

January 2001

# Major Management Challenges and Program Risks

U.S. Postal Service





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January 2001

The President of the Senate  
The Speaker of the House of Representatives

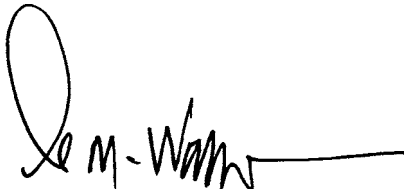
This report addresses the major performance and accountability challenges facing the U.S. Postal Service as it seeks to bind the nation together through the correspondence of the people, to provide access in all communities, and to offer prompt, reliable, and efficient postal services at uniform prices. It includes a summary of actions that the Service has taken and that are under way to address these challenges. It also outlines further actions that GAO believes are needed. This analysis should help the new Congress and administration carry out their responsibilities and improve government for the benefit of the American people.

This report is part of a special series, first issued in January 1999, entitled the *Performance and Accountability Series: Major Management Challenges and Program Risks*. In that series, GAO advised the Congress that it planned to reassess the methodologies and criteria used to determine which federal government operations and functions should be highlighted and which should be designated as “high risk.” GAO completed the assessment, considered comments provided on a publicly available exposure draft, and published its guidance document, *Determining Performance and Accountability Challenges and High Risks* (GAO-01-159SP), in November 2000.

The full 2001 *Performance and Accountability Series* contains separate reports on 21 agencies—covering each cabinet department, most major independent agencies, and the U.S. Postal Service. The series also includes a

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governmentwide perspective on performance and management challenges across the federal government. As a companion volume to this series, GAO is issuing an update on those government operations and programs that its work identified as “high risk” because of either their greater vulnerabilities to waste, fraud, abuse, and mismanagement or major challenges associated with their economy, efficiency, or effectiveness.

A handwritten signature in black ink, appearing to read "D. M. Walker", with a long horizontal line extending to the right.

David M. Walker  
Comptroller General  
of the United States

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# Overview

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In fiscal year 2000, the U.S. Postal Service employed nearly one-third of the federal civilian workforce, provided delivery services for almost 208 billion pieces of mail to more than 130 million households and businesses, and earned almost \$65 billion in operating revenue. Both Congress and the public expect the Service to fulfill its primary mission of providing universal postal service at reasonable rates while remaining self-supporting from postal revenues. Overall, during the late 1990s the Service improved its financial position through net income exceeding \$5 billion and improved the timely delivery of First-Class Mail. Moreover, in fiscal year 2000, the Service improved productivity and implemented cost-cutting measures while generally maintaining its overnight First-Class Mail delivery performance. However, mail volumes grew more slowly than expected, and postal costs were difficult to restrain. Thus, the Service incurred a deficit of almost \$200 million in fiscal year 2000. In addition, postal rates are scheduled to increase in early 2001.

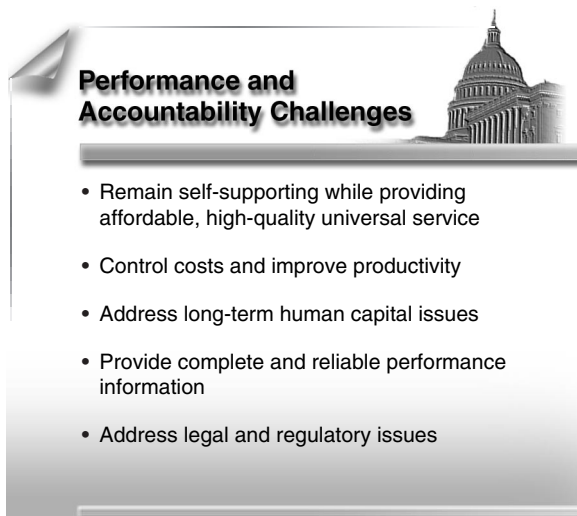
Looking ahead, we have reported that the Postal Service faces an uncertain future as competition increases in the communications and delivery services sectors. The Service has reported that it faces significant threats from electronic substitution of mailed bills and payments and anticipates a financial squeeze resulting from declining First-Class Mail volumes that cover most postal overhead costs. Thus, a key oversight issue we identified for the Postal Service, Congress, and the American people was whether the Service might be headed for financial shortfalls that could, in the long run, hinder its ability to remain self-supporting while carrying out its mission of providing affordable, universal postal services that bind the nation together. The potential consequences if the Service incurs a series of large financial deficits could be increases in postal rates, declines in service quality, consolidation or closure of some facilities, or reconsideration of the scope of postal services as well as postal operations.



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The Postal Service is also challenged to operate in an uncertain legal and regulatory environment, with unresolved regulatory issues about the Postal Service's future role and an ongoing debate over whether fundamental changes should be made to the legal and regulatory system governing the Service.

The Postmaster General recently said that the Postal Service is at a crossroads with regard to its ability to continue to provide affordable universal service. To be successful, the Service must address formidable challenges in five key areas.



**Performance and Accountability Challenges**

- Remain self-supporting while providing affordable, high-quality universal service
- Control costs and improve productivity
- Address long-term human capital issues
- Provide complete and reliable performance information
- Address legal and regulatory issues

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**Remain self-supporting**

We have reported that the Service faces growing challenges from competition, notably from private delivery companies and electronic communications alternatives such as the Internet. The Service projects that such competition will lead to substantial declines in the Service's First-Class Mail volume in the next decade. We have also reported that should this occur, the Service will likely face unprecedented challenges as it seeks to fulfill its primary mission of providing universal postal

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service at reasonable rates while remaining self-supporting from postal revenues. Although it is difficult to predict the timing and magnitude of further mail volume diversion to electronic alternatives and the potential financial consequence, the Service's baseline forecast calls for total First-Class Mail volume to decline at an average annual rate of 3.6 percent from fiscal years 2004 through 2008.

The Service has reported that it can sustain its viability over the next 5 years by "dramatically cutting costs and seeking new revenue sources within the current regulatory structure." However, the Service has also reported that planned reductions in its costs may not be sufficient to keep future rate increases below inflation, especially for any mail categories that take on a larger burden of supporting postal infrastructure costs as a result of volume loss in other categories. Further, the Service has recognized the difficulty of generating significant revenue from new products and services over the next 5 years. Historically, as our 1998 report showed, the Service's new product and service initiatives underway during the mid-1990s generally were not profitable.

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Control costs

We testified in 1998 and 1999 House postal oversight hearings that the Service's continued success will depend heavily on its ability to control operating costs and improve productivity. As the Postal Service and key stakeholders have recognized, long-term increases in its productivity will be essential to controlling costs and thus keeping postage rates affordable. Numerous reports, including some by us, have noted inefficiencies in the postal system and difficulties the Service has had in realizing opportunities for savings. Postal productivity has increased only about 11 percent over the past three decades, despite substantial investments in automation and information technology. The Service's goal is to achieve "breakthrough" productivity increases that

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generate \$3 billion to \$4 billion cost savings by 2005. Most of the savings are to come from productivity increases in mail processing operations, while additional savings are to come from administrative activities, purchasing, transportation, and other operations.

The Service's ability to improve productivity and control costs is, however, constrained by a number of factors, such as its requirement to maintain a national infrastructure of post offices, many of which are small and unprofitable. Despite heavy investments in automation over the past decade, postal labor-related costs continue to account for over three-quarters of total operating expenses. In addition, some employee-related expenses are rising and are difficult to control, such as retirement, health care, and workers compensation costs.

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Human capital issues

We believe that with a workforce of more than 900,000 employees, the Postal Service faces difficult human capital challenges that must be successfully addressed to maintain organizational effectiveness and improve the workplace environment as well as control workforce costs. These challenges include (1) restructuring the postal workforce and reducing the number of employees, (2) maintaining effective operations as most executives and about half of the postal workforce reach retirement eligibility over the next decade, and (3) ameliorating persistent problems in the workplace that have been exacerbated by decades of adversarial labor-management relations. The Postal Service's human capital problems can be seen as part of a broader pattern of human capital shortcomings that have eroded mission capabilities across the federal government. See our *High-Risk Series: An Update* (GAO-01-263, Jan. 2001) for a discussion of human capital as a newly designated governmentwide high-risk area.

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Progress, however, will not be easy. By law, a third-party arbitration board imposes a labor-management contract when the parties fail to agree, and binding arbitration has often been used to settle impasses in the contract negotiations. As of December 2000, contracts had expired between the Service and three of its four major labor unions, and the parties had been unable to reach agreement in contract negotiations. The Service has reported that it is bound by extensive work rules and other regulations that hamper flexibility and innovation. Further, the Service has stated it is already facing problems in recruiting, motivating, and retaining employees, especially in the technical, professional, and managerial categories, and it will face succession issues as a substantial number of managers reach retirement age. Moreover, as we have reported, persistent workplace problems have impeded efforts to improve efficiency and effectiveness. One indication of these impediments is the time and cost expended to handle about 146,000 pending or appealed grievances. We recommended that postal management and the heads of the postal labor unions and management associations develop a long-term framework agreement to improve the workplace environment. Although the parties have held a series of meetings, such a framework agreement has not been developed. On the other hand, the Service has reached agreements with some of the unions to address specific workplace issues such as the handling of employee grievances. Further, the Service has made the "Voice of the Employee" one of its top three corporate goal areas, established specific targets for improvement, and initiated numerous programs to improve the workplace environment.

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Performance  
information

We remain concerned about the quality and transparency of the Postal Service's performance information. Without complete and reliable performance data, the Service and other stakeholders cannot determine the Service's progress towards meeting its

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intended performance results. For example, we reported that the Service's financial data for its electronic commerce (e-commerce) initiatives were not sufficiently complete and reliable to assess the Service's performance. The Service agreed with our recommendation that it provide complete and accurate information on its e-commerce costs and revenues and said it is instituting a standard financial reporting procedure in this area.

In addition, we recently reported that the Postal Service's annual performance plans and performance reports may not have been as useful to Congress, postal managers, and customers as they could have been, in part because they contained incomplete and possibly misleading explanations of some results. We recommended, and the Service agreed, that the Service should make its future performance reports reflect straightforward and clearly stated comparisons of planned targets and results. In addition, we recommended that the Service's future performance plans should have clear criteria for measuring performance and provide more complete explanations of its goals and strategies. In response, the Service made changes that strengthened its final annual performance plan for fiscal year 2001.

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Legal issues

The Postal Service is challenged to operate in an uncertain legal and regulatory environment. As we have previously reported, postal stakeholders are engaged in an ongoing debate over whether the Service should be allowed to compete with private companies and, if so, under what circumstances. Congress, the Service, its competitors, and others have debated fundamental issues regarding the Service's legal authority and regulatory framework. Further, some stakeholders have raised antitrust and fair competition concerns relating to current and potential alliances and partnerships involving the Service and others, including private

sector companies such as FedEx, as well as foreign postal administrations. In addition, the Service has raised concerns about its lack of flexibility to set prices and the lengthy postal ratemaking process and has called for changes to the existing regulatory framework for setting domestic postal rates. Without a clear consensus among postal stakeholders, Congress is likely to be asked to consider various legislative proposals concerning the Service's role and what regulatory framework should apply to the Service.

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# Major Performance and Accountability Challenges

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The Postal Service, the single largest federal civilian agency, has a mission vital to the nation's communications and commerce. As an independent establishment of the executive branch, the Service is charged with providing postal services to bind the nation together through the personal, educational, literary, and business correspondence of the people. The Service has a statutory monopoly that restricts the private delivery of letters to enable the Service to fulfill its universal service mandates. To carry out its mission, the Service maintains a delivery and retail infrastructure that includes more than 235,000 city and rural delivery routes; more than 38,000 post offices, stations, and branches; and more than 350 major mail processing and distribution facilities. This physical infrastructure continues to grow, and the Service added about 2 million delivery points in fiscal year 2000. Further, the Service is required to break even over the long run by operating in a businesslike manner and currently receives little federal financial assistance to meet its public service obligations. To change domestic postage rates, the Service must file a proposal with the independent Postal Rate Commission (PRC)—starting a complex process that is to result in a PRC-recommended decision within 10 months and subsequent Service action.



### **Key Facts About the Postal Service**

- Total revenues of about \$65 billion in fiscal year 2000.
- Over 900,000 employees.
- Largest federal civilian agency.
- Ranks 2nd in employment and 8th in revenues compared to U.S. companies.



### **Key Aspects of Universal Postal Service**

- Mail delivery 6 days each week.
- Uniform postal rates for First-Class letter mail.
- Prompt, reliable, and efficient postal services to patrons in all areas, including rural areas, communities, and small towns where post offices are not self-sustaining.



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Remain Self-  
Supporting While  
Providing  
Affordable, High-  
Quality Universal  
Service

The Postal Service expects diversion of mailed bills and payments to electronic billing and payment alternatives to cause a substantial decline in First-Class Mail volume and “extreme financial pressure” for the Service. The financial squeeze—which has already begun—will challenge the Service to remain self-supporting while providing affordable high-quality service. To address this challenge, the Service’s basic strategy is a combination of aggressive cost-cutting and new revenue-generation. In the long term, the Service will be challenged to address the following questions: (1) Can the Service maintain and, where necessary, improve on the quality of mail delivery service? (2) Can the Service continue to provide affordable postal rates? (3) Can the Service remain self-supporting through postal revenues? (4) Can the Service continue in the long term to provide the current level and scope of universal postal service?

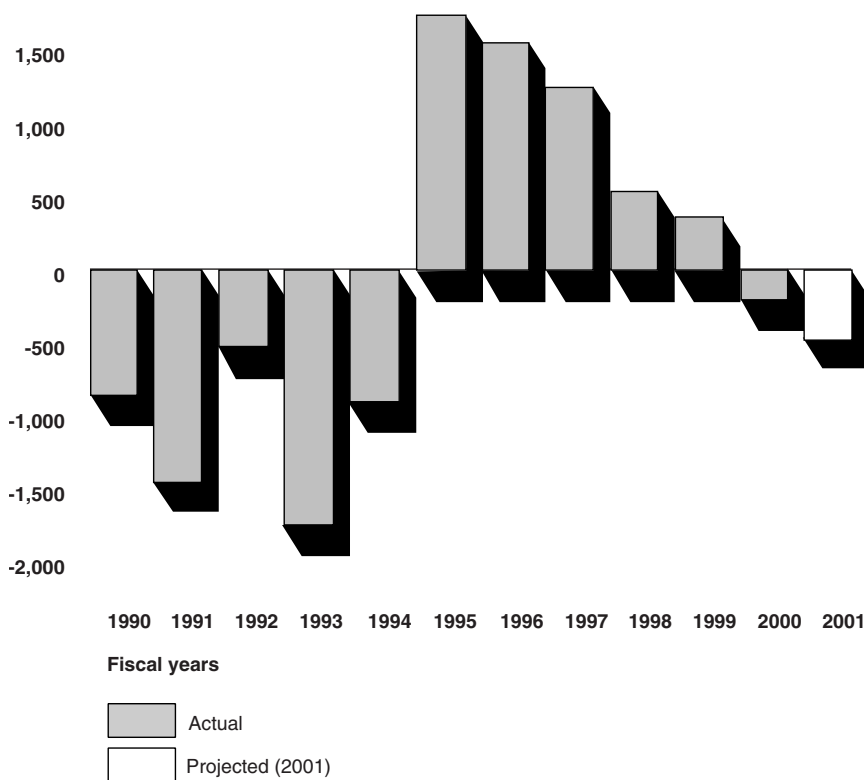
To put its financial and service outlook into context, in the late 1990s, the Postal Service improved its financial position through net income of about \$5.5 billion, which helped keep postal rates affordable. Over the same period, the Service also improved delivery performance as measured by on-time delivery of First-Class Mail. In fiscal year 2000, the Service achieved on-time delivery for 94 percent of overnight First-Class Mail and 85 percent for 2- and 3-day First-Class Mail. However, the Postal Service has encountered increasing financial difficulties as its net income decreased annually from fiscal years 1995 through 2000, when the Service incurred a deficit of almost \$200 million—its first deficit since fiscal year 1994 (see fig.1). Moreover, although in January 2000, the Service projected \$500 million in net income for fiscal year 2001, by October 2000, it projected a \$480 million deficit despite a planned rate increase midway through the fiscal year. The Service stated that increases in anticipated expenses, such as for fuel costs and cost-of-living allowances, as well as lower

**Major Performance and  
Accountability Challenges**

than expected revenue growth accounted for most of the difference.

**Figure 1: Postal Service Net Income Is Declining**

2,000 Dollars (in millions)



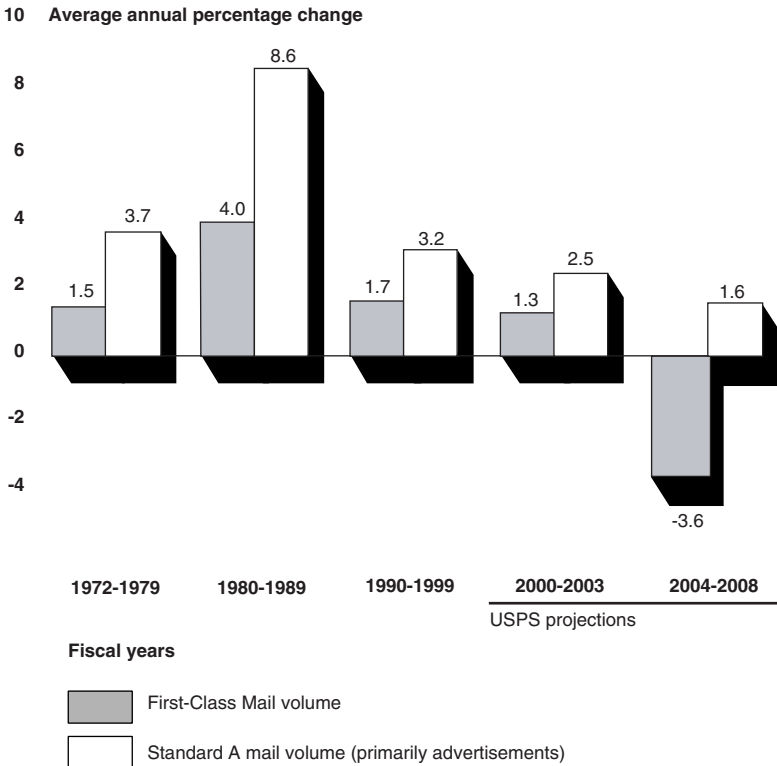
Source: U.S. Postal Service.

Looking ahead, competition is increasing from private delivery companies, foreign postal administrations accepting outbound international mail in the United States, and electronic communications alternatives such as the Internet. As an example of trends that have already affected the Service's mail volumes, federal

agencies are mandated to move as quickly as possible to reduce paperwork and to adopt electronic billing and payment. Two-thirds of the 880 million Social Security checks, tax refunds, and other payments that were sent by the Department of the Treasury in fiscal year 1999 were sent electronically, not mailed. Further, the banking industry's mail volume was almost 18 percent lower in 1999 than it was in 1996. According to the Service, longer term projections suggest that about half of the bills and payments that are currently mailed will eventually be replaced with electronic billing and payment alternatives. The Postal Service's 5-Year Strategic Plan for fiscal years 2001 through 2005 adopted a baseline assumption of First-Class Mail volume declining by an average of 3.6 percent annually from fiscal years 2004 through 2008 (see fig. 2). Such a decline would be significant because First-Class Mail generated 58 percent of the Service's total revenues and covered two-thirds of postal overhead costs in fiscal year 1999.

**Major Performance and  
Accountability Challenges**

**Figure 2: Postal Service Projects Decline in First-Class Mail Volume**



Source: U.S. Postal Service.

Should projected mail declines occur, one challenge for the Service would be continuing to cover its overhead costs that do not vary with mail volume—such as costs for maintaining delivery routes and post offices. The Service has warned that its planned cost reductions from its “breakthrough productivity” initiative and capital investment strategies may not be sufficient to keep future rate increases below inflation, especially for any mail categories that would assume more overhead costs as volumes decline in other mail categories.

Another challenge would be to cut mail processing and other costs that have traditionally been considered to vary with volume.

In addition to cutting costs, the Postal Service aims to increase net revenues from existing products such as Priority Mail (expedited delivery service), which is forecast to grow through fiscal year 2008 in its baseline planning scenario. The Service also aims to increase revenues from new products and services. For example, in the electronic-commerce area, which generally involves products and services provided through use of the Internet, the Service's new offerings face both traditional competitors in the delivery service sector, such as FedEx and United Parcel Service (UPS); and a broad range of competitors, such as technology companies, financial institutions, and foreign postal administrations. However, the Service's Strategic Plan has warned that no significant new revenue is forecast from new products and services during the next 5 years.

Finally, the Postal Service has noted that many forecasts suggest that the impact on the Service from electronic substitution may be even more dramatic than the Service believes. Accordingly, the Service presented a rapid diversion scenario in its Strategic Plan, in which electronic substitutes would supplant not only bill presentment and payment, but also business communications and direct mail. The Strategic Plan stated that such an outcome would threaten double-digit percentage increases in postal prices and require serious consideration of alternatives, such as revising delivery service standards, consolidating or closing some facilities, and reducing other services. Further, the Service would have to reduce its workforce at a significantly higher rate than could be absorbed through attrition or other means.

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## Control Costs and Improve Productivity

The Service has long struggled to reduce costs and increase its productivity. Adding to the difficulty of this task, the Service has experienced rising infrastructure costs of adding delivery routes and continued growth in total mail volume. Further, in 1998, the Service declared a moratorium on closing post offices and by law is not allowed to close small post offices solely for operating at a deficit. The Service has recognized that it needs aggressive cost management and anticipates the need for a “structural transformation” that is to include, among other things, achieving “breakthrough” productivity savings of \$1 billion annually. To help achieve productivity gains, the Service plans continued capital investments of over \$17 billion over the next 5 years in automation, modernization, and information technology. The Service also plans to standardize and improve work processes to reduce significant variations in quality, productivity, and costs across the system. The Service made some progress in fiscal year 2000 in controlling costs through reducing the number of workhours by 0.6 percent, which was the first such reduction since fiscal year 1992. The Service plans to further reduce workhours by 1.5 percent in fiscal year 2001.

However, as the Service has recognized, some employee-related expenses will be difficult to control. The Postal Service’s retirement-related and workers compensation expenses have increased in recent years, and these trends are expected to continue (see fig. 3). According to the Service, its retirement expenses are estimated to increase by \$554 million in fiscal year 2001 to \$9.1 billion and are projected to reach \$14.0 billion in fiscal year 2010. In addition to these costs, the Service has estimated that its retiree health benefit premiums will increase by \$114 million in fiscal year 2001 to \$858 million, and the Service has projected that these premiums will reach about \$2.0 billion in fiscal year 2010.

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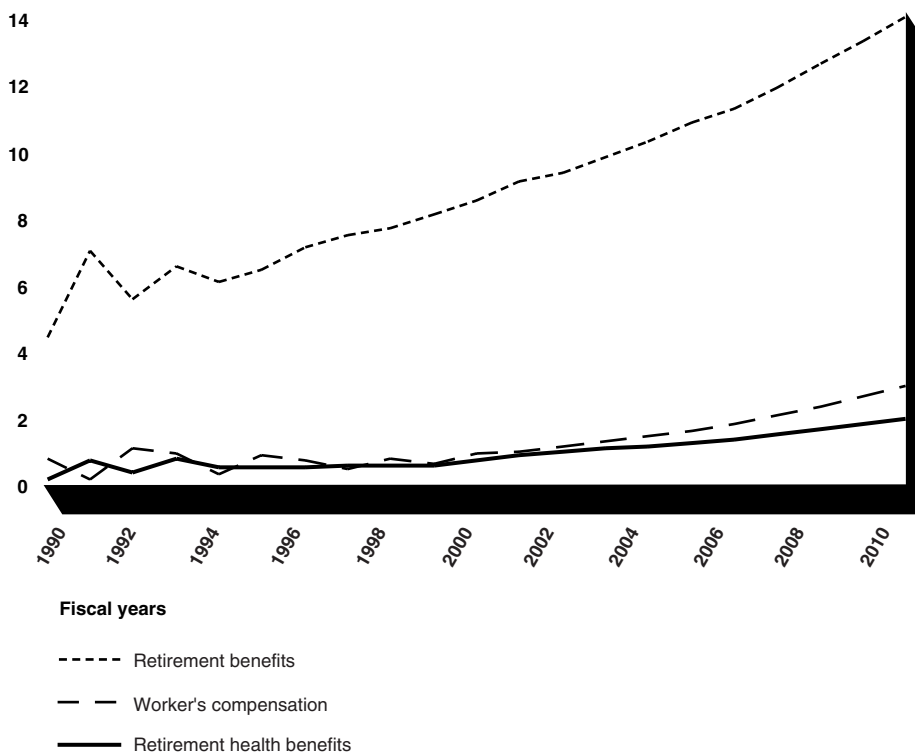
**Major Performance and  
Accountability Challenges**

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The Service is also dealing with rising workers compensation costs that have been difficult to control. According to the Service, its workers compensation expenses are estimated to increase by \$83 million to an estimated \$1.0 billion in fiscal year 2001 and are projected to increase annually to \$3.0 billion in fiscal year 2010. The Service reported making efforts to reduce workers compensation costs, such as efforts to help employees with work-related injuries or illnesses return to work. For fiscal year 2001, the Service established specific goals for improving its Occupational Safety and Health Administration (OSHA) injury/illness rate, its motor vehicle accident rate, and its safety program evaluation score.

**Figure 3: Postal Service Projects Increases in Retirement-Related Costs and Workers Compensation Costs**

16 Dollars (in billions)



Source: U.S. Postal Service.

Recent reports have identified specific opportunities for reducing costs. For example:

- In March 1999, a joint mailing industry/Postal Service operations review concluded that it had observed system inefficiencies in both postal and mailer processes that, along with other factors, had contributed to increases in the Service's costs of



handling Periodicals mail. The Service and the mailing industry have since agreed on some actions to be taken to address the recommendations of this review.

- In November 1999, we concluded that the Service still could not ensure that it is collecting all the revenue due from its business mail operations that handle about half of the Service's mail revenue. We reported the Service had made changes that were generally along the lines we recommended in 1996, and its controls over the acceptance of business mail appeared to have improved. However, we identified the need for further improvements and recommended additional steps the Service needed to take to ensure that Service business mail acceptance controls were working as intended. The Service has acted to implement the recommendations.

Stakeholders and the Service have recognized that achieving productivity gains is a key strategy to control costs. In March 2000, the Mailers Council, a coalition of mailers and mailing associations, reported that: "As a result of these factors, at a time when every competing technology is becoming less expensive, the cost of using the nation's mail system is becoming more expensive. To ensure the Service's survival, therefore, the Mailers Council believes postal management must focus its considerable skills and resources on those factors it can control, and thereby generate needed productivity gains."

Postal productivity—the relationship between the Service's outputs of delivering mail to an expanding delivery network and resources expended in producing them—increased only about 11 percent in the past three decades—despite vast changes in automation and information technology (see fig. 4). In recent years, the Service has had difficulty making improvements in postal productivity, which declined 3.3 percent from fiscal years 1993 to 1999. Although productivity

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**Major Performance and  
Accountability Challenges**

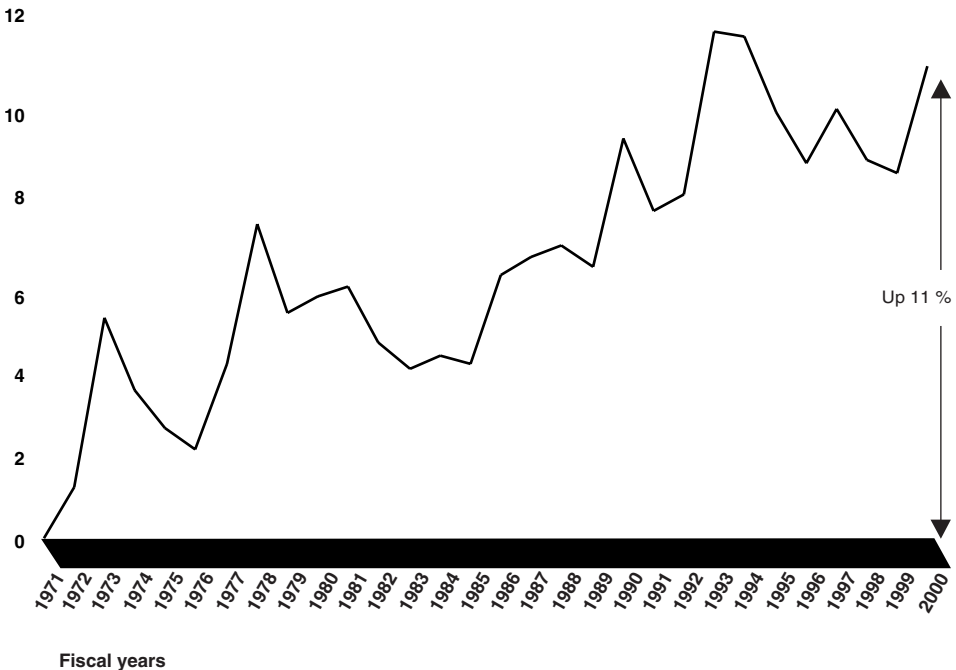
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increased by 2.4 percent in fiscal year 2000, it is expected to grow 0.7 percent in fiscal year 2001. As the Service and key stakeholders have recognized, long-term increases in its productivity will be essential in restraining postal rate increases and thus will be essential for the Service's future success.

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**Figure 4: Postal Service Productivity Growth Since Fiscal Year 1971**

14 Cumulative percentage change



Source: U.S. Postal Service.

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Address Long-  
Term Human  
Capital Issues

With more than 900,000 employees, the Postal Service faces difficult human capital challenges that include (1) restructuring the postal workforce and reducing the number of employees, (2) maintaining effective operations as most executives and about half of the postal workforce reach retirement eligibility over the next decade, and (3) ameliorating persistent problems in the workplace that have been exacerbated by decades of adversarial labor-management relations. The Service may face a major transition in each of these areas as it is increasingly affected by declining mail volumes and rising human capital costs that are difficult to control. The Service has recognized the importance of focusing on these human capital challenges by establishing the Voice of the Employee as one of its top three corporate goals and has implemented and planned a number of initiatives to deal with these challenges. However, to be successful in a competitive environment, the Service and its major unions and management associations will need to find common ground to address long-standing problems.

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Workforce  
Restructuring and  
Reductions

The Service's Strategic Plan stated that the expected decline in postal workload—in part due to automation and the implementation of information technology—“will inevitably result in both restructuring and a reduction in the workforce.” Some of the planned reductions are to be accomplished through eliminating staff vacancies and the work associated with them. In March 2000, the Postmaster General said that 11,000 career vacancies had been absorbed through attrition, and that number would reach at least 20,000 as the Service moves forward. The Service has reported other options that include using contracting services, overtime, and casual part-time employees instead of hiring new employees. However, the Service has also reported that extensive work rules and other regulations hamper its flexibility and innovation.

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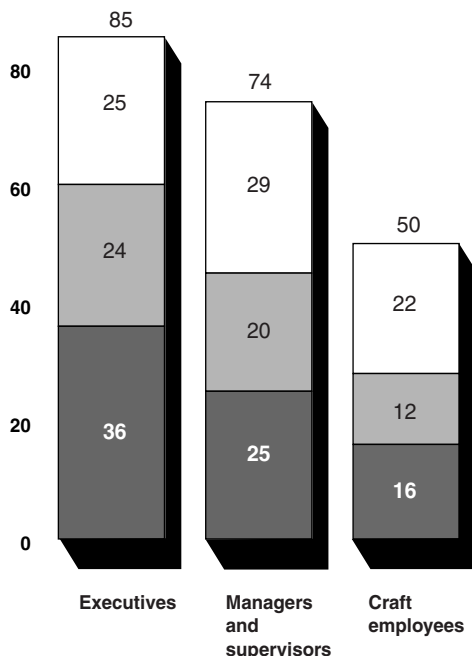
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**Retirement and  
Succession Issues**

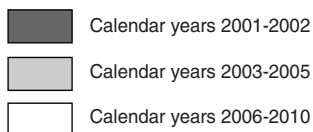
With a large percentage of the postal workforce nearing retirement eligibility, the Postal Service will be increasingly challenged to deal with succession, continuity, and associated cost issues. This challenge includes maintaining the continuity of service to customers as many experienced managers and workers retire and the Service restructures its workforce. The Service has projected that among its current employees as of October 2000, in calendar years 2001 and 2002 about 130,000 postal employees are already at or are projected to reach eligibility for regular retirement, including 36 percent of executives, 25 percent of managers and supervisors, and 16 percent of the career workforce. By calendar year 2010, 85 percent of postal executives, 74 percent of postal managers and supervisors, and 50 percent of the career workforce will reach retirement eligibility, according to Service projections (see fig. 5).

Figure 5: A Large Percentage of the Postal Workforce Is Nearing Retirement Eligibility

100 Percentage retirement-eligible



Postal workforce



Source: U.S. Postal Service.

The Service has reported it faces potentially serious succession problems in the managerial ranks. In replacing large numbers of experienced managers, the Service has said that executives, managers, and supervisors will require new and different skills from those in the past, with a premium on technical skills and

the ability to communicate with a more diverse workforce. The Service reported establishing programs for executive succession planning to develop people for corporate needs and to foster diversity among the leadership ranks, as well as programs for developing managers and first-line supervisors.

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**Address Problems  
in the Postal  
Workplace**

We have issued several reports related to the long-standing problems in the postal workplace that have been exacerbated by adversarial labor-management relations. As the Service's Strategic Plan recognized: "A solution to the need for improved workplace relations must be found if the Postal Service and the associated postal jobs are to survive in the more competitive world of the future." The Strategic Plan said that "the Postal Service has a long way to go to more effectively balance efficient management of the enterprise with the creation of a workplace that is safe and meets employee needs for dignity, respect, and opportunity." To this end, the Service has implemented a number of initiatives and established specific goals to improve the workplace environment, such as (1) improve employees' safety, security, and well-being; (2) improve workplace relations by building leadership skills and behaviors; (3) improve understanding of employee issues and concerns; and (4) ensure an inclusive and fair environment with opportunities for all employees.

Our past reports have found that postal workplace and labor-management relations problems had generally contributed to a sometimes contentious work environment and lower productivity, notably in mail processing and letter delivery operations. We have reported that the parties could not agree on common approaches for addressing the problems, which prevented them from sustaining the intended benefits of specific improvement efforts that could help improve the workplace climate. We recommended that postal management and the heads of the postal labor unions

and management associations develop a long-term framework agreement to improve the workplace environment. Although the parties have held a series of meetings, such a framework agreement has not been developed.

In other areas, however, the Postal Service reported taking a number of steps to improve the workplace environment. For example, the Service deployed a national mediation program in 1999 to resolve and expedite employee complaints at the lowest possible level. According to the Service's General Counsel, this program, called Resolving Employee Disputes, Reaching Equitable Solutions Swiftly (REDRESS), has helped to reduce the number of Equal Employment Opportunity (EEO) complaints, reversing the past trend toward more EEO complaints. In addition, the Service reached agreements with some of the unions to address specific workplace issues, such as the handling of employee grievances. Recently, the Service reported making progress in reducing the number of grievances filed by efforts such as streamlining the grievance process and placing more accountability on resolving grievances at the local level. We testified in September 2000 that as of the end of fiscal year 1999, the Service reported more than 210,000 pending or appealed grievances. By the end of fiscal year 2000, the Service reported reductions to under 147,000 pending or appealed grievances.

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**Provide Complete  
and Reliable  
Performance  
Information**

We remain concerned about the quality and transparency of the Postal Service's performance information, particularly in areas such as its e-commerce initiatives. Without complete and reliable performance data, the Service and other stakeholders cannot determine the Service's progress towards meeting its intended performance results. Postal stakeholders have also expressed considerable concern about the reliability and credibility of the Service's

ratemaking and performance data. As the Postal Service has recognized, timely, accurate, and relevant information will be critical for effective management as well as communications with customers, Congress, and other stakeholders. Although the Service has begun to take actions in this area, continued attention will be necessary to ensure that improvements are made and postal ratemaking and performance data are reliable and credible. For example:

- The Postal Service has recognized that it needs to take action to address long-standing issues related to the quality of data used in ratemaking. An April 1999 study on the quality of data used by the Service for ratemaking concluded that improvements are needed to ensure that ratemaking data will be sufficiently complete and accurate. The Postal Service has made a good start in addressing the study's recommendations by setting priorities and identifying the necessary actions and additional resources.
- Our September 2000 report found deficiencies in the financial information the Service provided for its e-commerce initiatives that raised concerns about its accuracy and completeness. In our view, these financial data were not sufficiently complete and reliable for assessing the Service's progress toward meeting its overall financial performance expectation, which is that aggregate e-commerce revenues are to cover the Service's direct and indirect costs and contribute to overhead. The Service agreed with our recommendation that it provide complete and accurate information on its e-commerce costs and revenues and said it is instituting a standard financial reporting procedure in this area.

We also recently reported that the Postal Service's annual performance plans and performance reports under the Government Performance and Results Act of



1993 might not have been as useful to Congress, postal managers, and customers as they could have been. Although we noted that the Service's fiscal year 1999 performance report contained several positive aspects, we believe that it was misleading for the performance report to highlight that the Service exceeded its targets for on-time delivery of First-Class Mail. This statement was based on performance in the second half of fiscal year 1999—excluding the peak holiday mailing season—when full-year performance showed on-time delivery met, but did not exceed, the target for overnight First-Class Mail, and was one percentage point less than the target for 2- and 3-day First-Class Mail. The usefulness of performance plans and reports depends upon their ability to communicate clearly and effectively.

We recommended, and the Service agreed, that the Service should make its future performance reports reflect straightforward and clearly stated comparisons of planned targets and results. In addition, we recommended that the Service's future performance plans should have clear criteria for measuring performance and provide more complete explanations of its goals and strategies. In response, the Service made changes that strengthened its final annual performance plan for fiscal year 2001.

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## Address Legal and Regulatory Issues

The Postal Service is challenged to operate in an uncertain legal and regulatory environment, with an ongoing debate over whether the Service should be allowed to compete with private companies and, if so, under what circumstances. For example, some private sector businesses believe that they are placed at a competitive disadvantage because the current legal framework allows the Postal Service to develop new products and enter into markets currently being served by the private sector but exempts it from some of the laws and regulations that apply to private sector

businesses. Further, some stakeholders have raised antitrust and fair competition concerns relating to current and potential alliances and partnerships involving the Service and others, including private sector companies such as FedEx. On the other hand, the Postal Service and some other stakeholders have said that current laws and regulatory oversight put the Service at a competitive disadvantage and have called for changes in the regulatory framework for setting domestic postal rates that would give the Service increased flexibility. The debate is likely to continue over whether changes are needed to federal law to ensure that the Service can continue to fulfill its mission while also ensuring fair competition.

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**Issues Relating to  
the Postal Service's  
Legal Authority and  
Regulatory  
Framework**

The long-standing debate over the Postal Service's role and what legal and regulatory system should apply to the Service has been fueled by the changing competitive environment. Since the Service was created as an independent establishment of the executive branch by the Postal Reorganization Act of 1970, it has been charged with overstepping its mandate by offering retail and service products that are claimed to be not directly related to its primary mission. These concerns have been exacerbated by vast changes in the communications and delivery sectors. When the Service was created in the early 1970s, it faced little direct competition. For example, FedEx did not exist, and the World Wide Web had not been developed. Now, the Service faces growing competition from private delivery companies, foreign postal administrations, and electronic communications alternatives. Moreover, the Service has ventured into new areas of competition by offering new electronic products and services as well as other nonpostal products, such as telephone calling cards and retail merchandise. In this context, the Service's private sector competitors and others have repeatedly raised concerns to regulatory authorities,

including the independent Postal Rate Commission, as well as to Congress.

Some competitors and others contend that the Postal Service should refrain from entering markets currently being served by the private sector and should limit its activities to providing traditional mail delivery services. In addition, some stakeholders assert that if the Postal Service is to compete in these markets, the laws should be changed so that they apply equally to the Service and its competitors. For example, some private sector businesses believe that they are placed at a competitive disadvantage because federal law exempts the Service from taxes and some of the laws and regulations that apply to private sector businesses. On the other hand, the Postal Service and some other stakeholders have said that current laws and regulatory oversight put the Service at a competitive disadvantage and have called for changes to give the Service increased flexibility. The Service has reported that its disadvantages include “heavy government oversight and regulation, significant limitations and restrictions on income, investments, pricing and employment, and many other areas including maintaining facilities in locations which are not self supporting.”

Debate continues about the Service’s role in areas that compete directly with the private sector, such as in the e-commerce area. The Postal Service, some competitors, and others have conflicting views on the extent of the Service’s legal authority to offer e-commerce products and services and under what circumstances it should offer such services. For example, the President and CEO of the Computer & Communications Industry Association recently objected to the Service offering competitive e-commerce products and services on the grounds that with an infrastructure established through taxpayer subsidies and its government-sponsored postal monopoly, the Service’s entrance into these markets would be unfair and detrimental to competition and

innovation. The Service has responded that it has an extensive history of applying the latest technology and that it makes sense to use the Internet in the same way to contribute to the accomplishment of its mission for the American people. To this end, the Service has stated that it approves only e-commerce initiatives that fit within the context of its mission and enable the Service to better serve its customers.

Another area of recent controversy has involved the application of antitrust and fair competition principles to the Postal Service's activities. For example, the Postal Rate Commission (PRC) recently considered the application of antitrust and fair competition principles to a proposed test of a postal product called Mailing Online, which allows mailers to electronically transmit material that is printed out and mailed closer to its destination. PRC found that competition and antitrust laws were relevant to its decision and concluded that Mailing Online, as recommended by the terms of PRC's decision, would not constitute unfair competition or result in an unfair competitive advantage for the Postal Service.

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**Concerns Relating  
to Postal Service  
Alliances and  
Partnerships**

Some stakeholders have raised additional antitrust and fair competition concerns relating to current and potential alliances and partnerships involving the Service and other private sector companies, such as FedEx. For example, some stakeholders, including members of Congress, have raised antitrust and fair competition concerns relating to the implications and regulatory review of a potential Postal Service alliance with FedEx that was under discussion during 2000. As of December 2000, it was unclear whether the parties would reach an alliance and, if so, what regulatory review might take place. In addition, UPS filed a formal complaint in October 1998 with PRC regarding a Postal Service electronic commerce service called PosteCS that is the product of an alliance between the Service

and the postal administrations of Canada and France. As of December 2000, this complaint remained under review.

These antitrust issues are being raised as the lines between public and private providers of postal services are blurring, with globalization of delivery services; privatization of some foreign postal administrations; and the integration of fulfillment, just-in-time logistics, and e-commerce services with traditional postal functions. For example, the German postal administration, Deutsche Post, is partially privatized, expanding globally through acquisitions in Europe and the United States, and offers a range of services including postal, express delivery, fulfillment, logistics, and e-commerce services. Also, the TNT Post Group NV of the Netherlands, a publicly traded company that includes the Dutch postal administration, has recently signed an agreement to form a global joint venture with the British and Singapore postal administrations to deliver international mail.

The Postal Service has stated that alliances and partnerships will be an important part of its strategy to grow revenues in the domestic package market. For example, the Service recently developed programs with Airborne and Emery to enable their customers to send packages to households using the Postal Service. The Service is also partnering with Mailboxes, Etc., to provide postal package services. In the international area, the Service has partnered with DHL to deliver certain packages sent abroad from the United States. Finally, the Service has also discussed a possible alliance with FedEx in which FedEx would reportedly deliver certain packages originating with the Postal Service, while the Service would reportedly deliver certain FedEx packages to their final destination.

More broadly, one recent study of the parcel service industry in the United States concluded that the traditional structure of governmental policymaking, planning, and regulation is increasingly mismatched to the freight transportation system. The study noted that parcel delivery services have grown to be a major player in the transportation field, as large or larger than most of the major traditional elements of the freight transportation system—airlines, pipelines, railroads, etc. According to the study, parcel delivery services exemplify the trend to integrating different transportation modes to meet different speed and other service requirements. For government, the study found that policies and programs based on the older modal view of transportation will need to change to take this trend into account and to adapt to the changing landscape of globalization, mass customization, and rapid customer response.

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**Issues Involving  
Regulation of Postal  
Rates**

Congress, the Postal Service, some competitors, and other stakeholders have debated whether changes are needed in the regulatory framework for setting domestic postal rates and, if so, what changes should be made. The Postal Service has called for changing the laws establishing the regulatory framework for changing rates for existing domestic postal products as well as establishing rates for new postal products. The Service has long contended that it has been hampered by lack of flexibility to set prices and by a lengthy postal ratemaking process. The Postmaster General has called regulatory reform “an absolute requirement,” saying that “we are going to wind up with an inferior Postal Service in the future if we do not change the regulatory environment.”

The Service cannot change its prices for existing domestic postal products or establish rates for new domestic postal products without prior regulatory review. Under the current ratemaking process, the

Service is required to file a request with PRC for a recommended decision on proposed changes in rates for domestic postal services. PRC decisions and actions must be based on evidentiary records developed in administrative hearings that are quasi-judicial and adversarial in nature. All interested parties, including the Service's competitors, have the opportunity to examine the Service's proposals and express their views. PRC is required to issue a recommended decision to the Service's Board of Governors on proposed rates within 10 months, and the Board of Governors makes the final decision.

Although the Postal Service, some mailer groups, and others have called for changing the current process of regulating postal rates to give the Service greater flexibility, some stakeholders, such as UPS and the Newspaper Association of America, have expressed concern about giving the Postal Service, a government entity with monopoly powers, additional pricing flexibility. Both have said that PRC's authority needs to be strengthened under the current ratesetting process.

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**The Continuing  
Debate Over the  
Legal and  
Regulatory  
Framework**

Fundamental issues concerning the Postal Service's role and authority have been raised in Congress, and various stakeholders have called for changing its legal and regulatory framework. Key questions that have been raised, and are likely to persist, include:

- What are the appropriate mission and role of the Postal Service? Should "universal postal service" be defined and, if so, how? Should the Service be privatized? Should the postal monopoly be narrowed or ended?
- Should the Postal Service be allowed to compete in areas served by the private sector and, if so, under what circumstances? To what extent should the Service be subject to the same laws as its competitors?

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**Major Performance and  
Accountability Challenges**

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- What should be the related regulatory framework providing oversight in the areas of pricing, new postal products, and fair competition? How should PRC and other pertinent regulatory authorities exercise oversight with respect to competition and antitrust issues?

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