission believes that the Postal Service should be more aggressive in this area, building for itself one of the most sophisticated and capable public-private transportation networks in the world. To even begin in this direction, every vehicle must be linked to the real-time insights of the Postal Service logistics nerve center. Beyond Intelligent Mail and smart processing technologies, this will require investments in global positioning systems (GPS) and the universal provision of onboard computing capabilities.

Here again, the Postal Service is significantly behind delivery companies who regularly read a package's barcode from hand-held devices that immediately communicate to their networks the item's successful delivery. In contrast, the vast majority of letter carriers and local post offices have no capacity to communicate in real time. While the Postal Service has distributed a device to some letter carriers that allows them to monitor the consistency of delivery time, the information collected is not processed until the end of the workday, so there is no real-time opportunity to adjust to weather, mechanical, or other unique challenges facing the mail delivery in that location on that day.

A much enhanced local communications ability, with integrated GPS and Intelligent Mail functionalities, would allow, for example, efficient re-routing of delivery vehicles to

compensate for peaks in demand, traffic or weather conditions, and vehicle breakdowns. For example, management would know if a carrier had completed delivery on his or her route and could be redirected to provide assistance on a route where the carrier's vehicle had broken down. The Commission recommends that the Postal Service put in place a system capable of tracking every vehicle on its route and allowing each to communicate in real time with appropriate fixed facilities.

### Leading the Nation Toward Energy Independence

*As a long-time innovator in transportation technology, the Postal Service already has a fleet of more than 30,000 alternative fuel vehicles. In addition, the Postal Service is examining new technologies such as hybrid electric vehicles, which if proven cost effective in use, may also be introduced. The Commission applauds these efforts and strongly encourages the Postal Service to continue this tradition of innovation by introducing hydrogen fuel cell vehicles and hybrids into its fleet. By using environmentally-friendly and fuel-efficient vehicles, the Postal Service can continue and expand its efforts to help the nation create a transportation network that stresses energy independence and environmental progress.*

### *Connecting It All to the Consumer: The 24x7 In-Home Post Office*

By integrating Intelligent Mail, sender identification, global positioning, and other readily available technologies and allowing real-time communication between postal transportation vehicles, local post offices, robust Internet systems, and the mail itself, the Postal Service would be capable of providing unprecedented information to consumers. With this capability will come profound pressure to truly place an always open, full-service post office in every American home and business via the Internet. Without question, the Postal Service should rise to the occasion, enhancing both the simplicity and the sophistication of its website to the point where it is virtually interchangeable with a local post office.

Specifically, the Commission recommends that the Postal Service expand the array of postal products and services available on its website ([www.usps.com](http://www.usps.com)). That would include, for example, all Postal Service forms, registered mail, certified mail, and return receipts. In addition, a number of new postal services should be made available, such as real-time mail tracking. Other relatively new features should be made more user-friendly. Current PC postage systems, for example, remain inconvenient and confusing to the individual user. These processes should be replaced by a more straightforward approach that is so convenient and inexpensive that anyone can buy stamps on-line.

Users, of course, should be able to print out “personalized” stamps, encoded with their sender identification information and other basic information, aimed at enhancing security, improving the efficiency of the postal network, and permitting mail tracking. The website, however, can also allow a far wider array of customer-pleasing “personalized” stamp services. For example, individuals could have the option to print a stamp with a family photo or a small business could print stamps with the company logo. This is a prime example of adding to the value of both personal and business correspondence. Personalized stamps will enable commercial mailers to use their mail pieces as advertising media and will enable individual customers to tailor their own stamps as they please.

“Personalized” stamps should be easily printable on standard commercial paper, directly on envelopes, or on adhesive labels. This may require some minor advances in technology, both in personal and business printers, as well as Postal Service and contractor barcode readers. The Commission is confident, however, that the market would respond to such a shift in the nation’s mail system. The Commission also believes that the Postal Service should charge a premium for personalized stamp services.

#### A “Personalized” Stamp



Source:  ESCHER GROUP™

The Commission recognizes that not all Americans have ready access to the Internet and a printer and others will be uncomfortable making this transition. Therefore, in addition to the website, stamp vending and printing machines—whether at a post office, a self-service kiosk, or in a contract facility—should be similarly equipped, so purchasing a personalized stamp is as convenient as purchasing a general stamp today (and, eventually, far more so with the planned expansion of retail points of access).

## The Need for Expert, Strategic Guidance

Without question, the Postal Service faces significant risk if it does not embrace the opportunities of information technology. However, given the substantial size of the investments contemplated and the rapidly changing nature of information technology,

in addition to the risk of doing *nothing*, there also exists a sizable risk of doing the *wrong* “something.” This could, for example, include investing billions of dollars in systems that are not compatible, that quickly are rendered obsolete, or simply are not best suited to the unique operations of the Postal Service.

Making technology work for the Postal Service by deploying it in an integrated and nimble fashion so it can adapt quickly to changes in those demands is no small order. Because of the size and complexity of the network envisioned, the Commission believes that the Postal Service must evaluate, acquire, and deploy technology in a far more structured and coordinated fashion. Developing this strategy and ensuring its successful execution will require the efforts of a team of experts devoted to the success of this vital endeavor. Already, the Postal Service has created the Mail Technology Strategy Council to provide candid, independent assessments of technology trends. With representatives from leading organizations

### Missile Mail: Ready, Aim...Fire?

*The Postal Service has a colorful and often proud history of not shying away from leading-edge innovation. It embraced railroads, automobiles, and airplanes in their infancy, seeing their vast forward-looking potential to speed the delivery of the nation's mail. In its bold ambition, however, it has occasionally overshot the mark.*

*The day? June 8, 1959. The location? At sea, aboard a surfaced Navy submarine. The event? As explained by the postal official on hand, “before man reaches the moon, mail will be delivered within hours from New York to California, to Britain, to India or Australia by guided missiles.” With those lofty words, the U.S.S. Barbero fired away, launching a guided missile carrying 3,000 letters from its crew*

*at the Naval Auxiliary Air Station in Mayport, Florida. It was perhaps the briefest experiment in postal innovation, but it also exemplifies the pioneering spirit of the Postal Service in seeking new ways to speed the delivery of mail.<sup>4</sup>*



Source: USPS.

in the mailing industry, including senior officials from the Postal Service, industry, and academia, the Council explores key technology issues, particularly Intelligent Mail.

The Commission believes the Council should be expanded as an independent body, reporting directly to the Postmaster General, and should be empowered to provide more than just trend assessments. The Council should include postal engineers, scientists, employees and major mailers and should meet on a regular basis. It should have the power to monitor technologies for their effects on the mail system and for their return on investment. The Council should produce an annual report assessing advances in technology. Most importantly, it should be the key advisory body for establishing a coherent Postal Service technology strategy.

As is apparent in the recommendations of this chapter, information technology investments can only achieve their full potential and value if implemented together, in an integrated fashion, as part of one seamless technology strategy, and as a key incorporated element of the Postal Service's overall business plan.

In performing its duties, the Commission suggests that the Council include in its deliberations two key lines of questioning. First, *what* should the Postal Service be doing? Is it burdening itself by taking on tasks that are not self-supporting and are non-essential? Is it missing out on revenue opportunities by conceding promising areas? Does it have untapped assets that could be released through specific technologies? Second, *how* should the Postal Service do its work? Are existing technologies being applied as efficiently as possible? Is there a coherent plan for the acquisition of new technologies? Can costs be cut through integration of currently distinct systems? In what areas would the Postal Service be best-served by outsourcing technological systems, or pursuing development of mailing industry advancements in cooperation with private-sector entities?

Because a technology strategy is only effective until a new development renders it obsolete, two key elements of its ongoing success are vigilance for the next big shift in capability or market demand and the technological wisdom to respond to it appropriately. This vigilance requires the hard science of exploring what new capabilities are available and when their potential savings justify the acquisition cost, as well as the softer science of what customers want from the Postal Service. To aid this latter effort, the Commission suggests that the Council should not only develop its own ideas for improving the mail system, but accept them from all sources, including the individual Postal Service customer.

## Conclusion

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Technologies exist today that have the ability to capture information through high-speed scanning, to store and forward the data through high-capacity computers, and to present the information to interested parties through the Postal Service website. This would allow for the creation of a national digital postal network that links the physical network of the Postal Service with customers, partners and the correspondence itself. The potential efficiency gains and value-added benefits of such a system are great. As such, creation of this network should be aggressively and strategically pursued. While the technology necessary to make this vision a reality will likely require significant investment, the Commission is confident that the resulting efficiency and revenue gains, as well as service improvements, will offer a substantial return on investment to the Postal Service and its customers.

While the Commission commends the Postal Service's technology-related work to date, it urges a far more ambitious and strategic effort in the future. This will require unifying good ideas and efforts into one coherent, integrated strategy, capable of delivering both near-term gains in efficiency and productivity as well as the enduring flexibility necessary to adapt to an ever-changing technological environment. Also, of key importance, the Postal Service's technology investments should continue in the proudest tradition of the enterprise, ensuring that the benefits made possible by these advances are accessible to *all* postal customers.

Despite the challenges posed by electronic diversion of mail volumes, the Postal Service's future success lies not in *resisting* technological change, but in embracing it. With a proactive, strategic and visionary approach, it has every opportunity today to enhance the value of the mail in the modern context and to deliver to the nation a capable, sophisticated and leading-edge 21<sup>st</sup> century Postal Service.

## Chapter 7 Recommendations\*

- T-3. **Intelligent Mail.** *The ability of the Postal Service to track individual pieces of mail can improve internal efficiency and satisfy postal customers that mail is delivered to the right location and on time. Technology to achieve this goal exists today and is now being used by some of the competitors of the Postal Service. The Postal Service should work to put mail tracking technology in place on a timely and more comprehensive basis, so that it is available to all users, large and small, at an affordable price.*
- T-4. **The Transportation Network.** *The Postal Service should integrate its facility automation efforts with its transportation network by using Intelligent Mail technology, GPS, and onboard computer technology. The Postal Service should put in place a cost-effective system capable of tracking every vehicle on its route and allowing each vehicle to communicate in real time, either by voice or electronic communication, with appropriate fixed facilities.*
- T-5. **Improved Postal Service Website ([www.usps.com](http://www.usps.com)) and Personalized Stamps.** *Postal services available at post offices should also be generally available on the Postal Service website and at Postal Service kiosks and contract stations at reasonable prices for all postal customers, from the individual to the large mailer. The Postal Service should develop and produce “personalized” stamps and make them available through appropriate sources, beginning with the Postal Service website. These stamps should be offered to postal customers at a reasonable premium.*
- T-6. **Security.** *The events of 9/11 and the Postal Service anthrax incidents have increased the need to ensure security in the mail system. A more secure system could be built using sender identified mail. The Postal Service, in coordination with the Department of Homeland Security, should explore the use of sender identification for every piece of mail, commercial and retail.*
- T-7. **Evaluation, Acquisition and Deployment of Technology.** *The Postal Service recently created the new Mailing Technology Strategy Council to provide assessments of technology trends. The Council should be strengthened to be an independent advisory body empowered to do more than provide assessments. The Council should not only originate ideas for improving the mail system, but should accept them from all sources, including the individual Postal Service user. It should study, evaluate and recommend to the Postmaster General technologies that could be used to upgrade the mail system. Postal Service management should provide an annual report to the Board of Directors on the work of the Mailing Technology Strategy Council.*

\* See Appendix C for a complete list of Commission recommendations.

### *Connecting It All to the Consumer: The 24x7 In-Home Post Office*

By integrating Intelligent Mail, sender identification, global positioning, and other readily available technologies and allowing real-time communication between postal transportation vehicles, local post offices, robust Internet systems, and the mail itself, the Postal Service would be capable of providing unprecedented information to consumers. With this capability will come profound pressure to truly place an always open, full-service post office in every American home and business via the Internet. Without question, the Postal Service should rise to the occasion, enhancing both the simplicity and the sophistication of its website to the point where it is virtually interchangeable with a local post office.

Specifically, the Commission recommends that the Postal Service expand the array of postal products and services available on its website ([www.usps.com](http://www.usps.com)). That would include, for example, all Postal Service forms, registered mail, certified mail, and return receipts. In addition, a number of new postal services should be made available, such as real-time mail tracking. Other relatively new features should be made more user-friendly. Current PC postage systems, for example, remain inconvenient and confusing to the individual user. These processes should be replaced by a more straightforward approach that is so convenient and inexpensive that anyone can buy stamps on-line.

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#### A “Personalized” Stamp



Source:  ESCHER GROUP™

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# Conclusion

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From the aging and increasingly outmoded nature of the postal network to the rising diversion of correspondence to electronic alternatives, the Postal Service faces significant challenges today. However, these challenges present their own solutions, as well as significant new opportunities for the Postal Service. By modernizing an outmoded postal network and combating technology's threats with its many opportunities, the Postal Service can ensure not only its own continued *viability*, but its relevance and value to the nation in the 21<sup>st</sup> century.

Coupled with the efforts already underway at the Postal Service, it is the Commission's view that the reforms proposed in this report can address the financial and technological challenges at hand and produce a stronger and more capable Postal Service. However, one significant challenge remains: The willingness of all parties—from customers to Congress, postal workers to private-sector partners—to support a fundamental overhaul of a vital American institution.

Some changes will be easy to embrace. Customers, for example, will see their postal service enhanced. The public benefit of billions of dollars in annual efficiency savings is self-evident. The vast expansion of retail access to postal services will be a great convenience. Private-sector companies also will see more opportunities to engage in partnerships with the Postal Service in the delivery of the nation's mail.

Other changes, however, will require extraordinary commitment to the ultimate public benefits of Postal Service modernization. Members of Congress, for example, will be asked to permit the rationalization of a 1950s-era postal network, including the closure of surplus postal facilities in the communities they represent. Postal employees, too, will plainly see one ultimate outcome of an ambitious modernization: A Postal Service that over time requires far fewer postal workers to deliver the nation's mail.

Rather than undermine the case for reform, it is the Commission's hope that these legitimate concerns will help guide its successful and constructive execution. The Commission, for example, took great pains to ensure a key leadership role for Congress in the postal facilities realignment process and to suggest a process giving local communities the opportunity to help determine the disposition of "low-activity" post offices.

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The Commission is equally aware of the central role that postal employees will play in the success or failure of this modernization effort. In recent years, the nation has been keenly reminded of the extraordinary service these men and women deliver to the nation every day. For this reason, this report focuses significant attention on ensuring Postal Service employees receive compensation comparable to the private sector, creating a more positive workplace climate, ensuring that the Postal Service workforce has the best tools with which to do its job, and establishing financial incentives for contributing to the efficiency, productivity, and service of the institution. Given the significant attrition opportunity on the horizon, the Commission also wishes to note that it is hopeful that the rightsizing of the Postal Service workforce can occur over time through a voluntary process.

Only with the leadership of Congress, the day-to-day commitment of postal employees, and the support of customers and partners can Postal Service modernization succeed. As a result, the fate of the Postal Service will not ultimately be determined by external, insurmountable threats, but by the actions, support, and commitment of the American people, their representatives in Congress, and the men and women of the Postal Service.

Having devoted nearly eight months to studying the extent of the Postal Service's fiscal dilemma and the trends shaping its future, the Commission urges speed and conviction in support of Postal Service modernization. Without question, an aggressive approach is needed to limit the mounting financial exposure of American taxpayers. But, more importantly, these reforms are essential to upholding the nation's commitment to *affordable* and *universal* postal services.

Yes, the nation's mailing habits are changing significantly. Many individuals and businesses depend on the nation's mail system far less today. Others continue to rely on the Postal Service to handle their correspondence in just the same way they have for decades. What the long-term future of correspondence ultimately will be in the Information Age is anyone's guess. Far more certain, however, is the continued importance of affordable universal postal service today and for the *foreseeable* future. Its value remains unequivocal, and its continued provision endures as a defining commitment of this country to each of its citizens.

It has been this Commission's honor to help shape the future of the mail and the vital American institution that for more than 225 years has ensured its delivery. We are indebted to the members of Congress, Postal Service leaders and employees, customers, partners, and numerous experts whose ideas and assistance have helped inform this report, and through it, we hope, a bright future for the Postal Service as it continues to serve our country.

# Appendix A: Executive Order 13278

76671

Federal Register

Vol. 67, No. 240

Friday, December 13, 2002

## Presidential Documents

Title 3—

Executive Order 13278 of December 11, 2002

The President

President's Commission on the United States Postal Service

By the authority vested in me as President by the Constitution and the laws of the United States of America, and to ensure the efficient operation of the United States Postal Service while minimizing the financial exposure of the American taxpayers, it is hereby ordered as follows:

**Section 1. *Establishment.*** There is established the President's Commission on the United States Postal Service (Commission).

**Sec. 2. *Membership.*** Commission shall be composed of nine members appointed by the President. The President shall designate two members of the Commission to serve as Co-Chairs.

**Sec. 3. *Mission.*** (a) The mission of the Commission shall be to examine the state of the United States Postal Service, and to prepare and submit to the President a report articulating a proposed vision for the future of the United States Postal Service and recommending the legislative and administrative reforms needed to ensure the viability of postal services.

(b) In fulfilling its mission, the Commission shall consider the following issues and such other issues relating to the Postal Service as the Commission determines appropriate:

(i) the role of the Postal Service in the 21st century and beyond;

(ii) the flexibility that the Postal Service should have to change prices, control costs, and adjust service in response to financial, competitive, or market pressures;

(iii) the rigidities in cost or service that limit the efficiency of the postal system;

(iv) the ability of the Postal Service, over the long term, to maintain universal mail delivery at affordable rates and cover its unfunded liabilities with minimum exposure to the American taxpayers;

(v) the extent to which postal monopoly restrictions continue to advance the public interest under evolving market conditions, and the extent to which the Postal Service competes with private sector services; and

(vi) the most appropriate governance and oversight structure for the Postal Service.

**Sec. 4. *Administration.*** (a) The Department of the Treasury or any organizational entity subject to the direction of the Secretary of the Treasury shall, to the extent permitted by law, provide administrative support and funding for the Commission. The Commission is established within the Department of the Treasury for administrative purposes only.

(b) Members of the Commission shall serve without any compensation for their work on the Commission. Members appointed from among private citizens of the United States, however, while engaged in the work of the Commission, may be allowed travel expenses, including per diem in lieu of subsistence, as authorized by law for persons serving intermittently in Government service (5 U.S.C. 5701–5707), to the extent funds are available.

(c) The Commission shall have a staff headed by an Executive Director.

(d) The Commission, with the concurrence of the Secretary of the Treasury, may establish subcommittees, consisting of Commission members, as appropriate, to aid in its work.

76672 Federal Register/Vol. 67, No. 240/Friday, December 13, 2002/Presidential Documents

(e) Consistent with such guidance as the President or, on the President's behalf, the Secretary of the Treasury, may provide, the Commission shall exchange information with and obtain advice from Members of Congress; Federal, State, local, and tribal officials; commercial, nonprofit, and residential users of the United States Postal Service; and others, as appropriate, including through public hearings.

(f) Insofar as the Federal Advisory Committee Act, as amended, may apply to the Commission, any functions of the President under that Act, except for those in section 6 of that Act, shall be performed by the Secretary of the Treasury, in accordance with the guidelines that have been issued by the Administrator of General Services.

(g) Nothing in this order shall be construed to impair or otherwise affect the functions of the Director of the Office of Management and Budget relating to budget, administrative, or legislative proposals.

**Sec. 5. Report.** The Commission shall submit its report, consistent with its mission set forth in section 3 of this order, to the President, through the Secretary of the Treasury, not later than July 31, 2003.

**Sec. 6. General Provisions.** (a) This order is intended only to improve the internal management of the Federal Government and it is not intended to, and does not create, any right or benefit, substantive or procedural, enforceable at law or in equity by a party against the United States, its departments, agencies, instrumentalities or entities, its officers or employees, or any other person.

(b) The Commission shall terminate 30 days after submitting its report and in no event later than August 30, 2003.



THE WHITE HOUSE,  
December 11, 2002.

[FR Doc. 02-31624  
Filed 12-12-02; 8:45 am]  
Billing code 3195-01-P

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## Appendix B. The Work of the Commission: Structure and Process

On December 11, 2002, President Bush established the President's Commission on the United States Postal Service through Executive Order 13278. President Bush designated James A. Johnson, Vice-Chair of Perseus, L.L.C., and Harry J. Pearce, Chairman of Hughes Electronics Corporation, as the Commission's Co-Chairs. President Bush also appointed the following individuals as Commission members:

- Dionel E. Aviles, President, Aviles Engineering Corporation
- Don V. Cogman, Chairman, CC Investments
- Carolyn L. Gallagher, former President and Chief Executive Officer, Texwood Furniture
- Richard C. Levin, President, Yale University
- Norman I. Seabrook, President, New York City Correction Officers' Benevolent Association
- Robert S. Walker, Chairman and Chief Executive Officer, Wexler & Walker Public Policy Associates
- Joseph R. Wright, President and Chief Executive Officer, PanAmSat

In addition, Dennis Shea was appointed as the Commission's Executive Director.

The Commission has operated as an advisory committee governed by the Federal Advisory Committee Act ("FACA") and its implementing regulations. Roger Kodat, Deputy Assistant Secretary of Treasury for Government Financial Policy, served as the Commission's "Designated Federal Official" to ensure compliance with FACA.

### The Commission Website

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The Commission is grateful for the assistance provided by the Department of the Treasury in establishing and managing an official Commission website. The website, located at <http://www.treas.gov/offices/domestic-finance/usps>, has been an invaluable tool in enabling the Commission to communicate with the public and in helping the public remain informed about, and participate in, the Commission's activities.

## Public Meetings

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During the course of its work, the Commission held nine public meetings, all of which were noticed in the *Federal Register* as required by FACA. Six of these meetings were convened in Washington, DC, on January 8, February 20, May 28, May 29, July 16, and July 23. The remaining three “field” meetings were conducted outside the nation’s capital in Austin, Texas (March 18), Los Angeles, California (April 4), and Chicago, Illinois (April 29).

More than 70 invited witnesses testified at the nine Commission meetings. These witnesses advocated a broad array of reform measures and represented the diverse elements of the postal community. Through witness testimony, the Commission heard from representatives of the major postal employee unions, the postal management associations, consumer advocacy organizations, organizations representing senior citizens, the direct mailing community, the advertising industry, the express delivery and parcel industry, the magazine and newspaper industry, academia, the greeting card industry, retailers of approved postal services, the mail pre-sort and consolidation industry, technology suppliers to the Postal Service, the postal automation industry, and the envelope manufacturing industry.

The Commission was grateful to receive the testimony of S. David Fineman, Chairman of the Postal Service’s Board of Governors; Postmaster General John E. Potter; Deputy Postmaster General John M. Nolan; and numerous members of the Postal Service’s senior management team. The Commission was also fortunate to receive the testimony of other Federal officials, including David M. Walker, the Comptroller General of the United States, and George Omas, the Chairman of the Postal Rate Commission.

In addition to those witnesses who were invited to testify, the Commission requested and heard statements from members of the public at the field meetings in Austin, Chicago, and Los Angeles and at the meeting in Washington, DC on May 29.

Following each public meeting, Commission staff promptly posted the prepared testimony of all witnesses invited to testify at the meeting on the Commission’s website. The certified minutes of each meeting were also posted on the website.

## Subcommittees

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At its first meeting on January 8, the Commission established the following four subcommittees to assist in reviewing all aspects of the Postal Service's operations: 1) the Business Model Subcommittee (Richard Levin, Chair); 2) the Technology Challenges and Opportunities Subcommittee (Robert Walker, Chair); 3) the Private-Sector Partnership Subcommittee (Joseph Wright, Chair); and 4) the Workforce Subcommittee (Carolyn Gallagher, Chair). The work of each subcommittee has played a vital role in assisting the Commission in preparing this report.

Over the past several months, the *Business Model Subcommittee* has studied the Postal Service's universal service obligation, the postal monopoly, the current rate regulation system, the issue of pricing flexibility, the corporate governance of the Postal Service, and the "commercial government enterprise" business model proposed in the Postal Service's Transformation Plan. The *Technology Challenges and Opportunities Subcommittee* has assessed the impact of new technologies on the Postal Service's business model, reviewed the Postal Service's own technology initiatives and their effect on productivity, and studied whether there are ways to make the mail more valuable to consumers through technological innovation. The *Private-Sector Partnership Subcommittee* has analyzed the current role of the private sector in the mail delivery system through outsourcing, worksharing and other business arrangements, identified appropriate opportunities for the Postal Service to enter into partnerships with the private sector, and studied the involvement of the Postal Service in "non-postal" activities. The *Workforce Subcommittee* has assessed the Postal Service's current collective bargaining process, reviewed issues relating to employee pay and productivity, studied the application of the Federal Employees' Compensation Act to the Postal Service, and assessed the status of the Postal Service's pension and unfunded retiree health care liabilities.

Each subcommittee held multiple meetings by conference call. Commission staff prepared materials for each of these telephonic meetings and responded to informational and other requests by subcommittee members. In addition, two of the subcommittees requested that outside parties prepare papers on specific issues of interest. Once received by the subcommittees, these materials were promptly posted on the Commission website for public review.

The chair of each subcommittee reported preliminary findings to the full Commission at the following Commission meetings: 1) Business Model (February 20, Washington, DC); 2) Technology Challenges and Opportunities (March 18, Austin, Texas); 3) Private-Sector Partnership (April 4, Los Angeles, California); and 4) Workforce (April 29, Chicago, Illinois).

### Subcommittee and Co-Chair Recommendations

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At the meeting in Washington, DC on July 16, the Business Model Subcommittee and Private-Sector Partnership Subcommittee submitted their final recommendations to the Commission, all of which were formally adopted. At the July 16 meeting, the Co-Chairs also submitted a set of recommendations to the Commission. These recommendations were adopted by the Commission as well.

The Technology Challenges and Opportunities Subcommittee and the Workforce Subcommittee submitted their final recommendations to the Commission at the meeting in Washington, DC on July 23. These recommendations were adopted in their entirety at this meeting.

All Subcommittee and Co-Chair recommendations adopted by the Commission are reflected throughout this report and compiled in Appendix C.

## The Public-Comment, Rebuttal, and Final-Comment Processes

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From the start, the Commission has been committed to ensuring that every affected and interested party has had an opportunity to share its views and concerns. To facilitate public interaction, the Commission established a formal public-comment process at its first meeting on January 8. At the meeting, the Commission announced three methods by which the public could submit statements for consideration and review on the subjects outlined in Executive Order 13278. The deadline for submission of these public comments was February 12, 2003. This information was published in the *Federal Register* and posted on the Commission's website.

Pursuant to this public-comment process, the Commission received statements from more than 330 parties, including 98 organizations representing every segment of the postal community. These statements were very helpful in framing many of the issues studied by the Commission. With a few exceptions, all statements received by the Commission pursuant to the public-comment process were posted on the Commission's website for public review.

At its meeting on February 8<sup>th</sup>, the Commission established a second process (the "rebuttal process") to give interested parties an opportunity to respond to the assertions and recommendations made by other parties during the public-comment process. The deadline for the submission of rebuttal comments was March 13, 2003. This information was published in the *Federal Register* and posted on the Commission website.

The Commission received more than 30 rebuttal comments from individuals, organizations, and government officials. All rebuttal comments were promptly posted on the Commission's website.

In addition, through the publication of a notice in the *Federal Register*, the Commission established a process for the acceptance of final comments. The deadline for the submission of final comments was Tuesday, July 8, 2003. The Commission subsequently received more than 80 comments from both individuals and organizations. All final comments were promptly posted on the Commission's website.

## The Retention of Outside Consultants

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During the course of its deliberations, the Commission has sought out specialized assistance and retained the following outside consultants:

- *Global Insight*, for a study on the costs associated with the non-standardization of mail entry standards, postal processes and operations;
- *Global Insight*, for an analysis of the past and current use of price caps in the telecommunications industry and other regulated industries and an assessment of their effectiveness in providing rate predictability and improving productivity;
- *AT&T Government Solutions, Inc.*, for an analysis of the Postal Service's current logistics network and the development of a network optimization model;
- *Black & Veatch (Hart Research and American Viewpoint)*, for a telephonic survey of consumer attitudes about the Postal Service, including its products and services and various proposals to reform the business model and operations of the Postal Service;
- *ADR Associates, L.L.C.*, for an analysis of the grievance processes and procedures utilized by the Postal Service and the four major postal unions;
- *Unisys (Watson Wyatt)*, for an evaluation of alternative compensation incentive systems engaging all levels of the Postal Service workforce;
- *Unisys (Watson Wyatt)*, for an analysis of the management structure of the Postal Service and a comparison to the "best practices" of the private sector;
- *Greg Schmid, Ph.D., Director, Global Mail Project, Institute for the Future*, for the development of future mail volume projections; and
- *Professor Michael LeRoy, Institute of Labor and Industrial Relations and College of Law, University of Illinois at Urbana-Champaign*, for an analysis of the collective bargaining model currently utilized by the Postal Service and its employee unions and an assessment of possible alternative models.

The Commission is grateful for the valuable help provided by its outside consultants. Once the Commission received the final work product of each of these consultants, the work product was promptly posted on the Commission's website for public review.

## Private Meetings and Transparency

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In addition to participation in the public meetings of the full Commission, individual Commissioners have occasionally met privately with representatives of organizations with an interest in its work. These meetings by individual Commissioners have served an important fact-gathering function and are fully consistent with the requirements of FACA.

Throughout this process, the Commission has been committed to conducting its business in a fair, impartial, and transparent manner. Consistent with this goal, the Commission has posted on the Commission website notices of all private meetings between individual Commissioners and interested parties. These notices indicate the name of the Commissioner involved in the meeting, the name and organizational affiliation of the interested party, the location and date of the meeting, and a brief meeting summary.

More than 50 of these meeting notices have been posted on the Commission website under the link “Commissioner Contacts with Interested Parties.”

## Survey of Postal Facilities

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During the course of our work, individual Commissioners have visited numerous postal facilities, including facilities devoted to fulfilling the Postal Service's processing, distribution, and retail functions. The facility visits have allowed Commission members to view Postal Service activities and equipment first-hand, including how letter carriers merge different mail streams and prepare the mail for carrier-route delivery, operating differences between rural and city-based post offices, and the automation equipment used for sorting the mail. Postal facilities visited by members of the Commission include the Processing and Distribution Facility in Merrifield, Virginia; the Great Falls, Virginia Post Office; the McLean, Virginia Post Office; the Central Park Station Post Office in Austin, Texas; the Phoenix Processing and Distribution Center; the Morgan Processing and Distribution Center in New York, New York; the Los Angeles Processing and Distribution Center; and the Bulk Mail Processing Center in Houston, Texas.

The Commission is grateful for all the assistance given by the Postal Service in arranging and participating in these facility tours.

## APPENDIX C: Commission Recommendations

Reference Recommendation	Responsibility
<b>Recommendations of the Commission Co-Chairs</b>	
<p>C-1. <b>Governance.</b> <i>In order to establish a governance structure that exemplifies the best practices of similarly-sized private-sector corporations, the current Postal Service Board of Governors should be transformed into a corporate-style Board of Directors with broad authority to oversee Postal Service operations. Further, the Board of Directors should consist of three Directors appointed by the President, the Postmaster General, and eight independent Directors initially selected by the three Presidentially-appointed Directors with the concurrence of the Secretary of the Treasury. Thereafter, the eight independent Directors would be selected by the full Board of Directors with the concurrence of the Secretary of the Treasury. All Directors should be selected based on business acumen and other experience necessary to manage an enterprise of the Postal Service's size and significance. Terms for all Directors should be three years with a mandatory retirement age of 70.</i></p>	Congress.
<p>C-2. <b>Management Flexibility.</b> <i>The Board of Directors and senior Postal Service management should be given greater flexibility to manage without the limitations imposed by statutory constraints. More specifically: 1) Postal Service management should be given the flexibility to take advantage of corporate best practices; 2) the Postal Service should be allowed to set rates within limits established by a new Postal Regulatory Board without obtaining prior approval; 3) the sub-limits placed on annual borrowing for capital and operating needs within the existing \$3 billion annual limit on borrowing should be repealed; and 4) the Postal Service should be allowed to retain earnings subject to limits established by the Postal Regulatory Board.</i></p>	Congress.
<p>C-3. <b>Accountability and Public-Policy Oversight.</b> <i>In order to ensure that a Postal Service management with greater latitude has appropriate oversight, the Postal Rate Commission should be transformed into a new Postal Regulatory Board with the responsibility to protect the public interest and promote public confidence in the fairness and transparency of postal operations. The new Postal Regulatory Board should have authority to: review and refine the scope of the Postal Service's universal service obligation; clarify and refine the scope of the postal monopoly; regulate rates for non-competitive products and services; establish limits on the accumulation of retained earnings by the Postal Service; ensure financial transparency; obtain information from the Postal Service, if need be, through the use of new subpoena power; and review and act on complaints filed by those who believe the Postal Service has exceeded its authority. The new Postal Regulatory Board should be comprised of three members who are appointed by the President and confirmed by the Senate, and no more than two should be members of the same political party. Members of the Postal Regulatory Board should be selected solely on the basis of their demonstrated experience and professional standing.</i></p>	Congress.

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| C-4.   | <p><b>Rate-setting Procedures.</b> <i>The existing rate-setting process should be replaced with an incentive-based rate-setting methodology in which the Postal Regulatory Board: 1) establishes baseline rates and rate ceilings for non-competitive products and services; 2) reviews, in advance, rate requests for non-competitive products and services that exceed established rate ceilings; and 3) ensures that rates for competitive products and services are not cross-subsidized by revenues generated by non-competitive products and services. The Postal Regulatory Board, upon written complaint, should be authorized to conduct after-the-fact reviews of rate increases for non-competitive products and services, and, if necessary, to require adjustments to these rates when they are inconsistent with established rate ceilings. The Postal Regulatory Board should also be authorized to review, upon written complaint, whether a rate for a competitive product or service is being cross-subsidized by revenue generated by non-competitive products or services and to take appropriate remedial action. In conducting after-the-fact reviews, the Postal Regulatory Board should ensure that affected parties have an opportunity to participate, but should also ensure that the timeframe for the review is dramatically reduced from that permitted under the existing rate-setting process. Participation by interested parties should be limited to written submissions, and all procedures should require a final determination within 60 days.</i></p> | Congress.                    |
| <p><b>Recommendations of the Business Model Subcommittee</b></p> |  |                              |
| B-1.   | <p><b>Basic Structure.</b> <i>The Postal Service should continue to operate as an independent establishment within the executive branch with a unique mandate to operate as a self-sustaining commercial enterprise.</i></p>   | No action required.          |
| B-2.   | <p><b>Mission.</b> <i>The 1970 Act should be amended to clarify that the mission of the Postal Service is to provide high-quality, essential postal services to all persons and communities by the most cost-effective and efficient means possible at affordable and, where appropriate, uniform rates. In doing so, the activities of the Postal Service should be limited to: 1) accepting, collecting, sorting, transporting, and delivering letters, newspapers, magazines, advertising mail, and parcels; and 2) providing other governmental services when in the public interest and where the Postal Service is able to recover the appropriately allocated costs of providing such services.</i></p>   | Congress.                    |
| B-3.   | <p><b>Monopoly.</b> <i>The Postal Service should maintain its current mail monopoly, and also retain its sole access to customer mailboxes. However, the 1970 Act should be amended to: 1) authorize the Postal Regulatory Board to clarify and periodically review the scope of the mail monopoly; and 2) clarify that the Postal Service does not have the authority to alter the scope of the mail monopoly or to determine the extent of access to customer mailboxes.</i></p>   | Congress.                    |
| B-4.   | <p><b>Financial Transparency.</b> <i>The Postal Service should voluntarily comply with applicable Securities and Exchange Commission reporting requirements. In addition, the Postal Service should periodically report on the allocation of costs among mail products and services in accordance with form, content, and timing requirements determined by the Postal Regulatory Board.</i></p>   | Postal Service and Congress. |

B-5.	<b>Processing Facilities.</b> <i>A Postal Network Optimization Commission (P-NOC), modeled in part after the Defense Base Closure and Realignment Commission, should be created to make recommendations relating to the consolidation and rationalization of the Postal Service mail processing and distribution infrastructure. The P-NOC should be comprised of eight members appointed by the President with the advice and consent of the Senate. Recommendations of the P-NOC, once submitted to Congress by the President, should become final, unless Congress disapproves them in their entirety within 45 days.</i>	Congress.
B-6.	<b>Post Offices.</b> <i>Efforts already underway by the Postal Service to expand access to retail postal services at venues other than post offices, such as banks, grocery stores, and other convenient locations, should be supported. When the Postal Service determines that a “low-activity” post office is no longer necessary for the fulfillment of its universal service obligation, the Postal Service should make every effort to maximize the proceeds from the sale of that facility. If the Postal Service determines that there is no adequate market demand for the purchase of a “low-activity” post office, the Postal Service should be encouraged to work with state and local governments, as well as not-for-profit organizations, to determine the means of disposition most beneficial to the local community. Such disposition could include transfer to a state or local government or not-for-profit organization, with or without reimbursement, as best serves the public interest. Existing statutes limiting the Postal Service’s flexibility with regard to the closing and disposition of post offices should be repealed and similar provisions in annual appropriation acts should be avoided.</i>	Postal Service and Congress.
B-7.	<b>Real Estate Asset Management.</b> <i>The Postal Service should be encouraged to include policy goals and objectives relating to the active management of Postal Service real estate in future strategic plans. As a first step, the Postal Service should obtain an independent appraisal of the current market values of its major real estate holdings. Further, the Postal Service should use its current statutory flexibility to dispose of real estate assets to strengthen its long-term financial position and provide benefits to the public in the form of moderated rate increases and improved products and services.</i>	Postal Service.
<b>Recommendations of the Private-Sector Partnership Subcommittee</b>		
P-1.	<b>Maximizing the Use of the Private Sector.</b> <i>Those Postal Service functions that can be performed better and at lower cost by the private sector should be outsourced to the private sector.</i>	Postal Service.
P-2.	<b>Utilizing the Postal Service’s Core Strength: “The First Mile” and “The Last Mile.”</b> <i>The Postal Service should continue to explore opportunities to utilize its core strengths in the “first” and “last” mile of the mail delivery stream through the development of mutually beneficial partnerships with the private sector.</i>	Postal Service.
P-3.	<b>Expanding Retail Access to Postal Products and Services.</b> <i>The Postal Service should develop additional private-sector partnerships to better serve the consumer and expand access to postal products and services beyond the traditional post office.</i>	Postal Service.

- P-4. **Worksharing Discounts for Non-Competitive Products.** *The Postal Service should continue to look for opportunities to offer discounts for additional workshared products and to expand opportunities for small mailers to participate in them, particularly as new technologies are developed, that reflect lowest combined public-private sector costs. The new Postal Regulatory Board should be required to conduct an expedited, after-the-fact review of a new worksharing discount upon written complaint by a party that the discount exceeds the costs avoided by the Postal Service. A discount that exceeds the costs avoided by the Postal Service should not be permitted. In addition, the Postal Service should ensure that the expected savings from worksharing discounts are actually captured in the form of reduced costs.* Congress and Postal Service.
- P-5. **Negotiated Service Agreements for Non-Competitive Products.** *The Postal Service should be given greater flexibility to enter into negotiated service agreements for non-competitive products. Specifically, the Postal Service should be allowed to enter into agreements based on general criteria established by the new Postal Regulatory Board. The Postal Regulatory Board should conduct expedited, after-the-fact reviews of such agreements when a written complaint is filed.* Congress.
- P-6. **Procurement Reform.** *There is a significant opportunity to improve the Postal Service's "bottom-line" through revision of its procurement regulations and the adoption of commercial best practices. Therefore, the Postal Service should revise its purchasing regulations to maximize the flexibility given to it under current law and to reflect commercial best practices. Congress should strongly support Postal Service procurement reform in acknowledgement of its substantial benefit to all ratepayers.* Postal Service and Congress.

#### **Recommendations of the Technology Challenges and Opportunities Subcommittee**

- T-1. **Automation Technology.** *The Postal Service should balance capital expenditures on new automation technology with consideration of outsourcing elements of the processing network. The Postal Service should neither acquire excess capacity that would only be used during peak periods nor undertake functions that the private sector could perform more effectively and at less cost than the Postal Service itself. Nonetheless, the Commission acknowledges the steps the Postal Service has taken to automate its system for processing single-piece letter mail and welcomes the progress made in the automation of the processing of flats and packages. The Postal Service should continue to develop an effective merging system that is responsive to customer needs and culminates in one bundle of mixed letters and flats for each delivery point.* Postal Service.
- T-2. **Processing Standardization.** *The Postal Service should study the problem of mail processing with the possible goal of redesign of the whole mail system, using the latest in 21<sup>st</sup> century technology systems. The Postal Service should examine every one of its "legacy systems" and question its purpose and whether it is needed. In addition, the mail processing redesign should include a standard or common footprint for each processing facility, with an identical level of technology and machinery in each. This would allow easy shifting of personnel to manage the mail flow more efficiently. This redesign study should be viewed as complementary to the Postal Service's current network rationalization initiative.* Postal Service.

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| T-3. | <b>Intelligent Mail.</b> <i>The ability of the Postal Service to track individual pieces of mail can improve internal efficiency and satisfy postal customers that mail is delivered to the right location and on time. The technology to achieve this goal exists today and is now being used by some of the competitors of the Postal Service. The Postal Service should work to put mail tracking technology in place on a timely and more comprehensive basis, so that it is available to all users, large and small, at an affordable price.</i>   | Postal Service. |
| T-4. | <b>The Transportation Network.</b> <i>The Postal Service should integrate its facility automation efforts with its transportation network by using Intelligent Mail technology, GPS, and onboard computer technology. The Postal Service should also put in place a cost-effective system capable of tracking every vehicle on its route and allowing each vehicle to communicate in real time, either by voice or electronic communication, with appropriate fixed facilities.</i>   | Postal Service. |
| T-5. | <b>Improved Postal Service Website (www.usps.com) and Personalized Stamps.</b> <i>Postal services available at post offices should also be generally available on the Postal Service website and at Postal Service kiosks and contract stations at reasonable prices for all postal customers, from the individual to the large mailer. The Postal Service should develop and produce “personalized” stamps and make them available through appropriate sources, beginning with the Postal Service website. These stamps should be offered to postal customers at a reasonable premium.</i>   | Postal Service. |
| T-6. | <b>Security.</b> <i>The events of 9/11 and the Postal Service anthrax incidents have increased the need to ensure security in the mail system. A more secure system could be built using sender identified mail. The Postal Service, in coordination with the Department of Homeland Security, should explore the use of sender identification for every piece of mail, commercial and retail.</i>  | Postal Service. |
| T-7. | <b>Evaluation, Acquisition and Deployment of Technology.</b> <i>The Postal Service recently created the new Mailing Technology Strategy Council to provide assessments on technology trends. The Council should be strengthened to be an independent advisory body empowered to do more than provide assessments. The Council should not only originate ideas for improving the mail system, but should accept them from all sources, including the individual Postal Service user. It should study, evaluate and recommend to the Postmaster General technologies that could be used to upgrade the mail system. Postal Service management should provide an annual report to the new Board of Directors on the work of the Mailing Technology Strategy Council.</i> | Postal Service. |

#### **Recommendations of the Workforce Subcommittee**

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| W-1. | <b>Developing an Appropriately-Sized Workforce.</b> <i>As the Postal Service works to meet the challenges of the 21<sup>st</sup> century, it must develop a world-class workforce appropriate to fulfilling its universal service obligation. Fortunately, the Postal Service will soon be presented with a unique attrition opportunity with some 47% of current career employees eligible for retirement by 2010. The Postal Service is urged to take full advantage of this attrition opportunity and to exercise maximum discipline in its hiring practices in order to rightsize and realign its workforce with minimal displacement.</i> | Postal Service. |
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- W-2. **Collective Bargaining: Process Improvements.** *The collective bargaining process should be retained. However, the collective bargaining process should be improved to create additional incentives for the parties to reach negotiated settlements, and, when the parties fail to reach a negotiated settlement, to ensure that arbitration awards are made within a reasonable period of time. In particular, the collective bargaining process should be as follows:*
- **Basic process.** *A negotiation process, beginning 90 days prior to the expiration of an existing agreement, followed by a 30-day mandatory mediation process and, if mediation fails, an immediate 60-day interest arbitration process.*
  - **Mandatory mediation and “Med-Arb.”** *The 30-day mandatory mediation process would be conducted by a mediator who would become a member of the arbitration panel should mediation fail. The purpose of the mediation process would be to either reach a negotiated settlement or to narrow the range of issues to be submitted to interest arbitration.*
  - **Interest arbitration.** *The 60-day interest arbitration process would be conducted by a three-person arbitration panel comprised of three neutral arbitrators, one having served as the mediator. The interest arbitration process would incorporate the Last Best Final Offer mechanism and a 10-day period during which the parties would have a final opportunity to reach a negotiated settlement prior to the arbitration panel’s final award.*
- Congress.
- W-3. **Collective Bargaining: New Subjects.** *The Postal Service’s pension and post-retirement health care plans should be subject to collective bargaining – meaning that the Postal Service and its unions should have the flexibility to develop new plans that are separate and apart from existing Federal pension and retiree health care plans. However, because of concern about the uncertain impact such a change would have on the Federal system as a whole and on other Federal employees in particular, the Postal Service should work with the Department of the Treasury, the Office of Personnel Management, and any other persons or entities deemed necessary to determine the impact separate Postal Service pension and retiree health care programs would have on the existing Federal systems. As a first step:*
- *The Postal Service should be authorized to negotiate Federal Employee Retirement System eligibility requirements and employee contributions;*
  - *The Postal Service should be authorized to negotiate the eligibility and retiree contribution requirements for the post-retirement health care component of the Federal Employee Health Benefit Program, specifically for future Postal Service retirees; and*
  - *The current statutory requirement that “[n]o variation, addition, or substitution with respect to fringe benefits shall result in a program of fringe benefits which on the whole is less favorable to the officers and employees than fringe benefits in effect on [July 1, 1971]” should be repealed.*
- Congress.

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| W-4. | <p><b>Pay Comparability.</b> <i>The 1970 Act should be amended to clarify the meaning of the term comparability, and the new Postal Regulatory Board should be authorized to determine comparable total compensation for all Postal Service employees. In determining comparable total compensation, the Postal Regulatory Board should be authorized to determine the appropriate sector(s) of the private-sector workforce to be used as the basis of comparison. The comparability determination of the Postal Regulatory Board should be enforced as a cap on the total compensation of new employees. In addition, if the Postal Regulatory Board determines that a total compensation premium exists for current employees, it should be authorized to determine the appropriate period of time during which the premium must be eliminated, and to review periodically its initial determination and the Postal Service's progress in eliminating the premium.</i></p> | Congress.                    |
| W-5. | <p><b>Pay-for-Performance.</b> <i>Performance-based compensation programs are effective tools that, when designed correctly, can be used to align the goals of management and labor and result in improved efficiency and service quality. The Postal Service should undertake a careful study of performance-based compensation programs for both management and represented employees, and it should work with the unions and management associations to design and implement a performance-based compensation program that is meaningful to Postal Service employees and assists the Postal Service in meeting its productivity and service quality goals.</i></p>   | Postal Service.              |
| W-6. | <p><b>Grievances.</b> <i>The current dispute resolution process must be revised if the Postal Service is to operate in accordance with the best practices of private-sector companies with highly unionized workforces. As a first step, the Postal Service should work diligently with its unions to implement best practice grievance procedures, including those recently implemented by the Postal Service and the National Association of Letter Carriers.</i></p>   | Postal Service.              |
| W-7. | <p><b>Workers' Compensation Claims.</b> <i>The Postal Service should be provided relief from the requirements of the Federal Employees' Compensation Act as follows:</i></p> <ul style="list-style-type: none"> <li>• <i>The Postal Service should not be required to pay benefits until after the expiration of a three-day waiting period;</i></li> <li>• <i>The Postal Service should be allowed to limit benefits to 2/3 of the maximum weekly rate; and</i></li> <li>• <i>The Postal Service should be allowed to transition individuals receiving workers' compensation to the Postal Service's retirement plan at such time as the employee would have become eligible for retirement notwithstanding the injury giving rise to the workers' compensation benefits.</i></li> </ul>   | Congress.                    |
| W-8. | <p><b>Executive Compensation.</b> <i>The current statutory salary cap should be repealed. Further, the Postal Service should be authorized to establish rates of pay for officers and employees at levels competitive with the private sector. Performance should be considered as a key component of senior executive pay.</i></p>   | Congress and Postal Service. |

- W-9. **Management Structure.** *The Postal Service should restructure its management to eliminate redundant positions and geographical divisions and to standardize and clarify job functions. The Postal Service should conduct a review of the entire management structure, size, and cost to determine whether each component is necessary and consistent with the best practices of the private sector, and it should require managers to justify their functions and the size of their staffs.* Postal Service.
- W-10. **Accounting for Retiree Health Care Obligations.** *The Postal Service should review its current policy relating to the accounting treatment of retiree health care benefits, and work with its independent auditor to determine the most appropriate treatment of such costs in accordance with applicable accounting standards and in consideration of the Postal Service's need for complete transparency in the reporting of future liabilities. The Postal Service should consider funding a reserve account for unfunded retiree health care obligations to the extent that its financial condition allows.* Postal Service.
- W-11. **Funding Military Service.** *Responsibility for funding Civil Service Retirement System pension benefits relating to the military service of Postal Service retirees should be returned to the Department of the Treasury.* Congress.

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## Appendix D: Additional Statement by Commissioner Seabrook

July 30, 2003

President's Commission on the United States Postal Service  
1120 Vermont Avenue, N.W.  
Suite 971  
Washington, DC 20005

Dear Commissioners:

I have reviewed the final recommendations to the Commission from the Workforce Subcommittee. I agree with recommendations 1, 6, 8, 9, 10 and 11. I disagree with recommendations 2, 3, 4, 5 and 7 for the following reasons:

I dissent from recommendation number 2 because it places artificial constraints on the bargaining process. Management and labor should be free to conduct arms-length bargaining and reach a decision through that process and the existing arbitration process. Cutting the time of the arbitration process to 180 days at the most is a worthwhile objective but is not the answer to the existing arbitration problem. The arbitration process takes too long because management often takes an unreasonable position. Adequate funding of the Postal Service as well as recognition of the financial and other interests of the employees is a better approach. Expediting an unfair process is not the answer.

I dissent from recommendation number 3 for the following reasons: Adding Postal Service pension and the post-retirement healthcare plan to the collective bargaining process puts these benefits at greater risk than is the case for other federal employees. The benefits of federal employees in the existing structure grow out of a long history of federal budgetary considerations and legislative initiatives. While the benefits could certainly be improved, this recommendation does not have benefit improvement as an objective. Placing pension and retiree health benefits into a collective bargaining process and then constraining that process by pressuring for settlements within "180 days" creates an environment that may be potentially harmful to active and retired postal workers. I prefer that the benefits for postal workers be considered in the same way as other federal employees.

I dissent from recommendation number 4 because the operationalization of the concept is problematic. Pay comparability is a concept best applied when public employees' salaries and benefits are not subject to collective bargaining. In a collective bargaining process, pay comparability inevitably enters any determination of salaries and benefits. However the dynamic of the bargaining process where management and labor meet on an equal footing and struggle through to a determination is quite different from an administrative process where "personnel types" organize groups of people into boxes of comparable worth and impose their view of a worker's value. The former is an equitable approach. The latter is quintessential bureaucracy.

I dissent from recommendation number 5 for the following reasons: Pay for performance is a disguised way in which management can attack the strength of a union by dividing its members. "Pay for performance" as a concept seems unassailable because who could argue that people who perform better should be paid more? In practice, however,

such systems are characterized by nepotism, favoritism and horrible morale among the workers. I challenge the subcommittee to demonstrate a successful pay for performance system in any large strongly unionized public organization. Personnel evaluations, performance evaluations, employee rating systems, etc., all have some value but only as an integral part of an employee management system that includes a strong labor component, which in the final analysis balances the outcome in favor of objective performance.

I dissent from recommendation number 7 because it implies that workers' compensation abuse is so rampant that a tested and respected system needs to be totally revamped to ameliorate the abuses. If one honestly believes that a worker has been injured and that the work-related injury must be subjected to an equitable process, these recommendations are troublesome. Only when read in the context of widespread abuse do these recommendations become logical. If the subcommittee assumes that there are abuses, the individual abuses should be dealt with in a detailed and aggressive way. However, encumbering an already difficult process by adding reduction in benefit payments and expedited retirements is unfair to the bulk of postal workers who are injured on the job.

In closing, I believe that recommendations 2, 3, 4, 5 & 7 require additional work by the subcommittee. Each of the recommendations focuses on an issue that we thought needed examination. However, the approach to the solution in my view is counterproductive and biased against the worker. The efficiencies enjoyed will be at the expense of the effectiveness of the employee and, therefore, the effectiveness of the organization. Under the circumstances, these issues should be left the way they are instead of changed by the recommendations brought by the subcommittee.

Thank you,

Commissioner Norman Seabrook

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# Acknowledgments

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The President's Commission on the United States Postal Service would have been unable to complete its work without the active help and support of the Postal Service itself. The Co-Chairs would like to thank S. David Fineman, the Chairman of the USPS Board of Governors; Postmaster General of the United States John E. Potter; Deputy Postmaster General John M. Nolan; USPS Chief Financial Officer Richard J. Strasser; USPS Treasurer Robert J. Pedersen; and the many members of the Postal Service management team who shared their insights with the Commission over the past several months. Much of this report is an affirmation of the efforts already underway to transform the Postal Service into a modern 21<sup>st</sup> century institution.

The Co-Chairs also wish to thank Margaret Spellings, Assistant to the President for Domestic Policy, and Peter R. Fisher, Under Secretary of the Treasury for Domestic Finance, for their encouragement and guidance during the course of this project.

The Co-Chairs want to express deep appreciation for the thoughtful, intelligent and effective work of the Commission's Executive Director Dennis Shea. Dennis truly did an outstanding job.

The Co-Chairs and the Executive Director extend a special thanks to Commission staff member Randall Lewis whose contribution to this project has been nothing short of indispensable. They also extend their thanks to Jana Sinclair White, whose tireless efforts were crucial to the completion of the report, and to James Cox for his valuable assistance throughout the past several months. In addition, Commission staff members Bridgette Kilkenny, Paul Revesz, Ryan Cunningham, Stephen Passman, Jennifer Streaks, and Ryland Sumner made important contributions.

Thanks are due to Brian C. Roseboro, Roger Kodat, Michael Scott, and Betsy Holahan of the Department of the Treasury, as well as Elizabeth Dougherty of the White House Domestic Policy Council, for the steadfast support they gave to the Commission and its staff. Commission consultants James I. Campbell, Jr., Robert Reisner, Carl Moravitz, and Robert Heiler also made valuable contributions to key aspects of the report.

Finally, the Co-Chairs and the Executive Director wish to acknowledge and thank Christine Hagstrom for bringing her considerable writing talent to bear on behalf of this project.

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