OVERSIGHT OF THE U.S. POSTAL SERVICE

HEARING

BEFORE THE

SUBCOMMITTEE ON THE POSTAL SERVICE

OF THE

COMMITTEE ON
GOVERNMENT REFORM

HOUSE OF REPRESENTATIVES

ONE HUNDRED SIXTH CONGRESS

FIRST SESSION

OCTOBER 21, 1999

Serial No. 106–110

Printed for the use of the Committee on Government Reform

Available via the World Wide Web: http://www.gpo.gov/congress/house
http://www.house.gov/reform

OVERSIGHT OF THE U.S. POSTAL SERVICE

OVERSIGHT OF THE U.S. POSTAL SERVICE

OVERSIGHT OF THE U.S. POSTAL SERVICE

OVERSIGHT OF THE U.S. POSTAL SERVICE

OVERSIGHT OF THE U.S. POSTAL SERVICE

OVERSIGHT OF THE U.S. POSTAL SERVICE

OVERSIGHT OF THE U.S. POSTAL SERVICE

HEARING

BEFORE THE

SUBCOMMITTEE ON THE POSTAL SERVICE

OF THE

COMMITTEE ON
GOVERNMENT REFORM

HOUSE OF REPRESENTATIVES

ONE HUNDRED SIXTH CONGRESS

FIRST SESSION

OCTOBER 21, 1999

Serial No. 106–110

Printed for the use of the Committee on Government Reform

Available via the World Wide Web: http://www.gpo.gov/congress/house
http://www.house.gov/reform

U.S. GOVERNMENT PRINTING OFFICE

63–821 CC WASHINGTON : 2000

COMMITTEE ON GOVERNMENT REFORM

DAN BURTON, Indiana, *Chairman*

BENJAMIN A. GILMAN, New York
CONSTANCE A. MORELLA, Maryland
CHRISTOPHER SHAYS, Connecticut
ILEANA ROS-LEHTINEN, Florida
JOHN M. MCHUGH, New York
STEPHEN HORN, California
JOHN L. MICA, Florida
THOMAS M. DAVIS, Virginia
DAVID M. MCINTOSH, Indiana
MARK E. SOUDER, Indiana
JOE SCARBOROUGH, Florida
STEVEN C. LATOURETTE, Ohio
MARSHALL "MARK" SANFORD, South Carolina
BOB BARR, Georgia
DAN MILLER, Florida
ASA HUTCHINSON, Arkansas
LEE TERRY, Nebraska
JUDY BIGGERT, Illinois
GREG WALDEN, Oregon
DOUG OSE, California
PAUL RYAN, Wisconsin
HELEN CHENOWETH-HAGE, Idaho
DAVID VITTER, Louisiana

HENRY A. WAXMAN, California
TOM LANTOS, California
ROBERT E. WISE, JR., West Virginia
MAJOR R. OWENS, New York
EDOLPHUS TOWNS, New York
PAUL E. KANJORSKI, Pennsylvania
PATSY T. MINK, Hawaii
CAROLYN B. MALONEY, New York
ELEANOR HOLMES NORTON, Washington, DC
CHAKA FATTAH, Pennsylvania
ELIJAH E. CUMMINGS, Maryland
DENNIS J. KUCINICH, Ohio
ROD R. BLAGOJEVICH, Illinois
DANNY K. DAVIS, Illinois
JOHN F. TIERNEY, Massachusetts
JIM TURNER, Texas
THOMAS H. ALLEN, Maine
HAROLD E. FORD, JR., Tennessee
JANICE D. SCHAKOWSKY, Illinois

BERNARD SANDERS, Vermont (Independent)

KEVIN BINGER, *Staff Director*
DANIEL R. MOLL, *Deputy Staff Director*
DAVID A. KASS, *Deputy Counsel and Parliamentarian*
CARLA J. MARTIN, *Chief Clerk*
PHIL SCHILIRO, *Minority Staff Director*

SUBCOMMITTEE ON THE POSTAL SERVICE

JOHN M. MCHUGH, New York, *Chairman*

MARSHALL "MARK" SANFORD, South Carolina
BENJAMIN A. GILMAN, New York
STEVEN C. LATOURETTE, Ohio
DAN MILLER, Florida

CHAKA FATTAH, Pennsylvania
MAJOR R. OWENS, New York
DANNY K. DAVIS, Illinois

EX OFFICIO

DAN BURTON, Indiana

HENRY A. WAXMAN, California

ROBERT TAUB, *Staff Director*
HEEA VAZIRANI-FALES, *Counsel*
JANE HATCHERSON, *Professional Staff Member*
ABIGAIL D. HUROWITZ, *Clerk*
DENISE WILSON, *Minority Professional Staff Member*

CONTENTS

	Page
Hearing held on October 21, 1999	1
Statement of:	
Corcoran, Karla W., Inspector General, U.S. Postal Service, accompanied by Thomas Coogan, legal counsel; and Richard Chambers, Assistant Inspector General for Audit, U.S. Postal Service	8
Henderson, William J., Postmaster General and Chief Executive Officer	115
Ungar, Bernard L., Director, Government Business Operations Issues, U.S. General Accounting Office, accompanied by Teresa Anderson, Assistant Director; and Gerald Barnes, Assistant Director, U.S. General Accounting Office	33
Letters, statements, et cetera, submitted for the record by:	
Corcoran, Karla W., Inspector General, U.S. Postal Service:	
Followup questions and responses	78
Prepared statement of	12
Henderson, William J., Postmaster General and Chief Executive Officer:	
Followup questions and responses	134
Prepared statement of	117
LaTourette, Hon. Steven C., a Representative in Congress from the State of Ohio, June 30, 1999, Report to Congress	412
McHugh, Hon. John M., a Representative in Congress from the State of New York, prepared statement of	4
Ungar, Bernard L., Director, Government Business Operations Issues, U.S. General Accounting Office:	
Followup questions and responses	108
Prepared statement of	36

OVERSIGHT OF THE U.S. POSTAL SERVICE

THURSDAY, OCTOBER 21, 1999

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON THE POSTAL SERVICE,
COMMITTEE ON GOVERNMENT REFORM,
Washington, DC.

The subcommittee met, pursuant to notice, at 10:10 a.m., in room 2154, Rayburn House Office Building, Hon. John M. McHugh (chairman of the subcommittee) presiding.

Present: Representatives McHugh, Sanford, LaTourette, Miller, Fattah, Owens, and Davis.

Staff present: Robert Taub, staff director; Heea Vazirani-Fales, counsel; Jane Hatcherson, professional staff member; Abigail D. Hurowitz, clerk; Denise Wilson, minority professional staff member; and Earley Green, minority staff assistant.

Mr. MCHUGH. Good morning. The hearing will come to order. On behalf of the subcommittee members, I'm pleased to welcome everyone here as we continue the oversight agenda for the 106th Congress.

Let me begin by saying to those who have suggested our Postal Service ain't broke, I think today's GAO testimony will serve as a wake-up call as we will hear GAO explain first class mail volume is expected to decline at an average annual rate of 2.5 percent in fiscal years 2003 to 2008. Such a decline would be unprecedented. Let me say that again. Unprecedented in the Service's history and will likely create severe financial and performance challenges. According to the Postmaster General, not only will this erosion place nearly $17 billion of total revenue at risk, but even worse, the Service's environment is changing so rapidly that we simply can't predict precisely when or to what extent competitive pressures may affect the Service's revenues. As a postal commentator by the name of Gene Del Polito recently quipped, "In today's world, Internet years are more akin to dog years than the Julian calendar."

So indeed we need to take heed when the GAO states again, "The Postal Service may be nearing the end of an era." Irrespective of Congress's progress in modernizing the Nation's postal laws, it is clear that these developments make it imperative for the Postal Service to resolve long-standing performance challenges that will be detailed by our first panel of witnesses.

Our first panel today will include Ms. Karla Corcoran, the Postal Service's Inspector General, and Mr. Bernard Ungar, the Director of Government Business Operations Issues for the General Accounting Office. Both the IG and GAO are on the front lines as America's postal watchdogs, and they have proven to be valuable

partners with the subcommittee in reporting to us on a broad range of postal operations. Although the GAO has been evaluating postal operations since the days of the Post Office Department, the Inspector General is still a relatively new player on the post scene. Unlike every other major Federal agency, when it came to the Postal Service, the American public did not have the benefit of the oversight provided by an independent Inspector General. Fortunately, in my opinion, we remedied that problem in 1996 when we enacted legislation to create the postal IG.

In that regard, the subcommittee certainly looks forward to hearing from Ms. Corcoran on the progress of establishing her office since her last presentation to this subcommittee in 1998. It is important that the American postal consumer be assured that the Inspector General has the necessary staff and resources to vigorously carry out all of her responsibilities under the IG Act. With a budget of some $62 billion and nearly 900,000 employees, the Postal Service rivals only the Department of Defense as the largest Federal agency. It would thus seem appropriate that the postal IG's budget would be comparable to the budgets of the Offices of Inspector General within the Department of Defense and other such agencies. I look forward to Ms. Corcoran's update on this matter today.

It is important as well to note that both the IG and the GAO have identified a number of initiatives that the Postal Service could undertake to improve its own performance. I look forward to Ms. Corcoran and Mr. Ungar highlighting these initiatives, especially the extent to which the Service has followed up on the questions raised by the IG and GAO in reports to Congress. Further, they have a number of assignments pending. I hope Ms. Corcoran and Mr. Ungar can report to us on the status of these assignments and the impact these reports will have in assessing the productivity and the efficiency of the Postal Service.

Our second panel consists of a single, yet a very important, individual, the Postmaster General, Mr. William Henderson. As Mr. Henderson notes in his written statement, mail delivery scores and net income appear today to be fine. However, he also underscores that the Postal Service faces considerable challenges in sustaining its current performance in maintaining a competitive role in providing mail service to the American public in the future. As both the IG and the GAO have found, the Postal Service requires significant attention to such areas as labor-management relations, internal controls, and revenue protection. The subcommittee looks forward to hearing Mr. Henderson's plans to develop innovative and workable solutions to these and other problems facing the Postal Service.

While today's hearing is not specifically devoted to initiatives regarding reform, the GAO's message makes clear that time appears to be growing short for the Postal Service to successfully address these challenges. Unless the Service can adopt to a rapidly changing communications environment and growing competition, we are facing a major crisis in the postal sector. Inevitably the issues of modernizing our postal laws will prove inherent in evaluating the operations of the Postal Service itself, and the subcommittee is interested in hearing Mr. Henderson's assessments of developments in the reform debate.

We thank all three of our panels of witnesses here today for joining with us.

With that, I would be happy to yield to the distinguished ranking member for any comments he may wish to make at this time.

[The prepared statement of Hon. John M. McHugh follows:]

Statement of the Honorable John M. McHugh, Chairman
Subcommittee on the Postal Service
Oversight Hearing - October 21, 1999

Good morning. The hearing will come to order. On behalf of the Subcommittee members, I am pleased to welcome everyone here as we continue our oversight agenda for the 106th Congress.

For those who have long suggested that our postal system "ain't broke," today's GAO testimony should be a wake-up call. As we will hear GAO explain, First-Class mail volume is expected to decline at an average annual rate of 2.5 percent in fiscal years 2003 to 2008. Such a decline would be unprecedented - let me reiterate the word *unprecedented* - in the Service's history and would likely create severe financial and performance challenges. According to the Postmaster General, not only will this erosion place nearly $17 billion of total revenue at risk, but even worse, the Service's environment is changing so rapidly that we cannot predict precisely when or to what extent competitive pressures may affect the Service's revenues. As postal commentator Gene Del Polito recently quipped, "In today's world, Internet years are more akin to dog years than the Julian calendar."

So indeed, we must take heed when the GAO states that "the Postal Service may be nearing the end of an era." Irrespective of Congress's progress in modernizing the nation's postal laws, it is clear that these developments make it imperative for the Postal Service to resolve the longstanding performance challenges that will be detailed by our first panel of witnesses.

Our first panel today will include Ms. Karla Corcoran, the Postal Service's Inspector General, and Mr. Bernard Ungar, Director of Government Business Operations Issues for the General Accounting Office. Both the IG and GAO are on the front lines as America's postal watchdogs, and they have proven to be valuable partners with the Subcommittee in reporting to us on a broad range of postal operations. Although the GAO has been evaluating postal operations since the days of the Post Office Department, the Inspector General is a relatively new player on the postal scene. Unlike every other major federal agency, when it came to the Postal Service, the American public did not have the benefit of the oversight provided by an independent Inspector General. We remedied that problem in 1996 when we enacted my legislation to create the postal IG.

In that regard, the Subcommittee looks forward to hearing from Ms. Corcoran on the progress of establishing her office since her testimony last year. It is important that the American postal consumer be assured that the Inspector General has the necessary staff and resources to vigorously carry out all of her responsibilities under the IG Act. With a budget of $62 billion and nearly 900,000 employees, the Postal Service rivals the Department of Defense as the largest federal agency. It would thus seem appropriate that the postal IG's budget would be comparable to the budget for the Offices of Inspector General within the Department of Defense. I look forward to Ms. Corcoran's update on this matter today.

It is important to note that both the IG and GAO have identified a number of initiatives that the Postal Service could undertake to improve its own performance. I look forward to Ms. Corcoran and Mr. Ungar highlighting these initiatives, especially the extent to which the Service

(more)

PRINTED ON PAPER MADE WITH RECYCLED FIBERS

has followed up on the questions raised by the IG and the GAO in reports to Congress. Further, they have a number of assignments pending. I hope Ms. Corcoran and Mr. Ungar can report to us on the status of these assignments and the impact these reports will have in assessing the productivity and efficiency of the Postal Service.

Our second panel consists of Postmaster General William Henderson. As Mr. Henderson notes in his written statement, mail delivery scores and net income appear to be fine. However, he also underscores that the Postal Service faces considerable challenges in sustaining its current performance and maintaining a competitive role in providing mail service to the American public in the future. As both the IG and the GAO have found, the Postal Service requires significant attention to such areas as labor-management relations, internal controls, and revenue protection. The Subcommittee looks forward to hearing Mr. Henderson's plans to develop innovative solutions to these and other problems confronting the Postal Service.

While today's hearing is not specifically devoted to reform issues, the GAO's message makes clear that time appears to be growing short for the Postal Service to successfully address its challenges. Unless the Postal Service can adapt to a rapidly changing communications environment of growing competition, we are facing a major crisis in the postal sector. Inevitably, the issue of modernizing our nation's postal laws will prove inherent in evaluating the operations of the Postal Service, and the Subcommittee is interested in hearing Mr. Henderson's assessments of developments in the reform debate.

###

Mr. FATTAH. Thank you, Mr. Chairman. I'm pleased to join you today for a general oversight hearing on the U.S. Postal Service and in welcoming our distinguished panelists.

Our focus on the Postal Service is timely. Two days ago the House Subcommittee on Regulatory Reform and Paperwork Reduction held a hearing on the U.S. Postal Service regulations regarding commercial mail receiving agencies. Last week the Postal Service Office of Inspector General released some 51 reports and agreed to savings of over $1.1 billion. A number of these reports, six to be exact, address the treatment of postal workers by their supervisors.

As a member of the subcommittee concerned, as we all are, with labor-management issues, I can tell you I'm concerned about the state of affairs at the Postal Service, particularly as it impacts better workplace relations. With over 826,000 employees, the Postal Service must move forward with real improvement in the way it treats its employees and improving labor-management relations.

Two weeks ago our staff was briefed by the Postal Service about e-commerce initiatives. The Postal Service is very interested in having every household connected to an e-mail address. This foray into e-commerce must first grapple with a report just issued by the IG on computer security within the Postal Service. The report identified many significant weaknesses in computer security. As the IG states, "the backbone of any successful e-commerce program must be built upon a secure and trustworthy computer network. Addressing deficiencies and shortcomings in the Postal Service's own computer system obviously must come first."

Diversity and equal employment opportunity are two issues I am most interested in seeing resolved. To that end, I've asked the GAO to review and report back to this subcommittee the progress of the Postal Service in achieving diversity in the Postal Career Executive Service. These are senior, high-level, high-paying positions which must adequately reflect the diversity of the work force.

With regards to OSHA, in the 105th Congress we enacted the Postal Employee Safety Enhancement Act. The Postal Service can now be cited, fined, and referred for criminal prosecution by OSHA for health and safety violations. Are postal facilities safe? Is the Postal Service in compliance with OSHA? I believe my colleagues on this subcommittee will agree that all postal employees deserve a safe working environment. I look forward to exploring this issue further with the IG and with the Postmaster General.

Recently, we have been hearing rumblings that a postal rate increase is looming. I just got used to paying 33 cents for a stamp. I wish to examine how, given enormous profits touted by the Postal Service, how we can be in a position again to face an increase in the price of a postage stamp. The dialog on this matter must continue.

Mr. Chairman, I can raise further issues forever. Suffice it to say that the general oversight of the Postal Service could not have come at a better time. I wish to thank the IG and the GAO for their time and reports and willingness to explore new issues and to find problems. I look forward to hearing how the Postal Service will tackle its current challenges and better position itself. Thank you.

Mr. MCHUGH. I thank the gentleman.

Any other Members seeking recognition at this time?

Mr. Davis.

Mr. DAVIS. Thank you very much, Mr. Chairman, and I want to thank you for convening this hearing regarding oversight of the U.S. Postal Service. Today's hearing is timely and very important. In fact, this is our second hearing concerning the Postal Service and its operations this Congress.

There are a number of issues that have emerged since our last oversight hearing. Among those issues include a report issued by the General Accounting Office concerning diversity within EAS 17 and above positions. In addition, there have been serious complaints and concerns regarding the number and amount of advertising dollars that are spent with small business vendors and in minority communities.

The diversity issue is one that concerns me greatly, and making sure that minorities and women are represented at every level of the Postal Service must continue to be a priority. In addition, ensuring the minorities and women receive an adequate share of contracts must continue to remain high.

Recently I had the opportunity to address a diversity forum sponsored by the Postal Service. At that forum were managers and senior managers discussing the importance of diversity. The Postal Service has been moving in the right direction with regard to this issue, and I want to commend them for that and urge that we continue with this progress.

The question of advertising dollars and how they are spent concerns me. I requested the Congressional Research Service provide to me a breakdown of the total advertising budget for the Postal Service and how it is spent. In particular, I wanted to see what dollars were being spent in what communities and with minority vendors. I was told by CRS that the Postal Service did not have such a breakdown. Now, if that is true, I would like for us to move in the direction of seeing how we can put one together. This is a question that I posed with the Census Bureau not long ago, and we were successful in passing an amendment that would target advertising dollars to minority communities and with minority vendors. I will be interested in hearing the Postal Service's views on this issue.

Finally, I, too, am concerned about the article that appeared in the USA Today newspaper yesterday that suggested that first-class mail could be in jeopardy by the year 2003 because of advances in technology and more people paying bills via e-commerce. The article also went on to say that the Postal Service could lose more than $17 billion in revenue over the next decade due to e-commerce. I'm interested in knowing what plans are being made to ensure the long-term competitiveness and viability of the Postal Service to continue providing universal service. I look forward to hearing GAO's full analysis of this issue, and again, Mr. Chairman, I thank you for convening this hearing and look forward to hearing all of the witnesses.

Mr. MCHUGH. I thank the gentleman for his comments.

I know his question relates to what the Postal Service is doing because the Postal Subcommittee has been working on H.R. 22 for 5 years. I just wanted to make sure we understood that.

Let me now call forward our first panel. Karla Corcoran, the Inspector General of the U.S. Postal Service, who, I understand—if you'd just please come up while I'm doing your introductions—who, I understand, is accompanied by Mr. Thomas Coogan, who is a legal counsel for the IG, and Richard Chambers, who is Assistant Inspector General for Audit, and also Bernard L. Ungar, the Director of the Government Business Operations Issues Office of the U.S. General Accounting Office, who, I understand, is accompanied by Teresa Anderson, Assistant Director, and Gerald Barnes, also Assistant Director. You can see they're veterans because they have not been seated, and they know they have to take the oath.

[Witnesses sworn.]

Mr. MCHUGH. The record will show that all of the witnesses responded to the oath in the affirmative. And again, once more, we welcome you all here. Thank you for joining us.

Starting from right to left because why not. Why don't we start with the Inspector General, and we do have your written testimony. I have read all of the testimony today in its entirety. It was all very interesting, and all of that will be submitted in its entirety for the record. We now turn our attention to you for your personal comments today.

STATEMENT OF KARLA W. CORCORAN, INSPECTOR GENERAL, U.S. POSTAL SERVICE, ACCOMPANIED BY THOMAS COOGAN, LEGAL COUNSEL; AND RICHARD CHAMBERS, ASSISTANT INSPECTOR GENERAL FOR AUDIT, U.S. POSTAL SERVICE

Ms. CORCORAN. Thank you, Mr. Chairman.

Chairman McHugh, Congressman Fattah and members of the subcommittee, I'm pleased to be here today to discuss with you the progress of the OIG and what we've seen as we started looking at the Postal Service. Joining me are my counsel, Tom Coogan, and my Assistant Inspector General for Audits Richard Chambers. With your permission, I'm going to ask that we enter the full statement into the record.

Mr. MCHUGH. Without objection.

Ms. CORCORAN. As you know, this is our third year as an independent Inspector General within the Postal Service. In the first year, we spent most of our time creating a separate mission from the Inspection Service. Our second year, we focused on hiring and initiating audits and investigations. You might be interested in knowing that we've identified over 1,000 projects that we believe need to be done within the Postal Service. And this is our third year we have spent reviewing key postal programs.

We are a new organization by almost any standard. However, we have numerous accomplishments and have made remarkable progress. In the last 6 months alone, we've issued over 100 reports with $1.1 billion, that's a B for billion, in savings and cost avoidance over the next several years. We have 190 ongoing investigations. Our investigations have yielded 17 criminal charges and $2.1 million in fines and recoveries. We also have proactive investigations that are targeting fraud and corruption.

In the last 6 months, our office has grown from 178 to 400—I'm sorry, in the last 18 months our office has grown from 178 to 400 and from four offices to six offices. With the Governor-approved

budget for year 2000, we will grow to 648 staff. We will have 5 additional offices for a total of 11 offices. I'm very excited about our diversity statistics. Our staff consists of 43 percent women and 42 percent minorities.

Each year the Inspector General community recognizes outstanding accomplishments within the community. I'm proud to say that this year, in fiscal year 1999, we received a total of eight Executive Council on Integrity and Efficiency Awards. This included four awards for excellence for our work in Y2K, labor-management, and developing a computer intrusion course for the entire community. This is the most awards received by any Inspector General within the community.

Today I'd like to highlight for you the work we have done in five areas. Those areas are performance, technology, financial management, labor-management, and oversight of the Inspection Service.

In the first area of performance, we have conducted 49 reviews of critical core business areas within the last 18 months. In the Corporate Call Management area, we identified nearly $1 billion in cost avoidances over the next several years by changing technology. In the transportation area, we issued two reviews identifying over $150 million in savings over a 5-year period. These were in the highway transportation contract area and the rail detention management area.

We also looked at the Priority Mail Processing Center. We found that the contractor network had not significantly improved on-time delivery, yet it cost $100 million more than processing that mail in-house.

Our investigators identified in the international arena as much as $20 million in revenue that could have been collected. However, the Postal Service had negotiated lower international rates even though the mail was processed totally within the United States.

We've also performed work in the environmental area. We reviewed Postal Service's use of natural gas vehicles, and found that these vehicles have been placed in areas where there is no supply of natural gas.

In the second area, technology, as you know, we have focused much of our work over the last 18 months in the Y2K area. We've issued nine reports. We testified before a joint committee subcommittee hearing in February. At that time we said Postal had a lot of work to do to be ready. Since then, with our assistance, Postal has made tremendous progress. However, challenges remain. In our latest report on Business and Continuity Plans, we identify many of our concerns about their plans and the testing of those plans.

In addition, in the technology area, we are doing work in electronic commerce, computer intrusion, and developmental projects.

We are also doing work in the financial management area. We include contracting and facilities in this area. We've done a total of 31 reports over the last 18 months.

In the Dinero Seguro money transfer program, we identified ways to reduce the risk of money laundering. You asked us, Mr. Chairman, whether the indictment of Postal Service's Mexican business bank partner would jeopardize the integrity of the program. We said that it would not. However, as a result of our re-

view, we did identify a previously unknown scheme, whereby drug traffickers would wire drug proceeds to Mexico. By partnering with other Federal agencies, we have made five arrests, and seized 25 kilograms of marijuana and 3 kilograms of cocaine.

The Postal Service purchases over $8 billion of goods and services each year. Therefore, we've done quite a bit of work in the contracting area, much of it for Congressman Fattah. For example, one of the reviews we have done is to look at why there has been a decline in minority contracting. In another review, we recommended that three contractors for the Postal Service be suspended and/or debarred for various improprieties.

Postal Service has 38,000 facilities. This makes Postal one of America's largest owners, developers, and managers of real estate. At your request, Mr. Chairman, we reviewed the Olympic facilities in Atlanta. We found that inappropriate approval and oversight had cost at least $9 million more than their original projections.

Postal Service has identified labor-management as key to achieving their goals into the 21st century. This has been one of the toughest areas for us to address, first, because of the sheer magnitude of complaints we have received—over 2,500 individual complaints. Second, this is an area that we get push back from management. We have more recommendations that have not been agreed to in this area than in any other area.

We're also extremely concerned about retaliation against employees that have assisted or worked with the OIG. Whenever we have allegations that employees are being retaliated against for working with the OIG, we immediately review them. We have 11 current investigations in this area under way, and 3 that we have completed.

In the labor-management area, we focus on systemic reviews. In the last 18 months we've done 30 reports and 60 congressionals. A major report in this area has been to look at the threat assessment program. We have found that violence prevention and response policies within the Postal Service have not been followed in three districts. We are extending that review now to look at 26 additional districts so that we can make Postal-wide recommendations for improvement.

The last area that I'd like to talk to you about is oversight of the Inspection Service. As you well know, that is one of the principal reasons why an independent Inspector General was created within the Postal Service. We have done 18 Inspection Service reports. These include crime lab certification, abuse of authority, and disciplinary actions. At your request, Mr. Chairman, we reviewed the classification of postal inspectors performing audits. We found that 250 inspectors who were performing audits were not spending at least 50 percent of their time in law enforcement as required by the Office of Personnel Management. The Inspection Service has agreed with our findings and has told us that they will no longer perform "Yellow Book" audits.

This will have a major impact on the OIG. We currently are reviewing this with a task force, and we will be getting back with the Governors and you to let you know what impact this will have on us.

One of our greatest challenges is continuing to develop effective relationships with the Inspection Service. I'm looking forward to working with the new Chief Inspector. We both have the same goal of improving postal operations. We have agreed to renew teambuilding to increase communication, trust, and coordination.

In summary, I'd like to thank you for allowing us to serve the Postal Service. We have been a truly independent voice and a venue for all stakeholders to confidentially report allegations. We have delivered objective information and analysis of postal programs, and we have provided greater economy, efficiency, and integrity to Postal Service programs. I look forward to continuing to serve you and the Postal community. This concludes my statement. I'd be pleased to answer any questions.

Mr. MCHUGH. Thank you very much both for your statement here today and, as I've mentioned earlier, your service over the past 3 years.

[The prepared statement of Ms. Corcoran follows:]

Statement of
Karla W. Corcoran
Inspector General
United States Postal Service
before the
Subcommittee on the Postal Service
Committee on Government Reform
U.S. House of Representatives
October 21, 1999

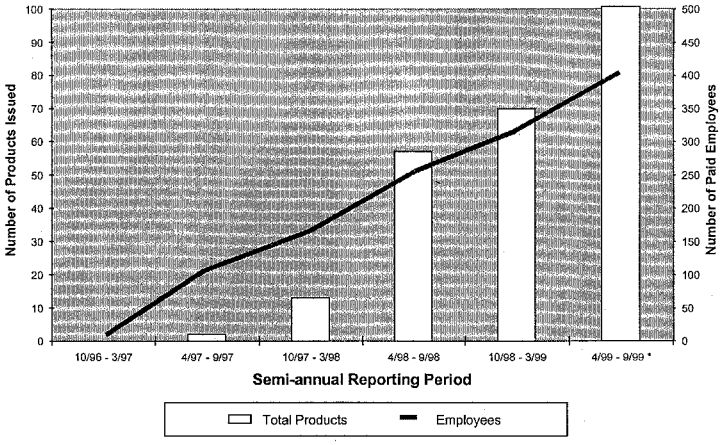
Chairman McHugh, Congressman Fattah, and Members of the Subcommittee, I am pleased to appear before you today to provide the Subcommittee with my perspective on current operations within the US Postal Service. Much of this perspective was gained during the audits, investigations, and other work performed by the Office of Inspector General since I testified before you in June 1998. In addition, I will provide a synopsis of the progress we have made in establishing our office, and some of the challenges that we face.

Joining me today are: Thomas Coogan, Legal Counsel, and Richard Chambers, Assistant Inspector General for Audit. With your permission, I would like to submit my full statement for the record.

Mr. Chairman, as you are aware, this is our third year as an independent Office of Inspector General within the Postal Service. In our first year, we established a separate mission from the Inspection Service, crafted a budget, developed a strategic plan, and drew up our initial organization plans. In our second year, we focused our efforts on hiring, identifying the universe of Postal operations and activities, and initiating audits and investigations. In this our third year, we have concentrated our efforts on reviews of key Postal Service programs, initiatives, and activities.

Our progress in hiring employees and accomplishing projects is illustrated in the following chart.

Staffing and Reporting Trends



Even though we still might be considered a fledgling organization by many standards, I am proud to report to you that we have achieved numerous accomplishments and made remarkable progress since my June 1998 testimony. In the last six months alone, we issued over 100 reports, including audits, investigations, management advisories, and Congressionals, with agreed-to monetary benefits of over $1.1 billion. We currently have over 190 ongoing investigations. Our investigations have yielded five arrests, seven indictments, five convictions, and $2 million in civil case recoveries, as well as over $100,000 in fines and restitution. In addition, we initiated proactive investigative projects targeting fraud and corruption in various areas.

IMPACT OF OFFICE OF INSPECTOR GENERAL ON POSTAL SERVICE OPERATIONS

One of the principal missions of this OIG is to improve the Postal Service's operations by providing timely and reliable information to its management. We

have provided Postal management with recommendations to improve Postal Service operations in five critical areas: performance, technology, financial management, labor relations, and Inspection Service oversight and other significant issues.

A. Performance

Ultimately, no business or government agency can be truly successful unless it excels in all of its core business processes. For the Postal Service, these core business processes involve accepting, processing, transporting, and delivering the mail, and marketing Postal products. During the past 18 months, we have completed 49 reviews in these critical core business areas. These reviews:

- Identified potential cost avoidance of nearly $1 billion in the Corporate Call Management program as a result of technology changes which will allow the Postal Service to handle the projected call volume without adding two additional planned sites.

- Determined that Postal Service could save over $100 million through better contract administration and oversight of highway transportation emergency and extra trip expenditures.

- Identified savings of nearly $50 million in rail detention costs by ensuring that facilities management does not use trailers to augment highway trailer fleets and store equipment, by considering the detention status of trailers before making dispatch decisions, and by seeking reimbursement for detention caused by mailers.

- Determined that a telecommunications contractor had subcontractors who billed for services not rendered, and provided incomplete and

defective work. Through our efforts, the Postal Service has recovered $2 million from the subcontractors thus far.

- Established that processing mail through the contractor-operated Priority Mail Processing Center Network did not significantly improve on-time delivery performance but did cost the Postal Service $101 million, or 23 percent, more than to process it in-house.

- Concluded that volume data for bulk mail centers was not accurate.

- Found that the International Business Unit did not have key processes in place to achieve projected revenue goals and that some initiatives fell short of revenue projections.

- In one international mail case, the Postal Service did not collect nearly $20 million in revenue because the Postal Service charged a lower negotiated international rate for mail actually processed completely as domestic mail.

These reviews highlight but a few of the issues facing the Postal Service. They raise questions about process integrity, data reliability, the accuracy of revenue projections, and achievement of service delivery and performance goals. We will continue to address these and other similar issues in reviews planned for this fiscal year and beyond.

B. Technology

The Postal Service depends on technology to deliver more than 650 million pieces of mail every day, maintain its network of over 38,000 post offices and facilities, and pay its more than 800,000 career employees. For just the Information Systems portion of the technology area alone, the Postal Service budgeted almost $1 billion in Fiscal Year 1999, not including budgets for all

technology-dependent equipment, systems, and initiatives. The Postal Service recognizes that technology is critical to its future and, therefore, its technology strategy is to provide convenient access to every customer, everywhere, every day, by fielding smarter retail systems, expanding into new electronic access channels, and providing electronic linkages that integrate customer and postal processes.

Mr. Chairman, because of this dependency on technology we have devoted considerable Office of Inspector General resources and energy on programs and systems that utilize technology to move the mail. We have dedicated extensive resources to oversee and contribute to the Postal Service's Year 2000 (Y2K) effort, issuing nine reports in the past 18 months that address such issues as remediation, validation, reporting quality, budgeting, contracting, and the adequacy of continuity planning. Our Y2K team was awarded the Executive Council on Integrity and Efficiency Award of Excellence for this work in September 1999.

These audits resulted in improvements in various aspects of the Y2K process, such as the independent verification process. Our recommendations helped improve the quality of systems sent into verification and helped reduce the workload by introducing system sampling to replace 100 percent re-certification. Likewise, our audit on Y2K reporting quality pointed out inconsistencies in information presented to senior management and presented an independent perspective on the progress of the Postal Service's Y2K readiness. I also testified before you in a joint House Subcommittee hearing on the Postal Service's Y2K readiness in February of this year.

In addition, we have four more Y2K projects ongoing. And to demonstrate that we practice what we preach, we have aggressively pursued Y2K readiness by obtaining vendor certifications for all Office of Inspector General office software and network-related hardware and peripherals. All of our personal computers will be compliant by the end of November.

We also looked at systems under development, such as the Postal Service's Point of Service (POS) ONE system, which replaces all outdated,

integrated retail terminals at post offices nationwide, and its Tray Management System, which automates the movement and staging of mail between sorting operations. Both systems had faulty system development practices and premature deployment. We believe the POS ONE system resulted in additional costs to the Postal Service and did not fully meet desired results and benefits. The review of the Tray Management System is yielding similar results. Both technologies are critical to the movement of the mail and revenue collection and represent a projected Postal Service investment of more than $1 billion combined.

Not to leave any stone unturned, we are also looking at the Postal Service's efforts to protect its investment in technology. We are examining several questions. First, what is the Postal Service's computer security vulnerability posture? Second, does it have proper controls in place to ensure data integrity? Third, are its systems vulnerable to hackers and can they be penetrated?

From the computer security controls perspective, we want to determine whether the Postal Service has established a comprehensive, Postal-wide computer security program. Sensitive, critical systems are vulnerable to penetration. We need to determine if procedures exist to identify and deter cyber attacks. We currently have two teams assessing these security areas and plan to brief management before the year-end.

We are proud that we developed one of the few computer intrusion units within the federal government. This group, along with individuals from the National Aeronautics and Space Administration, received a joint Award of Excellence from both the Executive and President's Councils on Integrity and Efficiency for providing intrusion training to 26 law enforcement agencies, including Office of Inspectors General and the Department of Justice.

Last, but certainly not least, is the area of electronic commerce. During this year, the Postal Service announced its high-level internet strategy, appointed a Vice President for Electronic Commerce, established a senior management Electronic Commerce Steering Committee, established the Internet Business

Group, implemented electronic commerce systems, and developed critical electronic commerce partnerships. We are aggressively addressing this issue and have several initiatives planned for Fiscal Year 2000. I am very excited about being part of the electronic commerce initiative and we are keeping pace with Postal Service developments in this most challenging area.

C. Financial Management

The Postal Service is a $60 billion business that relies on strong financial management to control costs and maximize revenues. The Postal Service purchased $8 billion in goods and services in Fiscal Year 1998 through contracts. In addition, the Postal Service is one of America's largest owners, developers and managers of real estate. In Fiscal Year 1998, the Postal Service spent close to $1.2 billion for contracts to repair, renovate, and construct facilities.

Since our June 1998 testimony, we have issued a total of 31 reports covering financial operations, including contracting and facilities. These reviews:

- Identified ways to reduce the risk of money laundering in the Dinero Seguro wire transfer program. Mr. Chairman, as you know, we previously informed you that the indictment of Bancomer did not jeopardize the integrity of the Dinero Seguro Program. Although it did not effect the integrity of the program, our review did uncover a previously unknown scheme whereby drug traffickers used the program to wire drug proceeds to Mexico. In subsequent partnering with another federal law enforcement agency, this investigation has yielded five arrests for violation of the Money Laundering Control Act, along with the seizure of 25 kilograms of marijuana and three kilograms of cocaine.

- Evaluated the Postal Service's compliance with the Bank Secrecy Act and discovered numerous areas where the Postal Service was noncompliant.

- Examined the financial profitability of international mail and determined that international mail services contribute positively to the financial position of the Postal Service and are not subsidized by domestic mail service.

- Aided the external auditor in independently verifying the reliability and accuracy of the financial data for each of the past two years, including electronic data processing systems.

In addition, we issued contracting and facilities reports which:

- Disclosed that the Postal Service, as compared to other Federal agencies, rarely suspends or debars contractors. The Postal Service agreed with our report and is establishing a task force to review and improve its suspension and debarment policies and procedures.

- Recommended suspension and/or debarment of three postal contractors, in unrelated cases, who engaged in illegal acts such as bribery and falsifying documents, and failing to adhere to generally accepted construction and quality control practices.

- Reviewed the Atlanta Olympic Facility Improvement Plan, at your request, Mr. Chairman, and found the plan did not receive approval and oversight at an appropriate level -- contributing to an increased cost of at least $9 million over original projections.

- Identified missed opportunities and questioned up to $72 million in costs because the Postal Service did not request sufficient pre- and post-award contract audits.

- Suggested ways to help reverse the Postal Service's recent decline in minority contracting by strengthening contracting officer accountability, directing that subcontractors specifically include minority businesses in their hiring plans, and clarifying qualifying regulations. This review was done at Congressman Fattah's suggestion.

Based on the results of these initial reviews, we will expand our coverage of these areas to add value, identify opportunities for cost savings, and promote improved financial management practices.

D. Labor Management

The Postal Service has characterized labor management as one of its most important challenges in achieving its goals in the 21st century. With approximately 800,000 career and 100,000 part-time employees, improving workplace relations among labor, management, and the unions and associations that represent them, is a key objective within the Postal Service. Because of the importance of labor management on Postal operations, the Postal Service has developed numerous initiatives and programs focused on reducing conflict in the workplace and improving the effectiveness of procedures to resolve disputes. In addition, established channels are available to help resolve Postal employees' complaints. These channels include contractual grievance arbitration procedures and the Equal Employment Opportunity process.

However, labor management is one of the toughest areas for us to adequately address. Since our inception, we have received over 2,500 individual labor management complaints. Because of the emotional involvement, potential financial impact, and the length of time to resolve these issues for the employee, management, and Postal Service, it is important that our involvement in this area

be meaningful and positive. Therefore, the approach we have developed to deal with the sheer magnitude of complaints is to step back and focus primarily on systemic issues and conduct Postal-wide reviews. These reviews are designed to identify and short circuit potential problems that can detract from a healthy and productive work environment.

Federal Inspectors General typically perform programmatic and operational audits. Most individual labor management complaints do not focus on programs and operations but on personal concerns. Therefore, we usually do not review individual complaints unless they involve potentially violent or other egregious situations. However, individual complaints provide us with extremely valuable information that we can use to identify Postal-wide issues and plan reviews that address these issues on a systemic basis. Members of Congress often ask us to address individual complaints, but to do this would require a substantial increase in our labor management staff and expanding our mission into individual reviews.

Since June 1998, the Office of Inspector General has completed 30 reports and approximately 60 congressional responses concerning labor management. Our Labor-Management team was recognized with an Executive Council on Integrity and Efficiency Award of Excellence this year for work in this area.

As a result of a request from Congressman Fattah, we have issued four reports that focused on the Postal Service grievance arbitration process. In Fiscal Year 1997, the Postal Service estimated that it spent at least $216 million on grievances. These grievance arbitration reviews provided suggestions on how to improve the process, reduce the backlog of grievances, and improve the labor climate.

In July 1998, Congressman Fattah sent us over 500 complaints, which he had received from a Postal union, representing the concerns of more than 1,200 individuals. We designed a series of reviews to address the systemic issues underlying these complaints.

The first report in this series addressed the consistency with which Postal management within one district communicated and enforced Postal Service policies regarding violent and inappropriate behavior in the workplace. We found that management had not effectively implemented many of the Postal Service's violence prevention policies and procedures. This is similar to the result we found when we looked at the December 1997 Milwaukee incident, at your request, Mr. Chairman. Based on the work at Milwaukee and the other district, we are reviewing the violence prevention and response programs at 26 additional Postal Service district offices and will issue reports upon completion.

Another area that has piqued our professional interest involves the implementation of the Postal Employees Safety Enhancement Act requirements and its effect on the organizational climate and Postal Service operations in general. A review of these issues will provide Postal Service employees with an independent evaluation of working conditions and provide information that may reduce the Postal Service's liability for penalties and third party litigation.

To address Postal Service challenges, the Postal Service must give labor management issues more visibility. We will continue to work with management and to consult with labor officials to ensure our reviews are pertinent and that our recommendations are appropriately addressed.

E. Inspection Service Oversight and Other Significant Issues

Mr. Chairman, the final Postal Service areas I would like to discuss include Inspection Service oversight and other significant issues. As you well know, one of the primary reasons an independent Office of Inspector General was established in the Postal Service was to provide oversight of Postal Inspection Service activities. Because this is one of our specific statutory responsibilities, we seek to review and resolve all individual complaints that we receive against the Inspection Service. We also perform systemic reviews of Inspection Service operations and activities, and investigate complaints against Postal Inspection Service executives.

The Inspection Service has approximately 4,500 employees, including 2,100 Postal Inspectors located in 185 offices who enforce over 200 statutes relating to crime against the U.S. mail and Postal Service employees and customers. In the past 18 months, we have conducted 18 reviews and investigations involving Inspection Service personnel and operations. During these reviews, we:

- Determined that approximately 250 Postal Inspectors performing audits did not spend at least 50 percent of their time performing the duties of a law enforcement officer. This review was done at your request, Mr. Chairman. As a result of this review, the Inspection Service decided that they would no longer perform "Yellow Book" audits. This decision will have a major impact on the Office of Inspector General. We have created a task force to evaluate the effect of this decision on our staffing needs, field structure, and the agreed upon designation of functions with the Inspection Service. We plan to discuss the results of the task force with the Governors as soon as the task force completes its evaluation.

- Evaluated the Fiscal Year 1998 Postal Inspection Service Leadership Conference as a result of a hotline allegation. We found that certain conference expenditures and agenda items appeared unnecessary or extravagant, including non-work related workshops, publications, and $82,000 in mementos.

- Established that a greater level of investigative effort by the Inspection Service was required to deter the use and sale of drugs on Postal premises.

As a result of our Postal Inspection Service oversight reviews, Congress, Postal management, and employees, including all levels of Inspection Service

employees, have an independent, unbiased, and credible view of Inspection Service activities and operations.

Turning from the Inspection Service to other significant work within the Postal Service, we:

- Provided a statement for the record on proposed sweepstakes fraud legislation in response to an invitation by this Subcommittee. We strongly supported this consumer protection legislation, and suggested that the Postal Service subpoena authority focus on sweepstakes mailings and include due process safeguards.

- Continued to monitor the Postal Service compliance efforts with the Government Performance and Results Act, and assessed the Postal Service's implementation of the General Accounting Office's observations on the Postal Service's draft strategic plan and preliminary annual performance plan.

- Noted opportunities to enhance the administration of the Postal Service Ethics Program.

- Questioned the appropriateness of a recent management decision to purchase insurance that included provisions to cover legal expenses of Postal Service officials in the event they are indicted on federal criminal charges.

Our work in these other significant areas provides an independent voice, not subject to Postal Service management, which renders objective information and analysis of Postal Service operations.

OUR PROGRESS

I would now like to discuss our internal progress. As mentioned earlier in my testimony, in June 1998 we were in the midst of establishing office space and hiring employees. The Inspector General community recognized our enormous accomplishment of establishing a new Office of Inspector General through its Award of Excellence. Since then we have grown from 178 to over 400 employees and from four to six offices in Arlington, VA; Dallas, TX; Minneapolis, MN; St. Louis, MO; San Mateo, CA; and Atlanta, GA. In August 1999, the Governors approved a budget for the Office of Inspector General that would support a total of 648 staff and allow us to establish additional offices in Chicago, IL; New York, NY; Los Angeles, CA; Denver, CO; and Raleigh, NC.

Of the 403 individuals on board as of September 30, 1999, 43 percent are women and 42 percent are minorities. Minorities include Blacks (28 percent), Hispanics (7 percent), Asians (6 percent), and Native Americans (1 percent). Based on the U.S. Bureau of the Census estimated data, as of November 1998, Office of Inspector General has met or exceeded the U.S. percentage of total population for each of these groups except for Hispanics, which is 11 percent. Our senior staff is 35 percent female and 26 percent minority.

The Office of Inspector General is proud of its diversity and is committed to developing and utilizing the diverse talents of all its employees. Many of our employees have advanced degrees and are certified public accountants, certified internal auditors, certified information systems auditors, certified fraud examiners, and certified acquisition auditors. In addition, a number of our investigators hold law enforcement specialty certifications in areas such as polygraphic examinations and seized computer evidence recovery. Our criminal investigators attend rigorous training at the Federal Law Enforcement Training Center or equivalent law enforcement academy. Employee education and professional certification enhances the Office of Inspector General's ability to add value to the Postal Service.

Our cultural and professional diversity reflects the hiring of the most qualified staff from the widest sources available. We have obtained staff from private industry, other federal and state agencies, and the Postal Service, including the Postal Inspection Service. Each employee undergoes a full background investigation to ensure his or her suitability for employment with the Office of Inspector General. Because of our desire to hire competent, talented individuals, we have been highly selective in filling our vacancies.

To develop a diverse pool of highly qualified candidates, we have attended numerous conferences, colleges, and career fairs. With the unemployment rate at historic lows, hiring competent, talented individuals continues to be one of our greatest challenges. For example, in order to meet our Governor-approved hiring level of 648 for Fiscal Year 2000, we need to hire over 200 individuals. In addition, as mentioned earlier, we may need to increase our staffing levels and, hence, our level of hiring, because of the Inspection Service's decision not to perform "Yellow Book" audits in the future.

We continued to build our infrastructure. Over the last 18 months, we established:

- Our human relations processes and systems, including: a 360 degree feedback evaluation system; an interim pay-for-performance system; an extensive screening process for potential new employees; a thorough pre-employment background investigation process; ten 1-week orientation classes for new employees; a bi-weekly employee newsletter; and a 3-week Postal-specific investigative training program.

- Our administrative resources services, including: management controls over our internal processes; development of our own contracting function; establishment of Office of Inspector General offices by identifying, leasing, and developing space to accommodate Office of Inspector General staff in various locations throughout the country; performance of numerous quality assurance and internal

reviews; and implementation of an automated tracking system for time and projects.

- Critical audit, investigative and administrative processes, including: developing internal policies and Postal-wide policies for describing Office of Inspector General authorities and responsibilities; continuing to notify Postal employees at all levels of their right to report wrongdoing to the Office of Inspector General without fear of retaliation; assuming responsibility from the Inspection Service for review of Postal Service legislation, policies, and procedures; engineering an electronic subpoena system to improve processing of Inspector General administrative subpoenas (for which we received an Executive Council on Integrity and Efficiency Award of Excellence); deploying a report processing review staff to expedite and standardize issuance of reports; working with Postal Service to ensure a valid tracking system for recommendations from the external auditor, General Accounting Office, Inspection Service, and the Office of Inspector General; processing over 100 Freedom of Information Act requests and over 100 Congressional responses; and providing quarterly firearms qualifications and defensive tactics training to criminal investigators.

- Strategic processes, including: revising the Strategic Plan, developing a universe of over 1,000 projects, preparing the Fiscal Year 2000 Annual Performance Plan, achieving over 80 percent of the performance measurements for Fiscal Year 1999 resulting in a Team Award for Office of Inspector General employees, and establishing computer intrusion and electronic commerce units.

Within the Inspector General community, the Postal Service Office of Inspector General is now a member of two important policymaking bodies of the

President's Council on Integrity and Efficiency. I am a member of the Investigations Committee and my Assistant Inspector General for Audit is a member of the Federal Audit Executive Council. In these positions, the Postal Service has a greater voice within the Inspector General community. In September 1999, the Postal Service Office of Inspector General was honored to receive more awards than any other Office of Inspector General, including four Awards of Excellence and four Honorable Mention Awards. This accomplishment is especially noteworthy since the Postal Service Office of Inspector General is one of the newest members of the Inspector General community.

Within the Postal community, the Office of Inspector General continued to gain respect and acceptance in numerous areas. For example, in March 1999, the Governors approved the Office of Inspector General's role as Co-Contracting Officer's Representative on the external certification of the Postal Service's financial statements. This role provides the Office of Inspector General with greater involvement in the external audit process.

In August of this year, I was a delegate to the Universal Postal Union in China and saw first hand the role of the Postal Service in the international arena. By attending the Postal management committee meetings with senior Postal officials, I keep informed of emerging issues, developing trends, and new initiatives.

Members of my staff and I continued to give numerous presentations to various groups including professional organizations, internal Postal groups, and major Postal stakeholders, informing them about the Office of Inspector General. We have also given over 30 fraud awareness briefings to Postal employees. With our upcoming Semiannual Report to Congress, we will issue a hotline poster, which will be disseminated to all Postal facilities.

CHALLENGES FACING THE OFFICE OF INSPECTOR GENERAL

As a new Office of Inspector General, we still have numerous challenges, which fall into three broad categories: our internal infrastructure, our internal Postal Service role, and our external role to Postal stakeholders. As I look to the future, the key challenges in these categories are:

- Internal Infrastructure: hiring additional talented and diverse staff; building our processes, policies, and procedures; promoting our values and culture; and continuing to forge ahead with our mission while being sensitive to the variety of extensive demands that are being placed on our employees in our evolving environment.

- Internal to the Postal Service: continuing to add value through our work by providing meaningful results on a timely basis; educating the Postal Service on our roles and responsibilities; resolving differences, including those of authority, roles, and responsibilities with the Inspection Service; maximizing the impact of Office of Inspector General work by instituting effective resolution processes; educating Postal management on the independence of the Office of Inspector General and its duty to report any significant issues to the Postal Service Governors and the Congress; informing Postal Service officials of our authority to make independent decisions on areas to review; performing work and continuing to gain expertise in Postal Service programs, operations, and emerging issues.

- External to the Postal Service: making the results of our work publicly available without affecting the Postal Service's competitive position; educating Postal stakeholders on our role; continuing to establish the Postal Service Office of Inspector General as a significant player in the

Inspector General and federal law enforcement communities; and effectively dealing with hotline and Congressional inquiries.

I would like to expand on one of these issues -- our ability to develop effective working relationships with the Inspection Service. As the Office of Inspector General has grown and initiated work into various Postal areas and operations, Postal employees have not always been familiar with Office of Inspector General authorities. Recently, Postal Inspection Service personnel challenged the Office of Inspector General's presence at a Postal facility while we were participating in a federal task force surveillance. As a result of this incident, executives of both agencies have renewed team-building efforts to increase communications, trust, and coordination. Situations like these illustrate the need for mutual respect and professional courtesy between the Inspection Service and the Office of Inspector General.

BENEFITS OF AN INDEPENDENT OFFICE OF INSPECTOR GENERAL

An independent Office of Inspector General benefits the Postal Service by providing not only Postal management but also the Governors and Congress with timely, objective, and complete information and analyses of Postal Service operations. For example, in our 2½ years of existence, we have issued 14 reports in the areas of new product development, new business processes, new and redesigned automated equipment, and automated systems development. These reports were provided to the Governors, briefed as appropriate to the audit committee and the Governors, and included in our Semiannual Reports to Congress. In contrast, records indicate that for the five-year period before this office was established, 15 developmental projects had been opened. While we understand issues were discussed with management, none of the developmental projects were reported in the Semiannual Reports to Congress until September 1998, after our office was established.

Other significant benefits to the Postal Service of an independent Office of Inspector General include the:

- Expansion of audit and investigative coverage of all Postal operations and activities, including rate making, contract administration, Inspection Service oversight, labor management, computer intrusion, electronic commerce, and marketing. This coverage will achieve cost savings, enhance contract and program administration, and increase employee and program integrity.

- Technological evaluations in areas such as Y2K, electronic commerce, and computer intrusion with experienced, specially trained staff.

- Independent review of complaints against the Inspection Service, which receive specific audit and investigative oversight.

- Audit resolution and follow-up processes, which will provide meaningful mechanisms for resolving findings and recommendations where Office of Inspector General and Postal management are in disagreement, and for assuring that management implements corrective action.

In summary, we believe that the establishment of an independent Postal Inspector General by Congress in late 1996 has resulted in:

- Greater Postal Service economy, efficiency, and integrity.

- A truly independent voice.

- A venue for all employees and other stakeholders to confidentially report allegations of fraud, waste, abuse, and mismanagement.

- Delivery of objective information and analysis of Postal Service operations to all Postal stakeholders, including Congress and the Governors.

CONCLUSION

The Postal Service is reevaluating the role it will play in an advanced technology and highly competitive environment. We will continue to assist the Postal Service, the Governors, and Congress by providing accurate and objective information upon which to base important decisions in the critical areas of performance, technology, financial management, labor management and Inspection Service oversight. As you can see, in the past 18 months we have achieved much and look forward to continuing to work with this Subcommittee and the Postal Service to improve Postal operations.

Mr. Chairman, this concludes my statement. I would be pleased to answer any questions you or the Subcommittee may have.

# # #

Mr. MCHUGH. I believe rather than breaking up the panel, if it's agreeable to the Members, we'd like to go to Mr. Ungar for his testimony, and then we can return to questions for both the witnesses.

So, Mr. Ungar, welcome to you again also. Thank you for being here, and we're looking forward to your comments.

STATEMENT OF BERNARD L. UNGAR, DIRECTOR, GOVERNMENT BUSINESS OPERATIONS ISSUES, U.S. GENERAL ACCOUNTING OFFICE, ACCOMPANIED BY TERESA ANDERSON, ASSISTANT DIRECTOR; AND GERALD BARNES, ASSISTANT DIRECTOR, U.S. GENERAL ACCOUNTING OFFICE

Mr. UNGAR. Thank you, Mr. Chairman, members of the subcommittee. We're pleased to be here today to assist the subcommittee in carrying out its oversight function over the Postal Service.

In our written statement, we really discuss three broad areas: the Service's historical performance, major challenges it faces in the next few years, and the results of our work since the last oversight hearing that the subcommittee had. In my summary, I would like to focus on the major challenges that we see and the change that we see over the horizon that the Postal Service is facing.

First, I would like to note that our work as well as work of the Inspector General and information from the Postal Service would indicate that the Postal Service's performance currently and in the recent years has been notable. It's earned profits consecutively over the last 6 years, which is kind of a first since it was established as the modern Postal Service. It reports improvements in on-time delivery in both overnight mail, first-class overnight mail, and 2- and 3-day mail. It's made some progress in the labor-management area and some progress in work force diversity, particularly after the report that Mr. Davis mentioned. It's in better shape today now than it was a few months ago for the Y2K situation, and it's improved controls that we previously found to be deficient in the areas of changing addresses when people move and the acceptance of business mail. It also, last but not least, has made notable progress, in our view, in implementing the Results Act over the last year.

However, as we indicated in our written statement, we see that the Postal Service may be nearing the end of an era. While the performance has been notable, we see formidable challenges in the future, first of which and foremost in our mind is sustaining its financial viability in the face of competition, increased use of electronic communications, and increased customer demands for more service, better, and cheaper.

Historically, increasing postal rates and increasing mail volume have provided the Service with additional revenues which have enabled it to take care of and finance wage increases, modernization, and improvements in the quality of service. However, as figure 1 in our statement shows, and as indicated by the board over to my right, first-class mail volume, as you indicated, Mr. Chairman, may be in for a downturn. The growth rate of mail volume has increased, as we have in the chart laid out by decade. During the 1970's, it was increasing. It continues to increase in the 1980's. However, in the 1990's, the rate of increases started to come down, and the latest projection from the Postal Service is that during the

next decade it's going to basically come down below where it was. In other words, not only will the rate decline, but the actual first-class mail is projected to volume decrease starting around 2003 and then continuing to go down from there as a result of electronic communication and technology.

In addition, the Postal Service faces increased competition, as you know, from a variety of sources, and this certainly could also affect the volume of first-class mail and the revenue that's associated with first-class mail.

Now, why is this important? One of the main reasons it's important is because first-class mail generates a large proportion of the Postal Service revenue overall, and it covers about—at least it has covered about—two-thirds of the Postal Service's overhead cost. So, if the volume of first-class mail goes down, the revenue goes down; it's going to have to make up that amount of money from someplace or cut costs substantially or both in order to cover the overhead, or the revenues from other classes of mail will have to increase.

Just to give you an idea as to the type of challenge that we see the Postal Service facing, let's take the year 2000, for example, and the goal the Postal Service has which is currently to earn $2 million—excuse me, $100 million in 2000. To achieve this goal, the Postal Service says it must realize a 1 percent reduction in work hours of its employees and increase productivity by 3.1 percent. Now, how is this going to happen? It faces, at the same time it wants to achieve this goal, a situation in which mail volume in 2000 is expected to grow nearly 4 percent, and the number of delivery points that its carriers make is expected to grow as well as it has over the last few years.

To top that off, if you look at the chart to my right again, looking at productivity historically since the modern Postal Service was established, it's only gone up 9 percent overall since 1972. And in 4 of the last 5 years, it has not gone up. It's gone down. And it's only gone up 3 percent on four occasions, 4 years over the entire period that's on the chart. So that puts in perspective its goal of 3 percent next year. That's not to say it's not achievable. I think, as we indicated, it's going to be a fairly significant and formidable challenge for the Postal Service to do this.

The second challenge that we see deals with maintaining its service delivery. Our discussions with some of its large customers indicate they are very concerned about the Postal Service's ability to do this in the future. And this largely will depend upon new indicators—the Service now doesn't measure all classes of mail. It's in the process of developing indicators for a number of those, and I think it's going to be very important for the Service to continue that to make sure it does have indicators for all its major classes of mail so its customers and stakeholders, including Congress, can see just how well it's doing, and hopefully it will be improving.

But both addressing its financial performance challenges and its service delivery performance challenges hinges heavily, in our view, and I think in terms of also the Inspector General, on its ability to forge a partnership or a better partnership with its employees. And as we've indicated in the past, as well as others, labor-management relations has been a very difficult problem in the Postal

Service. We have seen some progress since our last report. The Postal Service and its unions and management associations have been meeting. However, we haven't seen a whole lot of substantial progress. We're glad to note that there was a negotiated agreement with some of its unions. However, as you know, with the city carriers, that wasn't the case. And the implications of that for the future may not be positive in terms of how the Service is going to be able to deal with that.

Second, there is some indication from Postal Service data that the number of grievances has not gone down. As a matter of fact, it appears to have gone up, which is not a good sign in terms of improving the partnership with its employees, and it's going to be difficult, we think, for the Postal Service to accomplish its goals and meet the challenges if it can't forge a much better relationship with its employees.

Finally, the last challenge I'd like to summarize has to do with the integrity of the data that the Postal Service uses for both measuring performance and for ratemaking. It's critical, we think, that the Service has reliable data to report to its stakeholders and to its customers on its on-time delivery in all classes of mail as well as other indicators. It's also very important for the Service to provide reliable data for ratemaking purposes.

Mr. Chairman, this is an issue that you raised several years ago, as you know. The contract—excuse me, the Postal Service at your behest and urging—hired a contractor to assess the data. The report is issued. The contractor made 40—over 40 recommendations—as to improvements that could and should be made in the ratemaking data process. Unfortunately, when we've talked to the Postal Service, we can't get a clear signal from the Postal Service as to what specific actions it plans to take with respect to those recommendations and a timeframe. So in our testimony, we are making a formal recommendation to the Postmaster General to develop a plan and come up with some specific actions that it would propose to take. Obviously, it may not be able to address all those in the short term; so I would presume there would be some that the Postal Service could address in the short term and perhaps some that would take more time and effort.

That, Mr. Chairman, concludes my summary. We'd be happy to answer any questions that you may have.

Mr. MCHUGH. Thank you, Mr. Ungar.

[The prepared statement of Mr. Ungar follows:]

United States General Accounting Office

GAO

Testimony

Before the Subcommittee on the Postal Service
Committee on Government Reform
House of Representatives

Not to be Released
Before
10:00 a.m. EDT
Thursday
October 21, 1999

U.S. POSTAL SERVICE

Challenges to Sustaining Performance Improvements Remain Formidable on the Brink of the 21st Century

Statement by Bernard L. Ungar
Director, Government Business Operations Issues
General Government Division

GAO/T-GGD-00-2

Summary

U.S. Postal Service: Challenges to Sustaining Performance Improvements Remain Formidable on the Brink of the 21st Century

The Postal Service may be nearing the end of an era. During the past 5 years, the Service has made notable improvements in its financial position and delivery performance. The Service has recorded positive net income and has maintained or improved the overall delivery of certain specific classes of mail. However, the Service expects declines in its core business in the coming years. The growth of the Internet, electronic communications, and electronic commerce has the potential to substantially affect the Service's mail volume. As a result, the Service may experience growing difficulty in maintaining its position in a dynamic communications and delivery environment. These developments make it imperative for the Service to resolve long-standing performance challenges, which involve four major areas.

- Maximize performance: The Service's ability to maximize performance in the face of increasing customer demands and choices calls for establishing processes to accurately assess performance results and collecting and maintaining reliable data to support such assessments.
- Manage employees: The Service's management of employees, its greatest asset, will in large part involve continued attention to labor-management relations problems that have plagued the Service and its unions and management associations for several years.
- Maintain financial viability: The extent to which the Service can maintain financial viability by controlling costs and enhancing revenues will involve appropriately managing its capital investments in technology and infrastructure as well as working to improve productivity.
- Adapt to competition: The means by which the Service can adapt to a rapidly changing communications environment of growing competition will involve positioning the organization to meet changing customer needs, improve performance, and operate more efficiently.

GAO is also highlighting the need for the Postal Service to take action to address long-standing issues related to the quality of data used in ratemaking and recommending that the Postmaster General report to congressional oversight subcommittees on the actions taken and planned in this area.

In recent years, the Service has progressed in addressing various challenges and is continuing to initiate significant changes that respond to the challenges. However, as the Service stands on the brink of the 21st century, time appears to be growing short for the Service to successfully address its challenges so that it can sustain and improve current performance levels and remain competitive in a rapidly changing communications environment.

Statement

U.S. Postal Service: Challenges to Sustaining Performance Improvements Remain Formidable on the Brink of the 21st Century

Mr. Chairman and Members of the Subcommittee:

We are pleased to be here today to participate in the Subcommittee's oversight hearing on the U.S. Postal Service. In my testimony, I shall provide an overview of where the Service stands today, as we come to the end of the 20th century, by looking back at trends in its financial and service delivery performance and also looking forward to the major challenges confronting the Service at the start of a new millennium. Also, I will discuss ongoing work and work that we have completed since June 1998 related to four major challenges facing the Postal Service:

- maximizing performance in the face of increasing customer demands and choices;
- managing employees, the Service's most valuable asset, to maximize attainment of agency goals and continuous improvement of employee performance;
- maintaining financial viability by controlling costs and enhancing revenues; and
- positioning the organization to adapt to a rapidly changing communications and delivery environment with a growing number of competitors.

I will also discuss other major postal oversight issues related to work that we have completed during the past year. A list of the reports and testimonies we have issued since June 1, 1998, is included in the attachment to this statement.

Overview of Financial and Service Delivery Performance

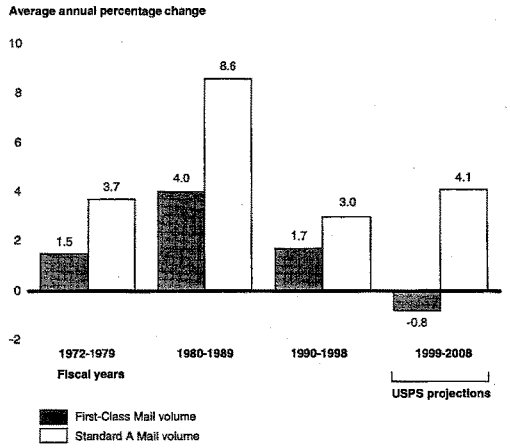
The Service has continued to report improvements in the areas of financial and service delivery performance and has undertaken a number of initiatives to respond to the four major challenges that we identified. Given the nature and extent of the challenges facing the Service, we understand that it will take time to implement and assess the impact of major initiatives intended to address the challenges. And, although the Service has made progress and is continuing to make significant changes, time appears to be growing short for the Service to successfully address these challenges so that it can sustain and improve current performance levels and remain competitive into the 21st century.

The Impact of Increasing Competition

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. Should this occur, the Service will likely face unprecedented challenges as it seeks to fulfill its primary mission of providing universal postal service at reasonable rates while remaining self-supporting from postal revenues.

The Service and other stakeholders agree that growth in the Service's core business of delivering First-Class Mail has already been affected by the rapid growth of the Internet, electronic communications, and electronic commerce. Although the Service's mail volume increased in the 1990s to record levels, the rate of growth has slowed. As figure 1 indicates, the Service projects that First-Class Mail volume will decline at an average annual rate of 0.8 percent in fiscal years 1999 to 2008. Specifically, First-Class Mail is projected to grow at an average annual rate of 1.8 percent in fiscal years 1999 to 2002—the projected peak—and then to decline at an average annual rate of 2.5 percent in fiscal years 2003 to 2008. Such a decline would be unprecedented in the Service's history and would likely create financial and performance challenges. As the Postmaster General has noted, the Service's environment is changing rapidly, and therefore the Service cannot predict precisely when or to what extent competitive pressures may affect the Service's revenues.

Figure 1: U.S. Postal Service Projects Future Decline in First-Class Mail Volume



Note 1: The U.S. Postal Service forecasts First-Class Mail to increase by an average annual rate of 1.8 percent in fiscal years 1999 through 2002 and to decline by an average annual rate of 2.5 percent in fiscal years 2003 through 2008. The Service also forecasts Standard A mail to increase by an average annual rate of 5.3 percent in fiscal years 1999 through 2002 and to increase by an average annual rate of 3.3 percent in fiscal years 2003 through 2008.

Note 2: Actual data for fiscal year 1999 are not yet available. Standard A mail is primarily advertising mail and includes letters, flats, and parcels that are not sent by First-Class Mail or Priority Mail.

Source: U.S. Postal Service.

Historically, increases in mail volume—including the volume of First-Class Mail—have helped the Service cover its costs. In the 1990s, increasing postage rates and mail volume helped provide the Service with additional revenue to finance wage increases, modernization efforts, and improvements in the quality of delivery service. The Service projects that total mail volume will continue to increase from fiscal years 2000 through 2008 by an average annual rate of 1.7 percent, with the growth rate tapering off during the decade and total mail volume peaking in fiscal year 2006.

Even if total mail volume increases, a decline in First-Class Mail volume would present the Service with the challenge of making corresponding reductions in the costs of handling First-Class Mail—that is, in costs that historically have varied directly or indirectly with changes in First-Class Mail volume—in order to hold down First-Class rates. Further, in fiscal year 1998, revenues from First-Class Mail covered about two-thirds of the Service's institutional costs.[1] A substantial reduction in First-Class Mail volume would reduce its contribution to institutional costs, which could lead to somewhat higher postage rates in the future.

The Service recently provided us with a detailed explanation of its volume forecast scenario and why it projects a substantial decline in First-Class Mail in the next decade. The Service's Chief Financial Officer wrote us on September 9, 1999, that First-Class Mail volume is projected to decline on the basis of the assumption that diversion of mail to electronic communications alternatives would accelerate in a new and vastly different environment in which the Service would operate. In this environment, changes in technology and business would create a climate in which current hypotheses about mailing behavior may no longer hold. Notably, the combination of consumer movement to alternative bill payment methods and the consolidation in the financial sector would reduce the number of bills, statements, and payments in the mail stream. Moreover, the movement of advertisers to the Internet would cause a slowdown in the growth of Standard A mail, while growth in Priority Mail and Parcel Post would continue to be robust as consumers embrace electronic commerce and more packages are shipped by Internet retailers. Specifically, the Service's forecast was based on the following assumptions:

- Potential Year 2000-related complications are largely avoided, increasing business and consumer confidence in electronic alternatives to traditional mail-based bill and statement streams.

- Businesses increase research and development and technology spending as a result of the easy Year 2000 transition, resulting in rapid implementation of on-line banking and financial applications and the spread of Internet-based small business Electronic Data Interchange.

[1]Institutional costs do not vary by changes in mail volume, such as costs to maintain a national network of over 38,000 post offices and postal facilities and to deliver to 130 million addresses 6 days a week.

- First-Class letter advertising reaches a saturation point because of consolidation in the banking sector, as well as the diversion of bills and payments away from the mail stream.

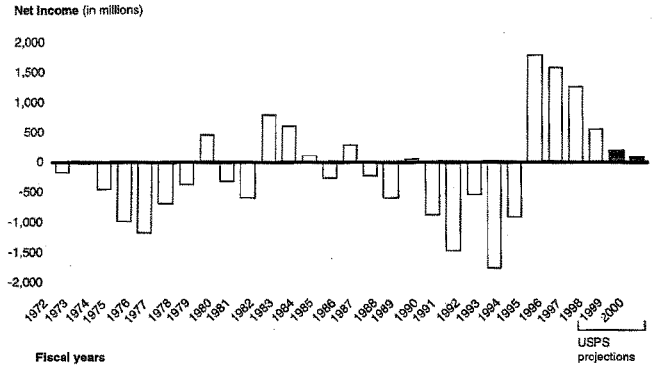
- Advertisers move away from traditional media to Internet-based platforms because of increased consumer use of the Internet.

Another key development has been the globalization of the Service's competitors in the delivery sector, which has contributed to recent declines in the Service's international mail volume. Further, the Service's competitors have charged that the Service is using its governmental status to compete unfairly. These developments have fueled the debate over whether the Service should be allowed to introduce new nonpostal products in competition with the private sector, or whether the Service should be limited to offering traditional postal services and wind down its operations as its core business declines. Regardless of how this public policy debate is resolved, the Service has recognized that it must continue to meet customer needs, improve its performance, and operate more efficiently in order to be successful in an increasingly competitive environment.

Financial and Delivery Performance Continues to Show Positive Results

The Service projects positive results for both financial and service performance for fiscal years 1999 and 2000. As shown in figure 2, the Service projects a net income of $200 million in fiscal year 1999, and its Integrated Financial Plan for fiscal year 2000 projects a net income of $100 million.

Figure 2: Trends in Postal Service Net Income Since Postal Reorganization Was Implemented



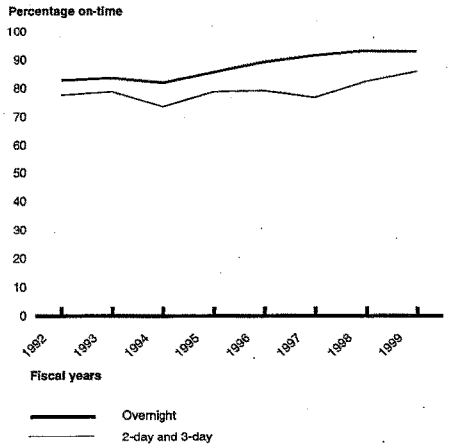
Source: U.S. Postal Service.

If the Service achieves these net income projections, it will be the first time that the Service has achieved positive net income for 6 consecutive years since postal reorganization was implemented in 1971. However, the Service's Integrated Financial Plan for fiscal year 2000 has reported that in order to accomplish net income of $100 million in fiscal year 2000, the Service would need to realize a 1-percent reduction in workhours. This plan projected that growth in total mail volume will be 3.8 percent in fiscal year 2000, which would add to the Service's workload. Also, according to Postal Service data, the size of the Service's city and rural delivery network has increased more than 1 percent in each of the past 4 years. If the Service's delivery network continues to grow, this would further add to the workload of mail delivery. In addition, the Service has established goals to maintain or improve mail delivery service in fiscal year 2000.

The Postmaster General has stated that the Postal Service is cutting costs to preserve affordable rates but that service will not be sacrificed. As shown in figure 3, during the 1990s, the Service improved on-time delivery of First Class Mail that is to be delivered overnight, as well as First-Class Mail that is to be delivered 2 or 3 days after it is mailed. The Service also

appears to be on track for achieving record delivery service performance for this year. The Service's Performance Plan for fiscal year 2000 sets goals to continue the improved performance in these areas, as well as setting an additional performance target for on-time delivery of advertising mail.

Figure 3: On-Time Delivery Performance for First-Class Mail



Source: U.S. Postal Service.

Challenges Facing the Service

We have identified four major challenges facing the Postal Service as the 21st century quickly approaches: (1) maximizing performance in the face of increasing customer demands and choices, (2) managing employees—the Service's most valuable asset—to maximize attainment of agency goals and continuous improvement of employee performance, (3) maintaining financial viability by controlling costs and enhancing revenues, and (4) adapting to a rapidly changing communications and delivery environment with a growing number of competitors.

Maximizing Performance

One of the major and continuing challenges that the Service faces involves its effort to maximize performance in the face of increasing customer

demands and choices. As part of this effort, the Service has established a results-oriented planning process. As required by the Government Performance and Results Act of 1993 (the Results Act), the Service has published annual performance plans. These plans were aligned with its planning process and identified the Service's major goals and objectives, strategies for accomplishing the goals and objectives, and some performance indicators to measure progress toward these goals.

The Service's performance plan should help guide its actions over the next year and provide information useful to the Service's ongoing dialogue with Congress and other stakeholders. The Preliminary Annual Performance Plan for Fiscal Year 2000 specified goals and targets for the Service's intended performance in such areas as providing timely delivery, improving workplace relations, and achieving its target for net income. In response to a report we issued in April 1999, the Service agreed to identify its top goals for fiscal year 2000 in its final performance plan.[2] Also, the final plan provided updated information on the Service's projected revenues and costs for fiscal year 2000 as well as an updated summary of the Service's efforts to reduce its costs.

Early next year, the Service is to publish its first annual program performance report under the Results Act as part of its Fiscal Year 2000 Comprehensive Statement on Postal Operations. This report should help the Service, Congress, and other stakeholders assess the Service's performance in the past fiscal year compared to the goals included in its performance plan. In this regard, it will be important to many postal stakeholders for the Service to continue to make tangible progress toward implementing a more complete set of performance measures and targets. For example, in fiscal year 2000, the Service intends to develop new measures of timely delivery of international mail, publications, and bill payments sent through the mail. As we observed in our January 1999 report on the Service's major performance and management challenges, the prospect of declines in the Service's core business has heightened the need for the Service to resolve long-standing performance issues and implement reliable indicators of postal performance.[3]

Ratemaking Data Quality

To date, limited assessments have been made of the reliability of the Service's performance data. Data integrity is vital to the Service's

[2] The Results Act: Observations on the Postal Service's Preliminary Performance Plan for Fiscal Year 2000 (GAO/GGD-99-72R, Apr. 30, 1999).

[3] Major Management Challenges and Program Risks: U.S. Postal Service (GAO/OCG-99-21, January 1999).

performance report as well as other mission-critical areas, such as setting postal rates. One study, which was initiated at the request of this Subcommittee, established a good beginning by assessing the quality of data used in postal ratemaking and identifying opportunities to improve the quality of these data.

The study involved a joint 1997 agreement among the Service, the Postal Rate Commission, and us to have an outside contractor conduct a comprehensive assessment of the quality of data used by the Service in setting postal rates. The study, conducted by A.T. Kearney, Inc., resulted in a report released earlier this year that included 47 recommendations designed to improve and enhance the completeness and the accuracy of data the Service provides for ratemaking.[4] The contractor found that providing sufficiently complete and accurate data is an evolutionary process that requires the Service to continually improve the quality of its ratemaking and related data systems. For example, changes in operations require ongoing improvements to data systems to ensure that appropriate data are collected.

The contractor concluded that the quality of the data provided by the Service for ratemaking has generally been sufficiently complete and accurate to enable subclass rates to be based on reasonably reliable data. However, the contractor reported concerns that in some instances, the best available data were used regardless of their inherent levels of error or obsolescence. The contractor concluded that "...improvements and enhancements can–and must–be made to ensure future data provided for rate making will be sufficiently complete and accurate." Some of the key recommendations related to the following areas:

- Mail processing: better measure costs related to mail processing;
- Delivery: update and improve the quality of special study data used to determine delivery costs;
- Capital and support: improve the measure of capital and support costs; and
- Revenue, volume, and weight: improve the completeness and accuracy of mail revenue, volume, and weight data as well as develop more accurate analyses of the impact of weight on costs.

[4]Data Quality Study, April 16, 1999, prepared by LINX, a division of A.T. Kearney, Inc. This report is available at the U.S. Postal Service Internet site at http://www.usps.gov/clr/dqs.htm.

We believe that the study has made an important contribution to analyzing the issues, making the case for change, and offering constructive recommendations for short-term and long-term improvements. Postal officials have indicated that they agree with most of the study's recommendations. They said that the Service is taking steps to implement some of the recommendations, such as updating some special studies used to help estimate postal costs. For a number of recommendations, they plan to conduct additional evaluation or analysis to assess what followup may be needed. Overall, it is not clear what specific actions the Service plans to take to improve the quality of data used in ratemaking and the timeframes for completion.

As you know, Mr. Chairman, you requested this study to address concerns raised by the Chairman of the Postal Rate Commission and others about the data deficiencies in the Postal Service's 1994 rate filing. Further, issues related to the quality of data used in ratemaking have been an important area of continuing oversight for this Subcommittee. Given the importance of data quality to setting postal rates, as well as the level of congressional concern in this area, we believe it is important for the Postal Service to demonstrate to Congress, the Postal Rate Commission, stakeholders, and the public that it is making progress in improving the quality of data used in ratemaking. Therefore, we are recommending that the Postmaster General report to the congressional oversight subcommittees on the actions taken and planned to improve the quality of data used in ratemaking.

Managing Employees

Management of its employees constitutes one of the Service's major challenges in meeting goals and maximizing performance. The Service employs nearly one-third of the federal civilian workforce and is the single largest federal civilian agency. To carry out its mission, the Service had a total of about 900,000 career and noncareer employees as of September 30, 1998.[5] To operate effectively in a rapidly changing environment, the Service has recognized that it will need to give human capital issues a higher priority and enhance each employee's contributions to organizational performance. The Service's Year 2000 Performance Plan states that its revised Voice of the Employee goal "elevates the quality of the overall workplace environment from a subgoal category to a corporate

[5]According to the Service, career employees generally are persons who have permanent work appointments and include such employees as clerks, postmasters, managers, supervisors, mail handlers, and city and rural letter carriers. Noncareer employees are persons who have limited-term work appointments and include such employees as some data conversion operators who work at postal remote encoding centers and substitutes for rural carriers.

goal, and emphasizes that the end result should achieve organizational and individual success."

Labor-Management Relations

We have previously reported on long-standing problems in labor-management relations that have affected the postal workplace environment. Although the Service has continued to make progress in improving its labor-management relations, problems still exist that appear to create barriers between the Service and its main employee organizations, including four major postal labor unions and three management associations. Such barriers have often stood in the way of agreements being reached among the eight organizations, including postal labor unions' collective bargaining agreements, that could help ensure the most effective management of the Service's employees. Also, disagreements have prevented the establishment of an overall framework agreement, which we recommended in our 1994 report on postal labor-management relations.[6] Such an agreement could help the eight organizations focus on common approaches for addressing persistent labor-management relations problems so that the Service's work environment can be improved and its competitive position in a dynamic communications market can be maintained.

The Service has identified a number of goals and strategies to improve its workplace relations and to enhance various employee programs, such as its diversity program. However, full success of these efforts is unlikely without a partnership between postal managers and employees. Without such a partnership, difficulties in the postal workplace are likely to persist and hamper the Service's ability to best achieve its overall performance goals.

One area that has historically posed a challenge to the Service and its unions and management associations involves compensation and benefits issues. The most recent contract negotiations occurred during the last year for three of the four major postal labor unions whose contracts expired in November 1998.[7] Negotiations for new contracts between the Service and two of the three unions—the American Postal Workers Union (APWU) and the National Postal Mail Handlers Union (Mail Handlers)—produced settlements without the use of arbitration. However, for one of

[6]U.S. Postal Service: Labor-Management Problems Persist on the Workroom Floor (GAO/GGD-94-201A/B, Sept. 29, 1994).

[7]The three major postal labor unions involved in 1998 contract negotiations with the Service included APWU, NALC, and Mail Handlers. The fourth union—the National Rural Letter Carriers' Association—did not participate in such negotiations because its contract is not due to expire until November 1999.

the three unions—the National Association of Letter Carriers (NALC)—interest arbitration involving a third-party negotiator was used to settle contract disputes regarding employee wages and benefits and to reach an agreement last month.

In recent months, concerns about compensation and benefits for postmasters have also been raised by members of two of the three management associations, including the National Association of Postmasters of the United States (NAPUS) and the National League of Postmasters of the United States (NLPM).[8] Unlike the unions, management associations, which generally represent the interests of postal managers, supervisors, and postmasters, may not collectively bargain for contract employment terms. However, the Service is required by the Postal Reorganization Act of 1970 to consult with the management associations on various issues that affect their members, including compensation and benefits. We briefed the Subcommittee earlier this year on the concerns that had been raised by organizations representing postmasters related to compensation issues. In August 1999, these management associations reached agreement with the Service on compensation matters. However, these associations have continuing concerns related to the extent of the differential in pay between bargaining unit employees and supervisory and managerial employees.

During the past year, our work related to postal employees has focused mainly on issues involving diversity and equal employment opportunity (EEO) and employee safety and health. I would like to briefly discuss the results of our completed work and provide information about our continuing work efforts in these areas.

Diversity and Equal Employment Opportunity

One of the Service's many challenges involving employees relates to the areas of employee diversity and EEO. In large part, our completed work in these areas has generally addressed the Service's efforts to achieve specific diversity goals, such as the promotion of women and minorities into higher postal management levels, and the Service's tracking and monitoring of specific data related to EEO complaints.

Concerning the promotion of women and minorities to higher management levels, we issued two reports to Congressman Danny Davis, one in

[8]The three management associations include NAPUS, NLPM, and the National Association of Postal Supervisors.

September 1998,[9] and one in February 1999.[10] In the September 1998 report, we discussed the results of our work on the Service's compliance with promotion procedures at three postal locations.[11] Specifically, we obtained and analyzed various data to determine the extent to which women and minorities were represented at the higher Executive and Administrative Schedule (EAS) management levels. The results of our work showed that for 117 promotions that were awarded in 3 postal locations, many of the applicants (62 percent) and those determined best qualified (64 percent) were women and minorities. Also, of the employees promoted to higher level management positions in the three locations, about 62 percent were women and minorities, compared with the 59 percent at the same grade levels in these locations before the promotions took place.

In addition, our February 1999 report to Congressman Davis supplemented the September 1998 report by providing comprehensive data on the extent to which women and minorities were represented at higher postal management levels, including promotion-related data. The February 1999 report also included information on other issues, such as (1) the lack of reliable EEO data on promotion applicants' progress through the promotion process and (2) the Service's progress in responding to specific recommendations made in 1997 by Aguirre International—an outside firm that reviewed the Service's diversity program—that were intended to help the Service strengthen its program.

In the February 1999 report, we recommended that the Postmaster General ensure that appropriate Service officials capture and use EEO group data to help improve the Service's diversity program, including the identification of any barriers that might impede promotions to high-level EAS positions. In response to our recommendation, the Vice President for Human Resources told us that she would emphasize to postal field facilities the need to enter data into the appropriate data system so that more complete and reliable information about promotions could be maintained and used as a tool to identify the points that impede the promotions of applicants to high-level EAS positions.

[9] U.S. Postal Service: Information About Selected Promotions of Women and Minorities to EAS Management-Level Positions (GAO/GGD-98-200R, Sept. 21, 1998).

[10] U.S. Postal Service: Diversity in High-Level EAS Positions (GAO/GGD-99-26, Feb. 26, 1999).

[11] The three locations where we reviewed applications for the 117 promotions included the Atlanta, Dallas, and Van Nuys performance clusters. A performance cluster is 1 of the Service's 85 geographic service areas and includes a customer service district, which is responsible for overseeing post offices, and 1 or more mail processing plants.

Also, the results of some of our completed work in the area of EEO complaints indicated that shortcomings existed in the collection and reporting of specific EEO-related data, such as the bases for complaints and issues involved in the complaints. Without reliable information, managers will not be able to determine how best to address problems regarding the nature and extent of conflict in the postal workplace or assess the extent to which improvements can be made.

In addition, as requested by Congressman Chaka Fattah, the Subcommittee's Ranking Minority Member, we are currently reviewing the Service's progress in achieving a diverse workforce in its Postal Career Executive Service (PCES), which represents the Service's senior level officers and executives. We are working to obtain information about diversity within PCES similar to the information that we provided in our February 1999 report about diversity within the Service's high-level EAS workforce.

Employee Safety and Health

Another significant challenge the Service faces is implementing the Postal Employees Safety Enhancement Act. Prior to the act, the Postal Service was required to comply with Occupational Safety and Health Administration (OSHA) safety and health program requirements for federal agencies. When OSHA found safety and health problems at postal facilities, it issued notices of unsafe or unhealthful working conditions, but it did not issue citations or levy monetary penalties. However, the act, which became effective on September 28, 1998, required the Postal Service to comply with OSHA requirements for private sector employers. Accordingly, OSHA may now impose citations and monetary penalties on the Postal Service for noncompliance.

In converting from requirements for federal agencies to provisions for private sector employers, postal officials stated that they would have to review and modify existing safety and health policies, programs, procedures, systems, training, and education programs, as well as modify recordkeeping procedures for accident and injury data. The officials said that challenges associated with implementing the requirements of the act include (1) modifying existing automated systems at the same time that government, industry, and the Service are dedicating their technical resources to ensure Year 2000 compliance; (2) developing and implementing training programs on the judicial and other processes that previously were not applicable to the Postal Service for safety personnel, legal staff, and key operations staff; and (3) modifying the Service's financial system to track expenses associated with implementing the new requirements.

Maintaining Financial Viability

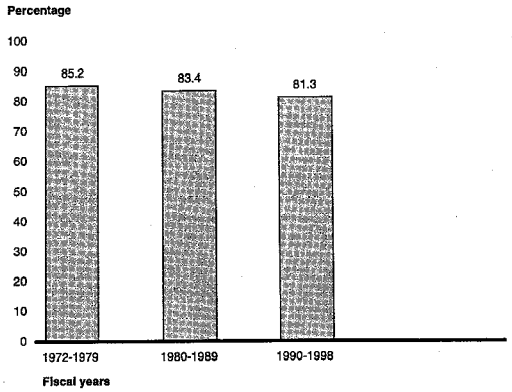
The Postal Service's ability to maintain financial viability by controlling costs, improving productivity, and enhancing revenues also presents a continuing challenge. The Service's strategic plan stated that aggressive cost management would be necessary to guarantee success in mitigating historic cost trends that drive price increases. The Service's Annual Performance Plan for Fiscal Year 2000 established goals for controlling costs through cost reduction programs as well as by achieving productivity gains. The plan also reported that it is not unusual for the Service's productivity to fluctuate from one year to another, but over the long run a successful organization will achieve positive growth in productivity. Further, the Service has recognized that it must have strong and effective internal operating controls to avoid unwarranted costs and protect its revenues.

Controlling Costs

Effective management of the Service's capital investments is critical if the Service is to achieve its projected return on investments. The Service reported that it has made aggressive capital investments in technology and infrastructure to improve the distribution and delivery of mail as well as reduce labor costs.

In September 1998, the Postal Service Board of Governors confirmed the Service's plan to spend $17 billion through fiscal year 2002 on capital investments that are intended to automate and modernize operations and control costs. The Service has reported in the past that it intends to substitute capital for labor to help it achieve its financial goals. As shown in figure 4, labor-related expenses accounted for more than 80 percent of the Service's total expenses in each of the past 3 decades. The Service's labor-related expenses declined somewhat during the 1990s but continued to represent 79 percent of the Service's expenses in fiscal year 1998, the most recent year for which data are available.

Figure 4: Labor-Related Expenses Accounted for Most of the Postal Service's Total Expenses



Note: Labor-related expenses include such costs as employee compensation and benefits, retroactive assessments for employee benefits, imputed interest expenses on retroactive assessments for employee benefits, interest expenses on deferred retirement liabilities, and workers' compensation expenses of the former Post Office Department. Percentages shown were compiled by dividing the Postal Service's total labor-related expenses for each period by the Service's total expenses for that period. Data for fiscal year 1999 are not yet available.

Source: U.S. Postal Service annual reports.

The Service stated in its Five-Year Strategic Plan for fiscal years 1998 through 2002 that the cost paid for labor resources is the primary driver of Postal Service prices, and that significant revenue growth must be matched by aggressive cost management for the Service to mitigate historic cost trends that drive price increases. Further, the Service has recognized that its stakeholders are also demanding aggressive cost management.

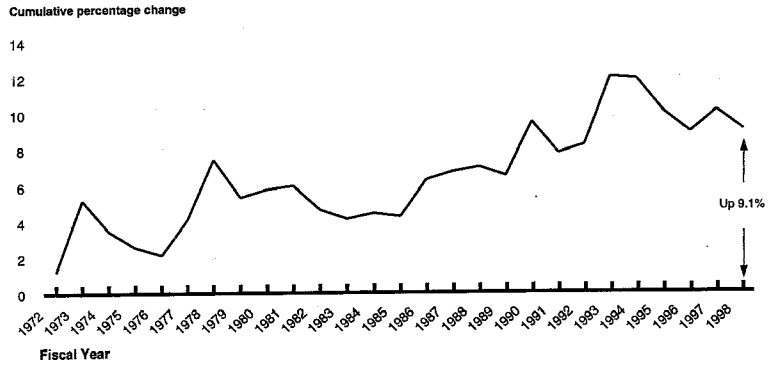
As mentioned earlier, although the Service has improved its delivery performance in some areas, questions remain about whether the Service is adequately realizing the anticipated savings from its capital investments. Last year, the Board of Governors approved a capital investment budget of $4.4 billion for fiscal year 1999, of which the largest component–$1.7 billion–was committed to facility projects, and $1.5 billion was committed to equipment projects. Last year, we reported to the Subcommittee on the

Service's shortfalls in reaching its projected carrier workhour savings from its investments in automated sorting equipment.[12]

Improving Productivity

The Service has reported that its Integrated Financial plan for Fiscal Year 2000 relies on "aggressive productivity improvement" in order for the Service to meet its "challenging bottom-line target" of $100 million in net income. The Service's performance plan for fiscal year 2000 set a target of increasing total factor productivity (TFP) by 3.1 percent.[13] To put this challenge into context, figure 5 indicates that TFP increased at least 3 percent in only 4 years since postal reorganization was implemented (1973, 1978, 1990, and 1993).

Figure 5: Growth in Postal Service Productivity



Note: Data for fiscal year 1999 are not yet available.

Source: U.S. Postal Service.

[12]U.S. Postal Service: Progress Made in Implementing Automated Letter Sequencing, but Some Issues Remain (GAO/GGD-98-73, Apr. 17, 1998).

[13]TFP measures the changes in the relationship between the Service's outputs and resources expended in producing those outputs. The Service's main outputs are mail volumes and servicing an expanding delivery network. By tracking outputs and resource usage, TFP provides a measure of historical performance.

In addition, TFP declined in 4 of the last 5 years for a cumulative decline of about 3 percent. The Service reported that the TFP decline in 1998, the most recent year for which data are available, was linked to an increase in its capital investments and the conversion of many transitional employees to career status. The Service reported that it expects to realize deferred benefits from automation that should help increase its productivity in the future.

The Service has reported that its aggressive capital investments, though consistent with its long-term strategy of substituting capital for labor, may have a short-term negative impact on TFP due to implementation costs and the difference between the timing of costs and the realization of savings. The Service's plan for $4.0 billion in capital commitments[14] in fiscal year 2000—compared with $3.9 billion in capital commitments in fiscal year 1998 when TFP declined by 1.1 percent—points to the challenge of increasing TFP by the target of 3.1 percent in fiscal year 2000. Moreover, the Service has reported that some investments improve service but do not improve TFP.

The Service has cautioned that TFP is best used to analyze long-term trends and is not effective as a short-term measure or snapshot in time. In this regard, as figure 5 shows, TFP increased 9.1 percent from the time that postal reorganization was implemented to fiscal year 1998. The Service has recently reported that its objective is to improve TFP over time while maintaining a balance with the service improvements necessary to achieve customer satisfaction and maintain a competitive position in the marketplace.

Enhancing Revenues

Another key area of the Service's financial goals is to enhance revenues. In the past, we have raised concerns about the adequacy of the Service's controls over its revenues in areas such as the acceptance of bulk business mail.[15] In fiscal year 1998, bulk business mail represented 49 percent of the Service's $58 billion in mail revenues and about 66 percent of the nearly 200 billion pieces of mail it processed. We are currently conducting a follow-up review to determine the status of the Service's actions to implement our recommendations. We expect this report to be issued within the next several weeks.

[14]The Service's capital commitments in its Capital Investment Plan represent expected contract awards or options. The Service generally does not pay for these expenses until the goods are delivered or a contractor meets its project schedule.

[15]U.S. Postal Service: Stronger Mail Acceptance Controls Could Help Prevent Revenue Losses (GAO/GGD-96-126, June 25, 1996).

The Service has also enhanced its revenues through leasing or selling some of its real estate. We recently issued a report that looked at two real estate projects where the Service leased space to private companies that developed and operated the buildings—the Grand Central Station Post Office in New York City and Rincon Center in San Francisco.[16] The Service reported obtaining about $16.5 million annually in revenue from renting space in the renovated buildings while preserving their historical characteristics. In addition, the Service recently sold the Rincon Center for $80.5 million, which the Service reported added to its net revenues.

Competing in a Rapidly Changing Environment

The Service's ability to adapt to increasing competition is critical if the Service is to maintain a competitive position in the rapidly changing communications and delivery environment. Increasing competition, particularly from electronic alternatives, has slowed the Service's revenue growth and is expected to have a continuing impact on the Service's revenues in the next decade.

Other issues related to the Service's competitive position have also been raised. Some concerns revolve around types of new products and services that the Service is allowed to develop. We recently provided information on the Postal Service Marketing Department's process for the review and approval of its new products. Also, some of our work has addressed various concerns regarding the Service's competitive position with respect to international postal organizations.

New Postal Products

The Service has for several years been concerned that its First-Class Mail business could become threatened as more and more traditional mail migrates to electronic mail. Coupled with this, the Service has encountered competition from the private sector that is significantly more challenging than in past years. To address these situations, postal management, in the early 1990s, established a corporate goal of initiating and growing new businesses, particularly in the electronic communications arena, in order to ensure its commercial viability as a mover of messages, merchandise, and money.

As a result of this corporate decision, in the mid-1990s, the Service began focusing resources on the aggressive development and introduction of new products—primarily nonpostal products. In November 1998, we reported on the challenges faced by the Service in moving in this new direction and

[16] Public-Private Partnerships: Key Elements of Federal Building and Facility Partnerships (GAO/GGD-99-23, Feb. 3, 1999).

presented a snapshot of the progress made to date.[17] We reported that the Service's new products initiative was controversial. Some Members of Congress were concerned that the Service was unfairly expanding its product line to compete in nonpostal-related markets and had introduced legislation to curtail such activity. Some private sector companies also complained about the Service's entry into nontraditional postal markets. They were concerned that the Service could use its governmental status to an unfair advantage when introducing products that compete with private sector companies. Notwithstanding this controversy, the Service moved ahead with several new products in the mid- to late-1990s.

The Service has established a formalized process to govern the introduction of most new products. To facilitate the process of developing and introducing new products and to ensure effective management control, the Service developed a formalized system of checks and balances that requires top management buy-in at critical stages of the product development process. The process is also to be used to review the performance of products and terminate those that do not perform to Postal Service expectations. For those products we reviewed in more detail, we found that the Service had generally followed the tenets of the newly established product development process. We also reported that most of the new products had not yet produced revenues that exceeded expenses. We cautioned, however, that it might not be reasonable to expect all new products to become profitable in their early years, because new products generally take several years to become established and recover their start-up costs.

International Competition

Congress has recently considered one of the major international competition-related concerns involving a potential conflict in the Service's dual role as the U.S. negotiator of international postal agreements and competitor with private carriers in the international mail arena. In a recent report, we compared the roles of the Service and the Department of State as representatives of the U.S. government in international organizations for the postal and telecommunications sectors.[18] The Department of State has the lead responsibility for developing U.S. international telecommunications policy and heads a formalized process for policy development. In October 1998, Congress transferred responsibility for formulating, coordinating, and overseeing international postal policy at the international postal organization, the Universal Postal Union (UPU), from

[17] U.S. Postal Service: Development and Inventory of New Products (GAO/GGD-99-15, Nov. 24, 1998).

[18] U.S. Postal Service: Postal and Telecommunications Sector Representation in International Organizations (GAO/GGD-99-6BR, Oct. 29, 1998).

the Service to the Department of State. We are currently reviewing how effectively the Department of State has implemented its new responsibilities in this area.

Our October 1998 report noted that differences in legal requirements contributed to differences in stakeholder involvement and the processes used to develop U.S. policies for international postal and telecommunications issues. One key difference was that the Department of State was legally required to obtain input from the private sector on international telecommunications policy issues; however, the Service was not subject to such legal requirements when it had the lead role for U.S. involvement in the UPU. In the international telecommunications sector, we found that government and private sector stakeholders had more direct involvement in U.S. policy formulation through a structured and documented advisory committee process headed by the Department of State and subject to the requirements of the Federal Advisory Committee Act (FACA).[19] FACA requirements include Federal Register notice of advisory committee meetings; detailed minutes of meetings; public access and participation at meetings; and annual reports to the General Services Administration, which is to report to Congress on the activities, status, and any changes in the advisory committees. In the postal sector, the Service was not subject to FACA. The process for involving government and private sector stakeholders in international policy formulation was more informal, involving ad hoc briefings with limited public notice or documentation of meetings. Our ongoing review will examine how the process for U.S. policy formulation, coordination, and oversight has changed this year with respect to U.S. participation in the UPU.

Other Major Issues

Other major issues we recently addressed include monitoring the Service's actions to meet the challenges of preparing for the Year 2000 as well as protecting consumers from deceptive mail practices, protecting the privacy of address changes, and improving its management of capital facility projects. Currently, we are also reviewing the effectiveness of the Breast Cancer Stamp as a fundraiser.

Regarding Year 2000 readiness, we testified that the Service started late in correcting and testing its systems, preparing a master schedule, and developing contingency and business continuity plans. However, the Service has made significant progress in reducing vulnerabilities identified

[19]FACA was enacted to ensure that (1) valid needs exist for establishing and continuing advisory committees, (2) the committees are properly managed and their proceedings are as open as possible to the public, and (3) Congress is kept informed of the committees' activities.

in previous assessments and in planning a recovery management process to restore its operations if Year 2000 problems should occur.

We also testified recently before this Subcommittee on our work related to protecting consumers from deceptive mail marketing practices.[20] We provided information on the extent and nature of consumers' problems with deceptive mail and identified initiatives various federal agencies and other organizations have made to address deceptive mail problems and educate consumers.

We also recently released a report on another issue of interest to consumers, the Service's protection of consumer address information from unauthorized disclosure.[21] We followed up on the recommendations we had previously made for specific actions the Service should take to strengthen oversight of its National Change of Address (NCOA) program. The Service had not taken action on our recommendation that it explicitly state, in the acknowledgment form signed by customers of the Service's address correction licensees, that NCOA program-linked data are not to be used to create or maintain new-movers lists. We have suggested that Congress may wish to consider amending the Postal Reorganization Act of 1970 to establish requirements concerning the language in the form so that the Service could help ensure that the use of NCOA program-linked data is limited to the purposes for which they were collected.

Year 2000 Problems

The Postal Service faces a major challenge in updating its computer systems, mail processing equipment, and infrastructure equipment to avoid Year 2000 malfunctions that could disrupt mail delivery. The Service has a special responsibility to correct its computers because a number of private sector and government groups may need to use the Service as a backup delivery system if their computers malfunction. For this reason, the Service is concerned about the prospect of a mail surge in January 2000. An early assessment by the Service's Office of Inspector General showed that the Service was slow to recognize the scope of the challenge and act to ensure that its computer systems were Year 2000 compliant.

In February 1999[22] we identified the major challenges facing the Service, including (1) completing system renovation and mail processing

[20] Deceptive Mail: Consumers' Problems Appear Substantial (GAO/T-GGD-99-150, Aug. 4, 1999).

[21] U.S. Postal Service: Status of Efforts to Protect Privacy of Address Changes (GAO/GGD-99-102, Jul. 30, 1999).

[22] Year 2000 Computing Crisis: Challenges Still Facing the U.S. Postal Service (GAO/T-AIMD-99-86, February 23, 1999).

equipment correction and testing, (2) ensuring the readiness of hundreds of local facilities, (3) determining the ability of key suppliers and electronic data exchange partners to be Year 2000 ready, (4) completing simulation testing of business process areas, and (5) completing the development and testing of business continuity and contingency plans.

Since February, the Service has strengthened its management approach to the Year 2000 problem and made significant progress in fixing its systems and determining that its key suppliers and electronic data exchange partners will also be Year 2000 ready. For example, as of this August, the Service reported to the Office of Management and Budget that it

- completed renovation of 136 of its 137 severe and critical computer systems and expected to complete all non-mission critical systems by September 30, 1999;
- certified all 38 critical mail processing equipment and embedded chip devices as Year 2000 ready;
- performed business impact assessments on all 353 critical field facilities and expected to finish remaining readiness activities by October 15, 1999;
- expected to complete impact assessments by November 30, 1999, for all 3,500 field activities that have automated systems and functions with life safety and security ramifications;
- obtained assurances of Year 2000 readiness for 273, or 99.6 percent, of its critical suppliers and completed site visits for all 34 "high profile" suppliers, i.e., those most integral to the continuity of mail operations;
- obtained assurances on Year 2000 readiness for 73 percent of suppliers critical to the Service's field operations; and
- certified all 737 severe and critical electronic data exchanges as Year 2000 compliant and reported that all 106 important, but not critical, electronic data exchanges would be certified as compliant by September 30, 1999.

The Service has also stepped up efforts to test applications and infrastructure equipment in a production environment—an important phase of the Year 2000 effort because Year 2000 conversions often involve numerous large interconnecting systems with many external interfaces

and extensive supporting technology infrastructures. Over 40 applications that support critical business processes were tested in the first of a two-phased testing effort that ended in August 1999. The Service is still analyzing the results of these tests; however, it has reported that at least one application will require additional testing.

Finally, the Service has completed over 500 business continuity and component contingency plans for its critical processes. This is another crucial phase of the Year 2000 effort because core processes may still be disrupted by Year 2000-induced failures and by errors in business partner systems or public infrastructure systems, such as power, water, transportation, and telecommunications systems. The Service's plans include preemptive measures and work-arounds to ensure critical business processes continue in the event of a Year 2000-related disruption or system failure. The field plans were distributed in August 1999, and all rehearsals and adjustments to these plans are expected to be completed by November 30, 1999.

With these actions under way, the Service is clearly much better positioned to face the upcoming century change. However, the challenge facing the Service is still significant: there are less than 3 months remaining before the Year 2000 deadline, the Service is now entering into the holiday business rush, and many important tasks—including the rehearsal and finalization of contingency and continuity plans—remain. Thus, the Service will need to sustain top management attention to the problem and continue to do everything necessary to ensure that the continuity of important postal operations is maintained into 2000.

Status of Antelope Valley Project Remains Uncertain

The importance of sustained management attention was evident in another area where we identified weaknesses in the management of a capital facility project. In August 1999, we reported on the Service's project approval process for a proposed project to relocate postal operations to a new mail processing facility in the Antelope Valley area in California.[25] We raised concerns about the unresolved status of the proposed project after almost 10 years. The Service purchased a 25-acre site in Lancaster, CA, for $6.5 million in 1991 that has since remained unused due to the Service's failure to decide on whether the proposed processing facility should be approved. Also, we estimated that accumulated interest costs associated with this $6.5 million investment totaled about $2.9 million from the time the site was purchased in October 1991 through June 1999, and they were

[25] U.S. Postal Service: Deficiencies Continue While Antelope Valley Project Status Remains Uncertain (GAO/GGD-99-147, Aug. 31, 1999).

likely to increase by over $300,000 each year. In addition, the Service has not addressed the long-standing problems, such as mail delivery problems and space deficiencies, that were the basis for the proposed Antelope Valley project. We recommended that the Postmaster General take action to resolve the status of the project and report on planned actions to address the operational deficiencies in the Antelope Valley area.

Breast Cancer Research Stamp

One of our ongoing efforts is a review of the Service's Breast Cancer Research Stamp. The "Stamp Out Breast Cancer Act," enacted August 13, 1997, required that the Service market, for 2 years, a semipostal stamp for breast cancer research. A semipostal stamp is a stamp that carries a surcharge for a special purpose.

The Service issued the First-Class Breast Cancer Research stamp on July 29, 1998. The stamp is currently priced at 40 cents—33 cents for postage with a 7-cent surcharge. The stamp is to be available for sale until July 29, 2000. The net proceeds from the surcharge are going to the National Institutes of Health and Department of Defense for breast cancer research. The Breast Cancer Research Stamp is the Service's first-ever semipostal stamp.

In addition to requiring the Service to market the Breast Cancer Research Stamp, the act also mandated that the Comptroller General report to Congress, between January 29, 2000, and April 29, 2000, on the effectiveness and appropriateness of using a semipostal stamp to raise funds for breast cancer research. Also, this report is to include information on the monetary and other resources required of the Service to produce and market the Breast Cancer Research Stamp.

After 1 year of sales, the Service reports that surcharge revenue generated by the Breast Cancer Research Stamp totaled approximately $8 million. We expect to issue our report on the stamp to Congress in the early part of the year 2000, as mandated by the act.

Recommendation

We recommend that the Postmaster General report to the House and Senate oversight subcommittees on the Postal Service on the actions taken and planned to improve the quality of data used in ratemaking, including

- actions taken to improve ratemaking data quality, such as those that relate to the recommendations included in the Data Quality Study conducted by A.T. Kearney; and

- actions planned to improve ratemaking data quality, including the priorities and time frames for short-term and long-term actions.

Mr. Chairman, this concludes my statement. I would be pleased to respond to any questions you or the Members of the Subcommittee may have.

Contact and Acknowledgment

For future contacts regarding this testimony, please contact Bernard L. Ungar at (202)-512-8387. Individuals making key contributions to this testimony included Teresa Anderson, Gerald Barnes, Anne Hilleary, Kenneth John, Sherrill Johnson, Roger Lively, Charles Wicker, and Lisa Wright-Solomon. Kim Raheb provided graphics support. Carl Urie and Greg Donnellon provided information on the Postal Service's Year 2000 compliance.

GAO Postal-Related Products Issued Since June 1, 1998

Performance Issues	The Results Act: Observations on the Postal Service's Preliminary Performance Plan for Fiscal Year 2000 (GAO/GGD-99-72R, April 30, 1999).
	Major Management Challenges and Program Risks: U.S. Postal Service (GAO/OCG-99-21, Jan. 1999).
	The Results Act: Observations on the Postal Service's Preliminary Annual Performance Plan (GAO/GGD-98-144, July 10, 1998).
Employee Issues	Equal Employment Opportunity: The Postal Service Needs to Better Ensure the Quality of EEO Complaint Data (GAO/GGD-99-167, Sept. 28, 1999).
	Equal Employment Opportunity: Complaint Caseloads Rising, With Effects of New Regulations on Future Trends Unclear (GAO/GGD-99-128, Aug. 16, 1999).
	Equal Employment Opportunity: Data Shortcomings Hinder Assessment of Conflicts in the Federal Workplace (GAO/GGD-99-75, May 4, 1999).
	U.S. Postal Service: Diversity in High-Level EAS Positions (GAO/GGD-99-26, Feb. 26, 1999).
	U.S. Postal Service: Information About Selected Promotions of Women and Minorities to EAS Management-Level Positions (GAO/GGD-98-200R, Sept. 21, 1998).
	Equal Employment Opportunity: Rising Trends in EEO Complaint Caseloads in the Federal Sector (GAO/GGD-98-157BR, July 24, 1998).
Financial Viability Issues	Public-Private Partnerships: Key Elements of Federal Building and Facility Partnerships (GAO/GGD-99-23, Feb. 3, 1999).
Competition Issues	U.S. Postal Service: Development and Inventory of New Products (GAO/GGD-99-15, Nov. 24, 1998).
	U.S. Postal Service: Postal and Telecommunications Sector Representation in International Organizations (GAO/GGD-99-6BR, Oct. 29, 1998).
	U.S. Postal Service: Competitive Concerns About Global Package Link Service (GAO/GGD-98-104, June 5, 1998).

Other Major Oversight Issues

U.S. Postal Service: Deficiencies Continue While Antelope Valley Project Status Remains Uncertain (GAO/GGD-99-147, Aug. 31, 1999).

Deceptive Mail: Consumers' Problems Appear Substantial (GAO/T-GGD-99-150, Aug. 4, 1999).

U.S. Postal Service: Status of Efforts to Protect Privacy of Address Changes (GAO/GGD-99-102, July 30, 1999).

Year 2000 Computing Crisis: Challenges Still Facing the U.S. Postal Service (GAO/T-AIMD-99-86, Feb. 23, 1999).

Proposed Legislation: Issues Related to Honesty in Sweepstakes Act of 1998 (S. 2141) (GAO/T-GGD-98-198, September 1, 1998).

Mr. MCHUGH. I recognize Mr. Fattah.

Mr. FATTAH. I just want to put this on the record. We have to go to vote. Immediately after the vote Title I is coming back to the floor. I have two amendments scheduled for debate on the floor. I may not be back with you for a while, but you are in capable hands. I will have some written questions that my staff will submit to the panel.

Mr. MCHUGH. We thank the gentleman. I appreciate his work on Title I. That's a very important bill. So we will go vote. It's a Journal vote, so it doesn't take a lot of time or thought. It's yes or no. And try—if I could ask those Members that can, return as soon as they can. We stand in recess. Thank you.

[Recess.]

Mr. MCHUGH. I'm here. You're here. Let's start.

Mr. Ungar, let's begin with you. Obviously your report has created some interest, and I think that's a good thing. I think it can help us to focus on the challenges that many of us had thought were certainly on their way, but most of us thought, I believe, that they were a little bit further away than what we're now hearing.

The projections you used are from the Postal Service itself. Did you have an opportunity to examine the probable validity, the accuracy, the level of confidence on those, and if so, how do you evaluate that? Pretty good projection, do you think? Reasonable?

Mr. UNGAR. We didn't do a full evaluation of that, Mr. Chairman. It seemed reasonable on the surface, but again, I'd have to say we did not certainly independently verify the information, and I think it's difficult to predict the future. I think the Service looked at the—looked historically at what the situation has been, and certainly what the current scenarios are, and what the likely trends are given electronic communication and competition, and put the estimate together.

Mr. MCHUGH. For your purposes, you took that figure as moderately reliable; might be higher, might be a little lower, but as far as we can tell sitting here today, 2½ percent within the next 3 years seems reasonable?

Mr. UNGAR. It's in the ballpark. Again, predicting exactly in what year, at what point in time and exact percent I think is going to be very difficult. It certainly seems to be reasonable given the scenarios.

Mr. MCHUGH. I remember when I graduated from high school that was an end of an era. It was the end of a not-so-good era and the beginning of a pretty good one. When I decided not to run for reelection in the New York State Senate, that was the end of an era. I came down here. It was the start of not such a good era. How do you phrase "end of an era" in your report?

Mr. UNGAR. Mr. Chairman, Mr. Davis, Mr. LaTourette, basically we're using it in the context of a major change. Now, whether it's positive or negative I think depends upon, as in your experience, how the Service and the Congress deal with the formidable challenges that the country faces in terms of what's facing the Postal Service. Obviously its performance in recent times is good. The Service may feel good at the end of one era, but as we approach the next millennium, I think the competitors are here. They're probably here in this room. They're out there.

Mr. MCHUGH. They're always out there.

Mr. UNGAR. That's right, yes. They're not only domestic competitors, but they're foreign competitors, too, as you know, who are here and there may be more on the way. That is coupled with electronic commerce, coupled with the kind of unique organization that the Postal Service is, sort of half governmental and half private, and some of the constraints it faces, it doesn't have, on the one hand, some of the flexibility that the private sector firms have. On the other hand, it has some protections. It doesn't have to do some things that the private sector has to do, although that's dwindling in some cases like in the area of worker safety. So it really is a situation in which the Service is going to have to face the challenge. It's going to probably have to change—I don't know if I should use the word reform.

Mr. MCHUGH. Go ahead.

Mr. UNGAR. But I think it can't do it certainly alone. I think the Congress is going to really have to work with the Postal Service, and as we mentioned in our statement, I think it's going to be very important for the Postal Service to effectively work with the human capital, the employees in the Postal Service, and somehow in some way, and I'm not quite sure how, to do better in terms of working relationships with the unions, particularly the clerks and the city letter carriers, than it has in the past. It's been very confrontational.

I think as we testified before, the implementation of delivery point sequencing was a major dilemma and a major difficulty for the Postal Service working with the unions, with the city letter carrier union. In the future there undoubtedly are going to be changes. I don't know exactly what those changes are going to be. We don't see how the Postal Service is going to make progress without more of a cooperative effort. We think the Results Act and the goals that the Postal Service has set and the goals it will set working with the stakeholders, including the unions, might be a vehicle to try to reach agreement on some common goals relative to its future viability for both the well being of its employees and its financial viability.

Mr. MCHUGH. You really segued into just the last part before I turn it over to my colleagues, and then if we have time, I'd like obviously to get back to Ms. Corcoran and also to you. This is what the Postmaster General later will describe, and I'm assuming you agree with this generalization as well. It could put at risk $17 billion of Postal Service revenues. That's almost 30 percent of its current operating stream. That's an enormous challenge.

I'm hearing you say that the Postal Service has certain inherent problems in House problems that it needs to stand up to. But as well, it probably can't go it alone; that the Congress and, I would assume, this subcommittee and this House has a role as well to try to—let's not use the word reform—reposition the Postal Service. I think I heard you say as well there are two things about that. One, to allow the Postal Service to respond to this new era in a way that all of us agree is appropriate, whatever that way may be, but also perhaps to level the playing field as that activity interfaces with the private sector. Is that a fair description of what you said?

Mr. UNGAR. Yes, sir. I think it will be, of course, a public policy decision on that level playing field and how far one goes and the consequences for the public in terms of universal service.

Mr. MCHUGH. Absolutely. I don't want to presume to ask you to help us there. That's supposedly what we get paid for. Thank you.

Let me yield to Mr. Davis.

Mr. DAVIS. Thank you very much, Mr. Chairman.

Ms. Corcoran, I was very intrigued by your testimony, especially the level of progress that you indicate in being able to identify areas of need and then coming up with movement toward some resolution of those. Did I understand that by contracting out priority services, that that had not been an increase in on-time delivery?

Ms. CORCORAN. A very small increase, less than 2 percent, I believe.

Mr. CHAMBERS. About 1 to 4 percent.

Ms. CORCORAN. About 1 to 4 percent.

Mr. DAVIS. Did I understand that this system, though, saved the Service $100 million?

Ms. CORCORAN. No, it cost an additional $100 million over doing it in-house because they have to put their own infrastructure together, the contractor does, to do this.

Mr. DAVIS. So we spent an additional $100 million to contract out priority services and yet did not experience much in the way of an increase of on-time delivery.

Ms. CORCORAN. That's correct.

Mr. DAVIS. That is, in discussions or conversations, did you get anything relative to what the rationale had been for making the decision to contract those services out?

Ms. CORCORAN. Yes, we did. The Postal Service realized at the time that they were doing the contracting that it was going to cost more to contract, and that's one of the things that they pointed out to us numerous times, that they had been aware of this from the start.

Mr. Chambers has been involved in a lot of the discussions with Postal Service, so I'd like him to address that.

Mr. CHAMBERS. Actually, as our report indicates, this really stemmed from a problem earlier in the decade with delivery rates for priority mail. This was an initiative on the part of the Postal Service. This network was created to try and get the on-time performance scores for priority mail to increase. They felt that a dedicated network that would be operated primarily on the east coast would increase those scores. In the process, they contracted out to a vendor, and again, as we've said, that is a more expensive proposition. We really haven't been able to document that it's increased the performance a lot. Part of that stems from the fact that they didn't create a baseline of performance in that area, so it's kind of hard to say that the performance in that region today is much better than it was before. So what we did was to compare the performance in that region with similar regions of the Postal Service where they operated without a contractor. That's the basis on which we say there was very little increase in performance.

Mr. DAVIS. Did we find that their projections were off or the analysis just was not good from the beginning? Were there changes

in the environment which took place that had not been foreseen that could have resulted in the lack of performance?

Mr. CHAMBERS. Well, again, the performance in that region today is comparable to what it is in other regions of the Postal Service. Also there is really no evidence that before the network there was a significantly lower performance in that region before. They were trying to get scores higher. The percentage of on-time delivery, they're trying to get that up to like 95–96 percent. It's coming close to that, but again it's not much lower than that in other highly developed urban type areas of the United States.

Mr. DAVIS. Thank you. Ms. Corcoran it is also my understanding that the Postal Service failed to collect $20 million in revenue because they charged a lower negotiated international rate for mail actually processed as domestic mail. If that is the case, is there something that they need to do? What can they do to get this under control?

Ms. CORCORAN. This, I believe, is a one-time instance as far as we know. We're certainly going to be looking at that. They do have rules and procedures in place. The mail was to be put in the mail stream outside the country; instead it was actually trucked into the country and put into the mail stream here. Had it been put into the mail stream outside of the country, the international rates would have been appropriate. But we even found they were losing revenue even at that, because it was costing them more than what it would have.

Mr. DAVIS. But you would think that the corrective action has been taken that would prevent any recurrence.

Ms. CORCORAN. We just issued that report at the end of September. We will be going back and working with them to assure that they have taken corrective action on it.

Mr. DAVIS. Thank you very much.

Mr. Ungar, the IG has identified a problem with the quality and integrity of data provided by the Postal Service. Obviously, this is some of the information that they would have used to make the prediction or the projection that there's going to be a substantial decline in first class volume in the next decade. How reliable do you find this data to be or think that it is?

Mr. UNGAR. Mr. Davis, as we indicated, we didn't make an independent verification of the data. I think the data we're really talking about relate to the future, the predictions for the future in terms of mail volume that's expected. So again, we aren't in a position to verify that, but on the other hand, I'm not sure how you verify a prediction. All you can do is ask, does it appear reasonable, do the assumptions appear reasonable?

And it's certainly clear that the competition is there. I don't think anybody would argue with that. I think the, you know, the trend toward more and more use of electronic communications, electronic commerce, and the Internet is there.

Now, again we certainly can't say with any certainty that the exact percent is accurate down to the tenth of a point, or we can't certainly say that the exact day or the time is there. But it's certainly—the direction that the Postal Service is projected—reasonable, based on all that information.

Mr. DAVIS. On page 16 of your testimony, you state, and I quote, that the Service reported that it has made aggressive capital investments in technology and infrastructure to improve the distribution and delivery of mail as well as reduce labor cost. How much have we been able to reduce labor costs or is that something that we've been able to determine?

Mr. UNGAR. Mr. Davis, I think it's come down slightly as a percentage of overall costs. I don't believe that labor costs have come down absolutely; is that correct?

Ms. ANDERSON. They have come down as a percentage slightly.

Mr. UNGAR. They've come down as a percentage of total costs. I don't believe they've come down in absolute terms.

I think that's going to be a fairly significant challenge for the Postal Service. I think the customers of the Postal Service, particularly the business mailers, have been expecting to see an actual drop in the cost of operations in the Postal Service and greater efficiency as a result of these capital investments. Unfortunately, it doesn't appear as though the actual savings have materialized as quickly or as greatly as the Postal Service had predicted.

Now one area that we specifically looked at and reported on last year was the delivery point sequencing initiative. There were significant problems in getting that going on schedule and keeping it on schedule. So there were some areas there where the Postal Service didn't realize as much savings as it expected.

Mr. DAVIS. Finally Mr. Chairman, if I might, Ms. Corcoran, you indicated that you had discovered, or that your office found $1.1 billion during the last 6 months in monetary benefits. Do you have any idea of what's actually out there, how much more there might be or how much more one could look for?

Ms. CORCORAN. I wish I did, but I don't. $1.1 billion—the cost avoidance through fiscal year 2007—is fairly significant to have found in a 6-month period. In all honesty, I would hope that we don't find that much every 6 months because it would indicate that things aren't going as well within the Postal Service as you would hope. But we will continue to look and to work with them to try to improve things, so there's not that type of monetary savings.

Mr. DAVIS. Well, I think you've done an outstanding job in that area. And I would hope also that you don't find much more because it's not there.

Thank you, Mr. Chairman.

Mr. MCHUGH. I thank the gentleman.

The gentleman from Ohio, Mr. LaTourette.

Mr. LATOURETTE. Thank you, Mr. Chairman, and thank you for having the hearing. Ms. Corcoran, I, having been a member of this subcommittee now for a few years, want to give you and your office praise—for every time you appear before the subcommittee first, and second of all, for the fine work that you've done and the reports that you've issued.

I do want to talk to you about your written testimony in two parts, one on page 4. There was a conclusion reached by you and your office that found that the international business unit of the Postal Service did not have key processes in place to achieve projected revenue goals and that some initiatives fell short of revenue projections. And then on page 8, in the list of reports that you've

issued, the second bullet point on page 8 indicates that your office examined the financial profitability of international mail and determined that international mail contributed positively to the financial position of the Postal Service and is not subsidized by domestic mail service.

I guess—can you reconcile those two paragraphs for me? Do I understand, in the international mail arena, the Postal Service has 14 what are called outbound mail services. And if I understand what you're saying on page 4, you're saying that not all of those are operating in a revenue positive position for the Postal Service, but on page 8 are you saying, overall, that the Postal Service's international mail operation is—it's covering its costs and it's not being subsidized by domestic mail?

Ms. CORCORAN. This is a little confusing when you compare those two. On page 8 what we're talking about there was a question that was asked quite often a year ago about whether or not international mail was cross-subsidized by domestic mail. And page 8 we did a review, and we found that that was not occurring.

The review that we talk about on page 4 was really a review of the international business unit as a whole, not necessarily of their products, but of their initiatives. We were looking at this separate business unit. In fact up until this point in time, I believe it was the only business unit that the Postal Service had identified as a separate unit. We took a look to see whether or not what they were expecting from this business unit was really going to occur and whether or not the projections in revenues that they had were really appropriate. We found that, as it says here, they fell short of some of the revenue projections.

Mr. LATOURETTE. My question is spurred by a report from June of this year to the Congress by the Postal Rate Commission that examined the 14 outbound international mail products, and they indicated that of the 14, four they found to be noncompensatory; that is, they didn't make as much money as it cost for the Postal Service to be involved in them. And I'm wondering if that squares with what you found, and if it does, in order to have the paragraph of the bullet point on page 8 make sense, are the other 10 making so much money that it covers the deficits in costs for the four that are not? And the four that are cited by the Postal Rate Commission are the surface printed matter and small packet surface periodicals, global priority mail and global package link.

Mr. CHAMBERS. I would like to answer that one for you. Actually when we completed our work, looking at international mail, the possible cross-subsidization, we concluded that there is not cross-subsidization between domestic and international; that is, as a whole, the international products are paying their way. We did, however, I believe in our report raise the possibility that there could be cross-subsidization within the international products; that is, one might not be paying its way and another would.

At the time we concluded our work, we planned to do a second phase. It was about the same time that the Congress gave the Postal Rate Commission additional oversight responsibilities in the international mail arena at which point we deferred to them to take a look at the possibility of cross-subsidization within those products.

Mr. LATOURETTE. Thank you.

Mr. Ungar, is that something you all looked at at GAO?

Mr. UNGAR. We didn't look, Mr. LaTourette, at revenue and expenses in the depth of the Inspector General. We looked at the GPL program last year and reported on that.

Did you want to say anything?

Ms. ANDERSON. We didn't look at whether or not it was being cross-subsidized. Again, we've been working with the PRC and with the Postal Service in looking at the general issue of the quality of ratemaking data, but we did not look specifically at the international area.

Mr. LATOURETTE. Did you make any recommendations relative to GPO?

Mr. UNGAR. Excuse me?

Mr. LATOURETTE. Did you make any recommendations as a result of your analysis, or are you deferring to the PRC in terms of rate?

Mr. UNGAR. Not on GPL. We did, however, make a recommendation to the Postal Service on ratemaking domestically in terms of the Postal Service's response to the contractor's recommendations. I think they only dealt with domestic rates; the contractor didn't look at the international area.

Mr. LATOURETTE. Thank you very much.

Thank you, Mr. Chairman.

Mr. MCHUGH. I thank the gentleman.

I'll come back to that line because I think the gentleman from Ohio has raised some very interesting points that I would like to pursue a little bit further.

But let me yield to my fellow colleague from the great State of New York, Mr. Owens.

Mr. OWENS. Thank you very much, Mr. Chairman. Unfortunately, we have a major bill on the floor for the Education and Labor Committee that I serve on; I won't be able to stay. But I have a couple questions related to the work force.

I'm the ranking Democrat on the Subcommittee on the Work Force, and you acknowledge—we would like to acknowledge the fact that we have seen some impressive efforts in identifying systemic problems in the labor-management area. Specifically I want to ask, has the Postal Service been receptive to your reviews on how to improve the grievance arbitration procedure, reduce the backlog of grievances, and improve the labor climate? And if they have not, why not? If so, what's changed, what's different?

Mr. CHAMBERS. I believe, as we took a look at the grievance and arbitration area, we actually did two or three different reports on that and found that there was an opportunity to review those processes. In fact, we found——

Mr. OWENS. Can you get closer to the mic, please.

Mr. CHAMBERS. We did take a look at the grievance and arbitration area. We issued a couple of reports. One report on the management information data found that they really needed to improve the information they had in the grievance and arbitration area. They agreed with us on our work and said that they would improve that area.

I think our second report dealt more with how the grievance and arbitration cases were handled in terms of working with the unions. If I'm not mistaken, I believe there was not a consensus on how those issues could be resolved. I don't have those details at my fingertips.

Mr. OWENS. Did you not have some reports on conditions in the workplace?

Mr. CHAMBERS. Yes, I believe we have issued a number of those reports as well. Again, specific reports don't come to mind right off, but I know we have issued several reports in those areas.

Mr. OWENS. You're not familiar with the one that deals with the Suncoast district?

Mr. CHAMBERS. Yes, I'm sorry. That's the district-wide review we did on the labor-management climate, and we did find a number of areas where there could be improvement. In fact, it was on that basis that we recommended expansion of our work; and we're now doing it nationally, we're looking at an additional 26 districts.

We did not get an agreement out of—it was an interesting situation, because we actually got more agreement at the local level on the issues than we did as we moved up to the area level within the Postal Service.

Mr. OWENS. Can you explain a little more, if the Postal Service has a zero tolerance for violence, how could that situation be so prevalent? I mean, can you explain?

Mr. CHAMBERS. Well, much of, I think, what we've disclosed dealt with the issue of the labor climate assessments and the fact that those climate assessments were not being done, and that some of the issues that were arising from them were not being corrected. It's on that basis, as we said, we want to do a more nationwide effort on that.

Mr. OWENS. But there was resistance as you went up the chain, you said.

Mr. CHAMBERS. That's my recollection on that particular one. I would have to double-check it, but as I recall—and this is something that's not uncommon—we have, in some cases, gotten more cooperation from management on labor-management issues at the lower levels than when we move up. In fact, the most consistent resistance we get on our labor-management recommendations actually comes at the headquarters level and at the area vice president level.

Mr. OWENS. What is the response of the Postmaster General to that?

Ms. CORCORAN. I have mentioned this to Mr. Henderson. We have been hoping that a Deputy Postmaster General would be put in place so we could start working with them. Now they have put in an executive vice president for Human Resources, and that was done last week. We will be addressing those issues with her.

Mr. OWENS. Would you say that massive labor-management problems are still not a priority, have not been made a priority?

Ms. CORCORAN. They are a priority, by all means. In fact, we have devoted a substantial amount of our resources to looking at these issues.

Mr. OWENS. On another subject, last year Representative Fattah contacted your office and requested an investigation of Postal Serv-

ice minority procurement opportunities. Your report revealed that the Postal Service did not enforce its requirements that contractors submit subcontracting plans and encourage including minority subcontracts. It also showed that contracting officers use their discretion in deciding when to comply with requirement, and that minority contracts have declined annually since fiscal year 1994.

To your knowledge, has the Postal Service begun to reverse the decline of the minority contracting opportunities? Has the Postal Service adopted any of the recommendations contained in your report?

Ms. CORCORAN. Yes, they have. While we have not done a followup review as of yet, we have been keeping tabs on this, what the Postal Service has done in this area, while we've been doing other contracting areas. We will eventually be doing a followup audit, probably toward, spring of next year. We want to give Postal Service long enough to actually put processes in place.

Also, Congressman Davis, you had mentioned earlier today your concern about minority contracting for advertising. We are going to be doing a local advertising job this year. We will be looking at whether or not minorities are given the same opportunity to compete for advertising as well as other individuals.

Mr. OWENS. You'll be recommending those things, or there is already a commitment from the top that those things will be done?

Ms. CORCORAN. We will be looking to see whether or not Postal has an adequate program in place to assure that minorities are included in local advertising.

Mr. OWENS. The commitment has been made; they have said they would put an adequate program in place to correct this. That commitment has been made already.

Ms. CORCORAN. No, not to my knowledge.

Mr. OWENS. You're going to recommend it.

Ms. CORCORAN. Well, I cannot say what we will recommend until we've done the review. But we will look to see whether or not they have adequate controls in place. And if they don't, then we certainly will make recommendations to assure that minorities are adequately included within the contract's consideration.

Mr. OWENS. Thank you.

Mr. MCHUGH. The vice chairman of the subcommittee, the gentleman from South Carolina, Mr. Sanford.

Mr. SANFORD. Thank you, Mr. Chairman. I want to apologize. I may have to run in just a second.

I guess my question would be for you, Mr. Ungar, that if you look at this as a theoretical question, but H.R. 22, for instance, the whole debate about the bill has been tied to, you know, what do we do to prepare the Post Office for what's coming its way; and I think that John created the perfect bill given the political confines he had to deal with.

In other words, I don't think you could have crafted a finer bill, given the political reality that exists on the Hill and with the different constituents tied to Postal. My question would be, assume you're just a raging idealogue, which is where I would be, not tied to the political reality that John has to deal with on a daily basis, if you were to look at it from that perspective and you look at the problems confronting the Post Office, would your goal be, in this

perfect world, to deal more with the cost side or on the revenue side, increasing revenue as a way of fixing the problem or decreasing cost?

Mr. UNGAR. That's a tough question. I think I would focus first on cost, but let me ask Ms. Anderson to address that more fully.

Ms. ANDERSON. I would think that the Postal Service would really need to focus on both. And you'll find that they have goals and they have strategies in their performance plans that I think really go to trying to achieving gains in both areas. And obviously the more successful they are in reducing their costs, that would put less pressure on the need to find additional revenues. But I think the efforts really have to go toward both sides.

Mr. SANFORD. One of my struggles has been, if you look at the cost part of the equation and you look at labor costs as measured against other private sector competitors—and again it's not a perfect match-up, given universal service and other constraints that the Postal Service has—would you really focus in on the labor portion of the cost segment?

Would that be a big star as you look at cost structure, Mr. Ungar?

Mr. UNGAR. Well, it has to be looked at, sir, because obviously there are different percentages, but it's roughly in the 80 percent area, plus or minus, that constitutes a cost. So I don't know how the Postal Service would be able to make any substantial progress without somehow addressing that.

Now, exactly how it's going to do that is a real challenge. As we indicated, productivity over the last many years hasn't significantly improved despite, you know, the amount of money that's gone into automation and capital improvement. Maybe that will change somewhat in the future as more progress is made. But I don't know how it's going to make substantial progress without looking somehow at the labor portion of that.

Mr. SANFORD. What would be benchmarks that you would see in the private sector in terms of productivity gains with private sector competitors in mail-related businesses?

Mr. UNGAR. I would presume you would have to look at organizations like Federal Express. If you are talking about individual companies, I would presume it would be those organizations that are involved in the same type of activity. Now, maybe foreign counterparts might be another.

Mr. SANFORD. Do you have any of those? Would you have any feel for what kind of productivity gains they've been looking at?

Mr. UNGAR. We have not addressed that, sir.

Ms. ANDERSON. We haven't looked at the private sector.

Mr. UNGAR. We haven't looked at that aspect of foreign postal organizations and what kind of data they have.

Mr. SANFORD. I thank the chairman.

Mr. MCHUGH. I thank the gentleman.

Mr. Ungar, as I said in my earlier comments, many of us expected this type of challenge that you generally outline in your report. But most of us thought it was some time away; we thought the wolf was out in the woods. I think you're showing us that if the wolf isn't at the door, he may in fact be coming up to the front steps.

I want to probe what you said a little bit earlier, because it may be worse than that. If I heard you correctly, you talked about the Postal Service's financial plan for next year, 2000, their projection of $100 million net revenue. I believe I heard you say that the factors on which that $100 million is predicated are, shall we say, optimistic, a 1 percent reduction in work hours, which goes against everything that we see in the workplace structure, in the numbers of stops, numbers of employees; 3.1 percent productivity increase, as opposed to an entire 9 percent increase since 1972, or 25 years.

So I believe what you're suggesting in your very judicious way is that $100 million based on $62 billion of revenue—I wish I had a $100 million in my back pocket. But if your entire budget is $62 billion, $100 million is not an enormous amount of money, so that's pretty optimistic.

Is that what I heard you say?

Mr. UNGAR. In our conservative way, I think so, yes. Although, again, predicting the future is awfully difficult, as you know. That's why we label this as a challenge and a fairly formidable challenge, because the forces seem to be going in the opposite direction.

Now, maybe there will again be some very big payoff that we're not seeing in some of the automation and capital improvements. But it would certainly seem to take—I hate to use the word "miracle," but it would certainly take some significant event or series of events that would appear to enable the Service to achieve its goal. Again, it certainly may do that, but it looks like a fairly significant challenge for all the reasons that we both cited.

Mr. MCHUGH. I understand that. I have been in government for nearly 30 years now and I know what it is to make 5-year budget projections and look 6 years back and laugh like crazy, no doubt about it, but we have to make certain assumptions.

But the point that I think needs to be kept in mind here is that a lot of good folks are here this morning because of, in large measure, what your analysis found. And I think they're here because they wanted to try to better understand how it is that now, within a timeframe as short as 3 years, we could have a problem facing the Postal Service that could total $17 billion, nearly 30 percent of its total operating revenues.

What I'm suggesting is, if you just forget about the 3 years from now when that $17 billion is driven largely by the challenge from electronic commerce and electronic communication, you've actually got a Postal Service that could be in big, big trouble starting as early as next year. I think in terms of what this subcommittee has been trying to do for the past 5 years, and, as the vice chairman said, as we've tried to react to the practical and the political realities of passing a bill in this town, 3 years, 2003 is just around the corner. Next year, for all intents and purposes, is here today.

So I think the message for this morning has to be, we don't have a lot of time anymore. The Congress has to be a part of this. We owe it to the Postal Service, but more importantly, we owe it to the American people.

The Postal Service itself has problems that it needs to meet head on. As Ms. Anderson said, there are certain cost constraints and cost problems that they can and should meet internally. But this is going to take some serious resolve by this Congress and by the

Postal stakeholders, a lot of whom are in this room today and a lot of whom I don't think truly believe the urgency of the problem. But I hope they're beginning to reassess this morning.

So, with that, we do have the Postmaster General. We've taken up almost 2 hours of your time, and I deeply appreciate your being here.

Ms. Corcoran, particularly, I've got a whole lot of questions I want to ask you. But with both of your indulgence, we'll submit those for the record.

[The information referred to follows:]

KARLA W. CORCORAN
INSPECTOR GENERAL

February 3, 2000

The Honorable John M. McHugh
Chairman, Subcommittee on the Postal Service
Committee on Government Reform
House of Representatives
Washington, DC 20515-6143

Dear Chairman McHugh:

Attached is our response to followup questions from my oversight testimony before the Subcommittee on October 21, 1999. We appreciate the opportunity to address your inquiries and provide you with this additional information.

If you have any questions regarding our response, or need further assistance, please contact our Director of Congressional and Public Relations, Ms. Laura Whitaker, at (703) 248-2347, or me at (703) 248-2300.

Sincerely,

Karla W. Corcoran

Karla W. Corcoran

Attachment

1735 N LYNN ST
ARLINGTON VA 22209-2020
(703) 248-2300
FAX: (703) 248-2291

Office of Inspector General, United States Postal Service Responses to Questions Submitted by the House Subcommittee on the Postal Service Following up on the October 21, 1999, Oversight Hearing

Major Challenges

Question 1

The Office of the Inspector General (OIG) has been in operation since January 6, 1997. Since that time the OIG has staffed up and developed an infrastructure and budget. The OIG appears to have established a strong presence and has made significant findings and recommendations in support of Congress, the Board of Governors, management and the employees of the Postal Service. The Inspector General's statement provides clear evidence that the OIG has made remarkable progress and particularly within the last six months when the OIG issued over 50 reports with monetary benefits of over $1.1 billion. It is clear that Congress's establishment of a truly independent Postal Service Inspector General has resulted in greater economy, efficiency and integrity. The Subcommittee would like to know how the OIG plans to build on its success.

(a) What are the major challenges that you face in meeting your responsibilities in the coming year?

Response

The OIG's biggest challenge is educating Postal Service management on the independence of the OIG. The OIG also needs to continue educating Postal management on the OIG's authorities, roles, and responsibilities; and its duty to report any significant issues to the Postal Service Governors and to Congress. In addition, the OIG must continue to gain expertise on Postal Service programs in order to add value to the Postal Service by providing meaningful results on a timely basis. Further, the OIG needs to finalize a process for resolving issues about which the OIG and Postal management disagree. The OIG is also sensitive to the need to make the results of its work publicly available without affecting the Postal Service's competitive position.

Internally, the key challenges facing the OIG include continuing to build an infrastructure by hiring additional talented and diverse staff, develop OIG processes, policies, and procedures, and promote the OIG's values and culture. At the same time, the OIG must continue to forge ahead with its mission while being sensitive to myriad demands being placed on its employees in an evolving environment.

(b) What areas of postal operations do you believe are high-risk and warrant close monitoring? What are your upcoming plans for reviewing these areas? What areas do you see where improvements have been made?

Response

The mission of the Postal Service is to provide prompt, reliable, and efficient universal mail service at reasonable rates. To fulfill this mission, the Postal Service's goals are to satisfy its customers, improve employee and organizational effectiveness, and strengthen financial performance. To achieve these goals, the OIG believes the Postal Service must address six significant areas:

- remaining competitive in a dynamic environment;
- leveraging technology;
- ensuring data reliability;
- enhancing financial and operational performance;
- increasing customer service and satisfaction; and
- improving the work climate and labor relations.

In its FY 2000 Annual Performance Plan, the OIG planned assignments to address each of these areas. For example:

- In the area of competition in the marketplace, the OIG plans to assess the use of the "Electronic Postmark" in establishing a Postal Service role in internet commerce, evaluating strategic and operational planning for electronic commerce, and reviewing the status of *PC Postage* and its potential for revenue generation.
- In the area of leveraging technology, the OIG plans to assess efforts to establish a Postal-wide computer security program and other critical infrastructure initiatives and to examine specific aspects of internet security.
- In the area of data reliability, the OIG plans to evaluate the accuracy and reliability of the External First Class Measurement System, examine the integrity and reliability of data used to compute Total Factor Productivity, and monitor implementation of the Government Performance and Results Act.
- In the area of financial and operational performance, the OIG plans to determine the effectiveness of the process for making major investment decisions within the Postal Service Decision Analysis Reports, determine whether the Mail Transportation Equipment Service Centers are achieving stated performance and financial goals, and ascertain if the Postal Service is adequately identifying and appropriately handling hazardous material shipments.
- In the area of customer service and satisfaction, the OIG plans to examine the sufficiency and appropriateness of the Priority End-to-End Measurement System, and evaluate delivery confirmation to assess whether packages are being scanned properly.
- Finally, in the area of work climate and labor relations, the OIG plans to review Postal Service initiatives to improve the organizational climate, assess implementation of the Postal Employees Safety Enhancement Act and its impact on

the organizational climate and operations, and evaluate the criteria supporting violence-prevention strategies.

The OIG has observed the following improvements made by the Postal Service:

- In the OIG's last Semiannual Report to Congress, the OIG identified the Year 2000 (Y2K) as the most urgent and critical technology issue facing the Postal Service. As a result of continuous oversight by the Postal Board of Governors, the Postal Service is to be commended for successfully meeting the Y2K challenge. With only minor exceptions, Postal Service critical systems were fully Y2K compliant, and no disruption to service occurred. The OIG is encouraged that the Postal Service's business continuity plans have been strengthened, which should facilitate recovery in the event of any future computer intrusions or security failures. The Postmaster General recently commended the OIG for its role in assisting the Postal Service in meeting this critical challenge.
- The OIG noted that the Postal Service preserved its financial goals for FY 1999 and exceeded its "Management Challenge" initiatives through extensive budget reductions in Headquarters and field programs. However, the OIG identified opportunities for improvement in the budget reduction process.
- As a result of the Postal Board of Governors' concern and an OIG audit of the Corporate Call Management Program, Postal management slowed the program's implementation process and recognized a potential cost avoidance of $962 million through FY 2007. Management agreed to notify the Board of Governors of the cost reduction and of future cost reductions as they are realized.
- Based on a number of reviews the OIG has completed in the transportation area, Postal management has taken steps to:

  - improve the reliability of the Rail Management Information System;
  - recover costs incurred because of customer delays in returning rail trailers; and
  - reduce costs by converting emergency contracts for highway routes to regular routes.

Managing Requests

Question 2

Last year you reported that you were particularly concerned for managing, evaluating, and responding to requests. At that time you indicated that more than 2,000 requests had been received by your office for further analysis and potential action.

(a) What is the current backlog of requests and how are you managing the workload?

Response

Since reporting to you in September 1998, the OIG has made substantial progress in dealing with the high volume of Congressional and public (Hotline) requests for audits, investigations, and other relief and information. As the OIG continues to add staff and

gain experience, it will assess future improvements in processing these requests in a timely manner.

Currently, the OIG has reviewed, screened, or determined what actions are needed to respond to all requests received. There are approximately 600 open requests that are currently being addressed: 100 from members of Congress and the Postal Service Governors and 500 from the OIG Hotline. As a result of the Postal Service Governors' approval of the OIG hiring plan, new auditors, evaluators, and investigators have been hired to help the OIG evaluate and perform this work. In addition to hiring more Hotline analysts, the OIG now has a full-time Director of Congressional and Public Relations.

As the OIG indicated last year, large numbers of its requests involve individual complaints that can be resolved through contractual grievance-arbitration procedures and the Equal Employment Opportunity process. The OIG screens these individual cases but generally does not review the circumstances of the request. Instead, the OIG categorizes the individual cases to identify systemic issues. Once a trend has been identified, the OIG focuses on performing Postal-wide reviews. The OIG believes that by performing systemic reviews rather than individual case reviews, its work will affect a larger number of people and have a wider-ranging, more beneficial impact on Postal Service operations.

Meeting Increased Staffing Goals

Question 3

For FY 1999 the OIG requested and was granted approval for a staffing level of 480 but you indicate that you currently have a staff of a little over 400. In your statement you report that the Governors have approved a hiring level of 648 for FY 2000 and, as a result, you will have to hire another 245 individuals. This is a significant increase, but as predicted in your testimony last year, your staffing needs would change as your knowledge of the Postal Service grows. It is clear from your statement today that in fact, you have increased the scope and depth of your work over the last year. An increase in your staff appears justified and the Governors should be applauded for their support. Nonetheless, you fell short of your FY1999 goal to staff up to 480.

(a) How do you intend to improve your recruiting efforts in order to meet your staffing target for FY 00?

Response

Hiring qualified, skilled employees who share the OIG values and fit the OIG culture is one of the top priorities of the OIG. As of January 17, 2000, the OIG had 424 employees with 70 candidates currently in the background investigation phase of the hiring process. To reach the OIG FY 2000 approved staffing level of 648, the OIG needs to hire an additional 154 individuals before June 30, 2000. Because of the current competitive job market, the OIG recently appointed a "hiring czar" to focus and

consolidate all recruiting efforts. Of the 154 open positions approximately one-third are located in major cities where the OIG believes it can quickly identify qualified, skilled employees. The remaining 104 positions are in Arlington, Virginia, and Dallas, Texas, with over half of these positions targeting recent college graduates.

The OIG has refined its recruitment strategy to better align the organization with sources that best meet its needs, including colleges and universities with strong curricula in analytical and writing skills and technology-related fields. The OIG plans to increase its participation at professional career fairs and will continue to participate and staff booths at professional conferences relating directly to law enforcement or evaluator/auditor professions. In addition, the OIG is working on an expedited process to hire these individuals.

The OIG will focus its advertising in professional journals and periodicals. The OIG also continues to advertise its vacancies in local newspapers and on the websites of the Office of Personnel Management and on the IGNet, which advertises for all federal Inspectors General offices.

The OIG is confident that by implementing these strategies it will improve recruiting efforts, reduce hiring time significantly, and meet its FY 2000 hiring goals.

(b) How is your staff divided among the OIG's six major organizational units?

Response

The following table shows the breakdown of staff among OIG's seven major organizational units as of January 17, 2000, and at the end of FY 2000.

Organizational Unit	As of 1/17/00	Budgeted for FY 2000
Inspector General & Counsel Staff	24	33
Strategic Planning & Quality Mgmt	41	64
Performance	109	175
Revenue & Cost Containment	118	181
Employee	84	137
Customer	48	58
Total	**424**	**648**

(c) Please indicate what your staffing level is at each of your field offices including the anticipated staffing level at each of the five new offices to be established in FY 2000.

Response

The following table shows OIG's current staff, by office, as of January 17, 2000, and at the end of FY 2000.

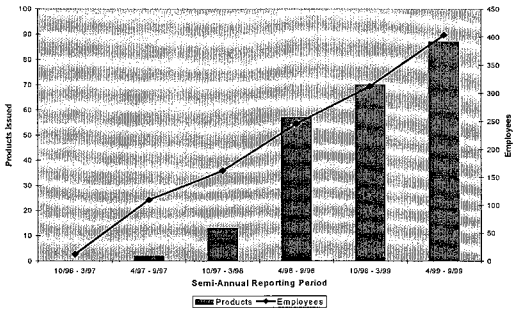
Office	As of 1/17/00	Budgeted for FY 2000
Headquarters (Arlington, Virginia)	332	462
Atlanta	10	17
Dallas	44	79
San Mateo	13	21
St. Louis	14	18
Minneapolis	8	20
Chicago		9
Denver	1	6
Los Angeles	1	11
New York		2
Raleigh	1	3
Total	**424**	**648**

(d) *To what extent have increases in your staff allowed you to take over work formerly done through audit and audit-related contracts? As a result, has the Postal Service reduced its expenditures accordingly on outside auditors?*

Response

As the OIG has increased its staff, the number of reviews completed has increased. The following chart illustrates the extent to which increased staffing has enabled the OIG to perform more reviews and issue more reports:

Staffing and Reporting Trends



The designation of functions between the OIG and the Postal Inspection Service approved by the Governors in March 1997 provided that all audit functions assumed from the Postal Inspection Service by the OIG would be transitioned to the OIG by FY 2001. Because of the increase in staff, the OIG was able to assume all the agreed upon functions by June 1999.

The OIG is currently discussing with the Postal Inspection Service assuming additional audit functions as a result of the Inspection Service's decision to discontinue performing audits based on the OIG audit entitled, "Classification of Inspection Service Personnel Performing Audits." The OIG anticipates the need for an increase in staff and funding to assume these additional audits.

The primary audit contract for the Postal Service continues to be the Financial Statement Audit, which is contracted to an independent external public accounting firm by the Governors. Title 39 gives the Governors the responsibility for contracting this service with an independent public accounting firm. The Governors view this as one of their primary responsibilities, and have elected to retain this responsibility. Therefore, the expenditures for outside audit and audit-related services, to the OIG's knowledge, have not changed.

Audits and Audit-Related Services

Question 4

Last year you also expressed particular concern for controlling postal management contracts for audits and audit related services. You also reported that you were working with senior management to more fully define what constitutes audit and audit related services within the Postal Service.

(a) What has been done to control audit and audit-related service contracts? Have you and senior management been able to more fully define what constitutes audit and audit related services? Has the IG taken over primary responsibility for audits?

Response

The OIG assumed primary responsibility for all audits following its establishment. To reaffirm this responsibility, in January 1999 the Postmaster General issued a memorandum to officers of the Postal Service which (1) notified the officers that the OIG is responsible for all Postal Service audits, and (2) established procedures for management request audits. Further, in July 1999, the Postal Service Administrative Support Manual identified the OIG as an independent entity and described its authority and responsibility to conduct audits. Although the OIG originally delegated specific audit responsibilities to the Inspection Service, the Inspection Service decided in September 1999 to no longer perform "Yellow Book" audits. The OIG is currently reviewing the impact of this decision to determine what additional audit coverage will be provided by the OIG.

The OIG has expressed concern about the Postal Service's reliance on contracts for audit and audit-related services. However, the January 1999 memorandum from the Postmaster General to officers of the Postal Service was a significant step in highlighting the OIG's responsibility for these engagements. The situation was further remedied by the March 1999 letter from the Postmaster General expressing concern about the Postal Service's growing reliance on consulting services and other contracting methods used to supplement the administrative workforce. While the OIG has not recently performed a detailed review to evaluate whether management is continuing to rely extensively on audit and audit-related contractors, it believes the practice has diminished. The OIG will continue to monitor the reliance on such contracts and remind management of its responsibility for audits within the Postal Service whenever warranted. It will also assist management in more fully defining audit and audit-related services.

Contracting Officer's Representatives

Question 5

You reported that the OIG became Co-Contracting Officer's Representative for the financial statements. Last year you reported that the Governors were considering your request to be designated as the sole contracting officer's representative for the financial statement certification contract in FY 1999.

(a) *Is your request pending before the Governors for FY 2000? If the Governors have determined that the OIG should not be the sole COR, how do you believe this will impact your ability to meet your audit responsibilities under the Inspector General Act?*

Response

In March 1999, the Governors approved the Audit Committee's recommendation to have the OIG serve jointly with Corporate Finance as the Contracting Officer's Representative for the annual financial statement audits. Under Title 39, the Board of Governors has sole authority to hire and retain the external auditors responsible for certification of the financial statements. In our new capacity as Co-Contracting Officer's Representative, the Governors recently sought and received the OIG's advice on the terms for extending the independent public accountants' contract. We will continue to evaluate the effectiveness of this joint arrangement.

Designation of Functions

Question 6

One of your major challenges has been to determine the designation of functions between OIG and Postal Inspection Service.

(a) Do you believe this issue has been resolved or are there some issue areas that are still in dispute or uncertain as to whether your office or the Inspector General ***[Postal Inspection Service]*** *has responsibility?*

Response

In March 1997, the Governors approved the original designation of functions between the Postal Inspection Service and the OIG. The designation of functions delegated many OIG responsibilities to the Inspection Service, allowing audits and investigations relating to fraud, waste, abuse, and mismanagement to continue without interruption. In 1999, the Chief Postal Inspector and the Inspector General agreed to reconsider the original designation of functions. By this time, the OIG had gained knowledge of Postal operations and believed that some core OIG responsibilities previously delegated to the Inspection Service should be revisited.

During the summer of 1999, discussions that focused primarily on investigations were held between the OIG and the Inspection Service. Generally, the OIG and Inspection Service representatives agreed on the areas of responsibilities. These discussions were never finalized because the OIG was conducting an audit of "Classification of Inspection Service Personnel Performing Audits," which was finalized in the fall of 1999 and resulted in the Inspection Service decision to divest itself of "Yellow Book" audits. As a result of this decision, the OIG is reevaluating all functions delegated to the Inspection Service. The OIG plans to discuss its evaluation with the Inspection Service, Postal management, and the Governors in the near future with an anticipated result of a revised designation of functions by summer. The OIG will keep Congress informed as to the progress of these discussions.

Since the original designation of functions, one major point of disagreement between the Inspection Service and the OIG has been whether Grade 15 Postal Inspectors are subject to OIG executive investigations. At the time of the original designation of functions, it was agreed that the OIG would investigate all Postal Career Executive Service (PCES) Inspection Service employees, including those paid at the Grade 15 level. After the designation, the Inspection Service changed its pay banding, which resulted in some PCES employees becoming Senior Executive Service; others became Grade 15. The Inspection Service has opposed the OIG investigating former PCES employees who are now Grade 15. Recently, the Inspector General spoke to the new Chief Postal Inspector about this concern but the issue has not yet been resolved.

(b) Have you met with the newly appointed Chief Postal Inspector to address pending issues regarding designation of functions?

Response

The Inspector General has met with the new Chief Postal Inspector and briefly discussed pending issues regarding designation of functions. In the course of these discussions, they agreed to resume the teambuilding meetings begun last year with the

former Chief Postal Inspector. At these meetings, the OIG and the Inspection Service will address important issues that directly affect the daily operation of both offices, such as the designation of functions.

Priority Mail Processing Center Network

Question 7

You established that processing mail through the contractor-operated Priority Mail Processing Center Network did not significantly improve on-time performance but did cost the Postal Service $101 million (or 23 percent) more, than to process it in-house. I find this to be a very important finding and may call into question whether this and other contracting out initiatives by the Postal Service makes sense.

(a) Please elaborate on your findings and recommendations. What caused these higher costs? Has management accepted your findings and have they agreed to your recommendations?

Response

As reported in the audit and subsequent testimony, the Postal Service spent more to process Priority Mail through the Priority Mail Processing Center Network than it would have spent to process the same volume in-house. This occurred primarily because the Postal Service still bears the costs for accepting and delivering Priority Mail processed through the Network. In addition, the contractor was paying a higher rate to ship priority mail on commercial airlines than the Postal Service's air system contract rate. Postal Service officials have indicated they anticipated that a dedicated Network would be more expensive than the conventional approach. However, from a cost-benefit standpoint, they believed improved service would justify increased costs.

During the audit, the OIG also evaluated the performance of the contracted Network. The OIG discovered that the Network was not meeting the overall delivery rate goals referenced in the contract. In fact, the audit revealed that the "within two-day" delivery rate for Priority Mail processed through the Network exceeded the rates for similar non-contracted operations within the Postal Service by a range of only about 2 to 4 percent. The OIG was unable to make a direct comparison of delivery rates within the Network area before and after the contract because Postal Service officials did not document a pre-contract performance baseline for the region. Instead, the OIG asked officials in the Postal Service Consumer Affairs Office to determine service scores for ZIP Code clusters similar to those in the region covered by the Network. Officials identified seven ZIP Code clusters in the mid-west and six ZIP Code clusters on the West Coast similar to the Priority Mail Processing Center Network ZIP Code clusters. The OIG compared the service scores for Priority Mail processed entirely by the Postal Service in these clusters with the service scores for Priority Mail processed through the Network in deriving the 2 to 4 percent differential.

Postal management generally agreed with the OIG recommendations. However, they disagreed with some of the findings and took exception to the methodology the OIG used to derive service score differentials. Management also expressed their concern that the audit was conducted during the pilot phase of the program and viewed many of the findings and recommendations as premature. The OIG plans a followup review of the Priority Mail Processing Center Network during the coming year.

Point of Service ONE and Tray Management Systems

Question 8

You looked at the Point of Service (POS) ONE System which is to replace outdated, integrated retail terminals at post offices nationwide as well as the Tray Management System (TMS) which automates the moving and staging of mail between sorting operations. You found that both systems had faulty system development practices and premature deployment. You found that this resulted in additional costs to the Postal Service and that POS ONE did not fully meet desired results and benefits. You indicated that your review of the TMS is yielding similar results. Both of these technologies alone are projected to cost the Postal Service over $1 billion combined. As the Postal Service is depending on these systems to improve operations and generate key information, failure to effectively deploy these systems will have a serious impact on the vision of a Postal Service information platform.

(a) *Please elaborate on your findings and whether management is taking corrective action to avoid major problems in the future.*

Response

POS ONE

The OIG audit of POS ONE disclosed that the system was not fully achieving the desired results and benefits outlined in the Decision Analysis Report approved by the Postal Service Board of Governors. In addition, Postal officials reduced the number of days allocated for testing the POS ONE software.

Some of the more significant problems the OIG observed relating to POS ONE included:

- the persistence of software and hardware problems despite several updated software releases designed to correct them;
- vendors modifying accountability and retail transaction data to correct accounting errors at POS ONE sites without obtaining prior approval by the appropriate Postal Service personnel;
- an increase in the number of accounting adjustments by 83 percent and dollar value of accounting adjustments by 500 percent in the three accounting periods after implementation as compared to FY 1998;

- a 2 percent increase in the work hours of window clerks and a 3.8 percent increase in the work hours of accounting staff at POS ONE sites in the three accounting periods after implementation as compared to FY 1998; and
- new business processes not being sufficiently mature to fully provide customer satisfaction and support retail operations.

Management agreed with the OIG recommendations and has initiated or completed actions that should correct the identified problems. They have revised their testing and certification process based on the evaluation of an independent contractor, improved and implemented controls over and monitoring of accountability changes, and continued to work with the vendors to improve the hardware and software deployment process. These actions should reduce the chance of major problems occurring in the future. However, POS ONE is continuously undergoing modification, and there is no assurance that additional problems will be avoided.

Tray Management System

The Tray Management System was designed to automate movement and staging of mail in Postal Service processing and distribution centers. In December 1998, the Postal Service Board of Governors approved the Tray Management System Phase III Decision Analysis Report Modification Request for $497 million to install the system at 23 sites.

The Tray Management System has proven to be a significant and challenging automation initiative for the Postal Service. This program has the potential to assist the Postal Service in becoming a leader in implementing and integrating mail-processing technology in the next century. Despite the progress made to date in designing and deploying the Tray Management System, the OIG audit identified several issues that warrant management's attention. Management is currently reviewing the OIG draft report. When the report is finalized, a copy will be provided to the Subcommittee.

USPS Quality Control

Question 9

Last year the Postal Service reported that to ensure quality in the external mail measurement studies it has built-in checks within each process, and quality verification checks conducted by a Quality Control team. In addition, following attempts by employees to undermine the integrity of the system the Postal Service has increased the number of postage meters and changed the test mail pieces to help prevent manipulation of the data.

(a) Has the OIG studied how well these checks and new mail induction procedures have enhanced the integrity of EXFC?

Response

While the OIG has not studied how well these checks and new mail induction procedures have enhanced the integrity of EXFC, the OIG visited the contractor's facilities where the test mail is processed. The OIG verified that the contractor:

- increased the number of postage meters, which ensured that each test location represented a postage meter with the local ZIP Code;
- redesigned test mail to include window, various sized, hand-addressed, and typewritten envelopes; and
- established a Quality Assurance Team to conduct, manage, and maintain EXFC Measurement System independence.

Recently, the OIG conducted an audit to determine if the EXFC model was designed to be a true representation of First-Class Mail delivery performance. The results of this audit are under discussion with Postal management and will be provided to the Subcommittee once the report is finalized. The OIG will continue to monitor EXFC and conduct appropriate reviews to evaluate the integrity of EXFC.

External First Class Mail

Question 10

The Office of the Inspector General issued two reports on EXFC in the first half of FY99: Survey of the Results of the South Florida District: EXFC Test Mail (DS-LA-99-001) and Survey Results of the Atlanta District: EXFC Test Mail (DS-LA-99-002). These reports confirmed in both cases that potential EXFC test mail had been handled separately. I understand you are conducting an audit of the PricewaterhouseCoopers external first-class test mail program methodology. I look forward to that report but in the meantime let me ask you some questions.

(a) What actions have you taken to determine whether such problems reflect, in any way, system-wide problems with EXFC service measurement?

Response

The objectives of the system-wide audit, currently in draft and under discussion with Postal management, are to:

- evaluate controls established by the contractor for detecting and preventing compromise of the EXFC Measurement System, and
- assess system capabilities to measure First-Class Mail service.

The OIG found that the contractor has adequate controls in place to execute the EXFC system. The audit also disclosed that the EXFC system satisfies several Postal Service business objectives and is a useful mechanism for improving First-Class service

performance. However, the audit identified several adjustments and improvements that could be made in the system to enhance its usefulness and to ensure its results are not misleading.

(b) *Has the Postal Service issued any directives to field managers and employees to assure that external measurement systems are not corrupted and mail service does not suffer from diverting resources to give special treatment to potential test mail? Please discuss their actions.*

The Postal Service Consumer Affairs Annual Report stresses the importance that all Postal employees contact that office to report any irregularities in EXFC test mail. The OIG queried the Postal Service as to what measures they had taken to prevent future occurrences of special treatment of EXFC mail. The vice president, Operations Planning, responded that the Chief Operating Officer had issued two memorandums since May 1996 to the area vice presidents stressing:

- the importance of integrity;
- the need to guard against subverting the measuring systems; and
- the need to share these messages with performance clusters and staff.

No further directives have been issued since February 1998.

(c) How, if at all, have managers who facilitated or in any way encouraged such practices been disciplined?

Response

The OIG contacted the Postal Inspection Service, which provided the following information:

Thirteen managers have been disciplined as follows:

- 4 were reduced in grade and reassigned
- 4 were suspended
  - 3 for 30 days
  - 1 for 14 days
- 4 received letters of warning
- 1 received counseling

The vice president, Operations Planning, substantiated this information and added that all employees involved forfeited their EVA bonus payments and did not receive a merit increase.

Postal Service Response to OIG Recommendations

Question 11

The Subcommittee is interested in knowing how Postal Service management is treating your recommendations.

(a) In general, what action has the Postal Service taken in response to the recommendations in your reports to date? Are you satisfied with its responses? If not, what should the Postal Service do to be more responsive?

Response

With some exceptions, the Postal Service has been responsive to the OIG audit recommendations and advisory suggestions. Management has agreed with a majority of our reviews; however, in several instances, management has offered alternative solutions to OIG recommendations. In these instances, the OIG and management have engaged in dialogue that generally has resulted in alternative solutions agreeable to both parties. In a few cases, management and the OIG have not agreed. In these cases, the unresolved recommendations remain open. The OIG believes two things will improve management's responsiveness in the future:

- an audit resolution process (discussed more fully in question 12) will ensure that disagreements are resolved – if not by Postal Service management, then by the Governors; and
- as Postal Service officials gain a better understanding of OIG's roles, responsibilities, and the audit process, they will work to resolve disagreements at the earliest possible stage.

Formal Audit Resolution Process

Question 12

Last year you discussed the need to establish a formal audit resolution process. I feel strongly about this issue. Without such a process many of the important and often controversial recommendations made by your office will be left unaddressed, undermining the potential value of your office to the Postal Service.

(a) Has any progress been made to in this area? What, if any, issues need to be resolved in order to establish this important process?

Response

The OIG has been working with Postal management to formulate a framework for an audit resolution process and has reached general agreement about the importance of this process and its basic elements. Questions that need to be addressed before

resolving this issue are identifying the final resolution officials and defining the role of the Governors in the process. The OIG anticipates that the proposed process will be submitted to the Governors for approval in the near future. Until a process is adopted, OIG considers all disagreements with management as "unresolved" and they remain "open" in our records and reported as such in the OIG Semiannual Report to Congress.

Setting Spending Limits on Postmaster Installations

Question 13

Last year you recommended that the Postal Service establish a policy setting spending limits for events similar to the event to celebrate the installation of the Atlanta Postmaster. The Postal Service agreed to develop parameters as to what defined "reasonable expense".

(a) Were these parameters ever developed? Please summarize them?

Response

Yes, the Postal Service did develop parameters. Initially, the Postal Service revised its Administrative Support Manual to address the types of expenditures for the postmaster installation ceremony, but the Manual did not define what constitutes a reasonable amount and did not establish monetary thresholds. The OIG did not view the revisions to the Manual as addressing the issue completely because the Postal Service did not specify acceptable dollar ranges for installation ceremonies. On October 1, 1998, the Postmaster General issued a policy memorandum to Postal Service officers stating postmaster installations and retirements are capped at $500 unless an exception is given by the Chief Financial Officer. This latest policy has not been incorporated into the Administrative Support Manual (updated through October 7, 1999). The OIG is following up on this issue.

(b) Did the OIG deem these parameters are appropriate?

Response

The OIG did not evaluate the appropriateness of the dollar amount, but was satisfied that management's action was responsive.

(c) Were all headquarters and field units advised of the new guidelines?

Response

On October 1, 1998, the Postmaster General issued a policy memorandum to Postal Service officers regarding the spending limits. The memorandum also states that the Chief Financial Officer is the only person with the authority to authorize an exception to this policy.

Corporate Call Management Program

Question 14

In a recent review of the Corporate Call Management program you advised management to recalculate operating costs because of improvements in technology and changes in call mix. As a result, management subsequently calculated a potential cost avoidance of nearly $1 billion through FY 2007. In a subsequent report you intend to determine whether the program objectives are being achieved.

(a) Was the reduced cost truly the result of improvements in technology and changes in call mix?

Response

Interactive voice response technology allows a caller to access information without the intervention of a call agent. As a result of this new technology, officials now project that the number of calls satisfied in this manner would increase from 10 million in FY 1999 to 78 million in FY 2004. The marginal costs for interactive voice calls is $.10 versus $.93 for agent-handled calls. Therefore, costs were reduced because of improvements in technology and changes in the call mix between agent-handled calls and interactive voice calls.

(b) To what extent did the Postal Service simply overestimate the cost of this new program?

Response

The overestimation of costs by the Postal Service resulted from an assumption that the call volume from one locality could be projected to the national population. The program office projected call volume of about 200 million agent-handled calls per year in May 1998. The program office now estimates the total call volume will exceed the original estimate by about 10 million calls, however 37 percent of these calls will be satisfied through automation.

Postal Service Cost Savings

Question 15

You recently reported on opportunities for savings in rail detention cost (the cost to the Postal Service for using rail trailers). In that report you noted the lack of reliable data to control cost and that the Service was inconsistent in seeking reimbursement from detention caused by mailers. In another recent report you found that the Postal Service officials did not limit use of emergency highway transportation routes to valid emergencies and did not negotiate special reduced rates or monitor excessive expenditures. In order for Postal Service managers and staff in the field to be aware

and sensitive to cost control they need to know the cost implications of their actions. In addition, it may be beneficial to have costly decision in some way hit their own bottom line.

(a) *Do you believe that Postal Service managers and staff are given adequate information with regard to the cost of their decisions? Are these problems indicative of a general lack of cost information at the field level -- information that would facilitate better cost control and accountability?*

Response

The OIG has not performed a Postal-wide review of cost or distribution data reliability. Problems with cost control are attributable to the lack of accessible cost information and the lack of financial accountability at the plant level. Mail operations personnel control transportation activities but do not have responsibility for managing the transportation budget. This is problematic, as the operational goals of mail processing plants take precedence over cost containment.

In the area of rail detention, Postal Service managers are given adequate information about the costs of their rail detention decisions. However, this information may not be provided to the plant personnel who make routing and dispatch decisions. In the area of highway transportation, managers are responsible for authorizing extra trips and have access to highway cost reports. However, the staff (headquarters and area transportation) managing the transportation budget do not have line authority over the mail operations staff, who are responsible for scheduling transportation.

(b) *What kinds of cost information do field managers and staff need in order to perform effective cost management at the area, district and local level?*

Response

First and foremost, field managers need timely and reliable information that is easily accessible. Past studies have indicated that data reliability is a real challenge for the Postal Service. The OIG evaluates data reliability during the course of its reviews. When appropriate, recommendations are offered to management to improve the reliability and distribution of data. Moreover, managers and staff need budgeted as well as actual costs.

(c) *Can you suggest any incentive systems to reward or penalize postal managers and staff for efficient or wasteful spending?*

The OIG has not performed a systemic review of this issue; therefore, it cannot propose a Postal-wide solution. However, the OIG is reviewing the Postal Service's Economic Value Added Program and will assess its value in terms of rewarding or penalizing postal managers and staff on the basis of performance. The OIG will provide a copy of the results of this review upon its completion.

Electronic Commerce

Question 16

Last year you indicated that you formed a specialized unit to evaluate the electronic commerce area. Apparently, as indicated in your statement, you are "up to task" as far as helping the Postal Service become successful in this most challenging undertaking. You indicate that you are aggressively addressing the electronic commerce issue. But unfortunately in the postal world (and the real world too) the past is often prologue.

(a) Has the OIG electronic commerce unit evaluated prior forays by the Postal Service into the electronic communications age such as ECOM and Electronic Commerce Services – a service that lost $20.3 million since inception according to the GAO?

Response

The OIG has not evaluated prior Postal Service initiatives into the electronic commerce area. However, the OIG has looked at recent initiatives such as POS ONE and Mailing On-Line, and currently is preparing to review the new PC Postage Program. The OIG electronic commerce team previously focused on the Y2K initiative, which was a time sensitive, high priority assignment. The team is now redirecting its efforts and is completing a global identification of prior initiatives, major systems, and emerging issues that warrant audit attention. Based on the level of risk identified, these systems will be considered for upcoming audit coverage.

(b) Has the OIG formed any views on the challenges facing the Postal Service in the area of electronic commerce and ways to avoid the difficulties encountered by the Postal Service in the past?

Response

The Postal Service faces many challenges in the area of electronic commerce. These challenges include:

- implementing a strategy for leveraging electronic commerce in executing its mission;
- developing and implementing electronic commerce systems;
- building the information technology infrastructure to support electronic commerce;
- ensuring the integrity and security of electronic systems and transactions;
- creating business partnerships and alliances; and
- ensuring privacy to customers and business partners.

The OIG, as it conducts work in this area, will attempt to identify ways to assist the Postal Service in avoiding the difficulties they have encountered in the past.

Management-Labor Relations

Question 17

One of the long-standing major challenges for the Postal Service is improving management-labor relations.

(a) Describe any studies that the Office of Inspector General (OIG) has completed related to postal labor-management relations for fiscal year 1999. What have been the overall results of those studies?

Response

In FY 1999, the OIG completed 30 reports and approximately 63 Congressional responses concerning labor-management issues, including the grievance and arbitration process, workplace environment, Equal Employment Opportunity (EEO), violence in the workplace, health care, and the Postal Employees Safety Enhancement Act. The OIG has identified the improvement of the labor management area as one of the major performance and management challenges that must be addressed if the Postal Service is to remain competitive in the 21st century. The OIG has found that working in this area is extremely difficult because of the vast workforce and decentralization of labor management. For example, policies and procedures are developed in Headquarters and their implementation is inconsistent from postal facility to district to area.

In addition, since inception the OIG has received over 2,500 individual labor management complaints. Because of the emotional involvement, potential financial impact, and the length of time to resolve these issues for the employee, it is important that the OIG's involvement in this area be meaningful and positive. Therefore, the approach the OIG has developed to deal with the sheer magnitude of complaints is to focus primarily on systemic issues and conduct Postal-wide reviews. These reviews are designed to identify and short circuit potential problems that can detract from a healthy and productive work environment. The following describes some of the OIG's efforts in the area of labor management.

In the area of grievance and arbitration, the OIG found that Postal management had not adequately resolved workplace disputes before they became formal grievances. The OIG also found that a comprehensive management information system to capture nationwide statistical case data had not been implemented. Further, the OIG noted that arbitration procedures were not administered as required by the national agreements.

In the area of workplace environment, the OIG found instances where Postal management did not investigate claims of sexual harassment and retaliated against an employee for participating in an OIG review. The OIG has received numerous complaints concerning unwarranted discipline, harassment and intimidation, and hostile

working environment. While the OIG has yet to perform systemic reviews of these issues, site specific OIG reviews have substantiated instances of these complaints.

In the area of EEO, the OIG has conducted one audit that revealed that pre-complaints and formal complaints were not processed by Postal management within the required time frames as established by law. These delays were attributed to insufficient staffing and high turnover in key positions.

In the area of workplace violence, the OIG found that Postal employees and managers have generally not been trained adequately in dealing with violence in the workplace. In addition, the OIG found that Postal management was not effectively implementing their violence prevention and response program. The Postal Service has developed violence prevention policies and procedures, which are outlined in the Threat Assessment Guide and the Crisis Management Plan. The OIG has initiated a broad review of the Postal Service's implementation of these policies and procedures, which is scheduled to be completed this year.

In the area of health care, the OIG reviewed a district process for submitting, controverting, and challenging injury claims. The results of this review have provided a basis for future health care assignments. Further, the OIG has initiated several audits to determine the impact of the Postal Employees Safety Enhancement Act.

The details of the completed reports are described in the last two OIG Semiannual Reports to Congress.

(b) To what extent have any of your recommendations or suggestions for improvement been addressed or implemented by postal management?

Response

The OIG has made 49 recommendations and suggestions to Postal management concerning labor management issues. Postal management has agreed to many of the individual recommendations in the labor management area. However, the OIG is concerned about:

- the tone of many of management's responses;
- the inconsistent responses among various levels of management over the same issues;
- the defensive posture the Postal Service takes in regard to the questionable actions of its managers;
- management not agreeing to take action on a number of recommendations /suggestions that could have major impact on labor management relations; and
- Postal management, generally, not taking corrective action against managers who do not follow policies and procedures.

At this time, no followup has been performed to verify improvements made by Postal management. However, the OIG believes that the Postal Service needs to apply the same standards of conduct to managers that they apply to craft employees. This includes ensuring that managers' personal behaviors comply with the Zero Tolerance Policy on violence in the workplace.

Equal Employment Opportunity

Question 18

Another important concern is whether the Postal Service is treating its employees and prospective employees in a non-discriminatory manner.

(a) What reviews has OIG completed that addressed diversity issues, including such matters as sexual harassment and EEO training, the EEO complaint process, and recruitment and hiring practices?

Response

The OIG Hotline and Congressional offices receive many individual complaints regarding workplace environment issues. These complaints include discrimination, recruiting and hiring processes, hostile work environment, and other similar issues. As a new agency, the OIG undertook individual reviews to develop a greater understanding of the Postal culture and to establish a working relationship with Postal management to ensure that employees' concerns are addressed. In FY 1999, a total of 42 audits and individual reviews were done in this area. In a majority of these reviews, the OIG made suggestions to Postal management on ways to improve the workplace environment.

In FY 1999, over 60 percent of the 478 individual complaints received by the OIG concerned workplace environment issues. Because of the magnitude of individual complaints received, the OIG refined its review process and, generally, no longer performs work on allegations involving individual employee issues that can be resolved through administrative procedures such as EEO. Instead, the information the OIG receives is used to determine systemic issues and areas for potential review. In this regard, the OIG has conducted six major reviews in four areas, EEO complaint processing, discriminating hiring practices, retaliation, and workplace climate. In FY 2000, the OIG plans reviews to evaluate the effectiveness of workplace climate assessments and the Postal Service's initiatives to improve the organizational climate. In addition, the OIG will be including recruitment as part of its continuing EEO work. The OIG will continue to monitor data collected from Hotline and Congressional correspondence to identify other areas for review.

(b) What have been the overall results of those reviews? To what extent have any of your recommendations or suggestions for improvement been addressed or implemented by postal management?

Response

The overall results of our reviews indicate that Postal management needs to improve its treatment of employees and the processes used to handle employee complaints. Management has agreed with many of the individual recommendations and suggestions that we made. However, we have not performed extensive followup to verify that improvements were made. If management has implemented the recommendations/ suggestions to which they agreed, the following actions have been taken:

- staffing adjusted when necessary to meet complaint volumes;
- technical support provided to improve complaint processing;
- controls improved over compliance with settlement agreements;
- workplace climate assessments performed;
- action plans to address workplace environment issues prepared and implemented;
- reiteration to management personnel that retaliation against employees is prohibited;
- managers reassigned where findings supported a conclusion of harassment; and
- supervisory and performance training provided when warranted.

The OIG is concerned about the Postal Service's defensive posture when our findings question the actions of its managers. Further, Postal Service's inaction on some of OIG recommendations may have a negative impact on efforts to improve strained labor-management relations.

In the Postal Service's FY 2000 Annual Performance Plan, it states that the OIG labor management reports are used by Postal management to aid and measure Postal success in meeting performance goals and improving their understanding of employee issues and concerns.

Postal Employees Safety Enhancement Act of 1998

Question 19

Under the Postal Employees Safety Enhancement Act of 1998, OSHA may now issue the Service citations and levy monetary penalties for noncompliance.

(a) Has OIG assessed the Postal Service's progress in complying with the Postal Employees Safety Enhancement Act and, if so, what conclusions has it reached?

Response

The OIG has begun several reviews of the Postal Service's implementation of Postal Employees Safety Enhancement Act, which mirrors the Occupational Safety and Health Act (OSHA) requirements, and the impact this will have on the Postal Service's organizational climate and operations. Currently, the OIG has a draft report on a midwest facility. Once the draft is finalized, it will be provided to the Subcommittee. These reviews will identify substandard facilities and the risk of being fined for non-

compliance with OSHA rules and regulations. The OIG believes an independent review of these issues will provide the Postal Service with information that can improve workplace safety and reduce potential liability.

(b) Has OIG looked into how much the Postal Service may have to spend to bring its operations into compliance with the Postal Employees Safety Enhancement Act and, if so, what did it find?

Response

The OIG has not identified how much the Postal Service will have to spend to bring its operations into compliance with the Act. However, the OIG reviews will attempt to identify systemic issues to assist the Postal Service in mitigating its potential for liability.

Breast Cancer Research Stamp

Question 20

In a September 30, 1998, report to the Service's Chief Financial Officer and Chief Marketing Officer, OIG observed that the Service needed to better define and track the costs to be deducted from the semipostal Breast Cancer Research Stamp's 7-cent surcharge.

(a) What steps has the Service taken to implement this recommendation?

Response

The OIG is currently conducting a second audit in this area. The objective of this review is to determine if the Postal Service has implemented the semi-postal stamp program in accordance with the Stamp Out Breast Cancer Act. This draft will be issued in February 2000. In the draft report, the OIG has identified concerns regarding whether the Postal Service recovered adequate and appropriate costs prior to remitting proceeds to the recipient agencies. A copy of the final report will be provided to the Subcommittee.

(b) Has the Service appropriately defined, tracked, and deducted its reasonable costs before turning over monies from the stamp's surcharge to NIH and DOD for breast cancer research?

Response

The ongoing audit discussed in 20(a) will address this issue and offer recommendations to management as appropriate.

Contracts

Question 21

As indicated in your statement, the Postal Service relies on strong financial management to control costs. The Service purchased $8 billion in goods and services and spent an additional $1.2 billion for contracts to repair, renovate, and construct facilities.

(a) What is your assessment of the Service's contracting procedures? Are there areas where improvements may be needed?

Response

The Postal Service has greater contracting discretion than other Federal agencies. While this discretion often facilitates sound and efficient procurement practices, OIG reviews have nonetheless revealed that improvement is sometimes warranted in the following areas:

- consistency in contracting practices;
- clarity of some contracting policies;
- integrity of some Postal Service's procurement operations;
- communication of best practices;
- efforts to attract and contract with minority and women-owned businesses;
- pre-qualification of contractors;
- determination of fair and reasonable contract prices;
- contract administration;
- evaluation of contractor performance; and
- certification of invoices for payment.

In addition, OIG audits have consistently shown the need for the Postal Service to provide appropriate supporting documentation and greater adherence to existing policies and procedures.

Revenue Generation

Question 22

You found that the International Business Unit failed to have key processes in place to achieve its projected revenue goals. In one international mail case alone you discovered that the Postal Service failed to collect nearly $20 million in revenue because the Service charged a lower negotiated international rate for mail actually processed completely as domestic mail. You also found that the IBU revenue forecast was unrealistic. This calls into question the very basis for the investment in a separate business unit for International. I understand you recommended a management review of the IBU.

(a) Please elaborate on your findings and recommendations regarding the International Business Unit. Please bring us up to date on whether management has taken acted on your recommendations.

Response

The OIG reviewed the International Business Unit and issued a report in September 1998. The report noted that the International Business Unit would not achieve revenue projections of either $2.1 billion for FY 2000 or between $7.8 billion and $11.5 billion by 2005. The inability to achieve revenue goals was a result of several factors, including initial unrealistic goals and inaccurate volume and revenue accounting. Additionally, management information systems did not provide adequate or timely information on international revenue, cost, and volume reporting. Thus, achievement of projected revenue goals and the financial viability of the International Business Unit as a separate business unit, based solely on its potential for revenue growth, was questionable.

The OIG suggested that the Chief Financial Officer and Senior Vice President direct an in-depth review of the International Business Unit processes and performance to determine whether the Unit was financially viable as a separate business unit or whether it should be incorporated into another operating component of the Postal Service. In his response, the Chief Financial Officer and Senior Vice President stated that he could not fully support this suggestion. He believed that the International Business Unit was established as a strategic business unit after careful consideration by the Postal Service's Management Committee only three years ago, and it would be premature to disband the business unit based only on inaccurate revenue projections.

The OIG continues to believe that an in-depth examination of the International Business Unit is warranted in order to evaluate its financial viability as a separate business unit. In its review of the International Business Unit, the OIG also suggested that the Postal Service implement recommendations contained in an internal report concerning International Business Unit financial and reporting systems. Management agreed with the OIG to develop action plans to address the needs identified. The OIG plans to reevaluate these issues in a future audit.

Y2K Readiness

Question 23

The OIG has been carefully monitoring the Postal Service efforts to be ready for the transition to the YR 2000.

(a) Do you think the Service is prepared for the Year 2000? What areas of vulnerability do you think need to be closely monitored?

Response

Considering its late start, the Postal Service did a remarkable job in preparing for the Year 2000. However, the OIG remained concerned with the Postal Service's vulnerability to Y2K problems throughout the rollover period. As a result, the OIG stationed its personnel at critical locations throughout the Postal Service to observe the rollover and report any observations. These personnel observed that Postal Service critical systems were fully Y2K compliant, and no disruption to service occurred.

During the final three months of 1999, the OIG issued four reports to management that highlighted progress and identified recommendations that management implemented to enhance Y2K readiness. Specifically, management agreed to monitor Day One activities to ensure that critical employees mentioned in the Y2K staffing plan would be available during the rollover period and that Day One activities would be completed as scheduled. Management also agreed with the OIG recommendations to expand testing to areas where contingency and continuity plans were not fully developed and to take appropriate quality assurance steps. The Postmaster General recently commended the OIG for its role in assisting the Postal Service in meeting this critical challenge.

Oversight of Contractors

Question 24

Your review of the Year 2000 Initiative identified opportunities for the Postal Service to improve its oversight of Y2K contractors. Specifically you noted that adequate controls were not always in place, unnecessary layers of contractor management existed, and in at least one case deviation from travel regulations were granted to a contractor. The Y2K Initiative is about to face the ultimate test and, presumably, contractors will be let go. Nonetheless, as indicated by your report the Postal Service may have failed to properly control and account for contractor work.

(a) What action has the Postal Service taken to address these issues? As the clock is winding down on this effort has the Postal Service's response been timely?

Response

The OIG did not conduct a formal followup review to assess the Postal Service's use of contractors for the Y2K initiative. When the initial report was issued, management was taking action to better manage the assigned contractors. Evidence before the end of the Y2K initiative indicated that progress had been made. Specifically, there were almost 200 contract employees at one Postal Service data center at the beginning of April 1999 and by November 1999 there were only 25 contractors remaining.

The Postal Service engaged a number of major contractors for the Y2K initiative. The OIG will monitor future contract-related costs for these and other major contractors as warranted.

(b) Do you know whether any contractors are or may be liable for failure to perform work under its contract with the Postal Service? If so, is there a role for the OIG in helping the Postal Service recover any losses?

Response

The OIG has not conducted any specific reviews to assess contractor liability in the event of Y2K induced failures, but given the evident success of Y2K preparations, contractor liability does not appear to be an issue. The OIG will continue to monitor Postal Service operations and will address the issue of contractor liability in the event of unforeseen or delayed Y2K induced failures. In the event that failures arise, the OIG can assist management by identifying the causes and effects of such failures.

Mr. MCHUGH. I want to thank Ms. Corcoran, who, I think, is doing an amazing job in establishing an office, and yet at the same time, not spending a lot of time getting acclimated, but rather going out, and as her testimony so adequately and, I think, accurately details, making a real difference in the quality of service that the Postal Service provides.

Thank you for that effort and that initiative.

And, Mr. Ungar, to all of you in the GAO, thanks for your partnership and you'll be hearing from us. Thank you so much.

[The information referred to follows:]

United States General Accounting Office
Washington, DC 20548

General Government Division

January 7, 2000

The Honorable John M. McHugh
Chairman, Subcommittee on the
Postal Service
Committee on Government Reform
House of Representatives

Dear Mr. Chairman:

As you requested in your November 22, 1999, letter, enclosed are our responses to various questions that you asked following our testimony at the Subcommittee's October 21, 1999, hearing on oversight of the U.S. Postal Service.

If you need further information or have additional questions about the responses, please call me on (202) 512-8387 or my Assistant Director, Teresa Anderson, on (202) 512-7658.

Sincerely yours,

Bernard L Ungar

Bernard L. Ungar
Director, Government Business
Operations Issues

Enclosure

Enclosure

GAO Responses to Questions Following U.S. Postal Service Oversight Hearing Held on October 21, 1999

Question 1. The Postal Service recently published its Annual Performance Plan for Fiscal Year 2000 as required by the Results Act. The Service will publish its first performance report next year on its performance in fiscal year 1999. What is your view on the value of these reports to the Service and the Congress? Can you give some examples of how they contribute to accountability and oversight?

GAO response. We believe that annual performance plans and reports provide valuable information to the Service and Congress in various ways. Most notably, such plans and reports can provide the Service opportunities for continuous review and improvement of its long-term goals and strategies for achieving the goals. In recent years, significant management challenges, such as increased competition from private delivery firms and electronic communications alternatives, have placed much of the Service's letter mail revenue at risk. As the Service stands ready to enter the 21st century, we believe that the process of preparing annual performance plans and reports can help the Service focus on goals and strategies for addressing challenges, mitigating risks, and achieving accomplishments. Also, the plans and reports can help the Service set the stage for initiating future actions to further its mission, so that the Service can maintain its unique position in the communications marketplace as the major provider of postal services that bind the nation together. In addition, annual performance plans and reports provide Congress information on the extent to which goals in the plans have been achieved and what actions may be needed to address or revise any unmet goals. This information is helpful to Congress in fulfilling its postal oversight responsibilities, which are critical in determining the Service's future direction.

We believe that some examples of how annual performance plans contribute to accountability and oversight can best be found in our most recent work involving observations that we made on the Service's preliminary performance plan for fiscal year 2000.[1] For instance, we observed that the preliminary plan for fiscal year 2000 represented a moderate improvement over the preliminary performance plan for fiscal year 1999, in that it corrected a number of weaknesses we identified in our assessment of the Service's preliminary plan for fiscal year 1999.[2] We observed that the Service's preliminary plan for fiscal year 1999 provided a partial picture of the Service's intended performance. We said that the Service's preliminary performance plan for fiscal year 1999 articulated well performance goals for many areas that defined expected performance that were quantifiable and results-oriented. However, we said that the preliminary 1999 plan did not fully capture

[1] The Results Act: Observations on the Postal Service's Preliminary Performance Plan for Fiscal Year 2000 (GAO/GGD-99-72R, Apr. 30, 1999).

[2] The Results Act: Observations on the Postal Service's Preliminary Annual Performance Plan (GAO/GGD-98-144, July 10, 1998).

the Service's mission and did not completely discuss the strategies and resources (i.e., human, capital, information, or other resources) that will be needed to achieve its goals. We made a number of recommendations directed at improving these weaknesses, and the Service was generally responsive in addressing these recommendations in its final performance plan for fiscal year 1999. In addition, Service officials said they would work to improve the Service's performance plan in future cycles. For example, Service officials stated that they would work toward improving linkages between performance goals, program activities, and budgetary resources, and planned to make adjustments in the budget reporting process to capture details on budgetary resources needed to meet performance goals.

Question 2. Your testimony pointed out that many stakeholders believe the Service needs to make tangible progress toward implementing a more complete set of performance measures and targets. Why is this important? What new measures are needed?

GAO response. We believe that performance measures and targets are an important part of the performance planning process. Performance measures help provide the Service feedback on how well its activities and programs have contributed toward achieving its goals. Also, the measures help identify ways for the Service to improve performance so that targets can be established for future performance.

In our observations on the Service's preliminary performance plan for fiscal year 2000, we stated that the plan is consistent with the intent of the Results Act that annual performance plans be aligned with a systematic management process that uses results-oriented goals and strategies as well as performance indicators to measure progress toward these goals. Also, the Service developed more measures and targets, which continued the process of developing a more complete basis for assessing the Service's performance. For example, the Service included two additional measures of timely mail delivery and two additional measures of workplace safety. We also stated that at the same time, it will be important for the Service to continue to make tangible progress toward implementing a more complete set of performance measures and targets. This information is also important to many postal stakeholders. For example, mailers and postal customers have expressed concern about the delivery service for advertising mail and periodicals and have said that measures are needed to track the Service's performance in these areas.

The Service's performance plan for fiscal year 2000 reported that a performance measure for on-time delivery of advertising mail was implemented and that the Service will develop a similar measure for periodicals. By adding performance measures in these areas, the Service and stakeholders will be able to assess the Service's progress and discuss targets for future performance. The Service has committed to implement additional measures and targets in future cycles. In working toward this objective, the Service has said that it intends to use a phased approach to develop performance measures for all of its products and services as soon as possible.

Enclosure

GAO Responses to Questions Following U.S. Postal Service Oversight Hearing Held on October 21, 1999

Question 3. With the assistance of the Federal Mediation and Conciliation Service (FMCS), the Postal Service, the four major postal labor unions, and three management associations have convened summit meetings since October 1997, to discuss a wide range of issues related to postal operations, including labor-management relations. To what extent does GAO believe that the meetings have contributed toward improving labor-management relations in the Service? What other alternatives exist that could further assist the eight entities in their efforts to improve such relations?

GAO response. Based on our discussions with postal and FMCS officials, we believe that the summit meetings have been beneficial for the Postal Service and its four major labor unions and three management associations. The meetings have helped reinforce to these eight organizations the importance of maintaining a network of open communications, which can help foster increased understanding of and commitment to the Service's mission. Also, we believe that the meetings have provided these eight organizations unique opportunities to reach agreement on alternative methods for testing proposed revisions to specific labor-management processes and initiating improvements.

For example, some of the unions, including the American Postal Workers Union (APWU) and the National Letter Carriers Association (NALC), established specific agreements with the Service to test revised procedures involving the employee grievance process. Also, other unions, including NALC, the National Postal Mail Handlers Union (Mail Handlers), and the National Rural Letter Carriers' Association (Rural Carriers), jointly signed a statement with the Service and the three management associations[3] to work to achieve a safer and more harmonious workplace throughout the Service with no tolerance for violence, harassment, intimidation, or threats of violence. Although such agreements can benefit both the Service and the unions, we continue to believe that a unified approach by the Service and its unions and management associations is a key factor in helping the Service effectively manage employees and improve productivity.

In recent years, labor-management relations problems have continued to plague the Service. Thus far, our 1994 recommendation for a long-term framework agreement involving the Service, its four major postal labor unions, and three management associations[4] has not yet been implemented. However, we continue to believe that to sustain improvement efforts, it is important for these eight organizations to agree on common approaches for addressing labor-management relations problems. In the face of competitive challenges to the Service's current standing in the marketplace as a major provider of mail processing and delivery

[3] The three management associations included (1) the National Association of Postal Supervisors, (2) the National Association of Postmasters of the United States, and (3) the National League of Postmasters of the United States.

[4] U.S. Postal Service: Labor-Management Problems Persist on the Workroom Floor (GAO/GGD-94-201A/B, Sept. 29, 1994).

services, we believe that the need for a single framework agreement signed by the eight parties has become even more significant than at the time of our 1994 labor-management relations report.

In addition to the framework agreement, we believe that other alternatives exist, which could provide the Service and its four major postal labor unions and three management associations opportunities to initiate improvements. For instance, as discussed in our October 1997 report,[5] the Service's establishment and use of strategic and annual performance plans, as required by the Government Performance and Results Act, can provide the eight parties, as well as other key postal stakeholders, opportunities to collectively focus on and jointly engage in discussions about the Service's mission and proposed goals and strategies to achieve desired results. Such discussions can provide the eight parties and other key postal stakeholders with opportunities to work together to develop and reach consensus on strategies for achieving various goals, including those that relate to the long-standing labor-management relations problems that challenge the Service.

Also, in October 1999, President Clinton issued a memorandum that reaffirmed the administration's commitment to implementing Executive Order 12871, which addressed labor-management partnerships. Issued in October 1993, the order was generally intended to revise the nature of federal labor-management relations so that managers, employees, and employees' elected union representatives could serve as partners in designing and implementing needed changes that could help improve agencies' operations. A key requirement of the order was for agencies to create partnerships in the form of labor-management councils that could help ensure the involvement of federal employees and their union representatives with managers in identifying problems and crafting solutions so that agencies could better accomplish their missions and serve customers.

The President's October 1999 memorandum set forth various requirements for agencies to follow in implementing Executive Order 12871. For example, the memorandum requires that beginning in April 2000, and each year thereafter, agencies are to submit to the President, through the Office of Management and Budget, reports that (1) provide information on the nature and extent of agencies' efforts to comply with the order and (2) identify improvements in customer service, quality, productivity, efficiency, and quality of worklife achieved as a result of labor-management partnerships. The reports are to be prepared with the involvement of and input from unions.

Since the Postal Service does not fall within the definition of an agency that is subject to Executive Order 12871, the Service does not have to adhere to any of the policies or

[5] U.S. Postal Service: Little Progress Made in Addressing Persistent Labor-Management Problems (GAO/GGD-98-1, Oct. 1, 1997).

requirements set forth in the executive order or the presidential October 1999 memorandum reaffirming that order. However, the Service is free to implement the policies contained in those documents to create and sustain labor-management partnerships, which we believe may help the Service and its unions address long-standing labor-management relations problems and initiate improvements.

Question 4. The General Accounting Office has been monitoring the progress of the Postal Service in preparing for the transition to the Year 2000. What is GAO's assessment of the Postal Service's readiness for the Year 2000? What concerns, if any, does GAO have in this area?

GAO response. As mentioned in our October 1999 testimony, we believe that since the issuance of our February 1999 assessment on Postal Service's readiness for the transition to Year 2000,[6] the Service strengthened its management approach to the Year 2000 problem and made significant progress in fixing its computer systems and determining that its key suppliers and electronic data exchange partners would also be Year 2000 ready. Also, the Service stepped up efforts to test applications and infrastructure equipment in a production environment—an important phase of the Year 2000 effort because Year 2000 conversions often involve numerous large interconnecting systems with many external interfaces and extensive supporting technology infrastructures. In addition, the Service completed over 500 business continuity and component contingency plans for its critical processes. With these actions underway, we believed that the Service was clearly much better positioned to face the upcoming century change.

Since our October 1999 testimony, we learned that the Service continued to make significant progress in remediating its data systems and establishing appropriate contingency and business continuity plans. As of December 1999, we found that based on information provided by the Postal Service to the Office of Management and Budget and our discussions with the Service's Year 2000 program management officials, all the Service's data systems were fixed and appropriate contingency and business continuity plans had been tested and were in place. Thus, we believed that the Service was reasonably prepared to make the transition to Year 2000 without major problems. In addition, we believed that the Postal Service did adequate planning to help ensure that its operations will continue to run smoothly after January 1, 2000. Finally, we monitored the Postal Service's Day-1 activities as it transitioned to the Year 2000 and observed no disruption of mail delivery or critical services through January 3, 2000.

[6] Year 2000 Computing Crisis: Challenges Still Facing the U.S. Postal Service (GAO/T-AIMD-99-86, Feb. 23, 1999).

Enclosure

GAO Responses to Questions Following U.S. Postal Service Oversight Hearing Held on October 21, 1999

During 1999, the Service took various actions as part of its efforts to make the transition to Year 2000 that we believe will result in significant benefits that should enhance information technology within the Service well beyond 2000. According to the Service's Year 2000 program manager, the actions included (1) the elimination of unnecessary software code, (2) the replacement of antiquated, locally developed software applications, and (3) the modernization of information technology equipment, including mainframe computer systems, mid-range computer systems, and desktop workstations. In addition, according to Service officials, the Service is implementing improved processes for documenting software, testing, quality control, and configuration management. Although we did not assess the Service's implementation of these actions, we believe that the actions should help ensure that the Service's data systems function more effectively.

Question 5. On October 26, 1999, the Postmaster General submitted his report to Congress as required by 31 U.S.C. 720 regarding the recommendations contained in the report of August 31, 1999, entitled, U.S. Postal Service: Deficiencies Continue While Antelope Valley Project Status Remains Uncertain. What are GAO's views on the Postal Service's response? Does the GAO view the Postal Service's response as resolving the project's status?

GAO response. The Postal Service's response has not resolved the ultimate use of the site acquired by the Postal Service in Lancaster in 1991, nor has it addressed the question of whether the proposed Antelope Valley project will be approved for construction. In the interim, the Postal Service identified some actions it plans to take to discontinue mail handling practices that contributed to delays in local mail delivery within Antelope Valley. In addition, the Service identified a short-term alternative for improving mail service that involved lease arrangements and building and site modifications that will take an estimated 12 to 15 months to complete. Meanwhile, the overall status and funding of the proposed Antelope Valley project have not been determined. Without a decision on the proposed project, the longstanding uncertainty associated with this project will continue, and the costs associated with unused property will continue to increase.

Mr. MCHUGH. The next person to testify, of course, is the Postmaster General and Chief Executive Officer of the U.S. Postal Service, Mr. William J. Henderson.

General Henderson, welcome. Raise your right hand.

[Witness sworn.]

Mr. MCHUGH. The record will show the Postmaster General responded to the oath in the affirmative, as I knew he would, because he's always a truthful man.

Mr. Postmaster General, Bill, welcome. Thank you for being here. Thank you for your patience. As you can see, we have a few topics to talk about. The stage has been set, and we're looking forward to your comments. I have read your testimony; it will be submitted in its entirety for the record. We now look forward to your presentation this morning.

STATEMENT OF WILLIAM J. HENDERSON, POSTMASTER GENERAL AND CHIEF EXECUTIVE OFFICER

Mr. HENDERSON. I won't read back my testimony to you. I'll just make a few brief comments, and then we'll go to the questions, if that's what you like.

First of all, thank you for all the help you've been. We've had—in a short term, we've had a very good year. In the Postal Service this fiscal year we set record goals in service and we also received a record rating of 94 percent by the consumers across America in rating the Postal Service good, very good and excellent.

We expect in this fiscal year to do about $100 million better than what we planned, so somewhere the neighborhood of $300-plus million. That's in spite of the fact—and you've been talking about it—the fact that we missed our revenue plan by $620 million. In other words, when we postponed the rates increase in June—that was scheduled for June, to January, we gave the American public an $800 million deficit. We didn't expect at that time to also have to make up another $620 million in revenue.

So, from an operating point of view, it was a difficult, but successful year.

We also, on the employee front, were very proud of the fact that we negotiated two labor agreements, one with the American Postal Workers Union, one with the Mail Handlers Union, that set the stage, I believe, for much better labor relations. We're in the process of negotiating, as we speak, with the National Letter Carriers Association. And we regrettably went to arbitration with the National Association of Letter Carriers, but that is now behind us. So I think it's been a very successful year for the Postal Service.

But I, like you, do not think that the future is potentially as good unless the Postal Service does something about the Internet, gets involved in it, gets active in it. And I also think that H.R. 22 is a very important piece of legislation that will help the Postal Service in its future.

I've talked about $17 billion which is the amount of money that people pay postage for to get bills and payments to one another. And there's no question all you have to do is read the paper: The conditions are springing up every day trying to put partnerships together in order to get that lucrative piece of business. So it's not

a matter of if, but when, and the impact on the Postal Service will be substantial when that occurs.

So I think all of the posts of the world face this and all of the posts of the world, with the exception of the U.S. Postal Service, all the industrialized posts, are actively engaged in reformation, including a major move toward privatization. So I think your work on this subcommittee is very important to the lifeblood and future of the Postal Service.

And I might add that you can't wait until the thing crashes, because by the time you recover from a crash, you will have injured a lot of businesses in America with forced higher rates.

So thank you.

[The prepared statement of Mr. Henderson follows:]

Statement of
William J. Henderson
Postmaster General and Chief Executive Officer
United States Postal Service
before the
Subcommittee on the Postal Service,
Committee on Government Reform, U.S. House of Representatives
October 21, 1999

Mr. Chairman and members of the Subcommittee, I appreciate the dedication and insight you bring to oversight of the United States Postal Service. I want to thank you for helping us fulfill our mission to bind our nation together by delivering to everyone, everywhere, every day.

Today, I am going to discuss a year, a season, and a century of postal service. With the help of the American public, postal employees made Fiscal Year 1999 one for the record books. Based on preliminary figures, the Postal Service earned record revenues of just over $62 billion, broke the 200 billion mark in total mail volume, achieved its best overall performance ever in First-Class Mail delivery, and recorded an unprecedented fifth straight year of positive net income.

The American people are the direct beneficiaries of this performance. First, it fulfills our promise to them to continue to restore the equity of the nation's mail system in accordance with the provisions of the Postal Reorganization Act. Second, it reflects our decision last year to delay the smallest rate increase in postal history by seven months, in effect providing the American public with an $800 million dividend. Finally, it keeps us on track to avoid a rate increase next year as we had originally planned. All told, these efforts will save America's ratepayers more than $2 billion.

We also made substantial investments in the mail as the Postal Service shifts from the age of automation to the age of information. While we continue to advance the automation of letter mail and flats, robots and sophisticated handling systems are being introduced into our plants. Within the next several years, fully automated processing facilities and a computer driven information platform will revolutionize the way we manage the mail and create an information rich mail

stream that will give postal managers and customers alike real-time performance information.

Information management is also driving change in the management and delivery of retail services. Our associate office infrastructure program is hard-wiring thousands of postal facilities into a national network that provides the communications backbone for new information technologies. This enabled us to deploy this year more than 22,000 of our next generation POS ONE retail terminals and over 300,000 hand scanners for delivery confirmation. More than 25 million documents and packages have been delivered and confirmed using this service.

Even the most advanced technology is only as good as the people who use it. The Postal Service has made it a top priority to build an inclusive and welcoming workplace that fosters employee success. We are committed to improved workplace safety, better workplace relations, systematic training for all craft and EAS employees, quarterly surveys to understand and measure employee concerns and issues, and the development of indicators and performance baselines to guide our progress in developing a fair and inclusive environment.

This year, for the first time in a decade, we reached negotiated contract agreements with two of our major unions. A third contract was settled at arbitration. We are disappointed that the arbitration decision failed to maintain parity with the negotiated agreements. Nevertheless, we are working cooperatively with our union and management associations. And we have made significant progress in developing faster, more effective means for resolving workplace differences. I think all parties realize that we must work better together if we are going to remain a viable enterprise.

Diversity is an imperative business issue for the Postal Service, which has one of the nation's most diverse work forces and a unique mandate to bind together a nation that grows more diverse every day.

This year we completed adoption of 23 diversity initiatives recommended in an independent study commissioned by the Governors of the Postal Service. Our

five-year Diversity Business Plan builds on this progress through comprehensive communications; appropriate recruitment, retention and promotion practices; an environment free of discrimination and sexual harassment; and establishment of a diverse supplier base.

Finally, each of you has received the Postal Service's Annual Performance Plan for Fiscal Year 2000, which embodies the results of our CustomerPerfect!, Baldrige-based management system. This plan will help us deliver today and prepare us to become a high-performing, operationally excellent supplier of choice for 21st century postal services in a competitive environment.

As spelled out in the plan, it is our aim to further restore the equity of the Postal Service through a sixth consecutive year of positive net income and a capital investment of $4 billion in technology, facilities, and other infrastructure. We will also continue on our path of cultural regeneration to make the Postal Service a great place to work as well as the preferred place to do business. We plan further service improvements in First-Class and Priority Mail, advertising, ground parcels, periodicals, and international mail. And we are committed to staying America's high value, low cost service provider by keeping future rate increases below the cumulative rate of inflation.

We are already more than a month into the new fiscal year and squarely in the middle of our busiest mailing season. We have been preparing for this season almost non-stop since last year. Working closely with the mailing industry, we have arranged for temporary airlift and work space capacity, 40,000 seasonal workers, and millions of dollars in mail trays, containers and other needed supplies. Our network operations communications network is ready and will run 24-hours a day during the height of the season. We are off to a strong start and confident that we will deliver.

This year the holiday season also brings with it a Y2K Grinch. But we have invested significant resources and talent to be ready for him, too. All of our mission critical information and mail processing systems have been addressed, tested, and independently verified. Live year-end mail processing simulations have been successful and our entire system has cleared the preliminary hurdles

represented by the start of Fiscal Year 2000 and the date of September 9, or 9/9/99, which some thought might crash older systems. We have also created more than 500 local contingency plans based on our considerable experience dealing with natural disasters that disrupt utilities, transportation, and other vital services. We will continue to prepare as the new year approaches and we will be ready to respond when it arrives.

The Postal Service is heading into the next century with the best performance, planning, technology, and management systems in our history. As always, we owe that success to the extraordinary effort of our managers, postmasters, supervisors, and craft employees.

At the same time, though, we enter the new millennium knowing full well that the most significant challenges in our history await us. Tomorrow's marketplace will offer Americans more powerful and plentiful communications choices than ever before.

Private delivery carriers will aggressively try to maintain domination in their respective markets. Newly privatized and deregulated foreign posts can be expected to offer an increasing range of international services to American customers and to begin creating delivery networks right here on U.S. soil.

We also face exponential growth in electronic communications. Computing power, bandwidth, innovation, and popular acceptance are rapidly expanding. And well-funded and highly motivated forces in the banking, telecommunications, and computer industries are building e-payment networks. As consumers grow more comfortable with logging on to pay their bills -- these efforts will reach critical mass. The result could be erosion of our total revenues. We believe nearly $17 billion is at risk.

Our market research suggests that First-Class Mail volumes may actually decline over the next five years, even though we increase mail's value by keeping costs low and quality high. This factor, along with the rising costs of maintaining a national infrastructure of 38,000 facilities and a delivery network that grows by a million stops a year, means we cannot sit still. We have to generate new growth if we are to maintain affordable prices and investments in better service.

That is why we have been vocal in calling for postal reform, and why we have worked closely with this subcommittee to develop a fair, meaningful reform bill. The legislation includes some tradeoffs, but on balance, we believe it provides pricing and product flexibilities we need to stay relevant and healthy.

We have a responsibility to the American people to ensure a healthy and meaningful postal system in the next century. What's at stake is not just the continuation of perhaps the most visible and personal of all federal services, but the endurance of a delivery system that touches every American, helps bridge our vast distances and differences, and binds our nation together.

The mail is an experience that we all share. We look forward to getting our mail. It is a unique and powerful moment in our day. It brings information, entertainment, opportunity, and basic necessities. There are magazines and catalogs; birthday presents and post cards; bills, coupons, and offers galore. Mail has become the gateway to the household, an unmatched channel for commerce and communication that connects families and friends, governments and citizens, businesses and customers, publishers and readers, charities and sponsors.

As we look to the next century and the turbulent change it will bring, we have to ask ourselves, "What will it take to preserve that connection for the next generation of Americans?" I believe an answer does exist and I think we can take our cue from the way this nation and its mail system managed the transition to the current century.

As the year 1900 approached, our postal system, the Congress, and the American people were grappling with a nation in transformation. America was becoming a world power and the postal system was expanding its reach around the globe to possessions and territories like Alaska, Hawaii, Puerto Rico and Guam and American troops serving in Cuba and the Philippines.

At home, the industrial revolution was in full swing. And the Postal Service, ever pushing the envelope of technology, was testing mail collections by automobile in Buffalo, New York. Postmaster General Charles Emory Smith ventured out on a limb to predict that "the substitution of motors for the horse and wagon will possibly become universal."

The real revolution, however, was taking place in rural America where our farmers demanded access to the information superhighway of rural free mail delivery. Many knowledgeable observers and some members of Congress feared that a universal mail system would drain the national treasury. But the voice of rural America prevailed.

In the end, rural delivery not only worked for America's farmers, it stimulated the entire nation. It increased the circulation of the press and periodicals, raised farm values, prompted the creation of roads, and expanded commerce. The mail-order industry blossomed as did private parcel firms.

Today, America and the Postal Service face a new century of opportunity and uncertainty. In many ways, the issues are far less controversial than a century ago, but the stakes are just as high -- America's place in the 21st century and universal mail service for all Americans.

The Postal Service's strategies are just beginning to take shape, and our role vis-à-vis the private sector will have to be defined in concert with all of you and our many stakeholders and customers. But some things are already very clear.

We must build on our strong Internet presence. Our public homepage is the most heavily trafficked government site, receiving about three million "hits" each month. Customers use this site to find ZIP Codes, calculate rates, buy stamps, track packages, and get other key postal information. We intend to use the speed and access of the Internet to offer customers information about their mail and access to our products and services.

As on-line purchases soar, both businesses and consumers want prompt, reliable delivery, and easy access to a carrier who can handle returns. The Postal Service is listening to the voice of America and we are working to earn our share of the growth. We believe we can be the carrier of choice for merchandise purchased on the Internet and the inevitable returns that result.

So, despite many challenges, the Postal Service sees the 21st century as another great opportunity to build on our legacy of service to our nation. We have worked hard to combine private-sector efficiency and customer focus with our public service responsibilities as good government. We look forward to working with this

subcommittee to assure that the American people can continue to rely on the Postal Service for high-quality, low-cost mail services.

Thank you, Mr. Chairman, that concludes my statement.

# # # #

Mr. MCHUGH. Thank you. I think that's certainly one of the messages here today insofar as the Congress' role in this. Three years is the blink of an eye; it takes us 3 years to decide what day of the week it is, and then we don't all agree. So the point being, I think, the challenge is immediately upon us.

I'm sure my colleagues are going to want to ask you about what you can do internally to make it up. But let me ask a broader-based question, just to begin. You're talking in your testimony and in other venues about at risk in this decline of first-class mail, $17 billion roughly. That is about 30 percent. If nothing else were to change, you've had no legislative relief, you've now had to go to this service cutback size, because you're locked in on contracts, et cetera, what does 30 percent in terms of cutbacks mean to an organization like the Postal Service? Are you even able to dream of such a thing?

Mr. HENDERSON. Well, it would be very traumatic not just for the Postal Service's workers; it would be traumatic for the American public. I mean, the Postal Service is forced by law to break even. So you would begin a huge cost-cutting effort, but you would also begin raising prices. I mean, I've used as a metaphor many times the Sears problems in the 1980's where they lost traffic in their stores across America. And if they had had the postal laws governing them, they would have had to raise their prices, which would have just sent them into a spiral.

So it's very important that these issues be addressed prior to this happening, not after it happens.

Mr. MCHUGH. Generally, for rate cases, I understand you roughly equate a 1-cent increase in the cost of a first-class stamp as a billion dollars in revenue; is that right?

Mr. HENDERSON. Right.

Mr. MCHUGH. That probably would not be true anymore, however, in the future, if your first class volume is coming down like that; but let's use that. If it were even semipractical to raise the price of a first-class stamp 17 cents above, making it 50 cents, have you projected or looked at what that might do to the volume of first-class usage? Wouldn't you just be digging your own hole deeper and causing more problems, and the higher you're forced to raise the cost, the less the return, diminishing return?

Mr. HENDERSON. That's absolutely right. We are looking at scenarios, operational scenarios, but as a general proposition, you can see it from prior rate increases, when you raise the rates, there's a deflation of volume for a period of time until stamps become a better bargain. It would be disastrous for the American community to have that happen, absolutely disastrous, and we would try every possibility not to allow it to happen. But $17 billion is a lot of money.

Mr. MCHUGH. Have you had an opportunity to prioritize your least favorite options? In other words, what do you do first? Let me pose the question that you never want to answer: Do you begin to close Post Offices or do you cut back on Saturday mail delivery or——

Mr. HENDERSON. We are in the process of developing those scenarios now. I don't have the priority today, but I mean you would look at every cost center you had. You would have to look at every-

thing. Service reductions, you would have to look at it across the board in order to make up a 30 percent drop in your revenues.

Mr. MCHUGH. You operate 38,000 post offices roughly across America. If you were forced to a point by which you had to close some, I would assume a large segment of the least efficient or most costly are probably in rural communities. Is that a fair statement?

Mr. HENDERSON. Yes.

Mr. MCHUGH. We do have some bells, for a vote, but before we do that, let me yield to Mr. Davis and maybe he can complete his questioning before we go vote.

Mr. DAVIS. Thank you very much, Mr. Chairman.

Mr. Henderson, we discussed a great deal with Ms. Corcoran—cost savings, cost-cutting, finding revenue that could be enhanced. Given the fact that we spent the $101 million contracting out Priority Service without any real discernible improvements, is there any rethinking of that decision?

Mr. HENDERSON. Well, let me say for the record that we don't agree that there was not any substantial improvement. We have an independently measured service, independent measure of service, that shows the PMPC network substantially higher than the rest of the country. The IG based that finding on the fact that we did not have a baseline. But if you look at absolute scores between what the PMPC network is doing and the rest of the country, there's a substantial improvement; and that improvement is based on the fact that we've created a network, hubs for processing of priority mail, not the fact that whether or not it's done in house or by private sector.

Mr. DAVIS. You indicate that they weren't looking necessarily at all of the factors in terms of a baseline. There has been some question relative to data generated and the integrity of data generated by the service and that data being used to make certain projections and analysis.

Is there any change taking place relative to the data-gathering process that you're using?

Mr. HENDERSON. Across the board, the answer is yes. I mean, we did—had an independent study done that generally gave the Postal Service a clean bill of health, but made a lot of recommendations for tightening up data collection. And we are in the process of implementing those recommendations. That doesn't relate to the PMPC, which is measured—it's not our—it's an independent measure of service data.

Mr. DAVIS. We raised the question earlier. As a matter of fact, I believe that Representative Owens raised the question to an investigation of minority procurement opportunities, and while that information was not available and forthcoming from the IG, do you have information relative to the changes that have occurred in relationship to that?

Mr. HENDERSON. Yes. We have a substantial effort to involve more minority businesses in purchasing, and it has been under way for some time; and we think when the IG goes back in and reviews, they'll see substantial progress being made.

Mr. DAVIS. I would like to yield to Representative Owens.

Mr. OWENS. I thank the gentleman for yielding. I have an amendment on the floor. I won't be able to return.

But you had mentioned a 94 percent consumer rating. Did I hear that correctly?

Mr. HENDERSON. Uh-huh.

Mr. OWENS. Can you explain that a little bit?

Mr. HENDERSON. We do an independent measure across the United States; we call it the customer satisfaction index. It's done by Gallup, and 94 percent rated the Postal Service good, very good and excellent on that. It's an overall question. It's a very detailed questionnaire.

Mr. OWENS. Is that broken down by districts or cities, or can I see a——

Mr. HENDERSON. Yes, it's broken down by districts, by major metropolitan areas. We would be happy to provide you the data.

Mr. OWENS. I would be very thankful.

Mr. DAVIS. Maybe the last question before we have to go, Mr. Chairman.

Mr. Henderson, would your office have the time that you could perhaps provide us with your own report of the procurement practices and changes that have occurred?

Mr. HENDERSON. Yes, absolutely. I'll provide it to you.

Mr. DAVIS. Thank you, Mr. Chairman.

Mr. MCHUGH. We have about 8 minutes for this vote. I understand it's just a single vote.

Mr. Postmaster General, with your forbearance, we'll be back very shortly.

[Recess.]

Mr. MCHUGH. As much as I'm tempted, I think we had better wait a moment for another responsible adult.

As you've heard here this morning, we do have a series of very important education bills that it happens a good number of the subcommittee members are very interested in and wanted to be on the floor. So I'm not certain when they'll get back.

So I will exercise the prerogative of the Chair and reconvene our discussion here. If they come back, I'll yield to them. In the meantime, why don't we talk?

Mr. HENDERSON. Sure.

Mr. MCHUGH. You have mentioned—I believe Mr. Ungar mentioned the letter carrier agreement that came about as a ruling of an arbitrator. What is the likely total financial impact of that agreement, including what it is likely to do in the future—and I'm not asking you to reveal your hand, but it does have significant implications for the first time. It decouples a number of the various employee units in a pay perspective that I assume the other employees units are going to want to reestablish, and it's probable that you're going to have to respond in some way.

If you're working on a ballpark figure, what do you think the total cost of that one ruling is going to be?

Mr. HENDERSON. Within the confines of the ruling itself, it's $2.4 billion. If you take it out—I mean, everybody in the internal postal community is very interested in that because it changes the relationship. So you'll have the rest of the unions going to reestablish that relationship, which means they want a higher level. You then have postmasters who have an existing differential with craft employees that will have—will want some differential, and then you'll

have supervisors wanting some differential. So we haven't tried to—I don't know if I could swallow that number; I haven't tried to calculate it yet. But it did have, you know, a ripple effect throughout all of the labor deals. It's affected the current negotiations that we're in.

Mr. MCHUGH. I not only understand, I certainly accept that. But the ball park, are we talking, more likely, tens of millions or, more likely, hundreds of millions of dollars?

Mr. HENDERSON. Hundreds of millions. Billions of dollars.

Mr. MCHUGH. Billions of dollars from this one ruling?

Mr. HENDERSON. Yeah.

Mr. MCHUGH. Your fiscal plan that Mr. Ungar referred to that is projecting $100 million net revenue based on some productivity assumptions, based on some work-hour assumptions, did that include anything to accommodate this ruling?

Mr. HENDERSON. No. No, it didn't. And this fiscal year will not be impacted because the level increase doesn't occur until next year.

I was interested in hearing him call making this budget this fiscal year a "miracle."

Mr. MCHUGH. Well, we're getting near the season of miracles. I believe he said he did not want to use the word "miracle," but he decided on "some major development."

But the point I wanted to make—and I believe you would agree, and if you don't, please respond. I'm not trying in any way to minimize what I think has been a string of remarkable net revenue years for the Postal Service, truly historic. But on a $62 billion revenue plan, $100 million is thin—a lot better than the reds that piled up year after year in previous times, but still thin.

So if you then have something thrown at you, so to speak, that is totally beyond your power, really totally beyond your ability to forecast, that only makes the picture more difficult. And when we're talking about hundreds of millions, billions of dollars, added onto your revenue projections and loss of first-class income of $17 billion, you've got a serious problem.

Mr. HENDERSON. Yes.

Mr. MCHUGH. And it's here today.

Mr. HENDERSON. And I would add that the activity in e-commerce, the Internet is very suppressed, and it's suppressed because of Y2K. You've got large corporations like IBM, large organizations like the U.S. Postal Service are really strapped down right now. In other words, we've frozen new projects until we get through Y2K. And that's been a common practice throughout industry and the public sector.

After January, after the Y2K problem starts to dissipate, or the potential problem, you're going to see much more activity than we predict on the Internet, than has been experienced thus far.

Mr. MCHUGH. And I agree. There's a likely technological snowball building here that is unleashed in certain part past Y2K and people's concerns about it, but continues to roll as more and more Americans find themselves wired into the Internet. As more communities across this country have Internet access, opportunities increase; and as people become more comfortable in engaging in that kind of commerce. A lot of folks today peruse the pages of the

Internet, looking at product, and then pick up the phone and call in the order because they're not just quite comfortable. But that's going to lessen as time goes on.

So the problem isn't something where you take the hit, you hunker down, accommodate it and you go on. It's something that's going to continue to increase and put more, rather than less, pressure on you.

Let me ask you one final question, and I'll yield to Mr. LaTourette. A lot of people say, well, electronic commerce did have its challenges, but it has its benefits as well. If you call up—if you wire in, call up on the Internet a mail order house, order a pair of snow boots or whatever it is, then the possibility of the Postal Service serving as the carrier certainly is there and increases your opportunity.

Have you been able to weigh or project revenue losses on first-class versus what you might pick up? I know those are total estimates, but——

Mr. HENDERSON. We think that the Postal Service would be used as a majority move for e-commerce because of the low-cost, high-quality service that's provided. The answer to the question depends on the rate of erosion. If it's—it erodes like business-to-business mail did, in which we made it up in other products, then it's OK. But if it's like what they call the "hockey stick," and that is, there's just enormous adoption of electronic bill payment that doesn't involve the Postal Service, then I don't think there's any way you can make up a $20 billion, $17 billion organization.

So it really is the—the key is the rate of erosion. And it's eroding right now, just so you'll know, at between 1 and 2 percent. But—less than 1 percent of all Americans pay their bills electronically today, but as I say, that's—the Internet is looking for sources of revenue. And clearly you and I have to pay our bills and there's a clear opportunity here to tap in. And I think, after the Y2K fiasco is over, then you'll see one heck of a move for a lot of players to get into this.

Mr. MCHUGH. Thank you.

The gentleman from Ohio, Mr. LaTourette.

Mr. LATOURETTE. Thank you, Mr. Chairman.

And, General, it's nice to see you again. I have about four areas of concern that I want to talk with you about. They're not all connected, so I apologize for skipping around. But I want to begin where the chairman left off, and that is that I know it's tough to guess after Y2K, but there has been some speculation and I think when you appeared over at the Senate at a similar hearing there was discussion about the fact that your priority mail services and your package services with the advent of e-commerce do—you do look at that as a potential to offset some of the losses in first-class mail.

I understood the "hockey stick" examination. But I know that I was startled when I read U.S.A. Today yesterday and saw the projection, and certainly all of us in the subcommittee take the GAO's testimony here seriously and recognize the chairman and all of the good work that he's done in postal reform to move through this Congress at a good rate, to position the Postal Service for the next century.

However, it would not be—rather than just being doom and gloom, couldn't the users of the Postal Service and the fans of the Postal Service take some comfort in the fact that people will not only be paying their bills over the Internet in the future, but if they order snow boots up in New York, that the Postal Service will be the dominant carrier of the snow boots to their homes. And that will, in fact, sort of be both a blessing and a curse of the Internet for the Postal Service in the next century.

Mr. HENDERSON. Yes. And if I painted that, I'll clear that up. I don't want to paint the Internet as a curse. The Internet is the Internet. It is a new channel into the home. It's how you leverage it that's going to determine whether it's a positive or negative impact. And we have people working very actively to make it a very positive impact on the Postal Service.

Mr. LATOURETTE. The second area of concern that I have, I believe in August of this year, the Postal Service launched its new PC postage program, which I think is a very exciting program and a great example of how the Postal Service can use new technologies to move forward. If I understand my history right, it hasn't been since 1928 that the Postal Service has taken a look at the postage meter market. In that line, I think on August 9th you had a press event and you actually have awarded some contracts to vendors.

Mr. HENDERSON. Yes, to two vendors.

Mr. LATOURETTE. And who are those?

Mr. HENDERSON. Stamps.com and e-stamp. We didn't award contracts; we certified that their encryption met our standards. There are two more, Pitney Bowes and Neopost, that will be coming out there and are in the testing phases now. So there are four companies in the world that we know about that are going for postage online.

Mr. LATOURETTE. And that actually leads into the question that I had. It was my understanding that there are two vendors that are looking for that seal of approval or that certification, and because this is such an exciting opportunity, I think if you look—you go back in time and say, this hasn't happened since 1928 that this market has been open to competition.

Do you have any qualms or difficulties or questions in indicating to the subcommittee that—and I say this because it's my understanding that the DOJ has an investigation dealing with some monopolistic practices dealing with postage meters at present. Is there any concern that you have that the opening of this new market is going to somehow be constrained, be anything but fair, and everybody that has the ability to meet your standards is going to have the ability to compete, which obviously is going to benefit consumers and the service?

Mr. HENDERSON. That's our goal, to make sure that it's open and fair. There's no indication to me, anyway, that there's anything but really open competition in the PC postage. You've got two unknown players right out of the box. I mean, they didn't exist; they're new companies.

Mr. LATOURETTE. I think that's what's exciting about it. You would think when this program, when I first read about it and saw that this program—you would think that the old standbys would be the ones that would be jumping on it. So when two firms that

I don't think I was familiar with get the first certifications, I think that that adds to some of the excitement by some of us that that is going to be a good, competitive growth area.

The second—or maybe it's third, I've lost track, but this subcommittee recently had the opportunity to look at legislation called Honesty in Sweepstakes Act of 1999. And the part of the issues that we discussed had to do with what happens when Federal regulation would somehow preempt or invade the jurisdiction of the States relative to what their postal regulations are or their regulations regarding mail coming into their States are.

Can you indicate just what procedures you have in place when your customers, the mailers, are subject to conflicting postal regulations as they relate to State laws? Is that something that you've taken a look at?

Mr. HENDERSON. I have to submit that for the record. That's a little beyond my range.

Mr. LATOURETTE. Then if you could, I'll send you a quick note, and I would appreciate that.

The last one has to do with what I was talking to the Inspector General about. You know from some of the hearings on H.R. 22, competition is something that is of concern to me. I talked to her about the international mail arena and specifically the Postal Rate Commission's report from June of this year, that if I had my numbers right, there are 14 international products, and that, at least as I understood the PRC's evaluation, four of those, at the moment at least, aren't carrying their weight, that they're being subsidized if not by domestic mails, as was indicated by the IG. The money has to be coming from somewhere. Is it correct that those four products, at the moment at least, are being subsidized by other international mail products? International mail is paying its own way, but you have——

Mr. HENDERSON. They are at the moment. I don't know at this moment, but there were four products. Most of the impact for those products occurred as a result of Asian flu where they were profitable, and their volume is sensitive. When the volume goes down, your infrastructure costs overwhelm your revenue. And we—it's not important who the customers were, but we talked with the customers, and they asked us to hold out to see if those markets would improve. We held out for quite a while, and then we were forced to raise the rates, and then we lost some of the business as a result of that. So it——

Mr. LATOURETTE. Of those, and again, if you want me to submit this one because you don't have the report in front of you, I don't want to sandbag you and ask you a question that's unfair, but that seemed to be the finding of the PRC relative to global package link. When it comes to global priority mail, they indicated that although the suppressed foreign markets may have been a factor, one of the things the Postal Service has indicated was that the loss was due to a rather high advertising budget for that product. And so in addition to not only raising rates, I think 14 percent in the instance of that particular product, there was going to be a suppression of the advertising budget for what was now deemed to be a product that wasn't carrying its weight. Has that occurred since the PRC report has come out?

Mr. HENDERSON. Yes, as far as I know, that has occurred. That was factual, what you just said. When you have a product, if I'm selling one box and I'm trying to sell it all over the country, the revenue generated from one package doesn't cover that infrastructure cost. There's a point at which you have to reach a certain volume, and they decided to pull back on the advertising and try some other technique.

Mr. LATOURETTE. The overall question, I think, that comes up in postal reform and also relative to the international mail, is there a procedure in place that when you launch a new product, you have 14 international products, four aren't making it, is there a time when you sort of cut them loose and say, we thought this was a good idea, but it doesn't appear to be that way? If the answer is yes, and I would hope it's yes because you wouldn't want to continue to lose—pour money down the hole that isn't yielding a result, have you reached that conclusion with any other foreign products cited by the Postal Rate Commission at this point?

Mr. HENDERSON. No, not yet, but we do look at that monthly. It's been difficult not only for us, but it's been difficult for the private sector and the international market, too. We have had companies that have gone as long as 7 or 8 years without making money, but there's a belief that American goods and services are going to be demanded in foreign countries, and the carrier of choice is going to be the folks that make the money, and we're very interested in making the money.

Mr. LATOURETTE. And then last, and then I'll get off of this subject and stop asking questions, again, going the global package link, as I understood, I think, the last time you might have been here and when you were over at the Senate a little earlier, there was some discussion about the fact that the rates are set because there's a requirement that a shipper send at least 10,000 packages a year. Somewhere recently I'd seen published up to one-third of the customers—and you're right, it isn't important who the customers are, but those who are enrolled or signed up for those discounted rates indicating that they would ship up to 10,000 packages a year, up to a third of them have not fulfilled that mark. Is that a correct report?

Mr. HENDERSON. Generally speaking, there's—they have a cutback. I don't know if the numbers are—I don't know that they're inaccurate. I just don't know. But there was a pullback because much of that mail was headed to Asia, and they are just pulling out of that market. They're pulling back trying to reduce the impact of the Asian flu.

Mr. LATOURETTE. If the rate structure is predicated on volume, which I assume—you know, you say I'm going to give you this rate to ship something overseas, but you've got to agree to send 10,000 pieces, for whatever reason if they find that not economically practical, has the Postal Service adjusted its rates upward for that product to reflect the fact that the premise upon which it's based, that you're going to use so much of our business, has not occurred?

Mr. HENDERSON. We did adjust the rates separate not because the volume didn't materialize, but because we were trying to cover more of our costs. It's a negotiated deal with various individual customers. We try to be accommodating to them. We don't want to

just pull out and leave them high and dry. That doesn't give us a good business reputation. So to the degree possible, we try to hang in there with them. They're certainly not in the business of losing money, and matter of fact, I think every indication is Asia is starting to come back.

Mr. LATOURETTE. So would it be your expectation that that particular program, which has a 10,000-piece-per-year floor, if the economy improves, that the Postal Service will make money on that product?

Mr. HENDERSON. We hope to. That's why we're here. That's my expectation.

Mr. LATOURETTE. Thank you.

Thank you, Mr. Chairman.

Mr. MCHUGH. I thank the gentleman. Excellent line of questioning, which also, by the way, would be covered under H.R. 22. It's been an unpaid political advertisement.

Mr. Sanford.

Mr. SANFORD. Let me go from the universal to the very parochial, if I may, and it may be inappropriate that I even ask you this question, in which case I just ask that you hand it off to whoever might know. That is, recently the Postal Service announced that they were canceling plans to build a facility at the old Air Force base in Myrtle Beach, SC. That sent up all kinds of red flags, with folks back home calling me. The reason that the Postal Service said that they were going to do this is because of the distance between Florence, SC, and Myrtle Beach. The logical question that people ask back home of me was, well, Myrtle Beach didn't move over the 12 months of them negotiating this site, tying down the land, whatnot; we stayed in the same spot. We don't understand this reasoning. And so my question would be, could you offer any insights that I could offer to my constituents back home on the change?

The other thing I think just procedurally, I think this is a very legitimate point, was one of the things that the Postal Service folks brought up back home was after the operational review, they decided the site no longer made sense, but in the process they got all kinds of people excited, thinking there were 200 jobs coming to Myrtle Beach. Shouldn't the operational review come first before communities, whether it might be—whether it's Myrtle Beach or L.A., get excited about the prospect of a postal facility coming to their neighborhood, and it turns out at the end of the operational review that doesn't happen?

Mr. HENDERSON. You're absolutely right. I'll give you the rationale for the record, the details to your office on what the reason for changing their minds. I do know that they are still looking in Myrtle Beach for an operating facility, but it is unfortunate when a community anticipates something that as a result of an operational review might not occur. So we—they should have done the operational review first. That's right.

Mr. SANFORD. If there's any way—because apparently it was talked about at the beginning of October, some sort of press release from the Postal Service just to squelch it, because people keep calling—not that I'm selfish about this, but I am—our office saying why this happened, some kind of explanation from the Postal Service to the local media outlets back home just so that they feel like

the question has been answered, because from their perspective it feels like it's still hanging out there, and they don't quite understand why.

Mr. HENDERSON. We'll put out a press release. We'll show it to you before we release it.

Mr. MCHUGH. Mention him.

Mr. SANFORD. I appreciate it.

I don't want to burn up any more of your time, but going back to this cost conversation we briefly had, any further insights that you could offer me or others on the committee on how to get ahold of the cost part of the income statement with Postal Service?

Mr. HENDERSON. It's substituting capital for labor. It's automation. If you take the productivity in the Postal Service in 1988 and assume that same productivity today, you'd have to add over 100,000 people to the rolls. There's a huge impact.

The thing that we have enjoyed over the last 25 years, 28 years I've been in the Postal Service, is continuous growth. In other words, you're just like an automobile plant with enormous demand that keeps escalating up. You keep expanding. That's what happens in the Postal Service. We have been in the past growing. We've made money in the last 5 years, and our expenses each year have been somewhere in the neighborhood of 5 percent. So that's good growth. These charts don't predict that for the future, but there was never anticipation that the Postal Service's absolute costs would go down because you have a growing workload, growing demand, and it shows up on your bottom line.

Mr. SANFORD. I thank the Chair.

Mr. MCHUGH. I thank the gentleman.

General Henderson, you may have heard Mr. Ungar in the response to one of the subcommittee members—I'm sorry, I don't remember which one—who asked about ratemaking data. Mr. Ungar cited the report that made some 40 recommendations, I believe he said, and then he went on to suggest that GAO had not yet been successful getting a response from you folks as to how, if at all, you were going to respond to any or all of those 40 recommendations. Are you familiar with where that might be?

Mr. HENDERSON. We're in the process of implementing those recommendations. I'll clear the problem up with GAO.

Mr. MCHUGH. Is it your plan to issue a response to the report or an implementing plan to the recommendations? In other words, how might we on the subcommittee be advised as to what you're going to do to pursue that?

Mr. HENDERSON. We didn't plan on it, but after this today, we'll put together a timeline and some milestones and provide you the report.

Mr. MCHUGH. Great.

[The information referred to follows:]

WILLIAM J. HENDERSON
POSTMASTER GENERAL, CEO

UNITED STATES
POSTAL SERVICE

February 29, 2000

Honorable John M. McHugh
Chairman, Subcommittee on the Postal Service
Committee on Government Reform
and Oversight
House of Representatives
Washington, DC 20515-6246

Dear Chairman McHugh:

Enclosed is the edited transcript and follow-up questions for the record from the October 21, 1999, oversight hearing before your Subcommittee.

I appreciate the opportunity to testify and look forward to working with you in the coming year. Please let me know if I may be of further assistance.

Sincerely,

William J. Henderson

475 L'ENFANT PLAZA SW
WASHINGTON DC 20260-0010
202-268-2500
FAX: 202-268-4860

Questions submitted to Postmaster General William J. Henderson in follow-up to the Oversight Hearing on October 21, 1999

1. The Postal Service reported that successful cost management in FY 1999 has the Postal Service on track to achieve its FY 1999 operating plan for a $200 million net income. It has been reported that net income may, in fact, be close to $300 million for FY 1999. According to the Postal Service, for FY 2000, it appears that cost-saving efforts and expected mail volume growth of 3.8 percent should enable the Postal Service to reach its FY 2000 net income target of $100 million. To its credit, this would mark the sixth consecutive year of positive net income; something never before achieved by the Postal Service.

(a) *How do you respond to those who question the need for a rate case in light of this strong financial performance?*

Expense reductions realized as a result of the "Management Challenge" initiative enabled us to record a net income of $363 million in FY 1999. However, inflation and other cost pressures continue to place strains on our financial performance. Eventually, our present rates will not produce enough revenue to cover our costs.

Looking forward to 2001, one major driver of expense increases will most likely be labor costs. Two of our major collective bargaining agreements will expire early in FY 2001 and the costs of new labor agreements are uncertain. A third major union contract, resulting from an arbitrated settlement, extends into 2001 and provides for a general pay increase, continuation of COLA, and a one-grade pay increase for over 200,000 workers early in FY 2001. Employee benefit costs such as health insurance are also forecast to rise.

The cost of our universal service infrastructure also continues to grow. The nation's growing population produces about one million new addresses that we must deliver to each year. This requires more letter carriers and mail handlers, as well as more trucks, processing equipment, and buildings. In addition, we must maintain and improve our current physical assets and prepare for the future with new technologies and services. This requires funding for our capital investment program.

While we are constantly improving our efficiency to help keep costs down, we simply cannot cover all these additional costs without some increase in our rates.

2. The current rates and classification schedule was implemented during FY 1999. Many stakeholders have argued that it would be good public policy to delay an omnibus rate filing until the FY 1999 cost figures are available in order to have the best possible data on which to base rates and classification changes.

(a) *Does the Postal Service agree with this viewpoint and is a delay under consideration for this reason?*

While fully understanding the potential benefits from basing the next rate case on cost data from FY 1999, as explained below in response to subpart (b), the Postal Service does not believe that those potential benefits would outweigh the financial costs of delay.

(b) *If not, please explain why using FY 1998 cost data as the basis for setting rates is necessary and acceptable to the Postal Service. Please include in your response a discussion of the financial and public policy considerations that the Postal Service takes into account in the deciding when to file for an omnibus rate change.*

The driving force behind the filing of any request for general postal rate increases is the need to maintain the financial viability of the Postal Service. In general, issues relating to the rate case process are secondary to the more fundamental issues that determine when a rate change is required. For example, once it is determined that the Postal Service's financial condition and other public policy considerations warrant a rate increase, issues regarding what exact data are available to employ in that process are unlikely to alter the primary determination that a rate case is required.

Specifically, complete information that would allow us to use FY 1999 as the base year for costing purposes in a rate case will not be available until spring of calendar 2000. If the Postal Service were to delay its filing (relative to an otherwise preferable filing date) in order to incorporate FY 1999 data, the inevitable result would be delay in implementation of the new rates. Depending on the ultimate magnitude of the overall rate increase, each day of delay in implementation could be worth tens of millions of dollars.

In theory, it would be preferable to use FY 1999 data instead of FY 1998 data. By the same logic, however, it would also be preferable to use FY 2000 data instead of FY 1999, because FY 2000 would be the first full year of data reflecting whatever changes might have been engendered by implementation of new rates in January 1999. Yet, obviously, to wait until complete data for FY 2000 is available would delay the filing until well into FY 2001.

The financial needs of the Postal Service could not be reconciled with such a delay, even if the result would be somewhat improved ratemaking data. Similarly, the potential advantages of even the more limited delay associated with waiting until complete data from FY 1999 are available do not appear to outweigh the financial consequences of such a delay.

With respect to the more general considerations associated with rate case filings, the Postal Reorganization Act allows the Postal Service to request changes in postal rates when it determines that "such changes would be in the public interest and in accordance with the policies of [the Act]." Primary among those policies are that rates be sufficient to enable the Postal Service to maintain and develop postal services of the kind and quality appropriate to the needs of the country, and that rates generate sufficient revenues to achieve financial breakeven. Postal management constantly monitors the ability of the existing rates to allow the Postal Service to achieve these objectives, both in the near term and over a reasonable forecast horizon. Management must be forward-looking because the process of changing postal rates (in an omnibus rate case) extends well in excess of a year when measured between the time the need for a change is first anticipated and the time that new rates can be implemented.

Each occasion in which a potential rate filing is contemplated requires consideration of a unique set of factors. Some factors must always be included, such as anticipated trends in postal revenues and expenses and anticipated progress towards the Postal Service's policy objectives with respect to the recovery of prior years' losses. Also important is the length of time since the previous general rate change and the magnitude of that change, both absolutely and relative to other price changes in the economy.

Other factors might be more specific to the existing circumstances, such as the existence of opportunities to reduce or defer any anticipated expenses, and the potential consequences associated with such reduction or deferral. The cash flow situation and options with respect to borrowing may also be relevant. Consideration must also be given to any conditions with the potential to cause financial results to diverge substantially (i.e., improve or deteriorate) from what is actually expected as the more likely scenario, and the levels of risk are involved.

A final factor to address would be any special circumstances that favor advancement or deferral of a general rate change. Of course, not only must all these factors be considered individually, but the results of such considerations must be balanced against each other to reach a determination that best serves the needs of the Postal Service and its customers.

(c) *How frequently does the Postal Service expect to file for omnibus rate changes? Does the Postal Service intend to file for an omnibus rate change whenever its net income is likely to be negative, no matter by how much, in any fiscal year?*

The Board of Governors decides the timing of rate change filings, balancing the various financial, operational, service, and public policy objectives of this organization. Apart from the Board's evaluation, the Postal Service has no policy that would automatically require filing for a rate increase under any specific set of circumstances.

There are two specific factors, however, which help guide decisions on the timing of rate increases. First, Resolution No. 95-9, established by the Board of Governors, requires postal management to plan for cumulative net income in each rate cycle to equal or exceed the cumulative prior years' loss recovery target for the same period, as established in the most recent rate case. Second, the Postal Service strives for rate increases at or below the rate of inflation that will provide sufficient revenues to enable the organization to maintain, improve, and develop necessary postal services.

(d) *Has the Postal Service established a policy to file for more frequent (e.g.- every other year rather than the historical pattern of approximately every three years) but smaller rate adjustments with the Postal Rate Commission?*

No. In the past, various customers have advocated that the Postal Service file for smaller increases more frequently, rather than less frequently for increases that would tend to be larger. As suggested by the response to 2(c), however, the Board's determination of when to initiate rate changes is based on its assessment of many different circumstances and a balancing of objectives, without regard to any simplistic formula.

The question assumes that "small" rate increases must be "more frequent." The new rates put in place in 1995, however, represented one of the smallest average increases up to that time, yet defied expectations in lasting four years, the longest stretch of stable prices in three decades. We continue to work towards implementing rate changes that are at or below the level of inflation and last as long as possible.

(e) *Will the Postal Service generate and make available a version of the Cost and Revenue Analysis (CRA) and Segment and Components Report for the base year using the Postal Rate Commission R97-1 costing methodologies? If not, please explain, in detail, why not.*

Yes.

(f) *Last year the Service reported that it continues to research "means for speeding up the production of reliable cost information and that it was conducting a review of the procedures used to organize data from the cost systems into the CRA." Please report on the results of your review. Have you been able to move up production of cost data? What is the earliest possible date when the CRA can be produced? With advances in automated data collection and information technology, why has the Postal Service been unable to move up production of this important information?*

The Postal Service continues to research means for speeding up the production of reliable cost data. The results of our recent review on speeding up the production of cost data were fruitful. Many timesaving and quality improving changes were made. For example, the spreadsheets that are inputs into the CRA were completely revamped, making error detection easier and making data entry into the CRA mainframe model simpler. Also, an automatic upload of much of the mainframe data was created, thereby reducing data entry and increasing data accuracy.

As we improve the production of cost data, we incorporate data from additional systems to enrich our CRA information. As a result, we have better quality data. However, as we bring additional systems into use, we must test and scrutinize these systems to ensure their quality, which takes more time.

The CRA is produced as quickly as is practical, but since it is such a very important piece of business information, it is critical that the information be as complete and accurate as possible. That is why we subject cost data to a lengthy auditing process by our external auditors and a thorough examination by postal management before it is released.

3. In his statement, the Postmaster General claims that the Service's recent "efforts will save America's ratepayers more than $2 billion." Apparently this figure is tied in some way to the delay in implementing the last omnibus rate increase (the so-called "$800 million dividend"). The Postmaster General testified last year that the Postal Service apparently overestimated the revenue requirement in the last rate case because of overly ambitious capital spending plan. In the Postmaster General's recent statement, these alleged savings are also related to the program to reduce the Service's negative equity and delaying rate implementation.

(a) *Please provide a detailed breakdown of the "more than $2 billion" figure.*

The figure represents the total savings to mailers through FY 2000 from the combination of the decision to defer implementation of the R97-1 rates and to extend the rate cycle an additional year. The delay in implementing the R97-1 rates saved mailers $350 million in FY 1998 and $450 million in FY 1999, for combined savings of $800 million. The extension of the rate cycle resulting from the delay in implementation will save mailers an additional $1.4 billion in FY 2000, bringing the total savings to $2.2 billion.

(b) *Wasn't the delay in the implementation of the last rate increase the result of the Postal Service's overestimation of its test year costs discussed by the PMG, particularly for "other programs?" Did the Postal Service really "save" anything for ratepayers?*

Yes. Originally, the Postal Service planned to increase its rates in the summer of 1998. The Postal Service's strong financial performance in FY 1998 factored into the Board of Governor's decision to delay the rate increase until January 1999. This delay "saved" postal ratepayers money that they would have had to spend several months earlier in the form of higher postage rates. The decision "cost" the Postal Service additional revenues it would have received in 1998, lowering its net income for that year by $350 million. It also required the Postal Service to implement aggressive cost containment and reduction programs in 1999 to make up for lost revenues. These actions produced additional "savings" for our customers. Additional information on reductions in "other programs" is provided in the response to Question 20(a).

(c) *Isn't this equity restoration just the result of paying down debt from operating revenue – revenue provided by ratepayers? What has the Postal Service done in this case to "save" money for the ratepayer? Is the Postal Service using the term "save" in this case with the meaning "to put aside money?"*

Equity restoration is not a synonym for paying down debt. Both prudent financial management and the federal courts distinguish between the two concepts. Use of prior year loss recovery in calculating the required revenues is part of the postal ratemaking process. Debt, on the other hand, is a means of funding losses when they are incurred.

The Postal Reorganization Act rests the fiduciary responsibility for the federal government's investment in the Postal Service with the Board of Governors. The Governors, in carrying out that trust, established a policy of restoring the equity invested in the Postal Service by the federal government. This is prudent financial policy. Any business organization needs a prudent reserve against the uncertainties of its markets and its costs. In its charge to the Governors, the PRA makes specific mention of the need to cover contingency and financing requirements such as sinking funds.

The financial performance of the Postal Service in the last five years has reduced the margin needed on revenues to restore the federal government's equity investment in the Postal Service. In addition, the dollar amount of required revenues in R97-1 needed to recover prior years' losses was substantially less than in R94-1, reversing the trend of increasing prior year loss recoveries included in postal rates. Lowering the amount of revenues for prior year loss recovery does "save" postal customers money by reducing the overall size of the rate case.

(d) *If by "save" the Postal Service means "to avoid unnecessary waste or expense" how can the Postmaster General's claim be reconciled with the fact that the Service's Total Factor Productivity has declined in 4 of the last 5 years for a cumulative decline of about 3 percent?*

In this sense, and as indicated in the answer to (a) above, "save" refers to the Postal Service's decision to delay implementation of the R97-1 rate increase and to make the rates last for an additional year beyond what was originally planned. Additionally, over time we also "save" the rate payer money by implementing process improvements and capital investment programs by increasing efficiencies. Examples are included in the answer to Question 92(d). In addition, efficiencies resulting in "savings" to the customer are not always reflected in the total factor productivity measure as explained in the answer to Question 10(a).

4. The U.S. economy has shown sustained growth over the last decade. It is said that "a rising tide lifts all boats." In his statement last year the Postmaster General characterized the Postal Service as a "very well-running ship." But, as indicated by the GAO testimony, there may be rough seas ahead. Postal Service volume trends are not encouraging. The Postal Service itself predicts that electronic diversion will seriously threaten its core business in the next decade. The Postmaster General has repeatedly warned of the threats from direct competitors including other postal administrations. Postal Service productivity has lagged behind private sector productivity despite the Service's investment in automation, undermining its stated goal to substitute capital for labor. It appears that the new labor agreements will negatively impact the Postal Service's financial performance unless there are significant gains in productivity. Indeed, in its statement, the GAO warns that the growth of the Internet, electronic communications, and electronic commerce have the potential to substantially affect the Service's volume. Consequently, the GAO feels it is imperative that the Service resolves longstanding issues in order to maximize performance, manage employees, maintain financial viability and adapt to competition.

(a) *Is management concerned that the Service's recent strong financial performance may be mainly due to the recent strength of the U.S. economy and, as a result, its employees may be lulled into a false sense of security and fail to understand that fundamental change is on the horizon?*

We believe that our string of financial and service successes have helped build employee pride, but not created unrealistic expectations. Even amidst the historic improvements of the past five years, we have continued to make it clear to employees that this organization has some tall hurdles to cross in the twenty-first century. There are undoubtedly some employees who refuse to accept the facts and may even believe that the Postal Service is "crying wolf" when it comes to the future. For the most part, however, our discussions with employees and their representatives lead us to believe that they do understand the competitive nature of the marketplace and are willing to work together to embrace change and turn potential threats into powerful opportunities for progress.

Postal management, for its part, clearly understands the cyclical nature of the economy and is working to establish a stable foundation of success. Although this organization has benefited from the strong economic environment, it is still working to control costs, improve efficiency, and identify new and steady sources of revenue. In FY 1999, for example, the Postal Service reduced costs by $800 million in response to the deferred rate case and soft revenue growth.

(b) *How do you respond to the GAO testimony? Do you agree with the GAO's warning that it is imperative that the Service resolve longstanding performance challenges in order to maintain its position in the dynamic communications and delivery environment?*

The Postal Service is like every other organization in the world that seeks to maintain a strong position in a highly competitive marketplace. It must improve every facet of its performance. It must improve productivity both through new technologies and more effective processes. It must manage its operations prudently and its costs rigorously. It must expand and strengthen its product lines to reflect changing needs and innovate to satisfy customers in entirely new ways.

The strength of our performance management system and the demonstrated capacity of postal managers and employees to respond to change gives us a fair measure of confidence in our ability to respond to fundamental shifts in the marketplace and the economy. We believe, however, that legislative reform is still needed to give us more effective tools and more flexibility to adapt to change and thrive in the new millennium. That is why we have joined with Congressman McHugh and other members of Congress in working towards the creation of a new legislative paradigm for the Postal Service.

(c) *How does the Service plan to meet each of these challenges: (1) maximize performance, (2) manage employees, (3) maintain financial viability and (4) adapt to competition.*

This question cannot be answered either simply or succinctly. Our response to each of these challenges is best summarized in our *Five Year Strategic Plan, FY 1998-2002*, mandated by the Government Performance and Results Act of 1993. The plan is in the process of being updated and a copy will be provided to the Subcommittee later this year.

5. The Postal Service forecasts that its First-Class Mail volume will decline substantially in the next decade. In addition, Standard A mail is forecast to grow at a slower rate.

(a) *Based on these forecasts what would the impact be on postal operations and postal rates? What is the Service doing to prepare for declines in its core letters and flats business?*

The Postal Service forecasts that First-Class Mail will begin to decline in real terms beginning in FY 2003 and an average of 2.5 percent from FY 2003 to FY 2008. Our analysis leads us to believe that barring economic distresses and revolutionary changes in technology that simply cannot be foreseen, overall mail volume will continue to grow over the next decade and will help compensate for the decreases in First-Class Mail volume and revenue. Given these forecasts, we feel confident that a continued focus on cost reduction, new revenue opportunities, and improved service will strengthen our product lines and enable us to hold rate increases at or below the rate of inflation over the next decade.

(b) *Recent "E-Sign" legislation introduced in the Senate and the House would facilitate and enable the use of electronic signatures by registered broker-dealers and others in the securities industry in their business dealings with customers and other transactional parties. Does the Postal Service have a forecast of how much more volume and revenue it would lose if such legislation is enacted? If so, please provide the forecast and explain how it was derived. If not, please develop your best estimate, including if appropriate, a range of values for volume and revenue loss.*

The Postal Service currently has no specific forecast for potential volume and revenue that might be lost if this legislation is passed. Much of the transaction volume in the industries affected by the legislation, however, travels outside of Postal Service mail streams. We estimate that the volume impacted by such legislation is extremely small and would not warrant a special study to determine its significance.

6. Commenting on FedEx's disappointing first quarter earnings report, some analysts related the result to the Internet effect. Some analysts said that the Internet might actually be cutting into FedEx's growth at the moment. One analyst said: "Volume trends are sluggish, and the reasons for that are still a little puzzling." He said: "Whatever incremental volume they're getting from electronic commerce that didn't move that way before ... appears to be offset and then some by what they're losing to electronic transmission of messages and computer files."

(a) *Does the Postal Service have any credible market research to indicate what the net effect of the Internet will be on its bottom line? What does this research indicate?*

The Postal Service constantly monitors market conditions and consults leading experts on electronic diversion. However, there is no consensus among the experts on what net financial impact the Internet will have on the Postal Service or even private carriers.

Nearly all analysts and industry experts believe that the growth of electronic commerce will generate significant increases in package volumes. Many believe that the complexities of on-line distribution and fulfillment will also increase the demand for logistics and related shipping services.

At the same time, the Internet is clearly being used to bypass the mail in a number of different ways. Virtually everything that can be done by mail can now be done via the Internet, from advertising to personal correspondence, from the transmission of financial data to catalog shopping. We are particularly concerned about trends in bills, statements, and remittances, and watch them closely. At present, mail retains its superior value in the eyes of the consumer. Major players in the banking sector and other industries, however, are stepping up their attempts to convert consumers to electronic payments.

The Postal Service will continue to track industry trends closely and will attempt to respond effectively to the threats and the opportunities created by the Internet and electronic commerce.

(b) *If, as at least one pundit speculates, the net impact of the Internet is negative for FedEx, wouldn't it be more so the case for the Postal Service whose volume mix is dominated by letters and documents, the very business that is most susceptible to electronic diversion?*

There is no consensus that the Internet is going to have a negative impact on the volumes of FedEx.

Analysts at Morgan Stanley Dean Witter recently stated:

> "In our view, the Internet should provide more and better access to FedEx's on-line system and stimulate more in-home buying. In addition, we believe that FedEx should benefit from the macroeconomic trends of value-added businesses and just-in-time inventories."

In September, Saloman Smith Barney also said that it believes that the Internet will gradually benefit FedEx, though admitting that the impact "over the next several years is far from completely clear." Another recent article in a computer magazine stated that "most analysts in the know say there's not enough evidence to demonstrate that e-mail has hurt shippers."

Even if it is assumed that FedEx will ultimately lose business to the Internet, one could argue that new Internet-based services would have a much greater impact on FedEx than on the Postal Service. FedEx specializes in time-sensitive letter and document delivery. A new technology that speeds delivery, or makes speedy delivery more cost-effective, will have a large impact on their business. Postal volumes, the large majority of which do not tend to be urgent, are somewhat less sensitive to these new technologies in the short run. In addition, the Postal Service's residential delivery network and low prices have helped give it a much larger share of electronic commerce package deliveries than FedEx. A survey of 1998 on-line holiday buyers indicated that the Postal Service delivered 32 percent of packages generated electronic commerce packages, while FedEx delivered 10 percent.

The Postal Service does remain concerned about the future of our bills, statements, and payments market, which we believe is vulnerable to electronic diversion over the Internet. To offset this diversion, we must continue to improve service and efficiency and take advantage of new opportunities provided by the Internet itself.

(c) *Does the Postal Service have contingency plans in the event that the growth in Internet-related revenue, such as package delivery, does not equal or exceed the loss of revenue from electronic diversion? Please discuss those plans.*

We are working to develop comprehensive, integrated business plans that allow us to adjust to forces taking place in the marketplace. In the meantime, we continue to focus on growing our business in the expedited and package delivery market; expanding our capacities in electronic commerce; growing our core products, and pursuing opportunities to boost productivity.

7. One of the Service's Voice of the Employee goals is to "have the right people in the right place with the right tools at the right time to consistently provide superior customer value and ensure commercial viability in a dynamic market." As labor costs account for nearly 80% of the Postal Service's total cost it is important to focus on how the Postal Service is managing its employee complement. Of particular concern is the number of career postal employees, the most expensive category of employee. Unlike casual and transitional employees, it is difficult and, in some cases impossible, for the Postal Service to layoff or reassign career employees. Therefore, it is important that the Postal Service carefully evaluate its short-term and long-term workforce requirements before hiring additional career employees. As workshare volume continues to grow and automation increases productivity in mail processing operations, it would seem that in order to reap the benefits of automation the Postal Service will have to hold the line on hiring career employees. Based on the Subcommittee's review of recent employment figures it appears that the Postal Service is aggressively shedding the "low hanging fruit" (i.e., casual and transitional employees) and trying to control the number of career employees relative to growth in mail volume.

(a) *Can you confirm that this is the case and will this trend continue? Do you anticipate that at some point the low hanging fruit may be gone and, as a result, you will have to implement other actions to manage labor costs?*

The Postal Service is not pursuing a deliberate strategy to reduce the number of casual and transitional employees and we do not regard these employees as "low hanging fruit" that will one day disappear. Casual and transitional workers give us needed flexibility to respond to seasonal and market-driven fluctuations in volume and will continue to play an effective role in our success.

Our approach to complement management is to anticipate and monitor changes in mail flow and to implement plans that enable us to maintain appropriate levels of service and productivity. While automation and worksharing efforts continue to move forward, mail volume also continues to grow. In recent years, we have been able to reduce complement successfully through attrition.

(b) *Can employees expect more of the same absent reform?*

See the response to Question 7(a).

(c) *Has the Postal Service initiated a hiring freeze at any organizational level?*

No.

(d) *Please discuss the nature and extent of the budget cuts associated with the Postal Service's recent cost reduction program, which the PMG described as a "life style change."*

In order to offset expected shortfalls in revenue and generate a positive net income for FY 1999 and FY 2000, postal management challenged managers across functional units to work together to create more efficient operations and reduce budgeted expenses without impacting service.

In FY 1999, the Postal Service achieved reductions of $870 million, including a reduction of $620 million at Headquarters and $250 million in the field. Of the headquarters contribution, $130 million was the result of scaling back or delaying major programs. The remaining savings were achieved by each functional area reprioritizing its activities and needs. Field managers were successful in meeting planned reductions of $250 million through local management initiatives designed to increase efficiency and reduce costs without impairing service.

In FY 2000, management reduced expenses by $1.2 billion during the budget allocation process, including reductions of $465 million in the field and $711 million at Headquarters. Due to a potential revenue shortfall again in FY 2000, current efforts are underway to remove another $400 million from Headquarters expenses. As in FY 1999, these reductions will be achieved without impacting service. In addition, VOE support funds are still incorporated in the budgets to support the Postal Service's training and safety goals.

(e) *Is the Service planning any downsizing or major restructuring of headquarters or headquarters units? If so, please discuss the timing and extent of such downsizing or restructuring and how it will be achieved.*

The Postal Service is always looking for opportunities to eliminate waste and redundancy through organizational redesign. At the present time, however, there are no plans for a major restructuring of headquarters or a headquarters unit.

8. PMG Henderson recently was quoted in the press as saying, "the Postal Service really has much less chance to survive without modernization and if we weren't around, the U.S. consumer would suffer dramatically."

(a) *Assume the Postal Reorganization Act (Title 39) is not amended and the laws that govern the Postal Service are not updated. Has the Postal Service developed any policies to minimize the impact on the U.S. consumer and taxpayer?*

In the absence of legislative reform, the Postal Service will simply have to make maximum use of the flexibility and authority it has been afforded by existing law. To meet the challenges posed by technological change and growing competition in the domestic and international arenas, the Postal Service will have to be both creative and aggressive. This will mean not only optimizing the delivery of existing products and services, but also developing new ones, both as a source of revenue and a response to market demand. Above all, however, the Postal Service will continue to have as its primary function providing universal public services that are prompt, efficient, and affordable.

9. The Postmaster General testified that for FY 1999 the Postal Service revenue was below plan by $620 million.

(a) *Please provide a detailed breakdown of the revenue variance from plan.*

Mr. Henderson's original statement was made using an estimate of our final FY 1999 revenue developed before our books were closed. The actual variance to plan is $640 million. The breakdown of revenue variance to plan is as follows, where a number in parenthesis indicates a shortfall to plan:

(in millions)

Service Option	Total
First Class	$125
Priority Mail	(279)
Standard (A)	(314)
Parcel Post	(125)
International	(63)
Other Revenue	16
Total Variance	$(640)

(b) *How much of the $620 million variance was the result of unanticipated declines in volume in response to the rate increase implemented on January 10, 1999?*

The forecast we present to the Postal Rate Commission in each rate case incorporates our best estimates of price elasticities by class of mail, and gives us an estimate of volumes after a rate change. It is impossible to determine, using these tools, how much of the variance was due to a response to the rate increase and how much was due to other factors.

10. In its testimony the GAO identified improving productivity as one of the major challenges facing the Service. The Postal Service produces a productivity measurement that takes into account all factors of production. The measurement, Total Factor Productivity (TFP), measures the changes in the relationship between outputs and the inputs or resources expended in producing those outputs. TPF provides a standardized measure indicating how well the Postal Service is performing considering the level and mix of resources it uses. A comparable measure in the private sector is Multifactor Productivity (MFP) for private nonfarm business.

    The Postal Service recognizes that it must improve its productivity to control costs and keep rates down. However, overall postal productivity has increased only 9.1 percent since postal reorganization, despite vast changes in automation and information technology. Further, productivity has declined in 4 of the past 5 years. The Service has projected that productivity will grow by 3.1 percent in fiscal year 2000, a rate that has only rarely been achieved in the past. The Service plans to reduce labor hours by 1 percent in FY 2000 while absorbing continued growth in mail volume and the size of its delivery network.

(a) *How does the Postal Service account for the fact that productivity has declined in 4 of the past 5 years and has not matched productivity gains in the private sector?*

    In recent years, the Postal Service has invested substantial sums to improve delivery service and customer satisfaction and to make infrastructure improvements. In 1998 and 1999 alone, the Postal Service committed almost $7.8 billion in capital spending. Many other service and customer satisfaction improvement efforts were charged against expenses.

    Many of these efforts have had a short-term negative impact on productivity. The Postal Service, however, believes that the service and customer satisfaction benefits were significant and worth the investment. For example, the on-time delivery of overnight First-Class Mail improved from 83 percent in FY 1994 to 94 percent in the second half of FY 1999.

    Although service quality improvement is not included in TFP, it is essential to the long-term future of the organization. Even productivity-enhancing investments such as automation often reduce TFP in the near-term, as the capital investment occurs up front, while the savings are realized over time. In addition, the Postal Service faces operational constraints and challenges that are not encountered in the private sector. It must continually invest to maintain and improve an infrastructure that includes 38,000 facilities and a fleet of more than 200,000 vehicles needed to serve every American household and business six days a week. These public service obligations constrain the Postal Service's ability to generate productivity improvements.

(b) *What measures is the Postal Service taking to improve productivity?*

Specific operational strategies have been developed for reducing work hours and expenses in FY 2000, while maintaining service at its current, high levels. The Postal Service will realize increased efficiencies from its substantial automation investments. In particular, the automatic sorting of mail into delivery sequence will increase, providing significant work hour reduction opportunities in the carrier craft. We also have plans to implement further automated sorting of non-letter shaped mail, which also creates substantial opportunities for work hour savings. Numerous other efforts are in place, both at headquarters and in the field, to identify and implement expense reductions.

(c) *How does the Service plan to achieve its ambitious goal to grow productivity by 3.1 percent in FY 2000?*

Because of the Postal Service's financial and operational success in FY 1999, the actual productivity improvement estimated needed to achieve its FY 2000 net income plan of $100 million has been reduced to 2.9 percent. It is important to understand that TFP is a measure of internal efficiency and the 2.9 percent target is the expected outcome of achieving the net income plan. The actual TFP result may differ by a few tenths of a percent.

(d) *Can this goal be achieved while maintaining the quality of mail delivery and retail services?*

Yes. Recent experience proves that it can be done. In the fourth quarter of FY 1999, the Postal Service matched a performance record by delivering 94 percent of local letters overnight, while achieving TFP of 2.3 percent. Management is committed to achieving its financial objectives without sacrificing service in the coming year.

(e) *Does the Service expect to downsize in any particular area or lay off postal employees to reduce workhours by 1 percent? Please explain how the 1 percent reduction will be allocated.*

Other than its previously announced intention to close 15 Remote Encoding Centers (RECs) by September 2000, the Postal Service has no current plans to downsize or lay off postal employees. The Postal Service is working closely with union and management associations to provide affected REC employees with employment options. The Postal Service's plans to decrease work hours will be accomplished primarily by reducing complement through attrition.

11. Recognizing that service improvement is an important component of output, the OIG has recommended that service performance be incorporated as a part of output in the calculation of total factor productivity.

(a) *What is the Postal Service's current position on this recommendation? Is the Postal Service developing such an adjustment to the TFP calculation?*

As the Inspector General noted in her report, it is essential to understand the linkages between service performance and TFP in order to make an informed evaluation of TFP performance. It is important to recognize that while TFP may have been negative in recent years, service performance has reached record levels.

As we noted in our response to the OIG's draft report, however, measuring service improvements relative to workload growth and resource usage is an extremely complex task. We have addressed this issue periodically since 1984 and most recently in 1997. At that time, we were not able to develop a statistically valid relationship between TFP and service performance to serve as the basis for an econometric model of TFP that included a service component. At the present time, the Postal Service is not developing such a measure.

12. On April 16, 1999 a contractor released a report that the Chairman requested on the quality of Postal Service data for ratemaking. The Subcommittee is concerned the Postal Service may be distracted from responding to the recommendations in the report as the managers and staff who are responsible for these data systems get bogged down in litigating the anticipated rate case. As discussed in the hearing, the Chairman is expecting a response to the GAO recommendation that the Postal Service issue a report to the Congress on actions to respond to the study recommendations and otherwise improve the quality of ratemaking data. This matter is of heightened importance in light of the upcoming rate case and the long-standing problems with the ratemaking data. It has been over four and a half years since the Chairman requested a study of the quality of ratemaking data and over six months since the contractor issued its report.

(a) *For the anticipated omnibus rate case, what improvements, if any, will be reflected in the quality of the cost, revenue and volume data used to develop rate proposals?*

The April 16 report both confirmed the adequacy of ratemaking data and provided useful suggestions on how it could be improved for both ratemaking and management purposes. Data improvements made since the Chairman's request for a study, as well as improvements recommended by the study that were anticipated before the recommendations were received, will be reflected in the next case.

The following general areas of improvement align with the study's recommendations and will be reflected in the next case.

- Evaluated and verified MODS data quality.
- Analyzed Delivery Redesign; its data will be incorporated into the next omnibus case where practical and appropriate.
- Prepared clear and complete TRACS documentation.
- Evaluated National Air and Surface System data quality pertaining to its use as a basis for TRACS samples.
- Examined institutional costs.
- Analyzed operational changes and impacts on the activities, cost pools and cost drivers currently used in the Postal Service's rate making process.
- Investigated how best to measure the effect of weight and other mail characteristics on costs.

(b) *What actions have you taken in the six months since the report has been issued to address the recommendations in the Data Quality Study Report?*

First, the work mentioned in Question 12(a) has been completed. Second, the Data Quality Study recommendations have been assigned to responsible managers, analyzed by management and staff, and placed into four action categories. For the most promising items, project goals have been incorporated in responsible managers' objectives.

(c) *When will we see improvements made to the attributable costing and revenue, pieces and weight systems?*

As part of the Postal Service's continual improvement process for rate making data, enhancements and improvements are continually made in response to new Postal Service operating conditions, new products and pricing strategies, and new information on the performance of current information systems.

(d) *What improvements can be made in the short run, the so-called "low hanging fruit," versus the recommendations for longer term improvements to the costing systems?*

The areas addressed in Question 12(a) could be considered the plucked fruit.

(e) *Does the Postal Service have a comprehensive plan that establishes goals and priorities for improving the quality of data used in rate making? If not, when will the Service develop such a plan?*

Yes. This information has been provided in the Postmaster General's letter to Chairman McHugh, dated December 17, 1999.

(f) *For the record, does the Postal Service agree with the study's conclusion that improvements and enhancements can—and must—be made to ensure future data provided for rate making will be sufficiently complete and accurate?*

The Postal Service has always agreed that data must be continually evaluated and enhancements, where possible, should and will be made to ensure high quality rate making data. For example, the Postal Service has made enhancements to its data systems independently from the Data Quality Study.

Some Data Quality Study recommendations were initiated by the Postal Service in advance of receiving the Study's conclusions. Other Data Quality Study recommendations, where called for and possible, will be implemented in time for future rate proceedings.

13. In regard to the Docket No. R97-1 omnibus rate case, the Postal Rate Commission (PRC) and the D.C. Circuit Court confronted the issue of inconsistencies in mail identification between the Revenue, Pieces and Weight System and the In-Office Cost System. In its Opinion and Recommended Decision, the PRC elected to make a conservative adjustment to attributable cost and the court affirmed. The Postal Service provided rebuttal evidence in Docket No. 97-1 but survey design flaws made it impossible for the PRC to know the exact amount of mismatching that occurred.

(a) *What, if anything, is the Postal Service doing to fix this and related problems? Will these fixes be in place for the next omnibus rate filing?*

It is the position of the Postal Service, as it was in Docket No. R97-1, that no adjustment to reported costs is warranted on the basis of the alleged "mismatch" problem. This alleged problem relates to the fact that, from time to time, mail that nonprofit mailers intended to submit at the nonprofit rates ended up being charged the regular rates instead. This might result, for example, when nonprofit organizations presented mailings that failed to comply with the statutory restrictions on the content of nonprofit mail pieces.

Although ultimately charging regular rates, the Postal Service, at the request of the nonprofit mailer, may have allowed the mail in question to enter the mail stream bearing the markings of nonprofit mail. Consequently, if data collectors sampled this mail downstream, they would have recorded their observations regarding such mail as if it were nonprofit mail. These circumstances created the possibility of a mismatch, to the extent that the revenues for such pieces were credited to regular rate mail, but the costs associated with such pieces when sampled were charged to nonprofit mail.

The Postal Service does not dispute that, in theory, the potential for this type of mismatch exists. What the Postal Service does dispute, however, is that the magnitude of this problem in actuality is sufficient to call into question the reported costs for nonprofit mail. (Recall that while the same potential problem existed in Docket No. R94-1, the nonprofit mailers did not see fit to question the reported cost data on that basis, when the reported data suggested the need for a nonprofit rate adjustment that was substantially below average.)

The key point to bear in mind is that all reported costs are estimates, and the nature of estimation requires an acknowledgement that no estimation process can reasonably be expected to be perfect. Given any cost estimation system as large and extensive as that of the Postal Service, which attempts to allocate costs among roughly 200 billion pieces of mail, the presence of a limited amount of statistical "noise" and random error is inevitable.

The above "mismatch" scenario is but one in a virtually unlimited number of hypothetical ways in which data collectors could fail either to identify accurately or to record accurately the appropriate subclass of a mailpiece. It is not the hypothetical possibility of these types of errors which creates concern, but only reliable indications of their actual occurrence with substantial and material regularity.

Thus, when this matter first surfaced in Docket No. 97-1, it was the initial judgment of knowledgeable postal personnel that the potential scale of the "mismatch" problem, in terms of material effects on reported costs, was quite small. Later during that proceeding, this judgment was supported by empirical analysis presented as rebuttal testimony. That analysis suggested that only a miniscule fraction of nonprofit mail could legitimately be viewed as candidate mail to fit the "mismatch" scenario, a fraction much too small to allow the "mismatch" theory to constitute a valid basis to question reported costs.

While the Postal Rate Commission questioned the accuracy of this analysis, it must be recalled that the Commission's response arose in the context of what were characterized as abnormal and unexplained increases in the reported costs of nonprofit mail in FY 1996. No such increases were reported in either FY 1997 or FY 1998. Therefore, no apparent need exists to adjust nonprofit costs for use in a rate case in response to the so-called "mismatch" problem.

14. It would appear that the problem of inconsistencies in mail identification would equally affect the other cost systems including but not limited to the City Carrier Cost System, the Rural Carrier Cost System and the Transportation Cost System.

(a) *For each of these cost systems and all other supporting cost systems and cost studies please provide a description of how the Postal Service intends to adjust the attributable costs to correct for misidentification problems.*

Please see the response to 13(a) for an explanation of why the Postal Service believes that no adjustment in any of the costing systems is warranted with respect to the so-called "mismatch" problem.

15. As the RPW system relies increasingly on mailing statements, mail markings have become increasingly unnecessary as a means of mail identification. On the other hand, the costing systems have not been fundamentally changed and still depend heavily on mail markings. Mailers have found mail marking requirements to be burdensome and costly. From a business standpoint it would make sense for the Postal Service to wean itself away from such reliance on mail markings and abolish or lessen these requirements.

(a) *Has the Postal Service considered adjusting its costing methodologies so as to eliminate the need for mail markings? Please discuss.*

Mail markings serve four primary purposes. First, they reinforce postal marketing and advertising strategies and brands, e.g., Priority Mail, Express Mail, etc. Second, they facilitate revenue protection efforts. Third, they allow appropriate mail processing and delivery priorities to be established. And fourth, they allow mail categories to be identified in the revenue, volume, and cost systems.

Numerous technologies are being developed that may ultimately reduce the reliance of costing on mail markings. Included among these are Planet codes, information rich barcodes, and information-based indicia. However, until these technologies are adopted by most mailers or used on an overwhelming majority of the mail, accurate costing methods will need to continue to rely on markings. Furthermore, even though RPW increasingly relies upon mailing statement data, it still depends on mail markings to allow data collectors to distinguish between categories whose estimates are obtained from mailing statement data and categories whose estimates are based on their observations.

(b) *What other purpose(s) besides ratemaking do individual piece mail markings serve in the processing and delivery of mail?*

See response to Question 15(a) above.

16. The Postal Service proposed but the PRC rejected a mail processing cost model in Docket No. R97-1.

(a) *Does the Postal Service intend to submit a corrected version of this model in the future or will it adopt the 100% volume variability estimate used by the PRC? Please explain why or why not.*

The Data Quality Study report requested by the Chairman and released on April 16, 1999, included the following observation on page 40:

> The Docket No. R94-1 assumption of 100% volume variable for mail processing costs can be traced to Docket No. R71-1 documentation that is based on an analysis of 1953 to 1969 manual operations data. It is more accurate to actively measure and calculate these elasticities than to continue to assume a 100% variability factor for all mail processing activities.

Even the Commission, while claiming to find inadequate support for the variability analysis presented by the Postal Service on the record in Docket No. R97-1, noted that "the Service's presentation advanced the state of knowledge," and further stated that the Commission "hopes and expects the Service and the parties to continue to explore this important area." (PRC Opinion and Recommended Decision, Docket No. R97-1 at iv.)

In the next rate case, the Postal Service hopes to be able to be responsive to these views as expressed in the Data Quality Study report and in the Commission's Opinion. Additionally, it perhaps bears noting that any further analysis addressing the concerns raised by the Commission has the potential to corroborate the original results, rather than suggest that those results in some fashion need to be "corrected," as implied by the question.

17. We understand the Postal Service is pilot testing an ABC standard costing system.

(a) *Please report on the results of the Postal Service's efforts to implement an ABC standard costing system.*

An Activity-Based Costing Model was completed for the Nashville, Tennessee, Processing and Distribution Plant in June 1999. Reports have been run for FY 1999. Process Action Teams are being formed to act upon areas of opportunity identified from the information. As we go to other sites in the year 2000, we will be able to compare activity costs across facilities and work on best practices.

(b) *Are these efforts primarily focused on cost management or improving the quality of data for ratemaking?*

The focus of our current efforts is on cost management. We have extensive data systems that collect data on a macro or national level. However, useful information for managing operations at a local level is more limited. Eventually, the data we are obtaining in our ABC model might be useful for some ratemaking purposes. This conclusion would have to be carefully evaluated.

(c) *How, if at all, can ABC standard costing support ratemaking which requires nationally representative estimates of cost for numerous classes, subclasses and rate categories?*

The current model would have to be modified for ratemaking purposes since it does not provide product costs along the rate categories. The suitability of any data used to allocate costs and design rates would have to be carefully evaluated and consistent with accepted principles of cost causation.

18. The original FY 1998 RPW estimates of parcel post revenues were greatly understated. Parcel Post revenues were understated by over 15%. The estimates have since been revised.

(a) *Please provide a full explanation as to why these figures were underestimated and explain how the figures were corrected.*

The most probable reason is that data collectors did not sample small permit imprint Parcel Post items. Upon seeing the permit imprint indicia, they incorrectly assumed the item was Standard Mail (A). In RPW sampling, permit imprint Standard Mail (A) is not counted.

Another contributing factor was the existence of a "Bulk Mail" marking on Parcel Post. This marking indicates that the parcel's postage has been paid by a special method involving weight averaging. Data collectors could have interpreted the "Bulk Mail" marking as "Bulk Rate", which is a Standard Mail (A) marking, and concluded the item was Standard Mail (A).

Finally, the shift to using mailing statement data for permit imprint Parcel Post estimates corresponded to our long-run plan to use, where possible, census-type estimates for RPW reporting, instead of sample estimates.

With respect to the correction of the figures in the official RPW report, use of the underestimated Domestic RPW sample data for the report was discontinued in Quarter 1, FY 1999. These data were replaced with data from mailing statements at that time.

(b) *Has the Postal Service corrected its data collection and/or estimation procedures to correct this problem in FY 1999 and in future reports?*

Yes.

(c) *Has the Postal Service reviewed its estimation procedure to determine whether a similar problem exists for all other classes, subclasses and rate categories of mail?*

Yes. We found that no similar problems exist in other categories of mail.

19. The OIG and the Inspection Service jointly conducted an audit of the Postal Service economic analysis and forecasting process. The audit found that there were differences between the actual performance and the revenue and cost projections, which may impair planning for growth, marketing and implementation of projects. In addition, the Subcommittee has particular concern for the accuracy of the forecast as it relates to the revenue requirement in rate cases. The OIG recommended that the CFO and Senior Vice President: (i) continue management meetings with other key stakeholders to discuss factors affecting the market environment, (ii) forecast to track short-term changes, (iii) reduce contracting cost through the use of internal resources, and (iv) benchmark the process to identify and implement best practices.

(a) *Please discuss, if and how, the Postal Service has implemented each of these recommendations to improve the economic analysis and forecasting.*

We now have in place a definite schedule of meetings between Forecasting, Marketing, Expedited and Package Services, and the International Business Unit. These meetings encompass a review of commercial and retail revenues, RPW reports, and budget and econometric reports compared to actual performance and outlook.

We continue to produce quarterly revenue and volume forecasts by mail class and subclass. Each quarter, we update these forecasts to take account of changes in the market, postal rates, and economic conditions.

The Postal Service now relies more extensively on staff and internal resources in completing the forecasts. Nearly all internal forecasts use the econometric forecast as a baseline.

The WEFA consulting group has presented a report to the Postal Service titled "Forecasting Best Practices: Re-Engineering the Passive Process into an Active Management Tool." Marketing and Finance are reviewing the report for specific practices that can be adopted by the Postal Service.

(b) *Will these improvements be in place for the next omnibus rate request?*

The econometric forecast is a continually evolving tool. We have implemented most of the OIG's recommendation into our forecasting process, and we continue to refine and enhance that process when new data, methodologies, and practices add value.

20. In the 1997 omnibus rate case the expenses estimated by the Postal Service for "other programs" for FY 1998 exceeded the prior year expense by over $2.5 billion. This engendered much angst among intervenors because this expense in large part drove the need for a rate increase. It became evident at the close of the case that the Postal Service was not going to require this level of funding for "other programs" in FY 1998.

(a) *Please provide for the record a table indicating the actual and projected FY 1998 cost for each of the programs in the "other programs" category.*

As indicated in the above statement, the $2.5 billion was estimated incremental expense growth. This was the sum of incremental growth in various expense categories estimated for FY 1998 over FY 1997 costs. "Other programs" includes costs reflected in specific programs initiated by management. Also included in the "other programs" category are changes in expenses not directly linked to operations, such as interest, depreciation and centrally budgeted personnel costs such as annuitant costs and workers' compensation.

In some respects, Postal Service accounting records reflecting actual operating results do not coincide perfectly with the categories used for estimating expenses in the rate case. In the rate filing, "other program" costs are estimated by cost segment and component. Although a trial balance is produced at the end of the year that provides cost segment data by account number, in most cases, cost segment and component data are not available by program or expense item as included under "other programs." In addition there are hundreds of programs included in this category. Included were several major programs that accounted for a significant portion of the increase in this category. They are listed below:

FY 1998 ($ Millions)	Actual	Projected	Variance
Priority Mail Redesign	289.9	301.3	-11.4
Delivery Confirmation	36.9	175.6	-138.7
MTE Service Center Program	16.8	87.8	-71.0
Associate Office Infrastructure	81.3	124.2	-42.9
Corporate Call Management	84.2	137.0	-52.8
Point of Service	29.5	89.5	-60.0
Stamp Programs	217.0	310.2	-93.2
Year 2000	91.2	255.3	-164.1
Total	846.8	1,480.9	-634.1

Reasons for these results vary by specific program or item. Examples of several of the major programs are listed below.

- Delivery Confirmation – Field deployment was delayed over three months because the scanner contractor was not able to pass acceptance testing. Additionally, the contractor did provide scanners at a cost less than their original estimates due to enhancements in technology.
- Mail Transport Equipment (MTE) Service Center Program – This program was delayed approximately five months due to ongoing discussions with the American Postal Workers Union and the National Postal Mail Handlers Union regarding outsourcing. Only four of the 22 sites were brought on line. In addition to the labor issues, protests were received from warehouse contractors over pre-qualification issues and sole source awards.
- Associate Office Infrastructure – Performance of the Managed Network Service provided by the contractor under this project was initially inferior and caused delays in equipment installation.

Other delays were caused in some cases by complexity of software and deployment. In other cases, the internal approval process took longer than originally anticipated.

The R-97-1 rate case was founded substantially on the need for funds for important strategic investments like Delivery Confirmation, Corporate Call Centers and MTE Service Centers, not only for FY 1998, but also for the entire rate cycle and for the more distant future as well. What appears on the surface as merely expenses being less than estimates in the hypothetical test year in most cases is the result of program delays. These delays shifted investment from FY 1998 to FY 1999 when the new rates took effect. The decision to postpone implementation of new rates until January 10, 1999, a full quarter after the test year ended, more than offset the temporary underrun of expenses caused by unforeseen program delays in the test year.

(b) *Has the Postal Service initiated efforts to improve the estimation of program costs to prevent an overstated revenue requirement in the next rate filing?*

Yes. We have heightened the awareness of program managers for the accuracy of their estimates, especially as they pertain to a rate filing.

21. As promised in the oversight hearing, please provide the following information for the record.

(a) *As requested by Mr. Davis, please discuss the Postal Service's views on targeting advertising dollars to minority communities and minority vendors. In addition, please provide a report on how procurement practices were adjusted and what changes have occurred to involve more minority businesses in purchasing.*

The Postal Service's general market media plan reaches a large portion of the multi-cultural segments. However, in cases where the general market plan under delivers against minority targets—or in cases where language barriers exist—the plan is supplemented with specific multi-cultural messaging. For example, we air Hispanic language commercials in targeted media such as *Univision TV* network promoting Priority Mail during key sales periods throughout the year.

Our advertising contract requires our lead media agency to undertake all media planning and buying activities for both general and ethnic markets and, in all cases, minority-owned suppliers are to be given equal consideration. Regarding ethnic targeted initiatives specifically, the agency has the opportunity to source minority-owned suppliers for both production and broadcast requirements.

Our record on supplier diversity, historically, is a good one. Over the past several years, we have ranked as a clear leader in doing business with small and woman-owned firms when compared to government agencies and the private sector. We fall in the mid-range with minority owned businesses. We regularly compare our performance to both public and private sector organizations.

Our preliminary results for FY 1999 continue that pattern. In direct contracting, we awarded over 5,888 contracts worth more than $363 million to minority firms, not counting credit card transactions. We awarded 6,598 contracts worth about $446 million to woman-owned firms, and small businesses won over 42,500 contracts for more than $4 billion, more than 47 percent of our total dollars spent. These figures, which do not include credit card transactions, reflect overall improvement over last year, both in terms of absolute gains and percentage of the whole.

Despite this progress, we are working to improve our focus, our capabilities, and our results. We are committed to remaining a leader in supplier diversity. Over the past two years, we have taken a number of steps to increase our focus on supplier diversity and to broaden it to all of our buying activities. The following are examples of these efforts:

- We completed and issued the "Supplier Diversity – Statement of Commitment" which was widely distributed internally and is available to suppliers on the Internet.

- We revised and reissued the Supplier Diversity Plan (SDP) to apply not only to our major purchasing organizations, but also to all postal buying activities. It includes the Supplier Diversity Statement of Commitment and begins with an open letter, jointly signed by the Postmaster General, the Chief Operating Officer, and the Deputy Postmaster General, that emphasizes a top-down, organizational-wide commitment. The plan was circulated to all officers, to managers in Purchasing and Materials, Facilities, Transportation, and Diversity Development departments, and others as appropriate. It is also available on the Postal Service Intranet. The plan embodies aggressive, year-to-year "continuous improvement" targets through the 5-year planning period.

- The Plan also established annual requirements that all buyers receive a level of training in supplier diversity/cultural diversity. In FY 1999, virtually all buyers received that training.

- In order to promote opportunities for small, minority, and woman-owned businesses to participate in our large contracting arena, we revised our subcontracting policy to require large contractors to submit subcontracting plans as part of their proposals, and are calling for periodic reports on small, minority, and woman-owned business usage. All told, we have clarified and broadened our policy, strengthened our focus on implementation, and improved our communication to both purchasing professionals and the supplier community of the types of data we seek to capture and assess.

- Guidelines have been issued to local buyers and credit card holders to promote consideration of small, minority, and woman-owned businesses. These include revisions to the *Administrative Services Manual* which were completed and published in *Postal Bulletin* 21974 in June 1998. Additionally, our handbook *Credit Card Policies and Procedures for Local Buying* was updated and reissued to emphasize our policy and focus on supplier diversity. The new handbook took effect in November 1998.

- We distribute a quarterly report on credit card transactions to enable major organizations to track and monitor their performance against small, minority, and woman-owned business goals. A credit card training video was also being updated to emphasize our focus on supplier diversity and encourage the use of credit cards for buys from minority and woman-owned firms.

- We require that all purchasing plans include a discussion of sourcing efforts targeted at identifying small, minority, and woman-owned firms.

- We believe that open communication with the supplier community is a critical component, and we consequently adopted the Postal Service web site as an important tool. We use the external web site extensively to communicate with suppliers, and we use the internal site to communicate with our procurement professionals. The external site puts a broad range of material at the suppliers' fingertips, and provides interactive linkages. For example, we provide a listing of buying locations, products and services bought from these locations, maps, telephone numbers, FAX numbers, and an e-mail hot-link to the supplier diversity coordinator at each site. This responds to the need most often cited by small, minority, and woman-owned suppliers.

- We have an interactive supplier registration vehicle called SADI (Supplier Automated Database on the Internet). Currently, over 3,500 suppliers have registered. SADI gives buyers on-line access to prospective suppliers. We are actively working to increase the numbers of registrants.

- We also initiated deployment BOB (Business Opportunities Bulletin Board), a web-based means of publicizing upcoming procurements, subcontracting opportunities, news and events, etc. Suppliers can download the RFPs, data packages, etc., which have been enhanced and added to a range of other Internet-based communications, including an open letter to suppliers, a listing of Frequently Asked Questions (FAQs), and downloadable documents like *Let's Do Business*, etc.

- On the internal web site, we have deployed a listing of "proven" minority and women-based suppliers on the Intranet and have provided a brief tutorial to help buyers use the Internet to help identify potential sources.

(b) *As requested by Mr. Owens, please provide the Customer Satisfaction Index scores broken down by districts and major metropolitan areas.*

See Attachment 1.

(c) *As requested by Mr. LaTourette, please explain how, if at all, does the Postal Service educate or work with mailers regarding any potential conflicts between Postal Service regulations and relevant state laws.*

The Postal Service provides trained customer service representatives to help mailers ensure that their promotional materials meet applicable federal postal laws and regulations. While these representatives are proficient at providing customers with guidance pertaining to federal requirements, they cannot help them sift through the laws and regulations of the 50 states, the District of Columbia, and the territories.

As a general matter, when the Postal Service becomes aware of a conflict between a federal and state law or regulation that potentially could affect the operation of the national postal system, it works with the appropriate officials to resolve the issue.

(d) *As requested by Mr. Sanford, please provide the Postal Service's rationale for canceling the plan to build a facility at the old Air Force Base in Myrtle Beach, South Carolina. As promised, has the Postal Service issued a press release regarding the cancellation of this plan? Please provide a copy for the record.*

A press release has been prepared. A copy is attached (Attachment 2). It explai the rationale for reassessing the plan to build a facility at the former Air Force Bas in Myrtle Beach. In addition, at the request of Representative Sanford, postal officials met with the Congressman and local leaders on December 17 to discuss this issue. We indicated at the meeting that recent improvements in service in the area, along with more stringent national financial restraints, have placed the proje on hold and subject to further review at the national level. A more definitive statu will be announced in the coming months.

22. An arbitration agreement was recently announced between the Postal Service and the National Association of Letter Carriers (NALC). The NALC had been without a labor contract since November 20, 1998. The contract had been in binding arbitration since last spring. An arbitration agreement was announced on September 20, 1999, which includes a three-year contract with wage and health benefit increases for 240,000 letter carriers. The contract covers the period from November 20, 1998, when the former agreement expired, through November 20, 2001. It includes general wage increases of up to 2 percent plus cost-of-living adjustments, and an increase in the Postal Service's share of health benefit contributions. These increases have been characterized in the press as "substantial."

(a) *Is the pay increase for the letter carriers retroactive? How will the Postal Service treat this payment in its FY 1999 financial statements?*

For the first year of the NALC contract, most carriers will receive a lump-sum payment in lieu of a retroactive pay adjustment. However, employees who are eligible to retire by November 20, 2002, will receive a retroactive pay adjustment. Lump-sum payments and retroactive pay adjustments are accrued on a pro-rata basis between FY 1999 and FY 2000. For FY 1999, about $226 million was expensed for these payments.

(b) *What does this increase do to net income for FY 1999 and projections for FY 2000 and FY 2001?*

The economics for the first two years of the interest arbitration decision, FY 1999 and FY 2000, are virtually identical to those negotiated between the Postal Service and the American Postal Workers' Union (APWU) and the National Postal Mail Handlers Union (NPMHU) at the end of 1998. Therefore, compared to our baseline forecast, expenses are $8 million higher in FY 1999, but $28 million lower in FY 2000. These small variances are attributable to the fact that some employees will be receiving lump-sum payments in lieu of retroactive pay adjustments.

In FY 2001, the full impact of the interest arbitration decision will be felt. This impact includes not only the salary upgrade, but also a 1.2 percent general increase plus two COLA payments. Such payments will add over $370 million to our baseline expense forecast in FY 2001.

(c) *How will this and the agreements with the clerks, mailhandlers and rural carriers impact the timing and extent of the next omnibus rate increase?*

Additional costs resulting from these labor agreements, as outlined above, have been factored into the omnibus rate case sent to the Postal Rate Commission in January. The Postal Service has committed to maintaining the current level of postage rates until at least January 2001.

(d) *How do you respond to the characterization of the award as "substantial"? In your view, why was the Postal Service unable to reach a negotiated settlement with the NALC? What were the main issues that divided the parties?*

Excluding the salary upgrade, the arbitration award does not provide "substantial" salary increases. As previously mentioned, the salary increases for the first two years of the award are identical to those negotiated with the APWU and the NPMHU. In the third year, the award provides for a 1.2 percent general increase and two COLA payments. While not substantial, this award continues the COLA formula for city letter carriers during a time when COLA provisions are diminishing.

However, the salary upgrade (approximately a 2.9 percent wage increase) is substantial. The salary upgrade and the general increase will raise letter carrier wages by 4.1 percent on November 18, 2000. There has been no increase of this magnitude in more than two decades. In that context, the upgrade results in a substantial wage increase.

It is not surprising that the Postal Service and the NALC were unable to reach a negotiated agreement in November 1998 because the main issue dividing the parties was the union's insistence on a salary upgrade for over 240,000 employees. It should be noted that the 1984, 1990, and 1994 contracts were not negotiated either.

(e) *Are there any concessions in the agreement that will facilitate management's goal to increase productivity in delivery operations? Such concessions might include, for example, changes in work rules and other initiatives under the delivery redesign program. In other words, are there new opportunities under the new agreement to pay for the wage increases through productivity gains?*

The interest arbitration decision contains no concessions on the part of the NALC that will facilitate management's goal to increase productivity.

23. The NALC arbitration agreement upgrades letter carriers to a higher pay grade that will increase salaries by about 3 percent in the third year (FY 2001) of the contract. The American Postal Workers' Union (APWU) current contract will expire two days after carriers are to be upgraded from grade 5 to grade 6. The President of the APWU recently issued a statement indicating the APWU will settle for nothing less than full parity with the NALC in its contract. The Postal Service Senior Vice President, Operations, said: "It is unfortunate that parity was not maintained with the negotiated agreements reached earlier with the American Postal Workers' Union, AFL-CIO, and the National Postal Mail Handlers Union, AFL-CIO."

(a) *Does the movement of carriers to a higher pay grade create a challenging precedent in the Postal Service's efforts to control costs?*

The movement of carriers to a higher pay grade creates a challenging set of circumstances in the Postal Service's efforts to control costs. As stated earlier, the salary upgrade, general increase, and COLAs will add more than $370 million to our baseline expense forecast in FY 2001.

(b) *How will the Postal Service address the APWU demand that they too should be paid at a higher pay grade in their next round of negotiations for a new contract in FY 2001?*

The Postal Service is a firm believer in free and good faith collective bargaining. We will approach 2000 national negotiations with the APWU as well as with the NPMHU with that in mind. Although we are mindful of Mr. Biller's comments concerning the Fleischli Award, we note that Arbitrator Fleischli determined that the outside work of city letter carriers had become more difficult, from a physical and mental standpoint, especially in the last several years due to the advent of automation and other work method changes. We do not believe that the same can be said of inside APWU or Mail Handlers work. We also believe that the Postal Reorganization Act, which created the principle of wage comparability, is still the standard by which to measure employee compensation. We will again look to the private sector to determine whether employees represented by the APWU and the NPMHU are fairly compensated.

(c) *Does the Postal Service expect that the mailhandlers and rural carriers will demand upgrading to higher level pay as well?*

Yes, the NRLCA advanced such a demand in the 1999 round of collective bargaining, and we expect the NPMHU to do likewise in the 2000 national negotiations.

24. In his Opinion in the 1999 Interest Arbitration, the Chairman of the Panel noted:

> By the time the award in this case is implemented, there will be little more than two years left to apply its terms. While the length of the agreement may put negotiation with the NALC "out of sync" with the negotiations with the APWU and Mail Handlers, that ought not prevent the USPS from continuing to pursue its goal of negotiating identical and moderate wage increases with its major unions. (Emphasis added.)

(a) *How does the Postal Service interpret the Chairman's characterization of the Postal Service's goal in labor negotiation as negotiating identical wage increases with its major unions?*

In the context of the third year of the NALC award, "identical and moderate wage increases" are not compatible. It is clear that the third year does not result in moderate wage increases. We certainly don't interpret Arbitrator Fleischli's statement to mean that the other unions should receive the salary upgrade. Absent this upgrade, however, we note that the 1.2 percent general increase and COLA payments in the third year are in fact identical to the second and fourth years of the Stark, Clarke, and Vaughn interest arbitration awards in 1995 and 1996. However, as stated previously, the Postal Service must look to the private sector to determine its wage strategies. Of particular interest is the Employment Cost Index, which measures wage and benefit growth in the private sector. We continue to define moderate restraint as postal wage growth equal to the ECI-1 percent per year.

(b) *Is the Postal Service concerned that this language is inappropriate and may prejudice its negotiations with other unions?*

Based on APWU President Biller's comments, there is no question that our other major unions will be attempting to interpret and apply the language in the Fleischli Award to the employees represented by such unions.

25. About 5 years ago, GAO recommended that the Service and its unions and management associations establish a framework agreement that could serve as a basis for helping to improve the sometimes contentious relationships that existed. To date, no such agreement has been established. However, in recent weeks, the Clinton administration has focused more attention on the implementation of executive order 12871, which involves labor-management partnerships. The order, which was established in 1993, called for federal executive agencies to, among other things, (1) create such partnerships by forming labor-management councils and (2) involve employees and unions with agency managers in identifying problems and crafting solutions to better serve agencies' missions and customers.

(a) *To what extent do such councils exist in the Postal Service? How effective have they been in helping to address persistent labor-management relations problems that have plagued the Service for several years?*

While we do not keep an exact count on the number of local labor-management councils, we believe there are at least 250 in the Postal Service.

Our various collective bargaining agreements provide for the establishment and regular meetings of Joint Labor-Management Committees in all installations. To ensure that this valuable source of communications is actively pursued in our field installations, a letter from the Vice President, Labor Relations, was sent to the field in March of 1999 emphasizing the importance of regular meetings with the unions.

Local Joint Labor-Management Committees, meeting regularly, provide a forum for our member unions to surface employee concerns for definition, discussion, and resolution before a concern becomes a dispute.

(b) *In recent years, to what extent do you believe that the Postal Service has made progress in attempting to involve employees and union and management association representatives as full partners with postal managers in identifying problems and crafting solutions? If you believe that progress has been made, to what do you attribute the achievement of such progress?*

The Postal Service has completed with the NALC, and is in the process of finalizing with the APWU and NPMHU, the development of a joint contract interpretation manual. These manuals, as we have learned with the USPS-NALC Joint Contract Administration Manual (JCAM), serve to address and alleviate many local workplace stresses. The NALC JCAM, distributed to all delivery units nationwide, has reduced the number of grievances filed and has increased the number of dispute resolutions at the local level. We attribute the progress in this area to a mutual realization with the unions that employees and managers at the local level are capable of addressing and resolving most disputes given the proper training and information.

Through the Labor Summit, the National Leadership Team, and local labor-management councils, the Postal Service continues to discuss issues of concern with its employee representatives. We believe that the dialogues taking place through these channels are contributing to our ability to identify and resolve problems and challenges together. While progress is difficult to measure, we believe that we are moving steadily forward towards a greater partnership with our unions and management associations. The number of new initiatives, from revised grievance-arbitration procedures to the new Joint Contract Interpretation Manual, is a sign of this progress.

(c) *Within the Service's organization, does the National Leadership Team, whose membership included not only high-level postal managers but also representatives of postal labor unions and management associations, still exist? If so, to what extent do you believe that the National Leadership Team has proved effective in helping to establish a meaningful working partnership among postal managers and the representatives of labor unions and management associations? How has the National Leadership Team communicated the importance of establishing and maintaining effective labor-management partnerships to other postal offices and facilities, particularly field locations?*

The National Leadership team was developed by former Postmaster General Marvin Runyon to engage the unions and management associations in a dialogue on the strategic focus for success of the Postal Service. The National Leadership Team continues its important work. Meeting each quarter, the National Leadership Team consists of both Postal Service, union, and management association decision-makers.

The dialogue in the meetings has often emphasized employee issues and has served to reinforce the Postal Service goal of improving the working environment. The Postal Service's commitment to this goal is reflected in the creation of measurable targets for improving the working environment. Improvement target scores on the Voice of the Employee (VOE) surveys have been made compensible measures for non-bargaining unit employees by Performance Cluster.

Postal executives, including the Postmaster General, also communicate the importance of positive labor-management relationships in speeches to executives and employee groups.

26. In November 1999, the contract for the National Rural Letter Carriers' Association (NRLCA) is due to expire. In past years, NRLCA has generally been able to achieve negotiated settlements with the Postal Service.

(a) *Thus far, have any issues arisen that may cause or appear to be causing an impasse in the negotiations between the Postal Service and NRLCA? If so, what do these issues involve? Does the Postal Service have any reason to believe that the current contract negotiations with NRLCA will not result in a negotiated settlement? Please explain.*

The 1995 Agreement with the NRLCA expired on November 20, 1999. Unfortunately, the parties were not able to reach a negotiated agreement by November 20, and the parties are currently at impasse. It is a virtual certainty that the failure of the parties to reach an agreement was caused by the Fleischli interest arbitration Award. The NRLCA made it clear in negotiations that rural carriers were entitled to an upgrade. Although the Postal Service is hopeful of still achieving an agreement with the NRLCA, we are prepared to go forward with the dispute resolution process.

27. In recent years, the Postal Service has reached agreements with the American Postal Workers' Union and the National Association of Letter Carriers to establish pilot tests that could help reduce the significant backlogs of employee grievances and improve the grievance process.

(a) *Does the Postal Service have any similar tests ongoing with NRLCA? If so, please describe the tests and provide an update on their results thus far.*

The Postal Service does not have any similar tests ongoing with the NRLCA with regard to employee grievances. Because there are significantly fewer grievances received from the NRLCA, the backlog of grievances is minimal.

(b) *Does the Postal Service currently have any other types of agreements with NRLCA to pilot test revisions to other postal work-related procedures? If so, please describe the agreements and the results of the tests thus far.*

The Postal Service does not have any agreements with the NRLCA for pilot testing of work rules. The parties have recently reached impasse in the 1999 collective bargaining session. However, the Postal Service is hopeful that the parties will continue to discuss several important issues, such as relief days for regular rural carriers and leave replacement issues, and reach agreement on new and innovative ways to approach this that will benefit both parties.

28. Last year the Postal Service reported that it was exploring a number of different options in the area of pay-for-performance for bargaining unit employees.

(a) *What is the status of this effort? Are there any pay-for-performance plans for bargaining unit employees under serious consideration?*

During the 1998 national negotiations, the Postal Service proposed to the APWU, the NALC, and the NPMHU that the current pay system should be modified to include variable pay provisions that would reward performance and recognize employee contributions to the Postal Service. None of the three unions was interested in such a pay system, and there are no future plans for pay-for-performance for bargaining unit employees. Our postal unions have made it clear to us that they do not want to substitute guaranteed general increases and COLA payments for uncertain lump-sum payments that do not become part of an employee's basic salary.

29. The Subcommittee is frequently contacted by postal employees regarding employee and labor-management problems within the Service. There are allegations of hostile working environments and the potential for violence. The Subcommittee places the highest priority on improvement in workplace relations. The Chairman's concern about the working environment and the potential for violence has been long-standing.

(a) *Given the Postmaster General's statement last year at our June 10th oversight hearing that labor-management issues would be his top priority, what has been done by the Postal Service to address these problems?*

After a successful period of testing, the Postal Service fully implemented REDRESS$_{TM}$, an EEO mediation program. The success of the REDRESS$_{TM}$ is reflected by the fact that, during FY 1999, the Postal Service mediated nearly 9,000 EEO disputes and closed 81 percent of those cases.

In addition to implementing REDRESS$_{TM}$, the Postal Service made a significant investment in workplace improvement with the establishment of the National Workplace Environment Improvement (WEI) office. The creation of this office brought together the Employee Assistance Program and the crisis management and threat assessment efforts under the leadership and coordination of one office. This new office provided the focus on employee issues that is necessary to improving working environments.

(b) *Please describe the responsibilities of the National Workplace Environment Improvement Office.*

The function was created to:

- Assess and integrate employee feedback information.
- Catalog and evaluate a broad array of workplace improvement initiatives and practices for use within USPS.
- Assist the field in establishing and addressing workplace improvement priorities, including recommending tools, resources and indicators of results.
- Ensure effective communications on workplace issues.

Since its inception, the office has accomplished:

- Improvement of the "troubled worksite" process by implementation of standardized procedures, including regular communication and structured data gathering and collection of specific action plans from the field.
- Ongoing consultation with the field on various area-based improvement initiatives and Voice of the Employee survey related activities.
- Implementation of an intranet-based resource including guidance and resources for workplace environment improvement with a focus on activities already demonstrated to be effective in USPS.
- Creation of a one-hour national message video as part of the four hours of workplace environment/interpersonal skills training required of all employees in FY 2000 and consultation with the field to ensure that remaining training hours are used effectively based on the needs of individual Areas.

30. The Postmaster General has stated that the Postal Service is to be a place where employees take pride and ownership in their work, as well as a place where their contributions are valued.

(a) What is the Postal Service doing to bring about this change?

We are taking two fundamental steps to improve the sense of pride, ownership, and contribution that our employees feel in their work.

First, we are measuring each of these issues in regular Voice of the Employee (VOE) surveys and using these measurements as part of our variable pay program. These surveys, for example, tell us that a majority of postal employees *are* proud to work for the Postal Service. In fact, this question receives some of the highest favorable responses on the VOE survey. To improve further, specific questions from the VOE survey relating to these three areas have been compiled into an index. This index provides the Postal Service with a snapshot of employee concerns, identifies problem trends, and helps each area and district formulate specific strategies and plans to address identified issues. We have made the index a compensable indicator in the Variable Pay Program for FY 2000 to further heighten the importance of these issues.

Second, as part of our ongoing effort to improve communication and the treatment of employees in the workplace, we are continuing our training requirements of 20 hours for management levels 15 and above and 8 hours for management levels 14 and below and craft employees. Of these training hours, each employee is required to dedicate 4 hours to building interpersonal skills. This is being achieved through distribution of a national video message, *Building a Better Workplace*, Sexual Harassment Prevention training, and 1-2 hours of relationship training determined by each area or headquarters function. These efforts should improve workplace relationships and impact employees' sense of being valued and having pride and ownership in their work.

31. In your statement last year you stated that two of your goals were to improve the "people" skills in the Postal Service and to make sure that employees are treated fairly.

(a) *What programs or communications have you initiated since last year to advance these goals?*

In addition to the VOE survey index described above, our corporate message to all employees, *Building a Better Workplace*, includes interviews of craft employees who gave their vision of what makes an effective work environment. This video also included some skill building tips on how to manage conflict and explained some "best practice" initiatives underway in several geographic areas.

In FY 2000, management employees are required to view the corporate message, *Building a Better Workplace*, and a 10-minute add-on piece entitled *Making the Commitment.* This segment shows managers how to establish goals to ensure that employees have input in the workplace as well as providing clear communication and expectations as to the role each employee plays in achieving organizational success. Employee-centered discussions are modeled in this message. The conclusion of this video contains a clear message from the Postmaster General directing management to utilize goal setting strategies to create a workplace where they would be proud to have their own family members work.

32. You have indicated that you are committed to world-class training, improved succession planning and firm support for diversity.

(a) *Please discuss in detail what actions you have taken since last year to meet each of these goals.*

Our commitment to world-class training is evidenced in the way we are meeting the need to develop USPS management workforce, in our continuing efforts to review and revise existing course materials, and in the quality of new technical/functional training initiatives.

The Associate Supervisor Program (ASP), which was created in 1996, continued in 1999. Today, all divisions of the USPS are participating in the program. The ASP prepares craft employees for supervisory positions and results in a promotion to Associate Supervisor upon successful completion of the program. The program has undergone several revisions to insure that it maintains its world-class quality. A major updating of the program is scheduled for the year 2000.

The Advanced Leadership Program (ALP) is designed to provide competent leadership to guide the USPS into the future. The program's content is based on the key competencies identified through executive/managerial needs assessment. It emphasizes personal awareness, a firm grounding in key aspects of our business, and the importance of meeting the challenges of a changing competitive environment. The USPS has partnered with the University of North Carolina and the University of Oklahoma in the design and delivery of ALP. In addition, one phase of the program requires the participant to complete coursework at an accredited college or university. Officers of the USPS address each ALP class. Last year, the Vice President of Diversity personally addressed each class to discuss the vision of the organization and policies related to zero tolerance of harassment and discrimination.

In the last year, the USPS partnered with the USDA Graduate School to offer a Career Management Program (CMP) in the Postal Service. The CMP prepares supervisors, managers and postmasters, levels 15-22, for the future by providing them the skills and knowledge they need to guide employees and operations toward greater efficiency, continuous improvement, and outstanding customer service. This program is described in more detail in the response to Question 48.

In addition to these efforts, the USPS contracted with the Public Broadcasting System – The Business Channel, to offer quality, up-to-date business programming via the Postal Service Training Network.

In the last year, a program was initiated to review and revise maintenance courses offered at the National Center for Employee Development (NCED). In addition to the course review at NCED, Employee Development and Diversity partnered to complete a corporate wide review of all courses, both field and headquarters sponsored, for diversity issues. Curriculum 2000 is a current effort to insure that participants who attend courses at the USPS National Center for Employee Development arrive with sufficient skill levels to be successful in the courses they are scheduled to attend. Review and revision of our Orientation for New Employees (ONE) will also take place in the coming year.

Recent initiatives also include Bulk Mail Acceptance Unit (BMAU) training and Sales and Services Associates Training. The BMAU Academy, which opened in January 2000, represents state-of-the-art training for Business Mail Acceptance personnel. The newly designed training will be offered at the NCED and will use computer-based simulations, actual mailings, and mock customer interactions in a newly designed classroom environment. The newly designed Sales and Services Associates Training replaces the standard Window Clerk Training program and emphasizes customer relations, and marketing skills, as well as technical/functional aspects of the job.

Our internal process seeks to identify qualified successors to entry level management and specific executive positions before a need arises and to develop identified individuals through training opportunities, detailed work assignments, and/or formal educational opportunities.

The processes that support this effort, known as Career Development Tracks and succession planning, target those individuals who demonstrate an ability to lead and can be expected to be successful as managers.

The Career Development Tracks process seeks to identify individuals who, with appropriate training and/or developmental assignments, have the potential to become unit managers within the Postal Service and, in the long term, possess the potential to become postal executives. Each individual so identified is given a thorough evaluation to determine what steps need to be taken to achieve as a manager. Following the assessment, each employee in the program completes an individual development plan designed to aid in the development process. The employee's progress is tracked and appropriate assignment opportunities afforded to enhance the development. Developmental activities may include the Associate Supervisor Program, Advanced Leadership Program, formal educational opportunities, or developmental assignments.

The Career Development Tracks process, through its development of qualified managers, serves as the springboard to move staff employees into entry level management or senior staff levels.

As part of the succession planning process, identified individuals nominated by Postal Service officers are given a thorough executive competency assessment to identify their strengths and areas where development is needed. Based on feedback from the organization performing the assessment, the potential successor, with guidance from the unit manager, creates his or her own individual development plan designed to map out any steps needed to enhance the employee's executive development.

As developmental activities are completed, they are documented and further evaluation of the potential successor's progress is done. A database containing the names and status or all identified successors is available from which the names of potential successors can be drawn. When a need arises, the officer having responsibility for the functional area can readily review the information available to assist in making his/her selection.

All of these efforts are integrated into the organizational support of diversity. Diversity Development created a Business Plan in January of 1999 that targets four principle objectives: (1) articulate a clear diversity message; (2) ensure the representation of all employee groups in all levels of employment; (3) create a work environment that is free of discrimination and sexual harassment; and (4) establish and maintain a competitive and diverse supplier base that is reflective of the American supplier base.

This plan, combined with senior leadership support, a Diversity Oversight Committee comprised of postal officers, and a department dedicated to objective achievement, helps to create the awareness and environment required to meet the organization's business and diversity goals.

33. Reports from GAO have shown that the poor state of labor-management relations within the Postal Service represents one of the most significant internal operational and managerial problems facing the Service.

(a) *What actions have you initiated to improve relations between the Postal Service and its postal labor unions?*

As stated in the response to Question 25(a), the Postal Service is nearing the completion of several joint efforts with its major postal unions involving the development of joint contract interpretation manuals that should have a direct, positive impact on workplace stress points. Additionally, newly jointly developed/negotiated grievance/arbitration procedures should produce faster and more responsive resolutions to workplace disputes at the local level.

Work continues with the NALC to decide how the test dispute resolution process will function and whether it will be implemented nationwide. In addition to completing this portion of national contract negotiations with the NALC, we are in the middle of national contract negotiations with the NRLCA. The parties are working intensely to bring closure to significant workplace relations issues.

(b) *What type of counseling/training (or other relevant action) is being given to those managers and supervisors who find it difficult to treat employees with dignity and respect?*

Employees, whether in the craft or management, are expected to treat their subordinates, co-workers, and customers with dignity and respect. We have instituted a Zero Tolerance policy on this issue. When abuses occur, management takes appropriate action, up to and including removal if warranted. Additional information is contained in the responses to Questions 29, 30, and 31.

The Postal Service has taken a proactive approach in ensuring that employees are treated with dignity and respect. In situations where managers and supervisors find it difficult to treat employees with dignity and respect, their immediate superior is expected to take appropriate action. Located at most districts are employee and workplace intervention analyst (EWIAs) and Employee Assistance Program (EAP) counselors. Both are specialists in helping to resolve situations where intervention is needed. The EWIA may consult with the employee and their superior in working together to demonstrate the need of showing others dignity and respect. If there are underlying problems of a personal nature, EAP counselors work to provide necessary counseling. In some cases, managers have been sent to outside sources for more intensive training.

Management training programs, such as the Associate Supervisor Program and Advanced Leadership Program, also include specific modules that discuss why it is important for managers and supervisors to show dignity and respect and how to do so. In addition, the Postal Service has instituted the *REDRESS*$_{TM}$ program, which involves EEO mediation. In this program, the supervisor and employee meet with a neutral party to resolve issues in EEO cases.

In FY 2000, the Postal Service has adopted six questions from the VOE survey that management will be held accountable for improving. One of the questions directly involves dignity and respect. The question reads: "Rate your immediate supervisor on treating me with dignity and respect."

34. You established a Commission last year on a Safe and Secure Workplace as an independent body to study workplace violence, and related issues such as the work environment, and stress.

(a) *What have been the Commission's findings so far? Please update the Subcommittee on the membership of the Commission and its activities to date.*

The Commission is examining a broad range of postal policies and practices, including specific violence prevention programs and potentially relevant policies such as hiring, dispute resolution, performance management, and training. To date, the Commission has:

- Met several times and heard presentations from USPS management, officials of unions and management associations, workplace violence experts, and others;

- Surveyed postal employees and conducted a national random sample of non-postal employees. The survey includes questions about work environment, such as attitudes about work and management, perceptions of policies, fears and perceived dangers, and questions about psychological factors such as aggression; and

- Carried out site visits in ten performance clusters, including focus groups with craft employees, supervisors, and managers, and interviews with managers at all levels and officials of union and management associations.

Finally, the Commission is analyzing data from the Postal Inspection Service on threats, assaults, and homicides, and national data on homicides by industry. The Commission plans to report publicly in the summer of 2000.

Joseph A. Califano, Jr., a former secretary of Health, Education, and Welfare and currently president of the National Center on Addiction and Abuse at Columbia University (CASA), chairs the Commission. Other members of the Commission are:

- Douglas A. Fraser, professor of Labor Studies at Wayne State University and former president of the United Auto Workers;

- Beatrix A. Hamburg, M.D., professor of Psychiatry at Mount Sinai School of Medicine, former president of the William T. Grant Foundation, member of the Institute of Medicine, and an expert in violence issues;

- David A. Hamburg, M.D., professor emeritus at the Carnegie Corporation of New York, former president of the Institute of Medicine, and former chief, Adult Psychiatry Branch of the National Institute of Mental Health;

- John E. Robson, senior advisor at BancBoston Robertson Stephens, Distinguished Visiting Fellow at the Hoover Institute at Stanford University, past president and chief executive officer of G.D. Searle & Co., deputy secretary of the U.S. Treasury in the Bush Administration, former chair of the Civil Aeronautics Board, and former dean of the School of Business at Emory University; and

- Robert B. Zoellick, a Research Fellow at the German Marshall Fund of the U.S., former John M. Olin Professor of National Security Affairs at the U.S. Naval Academy, former Executive Vice President of Fannie Mae, deputy chief of staff in the Bush White House, and former senior official in the Departments of State and Treasury.

Naomi Goldstein serves as the Commission's staff director. Ms. Goldstein was a senior project manager at the Urban Institute and holds a doctorate in public policy from Harvard University.

35. The Subcommittee receives numerous correspondence from postal employees regarding discriminatory practices. This includes discrimination in promotions, hiring, racially motivated actions, racial complaints, protection of rights under the discrimination laws, retaliation when complaints are filed, complaints about the grievance process; hostile working environments, racially hostile environments, harassment, violence in the workplace, problems with union representatives, and managers' abusive behavior.

    Employees are reluctant to reveal problems or errors to management for fear of retaliation. Even when we receive correspondence or any type of communication from postal employees, they are sometimes afraid to reveal their name for fear of retaliation or adverse action being inflicted upon them. It appears that fear of retaliation is widespread, and is particularly felt by those employees who are participating in an investigation, or those who may want to contact legislators.

(a) *Are Postal Service headquarters and area managers aware of the size and scope of these problems?*

    Yes. We keep track of employee concerns and issues through surveys, climate assessments, and discussions with employees and their representatives. Based on this feedback, we do not believe that fear of retaliation is a widespread or systemic problem in the Postal Service.

(b) *Does Postal Service management view these allegations as isolated incidents?*

    Yes. As stated above, we do not believe that fear of retaliation is widespread or systemic in this organization. We take this issue very seriously, however. When allegations of retaliation are made, we investigate them thoroughly and deal with offenders appropriately.

    To ease potential concerns about retaliation, we also give employees the option of reporting their concerns anonymously to the Postal Inspection Service or the Office of the Inspector General (OIG) and to use numerous formal structures to openly report alleged contract or discriminatory violations.

We also have a process in place at the national level to address systemic troubled workplaces, which can involve issues like retaliation. The Workplace Environment Improvement Advisory Committee is made up of various postal leaders from the Office of the Inspector General, the Postal Inspection Service, the management associations, and unions. One of the primary functions of this group at their regularly scheduled meetings is to address systemic problem work sites and work towards resolution.

(c) *Does Postal Service management consider these alleged problems to be systemic and therefore require nationwide attention?*

No, management does not view these problems as systemic. See the response to Question 35(b).

36. The Postal Service has been accused of deliberately delaying resolution of some grievances that sometimes go on for several years.

(a) *Does the Service have any evidence to confirm or refute these accusations?*

The Postal Service is bound by its contracts with employee groups on the time frames for grievance processing. According to these contracts, if a grievance is delayed by a postal manager, the union has the right to automatically appeal the case to next level.

Extensions of the time frames are sometimes granted at the request of one or the other of the parties for legitimate reasons. Dispute processing time frames are neither deliberately nor unilaterally extended, nor are resolutions deliberately or unilaterally delayed by either the Postal Service or the unions.

(b) *What is the volume of employee complaints against management?*

During FY 1999, 206,039 grievances were appealed to Step 2 of the grievance/arbitration procedure, 95,760 to Step 3, and 1,344 to Step 4.

(c) *What steps in general are being taken to investigate employee allegations?*

There is no set process that guides how managers investigate employee allegations. The response is determined by many different factors, including the specific type of complaint and where it is being made. In general, local managers try to determine the facts and respond in a way that best fits the situation. In many cases, employees use the more formal grievance process to lodge complaints.

(d) *How are complaints handled that are forwarded to Postal Service Headquarters?*

An employee complaint received at headquarters gets immediate attention. A written complaint is often sent to the Office of the Postmaster General and is normally forwarded to Labor Relations for handling. The letter is then sent to the lowest possible organizational level for investigation and response. This ensures the fastest and most effective handling. The employee is then notified by mail that the letter has been forwarded to the local level for response and told who is handling the letter. The office to which the complaint is forwarded is normally instructed to send a copy of its response to headquarters to clear a suspense file on the complaint.

37. The Postal Service has also noted in recent correspondence initiatives being implemented through the REDRESS (Resolve Employment Disputes, Reach Equitable Solutions Swiftly) program. REDRESS provides for mediation of Equal Employment Opportunity (EEO) complaints, and, through national initiatives to prevent workplace violence, ways to reduce conflict and identify and eliminate the potential for violence in the workplace.

(a) *What has been the outcome of these initiatives? What is the status of the accelerated arbitration process? Have any of the initiatives been discontinued?*

REDRESS, which began in 1994 as a pilot program in North Florida, was rolled out to every district in FY 1999. During FY 1999, nearly 9,000 cases were mediated and 81 percent of these were closed, leaving only 19 percent in which employees filed formal complaints after mediation. In comparison, where cases were not mediated, 44 percent became formal complaints.

Even taking into consideration that individuals who choose mediation may be more inclined to settle their disputes, this very large drop in the national percentage of formal complaints after mediation underscores the program's effectiveness. In addition, satisfaction studies continue to indicate that participants (supervisors, employees, and employee representatives) are very satisfied with the mediation process, the mediation itself, and the outcome. Additional information is contained in the answer to 42(c).

As a result of discussions between the Postal Service and the American Postal Workers' Union (APWU), the parties entered into a Memorandum of Understanding on May 8, 1997, that established an Accelerated Arbitration Initiative. Pursuant to the Initiative, two Performance Clusters per Area with the largest docket of pending proceedings were to be selected to test the program. A sufficient number of arbitrators, advocates, and arbitration dates were to be assigned to complete hearings of all pending cases, and after the elimination of the backlog, the arbitration dockets were to be monitored. If the dockets reached a mutually agreed upon threshold, the parties were to again provide sufficient arbitrators and hearing dates to complete hearings in a mutually agreed to time frame. The initiative ended with the expiration of the 1994-1998 Agreement.

38. Grievances can be resolved within the first two steps of the process at the local level, if a supervisor or postmaster can come to terms with local union leaders.

(a) *How many grievances are settled within the first two steps of the resolution process?*

During FY 1999, 110,279 grievances, or nearly 54 percent of the 206,039 cases, were settled at Step 2 of the grievance procedure. We do not currently track the number of cases filed or settled at the first step of the resolution process.

(b) *What are the most frequently cited issues in employees' discrimination complaints?*

Most complaints involve an employee's concern over why they have been disciplined by management.

(c) *What are the bases of the alleged discrimination?*

Employees believe that disciplinary action has been taken against them because of racial or other discrimination or in retaliation for an action they might have taken.

39. Representative Traficant recently contacted the Chairman in reference to alleged problems and abuses within the Postal Service in his Congressional District. The alleged problems in his district included gender, race and disability discrimination, sexual harassment, abusive supervision, retaliatory assignments, and irregularities in hiring, training, promotions, and disciplinary actions. He also felt that the "problem-solving mechanism", as he stated, is flawed because results and decisions take too long and can be costly for the employee. He also stated that complaints filed through the EEOC were too time-consuming. He also felt that there was a concern that employee frustration with these ongoing problems, and the lack of timely final resolutions, could lead to violent behavior. He informed the Chairman that during the forum that he co-hosted on the alleged problems within the Youngstown and Canton Postal District, a postal employee confessed that he was so angered by the volatile work environment that he considered using his guns against his supervisors.

(a) *What is the Postal Service doing to address the labor-management problems in Mr. Traficant's District?*

Postal management from the Akron District and Youngstown Post Office met with a committee of local officials and community leaders to address claims of perceived injustices in the Youngstown Post Office. Monthly meetings were held between November 1998 and July 1999 so that issues could be brought to postal officials with the authority to resolve them.

Many issues were resolved, but there were instances where claims could not be resolved through these meetings since the employees were already litigating their claims in formal proceedings. Labor climate surveys have also been conducted in the Akron District and specifically in Youngstown since 1998, and no significant problems were revealed from those surveys.

(b) *What is the Postal Service doing to alleviate the serious frustration that is being felt by aggrieved employees with the inability of the so-called problem solving mechanisms to resolve these complaints?*

During the latter part of FY 1999, the Postal Service introduced REDRESS$_{TM}$ to the Akron District. REDRESS$_{TM}$ is the Postal Service's alternative dispute resolution program for EEO complaints, and it employs the services of outside mediators to work with management and employees to resolve claims of discrimination at the pre-complaint counseling stage. Generally, the mediation sessions are scheduled within two weeks of the time the individual asks for pre-complaint counseling. During the first quarter of Fiscal Year 2000, the Akron District has a 75 percent participation rate in cases referred to mediation. Almost 80 percent of those cases are being settled at the table with the mediator.

To the extent that cases cannot be resolved and move to the formal complaint stage, Akron has a good track record of completing the investigative process on time. Akron currently has no cases over 180 days old at the investigative stage. Once the investigation is completed and the individual exercises the right to a hearing, the Equal Employment Opportunity Commission (EEOC) takes jurisdiction of the case and the time frame for processing can become quite lengthy due to backlogs at the EEOC.

40. Moe Biller, President of the American Postal Workers' Union, stated in his testimony to the Subcommittee in a recent hearing that the Postal Service's policy of "Zero Tolerance" is applied with zero fairness to bargaining unit employees. He claims that managers have been provided a protective shield which enables them to abuse employees verbally and physically, with any hint of resistance by employees met with swift disciplinary action. Mr. Biller asked that the PMG send a letter to each supervisor and manager stating that abuse of employees would not be tolerated.

(a) *How do you respond to these very serious accusations?*

We do not agree with Mr. Biller's assessment. The Postal Service does respond to all allegations of physical or verbal abuse. Based upon the specific circumstances, we then take appropriate corrective action. We believe that we have implemented this policy in a balanced way towards individual bargaining and/or non-bargaining employees.

(b) *Was this request honored? Did the PMG communicate directly to each supervisor and manager?*

Postmaster General Henderson has not mailed a letter to each employee and manager on this issue. However, since taking office, Mr. Henderson has widely communicated the need for treating every individual with dignity and respect.

He has addressed each of the management associations at their national conventions regarding treatment of employees. In his remarks to the thousands of attendees at these sessions, he has emphasized the critical role supervisors and managers have in maintaining a workplace that is perceived to be fair and free from unlawful and inappropriate behavior.

In an interview in the National Association of Postal Supervisors (NAPS) publication *The Postal Supervisor*, the Postmaster General outlined his philosophy on creating a leadership model that focuses on fairness and opportunity.

This organizational commitment continues in his taped endorsement of the recent "Building a Better Workplace" video currently being shown to both craft and management employees around the country as part of the Voice of the Employee training series. His comments, directed specifically to supervisors and managers in a separate segment, focuses on their responsibility for maintaining fairness within the workplace. The following is an excerpt from those comments:

> "I want you to think about your role, and whether you're doing your part to create an environment that you would be proud to have your own family members work in. Ask yourself, 'Am I part of the problem?' Because the bottom line is that it's really up to you to help create a model workplace for every single postal employee."

(c) *Please discuss the goals and strategies of the zero-tolerance program?*

The Zero Tolerance policy is based on the belief that no employee should have to work in an environment of fear or intimidation. Employees deserve a safe work environment. Our commitment at the performance cluster level is to provide this environment in reaffirmation of the *Joint Statement on Violence and Behavior in the Workplace.* Zero tolerance also means that every act or threat of violence will elicit a quick and firm response. A case-by-case review is made of each circumstance, and the response may involve discipline up to and including removal, regardless of whether the employee is a supervisor, manager, or craft employee.

41. The value of the Employee Assistance Program (EAP) has been called in to question by some employees.

(a) *Have you performed or been requested to perform a study of the effectiveness of the Employee Assistance Program (EAP)?*

The EAP evaluates its effectiveness through numerous methods, including:

- Client satisfaction surveys;
- Counselor assessments of client improvement;
- Site visits where clinical records are reviewed and various program customers are interviewed; and
- Client input before beginning and after receiving counseling about the impact of counseling on their emotional, social, and physical well-being as well as work attendance.

All of these data indicate that the Postal Service EAP is effective. One formal study on the USPS EAP was conducted by an independent contractor at the behest of Federal Occupational Health, the contractor providing EAP services. The study estimated the cost benefit of the program in reducing absenteeism. The results of that study were positive. Management also conducted an internal review of the financial aspects of the program in 1997 and implemented recommendations after that review.

(b) *What are the duties and responsibilities of a Workplace Intervention Analyst?*

Employee Workplace Intervention Analysts (EWIAs) are responsible for analyzing employee and workplace issues and concerns and recommending solutions, developing strategies and making recommendations for cultural/workplace change and conflict resolution, and ensuring that the USPS EAP is administered consistent with the contract for those services.

(c) *Does the Postal Service keep statistics on how many employees are served by the program? If so, please provide an overview of the program activities over the last fiscal year.*

The EAP provides free, voluntary confidential counseling services to USPS employees and their families by master's level and above counselors housed in or near postal facilities throughout the country. Counselors assist employees and their family members with a variety of issues, including emotional, financial, legal, chemical dependency, marital, and family problems. In FY 1999, 34,665 employees and their family members received counseling and 42,722 employees attended health and wellness seminars on topics ranging from stress management to elder care and substance abuse. The EAP also assisted over 9,800 employees in responding to over 800 critical incidents.

42. The Subcommittee receives complaints often concerning investigations being conducted by the Postal Service, and EEOC's handling of discrimination cases filed by federal employees. The EEO process can take as long as four months to a year or longer. Civil action may also be filed if the complainant has not received a final agency decision within 180 calendar days after the formal complaint was filed. This can be very frustrating for an employee, and if they have to file a civil action, very costly. Supposedly, the EEO process is by design, open-ended in that it affords employees many layers of review. The downside is the amount of time it takes to exhaust all levels of the process. Apparently there have been some efforts to streamline the system.

(a) *Please discuss those efforts that you are aware of to streamline the EEO complaint system and, in your opinion, have they been successful?*

The EEOC recently revised its regulations to address some of the problems that have persisted in the EEO complaint process. The EEOC now requires all agencies to establish alternative dispute resolution programs to better address claims early in the process. The EEOC has also given agencies the latitude to dismiss claims that involve abuse of process and have eliminated spin-off claims that involve allegations against the complaint process. EEOC Administrative Judges have also been given authority to dismiss frivolous claims. All of these changes are geared toward reducing the number of claims in the formal complaint process and to make it easier to adjudicate claims which have some merit. Since these changes have only been in effect since November 9, 1999, it is too early to tell what impact they will have on the federal sector complaint process.

(b) *What have been the Postal Service efforts to provide training to employees on sexual harassment, equal employment opportunity (EEO) as well as handling of EEO complaints?*

Over the past few years, the Postal Service has provided sexual harassment awareness training to supervisors and managers across the country. The purpose of the training is to heighten the awareness of our supervisors and managers on the problem of sexual harassment in the workplace and to provide guidance regarding the proper steps to take when a situation occurs.

In FY 1999, sexual harassment training was made available to all postal employees, but was not mandatory. In FY 2000, all craft employees are required to view a new one-hour training tape that will help increase their awareness of sexual harassment issues. Non-bargaining employees are required to take two hours of training that describes how to identify, investigate, prevent, and resolve sexual harassment situations in the workplace.

In addition to these courses, video "infomercials," web-based resource material for Diversity Development and Hispanic Program Specialists, and booklets for employees and managers will be provided. More materials (course training, a "tool kit" for sexual harassment prevention, and incident tracking) are under development.

In addition to the training on sexual harassment, the Postal Service has conducted extensive orientation and training sessions throughout the country in preparing managers and supervisors for the REDRESS Program. These sessions entail discussions of the EEO complaint process, the point at which mediation will be introduced into the process, and the expectations for management involvement in this program.

(c) *Have your programs to streamline or speed up the EEO process decreased the backlog of grievances? If so, in what areas?*

The primary initiative undertaken by the Postal Service to reduce the backlog of claims has been the introduction of the REDRESS Program. During FY 1999, REDRESS was rolled out to every district. REDRESS I, which provides for mediation at the pre-complaint stage, emphasizes speed in arriving at resolutions. The mediation sessions generally occur within two weeks of the time the individual requests pre-complaint counseling.

During FY 1999, more than 9,000 mediation sessions were conducted with a closure rate of 81 percent. This effort, coupled with resolutions through the normal counseling process, resulted in a reduction of over 2,000 formal complaints, or about 19 percent. The Postal Service has also introduced ADR at the formal stage of the process. This effort, known as REDRESS II, is geared toward resolving claims at the investigative and hearing stages, and is being piloted in the San Francisco area. REDRESS II employs outside mediators under the same model as REDRESS I.

Significant reductions in formal complaints have occurred in 10 of the 11 Areas in the Postal Service. These reductions have also enabled EEO professionals who perform investigative and appeals work to begin to reduce case inventories. After several years of steadily increasing inventories of cases, the Postal Service was able to reduce the inventory by over 2,700 cases, or approximately 20 percent.

43. In September 1999, GAO issued a report that discussed the quality of equal employment opportunity (EEO) complaint data maintained by the Postal Service. In responding to a recommendation in the report, a postal official indicated that the Postal Service planned to adopt comprehensive management controls to ensure that EEO data submitted to the Equal Employment Opportunity Commission are complete, accurate, and reliable.

(a) *Please describe in more detail the types of controls that the Service plans to implement. Also, what examinations of the controls would be done to determine whether the controls ensure that EEO data recorded and reported are complete, accurate, and reliable?*

The GAO report focused on annual reports made to the EEOC each year. The Postal Service developed a program to automatically produce the reports each year, and some flaws in the programming led to inaccurate figures. The major programming flaws have been corrected; nevertheless, an in-depth examination of each data element has been undertaken to insure that all of the formulas used to produce the data are consistent with EEOC requirements. The data produced by this program will then be matched against data developed by running individual programs for each data element to insure consistency. The data produced will also be examined by experienced EEO professionals who understand the process and can detect any anomalies that occur and recommend corrective action. Rather than waiting until the end of the year to run the data, it will be produced on a quarterly basis so that as the year proceeds, the Postal Service can ensure that any problems in data are noted and can be modified well in advance of the end-of-year reporting requirements.

44. Experts on workplace violence say it is a widespread misperception that office homicides erupt unexpectedly. However, they say most people contemplating homicide tell others, sometimes repeatedly of their intentions. Usually co-workers know on some level when they are at risk. Whether the threat becomes a reality depends on how well the company responds to the crisis.

(a) *What mechanisms do you have in place to identify potentially violent employees?*

Our EAP is a primary source in identifying and dealing with troubled employees. In addition, each performance cluster, as well as Postal Service headquarters, has a trained Threat Assessment Team (TAT) in operation to identify potentially violent individuals or situations. Each performance cluster conducts crisis simulations to prepare for possible emergencies through their trained Crisis Management Teams. Training is continuously provided to help identify employee danger signs. Workplace Violence Awareness, an 8-hour training course for management and 1-hour course for craft, helps employees to better understand their role in recognizing and defusing workplace violence.

(b) *What steps are taken to protect other employees?*

Besides enforcing a Zero Tolerance policy designed to protect all employees, during FY 1999 a newly created Area Security position was established and staffed within each of our eleven area offices. These individuals have assumed their positions and completed training and have since been focusing on improving general security. In addition, more than $27 million is being allocated this fiscal year to address high-priority physical security needs.

Management and craft training remain key initiatives to protect employees. As stated previously, management training at the performance cluster level includes Workplace Violence Awareness training. All newly hired craft employees receive training on Workplace Violence Awareness, which is also being expanded to existing craft employees in several Areas this fiscal year.

Employees also have access to well-publicized, toll free "hot line" numbers for the Inspection Service, Inspector General's Office, OSHA, and EAP. Calls may be made anonymously and receive prompt responses depending on the urgency required.

(c) *Please discuss the programs and procedures you have in place to minimize the threat of violence.*

The Postal Service supports an award-winning EAP that is available to all employees and their immediate families. Last year, more than 30,000 employees and family members utilized the counseling and information services provided through this program on a self-referral basis.

After being piloted during FY 1999, a "Safe Separations" training program for supervisors and managers will be implemented this fiscal year. This training will help supervisors facilitate meetings with employees who are being terminated from employment. It will assist supervisors in getting the support they need to conduct separation meetings. It will also instruct them in how to use other resources, including neutral postal personnel who can talk calmly with employees who are being terminated and discuss resources available to assist them during their transition of leaving the organization.

As stated previously, each performance cluster provides awareness training to management and craft employees. This year, in addition to maintaining a well-trained management Threat Assessment Team, Crisis Management Team, and conducting crisis simulations, all employees are required to complete a four-hour segment of their annual training that deals specifically with improving workplace relationships. These initiatives, in conjunction with enforcement of the Zero Tolerance Policy, are intended to minimize the threat of violence in the workplace and hold individuals accountable for their actions.

45. The aggressive management course was intended to teach Postal Service supervisors how to identify aggressive behavior and defuse and prevent workplace violence through unbiased communication.

(a) *Has this program been successful in defusing dangerous situations? Please provide evidence to support your statement.*

There is no nationally sponsored course by that name. However, there are national courses that do address the prevention of workplace violence. *Workplace Violence Awareness*, an eight-hour course for managers and supervisors, specifically addressed workplace violence prevention and was delivered to all postal managers and supervisors in 1995. In addition, each performance cluster has a trained Threat Assessment Team (TAT) in operation to identify potentially violent individuals or situations. Each performance cluster also conducts crisis simulations to prepare for possible emergencies through their trained Crisis Management Teams. Training is continuously provided to help identify employee danger signs. All newly hired craft employees receive training on *Workplace Violence Awareness*, which is also being expanded to existing craft employees in several Areas this fiscal year.

All of these efforts have better equipped postal employees to prevent incidents of violence or to deal with them when they do occur. Training is enhanced as new lessons are drawn from experience in dealing with these situations. Postal Service efforts, in fact, have become a model nationally and postal employees are routinely invited to present to external public and private agencies about our violence prevention activities.

46. With respect to sexual harassment, often the Subcommittee learns of incidents in which postal employees have been subjected to the most horrific and despicable acts that could be perpetrated against a person from supervisors, as well as co-workers. Unfortunately these employees are so intimidated that many are afraid to seek help.

(a) *What remedy is available to victimized employees for such incidents? Assuming the allegations are proven true, what action is taken against the perpetrator?*

The Postal Service takes the problem of sexual harassment very seriously. We have implemented a program to prevent sexual harassment in the workplace and to address promptly any incidents of sexual harassment that may occur.

Over the past few years, the Postal Service has provided sexual harassment awareness training to supervisors and managers at postal installations throughout the country. The purpose of the training is to heighten the awareness of our supervisors and managers on the problem of sexual harassment in the workplace and to provide guidance regarding the proper steps to take when a situation occurs.

The Postal Service's initial management inquiry process for sexual harassment complaints allows managers, postmasters, and supervisors to whom a complaint is brought to obtain enough information at the outset to:

- Determine whether there is an immediate need to separate the parties from one another.
- Determine whether there is an immediate need to recommend that an employee seek Employee Assistance Program (EAP) counseling. EAP is a confidential, voluntary counseling service for all Postal Service employees and their family members.
- Determine whether other employees are being harassed.
- Assess the nature and scope of the problem in the workplace.
- Decide whether the manager or supervisor can remedy the problem or whether referral to Human Resources for a full investigation is warranted because of the individuals involved or the nature and scope of the changes.

The inquiry imposes upon managers, postmasters, and supervisors the obligation to react promptly to complaints alleging sexual harassment and compels them to deal with the problem. In short, it avoids both wholesale dismissal of such complaints and referral of the issue to an EEO counselor.

When supervisory employees do not have the necessary authority to launch an inquiry, the complaint is brought to the attention of a higher level supervisor or manager with such authority.

The initial management inquiry does not replace the sexual harassment investigation normally conducted under the auspices of Human Resources. When in the course of the initial management inquiry, the manager learns that the nature and scope of the complaint warrants outside investigation and/or that resolution is not feasible, management refers the complaint to Human Resources for a full investigation.

Where there is evidence that an employee has engaged in sexual harassment, management will initiate appropriate remedial action that includes disciplining the harasser and taking steps to ensure that the harassment has ended. Where warranted, other appropriate administrative action may also be taken.

47. The Subcommittee is interested in how well the Diversity Department is meeting its goals.

(a) *What are the responsibilities of the Diversity Department in the Postal Service?*

The "Diversity Department" in the Postal Service is named Diversity Development. Its purpose is to:

- Create an inclusive organization with a sense of common purpose by promoting change and growth, so that diverse needs of employees, customers, and suppliers are integrated into how the Postal Service does business.

- Build an inclusive workplace environment that recognizes the uniqueness of every individual and encourages the contributions of people from different backgrounds, experiences, and perspectives.

- Be a social conscience in building on the foundation of affirmative action and equal employment opportunity so that all employees are empowered to do and be their best.

These responsibilities are carried out under:

- Twenty-three initial improvement initiatives, and eleven ongoing initiatives (see Attachment 3);

- Four principal objectives in the diversity business plan:

  - Articulate a clear diversity message;

  - Ensure representation of all employee groups in all levels of Postal Service employment;

  - Create a work environment free from discrimination and sexual harassment; and

  - Establish and maintain a strong, competitive, and diverse supplier base.

(b) *How does the Postal Service measure whether the Diversity Department is meeting its obligations?*

The Postal Service has a unique management system called *CustomerPerfect!* This system is modeled on the Malcolm Baldrige National Quality Award framework, core values, and performance criteria. Its annual planning cycle establishes program goals, business strategies, and measures of performance, including both indicators and targets.

Reporting is accomplished in several ways:

- Projects and milestones in support of the four principal objectives are tracked through a computerized project management system, with reports regarding projects meeting milestones and being completed.

- All executives establish diversity-related objectives as part of the merit performance evaluation system. Objectives and accomplishments are summarized and sent by way of the Area Vice Presidents to the Executive Vice President/Chief Operating Officer.

- Tracking activities in support of the Affirmative Employment Plan are maintained through Diversity Development Specialists in the field and executive liaisons at Headquarters.

- Progress reports are made to the Board of Governors and Diversity Oversight Committee regarding the improvement initiatives.

Measurement tools include:

- Diversity Reporting System, which collects data and provides reports on employment.

- Quarterly workforce profile, which tracks workforce hiring, separation, and promotion by unit across ethnic-by-gender groups. It includes breakdowns by key organizational level up to executives and corporate officers. It is reviewed by all officers and submitted by Postmaster General/CEO to the Board of Governors.

- Tracking sexual harassment training hours.

- "Inclusion index" for building representative applicant pools.

- Analysis of individual executives' diversity performance objectives and accomplishments; reporting is via Area Vice Presidents to the COO to ensure integration with the business plan and provide visibility to efforts.

- Tracking of developmental assignments and participation in succession planning programs.
- Tracking of local activities in support of the Affirmative Employment Plan.
- Quarterly Diversity Performance Review (See Attachment 4).

Measurement tools specific to supplier diversity include:

- Tracking number of transactions, dollars awarded.
- Recording events with suppliers.
- Tracking buyer training hours.
- National Minority Supplier Development Council database now available to selected purchasing personnel and Senior Diversity Program Coordinators.

(c) *Please summarize the action plans developed by the Postal Service for dealing with diversity issues.*

Specific activities that support diversity include:

- *The Affirmative Employment Program.* This program provides national guidance on the Postal Service's affirmative employment programs. During 1999, efforts were focused on Voice of the Employee issues that were identified in the *CustomerPerfect!* process, and diversity issues raised by the Aquirre six-month study commissioned by the Postal Service's Board of Governors. Diversity Development helped postal managers compile statistical information for the Affirmative Employment Program, which addresses the prevention of sexual harassment, employee group representation, discrimination complaints, recruitment and hiring, employment development, promotions, separations/retention, program evaluation, and veterans and people with disabilities.
- *The Diversity Reporting System* (DVRS). DVRS provides detailed work force statistical reports used to analyze postal work force data and identify employment trends. DVRS enhancements for 1999 include the development of tracking reports for applicant flow, awards, and EEO complaints.
- *The Quarterly Work Force Profile.* This profile provides the status of employee group representation within the postal work force. It is distributed to the Board of Governors, officers, and managers.

- *Prevention of Sexual Harassment.* One-hour mandatory training will be given to all craft employees to increase awareness of issues. Two hours will be given to all non-bargaining employees on how to identify, investigate, prevent, and resolve sexual harassment situations in the workplace. In addition to courses, video "infomercials," web-based resource material for Diversity Development and Hispanic Program Specialists, and booklets for employees and managers will be provided. More materials (course training, a "tool kit" for sexual harassment prevention, and incident tracking) are under development.

- *Noncompetitive Hiring Program.* The Postal Service sponsors a noncompetitive hiring program for people with disabilities. Applicants for designated entry positions, which represent the bulk of external recruitment, may have their qualification assessed by the Department of Veterans Affairs or by departments of vocational rehabilitation in the states. Applicants certified by these agencies are eligible for noncompetitive hiring.

- *National Hispanic Program.* This program is intended to identify high potential employees, provide orientation to applicants for entry hiring exams, conduct recruitment and community outreach, and establish and maintain contacts with Hispanic organizations.

- *Women's Program.* This program sponsors executive leadership training, analyzes issues concerning work and family life, initiates efforts regarding recruitment, retention, mentoring, and succession planning, and conducts focus groups to identify and resolve women's issues.

- *The Special Emphasis Program.* This program was created to address the special needs, obstacles, and concerns of various ethnic, racial, and other minority groups, including Blacks, Asian Americans/Pacific Islanders, American Indians/Alaskan Natives, individuals with disabilities, and veterans and white males. The programs focus attention on the needs of these groups when they are underrepresented in the Postal Service (though they may be well represented in the civilian labor force) or when they are underrepresented at higher levels of postal management (though they may be well represented in the bargaining units or in lower level management). The Special Emphasis Program's objective is to ensure that all employees are fully utilized in our workforce and have an equal opportunity to compete in every aspect of employment, including but not limited to recruitment, hiring, retention, training, career development, and promotions.

See also Attachment 3 for improvement initiatives.

(d) Are these programs having an impact on diversity?

The original initiatives are complete and have accomplished their intended goals. Accomplishments for the past fiscal year are highlighted in Diversity Development's section of the *Comprehensive Statement* (Attachment 5).

The attached FY 1999 Postal Work Force Profile Report (Attachment 6) provides statistical data showing the diversity employment representation within the Postal Service. Overall, the report continues to reflect positive trends and improvements in the hiring and promotion of women and minorities.

In FY 2000, we will continue to address the under-representation of the various groups in preparation for the next census. Mentoring, training opportunities, details, and reassignments are all part of our plans, and these activities will be carefully monitored to ensure access for all groups.

See Attachment 4 for more information. (Note: actual reports provided as examples, unit identification headings deleted.)

(e) What has the Postal Service done to improve diversity at the higher postal management levels? Please provide the number of minorities, in particular, African Americans, and Hispanic employees that are currently in PCES (Postal Career Executive Service) positions within the Postal Service, i.e., those whose salaries are in the $79,000 to $126,000 range? How many women and minorities currently hold executive or top management positions within the Postal Headquarters and in the field?

All Empl.		**White**		**Black**		**Hispanic**		**AAPI***		**AIAN****		**Total**	
M	F	M	F	M	F	M	F	M	F	M	F		
682	172	555	120	76	43	41	4	9	4	1	1	854	All
384	113	327	90	34	16	17	3	6	3	0	1	497	HQ
298	59	228	30	42	27	24	1	3	1	1	0	357	Fld.

* - Asian American/Pacific Islander
** - American Indian/Alaskan Native

The Postal Service tracks representation for succession planning for executive positions. There are also developmental programs, such as the Advanced Leadership Program, that prepare employees for senior management positions. Participation demographics are monitored.

(f) In light of the Aguirre report, what measures have been taken to improve the role of women and minorities?

The Aguirre Report resulted in 23 initiatives that have been completed. See Attachment 3.

(g) What are the latest statistics of women and different minority groups employed in the Diversity Department?

All Empl.		White		Black		Hispanic		AAPI		AIAN		Total
M	F	M	F	M	F	M	F	M	F	M	F	
10	16	2	2	3	12	4	1	1	1	0	0	26

(h) What initiatives has the Postal Service taken to assure fair consideration for women and minorities when applying for higher level positions, particularly those at the EAS (Executive and Administrative Schedule) 17 level and above?

The Postal Service has reinstated promotion review committees of diverse membership to evaluate applicant qualifications. Training for review committees and selecting managers was recently revised to emphasize efficient, effective, and fair assessment. Career development programs have been, or will be, implemented. These include the Career Management Program (mid-level management) and Career Development Tracks (general EAS). The General Accounting Office conducted an audit of EAS selections and found them to be done fairly, and according to procedure.

(i) What initiatives has the Postal Service taken to increase supplier diversity? What exactly is being done to simplify purchasing policies to provide small, minority and woman-owned enterprises easier access to Postal business?

The following activities are in place to increase supplier diversity within the Postal Service:

- Expand Supplier Diversity Program Communication
  We developed and published a Supplier Diversity "Statement of Commitment," and added a variety of communication tools and links to both the Intranet and Internet web pages (www.usps.gov.busctr).

- Expand Purchasing and Materials Diversity Operating Plan
  The Supplier Diversity Plan covering the years 1999-2003 will help ensure a continued focus on and improvement in our relations with small, minority, and woman-owned businesses. The plan consists of aggressive year-to-year continuous improvement targets for five-year planning.

- Link Local Buying to Supplier Diversity Program
  Guidelines have been issued to local buyers and credit card holders to promote consideration of small, minority, and woman-owned businesses.

- Improve Subcontracting Participation by Minority/Woman-owned Businesses
  Purchasing policy on subcontracting was revised and reissued. The focus has been heightened on subcontracting or second tier participation.

- Provide Supplier Diversity Training to All P&M and Other Buyers
  In 1999, we established training requirements for all buyers. By and large, the major buying functions and most local buyers completed their training requirements. Additionally, generic guidance for credit card buyers is now in the AS-709, Credit Card Policies and Procedures for Local Buying, which went into effect on November 30, 1998. Training modules for local buyers are also available on our Intranet pages. Supplier Diversity coverage has been added to the courses in the functional curriculum. We are currently assessing the need to add coverage to other core USPS training offerings.

- Establish Accountability for Complying with Supplier Diversity Program
  For 1998, we have moved from objectives to process and result indicators so that we can assess effort as well as results. Indicators are being tracked by both individual and buyer organization.

- Southern California Pilot Program
  A cross-functional pilot has been launched to explore new approaches and replicate those that are successful. The team represents all buying functions and diversity personnel. They are currently working on identifying best practices and will expand to other areas.

A variety of tools have been developed to obtain supplier input on ways to make it easier for suppliers to do business with the Postal Service. They include an annual supplier survey, mechanisms to provide supplier with direct electronic access to supplier diversity coordinators, and a supplier quality council. This council is a forum outside the purchasing process for suppliers to actively dialogue with the Postal Service to enhance performance and operations, and to act as mutual sounding boards on possible policy changes that may have some impact on the supplier community.

48. The Postal Service incorporated 23 initiatives into a business plan last year following a report by consulting firm Aguirre International on how the agency stacked up against the civilian labor force in terms of ethnic and gender diversity. In April, the Postal Service announced that it had tackled 17 of 23 planned diversity initiatives designed to make the agency better reflect the communities it serves.

(a) *Has any progress been made on the remaining initiatives?*

The 23 initiatives have been completed. See Attachment 3.

(b) *What are the results of the programs pilot-tested by Human Resources that were aimed at career development?*

The Career Management Program (CMP) prepares supervisors, managers, and postmasters, Levels 15-22, for the future by providing them the skills and knowledge they need to guide employees and operations toward greater efficiency, continuous improvement, and outstanding customer service. Course curriculum covers skills and information identified by the field as critical for effective supervision and management. The program consists of three educational and training tracks:

- General Supervisory Skills Training for newer supervisors.
- Advanced Supervisory Skills Training for more experienced supervisors.
- Management Skills Training for managers.

Employees complete a competency review, in consultation with their manager, to determine the skill areas they want to strengthen and the initial track they should attend. Employees may attend additional tracks and participate in elective courses throughout their career based upon a periodic review of their supervisory and managerial skills.

The nine pilot sessions of the Leadership Core were completed in June 1999. The ongoing end-of-course evaluation data collected from both the pilots and post-pilot sessions has been consistently excellent. In addition, the follow-up evaluation data collected from the pilot sessions support the usefulness of the program in building critical skills in supervisors and managers. Both participants and their bosses reported that the program helped provide skills used on the job in a variety of areas, including Oral Communication and Listening, Directing and Developing Others, and Decision Making and Problem Solving.

(c) *Have you developed a process to evaluate how you are doing in recruiting minorities and women?*

The Postal Service tracks recruitment for entry positions, which constitute the vast majority of positions filled from outside the Postal Service. Reporting systems are being established for specific breakdowns in higher level positions.

(d) *What has been done to strengthen and ensure the Postal Service's commitment to diversity?*

In addition to the activities described above and in Attachment 3, the Postal Service has accomplished the following as evidence of our continued commitment to diversity:

- Reorganized Headquarters Diversity Development Department to better achieve organizational goals.
- Upgraded level and responsibilities of Area Senior Diversity Program Coordinators.
- Established and identified Headquarters Diversity Liaison responsibilities with each functional department represented by an individual selected by the Vice President.
- Presented Diversity business plan to each Area office by the Vice President Diversity Development.
- Created and staffed Hispanic, Women's, and Special Emphasis Programs at the Headquarters level.
- Participated in community partnership programs.
- Emphasized succession planning.

(e) *What is the function of the Diversity Oversight group? How frequently does it meet?*

The Diversity Oversight Committee oversees implementation of diversity initiatives and serves as an advisory council for diversity issues. They meet at least quarterly. The membership and composition of the Oversight Committee includes Field and Headquarters executives, Officers, and Inspection Service leadership. The Chief Operating Officer (COO) and Chief Financial Officer (CFO) administer the Committee. A total of seventeen members are currently serving.

(f) *Has the Service developed a process to track, evaluate, and act on the results needed to establish accountability for diversity in PCES Merit Evaluations?*

The PCES Merit Evaluation process is intended to allow for individual objective setting in support of corporate goals and certain critical indicators. Beginning in FY 1999, individuals were required to establish objectives in the area of diversity, which would address the particular diversity challenges faced in their area of responsibility. The process of establishing specific goals and indicators takes place between the executive and his/her manager. The progress towards goal achievement is checked throughout the year. At the end of the year, the manager evaluates overall achievement of the individual objective.

49. The Diversity Development Strategic Plan is being updated and broadened to reflect the commitment embodied in the team's 23 recommendations.

(a) *Please provide the new Plan and discuss your current strategies for effective developmental and career progression for minorities and women.*

The Diversity Development Strategic Plan is in the process of being updated. A copy will be provided when it is complete.

The Diversity Development department has created positions staffed with program specialists dedicated to Hispanic, Women's, and Special Emphasis Programs.

Each of the programs is focused on recruitment, hiring, and retention initiatives. Emphasis is placed on identification and eradication of employment, developmental and promotional barriers for underrepresented groups. These efforts are aimed at ensuring representation of all employee groups at all levels of Postal Service employment.

An example of these efforts is represented by our sponsorship of the Career Management Program. In addition to the pilots sponsored by Human Resources, the Headquarters Diversity Development department sponsored eleven programs (see Question 48(b)) in each of the areas. These efforts are in support of our developmental efforts toward minorities and women. The demographic breakdown of those classes are as follows:

All Empl.		**White**		**Black**		**Hispanic**		**AAPI**		**AIAN**		**Total**
M	F	M	F	M	F	M	F	M	F	M	F	
112	166	52	92	32	52	20	16	8	7	1	0	278

50. The Voice of the Employee (VOE) Labor Training class was designed for management to make them aware of the voice of employees. The goal is to train managers to listen and respond to the needs of employees by providing managers with tools and resources to identify, remove and overcome barriers where under-representation exists to ensure equal opportunities for all employees and; to ensure that there is zero tolerance of discrimination and harassment in the workplace.

(a) *Has this program been fully implemented? Have you measured the effectiveness of the VOE (Voice of Employees) Labor Training program?*

We are not sure which specific labor relations training class you are referring to in the question. Please see Question 30 addressing Voice of the Employee (VOE) training requirements.

51. Governor Tirso del Junco has made comments regarding dissension between Blacks and Hispanics.

(a) *Is the PMG and his management team aware of his concerns and have they discussed these concerns with him?*

Yes, the Postmaster General and the Management Committee are aware of Governor del Junco's concerns and have discussed them with him.

(b) *What has been done to address this specific issue?*

The Heritage Coalition was created in response to this issue. It is composed of the leadership of internal employee groups representing all minorities and women. Coalition members include representatives from the Hispanic Organization of Postal Employees (HOPE), A+, Network, The Hispanic Society, Asian-American Postal Employees Association, and the National Alliance.

The initial meeting was held in December 1998; the second meeting took place in August 1999. The Coalition provides the opportunity for these groups to discover mutual concerns and pursue common goals. The idea for the coalition was originally conceived and established by members of the Board of Governors to address present and future concerns of these groups within the Postal Service. Both Governors Tirso Del Junco and LeGree Daniels have attended and participated in Coalition activities. We plan to reconvene the group in February 2000 to evaluate progress to date and provide a forum for ongoing dialogue and future collaboration.

52. Last year the Postal Service reported that it was implementing the new Voice of the Employee (VOE) survey because it feels that a direct "voice of the employee" is a critical input to its decision-making. At that time the Service reported that three management associations and two of the four unions were cooperating in the survey process. The Service expected that a significant number of employees would respond to the survey.

(a) *Please update the Subcommittee on the status of the Voice of the Employee Survey. Was the survey conducted? Is so, what was the response rate?*

The VOE survey has been conducted quarterly since Quarter 4 of FY 1998. The response rates for the six surveys has ranged from 45% to 55%.

(b) *What information did it provide and was that information used as input into the Postal Service's decision-making process?*

Survey results were used by managers to better understand the workplace environment and to determine actions needed to address specific issues. Information from the survey results has also been used to identify areas for national focus with the intent of improving our workplace environment. This year, the Postal Service is tracking six key questions from the survey concerning supervisor behavior and recognition.

(c) *Which management associations and unions cooperated with the Postal Service?*

All three management associations and the Rural Letter Carriers have consistently cooperated with the Postal Service on the VOE survey process. The APWU and National Postal Mail Handlers Union have not cooperated. The National Association of Letter Carriers cooperated with the Postal Service on the Quarter 4, FY 1998 survey, but has not continued their cooperation on subsequent surveys.

(d) *Were the results of the survey released and to whom?*

The results are provided to all areas and performance clusters at the end of each postal quarter. At the completion of FY 1999, the results were provided to all plants and post offices Level 24 or larger.

53. In what some have characterized as a bold move, the Postal Service initiated the Priority Mail Redesign effort to "contract out" the processing and transportation of Priority Mail. In April 1997, the Postal Service awarded a $1.7 billion, 5-year contract to Emery Worldwide Airlines (EWA) to establish a network of 10 Priority Mail Processing Centers (PMPC) on the East Coast.

The OIG reported that: (i) Priority Mail processed through the network cost 23 percent (or $101 million) more than Priority Mail processed by the Postal Service without the network, and (ii) there were missed opportunities to reduce commercial air and diesel fuel cost.

The OIG noted that the additional costs of network operations may not be justified since there is only "minimal" improvement in service. In addition, the OIG reported that the contractor received financial relief that in the opinion of the IG eliminated or reduced the cost benefits cited in the original comparative analysis that justified the contract.

The IG made six recommendations to control cost, capture savings, and improve service. Management agreed with the recommendations but had differences of opinion on some of the findings in the report. The OIG recommended that management: (i) ensure that pending and future contract rate adjustments are settled after fully reconciling costs, contractor performance and the original terms of the contract and, (ii) address the cost and performance issues identified by the IG before any future expansion of the PMPC network.

(a) *In light of the OIG's review, what are the Postal Service's current plans and timetable for further outsourcing the handling of Priority Mail?*

No decisions have been reached regarding the further expansion of a dedicated network for handling Priority Mail, although several alternative scenarios are under consideration. As a result, the Postal Service has not established a timetable for further outsourcing the handling of Priority Mail at this time.

(b) *How is management responding to the recommendations contained in the OIG's report?*

As indicated in management's response to the report, the additional cost of handling Priority Mail through a dedicated transportation and distribution network was recognized at the time the pilot was approved. The Postal Service continues to regard the additional cost as an investment in improved service.

We do not agree with the IG audit report's characterization of the service improvement demonstrated in the pilot. Rather, we believe the pilot (Phase 1) network has shown us that we can achieve consistent service at competitive levels through a dedicated, centrally-managed network.

(c) *What is the status of the experiment for postal employees to operate a Priority Mail Processing Center as part of the negotiated settlement with the APWU?*

The Memoranda of Understanding which were agreed to with the APWU and the NPMHU during the 1998 contract negotiations called for the parties to "make every effort to reach mutual written agreement on modifications to the National Agreement's provisions that the Postal Service determines are necessary with respect to the terms and conditions of employment that will govern the employees employed at said PMPC."

Discussions are currently in progress with both the APWU and the NPMHU in an effort to reach such agreement.

54. Concern has been raised for the security of mail processed through the Priority Mail Processing Centers (PMPCs).

(a) *How many incidents of stolen and rifled mail were reported, investigated and confirmed in the PMPC network?*

The Postal Inspection Service does not currently distinguish PMPC contractors from other categories of contract offenders. Since the first PMPC became operational at Miami, FL, on August 30, 1997, nine additional centers have been added. To date, no significant problems have been attributed to the PMPC network that would warrant modifications to automated tracking systems to account for specific types of theft.

(b) *How many, if any, PMPC employees were disciplined and in what manner with regard to such incidents?*

A manual review of Inspection Service Case Activity Reports (CARs) has been requested to identify the incidence of mail theft and related disciplinary action at PMPCs since implementation. The results of that review will be furnished to the Subcommittee upon its completion in approximately two months.

(c) *Compared to other postal operations of the same size and nature (i.e.- the number of packages) would you consider the PMPC network more or less secure? Please provide statistics to support your response.*

All PMPC sites follow security protocols similar to those in use at all postal owned and operated facilities. They include: 1) a network of surveillance cameras (Criminal Investigation System) that allow Postal Inspectors to monitor all mail processing activities; 2) a requirement that all incoming and outgoing mail be placed in sealed containers for transport; 3) a facility access control system; and 4) a requirement that all employees undergo a pre-employment screening to determine their suitability for employment.

55. The Subcommittee is interested in getting the Postal Service's view on how well the PMPC network is performing. In addition, the Subcommittee would like assurances that volumes and contractor performance is properly measured.

(a) *What were the service performance levels for the PMPC network in FY 1998 and FY 1999?*

While we recognize the Subcommittee's interest in evaluating the effectiveness of the Priority Mail Processing Center network, the Postal Service considers Priority Mail service performance data and contractor reliability index measures to be highly confidential business information.

As you know, responses to Subcommittee questions generally become part of the public record and, therefore, become available to our customers and competitors alike. In addition, we are concerned about unilaterally releasing data that may compromise the competitive position of Emery Worldwide (the PMPC contractor). The Postal Service proposes working with the Subcommittee staff to provide the data within a privileged environment that will protect both the Postal Service's and Emery Worldwide's business interests while allowing the Subcommittee to review the data.

(b) *Please report the number of PMPC service failures and the number of pieces.*

See the response to Question 55(a).

(c) *Is a separate contractor reliability index developed for each of the ten PMPCs? Is so, what were the scores for each of the PMPCs for FY 1998 and FY 1999?*

See the response to Question 55(a).

(d) *Is the contractor reliability index developed in aggregate for the whole PMPC network? Is so, what were the scores for FY 1998 and FY 1999?*

See the response to Question 55(a).

(e) *How often is the contractor reliability index calculated (e.g. – by accounting period, quarterly, or annually)?*

See the response to Question 55(a).

(f) *How often did the failures exceed four percent of the mail (less than 96 percent on-time) and a disincentive was assessed to the contractor?*

See the response to Question 55(a).

(g) *How often were failures less than three percent (more than 97 percent on-time) and an incentive was paid to the contractor?*

See the response to Question 55(a).

(h) *What were the total penalties assessed and incentives paid for FY 1998 and FY 1999?*

See the response to Question 55(a).

(i) Please discuss the challenges that Postal management faces in measuring volume and service performance in the PMPC network.

See the response to Question 55(a).

56. Last year the Postal Service stated that Priority Mail capable of receiving one-day service continues to travel on surface transportation as it did prior to the implementation of the Priority Mail Network. In addition, you noted that the expansive reach of this integrated pilot program network increases the number of Priority Mail one-day service commitments.

(a) What were the number of Priority Mail pieces that received one-, two- and over two-day service for FY 1998 and FY 1999? Please show the figures broken out four ways: (i) pieces originating and destinating in the network, (ii) pieces originating in the network and destinating outside the network, (iii) pieces originating outside the network and destinating in the network and (iv) pieces originating and destinating outside the network. Please provide a breakdown of the commitments broken down in the same manner.

See the response to Question 55(a).

57. Last year the Postal Service indicated that because you activated the PMPC pilot sites just before the busiest time of the year, you experienced start-up problems which led to delays in service. You stated that you were implementing a plan to address the lessons learned.

(a) Has that plan been implemented and, as a result, to what extent have you been able to avoid difficulties, particularly in the 1999 holiday period?

We assume the question's reference to the "1999 holiday period" refers to Fiscal Year 1999, or last year's holiday period in December 1998, which was actually the second holiday season experience under the PMPC contract.

In the first holiday season under the PMPC contract, FY 1998 (December 1997), serious problems did occur for the reasons stated in the question's preamble. Capitalizing on lessons learned from that experience, planning for the FY 1999 holiday period began earlier and was more thorough. The contractor increased the size of both the air and surface transportation fleets, the number of employees, the amount of equipment, and the square footage of work space acquired to handle the seasonal volume.

As a result of these measures, there were no significant service failures during the FY 1999 holiday season, as there were in the FY 1998 holiday season. Overall, any problems encountered were due to bad weather and surging volume, which are normal for the time of year, highly localized, and of short duration.

Carrying forward into this year's holiday mailing season, which will be the third year of operations under the contract, we anticipate continued improvement and even fewer problems.

58. Under the leadership of the Department of State, the U.S. government has made a number of proposals in Beijing that would have the effect of: (1) opening up the Universal Postal Union (UPU) to all U.S. stakeholders; (2) moving terminals dues toward a cost-based system, and; (3) facilitating the free flow of mail among private and public operators.

(a) *What is the Postal Service doing to support reform of the UPU mission, structure and management to increase participation of interested parties and better reflect the differences between the governmental and operational responsibilities of the UPU?*

The State Department has the policy lead on UPU reform. The USPS supports U.S. policy by providing State with technical advice and by facilitating contacts with other postal administrations. The USPS provides advice on how the UPU works and on the culture and perspectives of UPU members. The USPS makes recommendations on how to gain support for U.S. policy by integrating and balancing proposals for reform with support for universal service. Finally, the USPS helps explain the U.S. reform agenda to other UPU members, solicits their support, and provides feedback to State on the concerns and reactions of UPU members.

(b) *What is the Postal Service doing to support the development and full implementation of a cost-based terminal dues system?*

The Postal Service played a leadership role in the financial analysis work that led up to the successful adoption of a cost-based terminal dues system at the UPU Congress in Beijing in September 1999. Under the new UPU system, mail exchanges between industrialized countries (ICs) will be country-specific and based on a percentage of domestic rates in the destination country. This will put some 85 percent of the world's international mail volume under a cost-based system.

The Postal Service will also play an active role in the further development and implementation of such a system in the coming years. With the leadership of a UPU Postal Operations Council Terminal Dues Project Team, the Postal Service will support efforts to develop a more comprehensive cost-based terminal dues system for the UPU that would lead to inclusion of developing countries (DCs). The USPS is also collaborating with State, the Postal Rate Commission, and other agencies on the terms of reference for an independent study of Article 40 and terminal dues issues.

It should be emphasized, however, that progress in introducing a country-specific cost-based terminal dues system required acceptance of a two-tier structure, with participation in the cost-based system limited, at least initially, to industrialized countries (ICs), and with DCs continuing to be compensated on the basis of a global average cost system. This two-tier structure, in turn, has been challenged by Australia and New Zealand as being incompatible with World Trade Organization (WTO) principles, specifically MFN (Most Favored Nation) treatment. Australia and New Zealand have indicated that they will be competitively disadvantaged by having to pay ICs at the UPU country-specific terminal dues rates while neighboring developing country competitors will be able to access industrialized countries at UPU global average cost rates. Both countries made declarations upon signing the UPU Acts expressing reservations about participating in the terminal dues structure for ICs. It is possible, therefore, that on or both of these countries, perhaps joined by others, will attempt to continue settling accounts with other ICs on the basis of the global average cost system or will attempt to apply WTO dispute settlement mechanisms to resolve this matter.

The USPS is considering a two-track approach in response to the potential issue of WTO compliance. First, it will support efforts to bring developing countries into the cost-based terminal dues structure. Second, it will encourage Australia and New Zealand to support the two-tier structure, at least on an interim basis.

(c) *What is the Postal Service doing to ensure that the delivery of mail exchanged between industrialized countries and mail sent from industrialized countries to developing countries is not delayed by administrative procedures when properly compensated for?*

The Beijing Congress amended the regulations to relax the restrictions that caused delays of mail rerouted through third countries (so-called ABC remail). The Postal Service supported that amendment. The Postal Service itself does not currently apply these regulations to inbound mail from such countries and therefore does not cause any delays. The Postal Service will continue to work towards more compensatory terminal dues arrangements that will reduce the need for such administrative procedures.

(d) *How has the United States benefited from its participation in the UPU? Can you explain the relevance of this organization to postal patrons in this country?*

The UPU provides a forum for all countries of the world to come together and agree on arrangements to support universal mail service. Participation in the UPU permits the United States to reach agreement with other countries on types of services to provide, on standards, on compensation levels, and on operational and accounting procedures for mail exchanges much more efficiently than if the U.S. had to pursue separate bilateral arrangements with 188 UPU member countries.

As a result of the international mail network supported by UPU members, postal customers in the United States have access to standardized, affordable mail services to communicate with family, friends and businesses around the world.

(e) *Please list all Postal Service officials and staff by job title that attended or traveled to the UPU Congress in Beijing. Describe their specific duties and responsibilities at the Congress and denote who was on the delegation.*

The following U.S. Postal Service officers served on the U.S. delegation:

Officers -- Week 1	
Henderson, William J.	Postmaster General, Chief Executive Officer (5 days) Alternate Head of Delegation
Del Junco, Tirso	Member, Postal Service Board of Governors (5 days)
Corcoran, Karla	Inspector General (5 days)
Elcano, Mary S.	Senior Vice President and General Counsel (7 days) Regulatory Policies, Postal reform, Committee 3, General Debate
Kane, Allen R.	Chief Marketing Officer and Senior Vice President (7 days) Marketing Policies; World Conference on Direct Mail and Customer Day; General Debate
Willhite, Deborah K.	Senior Vice President, Government Relations (5 days) Regulatory Policies; General Debate
Grubiak, James F.	Vice President, International Business (5 days)
Reisner, Robert A.F.	Vice President, Strategic Planning, General Debate (5 days)
Ward, John H.	Vice President, Finance, Controller (5 days) Panelist on Payment Services Debate, General Debate, Finance Strategies
Conrad, Michael	U.S. Postal Inspector, PMG Security Detail
Lin, Sam	U.S. Postal Inspector, PMG Security Detail
Week 2	
Lewis, Clarence E.	Chief Operating Officer, Executive Vice-President (6 days) Operations Policies, Committees 4 and 6
Weeks 3 and 4	
Durazo, Jesse	Vice President, Area Operations, Pacific Area (9 days) Asia/Pacific Relations; Officer coverage for Weeks 3 and 4, Committees 4, 6 and 7

Entire Duration

Hunter, Kenneth J.	Chief Postal Inspector Chairman, Congress Committee 6 Chairman, UPU Postal Security Action Group (PSAG) Security of the Mails Policies
Porras, M. Richard	Chief Financial Officer and Senior Vice President Chairman, Postal Development Action Group (PDAG) General Debate, Committee 8 presenter, World Bank and Postal Sector Reform; Financial Policies

The following U.S. Postal Service managers, experts and support staff served on the U.S. delegation:

Duration of Congress:

Regan, Michael	Director, International Postal Affairs, Deputy Head of Delegation, Responsible for overall management of USPS participation in the UPU, Chair of CA Committee 1, Chair of the Direct Mail Advisory Board, Chair of the UPU-Private Operators Contact Committee, Designated to present proposals to Congress on behalf of CA
Alvis, William	Attorney - Committees 2, 3, 4 and 7, Legal Counsel on USPS international and UPU issues; Counsel to EMS Cooperative Chairman of the UPU Working Party on Recasting the Acts; Designated to present proposals to Congress on behalf of CA
Chandler, Peter	International Postal Affairs Specialist – Committees 2, 5 and 8, UPU budget; technical cooperation and Postal Development; quality of service; International Business Reply Service, delegation logistics
Delehanty, Dennis	Program Manager, EMS - Committees 3, 4, 6 and 7, Chairman, EMS Cooperative; Coordinator of US delegation positions; UPU policy issues
Emerson, Lea	Program Manager, UPU Policies – Committees 2, 3, 4, 6, UPU policy issues; Terminal dues policies; coordinator of CA issues, Presenter of Congress proposals on behalf of the CA
Grandjean, Walter	Program Manager – Committees 4, 5, 6, Mail Classification issues; UPU Convention issues; Responsible for writing USPS regulations to conform with New UPU Acts
Hill, Donald	Inspector in Charge, International Security Group, Postal Security Action Group ;(PSAG); support for U.S. chairmanship of Congress Committee 6

Ho, Eunice	Purchasing Specialist, Chinese-English translation and interpretation, delegation office support, logistics, USPS officer support
Levy, Allison	International Postal Affairs Specialist – Committees 3, 4 and 7, Parcel post; Prime-Exprès, Support for U.S. chairmanship of EMS Cooperative; Terminal Dues accounting and statistics issues
Wittman, Eliane	International Postal Affairs Specialist – Committees 5, 7 and 8, Officer schedules and programs; US Delegation coordinator; World Conference on Direct Mail; payment services; quality of service
Weeks 1 and 2 only	
McClung, Flori	International Postal Affairs Specialist, French and Spanish translation and interpretation; PUASP coordinator, logistics support; officer support
Weeks 2 and 3 only	
Alepa, John	Manager, International Pricing – Committees 4, 6 and 8, Chairman, Financial Analysis Team of POC Terminal Dues Working Party; Int'l rates and pricing, terminal dues financial issues, World Bank cost accounting project
Alvino, David	Manager, International Mail Operations – Committees 4, 6 and 8, Operations; Policies; Spokesman for USPS operations positions; quality of service
Barnwell, Patricia	Accountant – Committees 4, 5 and 6, International Postal Accounting and financial issues; Payment issues;
Shipman, George	Manager, Commercial Systems, Chairman, Technical Standards Board; Congress Committee 6; Telematics Cooperative

The following U.S. Postal Service officials participated in the World Direct Mail Conference and Customer Day held in conjunction with the UPU Beijing Congress. They did not serve on the U.S. delegation.

Anita J. Bizzotto	Vice President, Marketing Systems
John R. Wargo	Vice President, Customer Relations
James Wade	Manager, International Marketing & Sales
Robert Michelson	Manager, Mail Order, Moderator of Conference
Patrick McAfee	Manager, Marketing Research, Conference Panelist

Linda Craig Wilson	Program Manager, Direct Mail Advisory Board
William Johnstone	Managing Counsel, International & Ratemaking Law
Terrell Carter	Assistant Treasurer, Payment Technologies
Kaye DeShields	Manager, Retail Products and Services
Robert Chambers	Deputy Inspector General

(f) *Please provide for the record the total travel and administrative expense of participation in the Congress including all events and preparatory meetings such as the Council of Administration, Postal Operations Council and Regional Round Tables.*

The total travel and administration costs of preparation for and participation in the Congress are estimated to be $556,000. Costs of USPS participation at Meetings of the Council of Administration, the Postal Operations Council, and the Regional Round Tables were not included in this total, since these events addressed traditional UPU working issues not directly related to the Congress.

59. The U.S. submitted a proposal to reform the UPU through an Extraordinary Congress in 2001 to study on the mission, structure and management of the Unio work. It recognized the need to increase participation of interested parties in the UPU government policies and that the opening of domestic markets to foreign service suppliers should be made in accordance with principles derived from the World Trade Organization and the General Agreement on Trade in Services. The proposal noted that the UPU structure could better reflect the differences betweer the governmental and operational responsibilities and recommended that the UPU Acts be revised to reflect an expanded role for the UPU with respect to the activiti of all operators, public and private, while continuing to provide a basis for membe countries to assure the provisions of a universal service on a global scale. The U recommended cooperation with the World Customs Organization, including the possibilities for extending simplified postal customs clearance procedures to simil. shipments carried by all operators, public or private, and for revising the Kyoto Convention accordingly. The proposal noted the UPU should assure that other interested parties, including organizations representing users of postal services a private operators, are also consulted and given an opportunity to contribute. Although the U.S. proposal was not adopted in Beijing, a compromise was reache whereby an Extraordinary High Level group of some 15 countries were to study these issues. In addition, a plenipotentiary meeting some time before the next Congress in 2004 may consider recommended changes.

(a) *Will the Postal Service give its fullest cooperation to support the goals of U.S. pos policy as embodied in the U.S. resolution on Postal Reform as presented in Beijin*

Yes.

(b) *What will be the impact of the Universal Postal Union's new agreements on international mail rates and the quality of international mail service? Was progress made that will benefit the United States?*

The UPU's new agreement on international mail handling and delivery charges, i.e., terminal dues, represents a departure from previous UPU terminal dues arrangements. The new agreement moves all industrialized countries into a cost-based terminal dues system with country-specific, per item and per kilogram charges, initially based on 60 percent of domestic tariff with rate caps that gradually increase over a three-year transition period and a floor rate that will be held constant. This formula is more indicative of the costs associated with each individual country's mail flow. Further studies to be undertaken by the newly formed Terminal Dues Action Group (TDAG) will address whether the proportion of 60 percent of domestic rates should continue to apply to all industrialized countries or be scaled according to country-specific, cost-to-tariffs relationships. Terminal dues payments to developing postal administrations will remain unchanged, based on the worldwide flat rate of 3.427 SDRs per kilogram.

The agreement also established a quality of service fund to be financed by a 7.5 percent add-on for mail sent from industrialized to developing postal administrations. This fund will be used to help finance network development and service improvement projects in developing countries. This will benefit U.S. mailers who should receive faster and more reliable delivery for their mail items sent to developing countries. In principle, terminal dues payments for mail exchanges between industrialized countries may be linked to quality of service performance in the destination country after a study is conducted by the POC. It is believed that with the application of a suitable measurement mechanism of service performance, the global network will be improved and U.S. mailers will benefit from higher levels of mail service.

In strict financial terms, the impact of the new agreement will be a general increase in our international LC/AO rates through the transition period (2001-2003), especially to certain industrialized countries with higher domestic postage rates. There will also be a gradual expansion in the number of rate groups to accommodate a widening range of charges paid to industrialized countries.

A further new feature of the UPU terminal dues system is the provision for access to domestic postage rates in destination countries (domestic access). This new system could lead to lower international postage rates for qualifying mail entered directly into the destination country's domestic mail stream at rates reflecting volume and worksharing discounts. The consequence, therefore, could be overall increases in rates for single-piece mail that would not qualify for the offsetting price reductions resulting from the domestic access provisions of the terminal dues system.

(c) *How has United States benefited from its participation in the UPU? Can you explain the relevance of this organization to postal patrons in this country?*

See the response to Question 58(d).

(d) *What were your impressions at the UPU Congress in Beijing, China? What is your view on the issues regarding UPU reform?*

In general, the Congress in Beijing made progress in areas relating to the financing and development of the global postal network and the opening up of the UPU to wider private sector participation. The key issues in Beijing included terminal dues; service quality and the development of the global postal network; and reform of the Universal Postal Union, including opening up the UPU to wider private sector involvement.

On terminal dues, the Congress approved a separate terminal dues structure for exchanges of mail among industrialized countries. This new structure will more closely align terminal dues with domestic costs and rates in industrialized countries. On service quality, the Congress established a new Quality of Service fund to be financed by a 7.5 percent increase in the terminal dues rate for mail se from industrialized to developing countries. This fund will be used to help finance network development and service improvement projects in developing countries.

On UPU reform, the Congress approved two measures. First, it established a High Level Group to develop reform recommendations within a two-year time frame and to consider calling for a special plenipotentiary meeting to act on these recommendations prior to the next regularly scheduled UPU Congress in Abidjan, Côte d'Ivoire, in 2004. Second, it called for the establishment of an Advisory Group to be made up of non-governmental organizations (NGOs) that would represent private sector interests to the UPU.

All members of the U.S. delegation to the UPU, including postal members, were disappointed that representatives of the International Express Carriers Conference (IECC) were not admitted to key meetings during the Congress. The IECC had been invited by the 1999 UPU Council of Administration to attend the UPU Congress in Beijing as observers. The opportunity for improved dialogue and mutual understanding was diminished by their inability to participate. This outcome was not completely surprising, however, as the role of the UPU in respect to competition between universal service providers and other operators not sharing universal service obligations or other service obligations under the UPU Acts is still not clear. The decision in Beijing to constitute a High Level Group to pursue UPU reform on an urgent basis demonstrates recognition by many UPU members of the importance of this issue and the need for more analysis and better preparation to deal with it.

(e) *Please describe for the record the text of each U.S. proposal, the goal of each proposal as the Postal Service understands it, and the results of the vote on each proposal.*

The following are the results of the U.S. proposals submitted at the UPU Beijing Congress:

Proposal	Subject	Result
019	Flexible financing of UPU activities (This was a proposal by the UPU Council of Administration based on U.S. proposal to the Council)	Passed by vote (Yes-113 No-8 Abstain-5)
033	Continuation after the Beijing Congress of study on the mission, structure and management of the UPU work	Referred to the High Level Group per Congress resolution C 110
20. 0. 17	Codes used to identify exchange offices	Referred to forms subgroup of Standards Board
20. 0. 18	Publication of list of UPU compendia in UPU Manuals	Passed by consensus
20. 0. 24	Study on the color of the CN 22 Customs declaration	Amended version passed by consensus
20. 0. 31	Study on accounting-priority and airmail transit à découvert	Passed by consensus
20. 24. 2	Harmonization of carriage of hazardous materials in the UPU Convention with current provisions in the UPU Parcels Agreement, in conformance with IATA and ICAO regulations	Passed by consensus
20. 24. 91	Consequence of proposal 20. 24. 2.	Passed by consensus
20. 26. 3	Additional charge for return of undeliverable items	Passed by vote (Yes-90 No-62 Abstain-30)
20. 40. 4	Relaxation of restrictions on Article 40 "Posting abroad of letter-post items"	Rejected by vote (Yes-36 No-62 Abstain-31)
20. 41. 3	Harmonization of regulations concerning the carriage of hazardous materials in the UPU Convention with IATA and ICAO regulations	Passed by consensus
35. RE 301. 1	Consequence of proposal 20. 24. 2.	Passed by consensus

The following are the U.S. Proposals considered at the Postal Operations Council (November 22 – December 1, 1999 in Bern, Switzerland):

Proposal	Subject	Result
25. RE 201. 3	Expand the types of contents permitted in M bags (bags of international mail to a single addressee)	Amended version passed by vote (26-Yes)
25. RE 205. 2	Definition of sender of bulk items to specify that sender is originator of mail, not sender's agent or contractor	Rejected by vote (10-Yes)
25. RE 409. 3	International Business Reply Service accounting charges	Deferred to 2000 POC
25. RE 807. 4	International Business Reply Service letter bills	Deferred to 2000 POC
25. RE 832. 2	Provision to allow origin administration to indicate the eventual disposal of empty bags	Passed by consensus
25. RE 1015. 2	Transit charges and terminal dues accounts	Passed by consensus
25. RE 1018. 3	Required documentation of payment of transit charges and terminal dues	Passed by consensus
25. RE 1106. 5	Required documentation for settlement of general accounts between administrations	Passed by consensus
25. RE 1305. 1	Publication of UPU circulars to notify changes in addresses to which payments are to be made	Passed by consensus
29. 31. 2	Consequence of proposal 25. RE 832. 2.	Passed by consensus
29. 32. 3	Consequence of proposal 25. RE 832. 2.	Passed by consensus
35. RE 307. 4	Return of undelivered parcels by surface mail	Rejected by vote (20-Yes)
35. RE 617. 2	Provision to allow origin administration to indicate whether empty receptacles should be returned	Amended version passed by vote (29 in favor)
39. 78. 2	Additional box for verification note	Passed by consensus
45. RE 501.1	Add POST*Net electronic international money order process into Regulations	Passed by consensus

Note: At the POC, only "Yes" votes were counted; 21 votes were required to pass a proposal.

(f) What efforts did the Postal Service expend alone or in concert with the State Department to gain support for each proposal including but not limited to speeches, briefings, and meetings?

The most significant policy-related proposals that the U.S. formally submitted to the UPU Congress in Beijing were proposal 033 seeking comprehensive UPU reform and proposal 20.40.4 seeking to amend "remail" provisions in paragraph 4 of Article 40. In concert with the State Department, Postal Service officials worked diligently in the months leading up to Congress, as well as during Congress, to gain support for the U.S. position on these and other key policy issues. Prior to Congress, the Postal Service briefed and consulted postal and regulatory officials in other key UPU member countries in a number of bilateral, multilateral and regional meetings. These meetings included a conference of Caribbean postal managers in Miami hosted by the Postal Service; the Caribbean Postal Union Conference (CPU) held May 31-June 4 in Jamaica; the Postal Union of the Americas, Spain and Portugal (PUASP) Consultative and Executive Council Meeting held June 14-18; and a Beijing Congress Preparatory Conference hosted by the Postal Service in Potomac, Maryland, on July 14-15, which brought together postal operators and regulators from a number of influential UPU member countries to discuss significant policy issues. Subsequent to the meeting in Miami, five Caribbean UPU member countries decided to co-author selected U.S. proposals of a technical nature, which broadened the base of support for these proposals.

As a result of an intensive two-month policy review process, in mid-May, the U.S. government adopted a position to amend the ABC remail provisions of Article 40 (paragraph 4). With only one month remaining before the June 22 deadline to submit proposals to the Congress with the requisite support of eight other countries, the Postal Service contacted nearly 60 key countries to seek support for the U.S. proposal. One week prior to the deadline, the U.S. had only received formal support from three countries, despite numerous follow-ups on attempts to gain more support. The Postal Service succeeded in garnering the necessary number of countries in time to meet the deadline by conducting a number of informal meetings with a large number of member countries in the regional PUASP meeting held in Mexico. Going into Congress, the U.S. had 16 countries expressing formal support, while 12 countries confirmed non-support. Despite further attempts to brief other countries and seek support of the proposal during Congress, the amendment fell by a vote of 36 for, 62 against, and 31 abstentions. Perhaps this result was a reflection of the relatively low priority given to this U.S. proposal compared with the other key U.S. delegation priorities at Congress (i.e., proposal 033 on UPU reform, the Dutch Consultative Status proposal, and the IECC observer status issue).

During the Congress, the Postal Service worked in concert with the State Department on developing talking points on U.S. reform proposals. A series of talking points and position papers were given to each member of the U.S. delegation primarily on three key issues: 1) U.S. proposal 033 calling for a study on reforming the UPU; 2) the Dutch Consultative Status proposals that would open the UPU further to private sector participation; and 3) IECC observer status at meetings of Congress. The State Department and the Postal Service worked together to develop and implement a comprehensive plan to seek support from other countries, giving specific country assignments to key Postal Service personnel. The Postal Service arranged for the Head of Delegation to give a presentation of the U.S. position on reform to the 26 members of the PUASP regional union at the Conference held during the Congress. The Postal Service also identified the key countries for the Head of Delegation to contact personally as these countries usually influenced the voting block positions of several regions.

As part of its preparations for Congress, the Postal Service developed position papers and talking points for all U.S. proposals to Congress, as well as position papers for all 507 proposals put forward to Congress.

(g) *How do you see the modernization efforts of some foreign postal administrations, such as Deutsche Post or the Dutch TNT, impacting U.S. postal operations and rates?*

These Posts have clearly adopted more aggressive entrepreneurial and commercial strategies on regional and global levels, enabling them to adapt their services and prices to market conditions more effectively than other more heavily regulated postal administrations.

The U.S. market itself has become an increasingly attractive target for the commercialized Posts since the Postal Service ceased to apply the Private Express Statutes to outbound international mail more than a decade ago. These Posts are pursuing acquisitions and alliances in the U.S as part of a global strategy to gain customers and market share and to push larger volumes of traffic through regional and global networks.

As a result of the entry of more and more players in the U.S. outbound international mail market, the Postal Service has experienced declining international volumes and revenues over the past few years, adding increased pressure on costs and prices. However, we are reorganizing our international activity to control costs, counter these trends, and to improve international service offerings.

60. Questions have been raised as to how effectively the Postal Service enforces customs regulations.

(a) *Please describe how you ensure that all imported mail products, including letters and packages, comply with U.S. Customs requirements, including the payment of duties and other fees.*

The Postal Service is responsible for presenting all classes of mail from all foreign destinations for U.S. Customs inspection at locations designated by U.S. Customs. If any mail item is assessed duty by U.S. Customs, the Postal Service has the responsibility to collect the duty and associated fee(s) from the addressee.

(b) *Please estimate your accuracy in collecting and remitting all appropriate dues and fees on all imported mail products, including letters and packages, to the U.S. Customs Service.*

All duty and associated fee(s) are collected directly from the addressee using the existing accounting practices of the Postal Service. The collection of assessed duties and associated fee(s) are done prior to release of the item to the addressee.

61. On June 30 the Postal Rate Commission issued its initial report to Congress on the costs, revenues, and volumes of international mail handled by the United States Postal Service. The report analyzes fiscal year 1998 information. The Commission found that the data provided by the Postal Service are generally reliable.

The PRC reported that all international mail combined generated revenues equal to 112.9 percent of its attributable costs. In contrast, all domestic and international mail combined generated revenues equal to 158.3 percent of its attributable costs. Competitors of the Postal Service have argued that International mail rates are cross-subsidized by domestic revenues. It appears to some that a 112.9 percent cost coverage is unjustifiably low when compared to the system-wide average of 158.3 percent.

(a) *Does the 112.9 percent overall cost coverage for international mail demonstrate that there is no cross-subsidy of international rates by domestic ratepayers?*

Yes.

(b) *Does the Postal Service consider any cost coverage greater than 100%, even a cost coverage of 101%, for international products and services, as a whole, to be sufficient to prove no cross-subsidy?*

Yes.

(c) *How does the Postal Service justify such a low overall cost coverage for international products and service relative to the system-wide average cost coverage given the fact that over 80% of international mail is non-competitive?*

All international mail is subject to competition. This competition traditionally has produced more competitive pricing and lower cost coverages. Also, the cost coverage for outbound services was 130.6 percent, which is the more relevant comparison. First, inbound cost coverage results in part from factors that are beyond the control of the Postal Service. Second, overall international cost coverage reflects costs that are incremental to international, but are not a consequence of providing any specific international product. There is no analogous cost category for domestic mail services.

62. The PRC's Report to Congress on International Mail reveals that Global Priority Mail has a cost coverage of much less than 100% for FY 1998. According to the report, the Postal Service believes the contribution to institutional costs will improve because of expected reductions in advertising expense that accounted for the lion's share of product specific cost in FY 1998 and because of the 14 percent average rate increase that was effective in December 1998.

The Subcommittee is curious as to why the Postal Service would spend so lavishly on advertising a product with a relatively small volume. A significant proportion of the cost per piece for GPM was for advertising. In fact, over forty percent of your GPM cost was for advertising. In contrast only 1% of Domestic Priority Mail cost was for advertising. Granted, advertising a product is intended to increase volume and revenue but the advertising expense for this product seems absolutely inappropriate.

(a) *Is Global Priority Mail now covering its cost?*

Yes. As indicated in the question, advertising expenses were a significant part of the attributable costs of Global Priority Mail in FY 1998. We felt this advertising was necessary to publicize and launch this product. Expansion of the GPM's acceptance points and destination's price increases, and a reduced need for advertising, has resulted in profitable operations in FY 1999 and FY 2000.

(b) *Did the Postal Service conduct market research that indicated that market response to Global Priority Mail would be sufficient to justify such a large advertising budget?*

No market research was done regarding the particular advertising expense in FY 1998. Given the subsequent volume and revenue growth, however, it would appear that the GPM advertising program has been successful.

(c) *If so, has that market research been reviewed, since it appears that it may have been flawed?*

See the response to Question 62(b).

(d) *Does the Service attribute the cost of its direct mail advertising of its products and services to those products and services? Please provide the FY 1998 and FY 1999 cost of such advertising by product and service including costs for direct mail advertising for Global Priority Mail.*

The Postal Service attributes advertising costs that are identifiable to specific products to those products. We do not separately identify direct mail advertising from other media.

63. Global Priority Mail service is limited to only nineteen countries and, unlike Domestic Priority Mail which can be mailed up to 70 pounds, is limited to items less than 4 pounds.

(a) *Was the fact that GPM is a limited product offering factored into the projections of the market response to advertising? If the Postal Service did not conduct such market research, who decided that the Postal Service should spend so much on advertising Global Priority Mail?*

Advertising is part of the process of launching any product. While GPM is still a relatively new product (begun in March 1996), it has experienced financial success and now more than covers its cost. GPM service has been expanded to 22 additional markets bringing the current total to 41 countries.

64. The PRC's Report to Congress on International Mail reveals that Global Package Link (GPL), another competitive international product, had a cost coverage of significantly less than 100%. In its defense, the Postal Service claims that this is a result of an economic slowdown overseas. In addition, the Postal Service believes it has corrected the situation by recently increasing GPL rates by 9 percent and will implement some unspecified cost reductions. But a review of the history of this product might indicate why revenues failed to cover cost, at least in FY1998. This product which was originally called International Package Consignment Service was implemented December 22, 1994, offered service only to Japan, required that the mailer be within 500 miles of the JFK facility in New York and tender a minimum of 25,000 pieces in one year to each country. Supposedly these requirements were set to keep the unit cost of the service low to justify the rates. But since that time the Service has progressively lowered these minimums and lessened the requirements in such a manner so as to increase the unit cost without concurrent rate increases. In addition, the Subcommittee has heard that perhaps some mailers were not even meeting the new lower piece minimums. As with Global Priority Mail, the Subcommittee is concerned that management did not properly review the cost implications of its actions, in this case changing the mailing requirements.

(a) *Is Global Package Link currently covering its cost?*

GPL did not cover its costs in FY 1998. Final data for FY 1999 are not yet available.

(b) *Does the Postal Service estimate the cost impacts of changing international mailing requirements before they are implemented? If not, why not?*

Yes.

(c) *Did the Postal Service analyze the cost implications of changing the mailing requirements for Global Package Link?*

Yes, the Postal Service analyzed the costs for both this organization and the mailer.

(d) *Did all GPL mailers meet minimum piece requirements? In the event the minimum piece requirements were not met how was the Postal Service made whole? Was the mailer, for example, charged the full rates for the equivalent service for their GPL pieces that year?*

No. Section 622.11 of the *International Mail Manual* (IMM) provides that a mailer's failure to send 10,000 packages a year to all destination countries may result in the Postal Service terminating the right to mail packages as GPL. Pursuant to this section, the Postal Service works with mailers to determine their future mailing volumes and whether they will meet the minimum. As part of this review, several mailers have stopped shipping internationally and have stopped using GPL.

The Postal Service is currently reviewing the minimum requirements and is considering changes to the *IMM*.

65. In March of 1999 the Postal Service reported that it formed an "alliance" with DHL Worldwide Express. The Postal Service then launched Priority Mail Global Guaranteed -- a two-day 'documents only' service to 19 countries in Western Europe available from 11 metropolitan areas. The vice president for Package Services claimed that "the link with DHL gives the Postal Service the flexibility it needs to keep pace with the demands and rapidly changing requirements of the international market." In addition, he noted that "by coupling with a world-class provider, the Postal Service gains immediate access to an infrastructure it needs to meet customer demand." On November 1 the Service expanded PMGG service to 46 originating markets and 65 destinating countries.

(a) *What has been the market response to Priority Mail Global Guaranteed? What has the volume been since the service was introduced? Has the service met expectations? What percent of items were delivered on time? How many customers received a refund for not meeting the guaranteed delivery?*

Customer response to Priority Mail Global Guaranteed (PMGG) has been extremely positive and exceeded even the best of our expectations. In these first formative months, the shared USPS-DHL goal for PMGG has been to provide a service that achieves a high level of customer satisfaction. As such, internally tabulated raw numbers on delivery times and guarantees will not measure the success of this service since each case is different. On the whole though, on-time delivery scores have been very high and refunds few. Future customer satisfaction indexes will determine the future of this program.

66. In a recent letter to the Chairman the Senior Vice President of Government Relations noted that through the expansion of PMGG service "the Postal Service is strengthening its international presence and better fulfilling its congressionally mandated mission of delivering written and printed materials throughout the world." The Postal Service already has many service options for sending written and printed materials throughout the world. This includes Internal Airmail, Priority Airmail, Global Priority Mail and Express Mail as well as surface options for non-time sensitive written and printed material. The Subcommittee would like to understand why the Postal Service feels obliged to add another premium option at a high price of $23 to a limited set of countries, a service that is offered by many other U.S. service providers.

(a) *Has the Postal Service conducted any market research that indicates that there is a significant unfulfilled demand for a two-day guaranteed international product such as PMGG? If so, please summarize the results of the market research.*

The Postal Service believes that it must provide customers with reliable, credible, value-priced services in all legitimate venues and markets. Many Americans look to the Postal Service for safe, secure, and trusted communications and view us as the preferred delivery provider.

The significant erosion of our international express mail service in recent years made it clear that we were not meeting the needs of our customers. Given this fact, we realized that we needed to move forward quickly to improve this service. PMGG was the result.

(b) *What are the financial goals for PMGG? Does the Postal Service anticipate that PMGG will increase net contribution to overhead and approximately by how much?*

The prices for PMGG are designed to cover the costs incurred both by DHL and the Postal Service. More specific financial goals will follow as we gain experience with PMGG and demonstrate that it is a reliable service that gains customer confidence.

(c) *Was PMGG subjected to the 5.1 new product review process? Has PMGG revenues covered its startup costs yet?*

PMGG was subjected to the Strategic Alliance guidelines discussed in Questions 67 and 69. These guidelines incorporate some elements of the *CustomerPerfect!* review process.

Since PMGG was implemented less than a year ago, it has not yet recovered all of its investment costs. PMGG is priced to cover its operating costs and recover investment costs over time.

67. According to Postal Service guidelines a "business alliance" is a cooperative agreement between the Postal Service and a private entity to share property and/or personnel in the development and/or marketing of a joint product.

(a) *What is the true nature of the "alliance" with DHL? Specifically, does the Postal Service pay DHL for the delivery of items on a per-item and/or a per pound basis? Does the alliance share revenue from the product sales based on an agreed upon formula?*

The Postal Service's relationship with DHL Worldwide Express, Inc., is a strategic alliance entered into pursuant to the Postal Service's Strategic Alliance Guidelines, a copy of which is provided in response to Question 69(a). Consistent with those Guidelines, prices are set for PMGG that are designed to cover the costs incurred both by DHL and the Postal Service, with revenues in excess of costs being shared by the parties.

(b) *How do you respond to competitor accusations that the Postal Service/DHL alliance represents a form of collusion by postal monopolies since the German Post (DPDG) has an equity interest in DHL?*

It is common knowledge that Deutsche Post has a 25 percent stake in DHL International. The Postal Service has entered into an alliance with DHL Worldwide Express, Inc., an entirely separate entity. We believe that DHL International owns a minority stake in DHL Worldwide Express, but that relationship is unclear because DHL is a privately held company.

It is possible, therefore, that Deutsche Post could benefit in some small way by this alliance; however, that certainly does not constitute collusion between the Postal Service and Deutsche Post.

For example, United Parcel Service owns a stake in Tumbleweed Communications, which helps the Postal Service and other organizations conduct secure online communications. UPS may benefit indirectly from Tumbleweed's relationship with the Postal Service, but that does not constitute collusion.

68. Competitors have claimed that the Postal Service's alliance with DHL underscores the need for tighter controls on Postal Service forays into private-sector competition and the handling of its profits from the monopoly.

(a) *How do you respond to these charges?*

We do not agree with these claims. If private sector competitors have such concerns, however, they would do well to support H.R. 22, which seeks to address the issue of fair competition in a comprehensive and constructive way.

69. The Vice President for Package Services has been quoted as saying, "the future in the international arena is a series of international alliances." Some have argued that such alliances are laudable in that they will create competition among private operators and foreign postal administrations. Such alliances might indicate that the Postal Service is simply operating in a business-like manner in the interest of the American consumer. On the other hand, competitors of the Postal Service view such alliances as an anathema on the separation of government and private sector interests.

(a) *Does the Postal Service have criteria to judge whether business alliances are justified from financial, operational, service, and public policy reasons?*

Yes. A copy of the business alliance guidelines is attached (Attachment 7).

(b) *Where does the Postal Service "draw the line" between its status as a government agency and its interest in generating revenue when it comes to forming business alliances?*

The criteria in the business alliance guidelines direct the Postal Service in its decision-making on this issue.

70. Since the establishment of the International Business Unit in June of 1995 contribution to institutional cost from international mail has steadily declined from $360 million in FY 1996 to $273 million in FY 1997 to $185 million in FY 1998. This represents a 24% decline from FY 1996 to FY 1997 and a 32% decline from FY 1997 to FY 1998. These declines are unprecedented in the area of international mail. The Postal Service had high revenue targets for its international business when the IBU was created. As a result it staffed up to realize these great expectations. As recently as June of 1998 the PMG and Governor Dyhrkopp characterized the IBU as a "fledgling" business. Nonetheless, at the very least, one might expect the IBU could maintain the pre-IBU contribution to institutional cost. The Subcommittee would like to better understand the degree to which the Postal Service, admittedly in hindsight, may have overestimated the business potential for international services and, as a result misdirected its scarce resources to a declining business segment.

(a) *To what do you attribute the decline in contribution to institutional cost?*

These comparisons are misleading. The FY 1996 and FY 1997 contribution figures cited reflect USPS costing methodology. On the other hand, the FY 1998 contribution figure is based on PRC costing methodology, which – all other things being equal – results in significantly more attributable costs and correspondingly less contribution than does USPS methodology. The FY 1998 USPS Cost and Revenue Analysis indicates only a 5 percent decline in contribution between FY 1997 and FY 1998.

(b) *To what extent is this decline the result of (i) decreases in volume (ii) increases in attributable cost per piece (iii) increases in the incremental cost per piece (iv) increases in the IBU-related incremental cost and (v) declines in revenue per piece?*

See the response to Question 70(a).

(c) *International mail volumes have declined each year since 1996. Why are international mail volumes still declining? What is the Postal Service doing to reverse this trend?*

Recent volume declines are likely the result of a number of factors including: economic slumps abroad and the diversion of mail to remailers, private competitors, and electronic alternatives. To reverse this trend, the Postal Service plans to become more efficient and price more competitively.

(d) *What was the contribution from International mail for FY 1999?*

That information will not be available until March 2000. We will provide it to the Subcommittee at that time.

71. It has been reported that the Postal Service plans to open new International Service Centers (ISCs) in Oakland, San Francisco, and Los Angeles in 2000. The construction and outfitting of these new buildings in support of international mail service represents a significant investment by the Service in its international business. These plans are moving forward despite the decline in international volume. The director for the Postal Service's Strategic International Business Group for California is quoted as saying, "The new international processing plants provide California with the facilities and equipment needed to process international mail for the expanding global economy. They will enable the Postal Service to provide excellent service to our international customers while expanding our global business capacity."

(a) *What is the status of the International Service Centers program given declining international volumes? Isn't further investment in this area like "building a bridge over a dry river?"*

The International Service Centers were built both to grow business and to improve service levels. These centers will both enhance and modernize our operations, and we still consider these investments sound business decisions. For more information, see the response to 72(a).

72. The Office of the Inspector General has pointed out that the international revenue forecast used, in part, to justify the creation of the International Business Unit was inaccurate and that revenue goals were unrealistic. The comprehensive statement shows that $16 million is projected to be spent on the ISCs.

(a) *Are the costs of program still justified? Has the Postal Service established baseline service to determine whether the ISCs improve service? Has implementation of the International Service Center program resulted in improved service performance?*

Yes, the cost is still justified because of the service improvements they provide to our customers.

The Postal Service has established baseline service. Service performance is measured from deposit to delivery through the Unipost External Measurement system of UNEX (managed by the International Post Corporation, a consortium of 21 postal administrations).

The Postal Service has service data back to 1997. In January 1997, the performance for letter mail sent by U.S. customers to foreign postal administrations stood at 43.7 percent on time for mail sorted by the New York ISC and 31.5 percent on time for Dallas. In January 1999, those results had improved to 66.2 percent and 70.7 percent, respectively.

In September 1997, New York's outbound results stood at 65.2 percent and Dallas at 65.3 percent. In September 1999, New York had improved to 82.9 percent and Dallas to 84.2 percent.

Service performance is better now for mail going through New York ISC and Dallas ISC than it has ever been. Continuous improvement is expected as the rest of the ISC network is implemented.

73. The Postal Rate Commission's Report to Congress on 1998 International Mail Volumes, Costs and Revenues shows expenses for the International Business Unit of $52 millions that cannot be attributed to any class, subclass or rate category of mail and is included in international mail incremental cost. The Subcommittee is interested in the nature of these overhead costs and to what extent they may have contributed to the recent poor financial performance of international mail.

(a) *How many Postal Career Executives were assigned solely to international mail in June of 1995 just prior to the establishment of the IBU? How many Postal Career Executives are currently assigned to the international business unit?*

In June 1995, the Postal Service had one Vice President and six PCES managers assigned to international mail issues.

As of December 1999, the Postal Service had one Vice President and 16 PCES managers in its International Business Unit.

(b) *How many Executive and Administrative Schedule employees were assigned solely to international mail in June of 1995 just prior to the establishment of the IBU? How many Executive and Administrative Schedule employees are assigned to the IBU?*

In June 1995, there were 53 EAS employees. In December 1999, the IBU had 84 EAS employees, including one PCES employee in an EAS position.

(c) *Please report the annual cost for international travel and expenses for each year from FY 1990 through and including FY 1999. Please report the total cost of the office and facility space for the IBU for FY 1995 through and including FY 1999.*

Fiscal Year	Travel/Expenses	Office/Facility Space
1990	not available	
1991	$400,660	
1992	$905,250	
1993	$508,020	
1994	$575,026	
1995	$945,931	$254,636
1996	$2,148,314	$398,423
1997	$3,121,128	$587,813
1998	$4,109,349	$657,401
1999	$2,782,210	$655,810

Note: IBU travel constitutes less than half of the total for international travel.

74. It has been reported that the IBU has dropped the plan to create a "logistic service" for international customers but that the project, according to Postal officials, could be resumed.

(a) *What is the status of this project? How much has the IBU spent on developing this concept including salaries, benefits and travel expenses for managers and staff and total contractor supplies and service cost?*

An extensive analysis of the potential market for such services was performed with the support of a contractor. The total cost of this effort, which lasted approximately one year, was about $1.1 million in contracted services. The total salaries and benefits of the PCES manager and two EAS staff devoted to this project amounted to approximately $285,000. Travel expenses were about $15,000.

This project was completed in August 1997. No action has been taken on the results of this study to date.

75. In September 1998, the Office of the Inspector General (OIG) recommended that the Chief Financial Officer and Senior Vice President conduct a direct in-depth examination of the IBU to determine if the IBU is financially viable as a separate business unit. In response to the OIG recommendations, management argued that it was then too soon to evaluate whether the IBU should exist as a separate business unit. Management asserted that while generating increased revenue above the baseline was a goal of the IBU, there were a number of other premises on which the IBU was created. According to the Postal Service's Revenue, Pieces and Weight report, Total International Mail pieces when compared to the same period last year declined, 6.3% in FY 1998, 4.7% in Quarter 1, in FY 1999, 9.4% in Quarter 2, FY 1999 and 1 percent in Quarter 3, FY 1999.

(a) *Does the Postal Service still believe that after over four years it is still too soon to evaluate the financial viability of the IBU?*

The Postal Service reviews the performance and role of the international business unit annually and makes organizational changes as appropriate. The role of the IBU has evolved over time; it is now a smaller organization than in past years, focused on the marketing aspects of growing international revenues and contribution.

(b) *Considering the volume trends and contribution to institutional cost, why is the Postal Service reluctant to face the fact that a thoughtful and objective evaluation of the performance of the IBU is called for?*

See the response to Question 75(a).

76. In December of 1998 the Office of the Inspector General (OIG) made three recommendations to Postal management in the area of International Services (FR-AR-99-004).

(i) The OIG recommended that the Postal Service review sample designs to ensure that sample results yield sufficient data to produce reliable estimates of international mail. At that time management indicated that it had begun a review of all statistical systems underlying the measurement of international mail. The outcome was to be a list of specific design modifications with implementation of these design modifications this September.

(a) *Please provide the list of design modifications and whether these modifications have been implemented. Please indicate the degree to which these changes will increase the reliability of estimates of international mail.*

The design modifications include (1) increased use of mailing statement and other accounting/census data to enhance our estimates of revenues and volumes for outbound products; (2) use of weight controls by receptacle type to improve the precision of estimated inbound piece volumes in support of terminal dues settlement; and, (3) use of Electronic Data Interchange (EDI) data, exchanged between postal administrations, to improve the sample selection process for inbound mail. The first of these three design changes was partially implemented in FY 1999 and will be completed in FY 2000. The second and third design changes are currently being developed and will be implemented in FY 2000 and FY 2001.

(ii) The OIG recommended that the Postal Service evaluate the cost effectiveness of replacing current manual sampling procedures with automated solutions. Management cited some examples of how automation had been applied to data collection in the past and cited three technological advances that hold promise in this area (i.e., scanning product identifiers, electronic file exchange between postal administrations and use of POS data).

(b) *Please describe how the Postal Service has used automated solutions to improve data collection since the issuance of the OIG's recommendation.*

The scanning of mail type identifiers (i.e., letter trays, flat trays, bags) is being pursued aggressively in conjunction with a proposed change in the accounting of LC/AO weight exchanged between postal administrations. That proposed change would require the tracking and accounting of LC/AO weight by receptacle type. When implemented, this approach will greatly improve the estimates of inbound mail volume for terminal dues settlement purposes. The use of EDI information is also being pursued as an information source that would allow the automated selection of inbound mail receptacles for testing. We expect to see improvements related to these changes in FY 2000 and FY 2001.

(iii) The OIG recommended that the Postal Service emphasize proper sampling execution in the field. The Postal Service responded favorably to the recommendation and described efforts that had been undertaken to update manuals and improve training and communications. In addition, the Postal Service discussed plans to develop and release in May of 1999 a new Data Collection Users Guide for International Systems. In addition the Postal Service discussed plans to improve communications with the field through letters and to conduct other meetings, conferences and training sessions throughout the year.

(c) *Has a new Data Collection Users Guide for International Systems been released? Please discuss your efforts since the release of the OIG report to improve training and communications in this area.*

The new data collection handbook for the International Statistical Systems was released in June 1999. Also, a training initiative is underway to develop a structured, on-the-job training process for data collectors who conduct tests in our international statistical programs. This program, called the Process Activated Training System (PATS), was introduced in conjunction with our domestic programs. We expect PATS to result in increased data collector proficiency in our International programs in FY 2000 and FY 2001.

77. With regard to international mail the 1999 Comprehensive Statement stated: "1998 revenue fell in large part to three primary factors: 1) the adverse financial implications associated with the economic conditions in the Pacific Rim, 2) the entrance of foreign postal administrations into the North American market, and 3) the widespread use of the Internet and other forms of electronic diversion."

(a) *How much volume by mail category was lost as a result of each of these factors?*

The Postal Service has not quantified the separate effects of each of these factors on mail volume. It is clear that ISAL and GPL volumes were particularly affected by the Asian economic slump because a significant portion of the volumes for those products has always destinated in Asia. Single piece letter volume is vulnerable to electronic diversion, which is likely responsible for some of the decline in international letter mail. The decreases in letter volumes to Canada may be due in part to price increases for Canadian mail over the last decade. Finally, remailers have found niches in our price/cost structure where they can offer more competitive rates for certain types of mail.

(b) *Have these factors persisted through FY 1999 and to what degree? What strategies has the International Business Unit adopted to react to each of these factors?*

These factors appear to have continued to have an influence in FY 1999. As noted in our answer to Question 70, the Postal Service is working to become more efficient, reduce costs, and structure and price our services more competitively. For example, we recently instituted significant price reductions in our IPA product and have seen a significant growth in volume.

78. FedEx's premium service, International Priority, grew at a higher-than-predicted rate of 12% during the first quarter ending August 1999.

(a) *How did the Postal Service's equivalent product(s) perform in the same period?*

At this time, the Postal Service does not offer an equivalent service.

79. The International Mail Manual (IMM) states that "Licensed wholesalers or consolidators of foreign postal administrations or direct competitors of the Postal Service domestically or internationally that provide expedited or parcel delivery services or air transportation services are not eligible to be Global Package Link wholesalers." (IMM section 622.35).

(a) *Has the Postal Service fully enforced this eligibility requirement?*

Yes.

(b) *Has the Postal Service qualified any U.S. based international consolidator that is owned in whole or in part by a foreign postal administration?*

No.

80. The International Mail Manual (IMM) states that the Prequalified Wholesaler Program of the United States Postal Service (USPS) "will establish relationships between the USPS and wholesalers of international mail so that the business of both parties is increased through worksharing and volume pricing." (IMM section 631).

(a) *Please provide a technical definition of "volume pricing"? Are volume prices justified based on lower than average unit cost resulting from economies of scale and/or scope or are discounts based solely on volume requirements?*

Volume pricing is defined as a discount on the published rates for existing services. Discounts are provided for pre-qualified wholesalers for both of the reasons listed in the question. Operators have lower unit costs and must meet certain volume requirements.

(b) *To date how many operators have been prequalified as wholesalers?*

Twenty-two operators have been prequalified.

(c) *Please define the term "business" in IMM section 631? With regard to the Postal Service, does "business" mean contribution to overhead? If not, please explain what safeguards the Postal Service has in place to retain its contribution to overhead from international products and services.*

In *IMM* section 631, business means both revenue and total contribution.

(d) *Does the Postal Service have any mechanisms in place to evaluate the net impact of the wholesaler program on contribution to overhead?*

Yes.

81. On April 4, 1999, the Postal Service decreased rates for International Priority Airmail (IPA). In addition, the number of IPA acceptance points was expanded to any postal facility that accepts bulk mail. The Postal Service now offers some significant volume discounts to large IPA and ISAL customers. Postal rate reductions are not that common. In principle, rate reductions may be justified if postal costs decline significantly or the products and services have a price elasticity greater than one. At a time when the contribution to overhead from international products is on the decline, rate reductions seem to be ill advised unless there is clear evidence that they will generate compensatory increases in volume.

(a) *Were there significant reductions in IPA costs to justify rate reductions?*

Yes, IPA cost reductions were the principal justification for the price revisions that took effect on April 4, 1999.

(b) *If so, were the rates adjusted in such a manner as to be "contribution neutral", that is, was the price reduction based solely on a measured cost reduction?*

Rates were adjusted to take account of the cost reductions with the expectation that total revenue and total contribution would increase. Unit contribution is expected to decline.

(c) *If not, does the Postal Service have firm evidence that the price elasticity of this product is greater than one?*

Yes, the Postal Service does have evidence that the price elasticity of IPA is greater than one. The measure of IPA price elasticity has been tracked for several years. The most recent calculation is 1.237.

(d) *If these price reductions were neither cost-based or based on a measured (or assumed) IPA price elasticity greater than one, why did the Postal Service reduce these rates?*

See the response to Question 81(c) above.

(e) *Has the market responded as expected to the price reduction? How have volumes increased for each of the IPA rate groups and volume discount qualified customers since rates were reduced?*

The market response to the IPA price reduction has been quite positive. Overall, piece volumes have increased 42 percent, weight has grown 82 percent, and revenues have risen almost 10 percent. All statistics are on a cumulative SPLY basis since Accounting Period 8, FY 1999. Before and after rate group comparisons are not possible because the number of rate groups and country assignment by rate groups were revised effective April 4, 1999.

82. In its report "USPS Management of Personal Services Contracts" (March 29, 1999) the Office of the Inspector General reported that a personal services contract (102590-95-F-2406) to provide "professional expertise, leadership, and coordination in International Packaging Consignment Service" has increased from $82,400 to $352,226, a 327% increase, as of July, 7 1997.

(a) *How many individuals were paid under this contract? How much did each individual earn in each year of the contract? Please provide the total travel, lodging and meal expenses paid to these individuals. Please describe the duties and responsibilities of these individuals. What unique knowledge, skills and abilities did these individuals have that were not otherwise available to the Postal Service. Is this personal service contract still active?*

Only one person was paid under this contract. This individual was paid a total of $306,360, not $352,226. These payments covered a period from June 1995 to December 1997. From June 1995 through December 1995, payments of $34,271 were made. From January 1996 through December 1996, payments of $127,484 were made. From January 1997 through December 1997, payments of $144,605 were made. These payments include reimbursement for travel and other expenses. The total travel, lodging, and other expenses totaled $111,762.

This individual's duties involved discussing and finalizing international business opportunities with foreign postal administrations. The consultant has extensive experience in international relations and international business projects, skills that were critical in planning and coordinating partnership agreements with foreign postal administrations. His detailed knowledge of and experience with Postal Service products and services that IBU was proposing to implement in foreign countries, coupled with his ability to determine whether potential partners had the infrastructure necessary to support the IBU's proposed partnership activities, made him very valuable to the IBU initiatives. The consultant also understood the business culture of the countries the IBU was working with and spoke the appropriate languages.

This personal service contract is no longer active. The contract was closed when it expired in December 1997.

83. Concern has been raised regarding its use of government radio spectrum. Proposals in the House Commerce Committee show particular concern and interest in the issue.

(a) *Please describe how the Postal Service makes use of the government spectrum and whether and to what extent it is used to support the marketing, processing or delivery of non-monopoly postal products, such as parcel post.*

The government radio spectrum is critical to the effectiveness of the Postal Service and the safety of its employees. We use our nearly 3,000 radio frequency assignments on a daily basis. Virtually every processing plant, bulk mail center, air mail center, vehicle maintenance facility, and large post office has numerous frequencies that support important functions like processing, delivery, and maintenance.

The spectrum plays a key role in supporting the processing and delivery of non-monopoly products and services. Two-way radio systems are used to communicate, monitor, and manage the maintenance of Postal Service facilities in order to keep them operating in a safe and productive manner. The continual maintenance of sorting and mail processing equipment necessitates the need for communications to keep them operating at peak efficiency and limit downtime. Two-way radio communications are essential in assuring that the technicians are protected from harm while working on these large and cumbersome pieces of sophisticated equipment.

Government spectrum is extensively used in the delivery and transportation of non-monopoly postal products each day. Two-way radio equipment is employed in yard operations to help guide trucks to their proper bays within and around the facilities and to expedite unloading and loading of mail. Two-way radio systems also help direct support staff to the proper bays so they can load and unload mail for processing and transportation. This helps minimize idle time, fuel usage, and exhaust emissions by managing the flow of trucks in and out of a postal facility in an organized and efficient manner.

Two-way radios are also critical to the transportation of mail. Drivers communicate their position and status with two-way radio systems and advise on their anticipated arrival times so that facilities can plan to support the arrival of mail in the most efficient and expeditious manner. The drivers also use two-way radio systems to inform managers of mechanical malfunctions with their vehicles or any safety and health issues.

Two-way radio systems also support vehicle maintenance. Vehicle maintenance maintains communications with tow trucks and other vehicle maintenance elements to assure that any mechanical problems with the transportation system are remedied in the shortest time possible. The communications assure that the safety of personnel and the timely collection of the product are maintained.

The Postal Inspection Service uses more than 44 percent of the total radio frequencies. These frequencies are used on a daily and nationwide basis and are critical to protecting the safety of postal employees and ensuring the sanctity of the mail. They are the primary communications method for surveillance, license checks, hostage and assault situations, and undercover investigations into mail fraud, child pornography, theft, illegal drug trade, and other criminal activity. Inspection Service radio communications include two-way radios, body wires, and transmitters for tracking mail.

The Postal Service does not use the government spectrum for marketing purposes.

84. Proponents of this proposal argue that use of government spectrum gives the Postal Service an unfair advantage.

(a) *How do you respond to this argument?*

The Postal Service does not believe that its membership in the federal government's spectrum system and its participation in the Interdepartmental Radio Advisory Committee (IRAC) give it a competitive advantage. The following facts support our belief.

First, the Postal Service does not and cannot leverage its position on IRAC to benefit its competitive services. The National Telecommunications and Information Administration (NTIA) is responsible for assigning radio frequencies only for government use, not for commercial activities. By its very charter, the NTIA and IRAC would have no jurisdiction over the commercial use of radio frequencies used by any commercial carrier. In addition, the IRAC is an advisory board, not a governing body. The NTIA alone has decision-making authority.

Second, the Postal Service does not have easy access to frequency space within the government spectrum. The Postal Service must compete for spectrum space with a host of other federal agencies, including the Department of Defense. In addition, federal entities are often asked to share frequency assignments. Because the government spectrum is so crowded with users, the NTIA has mandated that all federal agencies narrow band their radio systems in the next few years to free up additional spectrum for the future.

Third, the NTIA is generally slower to grant licenses than the Federal Communications Commission (FCC). The NTIA takes as much as six to eight weeks to grant spectrum assignments. The FCC generally takes about three to four weeks to approve frequency requests of the same nature. In addition, the Postal Service is asked on virtually a daily basis to examine all new and modified government spectrum requests from other federal agencies to assure that these requests do not introduce harmful interference to current Postal Service assignments. This process involves substantial time and coordination with the other federal agencies. Commercial users, on the other hand, are not asked to safeguard frequency assignments for possible harmful interference from either new or potential users. The FCC performs this task for them.

Fourth, contrary to the claims of some competitors, the Postal Service does not obtain its licenses for free. As outlined in Public Law 104-134 of April 26, 1996, the Postal Service pays the NTIA for spectrum management, analysis, operations, and related services. According to a report prepared by the Congressional Research Service, it would be impossible to compare in any meaningful way the fees collected by the FCC to those collected by the NTIA because of the different rules and regulations governing FCC licenses and NTIA assignments.

85. Efforts are underway to keep the Postal Service away from the Internet to purportedly protect technology companies. Specifically, Representative Christopher Cox (R-California) has proposed to block the Postal Service from taking control of the .us domain. Various groups have endorsed this position claiming that private companies should oversee the management of .us addresses. In response, the Postal Service claims it is unfair to restrict the Postal Service from control of .us domain but indicated that it is not currently intending to seek control of the .us domain. Critics warn that the Postal Service does not have the expertise to run a top-level domain.

(a) *What are the Postal Service's current plans with respect to the .us domain? If the Postal Service intends to pursue a business strategy that involves .us domain, please indicate how that business strategy relates to its core mission. How do you respond to accusations that involvement by the Postal Service in managing the .us domain is inappropriate from a public policy standpoint?*

In the summer of 1998, the Department of Commerce asked for public comments on the enhancement of the .us domain space. Postal Service staff at Headquarters responded with its thoughts and ideas on August 17, 1998. The response was basically a placeholder with Commerce while our senior management examined the issue more thoroughly. The Postal Service's Management Committee later concluded that it had no interest in administering an Internet domain and decided not to pursue the effort.

86. The Postal Service intends to be involved in E-Commerce. Critics have questioned whether and to what extent the Postal Service should be engaged in Internet related products and services.

(a) *Please discuss how E-Commerce fits into the basic function of the Postal Service – to provide postal services to bind the Nation together through the personal, educational, literary, and business correspondence of the people, and provide prompt, reliable, and efficient services to patrons in all areas and shall render postal services to all communities?*

Over the past two centuries, the Postal Service has introduced a variety of innovations and service features that have boosted the effectiveness and relevance of the mail.

New options and services like adhesive postage stamps (1847), registered mail (1855), money orders (1864), international parcel post (1887), parcel post (1913), insurance (1913), collect on delivery (1913), airmail (1918), metered postage (1920), international airmail (1927), business reply mail (1928), certified mail (1955), Priority Mail (1968), Express Mail (1970), MAILGRAMs (1970), International Priority Airmail (1986), and delivery confirmation (1999) have made the mail a more effective communications tool for the American people. Bulk mail, presort, automation, and other worksharing discounts have also enhanced the value and targetability of the mail for business customers. Without these innovations, the mail's power and relevance to consumers, companies, and nonprofit organizations would be a shadow of what it is today.

Now, the rise of a new age of electronic interconnectivity presents new opportunities for the Postal Service to enhance the strength, convenience, and relevance of the mail. Our public Internet web site, for example, allows customers to buy stamps, find ZIP Codes, calculate rates, track packages, and obtain key information on the Postal Service and its range of services. PC Postage™, launched in August 1999, gives customers a convenient new way to pay for their mailings. A service the Postal Service plans to offer—the electronic postmark—would bring the security and integrity of a physical, government-sanctioned postmark to the realm of virtual messaging.

The Internet is changing how the nation shops and how businesses and government agencies operate and interact with the American people. The Postal Service owes its customers the most modern, convenient, and effective services it can provide. By extending the attributes of physical mail to the virtual world, we will ensure that the only medium that touches every American, every day will continue to fuel the nation's commerce and bind our nation together.

(b) *Under what specific power does the Postal Service believe it is authorized to enter E-Commerce business?*

We believe that it is appropriate for the Postal Service to engage in activities related to electronic commerce under the broad authority furnished by sections 403(a) and (b) and 404(a) of title 39. Those provisions direct the Postal Service to maintain a universal postal service and provide such other incidental services as it finds appropriate to its functions and in the public interest. In our view, electronic commerce activities are also appropriate under section 401(10) of title 39, which affords the Postal Service the incidental, necessary, and appropriate powers it needs to carry on its functions and exercise its specific powers.

(c) *Please discuss, even if in general terms, what types of products and services the Postal Service will offer as part of its E-Commerce business?*

The Postal Service is offering or planning to offer the following services as part of its eCommerce business:

- PC Postage;
- online stamp purchases;
- Digital Certificate;
- Merchandise Return;
- Electronic Postmark;
- PosteCS;
- Shipping Online;
- Mailing Online;
- hardcopy delivery of electronic messages.

(d) *Please discuss the nature and scope of business alliances that the Postal Service will form in support of its E-Commerce business?*

As we explore possible eCommerce opportunities, we plan to take full advantage of the best technology, current or emerging, in the marketplace. We will not discount any business alliance that brings to the marketplace a technological solution that best serves the American public.

(e) *Last year the Postal Service assured the Subcommittee that it would not be distracted from its core mission by venturing into electronic forms of communication. Does management intend to fill the position of Vice President of Core Business Marketing following the re-assignment of the incumbent to the position of Vice President of E-Commerce?*

Yes.

(f) *Please describe how the Postal Service intends to provide E-Payment service? What additional duties, responsibilities, staff and resources will the Treasurer take on now that he has the dual title "Treasurer and Vice President of e-Payments?"*

Stephen Kearney's title is Vice President, Treasurer and ePayments. In addition to his duties as Treasurer, he is responsible for exploring the electronic commerce market for potential opportunities by focusing on the unique value the Postal Service can bring based on interest from potential business partners and customers. Within Corporate Treasury, three managers and seven staffers lead this effort.

Corporate Treasury's electronic commerce focus will include the following areas:

Post Electronic Courier Service (PosteCS)
PosteCS is a joint effort between the International Postal Corporation (IPC) and the postal administrations of the United States, Canada and France. It is an Internet-based offering that securely delivers important documents using the USPS Electronic Postmark (EPM). Notification of document delivery is made via email for the recipients to pick up their electronic document at a secure Web site. Tumbleweed Communications currently provides the document delivery technology, which is integrated with the EPM.

Electronic Bill Presentment and Payment (EBPP)
EBPP is a new remittance channel that allows companies to deliver bills and receive payments over the Internet. Companies reduce bill preparation and mailing costs, check-processing costs, and float. Billers can either build an in-house system and bill customers directly or allow a consolidator to develop and run the systems. We are exploring our role in this arena.

(g) *Please discuss, even if in general terms, how, if at all, the Postal Service intends to link physical addresses with e-mail addressees.*

The Postal Service would create an electronic address that corresponds to each physical address. The link between electronic and physical address would augment our existing services and help bridge the digital divide by allowing the Postal Service to receive, print, and deliver electronic messages to those Americans without e-mail.

The electronic and physical addresses would be maintained in separate, secure databases. We would create a link between these databases with a unique and proprietary data structure that is designed to preserve the security of the information and provide appropriate consumer privacy protection.

87. There has been much controversy over whether the Postal Service should be allowed to offer "nonpostal" products. As reported by the GAO there is no statutory definition of a postal product. However, the courts and administrative decisions have held that products are considered to be postal if they involve an aspect of the posting, handling, or delivery of mail. H.R. 22 will clear up this confusion, but until then we have to live with the current working definition. As reported by the GAO, the Postal Service lost over $85 million on 19 new products from 1995 through 1997. These were nonpostal and international products and services that are not subject to PRC review. The GAO also reported that the Postal Service developed and subjected all new products to something called the *CustomerPerfect!* New Product Development Process since June of 1996.

(a) *Are the Postal Service's E-Business products and service being subjected to this process?*

The principles of the *CustomerPerfect!* New Product Development Process will guide the development of our eCommerce initiatives.

(b) *Will part of this process include a legal determination as to whether the proposed product is "nonpostal" or "postal"?*

Every new product or service is evaluated to determine whether it is subject to the ratemaking and classification procedures of chapter 36 of title 39.

In many cases, the Postal Service determines that the new product should be subject to that process and proceeds with an administrative filing at the Postal Rate Commission. In some instances, however, it is determined that the new product may be tested directly in the marketplace.

(c) *Will the Postal Service make a request that the Postal Rate Commission submit a recommended decision on changes to the mail classification schedule (Title 39, Chapter 36, Section 3623) for these new products and services?*

In every instance where it is determined that a new eCommerce service is subject to statutory ratemaking and classification procedures, the Postal Service will act accordingly.

88. In the early 1990s the Postal Service had great plans to enter the "E-Commerce" sector. The Postal Service went so far as to create a separate organization with a number of executive managers and support staff and spent a considerable amount of resources on product development. The GAO reported that "Electronic Commerce Services" did not generate any revenue and lost $20.3 million since its inception in 1993.

(a) *Did that organization successfully deploy <u>any</u> new product or service? Did that organization generate any contribution to the overhead of the Postal Service?*

In 1993, the Postal Service began to explore opportunities to provide electronic communications with the primary goal of leveraging its unique status as a trusted third provider of secure services. A group within the Marketing Department was established to execute this function. The group consisted of several postal managers and staff members and was augmented with contracted technical support to assist with the development of software for the Certificate Authority. The Certificate Authority was designed to provide security and privacy for electronic correspondence and transactions transmitted electronically. With the development of the Certificate Authority, the Postal Service would provide a system that administers and maintains digital signatures that are used to "sign" electronic communications.

With the rapid changes in technology during this time, however, it became increasingly difficult for the Postal Service to maintain the strategy of trying to develop this software in-house. Instead, the decision was made to take advantage of existing technology. At this point, a significant investment had already been made in research and development of the Certificate Authority.

The lessons learned from our experiences are proving to be very valuable in the rapidly changing electronic commerce environment, where time is of the essence. We are now using the Certificate Authority for PC Postage services and it also will be used for future e-Commerce initiatives. To date, the Postal Service has issued over 200,000 certificates for PC Postage customers.

In conjunction with the International Post Corporation (IPC) and the postal administrations of Canada (Canada Post) and France (La Poste), we have developed the Post Electronic Courier Service (PosteCS). PosteCS is an Internet-based offering that securely delivers important documents and offers USPS Electronic Postmark (EPM) service. This service was developed for business customers who are ready to use the Internet to securely transmit documents. PosteCS is designed to support global electronic communications and provide end-to-end security, confidentiality, and integrity for electronic communications. PosteCS provides customers with the ability to time/date stamp their messages and have the transaction signed with a digital signature. Additionally, recipients are able to verify the integrity of the document.

(b) *Has the Postal Service conducted any studies to draw out any lessons learned from that experience? If so, please discuss the findings. Are the lessons from that experience being applied to the Postal Service's recent efforts to develop E-Commerce?*

The organization did create the Business Evaluation group to provide oversight to the New Product Development efforts, evaluate business and financial performance, and validate Business Case assumptions. In the mid-1990s, the Postal Service was well ahead of most organizations in determining its role in eCommerce. We have learned that considering partnerships and alliances as an alternative to developing solutions in-house may, in some cases, be the best course of action for the Postal Service.

(c) *What became of the managers and staff who were hired from outside the Postal Service to develop "E-Commerce" products and services? Are some or all of those individuals involved in developing the Postal Service's "E-Commerce"?*

Three of the four managers and staff remain with the Postal Service; two are currently working within the eCommerce Group. The other manager left to head security at the New York Federal Reserve Branch.

89. At the oversight hearing last year the Chairman questioned the need for the rate increase given the huge surpluses run up by the Postal Service. In response the Postmaster General said that at the time the rate increase was proposed the Service had planned a "pretty significant" capital infrastructure spending program. The PMG said that the capital spending program was necessary to modernize the Postal Service. The PMG noted that most of the surplus in FY 1998 was the result of <u>not meeting those capital expenditure plans</u> and said that rather than spend the money he "let it hit the bottom line." He admitted that the plan was too ambitious.

(a) *In light of the PMG's previous testimony, is the Postal Service catching up to its planned spending on capital improvements?*

Since 1995, the Postal Service has taken an aggressive approach in the Capital Investment Plan. This plan provides for new technologies and investments that improve service, upgrade our infrastructure, and enable us to maintain affordable prices.

In FY 1994, our capital commitments were $1.6 billion dollars. With the new approach, the Postal Service committed $2.3 billion dollars in FY 1995, an increase of more than 40 percent. Since Fiscal Year 1995, our capital commitments have exceeded $3 billion dollars annually, with Fiscal Years 1998 and 1999 approaching the $4 billion dollar level. Our goal for FY 2000 is again to exceed the $3 billion dollar level.

(b) *Has the Postal Service taken any action to improve capital and program evaluation? Has the Postal Service taken any action to improve the annual budgeting process for capital programs?*

Yes, we are continuously improving how we plan for and implement our capital investments.

The traditional Capital Investment Plan is a five-year investment cycle. The first year represents the budget year, with the remaining four years targeted for planning purposes. In FY 1999 and 2000, we asked the Board of Governors to approve a one-year capital plan since this provides the organization with the flexibility to adapt to a changing business environment.

In the last few years, we have integrated our financing, capital, and expense plans into a *CustomerPerfect!* process that closely mirrors the Baldrige criteria.

Our performance in FY 1999 in capital commitments was only 4.5 percent under plan, while it was nearly 30 percent under plan in FY 1998. This performance improvement is the result of our continuing efforts.

(c) *Will the next omnibus rate filing revenue requirement include improved estimates of capital spending?*

Yes, any revised estimates of capital spending plans will be incorporated in the rate case development.

90. Some mailer groups are concerned that the Postal Service net capital investment as a percentage of operating revenues has dropped in recent years from a high in 1992 of 3.7% to a low of 1.2% in 1995. In 1998 the percentage stood at 2.5%. It has been recommended that net capital investment be increased to 3.7% as a percentage of total operating revenue as it was in 1992.

(a) *How do you respond to these concerns? Do you agree that these figures are useful indicators as to the appropriate levels of capital investment given current and future operating requirements?*

According to our records, the level of capital investment as a percentage of net operating revenue differs from the data cited in the question. In FY 1992, the level stood at 4.12 percent, not 3.7 percent. While commitments as a percentage of revenue did drop between 1992 to 1995, the percentage was 6.09 percent in FY 1999, an increase of more than two percentage points.

In any event, we prefer to use a different indicator, one that is used widely in the private sector. It is the ratio of cash flow from operations to capital expenditures, expressed as a percentage, which ties together our operating, capital, and financing plans. A result below 100 percent indicates that at least some capital spending cannot be funded from cash flow, but must be financed by borrowing or by reducing cash balances.

Companies push this ratio below 100 percent when they have the opportunity to make investments with a high rate of return, or when they are in a situation that requires investment in critical infrastructure to continue their business. In 1998 and 1999, our ratio was below 100 percent, which required increases in debt.

91. If the Postal Service hits its net income targets for FY 1999 and 2000, prior year losses would be reduced to $3.5 billion, a significant step toward restoring the financial health of the organization as envisioned in the Postal Reorganization Act. Some have argued that this strong financial performance, which is based on debt reduction, has come at the expense of much-needed capital investment including facility expansion to alleviate the reported overcrowded conditions in postal mail processing plants and delivery facilities. Some mailers claim that the Postal Service has invested a "paltry" amount to automate and upgrade its facilities.

(a) *How does the Postal Service determine the proper levels of spending on debt reduction and capital investment?*

Prior year losses have been reduced, dollar by dollar, by the amount of net income the Postal Service has earned in each of the five years since the end of Fiscal Year 1994.

During the same time period, the Postal Service has reduced its debt substantially, from $9.0 billion to $6.9 billion. For each of the past six years, we have borrowed only in amounts sufficient to maintain an adequate cash balance. In years when cash flows permitted us to reduce debt, we did so.

Capital Investments are determined in our integrated financial plan, which takes into account the capital, financing, and operating plan. The Postal Service has also created indicators relative to Capital Investments that serve as a guide when determining levels. One important indicator is the Cash Flow to Capital Cash Expenditures (CAPEX).

(b) *How do you respond to those who argue that debt reduction has been overemphasized to the detriment of responsible capital investment?*

We believe that managing Postal Service finances properly requires that we manage the amount of debt and interest expense on our books, that we continue to reduce prior year losses, and that we invest in our future. Achieving all three objectives requires some tradeoffs and difficult decisions, but we believe that we are managing our finances in a prudent fashion.

92. The Blue Ribbon Committee in its report "Finding Common Ground" recommended that the Postal Service invest more in information technology and increase and accelerate its capital spending to drive the business as well as to improve productivity.

(a) *What has the Postal Service done since the Blue Ribbon Committee issued its recommendations to introduce systems to track the movement of trays and containers?*

The Postal Service has several efforts underway for tracking the movement of trays and containers. We have recently completed concept testing of a tracking system utilizing Radio-Frequency-Identification (RFID) technology in several of our plants. This RFID system tracks unit loads from the time they leave a robotic sorting station at the originating site to when they reach two destinating facilities. The system uses small RFID tags attached to pallets or containers to automatically track the unit loads, and uses the Internet to provide real-time computer reports on mail status.

Barcodes represent the least expensive short-term method of uniquely identifying and capturing unit load data. Presently, our Engineering group is working on new tray labeling (including barcoding) requirements that will assist us in meeting our unit load tracking objectives.

Finally, tracking of unit loads (tubs, trays, sacks, and parcels) within the Integrated Processing Facility project is currently under discussion. Plans are consistent with the completion of proposed expansion and of current RFID/Barcode tracking operations and conclusions. It will provide tracking within and external to the plant in a near total automated environment.

(b) *What has the Postal Service done since the Blue Ribbon Committee issued its recommendations to reduce the unit cost of handling and delivering all classes of mail through increased capital spending?*

Based on recommendations of the Blue Ribbon Committee, the Postal Service has significantly increased its capital spending on technology designed to reduce and control costs. As an initial step, the Service streamlined its capital funding approval process by drastically reducing the time required to gain approval of viable capital equipment programs. As a result, our annual commitments in labor saving capital equipment programs have doubled during the last four years.

These capital programs have included a variety of technologies that help reduce costs for all shapes of mail—letters, flats, and parcels. Some programs have essentially completed our full-up letter automation program needs while others have enhanced the capabilities of existing equipment. Presently, we have about 12,000 automated letter sorting machines deployed throughout the country.

We have also finished deploying more than 340 new flats sorting machines and upgraded our exiting flat sorters with automated sorting capability. Our network of small parcel and bundle sorters now includes more than 340 machines and we have added automatic feed systems to the vast majority of these systems.

Finally, we have begun deploying various material handling technologies, including robotic and automated tray handling equipment, which help control the costs of handling containers of mail.

In FY 1999, a total of $1.2 billion was committed for equipment. A total of $1.4 billion is planned for equipment projects in FY 2000, which represents 37 percent of the total capital plan. Our core strategy for reducing costs and improving performance is to automate an increasing number of functions. The ability to perform tasks using equipment instead of manual labor not only saves work hours and associated indirect costs, but also allows for service improvements. The equipment category consists of investments in automation and mechanization that serves as the backbone of the initiatives to meet the business goal of strengthening our financial viability by managing costs.

(c) *How did spending on capital programs compare to the plan ($4.4 billion) for FY 1999? Please provide a comparison of plan to actual by major capital investment category.*

During FY 1999, our capital plan was reduced from $4.4 billion to $4.0 billion in response to our "Management Challenge." In FY 1999, the actual commitments were $3.8 billion.

FY 1999 Capital Plan ($ in millions)			
Category	**Actual**	**Plan**	**Variance**
Facilities	1,705	1,821	(116)
Equipment	1,158	1,113	45
Vehicles	285	266	19
Retail	194	209	(15)
Support	475	589	(114)
Total	3,817	3,998	(181)

(d) *Have the investments in technology and infrastructure resulted in measurable cost reductions and/or service performance improvements? Please present the results of your findings.*

Automation is revolutionizing mail processing operations as the Postal Service continues to invest in technology infrastructure to reduce costs, improve service, and increase operating efficiencies.

Through FY 1999, we estimate that our letter mail automation program has been responsible for cumulative labor savings of $16 billion. Viewed another way, last year it cost the Postal Service $57.64 to process 1,000 letters manually, $25.89 to process 1,000 letters on mechanized equipment, and only $5.20 to process 1,000 letters on automated equipment. Automation, along with process improvements, has also contributed to the dramatic improvements in service for First-Class Mail over the past several years.

93. In its recent report, U.S. Postal Service: Status of Efforts to Protect Privacy of Address Changes (GAO/GGD-99102, July 30, 1999), the GAO made specific recommendations to the Postmaster General on how to strengthen oversight of the National Change of Address NCOA program. The GAO recommended, as it did almost 3 years ago, that the NCOA office develop and implement written oversight procedures, and enforce all provisions of the licensing agreement. The GAO also recommended that the Postmaster General further restrict the use of NCOA-linked data to create or maintain new-movers lists by explicitly stating it on the acknowledgment form that is signed by customers of NCOA licensees.

The Postmaster General stated in his response that the Postal Service continued to believe that it is neither their legal responsibility nor the practical responsibility to regulate how the owners of mailing lists use those mailing lists once they have been matched against the NCOA database. He said that without an effective way to enforce the prohibition on the creation of new-movers lists, such as sending Postal Inspectors into mailers plants, revising the acknowledgement form to explicitly prohibit their use would be an "empty gesture". Your bottom line seems to be that since the prohibition can't be enforced anyway the Postal Service shouldn't even bother to inform customers that the practice is prohibited. It appears that the Postal Service's logic is a bit weak.

In commenting on your response, the GAO expressed the view that the challenges associated with enforcement should not preclude the Postal Service from notifying and receiving acknowledgement from licensee's customers that the use of the NCOA-linked data to create movers-lists is not permitted.

(a) *How does the Service explain its disagreement with GAO as to the legal requirement that the Service make every effort to protect NCOA-linked address change data from its improper use after it has been used to update mail address lists by the licensees?*

Our disagreement with GAO centers on the lawfulness of the development by customers of NCOA licensees of so-called "new movers" lists by the sortation of their own lists after correction with updated addresses from the NCOA file. GAO evidently believes that this is in conflict with the purposes for which the Postal Service collected the information, and therefore in violation of the Privacy Act. The Postal Service disagrees.

The practice of providing change of address information to the public for correction of commercial mailing lists began as early as 1924. Fifty years later, when the Privacy Act of 1974 came into being, the Postal Service established the requisite system of records for address change and mail forwarding records and adopted "routine uses", as provided for by the Act, to authorize the disclosures that were deemed necessary to postal operations.

One of these routine uses authorized the longstanding disclosure practice of providing change of address information to anyone upon request as a part of its address correction services. Similarly, the routine use that was adopted for change of address information in the NCOA database, which was instituted in 1986, states that "[d]isclosure of any customer's new permanent address may be made from the National Change of Address file to customers seeking corrected addresses for their mailing lists." This routine use is compatible with one of the stated purposes of the system, namely, "to provide address correction services to postal customers." The routine use does not by its terms place limitations on the recipient's use of its mailing lists. In addition, the Postal Service has not ever attempted, in the 75-year history of this disclosure practice, to control how a recipient uses change of address information.

The Postal Service believes that its NCOA program is in full compliance with the Privacy Act. It does not believe that the private sector development of "new movers" lists, which constitute just one of many kinds of specialized mailing lists, is either improper or illegal.

(b) *Assuming the legal responsibility issue is resolved, would you still argue that the lack of an enforcement mechanism still justifies not adopting a notification and acknowledgement requirement as recommended by the GAO?*

The Postal Service has not taken the position that the lack of an enforcement mechanism is what justifies its refusal to prohibit new movers lists. Difficulty of enforcement was simply offered as an observation about the realities of the mailing list industry. Also, the question is not so much one of "responsibility" as of authority. The Postal Service believes that it has no authority to prohibit private sector behavior that is neither unlawful nor contractually within its reach.

If it were really unlawful for private mailing list holders to break their NCOA-corrected lists down into more specialized mailing lists of recent movers, the Postal Service believes that simply obtaining the acknowledgement that GAO recommends would probably not be adequate to prevent "violations" or to absolve the Postal Service of responsibility for them.

94. The GAO also advised the Congress that it should consider amending the Postal Reorganization Act to address this issue. The Subcommittee would prefer that this issue be resolved without changing the law.

(a) *Can the Postal Service suggest any alternative course of action that would resolve this issue short of amending the PRA?*

The Postal Service regrets its disagreement with the GAO on this issue. We are opposed, however, to any legislation that would add substantially to the administrative problems or expense of the NCOA system, or burden the postal system with additional amounts of undeliverable mail.

95. The Point of Sales program is a major investment for the Postal Service that has great promise to improve retail operations and provide important information. The 1998 Comprehensive Statement detailed the deployment schedule for Stage 1 and Stage 2 during FY 1999. In the Postmaster General's statement he discussed information management as driving change in the management and delivery of retail services. He noted that the Service has deployed this year more than 22,000 of your next generation POS ONE retail terminals. He also noted that sophisticated handling systems are being deployed into your plants. He said that fully automated processing facilities and a computer driven information platform will revolutionize the way you manage the mail and create an information rich mail stream. But the Inspector General has found that the POS ONE system and the Tray Management System have had faulty system development practices and premature deployment. She found that this resulted in additional costs and that POS ONE did not fully meet desired results and benefits. The goals of automating retail and processing operations and developing an information rich mail stream are laudable but the Subcommittee is concerned, based on the OIG's findings, that perhaps there are problems in implementation that may prevent the Service from fully realizing its vision.

(a) *Has the Postal Service reviewed the findings by the OIG and taken any actions to more effectively manage the deployment of these important systems?*

Yes. Postal Service management is continually working to improve the POS ONE software and deployment process. The Executive Summary of the OIG issued Audit Report – Point of Service ONE (Audit Report Number DA-AR-99-002) dated September 20, 1999, stated: "Management agreed with our recommendations and has either taken or initiated the necessary corrective actions. Management's actions taken or planned are responsive to the issues raised in this report."

(b) *What feedback mechanisms are in place for personnel to report problems with new hardware and software?*

The POS ONE Program has several mechanisms in place to support the field with hardware and software issues.

The POS ONE Program has a Help Desk with a 1-800 number for users to report problems and receive assistance with operational issues. Both POS ONE and the respective vendors analyze Help Desk reports to:

- Identify specific software or hardware problems;
- Complete root cause analysis;
- Identify and schedule specific fixes related to problem areas.

The Help Desk also supports a field users group that provides feedback on the POS ONE system and the effectiveness of the Help Desk.

The Postal Service has improved the overall testing and certification process of the software and hardware. POS ONE has improved its feedback process from field users by implementing a pilot program that tests new hardware and software changes prior to general release.

(c) *Are field managers and staff actively engaged and consulted as new technology is designed, tested and implemented?*

All levels of Postal Service personnel, including managers and retail clerks, participate in the development, testing, and implementation of software and hardware changes.

The Postal Service has a small team of users located at the vendors' work locations that are actively involved in the design, development, and preliminary testing of changes. In addition, focus groups of POS ONE users are periodically formed to evaluate and provide feedback on new features during the design stage. An independent firm, with the assistance of POS ONE-field users, conducts functional testing for software and hardware prior to field release. The Postal Service has identified 20 pilot sites that test changes in the actual operating environment. Two weeks prior to software release, pilot sites provide daily feedback, which is essential for the final decision to proceed with a nationwide release.

(d) *Is POS ONE deployment on schedule as planned?*

The deployment is on schedule as presented to the Postal Service Board of Governors in a request for Stage 2A funding in June 1999. Stage 1 of the POS ONE project was originally approved in June 1996. Due to significant changes in the development process of the POS ONE system, an adjustment to the deployment schedule was made in May 1998, consistent with the funding levels approved by the Board of Governors. POS ONE has successfully been deployed in 4,000 retail locations. Further deployment is planned this year pending approval of funding for the next stage by the Board of Governors.

(e) *Is the POS data being warehoused?*

POS ONE data is being warehoused through the Retail Data Mart. The data mart began capturing sales and product information from POS ONE sites at the start of FY 2000. Every evening, data is transmitted from each site to the Postal Service's Computer Operations Service Center in Minneapolis. The Retail Data Mart is currently in pilot testing and targeted for production level processing in Quarter 4 of FY 2000. POS ONE will automatically capture sales and product data at the retail window for use by all levels of management and local field personnel. The Retail Data Mart will provide the capability for users to run queries for analyzing sales and product information.

96. The Subcommittee has heard anecdotal reports that the POS ONE system often locks up and, as a result, the retail operation shuts down.

(a) *Is there any truth to these reports and are there any contingency procedures for retail clerks to follow in the event of a lockup?*

It is unusual and extremely rare that a POS ONE system or all of the terminals in a retail unit would lock up at the same time. A POS ONE terminal occasionally experiences a freeze that requires users to reboot the system (approximately 5-minute process) or to call the POS ONE Help Desk for assistance. The majority of these occurrences are related to non-POS ONE issues such as power outages. In any event, there are contingency plans in place for continuing service to customers and a process for recovering financial information if the POS ONE system is inoperable.

97. In FY 1998 the Postal Service spent over $273 million on advertising. This is a rather large amount in absolute terms but relatively little for a $60 billion business in the service industry. Nonetheless, the question continues to be raised as to why a government agency needs to advertise at all.

(a) *How do you respond to those who argue that the Postal Service should not expend any funds on advertising?*

Given the highly competitive nature of the communications industry, coupled with increasing costs, the Postal Service needs additional revenue to hold down postage rates. That revenue growth is highly dependent on product and service promotion, as evidenced by the extensive advertising campaigns of our competitors.

(b) *Please describe the decision-making process used to establish the size of the annual advertising budget.*

During the annual budget call process, Product Managers and the field are asked to submit plans and budget requirements for the upcoming fiscal year. These requirements are considered in aggregate during the Deploy phase of the *Customer Perfect!* process. At this stage, management reviews resources available versus opportunity and the decision is made on the total level of advertising spending and allocation by product line.

(c) *Please describe the process for determining the funding levels for advertising individual products and services.*

See the response to Question 97(b).

98. In its 1998 Comprehensive Statement the Postal Service claims that the "What's Your Priority" advertising campaign was directly linked to the 16 percent increase for Priority Mail in volume share.

(a) *Please describe the methodology the Postal Service uses to directly link advertising campaigns to changes in market share.*

The statement in the *1998 Comprehensive Statement* concerning an increase in Priority Mail "volume share" actually refers to revenue growth rather than market share. In FY 1997, the first full year of the "What's Your Priority" campaign, Priority Mail revenue grew 16.1 percent. The Postal Service stated in its *1997 Annual Report* that "[w]hile we think our advertising campaign is responsible for a portion of this growth in volume and revenue, we also think that part of this growth was due to the strike at United Parcel Service."

Generally, sales are not attributed to any one single influence. Rather, they are influenced by a number of factors, including price, packaging, advertising, the economy, etc. In other words, the advertising may perform its role successfully, but the goal may not be achieved due to other non-advertising factors. To that end, we are in the initial phase of developing a statistical Sales Response Modeling (SRM) methodology to associate the impact of advertising to sales. SRM predicts sales response to individual market influences such as advertising, price, and distribution, competitive advertising, etc., by identifying how much each component contributes to sales volume.

(b) *Is the evaluation of the impact of advertising campaigns done by a neutral third party market research firm(s)?*

Advertising effectiveness is measured by Millward Brown International, Inc. (MBI), an independent marketing research firm. MBI specializes in advertising measurement and represents more than 50 percent of Fortune 100 companies. They are contracted by the U.S. Postal Service to conduct Sales Response Modeling. They also provide pre-concept and in market performance measures of USPS advertising effectiveness. Moreover, MBI is not associated with USPS advertising agencies.

99. In a recent speech before the National Postal Forum, PRC Chairman Ed Gleiman said the PRC conducted an analysis of the Priority Mail advertising campaign launched in the mid-90s. He said the analysis showed that volume increased but the resulting increase in contribution to institutional costs did not cover the cost of the advertising. "This means that, although volume increased," he said, "there may have been no overall financial benefit to the Postal Service." He cautioned that the Postal Service should carefully consider its return on investment with a new advertising campaign featuring "e-priority" mail service.

(a) *Has the Postal Service reviewed the PRC analysis of the Priority Mail advertising campaign? If so, does the Postal Service agree with the findings?*

The Postal Service has reviewed the PRC analysis of the Priority Mail advertising campaign; however, the Postal Service does not necessarily agree with its conclusions. The conclusions reached about 1998 appear to be extrapolated from an analysis of data for the period 1969-1996. In addition, the Postal Service has concerns and questions regarding the methodology used in the analysis. Modeling the impact of advertising on sales volume is an inherently difficult econometric exercise and may fail to capture less tangible effects of advertising including an enhanced brand image and the impact on other classes of mail.

(b) *What analysis has the Postal Service developed and applied to determine the appropriate level of advertising for "e-priority" mail service?*

See the response to Question 97(b).

(c) *Does the Postal Service judge the success of an advertising campaign by how much the campaign increases volume, revenue or net contribution to overhead? Which of these criteria is considered more important in measuring the success of an advertising campaign?*

Our goal is contribution to overhead. However, as noted in the response to Question 97(a), it is unrealistic to judge the performance of advertising solely on the basis of sales since sales are influenced by a number of factors. For this reason, we measure the success of advertising in terms of communications (versus sales) based on its purpose—to convey information and develop positive attitudes.

100. Some have questioned why the Postal Service spends money on advertising First-Class stamps since it has a monopoly.

(a) *How do you respond to these concerns?*

Like the U.S. Mint with its advertising of coins, the Postal Service promotes stamps as a hobby to grow the stamp collectibles business.

In addition to the approximately $200 million in net revenue generated annually from stamps retained and not used, postage stamps play an important role in documenting America's history. Promotional efforts surrounding First Day of Issue ceremonies also give us the opportunity to bring positive attention to the Postal Service and further increase awareness of stamp collecting.

(b) *Can the Postal Service demonstrate that advertising campaigns for First-Class stamps generate sufficient revenue to their cover cost and contribute positively to net income? If so, please provide the results of your analysis.*

Yes. The Postal Service spends between 3 percent and 3.5 percent of its annual advertising budget to promote stamp collecting as a hobby and to grow the stamp collectibles business. The net revenue generated annually by stamps collected and retained is $200 million. The advertising and promotional campaigns are focused on developing new collectors in order to keep this profitable business strong.

101. According to a survey released recently by the Colography Group the Postal Service share of the ground shipping market improved from 7.9% to 9.1% in 1997.

(a) *Did the Postal Service pay for the Colography survey?*

Yes. We have a contract with Colography to monitor the package business.

(b) *To what do you attribute the Postal Service's 2.2% increase in market share?*

It was mainly driven by the UPS strike in August 1997.

(c) *How is this increase broken down among the following market segments: business to business, business to household, household to household and household to business?*

The increase is primarily in the business to household segment.

(d) *To what extent have competitor surcharges for residential and rural delivery contributed to the Postal Service's increased market share?*

It has increased our volume in rural and residential areas, but only by a small percentage of the total increase.

102. Recent news articles have reported on customer dissatisfaction with the use of cluster boxes rather than door-to-door or curbside delivery.

(a) *What criteria does the Postal Service use in determining whether a new development receives cluster box rather than door-to-door delivery?*

The Postal Service makes every effort to provide our customers with convenient, affordable delivery services.

Postal Service policy provides a choice of two delivery options for customers in new delivery areas: centralized delivery or curbline delivery. Many years ago, customers in new delivery territories had the option of receiving door delivery service. Because of the rising cost of providing universal mail service, however, that practice was discontinued in 1978. As a comparison, the annual cost of providing door delivery is $243 per customer, compared with $154 and $110 for providing curbside or centralized delivery respectively. Because the Postal Service adds about one million new delivery points a year, the savings are substantial.

The only exceptions to this policy involve our hardship policy or fill-in situations. New deliveries in the same block where door delivery is already established are almost always extended as door delivery. In addition, we provide modified delivery to customers for whom existing delivery methods would impose an extreme physical hardship.

(b) *Please describe the procedures by which a customer who is physically impaired and unable to easily access cluster boxes can apply for and obtain an exemption allowing door-to-door or curbside delivery.*

The Postal Service recognizes that the location of mail receptacles may create a hardship for some customers. Changes in the type of delivery authorized will be considered where service by existing methods would impose an extreme physical hardship on an individual customer.

A request for a change in delivery methods must be submitted in writing to the postmaster. Approval of an individual customer's request will be based on humanitarian and not economic criteria. If the postmaster denies the request, it must be forwarded to the appropriate district office to ensure that our national policy has been properly applied.

(c) *How many of the exemptions described in (b) were sought in the past year? How many were granted?*

Because these decisions are made locally, no national database is kept to monitor how many exceptions are granted each year. In addition, there are cases where a hardship delivery is temporary, so the numbers are constantly changing.

103. With regards to the Triweekly Routes referred to at Sec. 651.4 of the July 16, 1998 Postal Operations Manual:

(a) *How many triweekly routes are there? What percentage of rural routes currently receive triweekly service?*

This information is not captured through any type of database or national system. A survey of areas and districts, however, identified a total of 346 triweekly routes. Eight are rural routes and the rest are Highway Contract Routes (HCRs) providing service to "rural" areas. Of the HCR routes, four were specifically reported as seasonal and/or operating on a 1- or 2-day per week frequency. Minor adjustments to these figures could occur as additional field information is received.

(b) *What percentage of rural routes currently receive triweekly service?*

Approximately 5.7 percent of Highway Contract Routes and .012 percent of rural routes are triweekly.

(c) *How many rural addresses receive triweekly service?*

A total of 17,697 customers receive triweekly service.

(d) *Have 6-day routes ever been downgraded to triweekly routes? What criteria are used to determine whether a downgrade in service is necessary? Is customer input sought?*

No instances of downgrades from 6-day to 3-day service were identified. There are no national criteria or regulations that provide for downgrading rural route customers from 6-day to triweekly service.

Our survey, however, did identify one route that was upgraded from 3-day to 6-day service, based on district criteria of total customer mail volume (pieces delivered and collected) greater than 100 pieces per month, per mile of route travel.

104. On March 14, 1999, the Postal Service finally raised the curtain on its Delivery Confirmation service for Priority Mail and Parcel Post. The retail rate is 35 cents for Priority Mail and 60 cents for Parcel Post. Rates are lower for customers who can send and receive Delivery Confirmation information electronically. For these customers, there is no charge for Priority Mail and a 25-cent charge for Parcel Select, Parcel Post, bound printed matter, special standard and library rate.

(a) *What has been the volume of delivery confirmation for retail and "electronic customers" since product inception?*

Fiscal Year	Retail Volume (000)	Electronic Volume (000)	Total Volume (000)
1999	12,451	16,340	28,791
2000 thru AP2 (11/5/99)	4,873	7,546	12,419
1999/2000			41,210

What has been the cumulative volume of delivery confirmation pieces for each of the mail classes listed above?

Fiscal Year	Priority Mail (000)	Standard B (000)	Total Volume (000)
1999	28,179	612	28791
2000 thru AP2 (11/5/99)	11,794	625	12,419
1999/2000			41,210

(All information is based on data starting with the , 1999 launch date through the end of Accounting Period 2, which ended November 5, 1999.)

(b) Has the customer response to delivery confirmation been below or above expectations to date?

Delivery Confirmation is generally meeting expectations. By any measure, it is fair to say Delivery Confirmation service has been a success attracting volume shippers and retail customers alike, recording over 41 million transactions in the inaugural eight months of operation.

(c) *What is the frequency of customer inquiries regarding delivery status of the items (i.e. – as a percent of total delivery confirmation volume)?*

The Postal Service allows customers access to delivery confirmation information in one of three ways: through the Internet, a toll-free telephone number, and electronic data files.

Unfortunately, we cannot provide a precise breakdown of the delivery confirmation inquiries made by customers because of the way these systems are set up.

For example, customers who originate 62 percent of the delivery confirmation volume can use electronic files supplied by the Postal Service, and we simply do not know how many inquiries are made through these files.

Through Accounting Period 4 of FY 2000, which ended December 31, we do know that 6.3 million inquiries were made either via the Internet or through our toll-free telephone number. However, some of these requests were made by postal employees.

(d) *What is the split between such inquiries made through the 800 number and the Internet?*

Of the 6.3 million inquiries mentioned in 104(c), 4.5 million came through the Internet and 1.8 million through the Call Center.

(e) *What is the most current scan at acceptance rate for delivery confirmation pieces?*

Delivery Confirmation service is intended to provide information about delivery. However, all customers who purchase Delivery Confirmation at a postal retail facility receive an acceptance scan. We currently receive approximately 80 percent of our retail items at these facilities.

(f) *What is the most current scan at delivery rate for delivery confirmation pieces?*

The current scan rate is 96 percent.

105. Last year you reported that you expect to meet the goals of the Energy Policy Act and Executive Order 12902. Specifically, a 20 percent reduction by the year 2000, based on 1985 levels and a 30% reduction in energy costs by 2005, also based on 1985 levels, respectively.

(a) *Is the Service still confident that you will meet these goals?*

We believe that the statement "a 30 percent reduction in energy costs by 2005" should be "a 30 percent reduction in energy consumption by 2005."

We achieved the 20 percent reduction goal for 2000 set by the Energy Policy Act of 1992. Our energy usage to date, excluding energy used in processing mail, has been reduced 20.9 percent relative to 1985.

Executive Order 12902 has been rescinded by Executive Order 13123 that sets a new energy reduction goal of 30 percent by 2005 and 35 percent by 2010 relative to 1985. Executive Order 13123 also sets a greenhouse gas reduction goal of 30 percent by 2010 relative to 1990 and goals for renewable energy and water conservation. The goals of Executive Order 13123 will be met assuming continued funding of energy projects and initiatives.

106. The Subcommittee has had many inquiries regarding double billing for magazine subscriptions, as in ordering to enter a sweepstakes. There are many instances where such duplicate billings, when a bill has already been paid, becomes a form of harassment. Dunning letters follow and the customer, client or patient, as the case may be, is compelled to issue another check -- many times out of fear of having a collection agency coming after their assets.

(a) *What role, if any, does the Postal Service have in such cases? Is there a law or regulation that covers fraudulent bills being sent through the mails? Is the Postal Service aware of an extensive or pervasive problem in this regard?*

The Inspection Service recognizes the potential for fraudulent activity by those companies that bill their customers over and over and threaten to forward the account to a collection agency. The Postal Service is charged with the enforcement of 39 U.S.C. 3001(d)(1). The Inspection Service Fraud Complaint System contains a specific category regarding false bills and solicitations in the guise of invoices. If the mailing is determined to be in violation of 39 U.S.C 3001(d) or the Domestic Mail Manual (DMM) provisions implementing that statutory requirement, the Postal Service may take administrative action against the violator. In FY 1999, the Inspection Service sent out over 2,500 letters to companies who were the subject of a false billing complaint. The DMM specifically outlines the criteria, such as the necessary language, font size, and color contrast, to be included on a proper invoice or billing notification. The DMM is available to the public at all post offices.

107. In its report USPS Management of Personal Services Contracts (March 29, 1999) the Office of the Inspector General reported that a personal services contract (104230-92-P-3543) "to support the remote barcode sorter team" has increased from $26,812 to $3,000,000, a 11,089% increase, as of January 26, 1998.

(a) *How many individuals were paid under this contract? How much did each individual earn in each year of the contract? Please provide the total travel, lodging and meals expenses paid to these individuals. Please describe the duties and responsibilities of these individuals. What unique knowledge, skills and abilities did these individuals that were not otherwise available to the Postal Service? Why did these contract costs increase so dramatically? Is this personal service contract still active?*

This was a competitive award to C&C Consulting for professional/personal services support originally issued to support the Remote Bar Code Sorter Team. Due to the 1992 restructuring and growth in workload (particularly large projects), which created occasional resource shortages, the contract was expanded to add various individuals with skills comparable to postal employees. These individuals supported Purchasing, Marketing, Engineering, and various other departments. There were 62 contract modifications made which added funds to extend periods of performance, added additional individuals, and dropped individuals when the additional resources were no longer needed. Payments were made directly to C&C Consulting, not to the individuals. The amounts include the company's markup. The amounts shown below reflect all expenses for each individual including travel, if any. The contract expired in August 1999.

Attachment 8 shows the individuals who worked under this contract.

108. In its report USPS Management of Personal Services Contracts (March 29, 1999), the Office of the Inspector General reported that a personal services contract (102590-96-F-1399) to provide marketing support services to stamp and product marketing to assist with the 1996 stamp marketing plan has increased from $72,500 to $569,500, a 686% increase, as of October 27, 1998.

(a) *How many individuals were paid under this contract? How much did each individual earn in each year of the contract? Please provide the total travel, lodging and meals expenses paid to these individuals. Please describe the duties and responsibilities of these individuals. What unique knowledge, skills and abilities did these individuals that were not otherwise available to the Postal Service? Why did these contract costs increase so dramatically? Is this personal service contract still active?*

This award was a professional/personal services contract awarded noncompetitively to Susan Isenberg Enterprises. The name of the organization was later changed to Planit International, Inc.

The purpose of the contract was to provide consulting and market support for programs such as Celebrate the Century and other special events for the stamp and product marketing department. The requirements office determined that Susan Isenberg was uniquely qualified through her experience to manage, coordinate, and support special projects and stamp marketing events. With the approval of management, the period of performance was extended several times, with additional funding added due to the need for continued services and the lack of postal resources. All contract extensions included work that was within the original scope of work for stamp marketing support. The total amount funded included travel expenses. The contract expired in May 1998.

109. The Office of the Inspector General issued an audit reported on September 21, Audit Report, Classification of Inspection Service Personnel Performing Audits (Report Number OV-AR-99-001). The report concluded that Postal Inspectors performing audits were not properly classified as criminal investigators. The OIG recommended that the Chief Postal Inspector establish controls to ensure that Postal Inspectors devote 50 percent or more of their work hours to law enforcement duties, or reclassify the positions to reflect work performed. In addition, the OIG recommended that the Vice President, Human Resources, should review Postal Inspectors' duties to ensure they meet the regulatory requirements of a law enforcement officer. Management concurred with the OIG's recommendations. The OIG deemed the corrective actions taken and planned by management to be responsive to the issues raised in the audit. The Acting Chief Postal Inspector stated in his response that it is "our intent to divest the Inspection Service of 'Yellow Book' audit work." In addition he stated that the Vice President, Human Resources, "has agreed to have her staff review the duties delineated in the postal inspector position descriptions." The Subcommittee would like to be assured that the Postal Service follows through and takes appropriate action.

(a) *Please provide action plan and time frames for the review of the position descriptions.*

The Inspection Service is in the process of changing its work hour reporting requirements and reporting system as well as revising the appropriate Inspection Service policies on this issue. These actions will ensure that the Inspection Service inspectors, supervisors, and managers understand the requirement that "Postal Inspectors devote 50 percent or more of their work hours to law enforcement duties." The changes in our systems and reporting requirements will ensure the actual percentage of hours worked in "law enforcement duties" for each inspector not in a secondary law enforcement position is calculated on a monthly basis. The policies being finalized make it the responsibility of each inspector and his or her manager to ensure the requirement is met. These actions are scheduled to be completed by the end of this calendar year.

(b) *Simply re-wording the duties and responsibilities in a job description does not ensure that the Postal Inspectors will, in fact, spend less than 50% of their time on non-criminal investigative duties. How does the Postal Inspection Service intend to enforce and monitor compliance with this requirement on an ongoing basis?*

Inspection Service managers will be responsible for ensuring that Postal Inspectors spend at least 50 percent of their time on criminal investigations. The Inspection Service has developed a monthly tracking form, PS Form 512-A, Law Enforcement Availability Pay Monthly Tracking Form, which is designed to provide the percentage of audit versus criminal hours performed each month. Every month this form is reviewed and signed by the Inspector's immediate supervisor. A copy of the form is attached (Attachment 9).

110. In July of 1998 the Postal Inspection Service issued a report to postal management on the impacts of Classification Reform on the Postal Operations, Case Number 070-1225508-SI (1). The review revealed that the Postal Service underestimated the response to Classification Reform. Volumes far exceeded the planned increases in customer applied barcoded letters and flat mail. The review also concludes that the Postal Service needs to process more of the barcoded mail in automated operations to maximize the full potential of Classification Reform. The Inspection Service report estimated that the Postal Service lost the opportunity to reduce operational costs by approximately $600 million in 1997 by not finalizing a larger amount of the barcoded letter and flat mail on automation.

(a) *The Inspection Service reported that up to 20 percent of barcoded letter mail was processed in manual and mechanized operations. What percent of barcoded mail in FY 1999 was processed in manual and mechanized operation?*

The Inspection Service claimed that up to 20 percent of barcoded letter mail was not sorted to at least the carrier route level on automation.

The Corporate Automation Plan (CAP) from May 1996 stated the Postal Service would automate letters to carrier route level for zones with five or more carrier routes. The CAP goal was 78 percent by the end of FY 1997 and 84 percent by the end of FY 1998. The audit indicates 80.7 percent and 83.6 percent of the barcodes were actually processed on automation to at least the carrier route level for FY 1997 and 1998 respectively, which are well in-line with the stated goals. The end of FY 1998 was to reflect a full-up letter automation environment.

These goals took into account barcode rejects from all up-stream barcode sorter operations, the portion destinating in zones with less than five carriers, and barcoded courtesy reply and business reply letters finalized farther up-stream. Barcode discounts also reflect that a portion of mail will destinate in non-automated zones and will reject along the way. However, that does not mean that the Postal Service did not use the barcode in previous, up-stream automated operations.

The portion of letters sorted on automation has since increased due to additional equipment deployments and the addition of some zones with less than five routes. FY 1999 ended with no more mechanized sorts to carrier route, and automated sortation of 86 percent of barcodes to at least the carrier route level.

Refinements to letter automation will continue to be made as new encoding software is being deployed to allow a finer level of coding for high-rise and garden-style addressing. Identification code sorting is also being deployed on barcode sorters and will provide a redundant method to reduce barcode read rejects, thereby allowing more barcodes to be sorted and finalized on automation.

The amount of savings opportunity the Inspection Service stated in their report was based on an assumed percentage of capture-ability without supporting data. The report did not fully take into account the Corporate Automation Plan goals or mail finalized in up-stream operations. Two recent GAO audits confirm that the USPS has made automation savings over DAR projections.

(b) *The Inspection Service reported at that time that Delivery Point Sequence volume was 20 percent below plan. Where does Delivery Point Sequence volume in FY 1999 stand with respect to the FY 1999 plan?*

The FY 1999 Actual Year To Date (YTD) volume was 49.56 billion pieces. The Plan YTD volume was 48.15 billion pieces. The actual volume was 1.51 billion, or 2.9 percent over plan.

(c) *The Inspection Service reported that flats processed on automation remained a constant 34 percent. What percent of flats in FY 1999 were processed on automation?*

In FY 1999, 42 percent of flat mail was processed using optical character readers and bar code readers.

(d) *What actions has the Postal Service initiated to increase the use of existing automation equipment to capture the savings on which Classification Reform and future workshare discounts are based?*

The Postal Service has an active automation/mechanization program that includes retrofitting existing equipment to meet the requirements of reducing costs associated with processing mail.

Examples of programs that are currently being approved and implemented that meet our requirements to make existing equipment more productive, and thus allow for more capacity are Flat Mail Optical Character Readers ($35 million FY 2000 savings) and Delivery Barcode Sorter Output Sub-systems ($13 million FY 2000 savings).

Additionally, a total of $465 million of local management initiatives has been allocated to the field. The field must utilize existing equipment and resources to meet the targeted reduction.

(e) *Has the Postal Service implemented an ongoing monitoring system in mail processing plants to gauge whether mail which is automation compatible is being processed on available automation?*

Operations Planning at Headquarters generates an "Operations Performance Review" national report on an AP basis. Included in that document are reports that provide barcode generation information as well as information on the amount and percentage of automated processing at the plants by area.

(f) *Are operations managers evaluated on whether they use automation effectively?*

One of the criteria for evaluation of operations managers during the yearly merit review process is how effective they are in addressing the elements outlined in the Voice of the Business (VOB), which include adherence to budget, meeting service objectives, and revenue generation. In addition, the evaluation determines how effectively managers use automation by measuring the Return On Investment (ROI) savings identified in the Decision Analysis Reports (DARs) for each piece of automated equipment.

(g) *What actions has the Postal Service taken to coordinate automation and transportation planning with classification and pricing planning in order to maximize the value of worksharing?*

The Postal Service solicits and reviews candidate worksharing initiatives that it might formally propose. The Headquarters Operations group, which is responsible for automation and transportation planning, actively participates in this effort and its input is factored into classification and pricing planning. The Operations group also participates actively in the Presort Optimization MTAC (Mailers Technical Advisory Committee) Workgroup and that Workgroup has sponsored various worksharing improvements that are consistent with the Postal Service's automation and transportation plans.

111. Workshare discounts have become the bedrock of the Postal Service's rates and classification system. Some have argued that worksharing constitutes, in essence, a private-public partnership which has led to reasonable rates and improved service for all customers. Nonetheless, as evidenced by the aforementioned Inspection Service report, workshare savings that justify these discounts are often not captured. The Subcommittee is interested in how well the Postal Service measures the actual cost savings from workshare programs. Currently the Postal Service only reports attributable costs at the subclass level. The actual cost avoided by the Postal Service for each workshare discount is not reported nor apparently calculated on a regular basis.

(a) *Why are these all-important figures not reported on an annual basis?*

The attributable costs referenced in this question are reported by the Postal Service in its annual Cost and Revenue Analysis (CRA). Though the CRA does not report cost information for each worksharing mail category, such reporting would not necessarily isolate the cost effects of worksharing since worksharing is only one of many cost driving factors.

The costs reported in the CRA represent the combined effects of all cost driving factors. For this reason, special studies are required to estimate the isolated cost avoidances for each worksharing category. Since worksharing discounts can only be changed during formal rate and mail classification cases, the Postal Service has determined that it is both practicable and efficient to time its special studies according to the timing of its planned rate and mail classification filings. While other approaches have been considered, this chosen approach provides timely data while avoiding the expense of conducting studies on a more frequent basis.

(b) *With the Postal Service's operating environment changing so rapidly, has the Postal Service initiated any efforts to conduct these studies on an ongoing basis and report the results publicly? If not, why not?*

As indicated in our answer to Question 111(a), the Postal Service conducts these cost studies on an ongoing basis, in accord with its rate and mail classification filings. These updated cost studies reflect the Postal Service's changing operating environment. Special Studies, a separate office in Headquarters Finance, conducts these studies. Study results are sponsored by expert cost witnesses who testify publicly during hearings held by the Postal Rate Commission.

112. As the Postal Service continues to deploy automation equipment, new technical and managerial knowledge, skill and abilities will be needed to operate and maintain some highly sophisticated equipment, such as the Robotics Containerization Systems (RCS) and the Tray Management System (TMS).

(a) *Does the Postal Service plan to create new job categories/positions tailored toward meeting the human capital requirements of the new automation environment? How and to what extent has the Postal Service committed to re-train current employees to meet its needs?*

The Postal Service is committed to using its present employee work force to meet our present and future automation staffing needs. In the event we are unable to fill our needs from our present workforce, we will hire new employees to meet our needs.

(b) *Does the Postal Service plan to hire new employees with the technical skills to support this new automation? How does the Postal Service anticipate that its employee complement will change as a result of automation?*

The Postal Service will attempt to fill our technical needs from our current complement. If we cannot fill a position from within the present complement, we will hire new employees to meet our operational needs.

(c) *Please discuss the Postal Service's short-term and long-term plan to meet the human capital needs, particularly with respect to its changing mail mix and the deployment of automation.*

The changing mail mix and deployment of automation is a gradual change to our daily operations, especially when looked at from a total organizational perspective. The changes in complement are subtle and handled locally.

113. Automation promises to have a major impact on controlling labor cost. For example, Robotics Containerization Systems (RCS) will provide a modular robotics solution to automate current manual efforts associated with mail tray and tub verifying, lifting, stacking, and separating into mail containers and pallets to meet transportation and delivery operations windows. It is anticipated that manual work hours and job related injuries will be substantially lowered by the introduction of this new technology. Based on past experience with automation it is alleged that potential savings have not been realized because work rules make it difficult for management to re-assign current employees to work centers where they can be more productive. As a result, some operations have been overstaffed. This problem will become increasingly severe as the plan to fully automate processing facilities comes to fruition in the next several years.

(a) *How does the Postal Service intend to manage the redeployment of labor as automation reduces the need for manual processing of mail? Does the Postal Service have a process to coordinate its capital investment strategy with human resource needs assessment at the national, area and district levels?*

The Postal Service has a procedure contained in the collective bargaining agreements with its unions on how to reassign employees in every situation, including those involving automation deployment. This process allows for reassignment to other work within an installation as well as reassignment to other installations with continuing work, as necessary.

The Postal Service is preparing for the impacts associated with the future deployment of Robotics Containerization Systems and various other automation initiatives by utilizing a complement management plan that is consistent with those provisions in the collective bargaining agreements. This plan has three major elements to ensure that employees are moved from diminishing work to continuing work—withholding, reassignment, and transitional employees.

Withholding:

When a major initiative is being planned that impacts the work force such as Robotics, the Postal Service at the Area level institutes a withholding clause in the contract. This allows the Postal Service to "hold" job vacancies (freeze them without hiring careers) that come open and will be needed after the deployment of the automation. These jobs are "held" for reassignment/ placement of those career employees who will be displaced.

In conjunction with this withholding clause, the Postal Service also eliminates impacted jobs through attrition by "reverting" them (eliminating them immediately) when they become vacant. This accomplishes two goals: it does not add to the career complement to cause overstaffing and allows for a reduction through attrition.

Reassignments:

The Postal Service and the unions have agreed that when the need arises to reassign employees, a certain procedure will be employed depending on the type of initiative. This procedure is accomplished essentially through reassignment based on a seniority system; the employees with the most seniority are reassigned after those with less seniority have been moved.

As an example of a successful implementation of this reassignment procedure, the Postal Service introduced the Remote Bar Coding System to replace mechanized keying on Letter Sorting Machines. At the beginning of the effort, there were approximately 47,000 Letter Sorting Machine Operators in the Postal Service. Due to the deployment of RBCS, this function was no longer needed, along with the labor force associated with it. Utilizing the reassignment procedure in the contract and a special agreement with the APWU, the Postal Service eliminated LSM operators and reassigned them to other continuing work in the installation or other installations with work force needs.

Transitional Employees:

During the withholding period described above, labor contracts allow the Postal Service to hire transitional employees. These employees work in the withheld jobs until the automation is deployed. This enables the Postal Service to place career employees in continuing jobs, capture the savings associated with the automation initiative, and maintain service levels.

These plans are developed through coordination with all levels of the organization. The unions are notified and consulted as the withholding, reassignments, and the hiring of transitional employees are taking place.

(b) *What assumptions are made with respect to the Postal Service's ability to realize the potential workhour savings from the automation program? How have these criteria been adjusted to reflect the experience to date in capturing workhour savings?*

The Postal Service's letter automation program is focused on barcoding mail and using those barcodes to automate the sorting of mail to help control costs. Savings estimates were based on replacing manual and mechanized sorting operations with the higher productivity that is achieved from fully automated letter sorting equipment. These operations included not only the manual/mechanized sorting of letters in our major processing plants, but also the manual sequencing of mail in the order carriers deliver it.

Our letter automation program has been a success. Currently, nearly 90 percent of all letters are barcoded. Moreover, studies have shown that benefits are exceeding those assumed when making our decision to invest in this technology.

114. The Postal Service has acknowledged in the past that there have been problems with periodical delivery. The Postal Service has previously reported that it has taken several actions to improve service including improved communications, refined Standard Operating Plans and participation in The Mailers Technical Advisory Committee (MTAC). The MTAC workgroup recently sent its recommendations to the Vice President of Operations Support to update delivery commitments for all classes of mail, and establish standards and measurement/reporting systems for its service performance for all classes of mail.

(a) *How does the Postal Service intend to respond to these recommendations?*

At the October 19, 1999, MTAC Steering Committee meeting, Nick Barranca, Vice President of Operations Planning, reported that the Postal Service essentially concurred with the recommendations contained in the white paper produced by the MTAC work group exploring this issue.

He noted that the successful implementation of many of the recommendations contained in that paper would be dependent upon development of the Postal Service's Information Platform. Noting the magnitude of that effort and highlighting the significant lead times and budget implications, Mr. Barranca advised the committee that the working group's recommendations had been provided to the Marketing department for integration with other customer requirements. This consolidated set of customer requirements would become part of the input to the Establish phase of the Postal Service's management cycle during which objectives and goals for the upcoming fiscal year are set and against which resources are subsequently allocated. Specifics regarding the work to be done to support the recommendations contained in the white paper can not be determined until those two phases of the management cycle are complete sometime in the spring of 2000.

115. Last year the Postal Service and representatives of the publications industry, including the Magazine Publishers of America, met to define the requirements for a joint study of issues relating to costs of handling publications mail in Postal Service plants and delivery units. A joint Postal Service-publications industry team visited a number of postal facilities to identify possible opportunities for cost reduction measures.

(a) *Please summarize the study teams findings and recommendations.*

The following recommendations were extracted from the team report:

"Issues 1&2: Mail Make-up And Containerization.
We will investigate opportunities for additional worksharing (*e.g.*, more cross-dock, 5-digit pallets, etc.), cost savings, and service improvements by aligning mail preparation standards more closely with local mail processing operations (*e.g.*, L-001 lists, etc.). We will make real time information available to customers via the Internet.

Issue 3: Address Quality.
We recommend several initiatives to encourage and facilitate improved barcode accuracy, thereby reducing rehandling costs.

Issue 4: Enforcement and Enhancement Of Entry/Acceptance Requirements.
We recommend that initial action taken by acceptance personnel be preventive in nature and emphasize notification of publishers, as well as their printers, of problems relating to presort and barcode quality so that future mailings will not contain errors. We recommend an active education effort, involving mailing associations, USPS Bulk Mail Entry Acceptance, and USPS Management personnel. We also recommend that local postal managers recognize that mailers who miss critical entry times should not expect the Postal Service to undertake measures to deliver such mail as if it were not delayed in entry.

Issue 5: Flats Operation Plan.
We recommend development and publication of a detailed operation plan for flats processing, similar to what already exists for letter mail. The plan should logically link equipment and technology, mailer workshare, and process improvements. The plan should include best practices with existing sorting equipment as well as a strategy for development and deployment of new and improved equipment to accommodate and automate the rapidly rising volume of flats in the postal system.

Issue 6: Combination And Separation Of Mail Classes In The Incoming Mail Stream
Opportunities exist for reducing costs without compromising service by combining flats of different mail classes in incoming sorting operations, as is already being done successfully in some locations.

Issue 7: Bundle Preparation And Handling.
We recommend several initiatives to address the long-standing problem of bundle breakage. Mailers need to strengthen bundles to withstand anticipated stresses caused by dumping postal packs and pallets. USPS should report breakage problems to both mailers and those who prepare the bundles for the mailers. The automated feed systems being installed on Small Parcel and Bundle Sorter (SPBS) machines appear to compound this problem by subjecting bundles to excessive stress. We recommend the sharing of best practices in the current use of bundle dumping equipment, and recommend that next generation SPBS processes consider methods to reduce excessive stress. (We understand that Engineering is already working on this issue.) Finally, if better and more effective strapping methods do not work, then further movement of mail from sacks to pallets and higher pallet presort levels should also be encouraged.

Issue 8: Operations Management.
We recommend a number of initiatives to strengthen management's attention to costs, provide better tools for management and supervision, and require more active supervision of operations.

Issue 9: Transportation.
We are disturbed by the rapid increase, over a number of years, in Periodicals transportation costs. We observed that in many sites, additional transportation was utilized as a strategy to improve service. We recommend that postal and transportation industry experts study periodical transportation costs further.

Issue 10: Mail Processing Annexes.
Plant managers, faced with crowded conditions due to rapidly increasing mail volume, often choose to "solve" the problem by deploying Periodicals flats processing to separate annexes. The result is additional transportation and handling costs for Periodicals. While the best long-term solution may be to build new and larger plants, we recommend steps be taken to mitigate the immediate problem.

Issue 11: Flats Automation.
We observed FSM under-utilization at many sites, and a tendency to send Periodicals flats (both polywrapped and not) meeting all FSM-881 compatibility standards to the slower FSM-1000s or to manual sorting. We recommend a close review of opening unit operations to improve overall efficiency, and particularly efficiency for periodical flats. We recommend a number of initiatives to improve machine utilization, assure that automation compatible flats receive automated sorting to the extent possible, and reduce the number of handling steps.

Issue 12: Interclass Cost Impact.
Processing decisions made in the interest of overall efficiency appear sometimes to be increasing Periodicals costs. We recommend further analysis of these cost effects to ensure that attributed costs accurately reflect causality and determine if a remedy is required.

Issue 13: Low Costs And Good Service Are Not Mutually Exclusive.
We recommend an active campaign to raise cost consciousness among managers and supervisors and encourage solutions that reduce costs while also improving service. We strongly believe that fast service and low costs are not mutually exclusive. Both can be achieved by eliminating unnecessary handlings.

Issue 14: Allied Operations And Cost Attribution Methodologies.
Due to piece sorting automation, increased levels of presort, and a greater number of separate mail streams, allied labor today represents a large and still growing share of total mail processing costs. Most of the measured rise in Periodicals costs is due to the class's rising share of allied labor costs. We recommend that the Postal Service continue to study and model the volume variability of mail processing operations, and that it examine alternative procedures for distributing allied labor costs to products.

Issue 15: Rate Design.
Although the study of rates was not part of this team's mandate, we recognize that mailer preperation affects USPS costs and that rates can affect mailer behavior. As a general matter, and consistent with provisions of applicable law and precedent, we recommend that USPS evaluate rate incentives that (1) recognize and encourage mailers' beneficial worksharing activities, and (2) encourage mail preparation that minimizes postal costs."

(b) *Has the Postal Service or the publication mailers adopted any of the recommended cost reduction measures?*

Yes. The increased use of automation, focus on improving the effectiveness of postal processes, increase in the amount of direct pallets going to delivery units, and improved bundle preparation and handling are all underway in the Postal Service. The industry is focusing on the bundle preparation to reduce breakage and ensuring that mailers understand the importance of taking mail to the correct entry location, with mail prepared as required. The Postal Service is tracking actions with an implementation plan that includes progress reports to responsible officers each fiscal quarter.

(c) *Will any of these cost reductions be reflected in the next omnibus rate case?*

The rate filing is based on a fiscal year that occurred prior to the year that the team was operative, and many of the cost reductions would not be reflected in that base year. However, the potential utilization of automation was recognized in the filing and reflects the increased efficiency that would result. As the rate process unfolds, the other cost reduction impacts will be examined and included where applicable.

116. Significant increases in Standard A Regular and Periodical Regular mail processing costs has led mailers to speculate that the Service has not been able to capitalize on the flat sorter automation program. Despite reported increases in bar code read rates, equipment, and efforts by the mailing industry to improve the quality of the flats mail stream, productivity apparently has not gone up.

(a) *How does the Service explain the large increase in costs for Standard A Regular mail?*

It appears that mail processing costs for flat-shaped mail have recently risen more than for all shapes combined. This affects the cost for Standard Mail (A) Regular because mail processing is an important cost component for that subclass, and a substantial portion of the subclass is flat-shaped.

(b) *To what extent is the reported cost increase of Standard A Regular the result of sampling and non-sampling error in the In-office Cost System?*

It is unlikely that the In-Office Cost System sampling and non-sampling errors are the cause of cost increases in Standard Mail (A) Regular. The sampling error (coefficient of variation) for mail processing costs of Standard Mail (A) Regular is approximately one percent. To the extent that there is non-sampling error, a portion of it would be reflected in the sampling error.

The effect of other potential non-sampling error is not known. However, both the data collection instrument and the automated edit processes are designed to limit the introduction of non-sampling error in the estimates. While a potential for non-sampling error will always exist in any sample survey, no significant potential source of non-sampling error has been identified for Standard Mail (A) Regular in the In-Office Cost System.

(c) *How does the Service explain the large increase in cost for Periodical Regular mail?*

The overwhelming majority of Periodical Regular mail is flat-shaped, so that subclass has been especially affected by the recent above-average mail processing cost increases experienced by flats. The Postal Service has worked with representatives of the Periodicals industry to seek improvements in mailer and postal operations affecting Periodicals. The report of the Periodicals Operations Review Team identifies various areas that appear to be adversely affecting the costs for Periodical Regular mail, including transportation and processing methods.

(d) *To what extent is the reported cost increase of Periodical Regular the result of sampling and non-sampling error in the In-office Cost System?*

It is unlikely that In-Office Cost System sampling and non-sampling errors are the cause of cost increases in Periodical Regular mail. The sampling error (coefficient of variation) for mail processing costs of Regular Periodicals is approximately 1.75%. To the extent that there is non-sampling error, a portion of it would be reflected in the sampling error. The effect of other potential non-sampling error is not known. However, both the data collection instrument and the automated edit processes are designed to limit the introduction of non-sampling error in the estimates. While a potential for non-sampling error will always exist in any sample survey, no significant potential source of non-sampling error has been identified for Periodical Regular mail in the In-Office Cost System.

117. The theory of the "automation refugee" postulates that as the Service automates the processing of letters fewer employees are needed in letter operations. These employees are then assigned to other operations, such as flat sorting, which drives down productivity in those operations.

(a) *Has the Postal Service conducted any studies to explicitly study the staffing practices in the field in response to automation to determine whether the automation refugee theory is correct? If so, please provide the findings of the study for the record.*

We have not conducted any explicit studies to determine if the automation refugee theory is correct.

(b) *Please report on how the Postal Service has and will assign remote barcode site employees made redundant by the Service's impressive gains in read rates for letter mail. Please include detail as to which other operations these employees have been or will be assigned (mail processing, retail, delivery, administrative, etc.). What percent of the total staff at the RBCS sites that have been or will be closed will be retained and reassigned?*

Approximately 27 percent of the staff in the Remote Encoding Centers (RECs) that have or will be closed are career craft employees. According to the labor agreement between the Postal Service and the American Postal Workers' Union, the Postal Service has specific obligations to these employees. This includes data conversion operators and electronic technicians (maintenance employees). For these displaced career employees, the Postal Service will provide offers of employment in other postal facilities. These offers will be vacant positions where workload still exists. The electronic technicians are highly skilled and knowledgeable about automated equipment. There are many vacancies for these skilled employees. The priority for these reassignment opportunities will be in the local geographic areas where the closing RECs are located. These job opportunities may be in the local Processing and Distribution Center or other Post Offices.

However, if productive work assignments are not available in the local area, then reassignments to positions elsewhere in the Postal Service will be offered. Again, these offers will only be made to positions where productive work assignments are available. It should also be noted that some employees will refuse to accept other postal positions if it is necessary to relocate to another part of the country. The need to relocate employees will vary from one REC location to another. At this time, we do not have enough experience in closing RECs to determine to what degree this will be necessary.

With regard to the non-career transitional workforce which accounts for approximately 70 percent of the total REC staff, the Postal Service is not obligated to offer these employees other postal employment. However, these employees have been a valuable asset to the overall success of our REC operations and we will be assisting them in securing jobs outside of the Postal Service. We will be working closely with state and local employment agencies to this end.

Approximately 3 percent of the total staff at the RECs are management employees. While there is no specific obligation to retain these employees, they possess valuable management expertise and will for the most part be offered positions elsewhere in the Postal Service. Again, these offers will only be made where productive work assignments exist and may be in the local geographic area or in another part of the country.

(c) *What is the status and timetable for deployment of the FSM1000's? Will the expected efficiencies from the FSM1000's be reflected in the test year attributable cost of flats processing in the next omnibus rate case?*

Deployment of all planned FSM 1000s (340 machines) was completed in June 1998, and barcode readers were added to all of them by March 1999. In addition, we are planning to deploy 175 Automated Flat Sorting Machine (AFSM) 100s from March to December 2000 to enhance and expand our existing flat processing capabilities.

The expected efficiencies from both the FSM 1000s and the AFSM 100s will be appropriately considered in future omnibus rate filings.

118. The Postal Service recently published its Annual Performance Plan for Fiscal Year 2000 as required by the Results Act. The Service will publish its first performance report next year on its performance in fiscal year 1999.

(a) *What is your view on the value of these reports to the Service?*

The four Annual Performance Plans published so far (both Preliminary and final Plans for 1999 and 2000) have provided an excellent opportunity to update all Postal Service stakeholders, both internal and external, on the performance goals, action plans, and programs that will be put into place during the next fiscal year.

The first Annual Performance Report for 1999 (to be published in February 2000) will complement the Performance Plan by providing information on how well the various performance goals for the preceding year were met. Both documents serve as a checkpoint on how the strategies listed in the Five-Year Strategic Plan are working.

119. GAO reported, in early 1998, on the Service's introduction of new products. At that time, only 4 new products, out of 19, were making a profit. The Subcommittee is interested in getting an update on how those new products are performing today.

(a) *Please provide summary financial data and an update of new products marketed and/or under development during fiscal years 1995, 1996, 1997, 1998, and 1999 (exclusive of capital and philatelic products); i.e., please update Table 1 on page 19 of GAO's November 24, 1998 report on new products (U.S. Postal Service: Development and Inventory of New Products (GAO/GGD-99-15, Nov. 24, 1998). As part of that update, please indicate any additional or discontinued new products.*

Through 1997, the Postal Service lost $84.7 million in the development of new products and services. Of this amount, $48.2 million was associated with products and services that have been discontinued. Since 1997, the products and services that were included in the original GAO report and that have not since been discontinued have generated a net surplus of $123.2 million, which more than offsets the $84.7 million loss.

(b) *In light of the GAO report on new products, has the Service implemented any changes to make the new product review process more effective?*

We believe the process is working effectively and have not made any changes.

120. The Postal Service's 1999 Performance Plan includes a goal to grow net income from new products and services by increasing revenue by $92 million.

(a) *What is the Postal Service's goal for increasing contribution (revenue minus attributable cost) from new products and services?*

The goal is to maximize contribution through better selection of new products, cost controls, and quicker and more effective reaction to market conditions. With most new products, immediate positive contribution is not achieved during the introductory or test phase of the product cycle. By emphasizing management oversight, budget justification, and enhanced process review, we are striving to maximize the opportunity to recognize a positive contribution during the life of the product.

(b) *Would the Postal Service consider itself to have achieved this goal if new product and service revenues increased by $92 million or more but those revenues failed to cover the attributable cost of those new products and services?*

Like private industry, we do not evaluate our products in the aggregate. Each one is evaluated on its own merit, and we believe there have been some successes and failures among our products. Those products that do not exhibit a potential to provide or create acceptable contribution margins are terminated.

121. It has been reported that the Postal Service is exploring the idea of negotiated service agreements. Apparently the Postal Service is benchmarking the concept in order to determine how to structure NSA agreements and will consult with the Mailers Technical Advisory Committee (MTAC) concerning possible options. Concern has been raised in the development of the NSA provisions in H.R. 22 that NSAs should not result in pure volume discounts and that NSAs be made available to similarly situated mailers.

(a) *Will the Postal Service address such concerns in its proposed NSA requirements?*

The Postal Service is currently analyzing operational, financial, regulatory, and legal issues raised by negotiated service agreements (NSAs). It is also studying the possibilities for establishing a process for the formal proposal and review of NSAs. This inquiry will include discussions with mailer groups designed to evaluate their interest in, concerns about, and suggestions for any proposed NSA review process.

Our framework for the NSA discussion centers on potential agreements that, through some combination of attributes (worksharing, mail preparation, drop-shipment, etc.), result in a net benefit for the Postal Service and the affected mailer. Another important consideration would be the effect of a NSA on other mailers. To facilitate creative thinking, our study team has been encouraged to think about NSAs in the broadest possible context within the boundaries discussed above.

While our study of negotiated service agreements within our current regulatory environment is only beginning, in the context of the proposed Postal Modernization Act of 1999 (H.R. 22), the Postal Service agreed that any negotiated service agreement should be made available to similarly situated mailers. In addition, we agreed that NSAs would not be a substitute for broader-based classification changes when the proposed NSA's terms and conditions could be readily extended to a significant proportion of mailers within a specific mail classification.

122. In Docket No. 97-1 a rate anomaly was uncovered after rate implementation. Regular rates were incorrectly set less than certain equivalent nonprofit rates.

(a) *Have measures been put in place to detect rate anomalies in the future?*

The complicated rate structures, especially in Periodicals, increase the likelihood of rate anomalies. In Docket No. R97-1, for example, no Regular rates were set lower than equivalent nonprofit rates; however, the combination of these rates for certain publications produced lower postage amounts using Regular rates than nonprofit rates. While we would like to be able to say we can identify every possible anomaly, we can not make such a sweeping statement. We are, however, closely monitoring our rate development to flag rate anomalies. We are also contemplating suggested changes to the Revenue Forgone Reform Act that would eliminate the possibility of anomalies in Periodicals.

123. Concern has been raised as to whether the Postal Service in its role as a regulator has treated potential vendors of new computer-generated postage, or PC Postage, on an equal basis with regard to testing, certification and product deployment.

(a) *What processes and internal safeguards has the Postal Service put in place to assure that all current and potential vendors be afforded equal treatment with regard to the PC Postage program specifications, technical and marketing support?*

The Postal Service has developed its performance criteria for PC Postage through public rule making processes published in the *Federal Register*. Published documentation for product submission and development is achieved through an iterative process with input from the general public, private companies, and academia. Commercial companies develop PC Postage products in response to published performance criteria that are publicly available. Product Submission Procedures that delineate comprehensive test and evaluation requirements are also publicly available. The approach is referred to as being in the "sunshine" because program advances are achieved through public forums and participation.

The Postal Service uniformly applies an extensive evaluation process to ensure product security and financial and operational integrity that includes participation from independent security specialists. Computer components of PC Postage products that account for postal revenues are evaluated by private companies certified by the National Institute of Standards and Technology (NIST). Extended field testing with customers is included as a critical element before products are approved by the Postal Service for commercial distribution. The field testing strategy is documented by the Postal Service and shared with participating product providers. The result of this process is the introduction of new products and new companies in the marketplace as they successfully demonstrate response to universally applied requirements.

124. Currently the "PC Postage" is restricted to usage on First-Class, Priority, Express and Standard B (parcel post).

(a) *What technical, legal or administrative constraints prevent the Postal Service from expanding use of PC Postage to international and other services, including insured, certified and registered mail?*

The initial service offerings were targeted to the basic mailing profile of small office/home office businesses. The first generation products provide a benchmark of experiences for the customer, the vendors, and the Postal Service in order to intelligently target expansion and usability features of the products.

The Postal Service is actively working with the product providers to respond to customer feedback regarding usability features. Incorporation of additional services such as insured, certified, and registered mail requires consideration of service specific mail processing and forms requirements. The Postal Service expects to support expansion to these offerings during FY 2000. Expansion to support International mail requires a technical solution to the security requirement for inclusion of the delivery point code in the indicia. A proposed solution is currently under review and the Postal Service expects to support expansion to include International mail during FY 2000.

(b) *When does the Postal Service anticipate that usage of PC Postage will be expanded to other categories of mail?*

See the response to Question 124(a).

(c) *Since PC Postage was approved on August 9 what has been the market response to PC postage?*

Stamps.com said it ended 1999 with more than 87,000 licensed customers. E-Stamp reported that it had in excess of 13,000 customers as of September 30, 1999. In late January, a spokesman of E-Stamp indicated that he did not dispute the current estimate of 30,000 customers that is being reported by financial analysts.

A study released in early February by the International Data Corporation (IDC) also reported that small businesses and home offices in America have spent $8.2 million on PC Postage products. IDC estimates that annual spending will approach $300 million by the end of 2000 and $600 million by the end of 2001.

(d) *What does the Postal Service's market research indicate as the anticipated market response to PC postage? Has the market response since rollout in early August met expectations thus far? Does the Postal Service anticipate a reduction in stamp production as a result of migration to PC postage?*

Market research data suggests the rate of adoption of computer-generated postage will be rapid, similar to the adoption of personal computers and the rapid growth of the Internet. The report by IDC mentioned in the response to Question 124(c) estimates that annual spending on PC Postage will approach $300 million by the end of 2000 and $600 million by the end of 2001. The initial market response, as described in the response to Question 124(c), has met expectations.

The Postal Service has not studied the impact of PC Postage on stamp usage, and does not predict a reduction in stamp production as a result of migration to PC Postage. Most customers who have begun using PC Postage (primarily small businesses) are likely to have used postage meters or postage strips attained at a postal counter rather than postage stamps.

(e) *Will the introduction of PC Postage have a capturable saving in window service workhours as a result of reduced purchases of stamps and meter setting at retail windows? If so, please provide an estimate of such savings.*

The Postal Service does not expect and has not estimated any window service work hour savings related to PC Postage. As discussed in the response to Question 124(d), we do not predict a significant decline in the use of postage stamps because of the use of PC Postage. In addition, mechanical meters are no longer set at retail windows. The transition to remote set meters was made in 1995.

125. A common complaint concerning PC-postage is that it cannot be used for pre-addressed envelopes because each stamp must be printed with the address.

(a) *How does the Postal Service intend to address this limitation? If the Postal Service does not intend to remove this limitation, please explain why.*

The Postal Service is working with the providers of PC Postage to develop new solutions to enhance these services. The current criteria requires the maintenance of a unique relationship between the destinating address and its associated printed indicia as a security feature. This required security element currently precludes the ability to print a "stamp" without its associated address. The Postal Service is working, however, with product providers and the industry on a security solution that will allow the use of window envelopes in the future without jeopardizing revenue protection security requirements.

126. Last year the Postal Service reported that additional transportation infrastructure has helped improve service performance.

(a) *To the extent that service performance has improved, how has additional transportation infrastructure contributed to that improvement?*

In July 1998, the Postal Service added dedicated air transportation to help improve the on-time performance of Priority and 3-day First-Class Mail. This new dedicated air transportation operates during the day and has reduced the volume of mail that is transferred at commercial air hubs. This transfer volume had often failed to connect with its intended flight resulting in sub-par service. The implementation of the dedicated daytime network has removed 2½ million pounds of mail per day from commercial air transportation. This network diversion allows the commercial carriers to more efficiently handle the remaining volumes.

The Postal Service's daytime dedicated network has an on-time performance rate of 91 percent. Performance by commercial air carriers has been 20 percent below that mark. In addition, the Postal Service operates two nighttime air networks for the purpose of transporting its overnight Express Mail products. These networks, which are commonly referred to as ANET and WNET, achieved a 98 and 97 percent on time performance, respectively, during the past year.

(b) *Has the Postal Service made further investment in transportation infrastructure or instituted other programs aimed at improving service performance? Please summarize the latest developments in this area.*

In FY 1999, the Postal Service increased spending for contractual transportation by $900 million, an 8.9 percent over FY 1998. We increased spending for domestic air transportation by more than $450 million and highway transportation by $200 million, or 7.1 percent. Other actions taken to improve service can be found in the response to Question 128(b).

127. The Postmaster General recently testified that every location in the contiguous United States had an EXFC score of 91 percent or better for local service. He reported that the national average stood at 94 percent and that scores for two-and-three day commitments were "your best ever."

(a) *For the record, what are the final FY 1999 scores for First-class overnight, 2-day and 3-day mail?*

The final FY 1999 service performance scores for Quarter 4 are 94 percent for overnight committed First-Class Mail and 88 percent for combined two- and three-day committed First-Class Mail.

The final FY 1999 aggregate scores for the year (Quarters 1-4) are 93 percent for overnight committed First-Class Mail and 86 percent for combined two- and three-day committed First-Class Mail.

(b) *Will the FY 1999 calculation of variable-based pay be based on the overnight or the composite EXFC score?*

The on-time delivery component of the FY 1999 Variable Pay Program was based on the performance scores for overnight committed First-Class Mail, two- and three-day committed First-Class Mail, and Priority Mail. Failure to obtain the overnight target excluded the Performance Cluster or Area from the entire Voice of the Customer (VOC) service component. If the overnight target was met, achieving the two- and three-day goal earned 50 percent of the VOC portion and achieving the Priority Mail goal earned the remaining 50 percent.

(c) *Has the Postal Service achieved its target for a 2-percentage point increase in 2-day and 3-day mail performance? If not, how do you explain the failure to achieve the targeted improvement?*

Yes, the Postal Service did improve its two- and three-day committed First-Class Mail performance by two percentage points in FY 1999. The FY 1998 two- and three-day combined aggregate score (Quarters 1-4) was 82 percent. As reported in response to Question 127(a), that score improved to 86 percent in FY 1999.

128. In its 1998 Performance Plan, the Postal Service established Voice of the Customer Performance goals to provide timely delivery. Specifically, the FY 2000 goals for First-Class Mail are to achieve overnight First-Class Mail on-time performance of at least 93% and two- and three-day delivery of 90%. The Postal Service has achieved 94% overnight and 87% two- and three- day delivery.

(a) *Given the latest figures has the Postal Service considered raising its First-Class overnight goal? Does it appear that the Postal Service is on track to achieve two- and three-day delivery of 90% on-time in FY 2000?*

The Postal Service has decided to maintain its 93 percent target for overnight committed First-Class Mail in FY 2000 as it ramps up service in other areas. The target for two- and three-day committed First-Class Mail has been set at 88.7 percent for FY 2000, one full percentage point above last year's result.

It is too early to tell if the Postal Service is on track to reach its two- and three-day target. However, the Postal Service is confident that it can achieve this goal.

(b) *Please update us on the status of actions the Postal Service has taken in the last year to improve the delivery of 2-day and 3-day mail and give specific examples of whether these actions contributed to improving timely delivery of 2-day and 3-day mail.*

The following list represents some of the actions taken by our operating areas in order to improve service:

- Established field traffic management positions in some of the Air Mail Centers (AMCs) to monitor internal and external processes, review ramp operations, address air carrier capacity issues, analyze daily volume conditions on flights, and inform local management of areas of opportunity for improvement.

- Developed process reviews that include a decision-making process map of how to deal with the top ten under performing intra-area city pairs. The approach was used to identify those routes with the most opportunity for improvement and those with the largest potential for improving performance scores.

- Reviewed and adjusted transportation configurations to maximize mail flow efficiencies between Hub and Spoke (HASP) operations and diverted mail from air to trucks to increase control over mail movement and reduce the risk of airline delays.

- Refocused efforts on the late arriving managed mail (LAMM) program that identifies late arriving transportation routes and patterns and targets them for improvement.

- Took steps to strengthen lines of communication between contiguous areas to ensure that performance issues and opportunities are honestly discussed so that improvements can be identified and made more quickly.

- Developed standard operating procedures for the Air Mail Centers to ensure that mail gets on the correct flights.

- Had AMC managers review area opportunity reports for two- and three-day mail, identify under-performing city pairs, and contact their counterparts in other AMCs to discuss root causes of problems and solutions that could be put in place to improve service.

- Focused on to intra-high failure contributing pairs by conducting weekly telecons with assigned personnel to pinpoint transportation problems and revamp transportation networks by instituting zero based procedures to meet service needs.

- Deployed Network Specialists to update and verify the accuracy of transportation management systems. This verification included correcting any discrepancies noted in distribution, labeling, routing, and dispatching.

- Adjusted critical entry and clearance times to facilitate the timely processing of high mail volumes.

These activities helped each of the Postal Service's operating areas to improve their performance for two- and three-day committed First-Class Mail.

129. The external first class (EXFC) service performance measurement system is audited by Ernst & Young as part of the financial audit.

(a) *Please provide a copy of the FY 1999 annual audit and discuss, in detail, the scope and method of the audit of the EXFC service performance measurement system.*

EXFC service performance is a compensable indicator in the EVA Variable Pay incentive program. Ernst & Young audits the results and payout information for each compensable indicator, comparing them to source documents.

The Postal Service does not have information on the audit methods used by Ernst & Young. A copy of the audit from the *1999 Annual Report* is attached (Attachment 10), as well as the Ernst & Young report entitled "Financial Statements, United States Postal Service, Years ended September 30, 1999 and 1998 with Report of Independent Auditors" (Attachment 11).

(b) *Did Ernst & Young find anything that required any adjustments to the results? If so, please describe the nature of those adjustments.*

No, Ernst & Young did not find any issues that required changes to the results.

130. In the past the Service has refused to publicly release the results of on-time delivery of Priority Mail.

(a) *Has the Postal Service changed its position? If so, please provide the results for the record.*

No, we have not changed our policy.

131. Some have argued that since Priority Mail is to a great extent protected by the statutory letter monopoly, the Postal Service should be obliged to release this data publicly, at least for the pieces that fall within the scope of the monopoly. This argument seems unassailable. The Postal Service told the Subcommittee last year that: "We believe that the general public is entitled to a level of information which allows them to grade our performance, particularly as it relates to the provision of First-Class Mail service, which benefits from the protections of the Private Express Statutes."

(a) *Please provide the results of on-time delivery for Priority Mail that falls within the scope of the Private Express Statutes.*

The Postal Service does not measure on-time delivery performance for the portion of Priority Mail that falls within the scope of the Private Express Statutes. On-time delivery performance is measured for Priority Mail as a whole.

(b) *Please provide the results of service performance measures for Standard A mail that falls within the scope of the Private Express Statutes.*

The Postal Service does not have a separate service performance measure for the portion of Standard Mail (A) that falls within the scope of the Private Express Statutes.

(c) *If your response indicates that the Service does not know which Priority Mail pieces fall within the scope of the Private Express Statutes, please provide the best available information or approximation of the percentage of monopoly-protected pieces and on-time delivery estimates for such mail.*

The Postal Service has not conducted a formal study of the percentage of Priority Mail pieces that fall within the scope of the Private Express Statutes. Any estimate of the percentage of Priority Mail falling within the Statutes would have to be based on the exterior shape or weight of Priority Mail pieces, and would not be statistically valid. The best available approximation of the on-time delivery estimates for this mail is the national on-time delivery data provided in the response to Question 131(e).

(d) *What was the split of total Priority mail pieces between letters/flats and parcels in FY 1998 and FY 1999?*

Priority Mail	FY 1998	FY 1999
Letters/Flats	34.9%	36.0%
Parcels	65.1%	64.0%

(e) *As we understand it, the external measurement system for Priority Mail uses only flat shaped pieces as test mail. Does the Postal Service have any external measurement service performance for parcel shape Priority mail? Please provide the Origin Destination Information System (ODIS) number of pieces by days to delivery (1 day, 2 day, 3 day, etc.) separately for flat and parcel shaped Priority mail for FY 1998 and FY 1999.*

The Postal Service does measure small parcels in its external Priority End-To-End (PETE) measurement system.

The following are the Origin Destination Information System (ODIS) results:

Shape	Fiscal Year	1-day Volume	2-day Volume	3-Day Volume
Flats	1998	114.2	155.8	50.5
Flats	1999	115.3	164.0	49.4
Parcels	1998	133.8	291.8	87.3
Parcels	1999	123.7	294.3	81.4

The above information excludes mail where the postmark information does not allow days to delivery to be calculated.

132. Last year, the Postal Service indicated to the Subcommittee that it intended to use delivery confirmation service performance information to evaluate the performance of Priority Mail.

(a) *Has that evaluation been done? Please report the results.*

The Delivery Confirmation system will be used to measure service performance in FY 2001.

133. The Executive Director of the National Federation of Nonprofits (NFN) wrote a letter to the Vice President of Field Operations Support at Headquarters. He reported that he is receiving an increasing number of complaints from members about severe delays in delivery of Standard A mail and about apparent non-delivery. He enclosed a letter and attachments from a member whose mail is about half the time late or not delivered. This situation is of great concern to the Subcommittee.

(a) *Please provide a copy of the response to the NFN's letter.*

A copy of the response is attached (Attachment 12).

(b) *What is the cause of such poor service performance?*

Service performance can fluctuate due to numerous variables, including the makeup of the mailing and the volume levels, staffing, routing processes, and even the weather at each individual location.

(c) *What actions has the Service taken to improve the service given to Standard A mail in general and Standard A Nonprofit mail in particular?*

We have taken a number of actions to improve Standard Mail (A) service. We have continued to deploy automated letter processing equipment, develop standard operating procedures for operations, and improve the readability of our equipment.

To improve service for flat-shaped mail, we have developed and deployed the Automated Flat Sorting Machine 100, added the Optical Character Reader to the FSM 881, added a barcode reader to the FSM 1000, and issued and updated a Strategic Improvement Guide for Flats Processing (October 1998 and September 1999).

(d) *Without a service performance measurement system for Standard A mail, how can the Postal Service ever hope to prevent and eradicate such poor levels of service?*

There are several methods used by mailers and the Postal Service to evaluate service. They include the use of Planet Codes to track mail and the use of diagnostics and reporting systems such as the Daily Mail Condition Report (DMCR) and review of on-hand volumes.

134. In June of 1997 the Postal Service contracted with REMITCO Management Corporation to operate a bill payment processing center in New York City. At that time, the Chief Marketing Officer (CMO) and Senior VP characterized REMITCO as one of several related service initiatives the Postal Service is working on to promote continued use of the mail for consumer bill payment and protect a strong revenue source. The REMITCO contract was seen as a logical extension of the core business of the Postal Service—processing First-Class Mail. The CMO claimed that slowing the migration of mail-based remittances to electronic and other alternative forms of payment will save Postal Service jobs.

In the 1998 Comprehensive Statement the Postal Service stated that REMITCO is a very high volume retail remittance payment service and that it is planned as a national network of processing locations. The GAO reported in November of 1998 that through Quarter 3 of FY 1998 REMITICO shows a loss of $6.3 million on revenue of only $2.3 million.

It has recently been reported that REMITCO was purchased by its management team. The Board of Governors reportedly deemed that it was inappropriate for the Postal Service to compete with the private sector in the payment processing business. The manager of retail payment programs reported that the Board of Governors didn't believe Service should be in the remittance processing industry.

(a) *What are the final revenue, cost and loss/profit from REMITCO for FY 1998 and FY 1999?*

For FY 1998, total revenue was $4.4 million and costs were $12.4 million, resulting in a loss of $8 million for the year. In FY 1999, total revenue was $5.7 million and costs were $13.9 million, resulting in a loss of $8.2 million.

(b) *What were the terms of the sale to REMITCO management? Did the Service recover its $2 million investment in the New York facility?*

In July 1999, the Postal Service completed a legal agreement to transfer the ownership of REMITCO from the Postal Service to the REMITCO Management Corporation. The primary goal of transferring REMITCO to the private sector was to ensure the continuation of excellent service to our customers. The secondary goal was to minimize the financial costs and risks to the Postal Service attendant to the transfer.

As part of the agreement, the Postal Service agreed to transfer to the REMITCO Management Corporation (RMC) all furniture and equipment at the facility in exchange for the ownership of the operation. The Postal Service also agreed to fulfill the contractual terms of the agreement with some of our major mailers that extended through 2001. Also included in the agreement was the cost of existing operations, maintenance contracts, and lease payments. RMC assumed the remaining terms of the existing contractual commitments and liabilities with our customers. With the Postal Service not currently in a position to rapidly expand the REMITCO operations to multiple sites throughout the United States, we felt it was most appropriate to transfer the business to a private company to ensure continued service to some of our largest customers for remittance mail. The Postal Service would have incurred further operating losses if it had continued to honor customer contracts with just one site in operation.

The $2 million associated with the New York facility was part of the start up costs of the REMITCO program and is reflected in the overall results reported in the response to Question 134(a).

(c) *What are the current duties and responsibilities of the manager of retail payment programs? What other new retail payment programs does the Postal Service have under development? What ever happened to Customer Initiated Payment System (CIPS)?*

CIPS has been discontinued and the position of Manager, Retail Payment Programs, has been abolished. No new payment programs are being developed.

(d) *Does the Postal Service believe that the REMITCO venture was at all successful in promoting the continued use of the mail for customer bill payment?*

The Postal Service's primary goal in establishing REMITCO was to encourage companies that send high volume of bills to consumers to maintain or increase their use of First-Class Mail. While limited to just the one site, the Postal Service was successful in attracting six major companies to process their remittances through the REMITCO operation. REMITCO also focused the Postal Service on remittance mail and remittance mailer needs. The remittance mail float model and a national firm hold out program grew out of the REMITCO program.

135. The Postal Service revenue protection program includes eligibility reviews that sometimes result in reversals of rulings. This often results in significant postage due bills for mailers.

(a) *Does the Postal Service collect information with regard to the nature, scope and size of such rulings? If so please provide a summary of all activity over the last year.*

The Postal Service's revenue protection program is an interdepartmental initiative involving Marketing, Finance, the Inspection Service, the Office of the Inspector General, and legal personnel. Through this program, the Postal Service strives to ensure that it is paid for the services that it provides. In the process, we seek to treat all customers equally, making sure no mailer has an unfair advantage over those who submit similar mailings.

The primary focus of revenue protection efforts is to ensure that the Postal Service is fully paid for mailings at the time of acceptance, thereby eliminating the need to review past mailings. The Postal Service is continually exploring new technologies and systems to help it achieve this goal, and a number of initiatives will be in place soon. The program also provides substantial training in mailing standards for customers and postal employees; these educational programs ensure that mailers design, prepare, and submit mailings that qualify for the rates claimed.

As the question indicates, a portion of the revenue protection program involves reviews that can result in findings that postage was underpaid on past mailings. These reviews may result in the assessment of postage due. Procedures for review and collection of these assessments have recently been revised with input from our customers. In the majority of cases, these assessments do not reverse previous rulings. The problems that arise are generally those that postal clerks or other personnel at the entry post office cannot practically review in an expeditious manner. There are a relatively small number of cases where mailers have received erroneous written information from postal personnel, usually at a local office. In these cases, postal finance officials are authorized to waive any assessments resulting from that erroneous advice.

One element of the revenue protection team is the Revenue Assurance Group in the Finance department. The Revenue Assurance Analysts develop reports that provide the basis for many revenue deficiency assessments. In FY 1999, the analysts identified $84.4 million in revenue deficiencies in 13 categories shown below.

($ in thousands)

Service Option	Amount
Standard Mail (A)	$31,914
Periodicals	$19,094
First Class Mail	$17,225
OMAS	$7,377
Postage Due/Business Reply	$4,282
Specialized Programs	$1,842
P.O. Box Rental	$888
Caller Service	$823
Express Mail	$400
Standard Mail (B)	$302
Postage Meters	$120
Bulk Mailing Fees	$61
Miscellaneous	$53
Total	$84,381

136. The lack of consistency in the application and interpretation of mailing requirements and regulations has been a major concern to mailers who often are victims of a reversal of historically and agreed upon practice.

(a) *Has the Postal Service beefed up its training efforts in this area to assure that mail eligibility personnel "get it right the first time"?*

As part of the Business Mail Entry Unit (BMEU) Proficiency Program, 16 hours of technical training is provided annually to the approximately 4,800 business mail entry employees. Each employee is taught probing skills to help them get more specific, accurate responses from customers.

Through the Mystery Caller program, we continually measure the proficiency of our clerks and provide them with additional training focuses areas that need improvement. The measurements are published quarterly.

In addition, training for new employees has been centralized at the BMEU Academy at the National Employee Development Center in Norman, Oklahoma. We expect to train approximately 500 new employees each year at this state of the art facility, which replicates the actual BMEU work environment. This approach will ensure greater consistency in the way training materials are presented and in the information that customers receive at different mailing locations.

137. In a 1996 GAO report, the Postal Inspection Service has said that theft of mail from mailboxes is a very serious problem. Last year in response to the Subcommittee questions the Service reported on efforts to prevent theft of mail from mailboxes.

(a) *Have these efforts been effective? Please update the statistics on mail theft you provided last year.*

The Postal Inspection Service has seen a decline in mail theft volume attacks over the past two years. A volume attack is defined as the theft of mail from a receptacle designed to hold large quantities of mail. In FY 1998, the number of volume attacks was 4,570; in FY 1999 the number was 3,435, a decrease of 25 percent. The Inspection Service believes that preventive measures, such as adding enhanced security features to the Neighborhood Delivery Collection Box Unit (NDCBU) and USPS Collection Box have significantly contributed to the reduction in the number of volume attacks.

Due to the decrease in the number of mail thefts, the Inspection Service has been able to put greater focus on the resolution of these crimes. In FY 1998, Postal Inspectors arrested 4,397 non-employees for mail theft; in FY 1999 the number of arrests increased by 4 percent to 4,550.

138. The "Stamp Out Breast Cancer Act," enacted August 13, 1997, required that the Service market, for 2 years, a semipostal stamp to raise money for breast cancer research. The Service's Breast Cancer Research stamp is priced at 40 cents—33 cents for postage with a 7-cent surcharge. The net proceeds from the surcharge are being given to the National Institutes of Health (NIH) and Department of Defense (DOD) for breast cancer research. If the Breast Cancer Research stamp is successful, and there is overwhelming support for additional semipostal stamp issues, how would the Service respond to such questions as:

(a) *Which types of causes should be supported by a semipostal stamp?*

In our view, if any new semipostals are issued, they should be reserved for causes that are of great national concern and critical, imminent need.

(b) *How many different semipostal stamps should be issued each year?*

Due to the complexity of the process, we would advocate that no more than one semipostal be issued each year.

(c) *If semipostal stamps were to become a permanent fixture within the Service, what changes, if any, would the Service make to its infrastructure to accommodate the new stamps?*

It is difficult to determine without further study. Specific criteria would have to be developed and a review committee established to determine what changes we would need to make to our infrastructure.

(d) *Assuming that the Breast Cancer semipostal is successful, what plans does the Postal Service have for independently issuing semipostal stamps, without awaiting Congressional mandates?*

The Postal Service has no plans to issue semipostal stamps without Congressional mandates.

(e) *Would the Postal Service consider developing a new process and separate criteria for the Citizens' Stamp Advisory Committee to use in making semipostal decisions?*

It would be extremely difficult for the Citizens' Stamp Advisory Committee to develop a new process and separate criteria for selecting semipostal subjects. There are hundreds, if not thousands, of worthy causes and organizations that exist today, and it would be difficult to rank one ahead of another. Another complicating factor is the fact that many organizations have asked for semipostals over the years and been turned down. Fairness would dictate that they be given due consideration.

139. The Stamp Out Breast Cancer Act states that the Postal Service is to deduct its reasonable costs from the surcharge associated with the sale of the semipostal Breast Cancer Research stamp.

(a) *What costs are the Service tracking, and what percent of the stamp's 7-cent surcharge is the Service retaining to cover costs?*

Through Accounting Period 5, ending January 28, 2000, the Postal Service has retained $200,000 in costs out of the $11.1 million raised for research.

The costs we are currently tracking include: stamp design, printing and manufacturing, employee training, the reprogramming of window automation devices, market research, advertising and promotion, the printing of customer receipts, stamp packaging, vending machine reconfiguration, and legal fees. If additional costs are ascribed, we will update our figures.

140. Last year the Postal Service reported on its relationship with Treasury. You reported that your meetings with Treasury had been cordial and have served to increase understanding regarding the other party's viewpoints. You reported that many questions remain regarding Treasury's capability to deliver certain important financial services. You reported that relatively straightforward issues have remained unresolved.

(a) *Please update us on your efforts to improve your working relationship with Treasury.*

Our working relationship with Treasury has improved substantially over the past year. We have reached agreement with Treasury on key borrowing and cash management issues, and we have ongoing dialog with Under Secretary Gary Gensler and Fiscal Assistant Secretary Donald Hammond and their staffs.

(b) *Have those supposedly straightforward issues been resolved?*

Yes. We have resolved all outstanding issues with Treasury.

(c) *What is the status of your dispute with Treasury over note purchases agreement language that, in your view, would dilute the Service's authority to determine its cash and debt balances?*

We have reached agreement on all issues. In March 1999, the Postal Service and Treasury signed a Note Purchase Agreement that addressed the concerns and met the objectives of each party.

(d) *Has the overnight borrowing cap been raised from $300 million to $1 billion as you expected last year?*

The Note Purchase Agreement contains terms that permit the Postal Service to borrow up to $600 million overnight on same-day notice. Together with other short-term borrowings available under the Agreement, the $600 million level meets the Postal Service's needs.

(e) *Has the Treasury been more timely than in the past in responding to the Service's needs for new products?*

Treasury has been quite responsive to the Postal Service. Overall, we are very pleased with Treasury's service and with the state of the relationship.

141. On September 10, the Subcommittee on Government Management and Technology gave the Postal Service a "D" on its listing of High Impact Federal Programs' Year 2000 Readiness. That Subcommittee did not at that time consider the Postal Service ready for Y2K.

(a) *Has the Postal Service reviewed the basis for the "D" grade? Do you understand why you got a "D"? Has the Service taken action to improve your grade as determined by that Subcommittee? Will the Postal Service be ready?*

While the Subcommittee's assessment included a number of important program elements, it was not an assessment of our overall readiness status. Rather, the Subcommittee reviewed information involving readiness of a limited number of key suppliers and electronic data interfaces. At the time of the assessment, one interface test had not been performed because the firm had not completed its system work. Testing, however, was successfully performed on October 4, 1999.

142. During the joint hearing before three House subcommittees in February, Chief Technology Officer Norman E. Lorentz expressed his confidence the Postal Service is taking on the challenge that everything possible is being done to minimize the potential for disruption that could arise from the Year 2000 computer problem. Though the Postal Service may be up and running, it is dependent on numerous contractors for its success.

(a) *Please update the Subcommittee on the readiness of Postal Service contractors.*

The vast majority of Postal Service critical contractors were Year 2000 ready. To be considered Year 2000 ready, a company needed a readiness program in place that has the support of executive management. In addition, the company must have remediated and tested its mission critical systems and facilities, investigated the Year 2000 readiness of its own suppliers, and put in place contingency plans to mitigate unanticipated Y2K-related problems. Our actual rollover experience validated the conclusions we had drawn regarding the readiness of our key suppliers/contractors.

(b) *On how many contractors and suppliers is the Postal Service dependent?*

As of December 1, 1999, Postal Service Headquarters identified 266 national critical suppliers, and the field organizations identified an additional 712 local critical suppliers.

(c) *How many Postal Service contractors are Year 2000 ready?*

By December 1, 1999, 100 percent of the Headquarters-identified critical suppliers were Year 2000 ready or expected to be Year 2000 ready. Of the critical suppliers identified by the field organizations, 99 percent were ready or expected to be ready. One percent of the local suppliers had Year 2000 related issues that required close monitoring. For these suppliers, contingency plans were developed to mitigate the potential risks. Our experience during the Year 2000 rollover period validated the assessment of supplier readiness.

(d) *What assurances does the Postal Service receive that the contractors are ready?*

The Postal Service assesses a supplier's readiness based on all available data, including SEC disclosure statements, responses to a USPS Year 2000 questionnaire, discussions with company representatives, publicly available information, and in the case of key suppliers, on-site visits. The readiness assessment efforts of the Postal Service are contingent upon supplier cooperation and are consistent with federal and commercial standards and practices. Having come through the rollover period with no significant issues—internally or externally—we believe that our preparatory and cooperative work with suppliers provided us with accurate assessments of their capabilities during that critical time.

(e) *Is there a penalty for affirmative assurances that prove to be erroneous?*

There is no special contract clause or other legal authority that authorizes the Postal Service to conduct Y2K-related audits, or to compel a company to provide Year 2000 information. However, if a company is unable (due to Year 2000 failure or any other problem) to provide the goods or services for which a contract is in place, the Postal Service would be able to take action under the default terms of the contract.

It should be noted that most affirmative assurances we have received from our suppliers contain a standard Information Readiness Disclosure Act notice that grants them some protection regarding the information disclosed if it was provided in good faith.

(f) *What are the contingency plans for alternative service?*

Supplier contingency planning may include alternatives such as a process change, a work-around, the stockpiling of supplies, the identification of alternate suppliers, or some combination thereof.

(g) *Is the Postal Service within its goals to have its mission critical systems tested and verified by September 1999? How many of the mission critical systems are compliant (what percent?)? Is the remediation system on schedule? Are the business continuity and contingency plans in place and verified? Is there a complete inventory of embedded chips? What is the status of the important but not mission critical systems?*

All 137 of the Postal Service's mission critical systems were certified as Year 2000 ready before January 1, 2000. As an additional level of assurance, each system also successfully passed an independent verification process. The deployment of our one remaining Important but Not Mission Critical system, the Organizational Management Staffing System, supports organizational staff planning and is not essential to the Postal Service's core business processes. A work-around for this system was implemented. Our Business Continuity Plans were developed and rehearsed. The Postal Service also assessed the processes that rely on embedded chips, consistent with recommendations of a recognized Year 2000 consulting firm. We are confident that the processes relying on embedded chips will operate correctly.

142. As we know, most computers exchange data with other computer systems. However, external data that is not Y2K compliant can easily corrupt computer systems that are Y2K compliant.

(a) *Is it part of your commitment to have a complete inventory of the data exchange, particularly with external exchanges? Do you know which ones of these exchanges are compliant? Is this data shared with any other agency?*

The Postal Service completed its external data exchange inventory before January 1, 2000. Our Year 2000 readiness efforts on external interfaces were also completed. Readiness efforts included sharing data with our government and commercial business partners where appropriate.

143. The Postal Service has a major responsibility, and some may even say an obligation, to avoid malfunctions so that mail services remain stable – even though the rest of the country may face computer malfunction. There is every possibility of a mail surge – not only because of the holiday season mail but also because other entities are relying on mail service over e-mail, e-commerce or fax. There is significant cost to avoiding these inherent problems.

(a) *Has the Postal Service stayed within its projected $500 to $700 million budget to fix the Y2K problem?*

Yes. When all accounting has been completed, it is likely that project costs will be at the low end of this range.

(b) *If there is cost overrun in this regard, how is it explained?*

There has not been a cost overrun.

(c) *Does the fact that the Postal Service got a late start in the Y2K correction process add to the cost?*

No. We have not experienced a material increase in cost over our original estimate.

(d) *Are Postal employees in full partnership with the contingency plans of Y2K?*

Yes. All contingency and continuity plans were distributed to appropriate functional units and reviewed by responsible individuals. Plan "dress rehearsals" were conducted from November 18 through December 6, 1999. More than 8,000 rehearsal tests involved over 10,000 employees in more than 40 job categories. Scenario categories were Marketing, Logistics, Finance, General Infrastructure, Engineering, Processing, and Delivering.

(e) *Are/will schedules for all tasks be posted in plenty of time so employees are on notice of the plan?*

Schedules were posted or reported to affected employees in sufficient time so that critical operations were staffed properly during the changeover weekend.

144. Prior to the Postal Employees Safety Enhancement Act of 1998, the Postal Service was required to comply with Occupational Safety and Health Administration (OSHA) safety and health programs for federal agencies. The act, however, requires the Service to comply with standards for private sector employers and, as such, OSHA may now issue the Service citations and levy monetary penalties for noncompliance.

(a) *Please describe the Service's progress in implementing the requirements of the Postal Employees Safety Enhancement Act, including challenges faced and time frames for completing remaining work.*

Upon implementation of Public Law 105-241, the Postal Service established a transition team to meet with OSHA officials to discuss how the two agencies could work together to ensure a smooth transition. The Postal Service's safety and health program has long complied with OSHA requirements for federal agencies contained in section 19 of the Occupational Safety and Health Act of 1970, applicable Executive Orders, and implementing regulations found at 29 Code of Federal Regulations Part 1960.

Because the basic intent of the PESEA is to treat the Postal Service like a private sector employer, the Postal Service had to review and modify existing policies, programs, procedures, systems, training, and education programs to convert them from federal agency requirements to those which apply to the private sector. With 800,000 employees, more than 35,000 facilities, and program policy documentation that historically has been recognized as comprehensive, this has been a major challenge which postal management has taken seriously. In meeting this challenge, we were careful not to abolish existing programs and policies that have served us well in the past and can serve us well in the future.

Accordingly, a multi-faceted plan was established to focus on organizational safety and health infrastructure, including policies, programs, systems (including recordkeeping), safety and health training and education programs, safety and health inspections, and safety and health compliance activities.

Cross-functional implementation teams were established to develop and implement the appropriate changes to meet the private sector requirements. Actions to date include, but are not limited to, the following:

- Postal Employees' Safety Enhancement Act seminars were provided throughout the Postal Service to ensure managers understand the impact of the law and their responsibilities to promote safe and healthful working conditions.
- Development and distribution of an executive/managers guide to complying with the act.
- Briefing of labor unions and management organizations concerning the PESEA.
- Continuance of an OSHA training program for maintenance supervisors and safety personnel.
- Establishment of an OSHA citation tracking system to monitor management actions and to notify headquarters, area, and field units to focus on conditions which have resulted in citations.
- Training programs for safety personnel, legal staff, and key operations staff on the judicial, and other processes that previously were not applicable to the Postal Service.
- Instructions were issued to field units to establish a new manual system of records in order to comply with OSHA's recordkeeping procedures. Recordkeeping training was conducted through the Postal Service's television network by the National Safety Council.
- Discussions were established with OSHA to determine their interest in participating in further recordkeeping training.
- Required OSHA posters were acquired, distributed, and posted throughout the Postal Service.

- Internal safety and health inspection procedures are in the process of being automated to assist Postal Service safety and health professionals conducting inspections.
- The Postal Service financial system has been modified to track the associated expenses.
- Safety and Health consulting services have been utilized to supplement internal resources.
- An enhanced system was established to measure safety and health performance modeled after OSHA's program evaluation profile.

The Postal Service's safety and health program contains the following program elements. These are ongoing activities, which did not begin or end with the PESEA.

- Safety and Health Administration
- Safety and Health Inspections
- Safety and Health Training
- Safety and Health Promotion and Education
- Safety and Health Standards
- Safety and Health Committee Activities
- Accident Investigation, Reporting, and Analysis
- Safety Engineering

The major challenges have largely been associated with modifying existing automated systems in a year in which government, industry, and the Postal Service are dedicating their technical resources to ensure Y2K compliance. This challenge was exacerbated by the intended change in recordkeeping procedures that OSHA was preparing for implementation beginning January 1, 2000. Subsequently, OSHA has adjusted their intended implementation date to begin January 1, 2001.

We established a manual system to comply with OSHA's private sector recordkeeping requirements. This is, however, unnecessarily burdensome and confusing, and is not considered an enhancement when compared to the existing requirements for federal agencies. Our transition team will continue to focus on recordkeeping issues in its discussions with OSHA officials and will work toward compliance with OSHA's proposed recordkeeping rule.

(b) *What are the potential effects (short and long-term) on the Service from provisions in the Postal Employees Safety Enhancement Act stating that (1) postage cannot be increased to help pay for compliance with the Occupational Safety and Health Act of 1970, (2) the Service may not consider compliance with the Occupational Safety and Health Act in determining whether to close or consolidate a post office, and (3) the Service may not restrict, eliminate, or adversely affect any service as a result of any penalty imposed under the Occupational Safety and Health Act?*

We believe it is too soon to evaluate the impact of the provisions of the law that restrict the Postal Service from increasing the cost of products/services and closing or consolidating post offices in order to comply with the Postal Employees Safety Enhancement Act.

(c) *Since enactment of the Postal Employees Safety Enhancement Act, how many citations has OSHA issued the Postal Service?*

During FY 1999, there were 121 OSHA inspections that resulted in citations involving Postal Service operations. During this period, OSHA initially issued 162 serious, 167 other-than-serious, and 9 repeat violations to postal establishments. Following discussions to clarify the respective issues, OSHA modified these to total 47 serious, 138 other-than-serious and 1 repeat violation. During FY 1999, the initial proposed penalties totaled $270,962. Following settlement, $79,273 was authorized for payment nationally. Several cases are pending further discussion. Once settled, changes will be made to these figures.

During FY 2000, OSHA has completed 25 inspections resulting in 25 serious, 35 other-than-serious and 1 repeat violation. The initial proposed penalties total $38,825. Thus far, the settlement of these cases has resulted in one serious and two other-than-serious violations with $575 being authorized for payment. Work is ongoing to bring closure to the remaining cases. It should also be noted that many additional inspections have been conducted for which no citation was issued.

(d) *For what type of safety or health violations were citations issued?*

The types of violations vary by location. The most frequent issues that arise during OSHA inspections involve partial obstruction of aisles, improper use of extension cords, inadequate documentation of training records, and contractor-related work involving the disturbing of building materials that may contain asbestos.

(e) *What progress has the Service made towards correcting violations?*

Prompt management attention is given to the abatement of OSHA citations and the resolution of safety and health complaints filed by employees and their representatives. Many cases have been settled and resolved, as discussed in the response to Question 144(c).

(f) *Since enactment of the Postal Employees Safety Enhancement Act, how much has the Postal Service paid in penalties?*

To date, nearly $80,000 has been authorized for payment nationally. More information is contained in the response to Question 144(c).

(g) *To what extent were the OSHA requirements a significant influence in the recent establishment of safety agreements with the labor unions?*

In addition to the safety and health provisions contained in applicable collective bargaining agreements, the Postal Service has entered into memorandums of understanding (MOUs) with the American Postal Workers' Union, the National Postal Mailhandlers Union, and National Rural Letter Carriers' Association that establish internal processes to jointly resolve unsafe conditions. These MOUs supplement established programs and processes and encourage the parties to utilize safety, maintenance, and other available resources to develop solutions to safety and health issues. While it is too soon to evaluate the success of the MOUs, we are optimistic that this approach will prove to be beneficial to both labor and management.

145. The Postal Service has said it is planning to undertake a major multi-year initiative to develop a definition of universal service and specify its meaning with respect to service requirements. The Service published a Review of Universal Service in Other Postal Administrations in its FY 2000 Performance plan. Last year the Postal Service indicated it would [conduct] a review of the experience of other industries as well that have sought to define universal service concepts (such as the telecommunications industry subsequent to the Telecommunications Reform Act of 1996 and the electric utility industry). The Service also indicated it would during FY 1999 launch a stakeholder outreach effort on universal service. The process was to involve input from Congress, your Board of Governors, residential and business customers, competitors, individual employees at all levels of the Postal Service, and unions and management associations.

(a) *Does the Postal Service intend to follow through on its plan to review and report on the experience in other industries with definition universal service?*

The Postal Service will provide this review in its Preliminary FY 2001 Annual Performance Plan, which will be included in the 1999 Comprehensive Statement on Postal Operations.

(b) *What is the status of the stakeholder outreach effort on universal service? When can we expect the findings to be reported?*

Limited discussions of universal service were held with various stakeholders during FY 1999. The Postal Service plans to address this subject in a stakeholder outreach effort during FY 2000 as part of preparations for its next five-year strategic plan. Postal universal service will be addressed in a *Federal Register* notice to be published by next April. The results of this outreach effort will be summarized in the Postal Service's FY 2001-2005 Strategic Plan, which will be published next September.

(c) *Has the Postal Service reviewed the study carried out for the European Commission by the Nera consultancy that estimated universal service costs at 5% of the EU Postal operators total revenue in the core letter mail area? Has the Postal Service formed an opinion as to the accuracy of the study? Does the Postal Service agree that the 5% estimate for the cost of universal service, as it currently defines universal service, is a close proxy for the cost of universal service in the U.S.? Has the Postal Service developed any estimate of such cost? If so, please report the results. If not, why not?*

The Postal Service has reviewed the NERA study. The review revealed two weaknesses that suggest caution must be used in considering its results. First, by its own admission, the study is based upon very limited data. Second, the study employs only one method of calculating the cost of universal service. This method, known as the "Net Avoided Cost" (NAC) method, is known to have theoretical drawbacks and typically produces low estimates of the cost of universal service.

Though the Postal Service has not developed any official estimate of its universal service costs, two postal analysts (including one postal employee) presented a paper on this topic at a recent conference. The paper, by Professor Michael D. Bradley of George Washington University and Jeff Colvin, Manager of Cost Attribution for the Postal Service, is entitled "Measuring the Cost of the Universal Service for Posts." A copy is attached (Attachment 13). The paper, which will be published in *Current Directions in Postal Reform*, ed., by M. Crew and P. Kleindorfer, presents data suggesting that the cost of the Postal Service's universal service obligation is significant.

146. The Subcommittee has heard reports that the Postal Service has a policy, at least in some districts, of shredding oversized postcards when they do not contain return address information. However, if there is a return address, the mail handlers are asked to place the postcard in a plastic mailer and it is returned to the sender. Postal officials in the Miami area [have] reportedly told the media that the oversized cards cannot be read by automated equipment.

(a) *Has the Postal Service done any sort of study to determine the efficiency of shredding the cards vs. hand-canceling?*

The Postal Service has not conducted any study of this nature.

The size of the postcards and postal cards, and whether or not they can be processed on automated equipment, are not and have never been discussed in our national policy on this issue.

The current policy concerning the disposition of postcards and postal cards has been in place since June 16, 1989. In the past ten years, the wording of our policy has been modified, but the intent and implementation have not changed. The current policy statement is found in the *Postal Operations Manual* Issue 8, (POM) Section 691.583. It reads as follows: "Dispose of postcards and postal cards without a return address if the post office can shred or destroy them completely. If not, they should be forwarded to the area MRC (Mail Recovery Center)."

(b) *Has there been and effort to reach out to the manufactures of such cards to alert them to this policy?*

Given the fact that this policy is more than a decade old, we cannot be sure if there has been an effort to make postcard manufacturers aware of this policy. We are not aware of any such efforts in recent years.

(c) *Has there been an effort to educate and alert postal consumers of this policy?*

Given the fact that this policy is more than a decade old, we cannot be sure if there has been an effort to make consumers aware of this policy. We are not aware of any such efforts in recent years.

147. In November 1998, 250 Mail Boxes, Etc. (MBE) Centers began a two-year pilot test program with the Postal Service as "Authorized USPS Retailers." The participating MBE Centers are allowed to sell stamps at cost, while continuing to sell all other postal products, including Priority and Express Mail, at full retail rates. Each test location is reported to receive incentives of 5, 10, 20, and 25 percent for Stamps, Priority, Express Mail and all other metered mail, respectively. In addition, the MBE's were given special support service and are allowed to sell certified, return receipt and insured mail. Expansion beyond the original 250 offices was to be considered after 6 months.

(a) *What is the status of pilot program? Are there any plans to expand the program beyond the pilot offices? If so, please discuss briefly the business case for expansion.*

The pilot program has just completed the first year of a test that is now expected to continue for up to three years. On February 11, 2000, the Postal Service announced that it will expand the pilot program with Mail Boxes, Etc. (MBE) to some 700 additional locations, primarily in the Southeast and Southwest regions of the nation.

The case for future expansion will be based on customer convenience and access, the ability to use technology for reporting and payment purposes to reduce administrative costs, and the expansion of expedited package service revenue through the small business/household customer base of MBE outlets.

(b) *What has been the impact of the program on postal and contract station revenues and cost? How much incremental revenue and contribution to institutional cost has been generated as a result of the pilot program?*

Limited migration studies did not show any significant impact on postal facilities or on existing contract stations. There is no cost correlation between the MBEs and post offices or contract stations. During the test phase, there is not sufficient data to measure incremental revenue and contribution.

(c) *How are the incentives structured? Are these percentages of revenue? For example, does the participating MBE store receive 1.65 cents (or 5 percent) for selling a 33-cent stamp?*

Participating pilot sites receive zero base pay. Franchisees receive 20 percent of sales for domestic Priority Mail and Express Mail packages. Stamps must be sold at face value and are compensated at five percent of sales. Compensation for other metered (products other than Express and Priority Mail for which a meter strip is affixed) and special services such as certified, return receipt, and insured is five percent. The average cost per revenue dollar is approximately 8.27 percent, compared to an average cost of 10 percent at existing contract stations.

148. Concern has been raised over the quality of the Classroom Periodicals cost and volume data. The Postal Service cost data on the Classroom Periodicals Subclass has been suspect, so much so, that it has not been used for ratemaking. The Subcommittee would like to know if the Postal Service is addressing the issues impacting this small but important subclass of mail.

(a) *Does the Postal Service recognize the intrinsic educational value of Classroom publications in developing its proposed rates?*

Yes. In general, as a preferred subclass, Classroom is assigned a markup that is one-half the markup of the Regular Periodicals subclass. The very low markup on periodicals considers the educational, cultural, scientific, and informational value of these publications.

(b) *How has the Postal Service worked with classroom publishers to reduce its handling costs by better automation techniques and closer cooperation?*

Classroom publishers have been very sophisticated in their efforts to take advantage of automation discounts and other cost-saving tools. We have had discussions with the Classroom publishers on many topics, most notably cost measurement issues.

(c) *Why does the In-Office Cost System sampling process for Classroom publications produce a standard deviation of as much as plus or minus 25% in any given year?*

Generally, the smaller the cost proportion being estimated by the In-Office Cost System (IOCS), the larger the coefficient of variation of the estimate. Classroom Periodicals account for less than one-twentieth of one percent of mail processing costs, creating the large coefficient of variation. For mail categories handled in only a few operations or in a limited number of facilities, it may be possible to improve the precision of the estimate by increasing the sample size in only those operations or facilities. However, Classroom Periodicals are handled nationwide in numerous operations, so it would be difficult to reduce the coefficient of variation of their estimated cost in any way other than an across the board increase in the IOCS sample size for clerks and mail handlers. To reduce the coefficient of variation from 25 percent to 10 percent, for example, would require 6 times as large a sample. Currently, with a sample size of 850,000 (468,000 clerks and mail handlers), the Postal Service spends approximately $12.5 million collecting IOCS data. To get Classroom Periodicals estimates with 10 percent coefficient of variation may require over 2.8 million samples of clerks and mail handlers, 0.4 million other samples, and cost an additional $34.5 million. Since the FY 1998 revenue from Classroom Periodicals was only about $12.2 million, such an augmentation of the IOCS sample size for the purpose of decreasing the sampling error for this subclass is not financially justifiable.

(d) *Does this anomaly suggest a need for revising the sampling process for classroom publications as suggested by the Postal Rate Commission?*

See the response to Question 148(c).

(e) *Is the Postal Service concerned that the annual volume of classroom publications has dropped significantly over the last five years and that the future of this educational product is endangered?*

Actually, revised figures made several years ago show that Classroom volume has remained in the 60-65 million range from 1992-1999. Nevertheless, volume loss is always a concern to the Postal Service, and certainly everyone understands the value of educational materials. We want to work with mailers to keep our costs low so that price increases can be restrained. The higher value our products offer, the more likely it is that volume will be sustained.

(f) *How do you respond to those who claim that the cost of implementing a discount for educational publications such as classroom can be absorbed since the cost of the discount represents a "de minimis" amount of the $60 billion annual revenue stream?*

Currently, Classroom publications are given favorable rate treatment under the Revenue Forgone Reform Act. Commercial rates are slightly higher to accommodate this preferred rate. If further rate preferences were extended, they also would be financed by commercial mailers unless a specific appropriation was provided. While the amount may be small relative to the total annual revenue, one should consider the public policy implications of shifting revenue burden to other parties, as well as the potential ramifications of pricing services below their costs.

149. Last year the Service reported on a three-year-old wage dispute between the Postal Service and pilots who fly Express and Priority Mail under the ANET contract. The Service contended that ANET pilots are paid the same wages for flying aircraft carrying mail that they are paid for transporting the commercial cargoes. At that time, the Service was a party to an ongoing administrative proceeding at the Department of Labor (DOL), involving the appropriateness of certain wage determinations issued in 1996 by the DOL Wage and Hour Division (WHD) under the McNamara-O'Hara Service Contract Act, as amended, 41 U.S.C. § 351 et seq. (SCA). Last year the WHA's decision on this issue was still pending.

(a) *What is the status of the WHA's decision on this issue?*

In a ruling on September 16, 1998, the Wage and Hour Administrator concluded that the ANET pilots at issue in the case were not professional employees and were thus not exempt from the Service Contract Act. The Postal Service, the ANET contracts, Emery Worldwide Airlines, Inc., and other postal contractors appealed this ruling to the Labor Department's Administrative Review Board (ARB). Briefs were filed. The Board heard oral arguments in June 1999. In addition to the professional exemption issue, the arguments addressed the mid-contract changes that the Wage and Hour Division made in its methodology for determining the pilot wages. These changes resulted in unprecedented wage increases (approximately 60 percent for first officers and over 100 percent for captains). The resulting wages were well above the prevailing market rates paid by air carriers in the business of providing dedicated cargo air transportation. The case is awaiting the decision of the ARB.

(b) *What was the impact of the decision, if any, on the wages paid to ANET contract pilots as well as total cost to the Postal Service?*

The WHA's decision has not yet had any impact on the wages paid to pilots. The decision was appealed to the ARB and is awaiting decision by the ARB.

(c) *What other ramifications does this decision have, if any, on other Postal Service services contracts?*

The final outcome of this matter potentially could affect all of the Postal Service's contracts for dedicated air service. If the Postal Service and the other appellants do not ultimately prevail, the wage determinations could negatively impact the Postal Service's air transportation programs by reducing competition for postal air contracts. Some of the key carriers that provide dedicated cargo contract service have stated that if they must pay minimum SCA wages so much higher than the prevailing rates, they might be forced to forgo future postal contracts in order to avoid adopting an above-market wage scale in their commercial work. Alternatively, if such contractors do take on postal work, then the higher wages will substantially increase the price that the Postal Service must pay for its dedicated air contracts.

150. Last year the Postal Service reported on the development and use of the Purchasing Assessment Report (PAR) and noted that it was then developing a Purchasing Review for Excellence Program (PREP).

(a) *Please report how PAR has been used to identify needed improvements in purchasing performance and internal control.*

The PAR was originally developed under the premise that in order to improve you must be able to measure. Since FY 1996, the PAR has provided a uniform set of measures that can be used to identify areas needing improvement, as well as those showing improvement. Some of these areas include customer satisfaction, professionalism of our purchasing personnel, cycle time, and diversity in our supplier base. The high level summary data provided assists managers in targeting opportunities and supporting process improvement efforts. A primary benefit of the PAR is having uniform purchasing statistics readily available when requested by both internal and external organizations. In the past, satisfying requests for purchasing statistics was a time-consuming and cumbersome effort.

(b) *What is the status of the PREP and has it been effective in enhancing the performance of the purchasing program?*

The Purchasing Review for Excellence Program (PREP) was designed to provide a results-oriented assessment of Postal Service purchasing activities. The program concept was piloted and completed during FY 1999. The pilot included review of two purchasing activities. Based on the results of these reviews, as well as current staffing and financial realities, the program was finalized and calls for performing two to three reviews each fiscal year.

As a result of related benchmarking studies, we also revised the PREP to include a self-assessment program using a cascading process. With the cascading process, copies of PREP, OIG, Inspection Service, or other oversight reviews will be cascaded down to applicable purchasing activities (which could reach up to 140 offices). The reviews will be used as a baseline to assess their various organizations and to report results. The emphasis of the self-assessment is to identify and correct existing or potential problems and to adopt best practices as appropriate. In FY 2000, we have already cascaded for self assessment one OIG audit and plan to cascade our pilot review of Operational Equipment Purchasing.

While it is still too early to assess the effectiveness of the PREP, we are confident that performance will be improved through on-site reviews and cascaded self-assessment reviews. Sharing select oversight reviews is a low cost and effective way to improve purchasing operations. It will permit discrepancies to be corrected locally, allow us to continuously reinvent our internal business practices, and bring enhanced efficiency and effectiveness in today's challenging and cost constrained business environment.

151. What is the current status of the Service's efforts to establish Mobile Services Antennas on postal property?

The Postal Service is not actively offering its properties to wireless telephone operators for the placement of antennas.

However, an agreement is in place with UniSite, Inc. of Tampa, Florida, to handle interest received from wireless operators on a specific postal property. That property is made available to the operator on the condition that it does not adversely effect postal operations and that a building permit is received for the placement of a rooftop antenna or supporting tower.

152. The Postal Service began a fuel management pilot program in November of 1998. The stated intent of the program is "to provide the highest quality fuel at the best prices in the market for all the gallons they buy; Postal and contractor gallons." Under the pilot program a storage facility operator under contract to the Postal Service buys fuel from a sole supplier and dispenses fuel to postal owned vehicles and transportation contractors. Transportation contractors, as we understand it, would be required to acquire fuel from the designated facilities under the program. They have expressed a number of concerns with regard to the pilot program.

(a) *Please provide a status report on the pilot program. Where is the program being pilot tested? Has the program, at least in the pilot areas, met the goal of providing the highest quality fuel at the best prices in the market? What is the Service's plan to expand the pilot test or implement the program nationwide?*

Through the end of October 1999, the pilot program has pumped over 5.5 million gallons of diesel fuel, saving more than $550,000 for postal contractors and therefore (since fuel cost is a pass-through) for the Postal Service.

The initial test site in Dallas, Texas was expanded to Memphis, Tennessee; Jacksonville, Florida; Chicago, Illinois; and Atlanta, Georgia.

From the data gathered since the pilot program began in the spring of 1998, the quality of fuel has been the highest that we are aware of, even meeting the temperature requirements of contractors fueling in one part of the country but expending the fuel in considerably different temperature environments. The price, when compared to other fueling methods and to other fuel suppliers using our program, has been the best value we have received or seen. This includes comparisons with the alternative fuel-pricing plan offered by the National Star Route Mail Contractor's Association.

The Postal Service's plan for expanding the pilot test is to include the 21 bulk mail centers (BMC) and selected Pickup and Distribution Centers, which are the largest transportation fuel consuming locations.

(b) *Can the Postal Service demonstrate conclusively that the savings in fuel cost, if any, from the pilot program are projectable nationwide? If so, how much would the Postal Service save annually in total fuel cost if the program were implemented nationwide?*

The pilot program has demonstrated conclusively that the savings are available and projectable throughout the entire postal system. The savings vary from location to location due to differences in state and local taxes and competitive fuel marketing pressures.

As the program is expanded to include 75 percent of the postal contractor diesel fuel gallons purchased, fuel savings will increase from $6 million to over $18 million per year. Seventy-five percent is a conservative projection of gallons included in the program since some locations may not have fueling systems available, or routes may extend into or through areas which do not have program fuel. We expect the savings to increase considerably as the program is expanded to include postal vehicle service (PVS) fuel. In those cases, we will use methods such as the alternative fuel-pricing plan offered by the National Star Route Mail Contractors' Association. Although the savings for the National Star Route Mail Contractors' Association plan are less, they have not been included in the program savings at this time, since the pilot test of this fueling method has not yet begun.

(c) *How do you respond to concerns that the program has been tested in too few areas to draw any conclusion?*

Although the pilot program has only been tested in five areas (Dallas, Memphis, Jacksonville, Chicago, and Atlanta), the original savings projections have been shown to be quite accurate. Since taxes, transportation, storage, handling, and marketing margins are ascertainable, we are confident that the next phase of the expansion will have similar results relative to projections. The program has demonstrated that although savings are available at all locations, there is no uniformity in the exact cents per gallon.

(d) *How do you respond to charges that by its reliance on a single supply source at location the program increases the Service's exposure to supply disruptions?*

Several points should be understood when reviewing this concern. The pilot program was a proof-of-concept program. It needed to focus all the fuel requirements on one supplier to attain the optimum volume discounts. We expect the expansion to require more competing suppliers. Also, some oil companies have a stronger market presence in some areas than others.

As the program expands, bids will be solicited from several suppliers, and we plan to nominate primary and back-up suppliers.

Experience in Dallas, Texas, has demonstrated that contracted customers enjoyed protected supply and price after a hurricane impacted the supply from Corpus Christi. Non-contracted fuel users in the Dallas area experienced supply outages and higher prices while postal fuel pilot program participants had no supply disruptions or price impacts.

Since the pricing is a reference price, the fuel price moves with an entire region of the country and is not subject to the price and supply vagaries of local supplier discretion.

(e) *How do you respond to the argument that it is unlikely that a single supplier will be interested in supplying all locations and therefore the advantages in price from volume purchasing will not be as large as projected?*

We agree that it is unlikely that any one supplier will be competitive in all regions of the country. Since postal diesel fuel requirements are so large, we believe that sufficient volume to warrant deep discounts from oil suppliers will be available in all areas.

(f) *Does the Postal Service believe that the increased activity at fueling facilities will increase the exposure of mishaps?*

The amount of fuel being consumed by contractors' vehicles through postal contracts will not change as a result of the fueling program. While there are no data covering mishaps (since the physical act of placing the fuel in the vehicle is done by a professional fueler rather than by a driver), it is logical to expect a safer operation under the program that is presently in operation. Additionally, since professional fuelers are used and drivers do not dismount their units, operators tell us that they have had fewer knee, ankle, hip, and back injuries. Therefore, we believe that exposure to mishaps is reduced under the fueling program.

(g) *Has the Postal Service considered the loss of flexibility for contractors to fuel in the logistically desirable location if forced to travel to one designated location to refuel? Please explain how you will address this concern. How will this requirement impact route time and service schedules? Wouldn't this increase the cost for a given contract? If not, please explain.*

So far in the pilot program, the Postal Service has succeeded in locating refueling stations near served postal facilities. The Postal Service has invited claims from contractors who have experienced negative financial impact from being required to refuel at a postal designated site, but no such claims have been received to date. This is understandable, since most previous fueling locations were further from the contractor's line of travel, slower, and more expensive than the postal designated site. The Postal Service recognizes that exceptions may occur, and therefore, continues to welcome claims from contractors who are negatively impacted.

The requirement for refueling at a designated location has thus far reduced route time. Therefore, service schedules have not been impacted. In the unlikely event that schedules are negatively impacted, contractors are invited to document those impacts and submit them to their contracting officer for adjustment. Since some of the fueling locations in the next phase of the program will likely be on postal Bulk Mail Centers, we do not expect that schedules will be negatively impacted.

Although the cost for a given contract has not yet been increased as a result of any required refueling, the possibility has not been excluded and, as previously mentioned, claims for any impact are invited. It should be noted that although some contractors have experienced reductions in route time and greater efficiencies in their operations, the Postal Service has not requested commensurate reductions in schedules or compensation.

(h) *Given these concerns why doesn't the Postal Service make the program voluntary?*

The facts developed by the pilot program have shown that significant savings are available if our purchasing is unified. Where the program has not been introduced, fuel cost data proves that contractors buying fuel individually is more costly than unified purchasing. The greatest savings in the program have been by the smaller contractors with no volume leverage.

(i) *The National Star Route Mail Contractors' Association has offered an alternative fuel pricing plan. Please provide a summary of this plan and your conclusions as to its potential to meet the goal to lower fuel cost.*

In order to properly respond, the various methods of refueling available to the Postal Service must be understood. Also, it must be understood that each method has a greater or lesser saving potential. Listed below are the various methods and a brief explanation of how they function. They are listed in order of declining savings:

(Best Savings) Fueling at postal facility tanks and pumps.
In this method, existing or new tanks and pumps are used at a postal facility to fuel both postal equipment and contractor equipment. Among the reasons for the savings being the best, are the improved usage of facilities (shared) and location (elimination of stem miles).

(2nd Best Savings) Private facility under postal contractor control.
In this method, a postal contractor with tanks and pumps near to the target postal facility provides program fuel to his own trucks and to other postal contractors. Stem miles are at a minimum, and time delays are held to a minimum by using high-speed pumps and attendants.

(3rd Best Savings) Utilizing a router.
A router is a software package that examines the route to be taken, then searches that route for the most economic fueling solution. The potential solutions include any negotiated discounts available from cardlock or commercial stations (truck stops). Stem miles are somewhat controlled; however, delays in pump lines are not.

(4th Best Savings) Cardlock facilities.
A cardlock facility is one which is unattended (generally) and secured by a fenced area through which access is gained with the use of a card. The card also operates the pumps and records the transaction. Cardlock facilities are somewhat less controlled for stem miles than the previous three methods, and pumps are usually standard speed (20 gallons per minute).

(5th Best Savings) Commercial stations or truck stops.
This method uses existing commercial truck stops and includes any applied discounts negotiated by the Postal Service and its contractors. Stem miles are similar to using routers and cardlock facilities, and delays can be significant due to traffic at the pumps. Pumps are usually standard-speed, although some offer attendants and high-speed pumps. Delays are often experienced.

The National Star Route Mail Contractors' Association plan is to negotiate discounts with a variety of local and nationwide truck stop chains and utilize those chains with their discounts for fueling. The plan's greatest potential is found in the long distance routes where the range of the initial fill-up is exceeded. The Postal Service plans to use this fuel purchasing approach in those instances where options one through four are not available.

153. The Postal Service's regulations regarding the use of Commercial Mail Receiving Agents (CMRAs) have resulted in strong dissatisfaction of CMRA operators and customers. The Postal Service is currently meeting with industry groups representing CMRAs and with groups representing specific classes of CMRA customers, such as victims of domestic violence, in order to revise the rules.

(a) What is the status of efforts to revise the regulations and when will the proposed rules be published?

Since June 23, the following actions have been undertaken:

- The Postal Service has provided CMRAs and their customers an additional 60 days to complete the revised Form 1583, until August 26, 1999.
- The Postal Service has provided CMRA customers an additional six months, until April 26, 2000, to notify correspondents of their new address and to deplete supplies of stationery with their former addresses.
- The Postal Service clarified the types of identification that may be used, including lists of permissible and impermissible types of identification. Among other things, this clarification stated that Social Security cards, credits cards, and birth certificates are not acceptable forms of identification.
- The Postal Service has authorized CMRAs to accept all accountable mail (except registered mail) from their customers for mailing at the post office.
- The Postal Service has announced that it will be permissible for customers to use the "three-line format" when the four-line format cannot be provided.

The above modifications were adopted following meetings with members of the CMRA industry and other interested parties. Since they eased the requirements for operation or use of a CMRA, they were not published in the *Federal Register.* A proposed rule describing procedures and policies for release of information provided on Form 1583 was published August 26 in the *Federal Register* for public comment. The final rule was published in the *Federal Register* on January 25, 2000. The proposed rule regarding the optional use of a number symbol (#) in lieu of the acronym "PMB" to identify a private mailbox in the address will be published for public comment in the *Federal Register* in early 2000.

(b) *Has the Postal Service developed and implemented a process to gauge the opinion of small business and privacy groups regarding these latest changes to the proposed CMRA regulations?*

The Postal Service has had a series of meetings with customers representing a wide variety of interests on these issues. Proposed rule changes have also been published in the *Federal Register* for public comment. We have also received input through other means, such as correspondence, publications, and Congressional hearings. The Postal Service has adopted significant modifications to its policies based on the input it has received.

154. The requirement of the address designation "PMB" has been the particular target of public criticism. We understand that the Postal Service is considering a revision that would allow only two address options for a boxholder, PMB or the "#". One or the other designations must be used and there would be no other option.

(a) *Is this the case? Are the CMRA industry groups in agreement with this revision? If so, when will the regulations be revised?*

The final rule, published on March 25, 1999, and effective April 26, 1999, required the use of the "PMB" designation only in the complete address of a private mailbox holder. The Postal Service agreed to publish a proposed rule in the *Federal Register* for public comment regarding the option to use the "#" symbol in lieu of the "PMB" designation. The use of the # number sign as an option was based on a suggestion by the CMRA industry group, and agreed to by industry representatives. Despite basic agreement in the CMRA industry, there are still different opinions on this issue. The Postal Service must emphasize that this process does not assure that the proposed rule will be adopted.

155. We understand that there will be no "grandfathering" of previous CMRA contracts that allow box customers to use such designations as "suite", "apartment", etc.

(a) *Is this the current proposal and has the CMRA industry and consumer representatives signed off on it?*

The current regulation (published in the *Federal Register* on March 25, 1999 and effective April 26, 1999) does not permit the use of designations such as "suite", "apartment", etc. As explained in the response to Question 154, the Postal Service has agreed to publish a proposed rule authorizing the optional use of the number symbol (#) as an alternative to the acronym "PMB."

In meetings with the CMRA industry, industry representatives have indicated their willingness to accept this alternative addressing format. It should be noted, however, that other industry observers do not favor this proposal and have indicated that they would not favor any change to the original policy. Instead, they prefer that all CMRA customers be required to use the "PMB" designation. Other groups, particularly small business interests, appear to believe that the proposed modification does not go far enough, and have asked for "grandfathering" provision allowing existing CMRA customers to use "suite," "apartment," or other terms. This proposal, however, would appear to perpetuate, and indeed intensify, misperceptions regarding CMRA addresses. The use of a "grandfathered" address can imply to the consumer that the private boxholder maintains a physical presence or an office at the address of a CMRA.

156. We understand that there is a proposal to conduct an intensive joint education program to assist consumers in identifying a CMRA location. The Inspection Service, Retail Operations and CMRA industry representatives would conduct this program. In addition, the Inspection Service and the CMRA industry will work together on indicators that will help CMRA owners identify potential fraudulent operations by a boxholder.

(a) *Is this the current proposal and has the CMRA industry signed off on it?*

Yes, this is the current proposal. Representatives of the Postal Service and the Inspection Service are working with Steve Silver, Attorney for the Coalition Against Unfair USPS Competition, and others on this issue. Together, we have drafted and agreed to guidelines that will assist CMRA operators in working with Postal Inspectors when fraud or other criminal activity is suspected. The proposal focuses on educating consumers on the meaning and use of "PMB" and how to determine if the "#" sign is a CMRA address. It also establishes a toll-free telephone number to assist consumers in obtaining information about CMRAs. We are now working on a training agenda for CMRA operators, which will provide an orientation regarding the noticeable signs of criminal activity and how to contact the appropriate authorities.

(b) *Does the Postal Service believe that such an education program will be effective in protecting consumers from fraud and identity theft schemes-the original intent of the CMRA regulations? Please explain how this program would be planned, coordinated and administered by the Postal Service and the parties.*

The Inspection Service believes that educational awareness campaigns will teach businesses and consumers to protect themselves from fraud. The Inspection Service has recently developed and produced a pamphlet titled "Identity Theft – An Awareness & Victim Guide." This pamphlet is being distributed to financial institutions, retail merchants, credit bureaus, and consumer groups as a means to educate consumers regarding identity theft schemes. The Inspection Service anticipates that this pamphlet will be become an official Postal Service publication later this year and will be available to consumers at post offices. The pamphlet will also be made available to CMRA operators as part of our continued working relationship with the CMRA industry. The Inspection Service, in conjunction with the International Association of Financial Crimes Investigators (IAFCI), has also developed a quick reference guide to assist financial institutions, retail merchants, and credit bureaus in the prevention of credit card fraud.

157. Concern has been raised as to the lack of information for users on the issue of post office and private mail boxes to understand the current situation and the impact of proposed regulations on customers and service providers.

(a) *Does the Postal Service know how many pieces of mail that were addressed to Post Office Boxes but did not include the address designation "P.O. Box" were returned to the sender in the past year?*

The Postal Service has not determined a need to collect or maintain such information; however, practices related to the return of mail addressed to post office boxes would not provide a meaningful comparison to mail addressed to CMRAs, because a "P.O. Box" designation is the primary delivery address, while the "PMB" designation is a secondary unit designation.

(b) *Are pieces sent to Post Office Boxes that use designations such as the word "Box" or a number sign ("#") returned to the sender?*

The use of "Box" in a post office box mailing address is not considered unauthorized. Mail pieces sent to post office boxes with an incomplete address are not returned to the sender if sufficient information is available to determine the exact mailing address. For a Post Office Box, there is no street address; yet, there is a post office name and a unique ZIP Code. This lets the customer know it is a post office box. A CMRA has a street address. Therefore a "suite" would imply an office at that street address.

(c) *How many pieces sent to post office boxes which used unauthorized, but innocuous, address designations such as "Box," "#," "No.," etc. were returned in the past year?*

The Postal Service has not determined a need to collect or maintain such information. It encourages all mailers to use a complete address with the accurate and appropriate elements at all times.

(d) *Please provide a detailed report listing all criminal investigations conducted by the Postal Inspection Service that involved the use of CMRA boxes. What percentage of all CMRA boxes is used in crimes?*

The Postal Inspection Service conducted 1,069 criminal investigations dating back to 1985 that specifically involved the use of CMRA boxes. These investigations involved theft of mail, fraud against consumers, fraud against business, child pornography, and distribution of narcotics. Of these cases, 77 percent were opened between 1995 and 1999. Many of these investigations involved the use of multiple CMRA boxes, so the amount of boxes used for crimes far exceeded the number of investigations.

It would not be possible for the Postal Service to calculate the percentage of all CMRA boxes used in crimes. First, it would be difficult to establish an accurate number of CMRA boxes. Even the industry uses estimates. Second, the Inspection Service does not have the ability to determine the number of similar CMRA-related investigations conducted by other law enforcement agencies, including the Federal Bureau of Investigation, the U.S Secret Service, State Attorneys General, and local District Attorney offices.

158. In a June 24 letter to the Chairman, the Postmaster General said he would clarify the definition of a CMRA to account for such entities as corporate executive suites. The Postal Service attempted to apply CMRA regulations to firms that rent office space, equipment and services. These businesses use the space primarily to transact business, not to receive mail. The Subcommittee thought the resolution of this issue was straightforward. Despite the willingness of the industry to agree to contract inspections and consideration of "course of performance" to determine whether the regulations apply, the Postal Service is still concerned over its ability to enforce such regulations. As a result, the industry representatives have recently suggested language that would clarify which business entities would be subject to the CMRA regulations. The Subcommittee is concerned that this issue is still unresolved.

(a) *When will the Postal Service come to closure on this issue and issue workable regulations agreeable to all the stakeholders?*

The Postal Service has been working with representatives of the corporate executive center (CEC) industry since May to develop guidelines to distinguish which portions of a CEC operation constitute a CMRA. Representatives of the traditional CMRA industry were also included in some of these discussions to ensure that the guidelines accurately describe that portion of a CEC operation that meets the criteria of a CMRA.

The parties agree in principle that a CEC will not be subject to CMRA rules for customers who primarily rent office space from the CEC, but that they will be subject to those requirements for customers who use the CEC for services similar to those provided by a CMRA. The CEC industry developed language spelling out his policy, and on February 2, 2000, the Postal Service published a proposed rule for public comment in the *Federal Register*.

159. The Postal Service is on record as having conducted no analyses to judge the extent of the criminal activity within the CMRA industry, how each of its proposed regulations would deter criminal activity, or the costs of compliance for stakeholders who subscribe to private mail boxes. It has been alleged that the Postal Service issued the proposed CMRA regulations without these analyses even though about 8,100 citizens objected to the rule during two comment periods in 1997. Almost all of the stakeholders' concerns for the regulations were listed in the Supplementary Information preceding the rule.

Although the Postal Service is exempt from the Regulatory Flexibility Act and the Paperwork Reduction Act as an executive agency of the federal government, it has been argued that it should act responsible and consider the cost and benefits of all the regulations. Supposedly when the Postal Service makes its business decisions like changing a resident's ZIP coding, offering new goods and services, putting Bugs Bunny on a stamp, sponsoring an American bicycle team, etc., it conducts analyses to weigh the merits against the detrimental effects.

(a) *How do you respond to those who argue that the cost of CMRA regulations to all the stakeholders should have been analyzed by the Service prior to issuing the CMRA regulations?*

While we did not make a formal study, the Postal Service knew from its experiences with other address changes that the cost of the new regulations would not be excessive. We have also taken numerous steps to minimize costs and respond to concerns raised by CMRA operators and customers.

For example, the original six-month grace period to deplete old stationery and notify correspondents of the new address was extended one year, to April 2000. Based on our experience with ZIP Code and similar address changes, the Postal Service believes one year will permit the vast majority of businesses to deplete old stock and notify correspondents of the change during the course of ordinary business instead of special mailings. The Postal Service is also sensitive to the possibility of potential customers using old addresses from older catalogs or promotions. The Postal Service has explained that receipt of this type of mail with the prior addressing formats will not be returned to the sender if the box holder has taken reasonable actions to notify its correspondents of the new address. The Postal Service has worked with the CMRA industry to develop procedures to implement this policy. When mail is received from potential customers, the box holder can then notify the sender of the new address.

In view of these policies, the Postal Service believes that the cost estimates suggested by some groups are highly exaggerated and that the overwhelming majority of CMRA customers will experience few, if any, additional expenses from the changes.

On a more general level, public policy decisions involving fraud and the cost of prevention are more complex than simple cost/benefit calculations. For example, the Deceptive Mail Prevention and Enforcement Act was passed by Congress and signed into law by the President last year even though it has cost the sweepstakes industry millions of dollars, resulted in negative publicity for these companies, and even lowered the revenues of the Postal Service. In that situation, Congress felt that the need to protect consumers and businesses from deceptive mailings outweighed the costs to sweepstakes companies and other mailers. In the case of the CMRA rule changes, the Postal Service believes that the benefits of preventing fraud and protecting the American people are worth the relatively low costs incurred by the CMRA industry.

(b) *How do you respond to those who argue that this is a good example of why the Postal Service should be subject to the Regulatory Flexibility Act and the Paperwork Reduction Act?*

The Postal Service believes that this is a good example of why the Postal Service should <u>not</u> be subject to the Regulatory Flexibility Act and the Paperwork Reduction Act. Under the existing statutory framework, we were able to work effectively with representatives of the CMRA industry and other interested parties to modify proposed new consumer protection rules. The end result, we believe, has avoided significant disruption or expense to legitimate businesses, but affords an important new measure of protection to the public.

(c) *How do you respond to those who argue that enforce of the August 26 Form 1583 regulations was premature given the fact that they were under reconsideration?*

The Postal Service understands these concerns, but believes that providing additional time to submit the revised PS Form 1583 would have unnecessarily postponed the crime-deterrent benefits of the revised rules.

The principal concern of those who objected to completion of the form related to the possible release of information contained on it. However, the Postal Service had previously advised the public that information on the forms would not be released at this time. Instructions were issued to postal employees on July 1, 1999, that information from Form 1583 must not be released to any member of the public until further notice. The Postal Service also agreed to publish for public comment a proposed permanent rule not to release address information from Form 1583 to consumers on those private mailbox renters doing or soliciting business with the public.

(d) *If the Service was still in the development stage of the series of regulations, didn't it owe those stakeholders the courtesy to not enforce the rule until it finalizes each regulation?*

When the rule of March 25, 1999, was published in the *Federal Register*, it was considered a final rule. Comments received after that rule was published, some of which were entirely new to the Postal Service, caused us to reexamine some of the revised regulations. Not all of the revised CMRA rules, however, are being or have been reconsidered. For example, regulations concerning the need to submit two forms of identification, including one bearing a photograph, were not being reconsidered, and the use of the Form 1583 was needed to implement these new regulations. These regulations, it should be noted, are critical to the deterrence of identity theft and other fraud.

160. Concern has been raised regarding the ease with which law enforcement agencies can gain access to Form 1583 information on file with the Postal Service. The Postal Service would require only that identification from a legitimate law enforcement agency be shown as part of a legitimate investigation in order to have access to the information. On the other hand, the National Coalition Against Domestic Violence wants no privacy information to be released without a warrant.

(a) *Please discuss why the Service's proposal, in contrast to requiring a warrant, is necessary to facilitate effective law enforcement.*

The Postal Service met with the National Coalition Against Domestic Violence regarding this issue. We proposed a compromise that would address the concerns of the Coalition without impeding law enforcement's ability to fulfill its responsibilities to protect the American public.

Our proposal would release box holder information only through a written request by a law enforcement or regulatory agency, written on agency letterhead and signed by an authorized agency official, and only when there is not a court order of protection on file with the Postal Service pertaining to the individual. If an agency requests information regarding the physical address of an individual who is under an order of protection, the Postal Service will not release the information but will refer the requesting agency to the judicial district from where the order of protection was issued. Under this procedure, individuals who are concerned that the release of information to a government agency might compromise their personal safety could, by obtaining a court order, endure that it would be left to a neutral court to determine whether any information could be released.

We believe the final rule published in January 2000 generally addresses the concerns of the National Coalition Against Domestic Violence. We have not heard from the Coalition since the final rule was published.

(b) *How would requiring a warrant, as recommended by the National Coalition Against Domestic Violence, impede the conduct of a legitimate criminal investigation?*

The time needed to obtain the warrant would delay government action, which could be crucial in matters involving security or law enforcement activities. This requirement would also prevent agencies with civil enforcement authority, such as the Federal Trade Commission, from obtaining a warrant. In addition, the procedures for obtaining a warrant entail significant administrative effort, and therefore, expense for government agencies. The same is true for the courts, and the requirement would add further burden to the judicial system.

(c) *How do you respond to concerns that law enforcement officers themselves can be abusers and that they can easily track down their victims through access to CMRA information using their law enforcement identification?*

The Inspection Service recognizes that law enforcement personnel can seek to take advantage of their position to secure information in an effort to locate a spouse, companion, etc. Our proposal will minimize opportunities for abuse by requiring requests to be made in writing, submitted on official agency letterhead, and signed by an authorized agency official. Moreover, even where these standards are met, the Postal Service will not release the requested information if a court order of protection has been submitted. We believe that these procedures provide a reasonable compromise between individual safety concerns and security and other significant governmental interests.

161. The Subcommittee has been told of reports that some postmasters have shut off mail service to CMRAs for non-compliance. It has been suggested that overzealous postmasters who wrongfully abuse the "death penalty" provision in the CMRA regulations which permits shutdown of mail service for failure to have all 1583s in place be disciplined in some manner.

(a) *How many cases have there been when mail service was shut off for noncompliance?*

To date, Postal Service Headquarters is aware of only one incident that resulted in suspension of delivery for noncompliance. In all other cases of noncompliance, the CMRA corrected the violation. A procedure has been developed that enables industry representatives to report questionable actions to Postal Service officials, who review the actions and take any necessary corrective measures. To date, all complaints have been resolved to the satisfaction of industry representatives.

(b) *Of these cases has the Postal Service determined whether service was shut off improperly?*

No service has been terminated improperly. The Postal Service used the proper procedures in suspending delivery in the one case mentioned in the response to Question 161(a). The office responsible for delivery to the CMRA took extraordinary steps to avoid suspending delivery. The CMRA in question failed to comply with the regulation that requires the submission of completed revised Forms 1583 for all current and new customers. After repeated failure to respond to Postal Service requests to come into compliance, delivery service was suspended.

(c) *In such cases were the postmasters disciplined in any manner?*

Relevant regulations and procedures were discussed with local postal officials to ensure that the policies were clearly understood and correctly applied. There have not been any further complaints at these offices. We believe that proper training, rather than discipline, is the most appropriate response in these situations.

(d) *Will the revised regulations and all supporting information be combined in one section in the DMM?*

The revised regulations are published in one section in the Domestic Mail Manual, §§ D042.2.5 through D042.2.7. Any additional changes will be incorporated into this section.

(e) *What other forms of communication will the Postal Service use to inform CMRA owners and customers of the new regulations?*

In addition to the *Domestic Mail Manual*, notices or articles relating to the new rules were published in the *Federal Register* and postal publications such as the *Postal Bulletin*, the *Mailer's Companion*, and *Memo to Mailers*. Information was also posted on the Postal Service's external web site. We are also working closely with the industry representatives. They have agreed to educate their franchisees.

162. Earlier this year, you provided a report on the proposed relocation of the Brewery Street Post Office in New Haven, Connecticut. Please provide an update on the following matters:

(a) *What are the current terms of negotiations with the developers?*

The terms of negotiation presently deal with issues of construction phasing, facility designs, reduction clauses, pricing, terms of the contract, legal, etc.

(b) *What is the status of Postal Service approval; specifically, has the project been approved by the Northeast Area Capital Investment Committees, the Northeast Area Vice President, and the Postal Service's headquarters Capital Investment Committee? If so, please provide the dates of approval and the basis upon which these decisions were made. Have you concurred in these decisions?*

The Brewery Street Project was approved by the Northeast Area Capital Investment Committee in September 1999, the Northeast Area Vice President in October 1999, and the Postal Service Headquarters' Capital Investment Committee in December 1999. The project was presented to the Postmaster General after approval by the Capital Investment Committee.

The approvals to date are based upon the cost/benefit data provided the decision makers, as well as the fact the Postal Service will be replacing older assets with new facilities built to our specifications and requirements. The City's desire for the Postal Service to relocate to the new site has also factored into our decision-making.

(c) *Given the current state of negotiations and project approval, when will the specific appraisals and breakdown of construction costs be released in conformance with the Freedom of Information Act?*

Any pre-decision information must be withheld until final approval of the project and the execution of the contract. Information conforming to the FOIA can be released if the project is approved by the Postal Board of Governors.

163. Earlier this year the General Accounting Office reported to the Subcommittee that it found that at nearly half of the Postal Service facilities visited in evaluating deceptive mail issues, postal employees did not properly refer consumers' deceptive mail complaints to the Postal Inspection Service. While the Inspection Service noted that postal facility managers were instructed to alert their employees on how consumers may report deceptive mail complaints, the GAO suggested that handouts or training on these instructions could be provided to postal employees who routinely deal with the public to help ensure that consumers' deceptive mail complaints are appropriately handled.

(a) *What handouts and training is provided to postal employees who routinely deal with the public to help ensure that consumers' deceptive mail complaints are properly referred to the Postal Inspection Service? Please provide copies of the handouts, if any, as well as the number of postal employees, if any, who have been trained on this matter.*

In the *Postal Bulletin* of May 20, 1999, the Inspection Service reported the revision of PS Form 8165, Mail Fraud Report. The article, listed on the front page of the *Postal Bulletin*, described the importance of the form and how it assists the Inspection Service in identifying new fraud schemes and enforcing civil and administrative remedies. The article described the possible mail fraud schemes that customers might report to employees and explained how to help customers complete the form. Finally, the article outlined the process for obtaining a supply of the new forms. The *Postal Bulletin* is distributed to all postal facilities, and all postal employees are expected to be familiar with information contained in the publication. A copy of the *Postal Bulletin* article, including PS Form 8165, is attached (Attachment 14).

(b) *If no handouts or training have been provided, when will the Postal Service undertake some relevant actions to address the GAO suggestion? If not, why?*

Information has been provided, as discussed in the response to Question 163(b).

164. As noted, GAO found that postal employees inappropriately referred consumer deceptive mail complaints to organizations other than the Postal Inspection Service, such as local postal consumer affairs offices or the Direct Marketing Association. GAO concluded that such inappropriate referrals may occur because within the Postal Service, local consumer affairs offices are primarily responsible for handling most consumer complaints. GAO suggested that perhaps a coordinated effort between the Postal Service's Office of Consumer Advocate, which manages the operations of local consumer affairs offices, and the Postal Inspection Service, could help ensure that the appropriate referrals of deceptive mail complaints are made.

(a) *In addition to giving employees handouts or training on how to handle deceptive mail complaints, how do you respond to the suggestion of a coordinated effort between the Consumer Advocate and the Inspection Service? How will this suggestion be implemented, and if not, why?*

The Inspection Service and the Office of the Consumer Advocate have fostered an effective partnership in addressing the referral of deceptive mail complaints. In 1997 and 1999, the Inspection Service made presentations on how to process customer mail fraud complaints at the Consumer Affairs Managers' (CAM) annual training conferences. The Inspection Service enlisted the assistance of the CAMs in correctly directing mail fraud issues coming to their offices and asked for their input on our revised Mail Fraud Report form. The Inspection Service is currently preparing to assist the Consumer Advocate's office in developing a Standard Operating Procedure to address mail fraud complaints, which will be included in its reference guide. The Inspection Service and the Office of the Consumer Advocate are also developing a plan to determine the viability of having customer complaints taken over the telephone. The Mail Fraud Report is also available to the public on the Inspection Service's web site.

The Inspection Service and the Office of the Consumer Advocate also work together every year to promote National Consumer Protection Week. Together, these offices plan and coordinate events throughout the country to educate consumers on current fraudulent promotions and schemes. This year we will be focusing on identity thefts, fraudulent telemarketing solicitations, fraudulent mail solicitations, and electronic commerce security. The Office of the Consumer Advocate also worked with the Inspection Service on the KNOW FRAUD project. They provided the Inspection Service with assistance in coordinating over 100 press conferences throughout the country.

165. GAO also reported that Postal Inspection Service officials mentioned that work was underway to ensure that the Fraud Complaint System (FCS) was Year 2000 compliant and that improvements were being made to help ensure that FCS could be more useful to the Postal Inspection Service. Indeed, the Postal Inspection Service testified that a project was underway to develop a new system that will provide more information fields, better search capabilities, and automatic lookups in other Inspection Service databases. The Inspection Service noted that this will include the ability to track the number of complaints by scheme type and category, as well as identify instances where senior citizens are being targeted and by what types of schemes.

(a) *What is the status of these improvements to FCS? When will the new system be fully operational with all of the features described by the Inspection Service? How is the Postal Service assured that FCS is Year 2000 compliant?*

The Inspection Service has worked aggressively to make improvements to the Fraud Complaint System (FCS), so that it provides more information and in-depth search capabilities. The new system is now fully operational, and has been expanded to the Postal Service's internal web site. The FCS was developed on a Y2K compliant hardware/software platform. The system testing included certifying the application is Y2K compliant.

With regards to senior citizen complaints, the system can only track these complaints if the individual voluntarily provides their date of birth when making the complaint.

Attachment 1

Customer Satisfaction Measurement - Residential
(CSM-R)
Overall Performance Results - Residential Households
(Percent Ratings)
PQ IV, FY 99

Performance Cluster	EX/VG/GD
ALBANY	98
SPRINGFIELD	97
MIDDLESEX-CENTRAL	97
PROVIDENCE	97
WESTERN NEW YORK	97
DAKOTAS	97
NEW HAMPSHIRE	96
MAINE	96
HARRISBURG	96
ERIE	96
GREATER MICHIGAN	96
HAWKEYE	96
PITTSBURGH	96
SUNCOAST	95
LONG ISLAND	95
SOUTH JERSEY	95
NORTHLAND	95
CENTRAL PLAINS	95
MILWAUKEE	95
HONOLULU	95
SOUTH GEORGIA	95
AKRON	95
NORTHERN VIRGINIA	95
SALT LAKE CITY	95
KENTUCKIANA	94
APPALACHIAN	94
CONNECTICUT	94
BIG SKY	94
SPOKANE	94
COLUMBUS	94
CENTRAL FLORIDA	94
PHILADELPHIA	94
MID-AMERICA	94
ARKANSAS	94
NORTHERN ILLINOIS	94
GREATER SOUTH CAROLINA	94
CINCINNATI	94
GREATER INDIANA	94
PORTLAND	94
LANCASTER	94
LOUISIANA	93
BALTIMORE	93
BOSTON	93
MID-CAROLINAS	93
RIO GRANDE	93

Customer Satisfaction Measurement - Residential
(CSM-R)
Overall Performance Results - Residential Households
(Percent Ratings)
PQ IV, FY 99

Performance Cluster	EX/VG/GD
ALABAMA	93
TENNESSEE	93
CLEVELAND	93
CENTRAL NEW JERSEY	93
WESTCHESTER	93
ALBUQUERQUE	93
GREENSBORO	93
GATEWAY	93
ARIZONA	93
SACRAMENTO	93
RICHMOND	93
CAPITAL	93
FORT WORTH	92
NORTH FLORIDA	92
ROYAL OAK	92
CENTRAL ILLINOIS	92
MISSISSIPPI	92
OKLAHOMA	92
NORTHERN NEW JERSEY	92
ALASKA	92
SEATTLE	92
COLORADO/WYOMING	92
SANTA ANA	92
VAN NUYS	91
SAN DIEGO	91
SOUTH FLORIDA	91
HOUSTON	91
CARIBBEAN	90
LAS VEGAS	90
ATLANTA	90
SAN JOSE	90
DETROIT	89
DALLAS	89
LONG BEACH	88
OAKLAND	87
LOS ANGELES	84
SAN FRANCISCO	83
TRIBORO	83
NEW YORK	83
CHICAGO	75

Attachment 2

UNITED STATES POSTAL SERVICE — POSTAL NEWS

November 4, 1999

FOR IMMEDIATE RELEASE
Contact: Irene A. Lericos
410-715-0070
Release #12
ilericos@email.usps.com

POSTAL SERVICE TO STUDY GROWTH IN GRAND STRAND AND PEE DEE AREAS

In response to a congressional inquiry made by U.S. Representative Mark Sanford during the Subcommittee on the Postal Service oversight hearing, Postmaster General Bill Henderson agreed to reevaluate post office expansion in the Grand Strand and Pee Dee areas.

Plant annexes are typically created to meet short-term mail processing requirements. The Postal Service has decided to address the increase in mail volume growth in the Myrtle Beach and Pee Dee areas with a long-term solution. Therefore, the proposal to construct a Myrtle Beach annex of the Florence Mail Processing facility at the former Air Force Base is being reassessed.

The Postal Service has already begun to study growth and trends in the area. This review will assure that postal services in these areas will be adequately met in the future. During the six- to eight-month process, local postal officials will continue to keep the community informed.

###

USPS EAGLE SYMBOL AND LOGOTYPE ARE TRADEMARKS OF THE UNITED STATES POSTAL SERVICE. ALL RIGHTS RESERVED.

Attachment 3

DIVERSITY IMPROVEMENT OPPORTUNITIES
COMPLETED AND NEW INITIATIVES

COMPLETED INITIATIVES	EXPECTED RESULTS	ACTION TAKEN/ACCOMPLISHMENTS	ONGOING/NEW INITIATIVE
1. Develop Corporate Policy Statement	To clearly define diversity and communicate how diversity can support the goals of the USPS.	The Statement was developed in coordination with all the functional Vice Presidents and the Diversity Oversight Committee. Issued in July 1998.	
2. Revise Diversity Development Strategic Plan	To integrate the Voice of the Employee (VOE) elements of Diversity Strategic Plan within Human Resources component of USPS Strategic Plan.	The revised Plan has been distributed to all Officers, executives and managers. In addition, a tri-fold brochure was developed and distributed to all EAS employees, supervisors, managers and postmasters.	
3. Establish Diversity Oversight Group	Two-fold purpose: (1) to establish an Oversight group appointed by the Deputy Postmaster General (DPMG) to oversee implementation of the initiatives; and, (2) to establish an Advisory Council made up of field and headquarters executives.	The Deputy Postmaster General established the Diversity Oversight Committee and appointed Mr. Clarence E. Lewis, COO and Mr. M. Richard Porras, CFO to co-chair the committee.	3a. Diversity Oversight Committee will continue to oversee/direct the activities o the ongoing/new initiatives. The commit will continue to be co-chaired by the Chie Operating Officer and the Chief Financia Officer.
4. Evaluate Diversity Development Structure	To establish a liaison between Headquarters and field Diversity Development (DD) structure and strengthen the overall effectiveness of diversity.	Ten Senior Diversity Development Coordinators positions were created and filled. 30 additional Diversity Development Specialists positions were created. All of the performance clusters will have a Diversity Development Specialist on staff. Diversity at Headquarters was realigned to support a more inclusive environment and to establish a liaison between headquarters and field diversity development structure.	

DIVERSITY IMPROVEMENT OPPORTUNITIES
COMPLETED AND NEW INITIATIVES

COMPLETED INITIATIVES	EXPECTED RESULTS	ACTION TAKEN/ACCOMPLISHMENTS	ONGOING/NEW INITIATIVES
5. Mainstream management of diversity under ***CustomerPerfect!***	To integrate diversity in the Voice of the Employee analysis in the ***CustomerPerfect!*** improvement process.	Several Diversity efforts have been identified as part of the ***CustomerPerfect! (CPI)*** improvement process under the Human Resources component. The following efforts have been completed: ➢ developed and implemented a process to track developmental assignments of all employees; ➢ developed a measurement process to evaluate the success of the Affirmative Employment Plan; and, ➢ developed a communication strategy and action plan, which addresses appropriate behavior, to ensure an environment free of sexual harassment and discrimination.	5a. Create a quarterly diversity overview report/update with Workplace Environme Indicators (WEI). 5b. Develop 1-hour of mandatory sexual harassment training for craft and 2 hours EAS employees. Also, Diversity Development will provide menu or list of available sexual harassme courses for managers to consider as part VOE training.
6. Establish Account-Ability for Diversity in PCES Merit Evaluation	To include a compensable diversity measure in variable pay.	The Management Committee and PMG decided that the merit evaluation and ***CPI*** Review process would be the means to ensure compliance. As a result, accountability procedures were established by adding diversity-related activities to the PCES merit performance evaluation process. A memorandum announcing the FY '99 merit evaluation program was issued to the Officers and PCES executives.	6a. Develop a process to review/evaluat the results of diversity as part of the meri evaluation process.
7. Promote USPS as an equal opportunity employer	To build corporate messaging around the theme that the Postal Service "An Equal Opportunity Employer" and a good place to work.	Diversity Development completed the advertise-ment plan and submitted it to the Marketing department for implementation. Marketing has incorporated the message "An Equal Opportunity Employer" on two advertisements this FY. In addition, 4 full-page advertisements will be included in several prominent magazines this	

DIVERSITY IMPROVEMENT OPPORTUNITIES
COMPLETED AND NEW INITIATIVES

COMPLETED INITIATIVES	EXPECTED RESULTS	ACTION TAKEN/ACCOMPLISHMENTS	ONGOING/NEW INITIATIVES
8. Develop job Applicant database	To develop a job applicant database to track underrepresented groups.	A job application card to track underrepresented groups has been deployed. Currently developing an implementation plan that will focus on large volume testing sites using centralized applicant data entry. Implementation started in February 1999, with rollout to all other sites to be completed by September 1999.	8a. Complete the implementation of the j applicant database and establish a syste to track applicants at various phases of tl recruitment process.
9. Develop a comprehensive recruitment process, focused on underrepresented groups	To enhance the recruitment process by the use of process management.	By the use of process management we have revised the recruitment process. In addition, a recruitment brochure was developed to attract applicants from diverse backgrounds. Additional recruitment tools to be developed based on process management and Quality Improvement (QI) activities.	9a. Develop a process to continuously evaluate the effectiveness of recruitment performance cluster.
10. Improve support for employees during probation	To improve the retention of minorities and women in the Postal Service.	The Postal Service's Retention Guide was revised, published and distributed service-wide. The Guide was issued in December 1998.	10a. Determine why employees leave th Postal Service.
11. Expand Corporate Succession Planning to promote entrance of underrepresented groups	It was determined that "succession planning," by definition would not be appropriate, but a similar process designed specifically to deal with the development of EAS employees would be. The new process was named Career Development Tracks (CDT). The intent of this process is to develop promising employees to become viable applicants for higher-level manager jobs.	Career Development Tracks (CDT) was designed to help employees acquire those attributes for higher-level management jobs. This initial design and pilot of this process has been completed. System-wide implementation will begin later this year and it is estimated that approximately 20,000 participants will go through this process.	11a. Complete the implementation of CI and monitor for diversity.

DIVERSITY IMPROVEMENT OPPORTUNITIES
COMPLETED AND NEW INITIATIVES

COMPLETED INIATIAVES:	EXPECTED RESULTS	ACTION TAKEN/ACCOMPLISHMENTS	ONGOING/NEW INITIATIVES
12. Establish Associate Manager Program	To design a developmental program for employees that will serve to fill the gap between the Associate Supervisor Program and the Advanced Leadership Program.	A new program, the Career Management Program (CMP), has been designed to provide skill based and developmental training opportunities for Postal supervisors, managers and postmasters at all EAS levels. Approximately, 375 participants are in pilot programs in the Great Lakes, Mid-Atlantic, and Southeast areas. Another 300 more employees will be going through CMP by the end of this fiscal year in coordination with Diversity Development. All CMP courses will be made available to all areas this summer.	12a. Complete the Implementation of Career Management Programs (CMP) and monitor for diversity.
13. Create greater diversity focus in selection process for promotions	To ensure a greater diversity focus in the selection process for promotions.	The "review committee/board" process has been reinstated. Data was gathered on the current use of review committee's and a policy making review committee's mandatory that was issued in November 1998. In addition, a memorandum discussing review committee training was sent to all District Managers in May 1999. This will reinforce the requirement that all members of review boards must have taken the EAS Selection Methods Training. HR managers have been advised that they must cover diversity considerations to be used throughout the selection process.	13a. Ensure/monitor that Promotion Revi Committees have been trained.

DIVERSITY IMPROVEMENT OPPORTUNITIES
COMPLETED AND NEW INITIATIVES

COMPLETED INIATIAVES:	EXPECTED RESULTS	ACTION TAKEN/ACCOMPLISHMENTS	ONGOING/NEW INITIATIVES
14. Develop diversity messaging to be integrated into the training curricula	To integrate diversity messaging into the training curricula in order to create a greater awareness of diversity in all facets of the Postal Service.	A video was completed as part of a coordinated effort to integrate diversity into the training curricula. Also, more than a dozen PowerPoint slides have been completed for viewing in Postal Vision. In addition, all training courses are being reviewed to ensure that diversity is integrated into all facets of the training curriculum. A diversity statement was prepared and is now included in all hard copy training materials used in the field, to be read prior to each session.	
15. Develop communications plan to promote diversity message	To integrate diversity in all facets of our communications and increase awareness of diversity in the Postal Service.	A comprehensive communications plan has been completed and is being implemented. It was also determined that each department needs to take responsibility for messaging related to its own initiatives.	
16. Expand Supplier Diversity program communication.	To increase levels of and instruments used for Supplier Diversity communicating to suppliers, prospective suppliers, and USPS buyers.	The initial 1998 targets have been completed though the effort will continue in line with our commitment to continuous improvement. For example, we have: issued Supplier Diversity - Statement of Commitment; dramatically increased information available to Suppliers on WEB; and, provided buyers with information on Supplier Diversity on the Internet.	
17. Expand Purchasing and Materials' (P&M) Diversity Plan	To expand Purchasing and Materials' Supplier Diversity Plan to the Postal Service at large and all USPS Buying Activities.	The Supplier Diversity Plan covering the years 1999-2003 was published in February 1999. The Plan, which applies to all-buying organizations and activities, embodies aggressive, year-to-year "continuous improvement" targets for the 5-year planning period.	

DIVERSITY IMPROVEMENT OPPORTUNITIES
COMPLETED AND NEW INITIATIVES

COMPLETED INITIATIVES	EXPECTED RESULTS	ACTION TAKEN/ACCOMPLISHMENTS	ONGOING/NEW INITIATIVES
18. Link local buying to commitment to SDP	To expand P&M commitment to supplier diversity beyond our formal purchasing activities to requirements activities, requisitions, and local buyers, particularly our credit card buyers.	Guidelines have been issued to local buyers and credit card holders to promote consideration of small, minority, and woman-owned businesses. Quarterly reports on credit card transactions with small, minority, and woman-owned businesses are being distributed and monitored.	
19. Improve subcontracting participation by minority and women-owned businesses	To strengthen efforts to promote subcontracting with small, minority, and woman-owned firms with our large contractors—and to track results.	We revised and issued new purchasing policy covering subcontracting planning and reporting requirements on February 25, 1999. We have developed and issued updated instructions and formats for reporting subcontracting efforts to Contracting Officers. We are also working a remedial program to secure voluntary compliance with these new requirements. Also, "benchmarking" public and private organizations to identify best practices. Finally, we have heightened our focus on promoting participation by diverse suppliers as subcontractors or second tier participants. We are now collecting and reporting 2d tier results.	
20. Make it easy for Suppliers to do business with us	To simplify policy, employee and supplier communications, and media approaches in order to create positive perceptions and build stronger supplier customer relations.	We have developed a variety of tools to obtain supplier input on ways to make it easier to do business with the Postal Service. They include an annual supplier survey; mechanisms to provide suppliers with direct electronic access to our supplier diversity coordinators from our "Locator" page on the Internet; a Supplier Quality Council; several supplier/postal teams to focus on cost, quality and cycle time improvement, and occasional ad hoc focus groups.	

DIVERSITY IMPROVEMENT OPPORTUNITIES
COMPLETED AND NEW INITIATIVES

COMPLETED INITIATIVES	EXPECTED RESULTS	ACTION TAKEN/ACCOMPLISHMENTS	ONGOING/NEW INITIATIVES
21. Provide supplier diversity training to all P&M and other buyers	To develop a training program to cover all contracting activities and all buyers outside P&M.	In 1999, we established training requirements for all buyers. By and large, the major buying functions, and most local buyers completed their training requirements. Additionally, generic guidance for credit card buyers is now in the AS-709, *Credit Card Policies and Procedures for Local Buying*, which went into effect on 11/30/98. Training modules for local buyers are also available on our Intranet pages. Supplier Diversity coverage also has been added to the courses in the functional curriculum. We are currently assessing the need to add coverage to other core USPS training offerings.	
22. Use supplier diversity data to measure the success of the Supplier Diversity Program	To be able to extract or share data from the three separate legacy systems used for Facilities, Transportation, and Purchasing and Materials.	Year-end statistical results were compiled and published for FY 1998. They cover buys made by Purchasing, Facilities and Transportation. Results improved in all areas over those of 1997. The number and dollar value of direct awards and the percentage of awards and dollars against total awards and dollars increased for each category, small, minority and woman-owned firms. We currently compiling data for FY '99. The long-term approach is to integrate the several major legacy systems now in use in some fashion to allow transfer and sharing of data. This approach has been deferred until the resolution of Y2k.	22a. Improve and expand the Supplier Diversity quarterly reports to monitor performance against the plan.

DIVERSITY IMPROVEMENT OPPORTUNITIES
COMPLETED AND NEW INITIATIVES

COMPLETED INITIATIVES	EXPECTED RESULTS	ACTION TAKEN/ACCCOMPLISHMENTS	ONGOING/NEW INITIATIVES
23. Establish Accountability for complying with SDP	To establish accountability for supplier diversity efforts and results.	For 1998, we have moved from objectives to process and result indicators so that we can assess effort as well as results. Indicators are being tracked by both individual and buyer organization.	
24. New Initiative	To establish accountability for supplier diversity efforts and results.	As our initial effort under this new initiative, we have launched a cross-functional pilot effort focused in Southern California. We are attempting to integrate all buying functions. The team is composed of the ASOs from the five Southern CA districts, the FSO, DNO, and PMSC, and Senior Area Diversity Program Coordinators. The goal is to explore new approaches, replicate those that are successful, integrate focus, and develop mutual support cultures. The team is functioning and working on identifying best practices and expanding to other areas.	24. Identify best practices and expand to other areas.

Attachment 4

KEY: Less than CLF
Less than PWF
Less than CLF & PWF

DIVERSITY DEVELOPMENT VOICE OF THE EMPLOYEE (VOE)
QUARTERLY PERFORMANCE REVIEW
SUBGOAL: Enhance Workplace Environment

Qtr-IV, FY-99

	Unit: Field Unit		All Employees M	All Employees F	White M	White F	Black M	Black F	Hispanic M	Hispanic F	[1]AAPI M	[1]AAPI F	[2]AIAN M	[2]AIAN F	TOTAL All
	CLF	%	52.31	47.69	37.34	31.89	10.74	12.14	2.14	1.73	1.92	1.76	0.14	0.13	
Qtr-IV, FY'98 data to Qtr-IV, FY '99 data	Total Area Workforce	#	18,046	11,671	7,986	3,838	8,243	6,504	338	156	1,434	1,142	45	31	29,7
		%	60.7	39.3	26.9	12.9	27.7	21.9	1.1	0.5	4.8	3.8	0.2	0.1	
	Accessions	#	179	105	45	17	71	44	3	3	58	41	1	0	2
		%	63.0	37.0	15.8	6.0	25.0	15.5	1.1	1.1	20.4	14.4	0.4	0.0	
	Promotions EAS levels 15-18	#	20	31	6	16	9	15	3	0	2	0	0	0	
		%	39.2	60.8	11.8	31.4	17.6	29.4	5.9	0.0	3.9	0.0	0.0	0.0	
	Promotions EAS levels 19 and above	#	189	116	62	37	96	66	6	4	25	9	0	0	3
		%	62.0	38.0	20.3	12.1	31.5	21.6	2.0	1.3	8.2	3.0	0.0	0.0	
Qtr-IV, FY '99 data	Workforce EAS levels 1-15	#	16803	10988	7326	3616	7724	6073	311	143	1401	1125	41	31	277
		%	60.5	39.5	26.4	13.0	27.8	21.8	1.1	0.5	5.0	4.0	0.1	0.1	
	A.S.P. Graduates	#	49	40	20	15	24	24	1	0	4	0	0	1	
		%	55.1	44.9	22.5	16.9	27.0	27.0	1.1	0.0	4.5	0.0	0.0	1.1	
	Workforce EAS levels 15-22	#	1303	827	698	311	535	483	26	13	39	18	5	2	21
		%	61.2	38.8	32.8	14.6	25.1	22.7	1.2	0.6	1.8	0.8	0.2	0.1	
	C.M.P. Participants	#													
		%	#DIV/0!	#DIV/0!	#DIV/0!	#DIV/0!	#DIV/0!	#DIV/0!	#DIV/0!	#DIV/0!	#DIV/0!	#DIV/0!	#DIV/0!	#DIV/0!	
	Workforce EAS levels 22 and above	#	138	49	73	12	58	34	6	2	1	1	0	0	1
		%	73.8	26.2	39.0	6.4	31.0	18.2	3.2	1.1	0.5	0.5	0.0	0.0	
	A.L.P. Participants	#	1	0	0	0	1	0	0	0	0	0	0	0	
		%	100.0	0.0	0.0	0.0	100.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
	A.L.P. YTD Participants	#	10	4	6	1	4	3	0	0	0	0	0	0	
		%	71.4	28.6	42.9	7.1	28.6	21.4	0.0	0.0	0.0	0.0	0.0	0.0	

Footnotes: [1]AAPI: Asian American / Pacific Islander; [2]AIAN: American Indian / Alaskan Native

ASP, CMP and ALP are compared to postal workforce only

Total males and females includes uncoded employees.

Sexual Harassment			
	Area	82.0%	1.0%
	Cluster 1	82.0%	0.0%
	Cluster 2	84.0%	2.0%
	Cluster 3	81.0%	1.0%
	Cluster 4	87.0%	2.0%

Analysis:

Data indicates **white males** are below CLFand are below both CLF and PWF in accessions and promotions. They are below PWF in ASP participation. **White females** are below CLF in the unit and in promotions 15-18. They are below both CLF and PWF in accessions and promotions 19 and above. They are also below PWF in ASP participation. **Black males** are above CLF but below PWF in accessions, promotions 15-18, ASP, and ALP participation. **Black females** are also above CLF but are below PWF in accessions, promotions 19 and up. **Hispanic males** are below CLF in all areas ex in promotions 15-18 and ASP participation. **Hispanic females** are below CLF in all categories with no promotions 15-18 and no ASP and ALP participation. **Asian males and females** are above CLF but data indicates negative trends in promotions and ASP and ALP participation. **Native American males** are above the CLF but demonstrate a negative trend in promotions and ASP participation. **Native American females** are below CLF by 23% and have had no accessions and promotions.

KEY: Less than CLF
Less than PWF

DIVERSITY DEVELOPMENT VOICE OF THE EMPLOYEE (VOE)
QUARTERLY PERFORMANCE REVIEW
SUBGOAL: Enhance Workplace Environment

Qtr-IV, FY-99

Unit: Headquarters Unit		All Employees		White		Black		Hispanic		[1]AAPI		[2]AIAN		TOTAL
		M	F	M	F	M	F	M	F	M	F	M	F	All
CLF	%	54.25	45.75	42.64	35.30	4.95	5.45	4.77	3.35	1.61	1.32	0.35	0.30	
Qtr-IV, FY99 data														
Total Unit Workforce	#	829	463	603	275	109	105	18	18	95	63	4	1	1,292
	%	64.2	35.8	46.7	21.3	8.4	8.1	1.4	1.4	7.4	4.9	0.3	0.1	
SPLY Total Unit Workforce	#	839	447	614	266	109	100	16	17	95	63	5	1	1,266
	%	65.2	34.8	47.7	20.7	8.5	7.8	1.2	1.3	7.4	4.9	0.4	0.1	
Workforce EAS levels 1-14	#	78	76	45	39	17	21	4	5	12	10	0	1	154
	%	50.6	49.4	29.2	25.3	11.0	13.6	2.6	3.2	7.8	6.5	0.0	0.6	
Workforce EAS levels 15-18	#	134	116	84	66	20	32	6	4	24	14	0	0	250
	%	53.6	46.4	33.6	26.3	8.0	12.7	2.4	1.6	9.6	5.6	0.0	0.0	
Workforce EAS levels 19 and above	#	594	263	453	165	71	51	8	8	58	39	4	0	857
	%	69.3	30.7	52.9	19.3	8.3	6.0	0.9	0.9	6.8	4.6	0.5	0.0	
Workforce PCES	#	23	7	21	5	1	1	0	1	1	0	0	0	30
	%	76.7	23.3	70.0	16.7	3.3	3.3	0.0	3.3	3.3	0.0	0.0	0.0	
FY99 YTD Data						**Diversity Activities**								
Promotions YTD EAS levels 15-18	#	3	9	2	5	0	4	0	0	1	0	0	0	12
	%	25.0	75.0	16.7	41.7	0.0	33.3	0.0	0.0	8.3	0.0	0.0	0.0	
Promotions YTD EAS levels 19 and above	#	56	50	39	37	11	8	0	1	6	4	0	0	106
	%	52.8	47.2	36.8	34.9	10.4	7.5	0.0	0.9	5.7	3.8	0.0	0.0	
Promotions YTD PCES	#	2	2	2	2	0	0	0	0	0	0	0	0	4
	%	50.0	50.0	50.0	50.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Workforce EAS levels 22 and above	#	443	157	346	97	50	27	5	4	38	29	4	0	600
	%	73.8	26.2	57.7	16.2	8.3	4.5	0.8	0.7	6.3	4.8	0.7	0.0	
A.L.P. Participants	#													0
	%	#DIV/0!	#DIV/0!	#DIV/0!	#DIV/0!	#DIV/0!	#DIV/0!	#DIV/0!	#DIV/0!	#DIV/0!	#DIV/0!	#DIV/0!	#DIV/0!	
A.L.P. T.T.D. Participants	#	1	0	0	0	1	0	0	0	0	0	0	0	1
	%	100.0	0.0	0.0	0.0	100.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	

Footnotes: [1]AAPI: Asian American / Pacific Islander; [2]AIAN: American Indian / Alaskan Native

ALP is compared to postal workforce only

Workforce Profile: Data indicates **white males** are above CLF in all areas except levels1-18. They account for 70% of all PCES. **White females** are under CLF in all categories. **Black males and females** are above CLF in all areas except in PCES positions. **Hispanic males and females** are under CLF in all categories. **Asian males and females** are above CLF in all categories except for females in PCES positions. **Native Americans** are under CLF in all areas except **females** in positions 1-14 and males in19 and above.

Diversity Activity: Data reflects **white males** had negative promotion trends except in PCES promotions, while **white females** had positive trends at all levels. **Black males** only had a positive promotion rate in levels 19 and above. **Black females** had a positive trend in both levels 15-18 and 19 and above. **Hispanics and Native Americans** had negative promotions trends at all levels. **Asian males** had positive trends in level 15 and above but not in PCES promotions and **females** had a positive rate in 19 and above. Only 1 **black male** had ALP activity.

the Postal Service's improvement strategy progresses from a traditional find and fix approach to a preventative systems approach, we hope to achieve world class breakthrough productivity.

5 Diversity

a. General

As one of the country's largest employers, the Postal Service needs to create an environment that capitalizes on the diversity of its workforce. There is also a need to develop a sense of inclusiveness and common purpose. In response to these needs, the Board of Governors commissioned a study conducted by Aguirre International to evaluate and assess the effectiveness of the Postal Service's diversity development program. As a result of this study, the Deputy Postmaster General (DPMG) established a Diversity Oversight Committee co-chaired by the Chief Operating Officer and the Chief Financial Officer to oversee the implementation of diversity improvement opportunities. The group established 23 diversity improvement initiatives to address the issues and developing concerns outlined by the Aguirre study.

In fiscal year 1999, the Postal Service completed the 23 diversity improvement initiatives. The Diversity Oversight Committee continues to review the progress of these initiatives as well as the new initiatives added for the Year 2000 and beyond to ensure that continued emphasis is placed on diversity. Based on the findings and recommendations of the Aguirre study, a corporate policy statement on diversity was developed and then issued to reinforce our commitment to diversity and specifically define diversity as it pertains to the Postal Service. Also in line with those findings and recommendations, a five-year Diversity Business Plan was prepared that included: recruitment strategies to increase the hiring of women and minorities, increased accountability among executives for ensuring inclusiveness of all groups through the merit evaluation process, and programs to improve promotional activities and increase inclusiveness of all groups. Moreover, qualitative and quantitative indicators to measure the progress of the recruitment, hiring and promotion programs were developed and deployed. These indicators are linked to the diversity business strategy.

The Postal Service's Supplier Diversity Program will be expanded to include the training of local buying personnel, collection of data for measuring the success of the program over time, and improving subcontractor participation to include more women and minorities.

Some of the specific initiatives for FY 2000 and beyond include: organization-wide communication of the corporate diversity policy statement, accountability for managing diversity in the merit evaluation for each postal executive, increased focus on underrepresented groups in the employee recruitment process, and expanding corporate succession planning to promote entrance of underrepresented groups into higher levels of management.

b. National Diversity Recognition Program

It is Diversity Development's goal to encourage and support the efforts of the U.S. Postal Service employees that (1) contribute to the acceptance of diversity within the workplace, (2) positively recognize our employee and customer populations, and (3) address the needs of every population we serve. In line with this mission, Diversity Development established a National Diversity Recognition Program to recognize managers and employees for their outstanding contributions to the diversity effort.

In 1998, the program shifted from a departmental to a corporate focus and awards were sponsored through the Management Committee. Identified as the largest peer recognition in Postal Service history, the awards program is aimed at providing employees an opportunity to recognize individuals and teams that have made significant contributions to encourage, promote, and celebrate diversity. The 1999 program resulted in approximately 1,400 employees nominated into the program, with a total of 34 National Award Winners. To date, a total of 131 employees at the craft, management, and executive levels have been recognized for outstanding contributions toward diversity corporate goals at an annual awards banquet in their honor.

Recognizing and valuing diversity continues to be a business requirement and is key to enabling our core processes to attain *CustomerPerfect!* goals. Rewarding postal employees and managers for their support of and accountability to diversity initiatives will help the Postal Service remain a more inclusive, versatile, and productive organization.

currently being revised. The revised Guide will be mailed to all postal employees' homes.

Publication 552, *Managers' Guide to Understanding Sexual Harassment*, was updated to include recent changes in the law and to add the Initial Management Inquiry Process (IMIP) to guide managers in handling and resolving sexual harassment complaints. This revised guide was distributed in June 1999 to all installation heads throughout the organization.

The establishment of a national tracking system to determine the extent to which sexual harassment is reported in the workplace has been placed on hold due to funding considerations.

Prevention and elimination of sexual harassment is an ongoing effort. Goals for the coming year include:

• the design, development, and distribution of new posters for sexual harassment prevention awareness throughout field units;

• the design, development, and distribution of a "tool kit" for sexual harassment prevention for facilitators and managers (to be provided in early FY 2000);

• a partnership with Human Resources to offer additional training courses through PBS the Business Channel; and

• a PSTN broadcast on the Initial Management Inquiry Process to guide and assist PCES and EAS employees in conducting initial inquiries into allegations of sexual harassment in the workplace.

In line with the mandatory, one-hour VOE training for craft employees, a new postal video entitled *Workplace Environment on Sexual Harassment Prevention* was developed to increase their understanding and awareness about the serious nature of sexual harassment and to maintain an environment free of sexual harassment. This mandatory, video-based training program will be rolled out next fiscal year. To assist with this effort, Service Talks also will be provided with the video to influence positive change within the organization and achieve a workplace free of sexual harassment.

A menu of course training materials also will be provided to assist EAS employees in meeting their two-hour sexual harassment VOE training requirement.

f. Training and Development

1. Bias-Free Awareness and Communication Training. The Postal Service's mission is to create an inclusive environment in our organization so that the diverse needs of our employees, customers, and suppliers are integrated into the business approach. Demographics, attitudes, and economics are all constantly changing. Language both reflects and shapes society; it goes hand-in-hand with social change. To ensure competitiveness in the global marketplace, the Postal Service must continue to make certain that the language used in directives and everyday business transactions is inclusive, bias-free, nonsexist, and gender-free.

To assist in this effort, from January 22 through August 4, 1999, Diversity Development sponsored 18 sessions of a three-hour course for headquarters employees entitled: *Bias-Free Editing, Writing, and Speaking*. The purpose of the course was twofold: (1) to teach techniques and provide resources for using bias-free writing and editing in U.S. Postal Service documents as well as internal and external communications; and (2) to help employees increase their awareness of biased terms and diversity issues, thus helping them to gain knowledge that can be called upon to modify everyday business writing and speaking.

The response and feedback was very positive. The requests received far exceeded the number of available slots. More than 500 managers and employees responded to the initial announcement, immediately filling the 270 available slots and creating the need for an ongoing waiting list. To fulfill VOE requirements and accommodate additional requests subsequent to the initial announcement, the Inspection Service sponsored two of the classes for its employees and Purchasing sponsored 11 for its employees, bringing the total number of classes to 31 and participants to 465.

Each attendee participated in and received a workbook of exercises to help them to: identify seven types of discriminatory language and to examine their subsequent material for such language; identify, prevent, and recover from biased-speech errors; use alternative terms for problem words and usage; and review the writing of others.

Participants also received a copy of Rosalie Maggio's book entitled *Talking About People: A Guide to Fair and Accurate Language*, a guide consisting of alternative terms, and a 7.0 Word macro, all to use as aids to assist in keeping writing bias-free.

g. Major Purchases

During 1999, the Postal Service made more than 59,000 contractual actions, totaling approximately $9.6 billion. The following are some of 1999's most significant purchases.

A series of contracts, valued at more than $1 billion, was awarded to five suppliers to expand the Mail Transportation Equipment Service Center (MTSC) network. MTSCs repair and maintain transportation equipment. There are 22 MTSCs in the network. A $250 million contract was awarded to the Ford Motor Company for more than 11,000 carrier route vehicles. In order to further environmental initiatives, all of the vehicles will be "flex-fueled," capable of running on ethanol or unleaded gasoline. Lastly, a contract valued at $66.9 million was awarded for a new robotics containerization system which will automate several mail processing steps and a performance-based incentive contract was awarded to continue improvements in the processing of handwritten mail.

In the design and construction area, a contract worth more than $31.6 million was awarded for the construction of a new 449,384 gross-square-foot Processing and Distribution Center (P&DC) in Greensboro, North Carolina.

A $62 million contract was awarded for the design and construction of a P&DC and vehicle maintenance center in Columbus, OH, and, a $6 million contract was awarded for the exterior renovation of the Bronx, New York, General Post Office.

h. Energy and Environmental Contracting

Partnering with Engineering's Environmental Management Policy organization, Purchasing and Materials continued to support the Postal Service's ongoing Energy Program. The former Utility Deregulation Oversight Committee, which was responsible for setting strategic focus on the deregulation of the electricity and gas industries, has broadened its scope and become the National Energy Program Committee. The Committee has full oversight of all Postal Service energy-related issues. The shared energy concept continues to provide benefits in both cost savings and energy efficiency. Thirty-five shared energy contracts calling for the retrofitting of existing facilities with energy efficient products have been awarded, and annual cost savings are estimated at $8.9 million.

The National Environmental Purchasing Steering Committee, another result of the Purchasing and Materials and Environmental Management Policy partnership, also continues in efforts to further the Postal Service's environmental commitment. During 1999, the committee developed model statements of work and contracts for recycling services and for hazardous waste disposal, as well as a model competitive shared energy solicitation. Training in the resulting new purchasing procedures has been completed at 10 field purchasing offices and is available to Area and District organizations. Field organizations also had an impact in the environmental area. In 1999, 30 contracts were awarded for such things as the nationwide Integrated Retail Terminal (IRT) removal, paper and undeliverable bulk business mail recycling, and other environmental services. Lastly, the manager of the Dallas Purchasing and Material Management Service Center received the White House's *Closing the Circle* award for his environmental efforts, and two employees at the Greensboro Purchasing and Material Management Service Center received the *Federal Energy and Water Management* award.

i. Supplier Diversity

The Postal Service's Supplier Diversity Program is a fundamental element of the Postal Service's corporate strategy to remain competitive and profitable in the marketplace. The purpose of the program is to ensure small, minority, and woman-owned businesses equal access to the Postal Service's purchasing opportunities.

Following the adoption and distribution of a general policy on Diversity in October 1998, the Postal Service issued its Supplier Diversity Statement of Commitment. The Statement was broadly disseminated and is featured on the Internet. In January 1999, the Service updated and reissued its five-year Supplier Diversity Plan which reinforces the message that "Supplier Diversity is everyone's responsibility"—the responsibility of the person generating the requirement, the person approving the purchases and the person making the commitment of postal funds. The Plan focuses on six key areas: (1) planning, (2) communication/assistance, (3) recognition, (4) sourcing, (5) training, and (6) accountability. It reinforces the precept that a strong, committed, and diverse supplier base is critical to our long-term interests. Our goal is to make the Postal Service a world-class leader in Supplier

Diversity. That goal was furthered by the issuance of the Supplier Diversity Plan, applicable to all Postal Service purchasing organizations.

Internal and external communications and training continue to be critical to the overall success of the Supplier Diversity Program. Buying organizations hold "supplier focus groups" to explore opportunities for process simplification. Supplier councils, supplier surveys, and various interagency linkages are also used to secure supplier feedback to make it easy for suppliers to do business with us. In February, our efforts to promote supplier diversity led to a significant revision of our subcontracting policy. Our efforts here were to improve and clarify our approaches and insistence that our prime contractors aggressively consider small, minority, and women-owned firms when they subcontract on our projects. The revised policy requires subcontract planning by our larger suppliers and quarterly accomplishment reports from most of our suppliers holding contracts valued in excess of $500,000.

We are also testing new business practices. In the Los Angeles area, local purchasing organizations have joined together, across commodity lines, to focus on more effective sourcing and communications methods. Should these prove successful, they will be used nationally.

In response to our VOC and VOB goals, in 1999 the Postal Service sponsored or co-sponsored industry events in cooperation with national supplier organizations such as: the U.S. Hispanic Chamber of Commerce, the National Council of LaRaza, the National Urban League, the Organization of Chinese Americans, the League of United Latin Americans, the National Association for the Advancement of Colored People, the National Congress of American Indians, and the Pan Asian American Chamber of Commerce.

We have participated in an estimated 50 trade, federal, Congressional, and special emphasis supplier-focused events. Local offices sponsored Supplier Diversity events across the country to provide opportunities for suppliers to demonstrate their products, services, and capabilities. The events also typically include supplier workshops and seminars on doing business with the Postal Service. These outreach efforts: (1) helped to create brand awareness, (2) increased contacts with the supplier community, (3) improved understanding of supplier capabilities, (4) enhanced our ability to "source" from a broader field of potential suppliers, and (5) heightened our image as a public sector organization that supports supplier diversity and economic development within the communities we serve.

The Postal Service also continued to cultivate business relationships with organizations that sponsor and promote small business and those owned and managed by minorities and women. Our partnerships with the Business Women Network, the National Association for Women Business Owners, the Pan Asian Chamber of Commerce, the U.S. Hispanic Chamber of Commerce, and the National Minority Supplier Development Council (NMSDC) have provided the Postal Service access to their supplier databases. As an example, this year the Postal Service acquired on-line access to the national database for the NMSDC, located on the Internet. The NMSDC advocates minority business development by fostering mutually beneficial links between minority suppliers and the federal and private business sectors. The Minority Business Information System (MBISYS 2000) provides comprehensive information on more than 15,000 of America's top minority-owned firms. Our partnerships with these organizations also yielded educational seminars, training, and technical assistance.

Annual Supplier Diversity training was expanded this year to cover all employees in buying functions. Over 650 professional buyers articulated Individual Development Plans that included experiential and training opportunities in cultural and supplier diversity.

During 1999, more than 71 percent of contractual actions (representing more than $4.1 billion) went to small businesses. More than $363 million (representing 9.8 percent of contractual actions) went to minority businesses, and more than $446 million (representing 11 percent of contractual actions) went to woman-owned businesses. These figures do not include the results of our new subcontracting policies. We have begun to collect this data and will include it in future reports.

USPS
MINNEAPOLIS POSTAL DATA CENTER
REPORT HREN98NT

U.S. POSTAL SERVICE
DIVERSITY REPORTING SYSTEM
NATIONAL SUMMARY REPORT
(BASED ON JOB LEVEL)

CREATE DATE: 09/09/
PAGE:
PAY PERIOD: 19/

CAREER EMPLOYEES (EXCLUDING IG)

POSTAL QUARTER: IV/

LEVEL	TOTAL MALE	TOTAL FEMALE	WHITE MALE	WHITE FEMALE	BLACK MALE	BLACK FEMALE	HISP MALE	HISP FEMALE	AAPI MALE	AAPI FEMALE	AIAN MALE	AIAN FEMALE	W/DIS MALE	W/DIS FEMALE	U M	TOT
CLF - %	54.25	45.75	42.64	35.30	4.95	5.45	4.77	3.35	1.51	1.32	.35	.30				
PCES	682	172	555	120	76	43	41	4	9	4	1	1	5	1	0	8
	79.9	20.1	65.0	14.1	8.9	5.0	4.8	.5	1.1	.5	.1	.1	.6	.1	.0	
01-14	454771	270425	301727	160914	83560	73525	36515	16350	30862	17818	2023	1792	36334	9981	110	725
	62.7	37.3	41.6	22.2	11.5	10.1	5.0	2.3	4.3	2.5	.3	.2	5.0	1.4	.0	
15-18	31027	19902	22453	12405	5398	5804	2041	961	957	604	176	124	1466	327	6	50
	60.9	39.1	44.1	24.4	10.6	11.4	4.0	1.9	1.9	1.2	.3	.2	2.9	.6	.0	
19-UP	14293	5263	11208	3259	1714	1501	846	272	419	195	102	35	291	73	5	19
	73.1	26.9	57.3	16.7	8.8	7.7	4.3	1.4	2.1	1.0	.5	.2	1.5	.4	.0	
TOTAL	500773	295762	335943	176698	90748	80873	39443	17587	32247	18621	2302	1952	38096	10382	121	796
	62.9	37.1	42.2	22.2	11.4	10.2	5.0	2.2	4.0	2.3	.3	.2	4.8	1.3	.0	

NOTE: MINORITY CODES
WHITE (E) = WHITE, NOT OF HISPANIC ORIGIN
BLACK (C) = BLACK, NOT OF HISPANIC ORIGIN
HISP (D) = HISPANIC
AAPI (B) = ASIAN OR PACIFIC ISLANDER
AIAN (A) = AMERICAN INDIAN OR ALASKAN NATIVE
UM = RACE NOT SELF-IDENTIFIED

Attachment 6

Attachment 7

October 7, 1996

STRATEGIC ALLIANCE GUIDELINES

1. DEFINITION

A strategic alliance is a cooperative arrangement between the Postal Service and one or more private entities. In return for a substantive benefit from cooperative efforts to develop and/or market a joint product, the Postal Service allows its alliance partner(s) the use of or access to Postal Service property, either tangible (e.g. retail lobby space) or intangible (e.g. trademarks, copyrights, patents and technical data) and/or the efforts of Postal Service personnel. The Postal Service may also obtain the use of or rights to the partner's property. Joint products may include a service or product sold to the public, joint marketing activities, a patented process or device, technical data, software, and cost savings strategies or devices. The cooperative effort may result in revenue or cost savings to the Postal Service from the joint product.

2. DISTINGUISHING A STRATEGIC ALLIANCE FROM A PURCHASE

The act of obtaining goods and services for the benefit of the Postal Service in exchange for Postal Service funds is generally a purchase governed by the Procurement Manual. Although the Postal Service may obtain the use of goods and services as a result of a strategic alliance, generally the goods, services and rights obtained are those employed in the common and mutually beneficial cooperative effort, and the acquisition of those goods and services cannot be the primary purpose of the arrangement. Purchasing and Materials and the Law Department should be consulted early in the project development in order to determine whether a particular undertaking constitutes a purchase or a strategic alliance.

3. SCOPE

These guidelines apply to the initiation, development, testing, and final implementation of any program in which a strategic alliance will be involved.

4. DEFINING THE PROJECT AND DETERMINING BENEFITS

Whenever a Postal Service department or organization is considering sponsoring a strategic alliance, it will assess and document the following:

Purpose: Identify the objective of the strategic alliance and the intended commitments as well as advantages to the Postal Service.

Market Demand Analysis: Perform and describe an analysis of the market place to determine if the proposed alliance will meet market expectations in the face of competitive alternatives and customer requirements. Determine (a) who wants the product and in what quantities, (b) what are the future prospects of the product or service or business opportunity in terms of customer acceptance,

(c) what is the net revenue generation for the Postal Service, and (d) what is the positioning of postal products and services in a competitive environment.

Financial Analysis: In conjunction with the Finance Department determine revenue projections and costs associated with the proposed alliance. Include data on expected initial market share and the target being sought, and perform an analysis of financial risk, an evaluation of costs and revenue sharing by the partners, and a forecast of sustained market share over a relevant period of time.

Infrastructure and Operations Impact: Assess the impact on the Postal Service's infrastructure and operations to determine if additional costs must be incurred and whether the potential return justifies any new investment. This assessment should include the personnel or labor relations plans for the venture.

Service Requirements: Evaluate existing service expectations in order to provide a framework to determine the required service standards for the proposed alliance.

Legal Analysis: Obtain an analysis from the Law Department of significant legal issues relating to the proposed alliance.

CustomerPerfect! Compliance: Show direct contribution to Postal Service Goals, Sub-Goals, and Indicators as part of the Establish Process. In addition to VOB and VOC considerations, there should be a clear consideration of any impact on VOE Human Resources strategies.

5. DEVELOPING THE PROJECT AND SELECTING THE PARTNER

New Product Development Process: These Strategic Alliance Guidelines are intended to complement the New Product Development Process. Instructions on integrating these processes are in Appendix A.

Alliance Partner Selection Process: Depending on the circumstances, the alliance may be achieved through a competitive or non-competitive process. In either case, a written justification for the selection of an alliance partner over other potential partners must be prepared. A list of factors to be addressed in the justification is in Appendix B.

The Strategic Alliance Agreement: Because alliances are not governed by Procurement Manual procedures, a detailed agreement must be negotiated in writing for each alliance. Procedures for creating an agreement are in Appendix C.

APPENDIX A

COORDINATION OF THE STRATEGIC ALLIANCE GUIDELINES WITH THE NEW PRODUCT DEVELOPMENT PROCESS

1. The Strategic Alliance Guidelines are intended to complement the 5.1 New Product Development Process (*CustomerPerfect* 5.1) by providing procedures to follow when the Postal Service is proposing to develop and/or market a new product with an alliance partner. In these circumstances, the Preliminary Business Plan should explain the value to the Postal Service of the joint product, as set out in section 4 of the Strategic Alliance Guidelines.

2. The Preliminary Business Plan should also include a section justifying the selection of the alliance partner, as set out in Appendix B of the Strategic Alliance Guidelines. Depending on the circumstances, the alliance may be achieved through a competitive or non-competitive process. In either case, the selection process should be followed in selecting an alliance partner for the test market phase as well as for the national roll-out. The Business Plan should consider whether it is in the best interest of the Postal Service to test market with one partner and then change partners when the national roll-out of the product occurs. If the sponsoring organization considers a change of partners detrimental to product success, then it must document this in the selection process and incorporate it in the selection justification before the market test begins.

3. Consistent with *CustomerPerfect* 5.1, all strategic alliance Preliminary Business Plans must be approved by the Management Committee and reviewed by the Board of Governors.

APPENDIX B

FACTORS TO BE ADDRESSED IN THE SELECTION JUSTIFICATION FOR A STRATEGIC ALLIANCE PARTNER

1. Competitive Selection: Generally, unless there are compelling reasons for the selection of one specific partner, several potential partners should be considered. If a competitive selection is used, the sponsoring organization will choose, with the assistance of Purchasing and Materials and the Law Department, an appropriate method for identifying and considering potential alliance partners. Appropriate methods for identifying potential partners may include the following:

A. Use of a market survey,

B. Publishing a notice requesting interested parties to submit their qualifications, and

C. Solicitation of detailed proposals from potentially qualifying parties.

2. Noncompetitive Selection: If a noncompetitive selection is made, explain the extent to which one or more of the following criteria affected the selection of the alliance partner:

Special Attributes - The alliance partner has special attributes that satisfy the intended objective and compares favorably with other firms that were considered (identify other firms considered). Examples of special attributes include, but are not limited to, the following:

(a) a patent on a device or process,

(b) technical data or knowledge not available anywhere else,

(c) access to a market that other firms do not possess,

(d) possession of trademarks, copyrights, or other intellectual property which the Postal Service wants to use,

(e) special knowledge or experience concerning a market, product or process, and

(f) special standing or position in a particular market.

Confidentiality - Discussions with other parties concerning a strategic alliance plan or joint product would cause significant harm to the Postal Service. The Chief Marketing Officer (or a designee) (or the VP of the sponsoring organization, if different) and the VP of Purchasing and Materials (or a designee) should concur in the need for confidentiality.

Nondisclosure Agreement - The terms of a nondisclosure agreement preclude discussions with other parties. If that is so, explain the necessity for entering into the nondisclosure agreement. Note: If the potential alliance partner requests that Postal Service personnel execute nondisclosure agreements before discussing a potential strategic alliance plan, consult Purchasing and Materials and the Law Department for advice before executing the agreement. The wording of such agreements can seriously hamper future activities.

Compelling Urgency - The Postal Service has a compelling urgency for proceeding with a strategic alliance; delay would seriously harm the Postal Service.

Best Interests of the Postal Service - A competitive procedure would not be in the interest of the Postal Service.

3. Written Justification: A determination that an alliance partner is suited for the strategic alliance should be in writing and should include appropriate documentation.

4. Identification of Firm: Analyze the relevant strengths and weakness of the firm chosen for the alliance. Describe with particularity how the idea originated and the circumstances which indicate that the chosen firm has the financial, management, and technical resources necessary to deal successfully with the Postal Service to achieve the intended objective.

5. Conflict: Those involved in the selection of an alliance partner, or making any decisions about the alliance itself, must not have any financial interests that could present a conflict or the appearance of a conflict. Organizational conflicts between the Postal Service and its contractors and alliance partners should also be avoided. The Law Department should be consulted immediately if there are any questions in this regard.

APPENDIX C

DRAFTING AND NEGOTIATING THE STRATEGIC ALLIANCE AGREEMENT

1. The Strategic Alliance Agreement is a contract and must be drafted and negotiated with the same care as any other Postal Service contract. The contract should define all relevant rights and obligations of the Postal Service and the alliance partner, including (1) damages/liability, (2) intellectual property, (3) indemnification, (4) termination, and (5) sovereign acts.

2. No agreement may be for an indefinite length. Unless authorized by the Management Committee, all agreements must provide for termination by the Postal Service upon notice or for convenience with defined damages.

3. Legal counsel and Purchasing and Materials should be included early in the process to assist in drafting and negotiating strategic alliance agreements.

4. Strategic Alliance Agreements must be signed by an official with contracting authority or who receives a delegation of such authority from the VP of Purchasing and Materials for the purpose of signing the agreement.

5. The contract should be reviewed by the Finance Department and other departments likely to be affected by the strategic alliance.

6. No binding contract should be signed with the alliance partner until the Management Committee and/or the Board of Governors have reviewed the strategic alliance at issue.

Attachment 8

Individuals who worked under Personal Services Contract 104230-92-P-3543

Name	Funded Amount (Includes travel)	Start	End
Sparks, Norman	$185,473.10	09/92	08/94
Letts, David	$305,912.92	01/93	09/96
Tyson, Preston	$404,069.24	02/93	12/93
Thompson, Ingrid	$169,898.10	02/93	06/95
Stringer, Rafael	$65,541.44	03/93	08/93
Olinger, Mark	$171,414.30	04/93	06/95
Vanderyt, Lawrence	$727,300.00	07/93	10/98
Osmond, Nancy	$157,080.00	11/93	08/94
Graff, Richard	$73,900.00	01/94	09/94
Hunter, Ken	$498,404.50	08/94	03/99
Amoroso, Frank	$409,910.00	02/95	08/99
Strunk, Herbert	$52,042.22	02/95	09/95
Harzer, Karl	$141,360.00	03/95	02/96
Hennessey, Vince	$218,202.50	06/95	12/96

Attachment 9

U.S. Postal Inspection Service

INSPECTION SERVICE EMPLOYMENT REPORT

1. WRN	2. Name	3. Month Year
4. Name of Division	5. QA	6. Team

7. Case Number	Hours	7. Case Number *(Continued)*	Hours
– – ( )		– – ( )	
– – ( )		– – ( )	
– – ( )		– – ( )	
– – ( )		– – ( )	
– – ( )		– – ( )	
– – ( )		– – ( )	
– – ( )		– – ( )	
– – ( )		– – ( )	
– – ( )		– – ( )	
– – ( )		– – ( )	
– – ( )		– – ( )	
– – ( )		– – ( )	
– – ( )		– – ( )	
– – ( )		– – ( )	
– – ( )		– – ( )	
– – ( )		– – ( )	
– – ( )		– – ( )	
– – ( )		– – ( )	

8. Leave		Hours	9. Administrative		Hours
Annual			Relocation	51	
Sick			All Other	52	
Holiday			10. Instructor		
Military	(ML)		11. Training		Hours
Relocation	(RL)		Physical Fitness	01	
Other	(OL)		Basic	11	
Leave w/o Pay	(LW)		Post Basic	12	
Comments:			Basic Functional	13	
			Technical	14	
			Developmental	15	
			Threat Management	16	
			12. Other		Hours
			Continuing Professional Education	71	
			Organized Crime	72	

13. Signature	14. Date

IS Form **512-A**, June 1998 (page 1 of 2) (20260-2172)

Audit Committee Chairman's Letter

Attachment 10

The Chairman of the Board of Governors selects the members of the Audit Committee. During 1999, the Committee, consisting of Governors Daniels, Winters and myself met six times in conjunction with the regularly scheduled monthly Board meetings.

The Audit Committee is responsible, on behalf of the Board of Governors, for reviewing the financial reporting process, ensuring the soundness of the accounting and control practices, and the integrity of the financial statements of the Postal Service.

The Committee recommends to the Board, subject to its approval, the selection of the independent accounting firm responsible for the external audit as well as oversees compliance with the terms of the audit contract. During the year the Board, upon the recommendation of the Committee, designated the Inspector General the co-Contracting Officer Representative, along with the Vice President, Controller, for the external audit contract and approved a one-year extension of the contract through the 2001 audit.

During 1999, the Committee reviewed the Board's Audit Charter and recommended no changes at this time. As a part of its responsibilities, the Committee also reviewed other related postal issues as appropriate. Two specific issues received special attention at each meeting: the Year 2000 (Y2K) initiative and the status of management's actions on the Office of Inspector General audit recommendations.

With regard to the financial statement audit for 1999, the Committee, at the start of the audit process, discussed the overall scope of work and the respective audit plans with the external auditors, Ernst & Young LLP, the Office of the Inspector General and the Postal Inspection Service. We also met regularly with them as well as management and the General Counsel jointly and independently to discuss the progress of the audit work. This included an evaluation of the organization's internal controls and the quality of the financial reporting process. This provided the opportunity for the Committee to assess the coordination of the audit work and ensure independence and objectivity in the respective internal and external audit programs.

Accordingly, the Committee recommended and the full Board in its deliberations approved the financial statements for 1999.

Ned R. McWherter
Chairman, Audit Committee
December 7, 1999

Report of Independent Auditors

Board of Governors
United States Postal Service

We have audited the accompanying balance sheets of the United States Postal Service as of September 30, 1999 and 1998, and the related statements of operations, changes in net capital deficiency and cash flows for each of the three years in the period ended September 30, 1999. These financial statements are the responsibility of the United States Postal Service's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards and the standards for financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the United States Postal Service at September 30, 1999 and 1998, and the results of its operations and its cash flows for each of the three years in the period ended September 30, 1999, in conformity with generally accepted accounting principles.

In accordance with *Government Auditing Standards*, we have also issued a report dated November 9, 1999, on our consideration of the United States Postal Service's internal control over financial reporting and on tests of its compliance with certain provisions of laws, regulations, contracts, and grants.

Ernst & Young LLP

Washington, D.C.
November 9, 1999

Historical Perspective

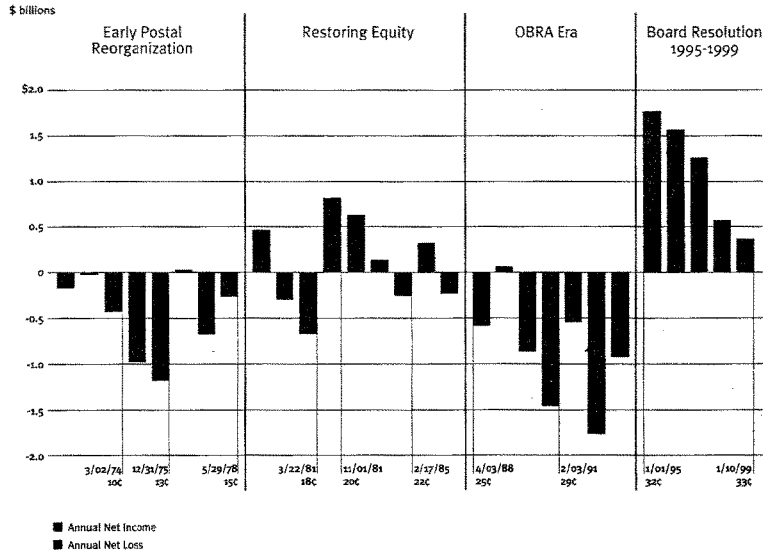
29-Year Net Income

Where did all the net income go? We may have been in the "black" for the past five years, but since the Post Office Department's 1971 reorganization the United States Postal Service has been in the "red" more often, totaling losses of $11.4 billion versus gains of $7.9 billion.

The Postal Service stopped receiving subsidies from Congress in 1982. However, the Postal Service's current financial position was greatly impacted by the 1990 Omnibus Budget Reconciliation Act (OBRA) legislation that made the USPS responsible for all health benefits and COLAs for its retirees since July 1, 1971. To date we have paid Congress approximately $14.9 billion.

At the beginning of 1995, the Postal Service had accumulated almost $9 billion in net losses since being established in 1971. In keeping with the intent of the legislation that created the Postal Service and mandated that revenues cover costs, the Postal Service Board of Governors adopted a resolution in July 1995 to restore the organization's equity by recovering these losses. The total net income of $5.5 billion earned during the five-year period from 1995-1999 has enabled the Postal Service to recover more than half of the prior years' losses. This remarkable financial turn around was accomplished with a below-inflation rate increase, rising mail volume and a moderate increase in expenses.

The Postal Service still has $3.5 billion in prior years' losses.



Financial History Summary

	1999	1998	1997
Statements of Operations			
(dollars in billions)			
Total revenue	**$ 62.7**	$ 60.1	$ 58.3
Total expense	**62.4**	59.5	57.0
Net income (loss)	**$ 0.4**	$ 0.6	$ 1.3
(dollars in millions)			
Operating revenue	**$62,655**	$60,005	$58,133
Revenue forgone appropriation	**71**	67	83
Total operating revenue	**62,726**	60,072	58,216
Compensation and benefits	**47,322**	45,588	43,835
Restructuring costs	**—**	—	—
Other expenses	**13,309**	12,190	11,038
Total operating expenses	**60,631**	57,778	54,873
Income from operations	**2,095**	2,294	3,343
Interest and investment income	**29**	44	115
Interest expense on deferred retirement liabilities	**(1,592)**	(1,597)	(1,597)
Imputed interest on retroactive assessment for employee benefits	**—**	(16)	(32)
POD workers' compensation expense	**(11)**	(8)	(258)
Interest expense on borrowings	**(158)**	(167)	(307)
Income (loss) before retroactive assessments and extraordinary items	**363**	550	1,264
Retroactive assessments for employee benefits**	**—**	—	—
Income (loss) before extraordinary item	**363**	550	1,264
Extraordinary item—debt refinancing premium	**—**	—	—
Net income (loss)	**$ 363**	$ 550	$ 1,264
Balance Sheets			
Assets			
Current assets	**$ 980**	$ 1,528	$ 1,463
Property and equipment, deferred retirement costs and other assets	**54,713**	53,015	51,675
Total assets	**$55,693**	$54,543	$53,138
Liabilities			
Current liabilities	**$15,120**	$14,913	$13,834
Other liabilities	**37,466**	37,652	37,439
Long-term debt	**3,554**	2,788	3,225
(Net capital deficiency)/equity	**(447)**	(810)	(1,360)
Total liabilities and (net capital deficiency)/equity	**$55,693**	$54,543	$53,138
Changes in (Net Capital Deficiency)/Equity			
Beginning balances			
Capital contributions of the U.S. government	**$ 3,034**	$ 3,034	$ 3,034
Deficit since reorganization	**(3,844)**	(4,394)	(5,658)
Total beginning balance (net capital deficiency)/equity	**(810)**	(1,360)	(2,624)
Net income (loss)	**363**	550	1,264
Ending balance***	**$ (447)**	$ (810)	$ (1,360)

* Certain reclassifications have been made to previously reported amounts.
** Relates to OBRA 1990 and 1993.
*** Some totals may not add exactly due to rounding.

1996*	1995*	1994*	1993*	1992*	1991*	1990*	1989*
$ 56.6	$ 54.5	$ 49.6	$ 48.0	$ 47.1	$ 44.2	$ 40.1	$ 38.9
55.0	52.7	50.5	49.8	47.6	45.7	41.0	38.8
$ 1.6	$ 1.8	$ (0.9)	$ (1.8)	$ (0.5)	$ (1.5)	$ (0.9)	$ 0.1
$56,309	$54,176	$49,252	$47,418	$46,151	$43,323	$39,202	$37,979
93	117	131	164	545	562	453	436
56,402	54,293	49,383	47,582	46,696	43,885	39,655	38,415
42,676	41,931	39,609	38,448	37,122	34,904	33,158	31,349
—	—	—	129	1,010	—	—	—
10,437	8,799	8,846	7,745	7,521	7,215	6,276	6,002
53,113	50,730	48,455	46,322	45,653	42,119	39,434	37,351
3,289	3,563	928	1,260	1,043	1,766	221	1,064
142	216	193	404	409	318	419	505
(1,449)	(1,364)	(1,336)	(1,346)	(1,269)	(1,172)	(1,056)	(1,020)
(47)	(79)	(97)	(70)	(81)	(91)	—	—
—	—	—	—	—	—	—	—
(368)	(566)	(601)	(620)	(638)	(480)	(458)	(488)
1,567	1,770	(913)	(372)	(536)	341	(874)	61
—	—	—	(857)	—	(1,810)	—	—
1,567	1,770	(913)	(1,229)	(536)	(1,469)	(874)	61
—	—	—	(536)	—	—	—	—
$ 1,567	$ 1,770	$ (913)	$ (1,765)	$ (536)	$ (1,469)	$ (874)	$ 61
$ 1,447	$ 2,775	$ 2,683	$ 4,478	$ 6,027	$ 4,863	$ 4,528	$ 5,448
50,157	46,146	43,733	42,803	41,638	38,403	32,977	31,324
$51,604	$48,921	$46,416	$47,281	$47,665	$43,266	$37,505	$36,772
$12,573	$11,299	$11,665	$10,140	$ 9,484	$ 7,400	$ 6,290	$ 5,898
37,746	34,794	32,985	33,503	32,291	30,474	25,825	25,103
3,909	7,019	7,727	8,686	9,173	8,139	6,668	6,173
(2,624)	(4,191)	(5,961)	(5,048)	(3,283)	(2,747)	(1,278)	(402)
$51,604	$48,921	$46,416	$47,281	$47,665	$43,266	$37,505	$36,772
$ 3,034	$ 3,034	$ 3,034	$ 3,035	$ 3,034	$ 3,034	$ 3,036	$ 3,039
(7,225)	(8,995)	(8,082)	(6,318)	(5,781)	(4,312)	(3,438)	(3,499)
(4,191)	(5,961)	(5,048)	(3,283)	(2,747)	(1,278)	(402)	(460)
1,567	1,770	(913)	(1,765)	(536)	(1,469)	(874)	61
$ (2,624)	$ (4,191)	$ (5,961)	$ (5,048)	$ (3,283)	$ (2,747)	$ (1,278)	$ (402)

Operating Statistics

(in millions of units indicated)

Mail Revenue	1999	1998*	1997	1996	1995
First-Class Mail					
Pieces, number	**101,936.5**	100,434.2	99,659.9	98,216.1	96,295.9
Weight, pounds	**4,299.9**	4,151.3	4,115.1	4,019.5	3,865.0
Revenue	**$ 34,933.2**	$ 33,861.2	$ 33,397.6	$ 33,116.5	$ 31,955.1
Priority Mail					
Pieces, number	**1,189.5**	1,174.4	1,068.2	937.3	869.0
Weight, pounds	**2,142.6**	1,980.0	1,860.6	1,562.8	1,483.7
Revenue	**$ 4,533.3**	$ 4,187.4	$ 3,856.9	$ 3,321.5	$ 3,074.7
Express Mail					
Pieces, number	**68.7**	66.2	63.6	57.6	56.7
Weight, pounds	**78.3**	77.7	76.3	63.7	62.5
Revenue	**$ 942.0**	$ 854.5	$ 824.7	$ 736.8	$ 710.9
Mailgrams					
Pieces, number	**4.1**	4.3	5.3	4.2	4.5
Revenue	**$ 1.6**	$ 1.7	$ 2.0	$ 1.6	$ 1.5
Periodicals					
Pieces, number	**10,273.8**	10,316.8	10,411.4	10,126.2	10,194.2
Weight, pounds	**4,482.6**	4,451.1	4,338.3	4,132.0	4,210.8
Revenue	**$ 2,115.3**	$ 2,072.3	$ 2,067.5	$ 2,013.9	$ 1,971.9
Standard Mail (A)					
Pieces, number	**85,661.7**	82,508.1	77,253.6	71,686.1	71,112.1
Weight, pounds	**10,648.3**	10,376.8	9,693.9	9,014.4	9,233.9
Revenue	**$ 14,435.8**	$ 13,701.7	$ 12,876.0	$ 12,175.1	$ 11,791.5
Standard Mail (B)					
Pieces, number	**1,043.1**	1,023.4	988.4	948.9	936.2
Weight, pounds	**3,533.2**	3,407.3	2,889.9	2,696.6	2,708.6
Revenue	**$ 1,828.5**	$ 1,754.3	$ 1,627.6	$ 1,524.1	$ 1,524.7
International Surface					
Pieces, number	**103.2**	95.6	97.4	104.5	105.5
Weight, pounds	**96.1**	95.6	102.0	106.5	114.2
Revenue	**$ 193.9**	$ 183.7	$ 192.0	$ 198.9	$ 205.3
International Air					
Pieces, number	**860.3**	848.4	909.5	948.6	695.6
Weight, pounds	**148.8**	149.0	157.2	147.0	135.2
Revenue**	**$ 1,434.2**	$ 1,416.1	$ 1,422.8	$ 1,449.9	$ 1,254.1
U.S. Postal Service					
Pieces, number	**382.3**	380.1	377.3	360.1	412.3
Weight, pounds	**102.6**	96.2	88.4	97.8	79.7
Free Mail for the Blind and Handicapped					
Pieces, number	**53.2**	53.2	53.3	50.0	51.7
Weight, pounds	**26.6**	27.2	30.6	32.6	32.1
TOTALS* **					
Pieces, number	**201,576.3**	196,904.7	190,888.1	183,439.5	180,733.7
Weight, pounds	**25,558.8**	24,812.3	23,352.4	21,873.0	21,925.7
Revenue	**$ 60,417.8**	$ 58,032.9	$ 56,267.0	$ 54,538.2	$ 52,489.7

* Revisions have been made to amounts previously reported in 1998.
** Includes foreign postal transaction revenue.
*** Agency and franked mail are included in their classes of mail.
Some totals may not add exactly due to rounding.

(in millions of units indicated)

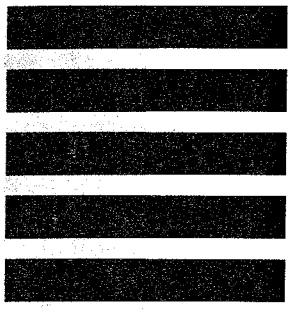
Mail Revenue	1999	1998*	1997	1996	1995
Registered**					
Number of articles	**13.7**	15.3	16.3	18.6	20.5
Revenue	**$ 95.2**	$ 89.2	$ 95.2	$ 113.3	$ 117.5
Certified**					
Number of articles	**268.1**	278.3	284.5	270.8	288.8
Revenue	**$ 377.3**	$ 385.7	$ 342.8	$ 558.5	$ 560.3
Insurance**					
Number of articles	**48.6**	40.8	33.7	28.7	28.9
Revenue	**$ 91.5**	$ 72.5	$ 61.0	$ 49.2	$ 51.8
Delivery Receipt Services***					
Number of articles	**249.3**	237.3	260.5	-	-
Revenue	**$ 284.7**	$ 262.1	$ 289.4	-	-
Collect on Delivery					
Number of articles	**4.0**	3.8	4.7	4.9	5.3
Revenue	**$ 19.8**	$ 17.8	$ 21.8	$ 21.3	$ 20.8
Special Delivery					
Number of articles	**—**	—	0.1	0.4	0.3
Revenue	**$ —**	$ —	$ 1.4	$ 3.8	$ 2.9
Money Orders					
Number issued	**220.9**	208.6	206.1	214.0	201.8
Revenue	**$ 228.3**	$ 210.1	$ 212.2	$ 221.3	$ 196.0
Face value of issues (non-add)	**$28,491.1**	$26,724.6	$26,180.4	$25,355.6	$24,608.5
Other					
Box rent revenue	**$ 667.2**	$ 617.4	$ 577.6	$ 570.3	$ 531.8
Stamped envelope and card revenue	**$ 30.7**	$ 17.4	$ 17.1	$ 15.9	$ 25.4
Other revenue, net	**$ 442.0**	$ 299.8	$ 247.0	$ 217.2	$ 180.0
TOTALS					
Special Services revenue	**$ 2,236.7**	$ 1,972.1	$ 1,865.6	$ 1,770.8	$ 1,686.5
Mail revenue	**$60,417.8**	$58,032.9	$56,267.0	$54,538.2	$52,489.7
Operating revenue before appropriations	**$62,654.5**	$60,005.0	$58,132.6	$56,309.0	$54,176.2

* Revisions have been made to previously reported amounts in 1998.
** Return receipts have been broken out from registered, certified, and insurance special service categories.
*** Delivery Receipt Services contains Return Receipts, Return Receipts for Merchandise, and Delivery Confirmation. Delivery Confirmation Service began during 1999.

	1999	1998	1997	1996	1995
Headquarters and Related Employees*					
Headquarters	**2,372**	2,231	1,949	1,951	1,825
Headquarters—Field Support Units	**4,357**	4,307	4,319	4,023	4,186
Inspection Service (field)	**4,334**	4,280	4,347	4,432	4,298
Inspector General	**387**	223	101	—	—
Subtotal	**11,450**	11,041	10,716	10,406	10,309
Field Career Employees*					
Area Offices	**1,875**	1,703	1,566	1,541	1,235
Postmasters/Installation Heads	**26,108**	26,156	26,256	26,489	26,564
Supervisors/Managers	**38,835**	36,508	35,708	35,282	34,732
Prof. Admin. Tech. Personnel	**11,097**	11,703	11,369	11,035	10,987
Clerks	**292,400**	293,829	280,818	276,964	273,526
Nurses	**188**	189	193	188	188
Mail Handlers	**62,237**	62,247	59,147	58,305	57,352
City Delivery Carriers	**242,300**	240,813	234,033	238,370	239,877
Motor Vehicles Operators	**9,270**	9,026	8,625	8,429	8,029
Rural Delivery Carriers—Full Time	**54,588**	52,241	49,957	48,340	46,113
Special Delivery Messengers	—	7	1,331	1,463	1,517
Bldg. & Equip. Maintenance Personnel	**41,873**	41,054	39,954	39,272	38,161
Vehicle Maintenance Personnel	**5,574**	5,524	5,501	4,882	4,794
Subtotal	**786,345**	781,000	754,458	750,560	743,075
Total Career Employees	**797,795**	792,041	765,174	760,966	753,384
Non-Career Employees*					
Casuals	**25,067**	25,711	32,615	24,696	26,401
Non-Bargaining Temporary	**707**	784	774	654	596
Rural Subs/RCA/RCR/AUX	**57,357**	56,265	54,834	53,768	50,269
PM Relief/Leave Replacements	**12,485**	12,613	12,687	12,724	12,774
Transitional Employees	**12,355**	17,222	26,789	33,066	31,548
Offices, Stations, and Branches					
Number of post offices	**27,893**	27,952	28,060	28,189	28,392
Number of stations and branches:					
Classified stations and branches	**5,788**	5,661	5,446	5,521	5,651
Contract stations and branches	**2,903**	2,974	2,907	2,897	3,480
Community post offices	**1,585**	1,572	1,606	1,605	1,626
Subtotal	**10,276**	10,207	9,959	10,023	10,757
TOTAL OFFICES, STATIONS, AND BRANCHES	**38,169**	38,159	38,019	38,212	39,149

* Complement data uses On-Rolls and Paid Employees Statistics database.

Attachment 11



Financial Statements

United States Postal Service

Years ended September 30, 1999 and 1998
with Report of Independent Auditors

ERNST & YOUNG LLP

Financial Statements

United States Postal Service

Years ended September 30, 1999 and 1998
with Report of Independent Auditors

United States Postal Service

Financial Statements

Years ended September 30, 1999 and 1998

Contents

Report of Independent Auditors 1

Financial Statements

Balance Sheets 2-3
Statements of Operations 4
Statements of Changes in Net Capital Deficiency 5
Statements of Cash Flows 6
Notes to Financial Statements 7-22

ERNST & YOUNG LLP

1225 Connecticut Avenue, N.W.
Washington, D.C. 20036

Phone: 202 327 6000

Report of Independent Auditors

Board of Governors
United States Postal Service

We have audited the accompanying balance sheets of the United States Postal Service as of September 30, 1999 and 1998, and the related statements of operations, changes in net capital deficiency and cash flows for each of the three years in the period ended September 30, 1999. These financial statements are the responsibility of the United States Postal Service's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards and the standards for financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the United States Postal Service at September 30, 1999 and 1998, and the results of its operations and its cash flows for each of the three years in the period ended September 30, 1999, in conformity with generally accepted accounting principles.

In accordance with *Government Auditing Standards*, we have also issued a report dated November 9, 1999, on our consideration of the United States Postal Service's internal control over financial reporting and on tests of its compliance with certain provisions of laws, regulations, contracts, and grants.

Ernst + Young LLP

November 9, 1999

United States Postal Service

Balance Sheets

	September 30, 1999	1998
	(dollars in millions)	
Assets		
Current assets:		
Cash and cash equivalents	**$ 15**	$ 395
Receivables:		
Foreign countries	**337**	514
U.S. government	**149**	154
Consignment	**58**	51
Other	**147**	154
	691	873
Less allowances	**113**	88
Total receivables, net	**578**	785
Supplies, advances and prepayments	**387**	348
Total current assets	**980**	1,528
Other assets, principally revenue forgone appropriations receivable *(Note 8)*	**376**	379
Property and equipment, at cost:		
Buildings	**16,513**	15,123
Equipment	**12,421**	11,179
Land	**2,407**	2,286
Leasehold improvements	**1,019**	916
	32,360	29,504
Less allowances for depreciation and amortization	**12,143**	10,785
	20,217	18,719
Construction in progress	**2,623**	2,073
Total property and equipment, net	**22,840**	20,792
Deferred retirement costs *(Note 6)*	**31,497**	31,844
Total Assets	**$55,693**	$54,543

See accompanying notes to financial statements.

	September 30, 1999	1998
	(dollars in millions)	
Liabilities and Net Capital Deficiency		
Current liabilities:		
Compensation and benefits	**$ 5,919**	$ 5,290
Estimated prepaid postage	**1,628**	1,673
Payables and accrued expenses:		
Foreign countries	**527**	780
U.S. government	**164**	148
Other	**657**	742
Total payables and accrued expenses	**1,348**	1,670
Prepaid box rentals, permit and metered mail	**2,049**	1,955
Outstanding postal money orders	**813**	692
Current portion of debt	**3,363**	3,633
Total current liabilities	**15,120**	14,913
Long-term debt, less current portion *(Note 5)*	**3,554**	2,788
Other liabilities:		
Amounts payable for deferred retirement benefits *(Note 6)*	**29,685**	30,138
Workers' compensation costs *(Note 2)*	**4,901**	4,923
Employees' accumulated leave	**2,041**	1,959
Other	**839**	632
Total other liabilities	**37,466**	37,652
Commitments and contingencies *(Notes 9 and 11)*		
Total Liabilities	**56,140**	55,353
Net capital deficiency:		
Capital contributions of the U.S. government	**3,034**	3,034
Deficit since reorganization	**(3,481)**	(3,844)
Total Net Capital Deficiency	**(447)**	(810)
Total Liabilities and Net Capital Deficiency	**$55,693**	$ 54,543

See accompanying notes to financial statements.

United States Postal Service

Statements of Operations

	Years ended September 30,		
	1999	**1998**	**1997**
	(dollars in millions)		
Operating revenue *(Note 8)*	**$62,726**	$60,072	$58,216
Operating expenses:			
Compensation and benefits *(Notes 2, 6, and 7)*	**47,322**	45,588	43,835
Transportation	**4,267**	4,207	4,026
Other	**9,042**	7,983	7,012
Total operating expenses	**60,631**	57,778	54,873
Income from operations	**2,095**	2,294	3,343
POD workers' compensation expense *(Note 3)*	**(11)**	(8)	(258)
Interest and investment income	**29**	44	115
Interest expense on deferred retirement liabilities *(Note 6)*	**(1,592)**	(1,597)	(1,597)
Interest expense on borrowings	**(158)**	(167)	(307)
Imputed interest on OBRA 1993 retroactive assessment for employee benefits *(Note 4)*	**--**	(16)	(32)
Net Income	**$ 363**	$550	$ 1,264

See accompanying notes to financial statements.

United States Postal Service

Statements of Changes in Net Capital Deficiency

Years Ended September 30, 1999, 1998 and 1997

	Capital Contributions Of U.S. Government	Deficit Since Reorganization	Total Net Capital Deficiency
		(dollars in millions)	
Balance, September 30, 1996	$3,034	$(5,658)	$(2,624)
Net Income	–	1,264	1,264
Balance, September 30, 1997	3,034	(4,394)	(1,360)
Net Income	–	550	550
Balance, September 30, 1998	3,034	(3,844)	(810)
Net Income	–	**363**	**363**
Balance, September 30, 1999	**$3,034**	**$(3,481)**	**$ (447)**

See accompanying notes to financial statements.

United States Postal Service

Statements of Cash Flows

	Years ended September 30, 1999	1998	1997
	(dollars in millions)		
Cash flows from operating activities:			
Net income	$363	$ 550	$ 1,264
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	1,795	1,579	1,673
(Gain) loss on disposals of property and equipment, net	(55)	7	19
Decrease (increase) in other assets, principally revenue forgone appropriations receivable	3	(7)	(18)
Increase (decrease) in USPS workers' compensation	19	195	(332)
(Decrease) increase in Post Office Department workers' compensation	(21)	(27)	258
Decrease in retroactive assessments payable to the U.S. government	–	(331)	(315)
Increase in employees' accumulated leave	82	101	236
Increase in other liabilities	207	143	46
Changes in current assets and liabilities:			
Decrease (increase) in receivables, net	207	(113)	55
(Increase) decrease in supplies, advances and prepayments	(39)	40	22
Increase in compensation and benefits	503	451	128
(Decrease) increase in estimated prepaid postage	(45)	(70)	20
Decrease in payables and accrued expenses	(322)	(154)	(1)
Increase in prepaid box rentals, permit and metered mail	94	31	332
Increase (decrease) in outstanding postal money orders	121	52	(40)
Net cash provided by operating activities	2,912	2,447	3,347
Cash flows from investing activities:			
Purchase of U.S. government securities, available-for-sale	–	(620)	(300)
Proceeds from sale of U.S. government securities, available-for-sale	–	622	300
Purchase of property and equipment	(3,917)	(3,055)	(3,233)
Proceeds from sale of property and equipment	129	49	26
Net cash used in investing activities	(3,788)	(3,004)	(3,207)
Cash flows from financing activities:			
Issuance of debt	4,129	5,696	1,964
Payments on debt	(3,633)	(5,147)	(2,011)
Net cash provided by (used in) financing activities	496	549	(47)
Net (decrease) increase in cash and cash equivalents	(380)	(8)	93
Cash and cash equivalents at beginning of year	395	403	310
Cash and cash equivalents at end of year	$ 15	$ 395	$ 403

See accompanying notes to financial statements.

United States Postal Service

Notes to Financial Statements

1. Description of Business

Nature of Operations

The United States Postal Service (Postal Service) provides mail service to the public, offering a variety of classes of mail services without discrimination among its many customers. This means that within each class of mail our price does not vary by customer for the levels of service we provide. This fulfills our legal mandate to offer universal services at a fair price. Our primary lines of business are First Class Mail, Standard Mail (A) and Priority Mail. The principal markets for these services are the communications, distribution and delivery, advertising and retail markets. Our products are distributed through our more than 38,000 post offices and a large network of consignees. As in the past, we continue to conduct our significant operations primarily in the domestic market, with our international operations representing less than 3% of our total revenue.

Our labor force is primarily represented by the American Postal Workers Union, National Association of Letter Carriers, National Postal Mail Handlers Union and National Rural Letter Carriers Association (NRLCA). Almost 90% of our career employees are covered by collective bargaining agreements. Three of our largest contracts representing 82% of our career employees expired November 20, 1998. New contracts were signed that expire in 2000 and 2001. The contract for the NRLCA that represents 7% of our career employees expires on November 20, 1999.

Postal Reorganization

The Postal Service commenced operations on July 1, 1971, in accordance with the provisions of the Postal Reorganization Act (the Act). The equity that the U.S. government held in the former Post Office Department became the initial capital of the Postal Service. The Postal Service valued the assets of the former Post Office Department at original cost less accumulated depreciation. The U.S. government remained responsible for all the liabilities attributable to operations of the former Post Office Department.

The Balanced Budget Act of 1997 charged the Postal Service with certain liabilities attributable to operations of the former Post Office Department for the first time since postal reorganization. Our 1997 financial statements contained a $258 million reduction to net income as a result with an additional expenses of $11 million in 1999 and $8 million in 1998 (note 3).

1. Description of Business (continued)

Price Setting Process

Since 1971, the Act has required the Postal Service to establish prices that cover the costs of operating the postal system. The Act established the independent Postal Rate Commission with oversight responsibility for mail prices, subject to approval by the Governors of the Postal Service. The Act provides for the recovery of operating losses through future rate increases.

2. Summary of Significant Accounting Policies

Basis of Accounting and Use of Estimates

We maintain our accounting records and prepare our financial statements on the accrual basis of accounting. This basis conforms to generally accepted accounting principles. Following these principles, we made estimates and assumptions that affect the amounts we report in the financial statements and notes. Actual results may differ from our estimates.

Cash Equivalents

Cash equivalents are securities that mature within 90 days or less from the date we buy them.

Current Values of Financial Instruments

We report the current value of our investments in non-marketable U.S. government securities based on the current value of equivalent marketable U.S. government securities. The current value of our debt is what it would cost us to pay off the debt if we used the current yield on equivalent U.S. Treasury debt.

Supplies, Advances & Prepayments

Supplies, advances and prepayments are primarily composed of our inventories of supplies, motor vehicle parts, repairable parts for mail processing equipment, and advances to employees for annual leave. We value our inventories at the lower of average cost or current market price. Total inventories amounted to $172 million at the end of 1999 and $158 million at the end of 1998.

2. Summary of Significant Accounting Policies (continued)

Property and Equipment

We record property and equipment at what it cost us to acquire the assets, including the interest we pay on the money we borrow to pay for the construction of major capital additions. This interest amounted to $59 million in 1999, $44 million in 1998 and $22 million in 1997.

We depreciate buildings and equipment over their estimated useful lives, which range from 3 to 40 years, using the straight-line method. We amortize leasehold improvements over the period of the lease or the useful life of the improvement, whichever time is shorter.

During 1997 we changed our policy for expensing minor asset purchases. We increased the limit from $2,000 to $3,000. As a result, we expensed $83 million of assets in 1997 that were under the new limit.

Estimated Prepaid Postage

This is the amount of cash we estimate that we collected by the end of the year for services that we will perform in the following year.

Compensation and Benefits Payable

This is the salaries and benefits we owe to current and retired employees, including the amounts employees have earned but have not yet been paid, current workers' compensation, unemployment costs, health benefits, and the current portion of the amounts payable for retirement benefits.

Deferred Retirement Benefits

This is the present value of our estimated legal obligation to the Civil Service Retirement and Disability Fund for the amount of retirement benefits payable in the future for our current employees' retirement and our present retirees and their survivors. The present value of our benefits payable for our current employees increases when management increases basic pay. The present value of our benefits payable also increases when Cost of Living Adjustments (COLAs) are granted to our retirees or their survivors. We capitalize

2. Summary of Significant Accounting Policies (continued)

Deferred Retirement Benefits (continued)

as deferred retirement costs the amounts due and payable in future years. We expense and pay these costs over periods of 30 years for amounts attributable to current employees and 15 years for amounts attributable to retirees, at 5% interest. We account for our participation in the U.S. government sponsored retirement plans as participation in a multi-employer plan arrangement.

Post-Retirement Health Benefits

Retiree health benefits costs are our obligation to pay a portion of the health insurance premiums of those retirees and their survivors who participate in the Federal Employees Health Benefits Program (FEHBP). We account for our participation in FEHBP as participation in a multi-employer plan arrangement. Therefore, we expense the costs of our retiree health benefits as we incur them.

Workers' Compensation Costs

We are self-insured for workers' compensation costs under a program administered by the Department of Labor (DOL). We record these costs, which include the employees' medical expenses and payment for continuation of wages, as an operating expense. At the end of the year, our liability represents our estimated present value of the total amounts we expect to pay for outstanding claims. We base our estimate of the total costs of a claim upon the severity of the injury, the age of the injured employee, the assumed life expectancy of the employee, the trend of our experience with such an injury, and other factors. In our calculation of present value, we use a net discount rate of 1.4% for medical expenses and 3.0% for compensation claims.

In fiscal year 1999, management adopted a change in the net discount rate used in determining the present value of estimated future workers' compensation payments for medical claims. The net discount rate for medical claims was changed from 0.1% to 1.4%. The effect of the adoption of this rate has been accounted for as a change in accounting estimate. It resulted in a decrease of $131 million in the fiscal year 1999 compensation and benefits expense. In management's opinion, this net discount rate better reflects the excess of rates of return on government debt instruments of comparable terms relative to expected future medical inflation.

2. Summary of Significant Accounting Policies (continued)

Workers' Compensation Costs (continued)

At the end of 1999, we estimate our total liability for future workers' compensation costs, excluding Post Office Department (POD) liability (Note 3), at $5,306 million. At the end of 1998, this liability was $5,287 million. In 1999, we recorded $603 million in workers' compensation expense, compared to the $760 million we recorded in 1998 and the $206 million we recorded in 1997.

Research and Development Costs

We record research and development costs as expenses when we incur them. These costs were $67 million in 1999, $77 million in 1998 and $68 million in 1997.

Advertising

We record advertising costs as expenses when we incur them. These costs were $241 million in 1999, $301 million in 1998 and $266 million in 1997.

3. Balanced Budget Act of 1997

Under the Postal Reorganization Act of 1971, the U.S. government remained responsible for payment of all Post Office Department (POD) workers' compensation claims incurred before July 1, 1971. This Act required that the newly created USPS would be responsible only for its own workers' compensation claims. However, under the Balanced Budget Act of 1997, the remaining liability for these POD costs has now been transferred to the U.S. Postal Service. We estimate the present value of these claims was $210 million at the end of 1999. At the end of 1998, this liability was $231 million. In 1999, we recorded an expense of $11 million, compared to the $8 million we recorded in 1998 and the $258 million we recorded in 1997. In our calculation we use a net discount rate of 3%.

4. Retroactive Assessments for Employee Benefits

Omnibus Budget Reconciliation Act of 1993

Under the Omnibus Budget Reconciliation Act of 1993, we were required to pay 5% interest on the $2.14 billion retroactive assessment from the Omnibus Budget Reconciliation Act of 1990. We paid this interest in three equal annual installments of $347 million during 1996, 1997 and 1998, totaling $1.041 billion.

5. Debt and Related Interest Costs

Under the Postal Reorganization Act, as amended by Public Law 101-227, we can issue debt obligations. However, we are limited to net annual increases of $2 billion in our debt for capital improvements and to $1 billion for operating expenses. Our total debt cannot exceed $15 billion.

Debt is due as follows (dollars in millions):

Year	Amount
2000	$3,363
2001	52
2002	1
2003	200
2004	–
After 2004	3,301

We paid in cash $202 million in interest in 1999, $236 million in interest in 1998 and $336 million in 1997.

The current estimated market value of our debt is $6,877 million in 1999 and $6,639 million in 1998 (Note 2). All notes payable to the Federal Financing Bank (FFB) may be repurchased at current value at any time with five days notice of intent to do so.

The following page details our debt, which consists of Notes Payable to the FFB and Mortgage Notes Payable:

5. Debt and Related Interest Costs (continued)

Our Debt Consists of the Following (dollars in millions):

Interest Rate %	Terms*	September 30, 1999	1998
Notes Payable to the Federal Financing Bank (FFB):			
8.075	Payable $32 million each year to May 31, 2000	**$ 32**	$ 64
7.800	Payable $15 million each year to May 31, 2001	**30**	45
8.761 **	Payable $36 million May 31, 1999 and each May 31 thereafter through May 31, 2001	**72**	108
6.274	Payable May 16, 2005	**500**	500
5.002 ***	Overnight revolving credit facility; final maturity date September 30, 2000	**279**	246
4.667	Payable November 15, 2026; repurchasable at par November 16, 1998 and every February 15, May 15 and August 15 thereafter	**–**	600
5.084	Payable March 30, 2000	**500**	–
4.977	Payable March 31, 2034; repurchasable at par December 31, 1999 and every March 31, June 30, September 30, and December 31 thereafter	**750**	–
4.971 ****	Short-term revolving credit facility; final maturity date September 30, 2000	**2,500**	2,700
5.568	Payable December 31, 2002	**200**	200
5.688	Payable August 15, 2007	**400**	400
5.546	Payable August 15, 2007	**150**	150
5.959	Payable November 15, 2027	**400**	400
5.726	Payable November 15, 2027	**100**	100
5.606	Payable November 15, 2027	**300**	300
5.426	Payable May 15, 2008	**200**	200
4.981	Payable May 15, 2008	**200**	200
4.910	Payable May 15, 2008	**200**	200
4.836	Payable November 15, 2027	**100**	–
		6,913	6,413
Mortgage Notes Payable:			
6.00 to 9.25	Maturing from fiscal years 2000 through 2039 secured by land, buildings and equipment with a carrying amount of $31 million.	**4**	8
		6,917	6,421
Less current portion of debt		**3,363**	3,633
		$3,554	$2,788

* All debt is repurchasable at any time at a price determined by then current FFB rates.
** Weighted average interest rate; prior year's weighted average interest rate was 8.761%.
*** Prior year rate was 4.491%.
**** Prior year rate was 4.667%.

6. Retirement Programs

With certain exceptions, employees participate in one of the following three retirement programs based upon the starting date of their employment with the Postal Service. Employee and employer contributions are made to the Civil Service Retirement and Disability Fund (CSRDF), which is administered by the Office of Personnel Management. Employees may also participate in the Thrift Savings Plan, which is a defined contribution retirement savings and investment plan. Postal Service employees are authorized to participate in the Thrift Savings Plan by the Federal Employees Retirement System Act of 1986. The Plan is administered by the Federal Retirement Thrift Investment Board.

Civil Service Retirement System (CSRS)

Under the Postal Reorganization Act, officers and career employees are covered by the Civil Service Retirement System, which provides a basic annuity and Medicare coverage. The CSRS fund covers substantially all employees hired prior to January 1, 1984. Effective January 1, 1999, participating employees contribute 7.25% of their basic pay to the CSRDF. Prior January 1, 1999, participating employees contributed 7% of their basic pay. We contribute an amount equal to 7% of each employee's basic pay to the CSRDF. We and the employee also contribute to Medicare at the rate prescribed by law. We do not match contributions to the Thrift Savings Plan for employees who participate in the CSRS.

Dual Civil Service Retirement System (Dual CSRS)/Social Security System

Employees with prior U.S. government service who were hired between January 1, 1984 and January 1, 1987 are covered by the Dual Civil Service Retirement System/Social Security System. We contribute 7% of the employee's basic pay to the CSRDF. Effective January 1, 1999, participating employees contribute 1.05% of their basic pay. Prior to January 1, 1999, participating employees contributed 0.8% of their basic pay. We and the employee also contribute to Social Security and Medicare at the rates prescribed by law. We do not match contributions to the Thrift Savings Plan for employees who participate in the Dual System.

6. Retirement Programs (continued)

Federal Employees Retirement System (FERS)

Effective January 1, 1987, officers and career employees hired since December 31, 1983, except for those covered by the Dual System, are covered by the Federal Employees Retirement System Act of 1986. In addition, employees hired before January 1, 1984 could choose during certain periods in 1987, 1988 and 1998 to participate in the FERS. This System consists of Social Security, a basic annuity plan, and a Thrift Savings Plan.

We contributed to the basic annuity plan 10.7% of each employee's basic pay in 1999 and 1998 and 11.4% in 1997. Effective January 1, 1999, participating employees contribute 1.05% of their basic pay. Prior to January 1, 1999, participating employees contributed 0.8% of their basic pay. We and the employee also contribute to Social Security and Medicare at the rates prescribed by law. In addition, we are required to contribute to the Thrift Savings Plan a minimum of 1% per year of the basic pay of employees covered by this System. We also match a voluntary employee contribution up to 3% of the employee's basic pay, and 50% of a contribution between 3 and 5% of basic pay.

The number of employees enrolled in each of the retirement plans at the end of 1999, 1998 and 1997 is as follows:

	1999*	**1998**	**1997**
CSRS	**281,062**	298,827	314,068
Dual CSRS/ Social Security	**12,598**	13,418	13,900
FERS	**503,233**	479,069	436,735

* From July 1998 to December 1998 workers covered by CSRS were allowed to switch to FERS. During this period only 3,436, or less than 1.2%, of our employees chose to change plans.

Deferred Retirement Costs

Deferred retirement costs consist of the following (dollars in millions):

	1999	**1998**
CSRS basic pay increases	**$25,545**	$25,827
CSRS retirees' and survivors' cost of living adjustments	**5,952**	6,017
Total	**$31,497**	$31,844

There are no deferred retirement costs associated with FERS.

6. Retirement Programs (continued)

Deferred Retirement Liability—Civil Service Retirement System

When we increase our employees' current basic pay, we are liable for the additional deferred retirement liability. The liability results from the increase in our employees' retirement benefits, which is based on this pay increase. The Office of Personnel Management determines the estimated increase in our deferred liability. We amortize and pay this amount in 30 equal annual installments, which includes interest computed at a rate of 5% per year. We make the first payment at the end of the year in which employees receive their pay increase.

The increase in our deferred liability for retirement benefits under the CSRS as a result of basic pay increases was $930 million in 1999, $836 million in 1998 and $560 million in 1997.

Deferred Retirement Liability—Retirees' and their Survivors' Cost of Living Adjustments (COLAs)

Congress determines the COLAs granted to our retirees. Under the Omnibus Budget Reconciliation Act of 1990, we are liable for our share of the cost of living adjustments granted to those retirees, and their survivors, retiring on or after July 1, 1971. We are not responsible for any costs due to Federal civilian service before that date.

Each year the Office of Personnel Management determines the estimated increase in our liability under this law for the current year. We amortize and pay each year's amount in 15 equal annual installments, which include interest computed at a rate of 5% per year.

The increase in our deferred liability for our retirees' COLAs was $537 million in 1999, $790 million in 1998 and $1,041 million in 1997.

Future Minimum Payments

We estimate the future minimum payments we have to make in order to fund CSRS benefits and retirees cost of living adjustments as of September 30, 1999, are as follows (dollars in millions):

6. Retirement Programs (continued)

Future Minimum Payments (continued)

Year	Amount
2000	$ 3,399
2001	3,381
2002	3,310
2003	3,231
2004	3,110
After 2004	31,331
	$47,762
Less amount representing interest	16,255
Total future minimum payments	$31,507
Less: Portion classified as a current liability in compensation and benefits	1,822
Long-term portion of future minimum payments	$29,685

Expense Components

Listed below are the components of our total retirement expenses that are included in our compensation and benefits expense and related interest expense in the Statement of Operations for 1999, 1998 and 1997 (dollars in millions):

	1999	1998	1997
CSRS	**$ 816**	$ 849	$ 870
FERS	**1,824**	1,640	1,590
FERS—Thrift Savings Plan	**681**	608	552
Dual CSRS/Social Security	**35**	36	36
Social Security	**1,337**	1,241	1,162
Amortization of deferred cost:			
CSRS	**1,214**	1,142	1,064
Annuitant COLAs	**602**	569	552
Interest expense on deferred Liabilities	**1,592**	1,597	1,597
Imputed interest on OBRA '93	–	16	32
Total retirement expense	**$8,101**	$7,698	$7,455

6. Retirement Programs (continued)

Expense Components (continued)

Employer cash contributions to retirement plans were $6,756 million in 1999, $6,647 million in 1998, and $6,481 million in 1997. These amounts do not include Social Security and Medicare contributions.

7. Post-Retirement Health Benefit Programs

Employees of the Postal Service who participate in the Federal Employees Health Benefits Program (FEHBP) for at least the five years immediately before their retirement may participate in the FEHBP during their retirement. Under the FEHBP, we pay a portion of the health insurance premiums of participating retirees and their survivors. This program is administered by the Office of Personnel Management.

The Omnibus Budget Reconciliation Act of 1990 requires us to pay the employer's share of health insurance premiums for all employees, and their survivors, who participate in the FEHBP and who retire on or after July 1, 1971. However, we do not include the costs attributable to Federal civilian service before that date. Our FEHBP costs amounted to $593 million in 1999, $581 million in 1998 and $548 million in 1997. We include these costs in our compensation and benefits expense.

8. Revenue Forgone

Our operating revenue includes accruals for revenue forgone. Revenue is forgone when Congress mandates that we provide free or reduced mail rates for certain mailers. The difference between the price Congress has mandated and the price we would have charged the mailer determines the amount of forgone revenue. Congress appropriates money to reimburse us for only a portion of the revenue forgone that we have incurred in past years. In our operating revenue, we have included as revenue the amounts appropriated by Congress for revenue forgone of $71 million for 1999, $67 million for 1998, and $83 million for 1997. Legislation that was passed during 1999 appropriated the $71 million for 1999 but delayed the payment until fiscal year 2000. Accordingly, we have recorded this as a receivable in 1999.

Under the Revenue Forgone Reform Act of 1993, Congress is required to reimburse us $29 million annually through 2035 (42 years). This reimbursement is for two purposes: services we performed in 1991, 1992 and 1993 for which we have not yet been paid; and

8. Revenue Forgone (continued)

for shortfalls in the reimbursement for the costs we incurred for processing and delivering certain nonprofit mail from 1994 through 1998.

The Revenue Forgone Reform Act of 1993 authorized a total of $1.218 billion in payments. We calculated the present value of these future reimbursements to be approximately $390 million at 7% interest. We recognized the $390 million as revenue during fiscal years 1991 through 1998. The amounts receivable as of September 30, 1999 and 1998 were $378 million and $380 million, respectively. We recognized no revenue in 1999, $10 million in 1998 and $22 million in 1997.

9. Commitments

At September 30, 1999, we estimate our financial commitment for approved Postal Service capital projects in progress to be approximately $3,799 million.

Our total rental expense for the years ended September 30 is summarized as follows (dollars in millions):

	1999	**1998**	**1997**
Non-cancelable real estate leases including related taxes	**$ 766**	$711	$659
Facilities leased from General Services Administration subject to 120-day notice of cancellation	**36**	37	34
Equipment and other short-term rentals	**431**	234	154
Total	**$1,233**	$982	$847

9. Commitments (continued)

At September 30, 1999, our future minimum lease payments for all non-cancelable leases are as follows (dollars in millions):

Year	Operating	Capital
2000	$ 743	$ 68
2001	694	68
2002	644	68
2003	597	68
2004	559	68
After 2004	5,284	439
	$8,521	$779
Less: Interest at 5.5%		202
Total capital lease obligations		577
Less: Short-term portion of capital lease obligations		37
Long-term portion of capital lease Obligations		$540

Most of these leases contain renewal options for periods ranging from 3 to 20 years. Certain non-cancelable real estate leases give us the option to purchase the facilities at prices specified in the leases.

Capital leases included in buildings were $663 million in 1999 and $449 million in 1998. Total accumulated amortization is $122 million in 1999 and $86 million in 1998. Amortization expense for assets recorded under capital leases is included in depreciation expense.

10. Impaired Assets

In 1997, we began to record losses on long-lived assets when events and circumstances indicate that the assets might be impaired. In accordance with FASB Statement No. 121, "Accounting for the Impairment of Long-lived Assets and for Long-lived Assets to Be Disposed Of," we have written down our impaired assets to the lower of cost or fair value. We have identified several properties that qualify due to either obsolescence or earthquake damage. We recorded impairment losses of $12 million in 1999 and $57 million in 1997. These losses are included in other operating expenses in the statements of operations. No material impairments were recorded in 1998.

11. Contingent Liabilities

Each quarter we review litigation pending against us. As a result of this review, we classify and adjust our contingencies for claims that we think it is probable that we will lose and for which we can reasonably estimate the amount of the unfavorable outcome. These claims cover labor, equal employment opportunity, environmental issues, traffic accidents, injuries on postal properties, personal claims and property damages, and suits and claims arising from postal contracts. We also recognize the settlement of claims and lawsuits and revisions of other estimates.

As a part of our continuing evaluation of estimates required in the preparation of our financial statements, we recorded approximately a $104 million increase in liabilities in 1999 to recognize increases in the estimated cost of litigation and claims asserted prior to 1999. We recognized settlement of claims and lawsuits and revised other estimates in our changes in contingent liabilities. Management and General Counsel believe that we have made adequate provision for the amounts that may become due under the suits, claims, and proceedings we have discussed here.

12. Year 2000 Disclosure (Unaudited)

Since our major Year 2000 efforts began, we have operated from the premise that the Year 2000 problem while technical in origin, represents a business problem, not a technology problem. .This problem stems from the practice of using only the last two digits of a year in many computer programs. When the year changes from 1999 to 2000, the two-digit representation "00" may not be recognized by some systems causing errors ranging from simple miscalculation to a complete computer shutdown. Our objective is to limit the impact on our customers, employees, and business.

Our Year 2000 preparation program involves three distinct elements: remediation, business continuity and contingency planning, and recovery management. We completed the remediation, or fixing, of our mission-critical systems, including both mail-processing equipment and business applications.

Since we interact with a wide range of suppliers and business partners, we completed the development of a broad spectrum of continuity plans in case our critical business process is interrupted externally. In addition, our Supplier Management Office has performed in-depth assessments of the ability of our key national and local suppliers to provide us with necessary products and services into 2000. We also completed the development of

12. Year 2000 Disclosure (Unaudited) (continued)

contingency plans or "workarounds" in case any element of our internal critical systems and some non-critical supporting systems fail. For both types of plans, we conducted tests and rehearsals. This included tests of our electronic interfaces with our customers and business partners, as well as the readiness of our safety, security, and other building systems at more than 4,000 of our key facilities.

The final element of our program, recovery management, builds on our extensive experience in moving the mail through such impediments as severe weather conditions and natural disasters. We established and tested a well-defined communication structure to handle any problems that may occur. So far, we have spent $385 million, and the total cost is expected to be between $450 and $500 million for upgrading our systems and preparing for Year 2000 readiness. We believe we will be ready. We also believe that our extensive preparation by thousands of dedicated personnel prepares us for unforeseen Year 2000 problems and limits the consequences to minor effects on administrative or financial systems or limited impacts on our ability to deliver the mail.

Attachment 12

December 1, 1999

Mr. Joel MacCollam
World Emergency Relief
PO Box 1518
Carlsbad, CA 92018-1518

Dear Mr. MacCollam:

This is in reference to the letter you wrote Lee Cassidy, Executive Director of the National Federation of Nonprofits and his subsequent letter to John Rapp, vice president, Delivery. You were concerned about the level of service you were experiencing with some of the charitable mailings you were sending out this year.

Dan Leonard of my staff spoke with you in mid-October regarding the mailings and as a result he was put in contact with Eric of your staff. In two telephone conversations it was agreed that Eric would provide additional information relative to the mailings. To date this information has not been received, which has precluded us from taking immediate corrective action to improve the level of service to you.

If someone from your staff could please provide Dan Leonard with the requested information, we will try to resolve your concerns as quickly as possible. Dan can be reached at USPS Headquarters, Room 7142, 475 L'Enfant Plaza, SW, Washington, DC 20260-2802 or by phone at (202) 268-4656. Thank you very much for your assistance.

Sincerely,

Signed

Michael F. Spates
Manager, Delivery

cc: Lee Cassidy, Executive Director, National Federation of Nonprofits
John Rapp

bcc: MSpates, WBothwell, DLeonard, DPP-SF, D-RF
OS010:Leonard:bgw:2802:DPP-211-99:s/dpp/leonard/D#21199.doc (FOS 99-258)

Attachment 13

Measuring the Cost of Universal Service for Posts

Michael D. Bradley
Department of Economics
George Washington University

Jeff Colvin
United States Postal Service

Presented at the Seventh Conference on Postal and Delivery Economics: Current Directions in Postal Reform

June 23 – 26, 1999
Sintra, Portugal

Measuring the Cost of Universal Service for Posts[1]

Michael D. Bradley
Department of Economics
George Washington University

Jeff Colvin
United States Postal Service

1. INTRODUCTION

The recent introduction of legislation designed to reduce the scope of the postal monopoly, in the United States and elsewhere, has sharpened interest in understanding the cost borne by a postal operator when it serves customers at noncompensatory prices.[2] The measurement of such universal service obligation costs (USO) is directly relevant to the scope of entry restriction. A rationale sometimes employed for granting an exclusive franchise to a postal operator is that such restrictions are necessary to finance the cost of universal service.[3] That is, the postal operator is simultaneously charged with serving all customers, irrespective of cost differentials, and allowed, via the exclusive privilege on letter carriage, to charge certain customers prices above cost to fund the mandated loss-making activities. Since there necessarily exists some vector of prices that eliminates all loss-making mail flows, rendering profitable any flows for which the price is less than the willingness to pay and eliminating the rest, the USO is intimately related to the constraint that postal operators offer services of the same quality at uniform prices, despite cost differences. An additional limit generally placed upon the prices chosen by the postal operator is that the universal services be provided at an "affordable rate."

Most estimates of USO costs[4] for posts have been thus far based on methods derived from the telecommunications industry,[5] methods which

---

[1] The views expressed in this paper are those of the authors and do not necessarily represent those of the United States Postal Service or any other organization. The authors are indebted to Donald Baron for assistance with the calculations.

[2] United States Congress (1997) would open the delivery of letters with postage of $2 or more to competition. European Commission (1998) suggests that significant liberalization of postal markets may take place by 2003.

[3] See European Commission (1992).

[4] See Elsenblast, Pieper and Stumpf (1995) and Castro and Maddock (1997).

[5] See Cave (1995).

several authors have argued are not perfectly suitable for posts.[6] In fact a small but growing body of work has developed that suggests several alternatives to the "net avoided cost" (NAC) methodology, as the telecom procedure has been dubbed.[7]

After a brief review of the literature on the universal service obligation in the postal industry (Section 2), we compare the net avoided cost approach with the entry pricing (EP) approach suggested in Rodriguez, Smith and Storer (1999). Section 4 then addresses essential issues in implementing the entry pricing approach. In Section 5, we present some preliminary estimates of the cost of the United States Postal Service's universal service obligation utilizing the EP approach. Finally, in section 6 we provide an analysis of the cost incurred by the Postal Service in order to maintain a system of retail operations, many of which generate more costs than revenue. As we rely upon very simple assumptions regarding the cost function of potential entrants, our quantitative results are useful primarily as an illustration of how certain methods might be applied to actual data on postal operations. Nevertheless, the results strongly suggest that further research would uncover nontrivial USO costs for the United States Postal Service.

2. METHODS OF MEASURING THE COST OF UNIVERSAL SERVICE

As mentioned above, there are two different approaches that have been suggested for measuring the cost of the USO: the net avoided cost methodology and the entry pricing methodology. The net avoided cost methodology was developed for use in the telecom industry and has been applied to postal operations by Elsenblast, Pieper, and Stumpf (1995), Kowalewski and Muller (1995), and Castro and Maddock (1997). In concept the NAC approach amounts to an incremental cost test applied to each service.[8] The sum of the net losses from those services that fail the test, less the losses from deficit-earning services that are offered for reasons

---

[6] See Crew and Kleindorfer (1997), Dobbs and Golay (1995), Gallet and Toledano (1997), and Rodriguez, Smith and Storer (1999).

[7] Cremer, De Rycke, and Grimaud (1997), Crew and Kleindorfer (1997), Dobbs and Golay (1995), Gallet and Toledano (1997), and Rodriguez, Smith and Storer (1999).

[8] In practice, any application of NAC methodology to actual postal operations would require some aggregation of services.

other than to meet the USO,[9] is referred to as the net avoided cost. The NAC is conceived as the cost that would be avoided if the postal operator were not constrained by the USO.

There as been substantial criticism of the NAC approach as applied to posts.[10] Of particular interest is the line of argument beginning with the criticism of the NAC method found in Gallet and Tolledano (1997). Their central argument is that the NAC cost will not equal the cost of the USO once competition is present for some (or all) surplus services. That is, one should not begin with an avoided cost calculated for a monopolist and then apply it to a postal service operating in a (partially or fully) liberalized market. This is because in a liberalized market, the most profitable services will be (partly or wholly) cream-skimmed away. The resulting loss of market share for the incumbent will raise the cost of the USO as the incumbent loses its scope and scale advantages. Gallet and Tolledano (1997) find that the NAC method is inappropriate when it is applied to the problem of determining whether (and to what extent) services should be protected from competition. The argument of Gallet and Tolledano (1997) is taken up by Rodriguez, Smith and Storer (1999), who develop the logic into a method for assessing the cost of the USO. Under their "entry pricing" (EP) approach, RS&S (1999) investigate the impact of liberalization on the cost of the USO, given that the postal operator remains constrained to serve all customers at uniform prices. The EP method calculates the lost contribution due to such liberalization. Key to the approach are the prices at which entrants would be willing to serve the market.

In order to understand the EP method, it is necessary to realize that the function of entry restrictions is to finance loss-making activities through above market prices on other activities. If the protection is removed, then all prices fall to those at which entry occurs. The contribution that is lost as a result is equal to the subsidy required to fund the loss-making activities.

Under this view, it is the obligation to provide similar services at uniform prices that causes the operator to incur its net losses on certain activities as well as a portion of institutional cost. Prior to liberalization, the operator was unable to set a differentiated price for high cost customers, but he was able to extract rents from low cost customers to finance losses on high cost services. Entry removes this source of financing, leaving the operator with the stand alone cost of high cost services, which consists of the direct cost plus the institutional cost that remains after the surplus earning activities are no longer performed by the incumbent. This is

---

[9] It has been frequently noted that some price averaging would occur even for a unregulated operator. See, for example, Elsenbast and Stumpf (1995).

[10] See Crew and Kleindorfer (1998) and Dobbs and Golay (1995).

precisely the cost of universal service, as measured in the EP methodology. Said otherwise, the cost of the USO includes the contribution to institutional cost the operator would earn if it were not constrained to serve all customers at the same price. The net avoided cost measure, by contrast, ignores the institutional cost that the USO causes an operator to incur.[11]

3. COMPARING THE NAC AND EP METHODS

In this section, we construct an economic model that permits explicit comparison of the net avoided costs and entry pricing methods. In any method of calculating the cost of universal service, the basic issue is that the postal administration must perform actions for which the compensation does not cover the costs. Analysis of a postal USO typically focuses on delivery and reflects the operating reality that universal delivery is required for all or virtually all products at a uniform price.[12] This approach, however, need not preclude the postal operator from offering differential products or differential prices, as upstream activities such as sorting or delivery need not be at a uniform price. For example, a postal administration could provide presort discounts in mail processing or zoned rates for transportation and still face a universal service cost in delivery.

While it is not required for the existence of a cost of universal service, a uniform price has generally been part of USO analysis in the postal context. A postal administration can face a universal service cost even without the additional requirement of a uniform price for certain products. However, because postal administrations generally do face this additional constraint we embody it in our economic model. We impose this restriction only on the USO or "monopoly" product, not on competitive products. When a uniform price is not required on the competitive product, then the postal administration does not face erosion of this product's volume from liberalization.[13]

We thus build a model with two products, a "monopoly" product that has a uniform price and a competitive product that can be priced

[11] In one sense, this may be unfair. In some versions of the NAC approach, fixed and common costs are ignored only in the very first approximation. See Elsenbast and Stumpf (1995). In further rounds, costs that are common to the NAC routes are added to the estimate of the USO cost. However, this refinement adds significantly to the difficulty in applying the NAC methodology.

[12] See Cremer, Grimaud and Laffont (1999).

[13] It is possible, although unlikely, that the cost of delivery is so high in some areas that no delivery service would be purchased at a profit-making price.

differentially. A postal operator typically serves some areas which are "high cost" delivery areas and some areas which are "low cost" delivery areas. By this, we mean that there are some areas for which the total revenue generated by the mail delivered in that area is not sufficient to cover the total cost of delivering the mail to that area, including upstream processing and delivery costs. Accordingly, our model has two areas or groups of delivery routes, a high cost area for which product revenue is less than cost and a low cost area with the opposite condition. Finally, to expedite the analysis we assume that upstream costs are linear but different for the two different products. Upstream costs do have material fixed costs and thus experience increasing returns to scale.

We use the following notation. We can now describe the cost structure of the postal operator.

Delivery cost for the high cost area:

$$C_i^D = F_i + a_1 V_{Mi} + a_2 V_{Ci} - a_3 V_{Mi} V_{Ci}$$

Delivery cost for the low cost area:

$$C_j^D = F_j + b_1 V_{mj} + b_2 V_{Cj} - b_3 V_{Mj} V_{Cj}$$

Upstream cost:

$$C^U = F + d_1 (V_{Mi} + V_{Mj}) + d_2 (V_{Cj} + V_{Ci})$$

Where:

V_{Mi} is the volume of the monopoly product in high cost area,
V_{Mj} is the volume of the monopoly product in low cost area,
Vc_i is the volume of the competitive product in high cost area,
Vc_j is the volume of the competitive product in low cost areas,
F_j is low-cost area specific fixed delivery cost,
F_i is high-cost area specific fixed delivery cost, and
F is upstream common fixed cost.

Because the competitive product is not subject to a uniform rate requirement, there are two competitive prices, one for each area, P_{Ci} and P_{Cj}.

There is only one monopoly price, P_M. The postal administration operates under a breakeven constraint:

$$
\begin{aligned}
P_M\left(V_{Mj} + V_{Mi}\right) + P_{Cj}V_{Cj} + P_{Ci}V_{Ci} \quad = \\
& F_i + a_1 V_{Mi} + a_2 V_{Ci} - a_3 V_{Mi}V_{Ci} \\
& + F_j + b_1 V_{Mj} + b_2 V_{Cj} - b_3 V_{Mj}V_{Cj} \\
& + F + d_1 (V_{Mj} + V_{Mi}) + d_2 (V_{Cj} + V_{Ci})
\end{aligned}
$$

Given this cost structure, we can calculate the contributions from each of the products. The contributions will be given by the difference between the product's revenue and its incremental cost. For the monopoly product, the contribution is:

$$
\begin{aligned}
\lambda_M \quad = \quad & P_M\left(V_{Mj} + V_{Mi}\right) - (a_1 V_{Mi} - a_3 V_{Mi}V_{Ci}) \\
& - (b_1 V_{Mj} - b_3 V_{Mj}V_{Cj}) - d_1 (V_{Mj} + V_{Mi})
\end{aligned}
$$

The contribution from the competitive product can be decomposed into the contributions from the two areas. The competitive product's contribution from the high cost area is given by:

$$
\lambda_{Ci} \quad = \quad \left[P_{Ci} \quad - (a_2 - a_3 V_{Mi}) - d_2\right] V_{Cj}
$$

The competitive product's contribution from the low cost area is given by:[14]

[14] The calculation of the cost of the universal service obligation is made more complicated by the existence of scope economies. In particular, when a postal operator benefits from

$$\lambda_{Cj} = \left[P_{Cj} - (b_2 - b_3 V_{Mi}) - d_2\right] V_{Cj}$$

We can now use this framework to investigate the two different, but related, approaches to calculating the cost of universal service for the delivery activity. The net avoided cost measure attempts to measure the cost of universal service under the assumption that the current regulatory regime will persist. This approach operates under the premise that the postal operator will continue to benefit from restrictions on entry into the market for the monopoly product. Even with this protection, there will be areas of the country for which the revenues generated are insufficient to cover costs. The difference between the revenues earned and these costs is called the net avoided cost of universal service. In our model, this USO cost is captured by the difference between the revenues earned on high cost routes and the incremental cost of serving those routes:

$$\begin{aligned} COUS^{NAC} = \; & F_i + a_1 V_{Mi} + a_2 V_{Ci} - a_3 V_{Mi} V_{Ci} \\ & + d_1 V_{Mi} + d_2 V_{Ci} - P_M V_{Mi} - P_{Ci} V_{Ci} \end{aligned}$$

Note that because we are looking at the universal service cost of an activity, the calculation of cost does not focus solely on the volume of the monopoly product. The postal operator is earning loses, in the current regulatory environment, on all mail delivered to the high cost areas and it could increase its profits by simply ceasing to provide service to this part of the country.

The alternative approach to measuring the cost of universal service examines that cost in a liberalized environment. The entry pricing approach looks at the costs incurred by the postal operator when the monopoly restrictions are lifted and entry in profitable areas of the country is allowed. In its simplest form, the entry pricing approach assumes that competitors will replace the monopolist's volume in the low cost region. When this happens, the postal operator is left providing service for the former monopoly product only in the high cost areas. The postal operator thus loses the revenue and contribution from the former monopoly product on low cost routes. The formula for the entry price cost of universal service is given by:

---

scope economies, one cannot simply add up the contributions from the individual products and set them equal to total fixed cost. By using the breakeven constraint, one can show that the sum of the contributions must exceed total fixed cost.

$$COUS^{EP} = P_M V_{Mj} + P_{Cj} V_{Cj} - F_j - b_1 V_{Mj} - b_2 V_{Cj} + b_3 V_{Mj} V_{Cj} - d_1 V_{Mj} - d_2 V_{Cj}$$

As with the net avoided cost approach, the entry pricing approach for the delivery activity includes all surpluses made on the low cost routes, regardless of the products delivered. The assumption being made here is that the competitors are replacing the postal operator in the delivery of all the mail to the low cost area.[15] There are several issues here that merit discussion. First, the postal operator may only lose the monopoly product on the low cost routes, not the competitive product. After all, the competitive product already facing competition and liberalization should not affect that product's competitive stance. (This is not strictly true because loss of the monopoly product will imply a loss of economies of scope and an increase in the unit cost of the competitive product.)

Second, if the postal operator has a cost advantage in upstream operations like mail processing, then it is possible to consider a situation in which competitors replace the delivery function only. The postal operator would be responsible for collecting, processing, and transporting the mail to the competitor's delivery station but would not provide delivery. This is simply the inverse to the United States Postal Service's current drop ship presort discounts. In this circumstance, the upstream costs would have to be removed from the cost of universal service and the price of the products delivered in low cost area would have to be modified to reflect only the marked up upstream costs.

Third, we can investigate the meaning of the entry pricing measure of the cost of universal service. The entry pricing universal service cost for the delivery activity is equal to the difference between product revenue and stand-alone cost for the high-cost delivery area. If one combines the break-even constraint and the expression for the entry pricing cost of universal service, one can derive a useful expression:

[15] If the incumbent's cost is so far below the potential entrant's cost that no entry will occur, then the incumbent will not lose revenue on the low cost route. In this case the EP cost of use will degenerate to the NAC cost.

$$COUS^{EP} = P_M V_{Mi} + P_{Ci} V_{Ci} - F_i - a_1 V_{Mi} - a_2 V_{Ci} + a_3 V_{Mi} V_{Ci} - d_1 V_{Mi} - d_2 V_{Ci} + F$$

This expression is just the difference between the revenue earned on mail delivered on high cost routes and the stand-alone cost of handling that mail.[16] Comparing the expressions for the entry pricing and net avoided cost measures of the cost of universal service, yields the result that, under the breakeven constraint, the entry measure is simply the net avoided cost measure plus fixed costs.

4. ISSUES IN IMPLEMENTING THE ENTRY PRICING APPROACH

As discussed above, the entry pricing approach focuses on measuring the lost contribution from allowing entrants to capture profitable services. To implement the entry pricing approach, it is important to be able to identify which of the postal operator's routes are susceptible to entry and which are not. This identification permits estimation of the lost net revenue from all such routes. To facilitate the identification, we consider the three key variables that will determine if entry will take place:

Define R_i as the revenue generated by route i.

Define C_{mi} as the incremental cost of the route. (This includes the delivery cost and the upstream costs per piece.)

Define C_{ei} as the cost to the entrant from serving the route. If the entrant is providing no other services C_e would be the stand alone cost (SAC) for the entrant. If the entrant is providing other services, then C_e would be the incremental cost for the entrant.

The relationship among these variables across the delivery network determines where entry will occur and ultimately the cost of universal service. To organize the set of all possible conditions on routes, we must relate these three variables in a comprehensive way. Our organizing structure will focus on the relationship between the incumbent's cost and the entrant's costs. There are obviously three possibilities; the incumbent's cost is greater, lesser, or equal to the entrant's cost. Entry will occur when an entrant can price below the incumbent but still make a profit on the route. This requires the entrant's cost to be less then revenue generated by the route. Generally this will mean that the incumbent's costs are also less then the revenue generated on the route, although if the entrant's costs are

[16] We note that this result is general and does not require the existence of economies of scope as we model them. Economies of scope emanating from common fixed cost are sufficient to ensure this result. Nevertheless, we believe the operational scope economies are an important part of the cost structure of delivery and will be embedded in our empirical measures. Thus, we include them in our analytical structure.

below the incumbent's cost, entry is possible even if the revenue generated is less than the incumbent's costs. We can define the set of relationships between C_m, C_e and R as follows. In each case we can determine if entry will occur:

Case I: Routes for which $C_{mi} = C_{ei}$

a) If $R_i > C_{mi}$ then entry will occur and the incumbent will lose contribution.
b) If $R_i < C_{mi}$ or $R_i = C_{mi}$, then entry not will occur.

Case II: Routes for which $C_{mi} < C_{ei}$

a) If $R_i > Cmi$ and $Ri > C_{ei}$ then entry will occur and the incumbent will lose contribution.
b) If $R_i > C_{mi}$ and $R_i < C_{ei}$ then entry will not occur.
c) If $R_i < C_{mi}$ or $R_i = C_{mi}$, then entry will not occur.

Case III: Routes for which $Cmi > C_{ei}$

a) If $R_i > C_{mi}$ then entry will occur and the incumbent will lose contribution.
b) If $R_i = C_{mi}$ then entry will occur but no contribution will be lost.
c) If $R_i < C_{mi}$ and $Ri > C_{ei}$ then entry will occur and the incumbent will reduce its loss.
d) If $R_i < C_{mi}$ and $R_i < C_{ei}$ then entry will not occur.

This set of conditions can be presented in tabular form as:

Various Conditions of Competition on Routes			
	$R > C_m$	$R = C_m$	$R < C_m$
$C_m > C_e$	Entry	Entry	Entry if $R > C_e$
			No Entry if $R < C_e$
$C_m = C_e$	Entry	No Entry	No Entry
$C_m < C_e$	Entry if $R > C_e$	No Entry	No Entry
	No Entry if $R < C_e$		

When the above structure is applied to all modes of delivery, certain adding up restrictions can be applied. If we calculate the difference between total revenue and total cost for the routes in each of the above cells, we can calculate the net contribution to defraying fixed costs and, ultimately profit. For a break-even operator, the sum of the net revenues from all of the cells will equal the operator's institutional cost.

With this in mind, we can begin to operationalize the entry pricing definition of cost of universal service. Under this approach, one calculates the change in net contribution associated with permitting entry. Formally, RS&S (1999) argue that one can measure USO as the change in net revenue on those routes on which entry occurs:

$$USO^{EP} = \left(\sum_{i}^{n} \left[(\hat{R}_{mi}) - (\bar{R}_{mi}) \right] \right) - \left(C_m(\hat{Q}) - C_m(\bar{Q}) \right)$$

where n is the number of routes on which entry occurs.

In this expression, the "hat" notation identifies revenues and costs for the monopoly before entry occurs and the "bar" notation identifies similar quantities for the monopoly after entry.

This equation shows that RS&S (1999) have a dynamic measurement of the cost of universal service in mind. Their framework allows for the partial loss of volume on a route, the migration of volume from one route to another, changes in unit costs associated with changes in volumes on the routes, as well as the iterative effect of entry on output through increases in the break-even uniform price and the demand response. Although this dynamic approach is desirable, it is quite difficult to implement because it

requires detailed knowledge of how volumes will migrate on routes, of how the incumbent's unit costs will vary with changes in volume and of how the entrant's cost structure will be influenced by different volume migrations. Because of the informational difficulties associated with this analysis, we begin our research with a static version of entry pricing. To facilitate calculation we make two simplifying assumptions. First, we assume that when entry occurs, it is complete. A route is either served by the incumbent or by the entrant but not both. This simplifies the analysis by eliminating the need to determine the amount of mail that migrates from the incumbent to the entrant on any given route. Our second assumption is that the incumbent's cost on the remaining routes is not affected by the loss of volume on any one given route. This assumption is made solely for computational ease.

Because of this last factor, the static approach to entry pricing that we follow in this paper is likely to understate the actual cost of universal service. Nevertheless, it is of value to calculate because it is the first step beyond the restrictive net avoided cost approach and begins to look at the cost of universal service in a way that takes into account potential entry of competitors. It is thus closer to answering the question of what is the universal service obligation in a competitive environment.

The entry pricing approach to measuring the cost of universal service is based on analyzing those costs under a potentially competitive situation. By its very nature, the entry pricing approach seeks to answer the question of how much universal service would cost in an environment in which competition was allowed on profitable routes. This is to be contrasted with the Net Avoided Cost approach, which does not permit competition in those routes and thus measures the cost of universal service from a non-competitive perspective.

The entry price approach attempts to measure how much it would cost to serve the set of USO routes (whose costs are greater than their revenue at the uniform price) when competitive firms can and will service the profitable routes. If competitive firms are able to under-price the incumbent on profit making routes, two things will happen. First, the incumbent will lose the revenues on those routes and, second, the incumbent's cost will decline. Because of scale and scope economies, however, the incumbent's cost will fall by more than the direct costs of the routes. The incumbent's total cost will decline, as a result, by the incremental cost of serving the set of profitable routes. Consequently, the costs that remain are the standalone costs of the USO routes. By definition, the revenues on this set of routes are less than the total cost of serving those routes and a subsidy is required if the postal operator is to break-even. That

subsidy is the difference between the revenue lost when the profitable routes went to competitors and the incremental cost of those routes. That subsidy is also the cost of universal service for a break even postal operator who has lost its profitable routes to competitors. This measure of the cost of universal service can be contrasted with the net avoided cost approach. Under NAC, the monopolist's retains the profitable routes and their contribution and simply stops serving the USO routes. When this set of routes is no longer served both the revenue from the routes and the incremental cost of serving them disappears. The resulting gain in profit to the postal operator, or to customers under the break-even constraint, can be then be thought of as the cost of the previously enforced universal service obligation. Obviously, this measure of the cost of universal service, which permits the monopoly to keep its protection, will be different from one calculated for the case in which the postal operator faces competition. It is the entry pricing approach that was designed for this latter case.

We can use our descriptive structure of routes to understand more fully the relationship between the net avoided cost approach and the entry pricing approach. Under the net avoided cost approach, the cost of universal service determined from the set of routes on which the postal operator does not earn sufficient revenue to cover its incremental costs of serving the route. Based upon the categorization listed above that would include routes in categories I.b, II.c, III.c, and III.d.

It can be presented as the highlighted areas in the following table:

Universal Service Obligation as Measured by Net Avoided Cost			
	$R > C_m$	$R = C_m$	$R < C_m$
$C_m > C_e$	Entry	Entry	***Entry if $R > C_e$***
			No Entry if $R < C_e$
$C_m = C_e$	Entry	No Entry	***No Entry***
$C_m < C_e$	Entry if $R > C_e$	No Entry	***No Entry***
	No Entry if $R < C_e$		

The cost of universal service from the entry pricing approach can also be identified in our descriptive structure. Under that approach the cost of universal service is the net contribution lost when entry is permitted. Entry would occur for routes I.a, II.a, III.a, III.b. These routes are presented as the highlighted areas in the following table. Note that in the case that $R < C_m$, but $C_m > C_e$, entry actually saves the existing operator lost revenue because the lower cost entrant can service the "USO" route at a positive profit and thus relieves the operator of the burden.

Universal Service Obligation as Measured by Entry Pricing Approach			
	$R > C_m$	$R = C_m$	$R < C_m$
$C_m > C_e$	***Entry***	Entry	*Entry if $R > C_e$* No Entry if $R < C_e$
$C_m = C_e$	***Entry***	No Entry	No Entry
$C_m < C_e$	***Entry if $R > C_e$*** No Entry if $R < C_e$	No Entry	No Entry

There is a relationship between the NAC and the EP approach for a break-even operator. If our table covers all modes of delivery, then the revenue of all cells in the table must exceed the total cost of providing the volume and must approximately equal the institutional costs of the operator. Putting aside the unlikely case of entry taking place on a route on which the incumbent's revenue is less than its incremental cost, there is a rough correspondence between the entry pricing measure of the cost of universal service and the first column of the table and the net avoided cost measure and the last column. In essence, the entry pricing approach embodies the net avoided cost approach but goes beyond it in considering the existence of institutional costs and the effects of entry. This latter characteristic of the entry pricing approach was illustrated analytically in Section III by examining its relationship to the net avoided cost approach.

An exception to the correspondence described above occurs when the incumbent's costs are well below an entrant's cost. In this circumstance, the incumbent maybe able to earn net revenues on all low cost routes without attracting entry. If this occurs, the entry pricing measure for the cost of universal service will degenerate to the NAC cost and this will be less than the sum of the net avoided costs and institutional costs. This comparison also makes clear a fundamental weakness of the net avoided costs. It does not account for the fact that a postal operator must make sufficient revenue to cover its institutional costs.

5. EMPIRICAL IMPLEMENTATION

In this section we apply the EP methodology to 1995 U.S. Postal Service cost data. We note again that this is a first step, as we are employing a static approximation to the dynamic entry price approach. The procedure that we follow is described in this section. First, we identify a

sample of rural carrier routes and city carrier routes for the U.S. Postal Service.[17] The Postal Service collects information on the sample of routes as part of its responsibilities in responding to regulatory oversight. Once the routes in the sample are selected, the next step is to find the actual delivery cost on each of the sample routes. But delivery costs are only part of the costs of handling the mail that is delivered on the route and we must take into account any other costs that were incurred. With this addition, the definition of a "route" becomes more difficult. The entry pricing approach requires identification of "routes" that contribute surplus and are potential sources of entry. While perhaps straightforward in concept, this is not easy in practice. Most generally, routes are aggregates of origin-destination pairs utilizing the full set of postal activities: induction, transportation, processing, and delivery. The direct estimation of costs for disaggregated services or mail flows is unworkable for a postal service with tens of millions of delivery points. As some level of aggregation is necessary, we make two such aggregations. The first aggregation is across products. That is, we consider a route to be the delivery of all classes of mail from origin to destination. The second aggregation is to assume a diffuse origin for each destination. We cannot trace the origin of each piece of mail that is delivered on a particular route, so we assume that each piece of mail is equally distant from the carrier's route. In other words, we construct standard costs for the induction, transportation and mail processing costs per piece at a detailed product level. Using these standard costs, we construct the "upstream" cost of handling and transporting the mail delivered on each route. We combine this upstream cost with the route's actual delivery costs and then calculate the total incremental cost for the route.

Under the entry pricing approach, this cost must be compared with the revenue generated by the volume delivered on the route to determine where entry will occur. The Postal Service's data systems permit identification of the volumes of each type of mail product on the route at detailed level. That is, one can obtain information on the number of pieces delivered on a route that are First Class letter sized or Standard A flats. We then use these detailed volumes to calculate the revenue generated by each route. This calculation is done by multiplying the revenue per piece for each product/shape category by the volumes of the product shape category in the route.

We have now calculated the total revenue generated by the volume on each route and the total incremental cost (both delivery and upstream) of providing service on the route. By comparing the two quantities for each

---

[17] The sample consists of 231 city carrier routes (out of 139,000) and 4,686 rural carrier routes (out of 54,379). Revenues, volumes, and costs are from 1995.

route, we can determine where entry will occur and thus construct the entry pricing measure of the cost of universal service. Before those calculations can be made, however, one final issue must be addressed. With the information that we currently have available, it is not clear on which routes entry will take place. We currently do not have data on the entrant's costs and so it is impossible for us to predict on which of the incumbent's surplus routes entry will take place. We do know, however, that entry will occur when revenue exceeds the entrant's costs. We also know when revenue exceeds the Postal Service's costs. Thus to calculate measure of the cost of universal service with the entry pricing method, we must make an assumption of how the entrant's cost relate to the Postal Service's cost.

If one believes that the Postal Service does not benefit from any scale and scope economies, then it is easy to believe that the entrant's cost would equal the Postal Services cost on any route. Under this assumption, we can calculate the cost of universal service with the entry pricing method by simply identifying all routes for which revenue exceeds the Postal Service's incremental cost. If the entrant's cost is equal to the Postal Service cost, then entry should occur on all of these routes. In contrast, if one believes that the Postal Service does benefit from scale and scope economies then one would expect the entrant's cost to be above the Postal Service cost. We do not have a measure of how much higher the entrants cost would be, so we perform a sensitivity analysis by assuming that the entrant's costs are 5 percent, 10 percent and 20 percent above the Postal Service's cost.[18]

The calculated cost of the universal service obligation under the entry pricing method is presented in the following table for the four scenarios discussed above. The values range from a high of nearly $ 10 billion to a low (under 20% higher entrant costs) of $4.5 billion.

---

[18] The theoretical cost concept applicable to the estimation of the cost of universal service is the incremental cost of the set of profitable routes. We do a good job of approximating the incremental delivery costs of those routes, but our approximation of upstream incremental costs is less precise. Recall that our calculation method makes use of standard costs for upstream operations. That means we are assuming that the unit costs are constant with respect to changes in volume and that assumption is inconsistent with the existence of scale and scope economies in upstream operations. In future work, we will attempt to account for this characteristic of postal operations and our current estimates of the cost of the universal service obligation must be interpreted with this assumption in mind. To the extent that the incremental cost of the set of profitable routes is higher in future calculations, the resulting estimated cost of universal service will fall.

THE ENTRY PRICING APPROACH TO MEASURING THE COST OF THE UNIVERSAL SERVICE OBLIGATION *All costs expressed in thousands of 1995 dollars*	
Cost of Universal Service on City Carrier Routes: Entrant Costs equal USPS costs.	$ 7,087,098
Cost of Universal Service on Rural Carrier Routes: Entrant Costs equal USPS costs.	$ 2,727,625
Cost of Universal Service on All Carrier Routes: Entrant Costs equal USPS costs.	$ 9,814,722
Cost of Universal Service on City Carrier Routes: Entrant Costs are 5% greater than USPS costs.	$ 5,953,278
Cost of Universal Service on Rural Carrier Routes: Entrant Costs are 5% greater than USPS costs.	$ 2,375,258
Cost of Universal Service on All Carrier Routes: Entrant Costs are 5% greater than USPS costs.	$ 8,328,536
Cost of Universal Service on City Carrier Routes: Entrant Costs are 10% greater than USPS costs.	$ 4,891,486
Cost of Universal Service on Rural Carrier Routes: Entrant Costs are 10% greater than USPS costs.	$ 2,037,807
Cost of Universal Service on All Carrier Routes: Entrant Costs are 10% greater than USPS costs.	$ 6,929,293
Cost of Universal Service on City Carrier Routes: Entrant Costs are 20% greater than USPS costs.	$ 3,138,817
Cost of Universal Service on Rural Carrier Routes: Entrant Costs are 20% greater than USPS costs.	$ 1,423,479
Cost of Universal Service on All Carrier Routes: Entrant Costs are 20% greater than USPS costs.	$ 4,562,296

6. POST OFFICES

The Postal Service maintains over 28,000 post offices. It has often been suggested that some of them earn revenues less than the expenses they incur. [19] As the losses from such operations, where they exist, are logically part of the cost of the USO, we have made a preliminary attempt to calculate them. To do this, we have tallied the revenues from 25,000 post offices in Accounting Period 9 of Fiscal Year 1999. The total revenue taken in by a post office, however, is far in excess of the revenue it has

[19] US Comptroller General (1975).

'earned.' One would not argue, for instance, that an individual post office should be credited with 33 cents for every letter that is taken in over the window. This is because a huge proportion of the costs of the provision of the service for which the 33 cents is paid (delivery, transportation, sorting, etc) is incurred in other offices. The revenue 'earned' is more akin to a sales commission.

Therefore, we discounted the total revenue taken in by each activity at each post office by factors designed to allocate the appropriate amount of revenue to each office/activity. The factors, which come from an internal Postal Service study, are based on the proportion of national total cost made up by each of the revenue gathering activity expenses.

We calculated the cost of each post office as the sum of the window clerk salaries, plus a mark up to account for supervisory labor, equipment, rent, building depreciation, etc. In cases where no window clerks were employed, which would be smaller post offices run by the postmaster him/herself, we included the postmaster's salary as part of the cost.

We examined 27,166 post offices. Of these, 4245 earned positive contributions and 22,920 made losses (one broke even). The sum of losses from post office operations (costs less earned revenue) for Accounting Period 9 of FY99 was $97,692,000. To the extent that AP 9 (April 24 through May 21) is representative of the entire year, the estimate of the cost of this part of the universal service obligation is $1.27 billion.

7. CONCLUSION

This paper has examined several methods of calculating the USO cost for posts. We have argued, as have others, that the NAC method is less useful for measuring the cost of the universal service obligation, to the extent that the point of the measurement is to help decide the size of the reserved sector. We have argued that the entry pricing approach, developed by RS&S (1999) provides a potentially better measure, and we have presented a preliminary implementation of the method. The results indicate that the EP approach may be usefully applied to postal operations and that the cost of the universal service obligation of the U.S. Postal Service, as measured by this approach, is significant. The EP method implies that the USO cost falls as the presence of scale and scope economies in the operator's cost function cause the entry price to rise relative to the incumbent's cost; since the Postal Service has significant

scale and scope economies,[20] it is likely that the true USO cost is less than $10 billion. Further research involves, (1) obtaining cost and volume data on a large sample of routes, (2) gaining information on the cost structure of potential entrants in order to understand more precisely the impact of any given liberalization scenario, and (3) investigating the impact of entry on the incumbent's unit costs. Finally, we have offered a preliminary estimate of the cost of maintaining loss-making post offices. This significant figure constitutes another part of the overall cost of the universal service obligation.

REFERENCES

Allen, R. 1997. "Competitor Access to the Postal Pipeline: The New Zealand Experience." In *Managing Change in the Postal and Delivery Industries,* edited by M.A. Crew and P.R. Kleindorfer. Boston: Kluwer Academic Publishers.

Bradley, M., and Colvin, J. 1995. "An Econometric Model of Postal Delivery." In *Commercialization of Postal and Delivery Services: National and International Perspectives*, edited by M.A.Crew and P.R. Kleindorfer. Boston: Kluwer Academic Publishers.

Castro, M. and Maddock, R. 1997. "The Universal Service Obligation for Post: Some Australian Calculations." In *Managing Change in the Postal and Delivery Industries,* edited by M.A.Crew and P.R. Kleindorfer. Boston: Kluwer Academic Publishers.

Cave, M. 1995. "Meeting Universal Service Obligations in Competitive Telecommunications Markets: Lessons for the Postal Sector." In *Cost of Universal Service,* edited by U. Stumpf and W. Elsenblast. Papers presented at the 3rd Konigswater Seminar, WIK Proceedings.

Christensen, D., Christensen, L., Guy, C, and O'Hara, D. 1993. "U.S. Postal Service Productivity: Measurement and Performance." In *Regulation and the Nature of Postal and Delivery Services*, edited by M. A. Crew and P. R. Kleindorfer. Boston: Kluwer Academic Publishers.

Cremer, H., De Rycke, M and Grimaud, A. 1997. "Costs and Benefits of Universal Service Obligations in the Postal Sector." In *Managing Change in the Postal and Delivery Industries,* edited by M.A. Crew and P.R. Kleindorfer. Boston: Kluwer Academic Publishers.

Cremer, H., Grimaud, A., Laffont, J-J. 1999. "The Cost of Universal Service in the Postal Sector." Paper presented at the IDEI Conference on Competition and Universal Service in the Postal Sector. University of Toulouse. March.

Crew, M.A., and Kleindorfer, P.R. 1998. "Efficient Entry, Monopoly and the Universal Service Obligation in Postal Service." *Journal of Regulatory Economics.*

Dobbs, I. And Golay, J. 1995. "Universal Service Obligation and Reserved Sector." In *Cost of Universal Service,* edited by U. Stumpf and W. Elsenblast. Papers presented at the 3rd Konigswater Seminar, WIK Proceedings.

Elsenblast, W., Pieper, M. and Stumpf, U. 1995. "Estimating the Universal Service Burden of Public Operators." *WIK Discussion Paper* No. 150.

---

[20] See Bradley and Colvin (1995) and Panzar (1991).

Elsenblast, W., and Stumpf, U. 1995. "The Cost of Universal Service Obligations in a Competitive Environment." Papers presented at the 3rd Konigswinter Seminar. Wissenschaftliches Institut fur Kommunikationsdienste.

Gallet, C. and Tolledano, J. 1997. "The Cost of the Universal Postal Service in a Competitive Environment: Lessons from Telecommunications." In *Managing Change in the Postal and Delivery Industries,* edited by M..A.Crew and P.R. Kleindorfer. Boston: Kluwer Academic Publishers.

Federal Communications Commission. 1996. Recommended Decision In the Matter of Federal-State Joint Board on Universal Service. CC Docket No. 96-45.

Kowalewski and Muller. 1995. "The Cost of Universal Service Obligation - the German Perspective." In *Cost of Universal Service,* edited by U. Stumpf and W. Elsenblast. Papers presented at the 3rd Konigswater Seminar, WIK Proceedings, 1995.

European Commission. 1998. Green Paper on the Development of the Single Market for Postal Services. Brussels.

European Commission. 1998. "Directive No 97/67/EC of the European Parliament and of the Council on common rules for the development of the internal market of Community postal services and the improvement of quality of service." *Official Journal of the European Communities*, 12/01/98, No L 15/14.

Panzar, J. 1991. "Is Postal Service a Natural Monopoly?" in *Competition and Innovation in Postal Services*, edited by M.A. Crew and P.R. Kleindorfer. Boston: Kluwer Academic Publishers.

Panzar, J. 1999. "A Methodology for Measuring the Costs of Universal Service Obligations." *Mimeo.*

Rodriguez, F., Smith, S., Storer, D. 1999. "Estimating the Cost of the Universal Service Obligation in Posts." In *.Emerging Competition in Postal and Delivery Serivces* edited by M.A. Crew and P.R. Kleindorfer. Boston: Kluwer Academic Publishers.

Stumpf, U. 1997. "Providing Universal Service in Competitive Postal Markets." In *Managing Change in the Postal and Delivery Industries*, edited by M.A. Crew and P.R. Kleindorfer. Boston: Kluwer Academic Publishers.

United States Comptroller General. 1975. Report to the Congress by the Comptroller General of the United States, "100 Million Could Be Saved Annually in Postal Operations in Rural America Without Affecting the Quality of Service." GCD-75-87.

United States House of Representatives. 1997. House Bill H.R. 22.

Attachment 14

POSTAL BULLETIN

PUBLISHED SINCE MARCH 4, 1880

PB 21998, May 20, 1999

ALL POST OFFICES

PS Form 8165, Mail Fraud Report, Recently Revised

The U.S. Postal Inspection Service recently revised PS Form 8165, *Mail Fraud Report* (see pages 3–5), formerly named the *Mail Fraud Complaint Questionnaire*, for the public to report suspected mail fraud committed using the U.S. Mail. Though the Inspection Service cannot guarantee recovery of money lost to fraud, the information the public provides on PS Form 8165 will help postal inspectors identify new fraud schemes and enforce civil and administrative remedies. These remedies are available to the Postal Service to shut down fraudulent operations and prevent additional victimization. The revised form is now in the material distribution center (MDC) and can be ordered through normal requisition procedures or obtained by sending an e-mail to *fraud@uspis.gov*.

Alert Your Employees to Provide PS Form 8165 to Customers

Please do the following:

1. Provide PS Form 8165 to customers for reporting suspected mail fraud whether or not they have lost money.
2. Understand the possible mail fraud schemes customers may report. These may include but are not limited to the following:
   - Money lost in transactions involving the use of the mail.
   - Concerns about companies or individuals sending mail offers such as:
     - Chain letters.
     - Lotteries.
     - Nigerian scams.
     - Travel offers.
     - Sweepstakes.
     - Work-at-home offers.
     - Multi-level marketing.
     - Employment offers.
     - Medical cures.
     - Charitable solicitations.
     - Investment or business opportunity fraud.

Continued on page 2

Continued from page 1

   - Merchandise that is ordered but not received by the customer.
   - Merchandise that is misrepresented.
   - Internet promotions that involve the use of the U.S. Mail.

Advise Your Customers How to Complete PS Form 8165

Please ask your customers to complete the following steps:

1. Include copies of the solicitations and other pertinent documents.
2. Mail the completed form to the address indicated on the form.
3. Await an acknowledgment letter from the Inspection Service Operations Support Group after the form has been received and processed into the Inspection Service fraud complaint database.

How to Order Additional Copies

To order copies, call MDC Customer Service at 1-800-332-0317, or send PS Form 7380, *MDC Supply Requisition*, to:

ATTN SUPPLY REQUISITIONS
500 SW MONTARA PKWY
TOPEKA KS 66624-9602

— Business Investigations, Inspection Service, 5-20-99

U.S. POSTAL INSPECTION SERVICE

Mail Fraud Report

See Privacy Act Statement on Page 3

Complainant Information

Your Name	SSN*	Year of Birth*

Address

City	State	ZIP Code	Country

Home Phone No. *(Include Area Code)*	Work Phone No. *(Include Area Code)*	E-Mail

*These two fields are optional, but the information may be helpful to Postal Inspectors tracking your complaint. Also, penalties may increase when certain crimes target particular age groups.

Complaint Filed Against

Company Name	Person's Name and Title

Address

City	State	ZIP Code	Country

Home Phone No. *(Include Area Code)*	Work Phone No. *(Include Area Code)*	E-Mail

Fax No. *(Include Area Code)*	Web Address

Details of Mail Fraud Complaint

Did You Lose Money?
☐ Yes, If so, how much? _____ ☐ No

What Was the Advertised Cost of the Offer?

How Did You Pay? *(Check one)* ☐ Cash ☐ Check ☐ Postal Money Order ☐ Other Money Order ☐ Electronic Transfer ☐ Credit Card ☐ Debit Card ☐ Telephone Bill

Date of Payment

Find the General Category Below that Describes Your Area of Concern, and Check the Specific Item. *(Check one only)*

Advance Payment
- ☐ Loan
- ☐ Credit Repair/Debt Consolidation
- ☐ Credit Card
- ☐ Student Loan
- ☐ Mortgage

☐ **Chain Letter**

☐ **Charity Fraud**

Education
- ☐ School
- ☐ Degree

Employment
- ☐ Postal Job
- ☐ Overseas Job
- ☐ Work at Home *(Such as envelope stuffing)*
- ☐ Distributorship/Multilevel Marketing

False Bill or Notice
- ☐ Office Supplies
- ☐ Directory Solicitation
- ☐ Subscription/Periodical
- ☐ Classified Ad
- ☐ Taxes

☐ **Harassment** *(Merchandise ordered in your name without your consent.)*

Investment
- ☐ Real Estate
- ☐ Gems, Coins, Precious Metals
- ☐ Securities

Lottery *(You pay to play.)*
- ☐ Domestic
- ☐ Foreign

Medical Quackery
- ☐ Weight Loss
- ☐ AIDS Cure
- ☐ Cancer Cure
- ☐ Sexual Aid

Merchandise or Service
- ☐ Failure to Pay
- ☐ Failure to Provide
- ☐ Misrepresentation of Product/Service

☐ **Nigerian Fraud**

Personals
- ☐ Mail-Order Bride
- ☐ Dating Service
- ☐ False Divorce Decree

☐ **Prize or Sweepstakes**

☐ **Sexually Oriented Advertisement**

☐ **Vacation or Travel**

On What Date Did You Receive the Solicitation?

How Were You Contacted? *(Check one)*
☐ U.S. Mail ☐ Newspaper ☐ Radio/TV ☐ Internet ☐ Fax
☐ Telephone ☐ Magazine ☐ In Person ☐ E-Mail ☐ Other

If by Mail, Do You Have the Envelope It Was Mailed in?
☐ Yes ☐ No

Does the Envelope Have a Permit Number Instead of a Stamp?
☐ Yes; Permit No.: _____ ☐ No

Does the Envelope Have a Postage Meter Number Instead of a Stamp?
☐ Yes; Meter No.: _____ ☐ No

How Did You Respond to the Offer?
☐ U.S. Mail ☐ Telephone ☐ Internet ☐ E-Mail ☐ Fax

Do You Have a Mailing Receipt From Your Response (Such as for certified, insured or Express Mail)?
☐ Yes; Mail Receipt No.: _____ ☐ No

To What Address Did You Mail Your Response?

What Did You Receive?

How Did It Differ From What You Expected?

Do You Have the Item?
☐ Yes ☐ No

How Was It Delivered?
☐ U.S. Mail ☐ Private Courier ☐ In Person

Have You Contacted the Company or Person About the Complaint?
☐ Yes
Date of Last Contact: _____
☐ No. Why? ☐ Delivery Attempted, Returned Endorsed Moved, Left No Address ☐ Disconnected Telephone ☐ Unlisted Telephone ☐ Unanswered Telephone ☐ Address Unavailable

Legitimate businesses appreciate feedback. Check the offer for the delivery time frame, usually 6 to 8 weeks, and then contact the company. Please wait 2 weeks after contacting them before sending us this form. When a delivery time is not specified, a Federal Trade Commission rule mandates fulfillment within 30 days, unless you applied for first-time credit with the company.

Additional Information You Feel Is Important

Print Your Name | Today's Date

Thank you for completing this form. Please mail it with copies *(not originals)* of any bills, receipts, advertisements, canceled checks (front and back) or correspondence related to your report to the address below.

The U.S. Postal Inspection Service is a federal law enforcement agency. Postal Inspectors gather facts and evidence to determine whether a violation has occurred under the Mail Fraud or False Representation Statutes. While the Postal Inspection Service can't guarantee that you'll recover money lost to fraud, the information can help alert Inspectors about new fraud schemes and prevent others from being victimized.

Postal Inspectors base mail fraud investigations on the number, substance, and pattern of complaints received from the public; therefore, we ask you to keep all original documents relating to your complaint, including the solicitation, any mailing envelopes, and canceled checks. Under our Consumer Protection Program, Postal Inspectors may contact individuals or businesses on your behalf to request that complaints be resolved. We will contact you if more information is needed.

Postal Inspectors caution that, once you've been targeted in a fraud scheme, your name may be passed along to other con artists, so beware of future solicitations. If you know of others who believe they were victimized in a fraud scheme, we recommend that you encourage them to submit a Mail Fraud Report as well.

Avoid being a victim: Postal Inspectors recommend that, before completing a business transaction, contact the Chamber of Commerce, Better Business Bureau, or county or state Office of Consumer Affairs in the area where the firm is located to get any information available on the company. If you have Internet access, you can get information from the Better Business Bureau online at: www.bbb.org, and from the individual state Attorneys General Consumer Protection Divisions at www.naag.org. Also, check the Postal Inspection Service Web site at: www.usps.gov/postalinspectors for more information on fraud schemes that involve the use of the mail.

Remember: If a deal sounds too good to be true, it probably is!

Please return this form to your postmaster, or mail to this address:

INSPECTION SERVICE SUPPORT GROUP
222 S RIVERSIDE PLAZA STE 1250
CHICAGO IL 60606-6100

Mr. MCHUGH. Anyone else on the subcommittee?

Mr. LaTourette.

Mr. LATOURETTE. I don't have any more questions, but if I could just make a request to the chairman. In my questions to the Postmaster General, I referenced a report from the Postal Rate Commission to the Congress dated June 30, 1999. For some reason—it doesn't look quite as bad as some of the redacted documents I used to get when I was a prosecutor—some of the figures have been redacted. I would ask unanimous consent if that's an appropriate request, the unredacted version of this report be made a part of the record of this hearing.

Mr. MCHUGH. Without objection, so ordered.

Mr. LATOURETTE. Thank you.

Mr. MCHUGH. Do you have the unredacted?

Mr. LATOURETTE. I was hoping that maybe Robert, who is so resourceful, can find it for us.

Mr. MCHUGH. We'll have to put a codicil on that. If we can get it, we'll put it in the record. I don't believe we redacted it, did we? We're not like that. Oh, it's being litigated. When it's litigated, if we can get the unredacted report, without objection it will be entered into the record in its entirety. I thank the gentleman.

[The information referred to follows:]

REPORT TO THE CONGRESS

1998 INTERNATIONAL MAIL VOLUMES, COSTS AND REVENUES

POSTAL RATE COMMISSION
1333 H Street, NW
Washington, DC 20268-0001

June 30, 1999

NOTICE: *This Report contains information that the Postal Service considers to be of a commercial nature, including trade secrets, which under good business practices it would not publicly disclose. The Postal Service provided this information as required by 39 U.S.C. 3663(b), but it requests that this information be kept confidential.*

SUMMARY

This is the initial report to Congress on the costs, revenues, and volumes of international mail handled by the United States Postal Service. This report analyzes fiscal year 1998 information.

The Commission finds that the data provided by the Postal Service on its international mail costs, revenues and volumes are generally reliable and the Commission has included an analysis of the coefficients of variation for the attributable costs per piece of international mail products.

All international mail combined generated revenues equal to 112.9 percent of its attributable costs. In comparison, all domestic and international mail combined generated revenues equal to 158.3 percent of its attributable costs. The financial performance of international products is summarized in a table appearing at page 9 of this report.

Financial results are presented separately for outbound international services and inbound international services. The Postal Service has unilateral authority to set the rates for mail sent from the United States to other countries. In total, Outbound International Mail recovers its attributable costs and makes a contribution to the institutional costs of the Postal Service, although at least four individual international services do not earn revenues sufficient to cover their attributable costs. See page 35.

The Postal Service does not set the rate of compensation it receives for delivering a substantial portion of the mail sent from other countries to the United States. The Universal Postal Union (UPU) establishes schedules of terminal dues that countries must accept as payment for the delivery of letters and printed matter. In total, Inbound International Mail does not recover its attributable costs, largely because terminal dues do not fully compensate the Postal Service for the delivery of inbound letters and printed matter.

The Postal Service was cooperative in providing data requested by Commission, however it failed to provide sufficient information to enable the Commission to evaluate two small international services, Value Post/Canada and Bulk Letter Service to Canada. Rates for these services were recently increased, which may be an indication that the revenues for these service have not been covering costs.

TABLE OF CONTENTS

Page

I. INTRODUCTION 1

II. GENERAL DESCRIPTION OF INTERNATIONAL MAIL 5

A. The Basic Categories of International Mail Service 5

B. Characteristics of International Mail Rates 6

C. Description of Specific International Mail Services 7

III. MEASURING THE COSTS, REVENUES, AND VOLUMES OF INTERNATIONAL MAIL 12

A. Description of Data Sources and Data Development Methodology 12

(1) Outbound Revenue, Pieces, and Weight 12
(2) Inbound Revenue, Pieces, and Weight 13
(3) The Development of Attributable Costs for the Standard Services 14
(4) The Development of Attributable Costs for the Initiatives 16
(5) International Mail Incremental Costs 17

B. Evaluation of Data Sources and Data Development Methodology 17

(1) Outbound Revenue, Pieces, and Weight 18
(2) Inbound Revenue, Pieces, and Weight 19
(3) The Attributable Costs for the Standard Services 20
(4) The Attributable Costs for the Initiatives 21
(5) Analysis of Unit Attributable Costs 22

IV. PRESENTATION OF COST, VOLUME, AND REVENUE DATA 29

A. Aggregate Data 29

B. Individual Services 32

(1) Outbound Mail 33
(2) Inbound Mail 37
(3) Other Comments 38

LIST OF TABLES

Table II-1 Summary of Volume, Revenue, and Attributable Cost for Section 3663 International Mail Services 9

Table III-1 Coefficients of Variation for SIRV/O Estimates for Selected Categories 19

Table III-2 Cost per Piece, Revenue per Piece and Coefficients of Variation for International Mail 25

Table IV-1 Summary of FY 1998 Revenue and Attributable Cost for Outbound and Inbound International Mail 30

Table IV-2 Summary of Revenue, Volume, and Costs for Outbound and Inbound International Mail 34

Table IV-3 Comparison of Revenue and Cost Data and Percentage Distribution of Originating Volume for Selected International Mail Categories 39

LIST OF APPENDICES

Appendix A List of Reference Sources

Appendix B Outbound International Services

Appendix C Measuring the Costs, Revenues and Volumes of International Mail

Appendix D Derivation of Approximations for Attributable Cost Per Piece (ACP) and Its Coefficient of Variation (CV)

Appendix E Outbound Regional Data

Appendix F The Postal Service's Revised Treatment of International Air Transportation Costs and the Settlement Difference

Appendix G Reference Material – Postal Service Views

I. INTRODUCTION

On October 21, 1998, the President signed into law H.R. 4328. H.R. 4328 contained a new § 3663 of title 39, United States Code. Section 3663(a) directs the Postal Rate Commission to submit to Congress a comprehensive report on the costs, volumes, and revenues of the Postal Service's international mail services by July 1 of each year. Section 3663(b) directs the Postal Service to provide to the Commission, by March 15 of each year, the data it needs to prepare its report. This is the first such report prepared by the Commission.

Because the Commission's task is novel, several issues of first impression had to be addressed during the course of preparing its report. The Commission opened Docket No. IM99-1 to consider these issues. The most significant issues raised in Docket No. IM99-1 were the precise nature of the data to be provided to the Commission by the Postal Service, the proper definition of individual international postal products for purposes of § 3663 analysis, the proper method for attributing costs to individual international mail products, and whether data provided by the Postal Service should be available for public inspection and comment.

Issues that the Commission needed to address were first raised in a round of pleadings prompted by a petition for rulemaking filed by United Parcel Service (UPS). UPS requested that the Commission commence a rulemaking to determine "(1) the data to be provided to the Commission by the United States Postal Service and (2) the methods to be used by the Commission in analyzing the costs, revenues, and volumes of each international mail product" to prepare the report required by § 3663. Petition of UPS to Institute Rulemaking Proceeding to Study International Costs and Revenues, December 16, 1998, at 3. In response, the Commission invited interested parties to submit comments identifying the specific international mail products or services that should be analyzed. The Commission included a preliminary list of possible international mail products and asked interested parties to comment on the

completeness of the list and the appropriateness of the level of disaggregation reflected by the list. Order No. 1226 (January 15, 1999) at 3.

Upon review of comments submitted, the Commission published a revised list of international mail products or "subclasses," while recognizing that the Postal Service might not be able to produce reliable data on some products in time for the FY 1998 report. The Commission also decided that, to the extent possible, its report should include cost coverages for these international mail products, Order No. 1228 at 2, 5, even if the calculations of those cost coverages could not be revealed because of the commercial sensitivity of the underlying data. Order No. 1228 (February 16, 1999) at 6-7.

The issue of commercial sensitivity, however, was revisited when UPS sought access to essentially all the international mail data filed with the Commission by the Postal Service. UPS made its request in the form of a motion in Docket No. IM99-1. Motion of United Parcel Service to Provide Public Access to International Mail Data Requested in Order No. 1228 and for Opportunity to Provide Public Comment, March 26, 1999. In declining to disclose all of the international mail data provided by the Postal Service, the Commission distinguished the § 3663 reporting procedure from the Commission's formal rate hearings, where the Commission must balance a litigant's need for discovery of facts against a need for protection of commercially sensitive information. The Commission also noted that the Postal Reorganization Act reiterates the exemption from the mandatory disclosure policy of the Freedom of Information Act (FOIA) for commercially sensitive information, and that Congress had taken no steps to alter the Service's eligibility for that exemption when passing § 3663. The Commission concluded that there was no basis for applying a blanket disclosure policy to information provided through the § 3663 reporting process. Order No. 1245 (May 21, 1999) at 3-4.

The March 15 deadline established in § 3663(b) is well ahead of the date by which the Postal Service had traditionally completed its International Cost and Revenue Analysis (ICRA). Nevertheless, the Postal Service was able to supply a large portion of the data requested in Order No. 1228 by March 15, 1999. Between March 15 and June 15, 1999, the Postal Service submitted additional clarifying information in response to six additional Commission data requests.[1] The Commission's data requests were promulgated via Order Nos. 1236, 1240, 1244, 1246, 1251, and 1252. The Commission's data requests generally sought information underlying the Postal Service's estimates of the costs, volumes, and revenues of international "subclasses."

The Commission has been able to evaluate the reasonableness of the Postal Service's methods of collecting international mail data and the reasonableness of its procedures for developing estimates of systemwide totals from those data. They should yield generally reliable results. However, the short time available for reviewing the data on international mail provided by the Postal Service has not allowed the Commission to evaluate that data as thoroughly as it evaluates such data in the context of a domestic rate case conducted under Administrative Procedures Act standards. The Commission has had less opportunity to independently confirm that data were sampled or compiled according to the established procedures. It also has had less opportunity than is available in a domestic rate proceeding to scrutinize the data for anomalous results. Although the Commission concludes that the Postal Service's estimates for international mail are generally reliable, this conclusion is more tentative than it typically would be if data on domestic mail were being evaluated in the context of a domestic rate hearing. As the Commission gains experience with the unique

[1] For convenience, this report uses a nontraditional method for citing references. Appendix A contains a list of numbered references with their complete titles. In this report, citations using the word "Source" followed by a page number or other location reference (*e.g.*, Source 1, p. 3-1) refer to the specific numbered source listed in Appendix A.

characteristics of the data collection systems, rate structures, and markets for international mail, its subsequent § 3663 evaluations will be more definitive.

On June 7, 1999, the Postal Service submitted the FY 1998 ICRA Report — Postal Service Version. It included a new method for estimating attributable international transportation costs, and a new approach to analyzing the difference between imputed settlement costs and the settlement costs in the Books of Account. Because the Commission has not had time to fully consider the merits of the methodological changes in the postal Service version, it is not able to validate them. Nevertheless, the Postal Service's recent methodological changes, if subsequently determined to be valid, would have a noticeable impact on international mail costs and cost coverages. The impact that they would have is shown in Appendix F.

II. GENERAL DESCRIPTION OF INTERNATIONAL MAIL

A. The Basic Categories of International Mail Service

The Postal Service provides three broad categories of international mail service: letter post, parcel post and Express Mail. These categories reflect Postal Service agreements to provide a common set of services on a reciprocal basis with other members of the Universal Postal Union (UPU). With respect to outbound mail, the Postal Service provides mailers in the United States with access to the domestic delivery services offered by the postal administration of the destinating country. With respect to inbound mail, the Postal Service provides access to its domestic delivery services to the postal administration of the originating country.

Generally, the letter post and parcel post categories are divided into "air," or premium service, and "surface," or regular service. The UPU distinguishes between mandatory international services, which all members are obligated to provide, and optional international services. The exchange of international letter-post services on reciprocal terms is mandatory among UPU members. These services include letters and cards (LC), whose content is most comparable to domestic First-Class Mail, and other articles (AO, from the French term "autres objets"). The content of AO is comparable to domestic Standard A, Standard B, and Periodicals mail. Printed papers, literature for the blind, and small packets, are mandatory AO services. Services that are optional under the UPU structure include international parcel post (the air portion of which is analogous to domestic Priority Mail and the surface portion of which is analogous to domestic parcel post), and international Express Mail Service (EMS), which is analogous to domestic Express Mail.

There are subcategories of LC, AO, and parcel post that provide service enhancements to, or volume discounts from, these basic categories of service. Within

these subcategories are numerous rate groups. They reflect differences in terminal dues (the amount that postal administrations have agreed to charge for domestic delivery of mail originating in another country). They also reflect regional differences in international transportation costs, which are important for bulk mail and parcel services.

B. Characteristics of International Mail Rates

The Postal Service's international mail rates are designed to cover two sets of costs: (1) the cost that it incurs to collect and forward mail to the postal administration of the destinating country and, (2) the amount that the postal administration of the destinating country charges the Postal Service for domestic delivery of that mail. In aggregate, just about half of the costs of the Postal Service's outbound international mail consists of charges for domestic delivery in the destinating country.

Charges for delivering the Postal Service's outbound international mail in the destinating country are of three types. LC/AO mail is charged "terminal dues," parcel post is charged "inward land rates," and Express Mail Service is charged "imbalance charges." The terminal dues that are charged for delivering LC/AO mail are set by the UPU. These are based on a global average cost, and are the same for all UPU members. This reflects a universal service obligation on the part of UPU members to take all letter post items sent by other UPU members.

Terminal dues rates are set by the Congress of the UPU, which convenes every five years. The Postal Operations council of the UPU, however, can amend them between Congresses. The Postal Service unilaterally determines what it will charge to deliver optional categories of inbound international mail. It sets the inward land rates that it charges to deliver inbound parcel post. It may revise them annually. It also enters bilateral agreements that set the imbalance charges that it applies to inbound Express Mail Service.

Currently three terminal dues rate structures may be applied to the LC/AO mail of UPU members. The first is the basic dues structure, which is a flat rate per kilogram. Where the mail flow between a pair of member countries is above a 150-metric-ton-threshold, a second dues structure known as a "revision mechanism" may be invoked. The revision rate is a combined per-item and a per-kilogram rate that may be invoked for mail flows that are either considerably lighter than average, or considerably heavier than average, in terms of the number of pieces per kilogram. Invoking the revision mechanism has the effect of reducing terminal dues charged to deliver mail that is heavier than average, and of increasing terminal dues to deliver mail that is lighter than average.[2] The third structure is a bulk mail option. Of minor importance is the lower terminal dues rate that applies to M-bags. (M-bags contain the AO mail of one mailer all going to a single foreign address.). The Postal Service also enters into multilateral payment agreements to settle its accounts outside the UPU structure. The Postal Service entered into separate agreements with the European Bilaterals (EURB)[3] and Canada.

C. Description of Specific International Mail Services

Section 3663(a) of title 39 requires the Commission to prepare "a comprehensive report of the costs, revenues, and volumes accrued by the Postal Service in connection with mail matter conveyed between the United States and other countries." Section 3663(b) indicates that the Commission's report should "analyze the costs, revenues, and volumes for each international mail product or service, under the methods

[2] The revision mechanism is asymmetrical. It can be invoked to reduce terminal dues for flows of heavier-than-average mail from developing countries to industrialized countries, but cannot be invoked to reduce terminal dues for flows of heavier-than-average mail from industrialized countries to developing countries. See Appendix A, Source 14.

[3] Belgium, Denmark, Finland, France, Germany, Great Britain, Iceland, Ireland, Italy, Luxembourg, Netherlands, Norway, Spain, and Sweden. See Appendix A, Source 13.

determined appropriate by the Commission for the analysis of rates for domestic mail." Section 3663(b) does not specify which of the over 70 international products and services that the Postal Service offers should have its "costs, revenues, and volumes" separately analyzed in this report. The Commission, therefore, must decide at what level of detail a presentation of costs, revenues, and volumes would most meaningfully aid Congress' understanding of the financial posture of the Postal Service's international mail services.

The Commission infers from § 3663 that Congress contemplates a report that provides data and analysis from which the Congress can draw conclusions about the adequacy of the rates charged for international services, whether viewed from the standpoint of the Postal Service's domestic users, or from the standpoint of the competitors of the Postal Service's international services. From either viewpoint, it would appear that an important consideration is identifying which categories the Postal Service itself focuses on when it relates international mail rates to costs. Consequently, this report attempts to display the financial posture of the international services for which the Postal Service consciously designs a specific margin of revenue over costs (or "cost coverage") when it chooses rates for its international services. In subsequent reports, the Commission will have an opportunity to consider whether additional criteria might be appropriate for determining the list of international services to be included in reports submitted under § 3663. The Commission's first report under § 3663, however, presents cost, revenue, and volume data for a list of international services for which the Postal Service itself designs specific cost coverages. See Table II-1, below.

TABLE II-1
SUMMARY OF VOLUME, REVENUE, AND ATTRIBUTABLE COST
FOR SECTION 3663 INTERNATIONAL MAIL SERVICES

International Mail Category	Volume (1)	Revenue ($) (2)	Attributable Cost ($) (3)	Contribution ($) (4)=(2)-(3)	Cost Coverage (5)=(2)/(3)
OUTBOUND MAIL					
Surface					
Printed Matter & Small Packets, excl. ISAL & Per.	28,215	57,461	69,326	(11,865)	82.9%
Periodicals	65,082	68,615	81,708	(13,093)	84.0%
Parcel Post	2,312	57,607	48,107	9,500	119.7%
Int'l Surface Airlift	163,587	116,120	111,739	4,381	103.9%
ValuePost/Canada 1/	-	0	0	0	-
Subtotal, Surface	259,196	299,803	310,880	(11,077)	96.4%
Air					
Letters and Letter Packages	510,053	451,943	275,166	176,777	164.2%
Postcards, Postal Cards, and Aerogrammes	63,010	31,299	20,477	10,822	152.8%
Printed Matter and Small Packets (AO)	45,017	194,833	139,277	55,556	139.9%
International Priority Airmail Service	52,843	39,219	22,101	17,118	177.5%
Bulk Letter Service to Canada 1/	-	0	0	0	-
Parcel Post	4,240	124,029	97,897	26,132	126.7%
Express Mail International Service	4,694	125,363	78,366	46,997	160.0%
Subtotal, Air	679,857	966,686	633,284	333,402	152.6%
Initiatives					
Global Priority Mail	4,219	30,265	38,886	(8,621)	77.8%
Global Package Link	1,513	23,630	26,635	(3,005)	88.7%
Direct Entry/Inbound	16,837	3,351	3,115	236	107.6%
International Customized Mail	10,433	9,061	7,720	1,341	117.4%
Subtotal, Initiatives	33,002	66,307	76,356	(10,049)	86.8%
Total Outbound	**972,055**	**1,332,796**	**1,020,520**	**312,276**	**130.6%**
INBOUND MAIL					
Surface LC/AO	46,735	36,637	52,574	(15,937)	69.7%
Surface Parcel Post	2,142	16,752	9,987	6,765	167.7%
Surface Subtotal	48,877	53,389	62,561	(9,172)	85.3%
Air LC/AO	587,926	163,179	180,632	(17,453)	90.3%
Express International Mail Service	3,763	30,137	29,742	395	101.3%
Air Parcel Post	2,192	20,029	11,707	8,322	171.1%
Air Subtotal	593,881	213,345	222,081	(8,736)	96.1%
Direct Entry/Inbound	301	116	23	93	504.3%
Global Parcel Services	1,049	2,552	2,714	(162)	94.0%
Other 1/	-	12,909	0	12,909	-
Total Inbound	**644,108**	**282,311**	**287,379**	**(5,068)**	**98.2%**
International Service Incremental Cost	-	0	122,445	(122,445)	0.0%
Total International Mail	**1,616,163**	**1,615,107**	**1,430,344**	**184,763**	**112.9%**

Source: Table IV-2

1/ See Table IV-2 for caveat.

A second concern causing the Commission to modify the list of international services covered by its report is that some international services are so small, and the sample data are so thin, that separating their cost, revenue, or volume data from the larger subclass to which they belong yields results that may not be sufficiently accurate to support meaningful conclusions. Accordingly, some services (specifically M-Bags) are combined with their parent subclass (AO) for purposes of calculating their cost coverages.

Table II-1, therefore, displays costs, revenues, and volumes for all of the outbound international services for which the Postal Service separately selects a target cost coverage, except for Valuepost/Canada, Bulk Letters to Canada, and M-bags. It is apparent that Table II-1 disaggregates outbound services to a greater extent than inbound services. This reflects the fact that the Postal Service determines what it charges for outbound services, but has only limited influence over the charges promulgated by the UPU for inbound LC/AO services. The Postal Service sets rates, and has distinct revenue targets, for more outbound services than there are distinct inbound services.

The outbound and inbound flows of the broad, UPU-defined subclasses of international mail are related in the sense that country pairs exchange mail service that is similar in content and service features. In the case of LC/AO mail, the same terminal dues rates are applied to both directions of the exchange. All things being equal, an increase in terminal dues will increase the markup on inbound mail and decrease the markup on outbound mail. It can be argued, therefore, that the outbound and inbound costs, revenues, and volumes of like services should be combined to determine the financial posture of a given service. Counter-arguments are that many outbound mail services do not have direct inbound analogues, and that outbound flows are not the primary cause of inbound mail flows. Furthermore, the costs and service features of outbound mail are largely within the control of the originating postal administration,

while the charges and service features that apply to inbound mail are largely determined by the UPU. It can be argued that because of this bifurcation of responsibility, the financial posture of a given outbound international service should be analyzed separately from its corresponding inbound service.[4] The Commission has concluded that both points of view can be accommodated by presenting the costs, revenues, and volumes of outbound and inbound mail flows separately for the services included in Table II-1. The separated data can be readily combined by those who view particular outbound and inbound services as sufficiently related to warrant combined analysis.

The Postal Service characterizes some of its newer products that are designed to compete directly with privately provided international mail services as its international mail "initiatives." These are displayed together in Table II-1 at lines 15 through 19. A description of the international services listed in Table II-1 is presented in Appendix B.

[4] The Postal Service itself has changed its position on this issue. Prior to 1986, the Postal Service pooled outbound and inbound costs in selecting target cost coverages for its international services. This had the effect of burdening outbound ratepayers with the cost of delivering inbound, foreign-origin mail. After it suspended application of the Private Express Statutes to its international services in 1986, the Postal Service designed rates for its outbound international services to cover the costs only of the outbound portion of each service.

III. MEASURING THE COSTS, REVENUES, AND VOLUMES OF INTERNATIONAL MAIL

A. Description of Data Sources and Data Development Methodology

The Postal Service uses many of the same data sources for international mail that it uses for domestic mail. For volumes, this includes the Permit system. For costs, this includes the In-Office Cost System (IOCS), the Transportation Cost System (TRACS), and the City Carrier and Rural Carrier data collection system. Where necessary, the Postal Service augments its data needs with additional data systems like the System for International Revenue and Volume — Outbound (SIRV/O) or the System for International Revenue and Volume — Inbound (SIRV/I). The Service also has to account for its new offerings referred to as initiatives. Because some of the existing data collection systems do not generate sufficient information on the initiatives, the Service uses alternative data sources to obtain estimates. This section briefly describes the data sources and the methodology the Postal Service uses to calculate the revenue, pieces, weight, and attributable cost for international mail. A more detailed description is contained in Appendix C. It should be noted that the Postal Service has provided attributable costs using the Commission's costing methodology, *i.e.*, the same costing methodology that underlies the recommended rates in the Commission's most recent decision in an omnibus domestic rate case.

(1) Outbound Revenue, Pieces, and Weight

In FY 1998, the Service obtained its volume and revenue data from the Permit system or permit-like systems. These systems identified 33 percent of outbound piece volume. See Appendix C at 3. The remaining 67 percent were obtained from the SIRV/O. The Permit system tracks the data from mailing statements on a census basis,

as do the permit-like systems. These census systems cover (1) Periodicals, (2) International Surface Airlift (ISAL), (3) International Priority Airmail Service (IPAS), (4) ValuePost/Canada, (5) Bulk Letter Service to Canada, (6) Global Package Link (GPL) (except for a small portion), (7) Direct Entry, (8) Express Mail International Service (EMS), (9) Global Priority Mail (GPM), and (10) International Customized Mail (ICM).

The SIRV/O is a stratified random sampling system that collects revenue and volume data for (1) Surface Printed Matter, (2) Surface Parcel Post, (3) Air Letters and Letter Packages, (4) Air Cards and Aerogrammes, (5) Air Printed Matter, and (6) Air Parcel Post. The SIRV/O is supported by the Military and International Accounting and Dispatch System (MIDAS). This operational system provides a census count of the weight of outbound mail by destination country. It provides a control weight figure for adjusting sample estimates to coincide with a direct measure of the actual weight of international mail.

The Service also uses an auxiliary sample data collection system independent of the SIRV/O to provide an estimate of GPM volume by country. The accounting systems do not track GPM volume by destination country. The sampling process is similar to the SIRV/O.

(2) Inbound Revenue, Pieces, and Weight

The Postal Service's International Accounts Branch (IAB) routinely collects volume information on inbound international mail from the manifests that accompany the mail. Source 1, p. 6-1 and Source 8, Response to Item 2. Through this process, it collects piece and weight data for parcel post, EMS, and M-bags. For LC/AO mail it collects only weight information. To develop the number of pieces for this mail, the Postal Service estimates the average number of pieces per kilogram by transportation mode and country or country groups. This estimate is obtained from the SIRV/I, which

is a stratified random sampling system similar to SIRV/O. The Service multiplies the total weight of inbound LC/AO mail for each country by the applicable piece per kilogram. Source 1, p. 8-2 and 8-5.

To develop inbound revenue for mail, the Service multiplies the volumes, described above, by the applicable terminal dues rate, inward land charge, or imbalance charge, adjusted for the appropriate exchange rate. The Service knows these charges from agreements with other countries and published schedules. Source 1, p. 6-1. The Postal Service maintains a separate system for accumulating revenue and volume information on inbound mail from Canada. The Service uses the same calculation procedure for Canadian mail as described above. Source 1, pp. 6-1 and 6-3.

Since the described procedure provides imputed values for revenue, the Postal Service adjusts the figures to match the revenues included in the Domestic RPW Report. Air conveyance dues and transit fees are obtained from the books of accounts. Source 1, p. 6-3.

(3) The Development of Attributable Costs for the Standard Services

There are six generalized components for international mail costs: (1) mail processing; (2) delivery (in-office and street), (3) domestic transportation; (4) international transportation; (5) settlement charges; and, (6) "all other" costs (primarily costs that piggyback on the directly variable costs). This categorization accounts for all cost elements in the Domestic Cost Segments and Components Report and the Domestic Cost and Revenue Analysis (CRA), which has a line item for international mail.

Outbound services incur domestic mail processing, domestic transportation, international transportation, terminal dues (the cost of delivery in the destination foreign country), and applicable "all other costs." Outbound costs do not require domestic

delivery. Inbound mail incurs domestic mail processing, domestic transportation, delivery, and applicable all other costs. Inbound mail does not incur settlement charges or international transportation costs.

The costs for mail processing are based on a combination of the Management Operating Data System (MODS) activity cost and In-Office Cost System distribution keys. Delivery costs are based on IOCS information and the data in the city and rural carrier cost system. This report is based on an ICRA that uses the Commission's methodology.

Domestic transportation costs are obtained from the book of accounts and distributed to international services on the basis of distribution keys derived from TRACS. For some expense categories, the TRACS data are not sufficiently detailed. In these cases, the Postal Service uses the outbound and inbound volumes described above as a distribution key. Source 1, p. 2-1.

International transportation cost is attributed only to outbound mail. The applicable cost for each service is obtained in four steps: (1) from International Accounts Branch (IAB) data, unit cost by country and mail category is calculated, (2) unit costs are multiplied by more detailed mail category information to develop country totals, (3) country totals are grouped into applicable rate groupings, and (4) the country group totals are reconciled to the book of accounts. Source 1, p. 4-1. Costs for Canada and Mexico mail are estimated using analogous domestic unit costs. Source 1, p. 4-4.

Settlement costs apply only to outbound mail. They reflect payment to foreign postal administrations for delivering or forwarding U.S. mail. Source 1, pp. 5-1 and 5-2. The Postal Service calculates an imputed value for these costs by multiplying the outbound volumes by the applicable settlement charge. The Postal Service does not reconcile the total imputed value to the book of accounts' value because the latter figure is accrued on a conservative basis to avoid underestimating expenses and

reflects other factors that are not a function of current volumes. In FY 1998, the Book of Accounts value was $70 million higher than the imputed value. The Postal Service treats this difference as an incremental cost of providing international mail service as whole. Source 7, Response to Item 10.[5]

"All other" costs encompass all attributable costs not included above. These are mostly cost items that are treated as varying in proportion to directly variable cost. These costs include the costs of some lower level regional and headquarters administration, rents, fuels, utilities, supplies and services, and other support costs. There are also directly variable costs for supervision and for clerk and mailhandler nonmail processing activities.

(4) The Development of Attributable Costs for the Initiatives

Cost data for the initiatives are gathered from sources outside the main data collection systems because the initiatives are seldom observed in these systems with the exception of GPM, which is obtained from the IOCS. GPL costs are based on an engineering approach by which the operations are mapped out and classified as variable or fixed. Unit costs are estimated for each of the operations deemed variable and multiplied by volume to calculate total attributable cost. Source 3, Response to Item 9. The Postal Service also identified product-specific costs for GPL. These costs reflect advertising, promotional, and other costs related solely to GPL. GPM also had product-specific costs for the same activities. Source 7, Response to Item 9.

[5] On June 7, 1999, the Postal Service submitted the FY 1998 ICRA report — Postal Service Version. The report contained a revised methodology for calculating international transportation cost and a different treatment of the difference between imputed settlement costs and the settlement costs in the Books of Account. Because of time constraints, the Commission has not been able to evaluate the merits of the changes. For this reason, the attributable costs in this report reflect the FY 1998 ICRA Report — PRC Version.

The costing for Global Direct Services (Direct Entry/Inbound) and ICM reflects the costs of operations that vary by specific customer. Source 1, pp. 9-3 and 9-4.

The Postal Service estimates the costs for Global Parcel Services (GPS), an inbound service, using a proxy unit cost estimated for domestic Priority Mail. Transportation costs are adjusted to reflect weight differences between Priority Mail and GPS. Source 1, p. 9-5.

(5) International Mail Incremental Costs

The Postal Service has included costs that it views as incremental to International Mail as whole. The cost has two components. As discussed above, the first component reflects the difference in settlement charges between imputed costs used in the ICRA as attributable settlement cost, and the booked cost in the system of accounts. This cost amounted to $70 million in FY 1998. The second component reflects expenses for the International Business Unit that amounted to $52 million in FY 1998. ICRA Report, p. A-1, footnote 1. The reported amount includes the salaries and benefits for IBU personnel, supplies and services, rents, utilities, and other related expenses. Source 3, Response to Item 4. Together, these expenses amount to $122 million.

These costs cannot be causally related to specific international services on the basis of current information, but can be causally related to international services as a whole. Accordingly, the cost coverages for specific products shown on Table II-1 do not reflect these incremental costs.

B. Evaluation of Data Sources and Data Development Methodology

This section discusses the reliability of the volume, cost, and revenue data. The organization of this section generally follows the preceding section. There is an

additional section that discusses data quality with respect to unit costs and cost coverage.

(1) Outbound Revenue, Pieces, and Weight

The volume and revenue data that the Postal Service uses for outbound international mail are quite reliable. Thirty-three percent of the volume data are collected using census data systems, and the other 67 percent is estimated using the SIRV/O system that has control numbers from the MIDAS system. The coefficients of variation (CV) for these data are very small.

Most of the census data (94 percent) comes from the Permit system. The Permit system has been accepted in omnibus domestic rate cases as reliable. It provides volumes and revenues for Domestic Standard A mail, which amounted to 83 billion pieces of mail in 1998. The system is based on mailing statements that contain the detail of a mailing related to pieces, weight, and revenue. The statements are checked by an acceptance clerk and entered into an automated accounting system. It is therefore well suited to the task of accurately accumulating volumes and revenues for any service. The data sources for the other 6 percent collect the same type of information without it being entered into an automated accounting system. These reports are similarly well suited to accurately generating volumes and revenues.

The SIRV/O is a well-designed system for randomly sampling containers of outbound mail. The cornerstone, however, is the MIDAS system, which provides a census count of the gross weight of all outbound mail by country, transportation mode, and UPU class. The Postal Service uses the MIDAS numbers as control totals in the expansion process. This adds to the reliability of the SIRV/O estimates.

The Commission's confidence in the reliability of the outbound RPW estimates is further bolstered for most of the major categories of outbound mail by their small coefficients of variation as shown by the CVs below.

TABLE III-1

COEFFICIENTS OF VARIATION FOR SIRV/O ESTIMATES FOR SELECTED CATEGORIES

Mail Category	Coefficients of Variation Revenue	Pieces	Weight
Air LC	1.3%	2.0%	1.0%
Air AO	1.7%	2.6%	2.0%
Air Parcel	1.7%	3.2%	2.9%
Surface AO	5.0%	6.7%	5.0%
Surface Parcel	2.9%	2.6%	3.4%

Source: Source 7, Response to Item 17

(2) Inbound Revenue, Pieces, and Weight

The Commission believes the Inbound RPW estimates are generally reliable because the SIRV/I sampling system underlying the estimates is well designed. The estimates may suffer from unquantifiable nonsampling error. Nonsample error, however, is not likely to be substantial for the reasons discussed below.

Like the SIRV/O, the SIRV/I estimate of pieces per kilogram relies on a set of control numbers that allows the Postal Service to calibrate sampled volumes to census-based volumes kept in the IAB. The control numbers are total kilograms by country and transportation mode. The IAB maintains a count of the weight of mail entering the U.S. based on the manifests that accompany the mail. Operations personnel check the contents of inbound containers against the manifests. When there is a discrepancy, these personnel prepare and dispatch to the origin country documentation known as a Bulletin of Verification. Data files are updated accordingly. Source 8, Response to Item 2. Thus, the Postal Service continuously takes steps to insure the accuracy of

inbound volume data. Since the control numbers appear to be accurate, the conversion of pieces per kilogram to total pieces should be reasonably accurate.

The Postal Service identifies two nonsampling error problems that have emerged. First, some inbound Canadian mail arrives in Postal Service containers and is not sampled because it is mistaken for U.S. Domestic mail. Second, the Postal Service has some indication that not all sampled mail containers from Canada and Europe are selected randomly. The Postal Service explains that the magnitude of the potential sampling problem is unknown as is the impact on revenue. The Postal Service adds, however, that it has taken three steps to address the potential problem. Source 8, Response to Item 1.

First, in the summer of FY 1998, the Postal Service began to clarify and improve field data collection and administrative procedures. Second, the Postal Service held a conference in November 1998 on international statistical programs bringing together data collectors, data collector supervisors, and headquarters personnel to discuss the issues. The Conference included workshops for each major program area, including SIRV/I. Third, the Postal Service is preparing and will soon release Handbook F-85, Data Collection Users Guide for International Systems. It contains updates of out-of-date field procedures and consolidates data collection policy and procedures for all international statistical programs. Source 8, Response to Item 2.

These corrective measures will only affect RPW data collected after FY 1998. The impact of these potential problems on the FY 1998 RPW data is unknown.

(3) The Attributable Costs for the Standard Services

These costs are generally reliable. On average, settlement costs and international transportation costs account for 71 percent of the total attributable cost for outbound services. The Commission has reviewed the underlying workpapers and found no material errors. The calculation of settlement costs is based on outbound

volume estimates which the Commission has concluded are reliable, as discussed above, and known and certain schedules for the various forms of settlement charges. International transportation costs are based on the generally reliable outbound volumes and unit cost figures developed from the IAB report which collects the actual outbound weight and cost by country. Moreover, these costs are ultimately adjusted to match the Book of Accounts. Thus, these costs should be reliable.

The other 29 percent of outbound costs and all inbound costs are based on the costing methods that underlie the domestic CRA. In domestic rate cases, the Commission has concluded that the data systems that underlie these costs are reliable. For this reason, the Commission believes these costs should be reliable here.

The Commission also used the Service's input data in its own cost model. The Commission's cost for international mail matched the Postal Service's segment by segment. For this reason, the Commission believes the attributable costs for the standard services as calculated by the Service accurately portray the Commission's methodology.

(4) The Attributable Costs for the Initiatives

The Commission has not been able to verify the accuracy of the input data for the initiative cost models. It was able to review the model methodology underlying the models. The Postal Service here employs models generally similar to ones it has introduced in domestic omnibus rate cases and classification cases to support new classifications, discounts, or special services. These models are referred to as engineering models or special studies. In the domestic area, the Commission has relied on broadly similar models to support recommended rates and classifications.

Under this modeling approach, the Postal Service identifies all the operations that accompany a particular service. It then obtains unit cost estimates for each of the operations. Typically, the Postal Service obtains the unit costs from a special study

conducted to estimate the cost of a specific operation or group of operations or it uses a unit cost from the CRA for an analogous service and operation. After it has put together the applicable unit costs, the Postal Service obtains volume estimates to apply to them. If the service is already operational, actual volume estimates may be available, as they are for each of the initiative cost models.

All the models incorporate the approach described above. They appear to account for relevant operations and the unit costs estimates appear to be reasonable. For these reasons, the Commission uses these costs.

(5) Analysis of Unit Attributable Costs

The Postal Service computes estimates of Attributable Cost per Piece (ACP) for many categories of inbound and outbound International Mail for its annual "International Cost and Revenue Analysis" (ICRA) reports. These estimates of ACP are the result of complex calculations performed on uncertain values for parameters and variables derived from a number of Postal Service data systems and special studies. In this respect the international ACPs differ little from their domestic counterparts in the Service's annual CRA Report.

Like the estimates of ACPs for domestic subclasses, the ACPs for International Mail categories are subject to two kinds of errors. These are known as sampling and non-sampling errors. Sampling errors arise because, as a practical matter, it is usually possible to observe only a small fraction of the mail as it is collected, processed, transported and delivered by the Postal Service. Non-sampling errors arise if the sampling processes produce errors with an expected value that is unequal to zero; that is, if repeated applications of the sampling processes do not leave errors with an average of zero. Therefore, non-sampling errors cause unwanted biases in the value of the parameters or variables being sampled.

Eliminating non-sampling errors is one of the objectives of good sampling design and statistical methodology. Some sampling error, on the other hand, is inevitable. It can be reduced by taking larger samples but can only be eliminated by sampling all of the mail. Consequently, a prudent user of the Postal Service's estimates of ACP would want to have a measure of the likely size of the sampling errors that these estimates inevitably contain.

The coefficient of variation (CV) for the attributable cost per piece (ACP) of a subclass or category of mail is a general-purpose measure of the accuracy of the estimated ACP. The CV is defined as the ratio of the standard deviation of the estimation error divided by the estimate of ACP. It is usually expressed as a percent. As a rule of thumb, plus-and-minus two times the CV gives the interval around the estimate of ACP within which the unknown true value of ACP will fall with 95 percent confidence. For example, a CV of 4 percent for an estimated ACP of $1.00 means that one can be 95 percent certain that the true value of ACP will lie within the range between $0.92 and $1.08.

Table III-2 displays approximate values of the CVs for the ACPs of the major categories of inbound and outbound International Mail. The calculations have been made using an approximation formula derived in Appendix D and from estimates of ACPs and CVs for the components of the formula provided to the Commission by the Postal Service.

The column labeled "ICRA Cost per Piece" is the ACP for the corresponding category of mail as it appears in the Service's 1998 ICRA report where it is referred to as "unit volume-variable cost". "Revenue per Piece" is also as shown in the 1998 ICRA. "Percentage Cost Coverage" is the ratio of revenue to attributable cost expressed as a percent. The overall CVs for the fifteen major categories of inbound and outbound International mail are shown in the column labeled "CV of Cost per Piece". These overall CVs are derived directly from CVs for the various cost components and volume

as shown in Appendix D. Finally, the column labeled "Coverage t-value" on the far right holds t-values for statistical tests of hypotheses that the coverage is greater or less than100 percent.

The t-values are defined as the Percent Cost Coverage minus 100 divided by the CV of Cost per Piece. The t-value is positive if the coverage is greater than 100 percent, as is the case for most categories of International Mail. A positive t-value is used to determine if there is any significant probability that actual coverage is less than 100 percent. Mail categories with cost coverages of less than 100 percent have negative t-values. For these categories the t-value is used to determine if there is any significant probability that the actual coverage is above 100 percent.

TABLE III-2 COST PER PIECE, REVENUE PER PIECE AND COEFFICIENTS OF VARIATION FOR INTERNATIONAL MAIL

Summary International Mail Category	ICRA Cost per Piece ($)	Revenue per Piece ($)	Pct. Cost Coverage	CV of Cost per Piece	Coverage t-value
Outbound:					
Letters and letter packages	0.538	0.886	164.68%	3.00%	21.53
Postcards, postal cards	0.324	0.497	153.40%	6.00%	8.89
International Priority Airmail	0.418	0.742	177.51%	1.80%	43.12
Air AO	3.09	4.328	140.06%	4.50%	8.91
Air Parcel Post	23.064	29.252	126.83%	5.07%	5.29
Express Mail International Service	16.688	26.709	160.05%	3.20%	18.78
Surface AO	2.453	2.037	83.04%	8.63%	-1.96
Surface Publishers Periodicals	1.254	1.054	84.05%	2.60%	-6.13
International Surface Airlift	0.683	0.71	103.95%	0.37%	10.61
Surface Parcel Post	20.768	24.917	119.98%	9.42%	2.12
Inbound:					
Surface LC/AO	1.119	0.784	70.06%	9.76%	-3.07
Surface Parcel Post	4.644	7.821	168.41%	21.35%	3.20
Air LC/AO	0.305	0.278	91.15%	7.70%	-1.15
Express Mail International Service	7.874	8.008	101.70%	53.54%	0.03
Air Parcel Post	5.316	9.137	171.88%	17.49%	4.11

The calculated CVs are approximate values for several reasons. First, ACP is a non-linear function of various estimates of volume-variabilities, distribution key shares and mail volumes produced by the Postal Service's data systems and special studies. For this and other reasons, the formula used to compute the overall CV for each category of mail from the CVs of its components can provide only a close approximation. Second, some of the CVs of the sampling statistics used in the formula are missing from the Service's responses to the Commission's information requests. In particular, there are no CVs for any cost pool volume-variabilities. These variabilities are all assumed to be equal to one and their CVs are assumed to be zero. It is

frequently the case that the CVs for distribution key shares and mail volumes are reported for aggregations of more than one category of mail, or in other ways that do not exactly match the ICRA report. For example, the cost pool definitions used to report ACP in the ICRA do not exactly match the cost categories for which the Service has reported CVs for the IOCS distribution keys. These and other defects in the data have been overcome by using proxies and by making other assumptions as needed to use whatever data has been supplied. Inevitably, the results of applying the formula, which follows the category definitions used in the ICRA, are approximations. The specific assumptions made to apply the approximation formula and the details of the calculations are described in Appendix D. The actual calculations were performed within a Lotus 1-2-3 worksheet.

The calculations of the overall CVs for Cost per Piece have been made under the assumption that all of the necessary estimates of volume-variabilities, distribution key shares and mail volumes are free of any biases that might be caused by non-sampling errors. The use of this assumption to calculate CVs does not mean that the Commission believes that Postal Service estimates are completely free of non-sampling errors. It means only that, if non-sampling errors are present, their effects are unknown. In Appendix D it is shown that correcting for an additive bias in most of the estimates would not strongly affect the CVs.

Table III-2 shows that for most categories of International Mail the Postal Service has collected cost and volume data with sufficient accuracy to allow statistically significant conclusions to be drawn regarding the coverage of ACP by revenues per piece as shown in the 1998 ICRA. The exceptions to this finding are inbound LC/AO, and inbound International Express Mail Service.[6] The cost coverages shown for these services are not statistically meaningful since it is not possible to reject with 95 percent

[6] These findings apply to the estimates of ACP found in the 1998 ICRA and not to the Service's estimates of Revenue per Piece which are regarded as accurate for this analysis.

confidence the null hypothesis that the actual cost coverage (the cost coverage without the sampling error) is greater or less than 100 percent.

The column of t-values provides the evidence of statistical significance. The critical value of "t" for a one-tailed test with an assumed confidence level of 95 percent is 1.645. For this test a t-value greater than 1.645 means that the Postal Service's measurement of ACP is sufficiently accurate to leave it more than 95 percent certain that revenue per piece covers the actual (but unknown) true ACP. Conversely, a t-value of less than –1.645 means that the measurement of ACP is accurate enough to make it more than 95 percent certain that revenue per piece will fall short of ACP. Higher (in absolute value) t-values make it possible to draw more precise conclusions about coverage. For example, the t-value of 21.53 for outbound letters and letter packages shows that the coverage for this category of mail is much greater than the margin needed to establish statistical significance. T-values near 2.00, such as those for outbound Surface AO and outbound Surface Parcel Post, show that the coverages for these categories fall much closer to the boundaries that mark statistical significance. Nevertheless, there is less than a 5 percent chance that the cost of outbound "Surface AO" is covered by revenue, or that the cost of outbound "Surface Parcel Post" is not covered.

Only inbound Air LC/AO and inbound International Express Mail Service have t-values with absolute values of less than 1.645. The cost coverage for inbound Air LC/AO is only 91.15 percent, however, the t-value of –1.15 shows that there remains a modest probability of around 12.5 percent that revenue per piece actually covers ACP. For inbound International Express Mail Service the cost coverage of 101.70 percent is so close to 100 percent that it has little statistical significance. The t-value of 0.03 means that the probability that revenue per piece actually covered ACP is only about 50.9 percent while the probability that revenue fell short of attributable cost is almost as large at 49.1 percent.

On the whole, the Commission is able to more accurately estimate ACP on outbound categories of International Mail than inbound categories. This occurs because a large share of the cost of outbound mail consists of international transportation costs and terminal dues while these components are completely absent from the ACPs for inbound mail. The Service's data systems can identify international transportation costs and terminal dues by mail category fairly precisely as shown by the low CVs for these cost categories in the table in Appendix D. On the other hand, the Service's data systems do a poor job of identifying the shares of domestic costs for most categories of International Mail as described by the much higher CVs for the domestic cost categories entitled "Mail Processing," "Delivery," "Other," and, especially, "Domestic Transportation".

The approximation formula makes evident the fact that the CV associated with the ICRA estimates of volume are particularly important as determinants of the overall CV of ACP for a category of mail. Fortunately, the Postal Service's estimates of volume by International Mail category are good, even for categories with relatively few pieces. The highest CV for volume, 6.67 percent, is reported for outbound surface AO, a fairly small category of mail. The largest categories of international mail are inbound and outbound letters, cards and letter packages. The ICRA volumes for these categories appear to be accurately estimated as evidenced by their volume CVs of 2.01 percent outbound and 2.50 percent inbound.

IV. PRESENTATION OF COST, VOLUME, AND REVENUE DATA

This section presents the volumes, costs, and revenues for international mail. As noted elsewhere, the costs underlying the calculated cost coverages (*i.e.,* the ratio of revenue to attributable cost) reflect the methodology the Commission has applied in setting current rates for domestic subclasses. Generally, this methodology results in attributable costs that are somewhat higher than the method that the Postal Service advocates, and leads directly to lower cost coverages than the Postal Service would obtain.

The Postal Service has introduced a cost for international mail which has no counterpart in domestic mail, namely, the incremental costs for international mail service as a whole. As noted earlier, this includes the cost of the International Business Unit and the difference in settlement costs between booked costs and imputed costs (booked costs are higher than imputed). This is discussed further in Section IV.A and Appendix F. It should be noted that on June 7, 1999, the Postal Service submitted an ICRA reflecting its preferred cost methodology. That report incorporated changes to its previous methods for estimating international transportation and settlement costs not reflected in the ICRA provided to the Commission on March 15, 1999 or the revised PRC Version submitted on June 11, 1999. Because of time constraints, the Commission has not been able to evaluate the merits of these new estimation methods. For this reason, the data presented below reflect the March 15, 1999, FY 1998 ICRA Report — PRC Version.

A. Aggregate Data

International mail is separated between outbound and inbound services. The Postal Service states it designs rates for each of the outbound services so as to recover all domestic handling and transportation costs, international transportation costs,

settlement costs, and a markup. Source 7, Response to Item 18. For inbound mail, the Postal Service recovers costs through settlement charges. For LC/AO inbound mail from UPU countries, the Postal Service agrees to accept as payment a terminal dues rate that is based on a worldwide average cost. This rate does not fully compensate the Service for the cost it incurs delivering inbound mail. There are important constraints on the ability of the Postal Service to make terminal dues compensatory. The Service is one of many voices at the UPU Congress. Further, because the UPU Congress only meets every five years, terminal dues rates generally remain in effect for five years. For these reasons, the Service seeks to obtain cost based bilateral agreements with other countries. Despite bilateral agreements, as Table IV-1 shows, inbound mail still does not pay its own way.

TABLE IV-1
SUMMARY OF FY 1998 REVENUE AND ATTRIBUTABLE COST
FOR OUTBOUND AND INBOUND INTERNATIONAL MAIL
(Amounts in Thousands)

Category	Revenue ($) (1)	Attributable Cost ($) (2)	Incremental Cost ($) (3)	Total Attributable Cost ($) (4)	Contribution ($) (5)=(1)-(2)	Cost Coverage (6)=(1)/(4)
Outbound Mail	1,332,796	1,020,520	-	1,020,520	312,276	130.6%
Inbound Mail	282,311	287,379	-	287,379	(5,068)	98.2%
Subtotal	1,615,107	1,307,899	-	1,307,899	307,208	123.5%
Int'l Mail Incremental Cost	-	-	122,445	122,445	(122,445)	-
Grand Total	$1,615,107	$1,307,899	$122,445	$1,430,344	$ 184,763	112.9%

Source: Table IV-2 – Reflects ICRA Report released 6/11/99

In contrast, Table IV-1 shows that outbound international mail makes a contribution to the Postal Service's institutional costs. There are a number of factors that affect the amount of this contribution. One is that unlike inbound LC/AO mail, the Postal Service has direct control over the rates that it charges for outbound LC/AO mail.

Another is that terminal dues charged to the Postal Service for LC/AO mail are low relative to what it costs industrialized destinating countries to deliver this mail. As a net exporter to these countries, the Postal Service is in a position to benefit from the relatively low terminal dues that other industrialized countries are currently paid to deliver LC/AO mail.

As Table IV-2 shows, the United States exports about 1½ times as much mail as it imports. Low terminal dues help keep the total unit cost of the mail that the Postal Service exports low, thereby increasing the Postal Service's ability to set rates on that mail which generate net revenue. Moreover, the Postal Service's cost of delivering inbound mail is relatively low, which minimizes the losses to the Postal Service from delivering inbound mail.[7] Low terminal dues combined with the Postal Service's position as a substantial net exporter of international mail are important factors making it easier for the Postal Service to set rates that generate the net revenue it seeks from international mail.

In FY 1998, the cost coverage for outbound mail was 130.6 percent while the cost coverage for inbound mail was 98.2 percent. Adding the figures for inbound mail to the figures for outbound mail reduces cost coverage from 130.6 percent to 123.5 percent. The reduction in contribution to institutional cost is $5 million.

Inbound mail is not the only drag on international mail cost coverage; incremental costs also reduce cost coverage. The incremental costs of international mail service as a whole are costs which cannot be causally associated with specific international services based on the information currently available, but that would be eliminated if all international services were eliminated. Some of these costs, those

[7] The Postal Service's unit operating costs have historically been among the lowest of the postal administrations of the 21 most industrialized countries. Source 12, p. 100. This implies that for most of the industrialized world, terminal dues are less than the economic cost of delivering inbound mail.

associated with the International Business Unit, cannot even be traced exclusively to outbound mail or to inbound mail. The incremental cost for which international mail service as a whole is responsible is included in the calculation of the overall contribution to institutional cost and the cost coverage of international mail as a whole. As a result, the cost base for determining the cost coverage for international mail as a whole is greater than the sum of the cost bases of the individual international services. Using this approach, the contribution of international mail as a whole is reduced from $307 million to $185 million, and its cost coverage declines from 123.5 percent to 112.9 percent. See Table IV-1.

For comparison purposes, the systemwide cost coverage for domestic and international mail combined in FY 98 was 158.3.

B. Individual Services

This section highlights some of the FY 1998 results for individual services. The section discusses outbound and inbound mail separately and adds some further comments and observations in the last subsection.

In preparing this report, the Commission has not attempted to assemble a list of international mail products or services comparable to the domestic mail classification schedule. The list of international services in this report is not grouped according to homogeneous cost or demand characteristics designed to facilitate comparison of their cost coverages and rates with those of other international services, or with corresponding domestic mail services.

There are several factors that make compiling such a list difficult for international services. The structure of international mail classifications is, in large measure, determined by the Conventions of the UPU, and must be taken largely as given. The categories of mail defined by the UPU are broader than the corresponding subclasses of domestic mail in terms of content and service level, and therefore less homogeneous

in terms of cost and demand. AO mail, for example, includes mail that is similar to domestic Standard A, Standard B, and Periodicals mail. Service levels for the various categories of LC/AO mail are somewhat difficult to compare, either with other international categories or with domestic services. Some AO service is "surface" (non-priority) and some is "air" (priority) mail, while the corresponding domestic services generally receive non-priority service. Some AO mail (ISAL) is a hybrid of priority and non-priority service (receiving priority handling and air transportation within the U.S., but non-priority handling and ground transportation within the destinating country). A final factor making it difficult to compare the rates and cost coverages of international and domestic services is that terminal dues for LC/AO mail are not closely aligned with the cost of delivering such mail as they reflect a global average cost, and the level of terminal dues is sometimes below the economic cost of delivering mail in the destinating country.

The Postal Service submitted two documents that may assist the reader to more fully understand the scope of this issue. The first is a chart attempting to relate international and domestic services, Source 7, response to item 23, and the second is the Postal Service's description of how it develops international mail rates, Source 7, response to item 18. These documents are Appendix G.

(1) Outbound Mail

Table IV-2 summarizes revenue and cost data for each international mail service.

TABLE IV-2
SUMMARY OF REVENUE, VOLUME, AND COSTS FOR OUTBOUND AND INBOUND INTERNATIONAL MAIL
(COSTS REFLECT COMMISSION ATTRIBUTION METHODOLOGY)
(Amounts in Thousands)

U.S. Total International Mail Category	Volume (1)	Revenue (2)	Volume Variable Cost (3)	Product Specific Cost (4)	Attributable Cost (5)=(3)+(4)	Contribution (6)=(2)-(5)	Unit Revenue (7)=(2)/(1)	Unit Attributable Cost (8)=(5)/(1)	Unit Contribution (9)=(6)/(1)	Cost Coverage (10)=(2)/(5)
OUTBOUND MAIL										
Surface										
1 Printed Matter & Small Packets, excl. ISAL & Per.	28,215	$ 57,461	$ 69,326	$ -	$ 69,326	$ (11,865)	$ 2.037	$ 2.457	$ (0.421)	82.9%
2 Periodicals	65,082	$ 68,615	$ 81,708	$ -	$ 81,708	$ (13,093)	$ 1.054	$ 1.255	$ (0.201)	84.0%
3 Parcel Post	2,312	$ 57,607	$ 48,107	$ -	$ 48,107	$ 9,500	$ 24.917	$ 20.808	$ 4.109	119.7%
4 Int'l Surface Airlift	163,587	$ 116,120	$ 111,739	$ -	$ 111,739	$ 4,381	$ 0.710	$ 0.683	$ 0.027	103.9%
5 ValuePost/Canada	-	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	0.0%
6 Subtotal, Surface	259,196	$ 299,803	$ 310,880	$ -	$ 310,880	$ (11,077)	$ 1.157	$ 1.199	$ (0.043)	96.4%
Air										
7 Letters and Letter Packages	510,053	$ 451,943	$ 275,166	$ -	$ 275,166	$ 176,777	$ 0.886	$ 0.539	$ 0.347	164.2%
8 Postcards, Postal Cards, and Aerogrammes	63,010	$ 31,299	$ 20,477	$ -	$ 20,477	$ 10,822	$ 0.497	$ 0.325	$ 0.172	152.8%
9 Printed Matter and Small Packets (AO)	45,017	$ 194,833	$ 139,277	$ -	$ 139,277	$ 55,556	$ 4.328	$ 3.094	$ 1.234	139.9%
10 International Priority Airmail Service	52,843	$ 39,219	$ 22,101	$ -	$ 22,101	$ 17,118	$ 0.742	$ 0.418	$ 0.324	177.5%
11 Bulk Letter Service to Canada	-	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	0.0%
12 Parcel Post	4,240	$ 124,029	$ 97,897	$ -	$ 97,897	$ 26,132	$ 29.252	$ 23.089	$ 6.163	126.7%
13 Express Mail International Service	4,694	$ 125,363	$ 78,366	$ -	$ 78,366	$ 46,997	$ 26.707	$ 16.695	$ 10.012	160.0%
14 Subtotal, Air	679,857	$ 966,686	$ 633,284	$ -	$ 633,284	$ 333,402	$ 1.422	$ 0.931	$ 0.490	152.6%
Initiatives										
15 Global Priority Mail	4,219	$ 30,265	$ 19,973	$ 18,913	$ 38,886	$ (8,621)	$ 7.174	$ 9.217	$ (2.043)	77.8%
16 Global Package Link	1,513	$ 23,630	$ 20,484	$ 6,151	$ 26,635	$ (3,005)	$ 15.618	$ 17.604	$ (1.986)	88.7%
17 Direct Entry/Inbound	16,837	$ 3,351	$ 3,115	$ -	$ 3,115	$ 236	$ 0.199	$ 0.185	$ 0.014	107.6%
18 International Customized Mail	10,433	$ 9,061	$ 7,720	$ -	$ 7,720	$ 1,341	$ 0.868	$ 0.740	$ 0.129	117.4%
19 Subtotal, Initiatives	33,002	$ 66,307	$ 51,292	$ 25,064	$ 76,356	$ (10,049)	$ 2.009	$ 2.314	$ (0.304)	86.8%
20 Total Outbound	972,055	$ 1,332,796	$ 995,456	$ 25,064	$ 1,020,520	$ 312,276	$ 1.371	$ 1.050	$ 0.321	130.6%
INBOUND MAIL										
21 Surface LC/AO	46,735	$ 36,637	$ 52,574	$ -	$ 52,574	$ (15,937)	$ 0.784	$ 1.125	$ (0.341)	69.7%
22 Surface Parcel Post	2,142	$ 16,752	$ 9,987	$ -	$ 9,987	$ 6,765	$ 7.821	$ 4.662	$ 3.158	167.7%
23 Surface Subtotal	48,877	$ 53,389	$ 62,561	$ -	$ 62,561	$ (9,172)	$ 1.092	$ 1.280	$ (0.188)	85.3%
24 Air LC/AO	587,926	$ 163,179	$ 180,632	$ -	$ 180,632	$ (17,453)	$ 0.278	$ 0.307	$ (0.030)	90.3%
25 Express International Mail Service	3,763	$ 30,137	$ 29,742	$ -	$ 29,742	$ 395	$ 8.009	$ 7.904	$ 0.105	101.3%
26 Air Parcel Post	2,192	$ 20,029	$ 11,707	$ -	$ 11,707	$ 8,322	$ 9.137	$ 5.341	$ 3.797	171.1%
27 Air Subtotal	593,881	$ 213,345	$ 222,081	$ -	$ 222,081	$ (8,736)	$ 0.359	$ 0.374	$ (0.015)	96.1%
28 Direct Entry/Inbound	301	$ 116	$ 23	$ -	$ 23	$ 93	$ 0.385	$ 0.076	$ 0.309	504.3%
29 Global Parcel Services	1,049	$ 2,552	$ 2,714	$ -	$ 2,714	$ (162)	$ 2.433	$ 2.587	$ (0.154)	94.0%
30 Other 2/		$ 12,909			$ -	$ 12,909	-	-	-	-
31 Total Inbound	644,108	$ 282,311	$ 287,379	$ -	$ 287,379	$ (5,068)	$ 0.438	$ 0.446	$ (0.008)	98.2%
32 International Service Incremental Cost	-	-	-	$ 122,445	$ 122,445	$ (122,445)	-	-	-	-
33 Total International Mail	1,616,163	$ 1,615,107	$ 1,282,835	$ 147,509	$ 1,430,344	$ 184,763	$ -	$ -	$ -	112.9%

Source: FY 1998 International Cost and Revenue Analysis Report-PRC Version, June 11, 1999, pp. A-1, A-2, A-6, and A-7; USPS Response to Fifth Notice, Item 1.

Note: International Service Incremental Costs reflect (1) the cost of the International Business Unit and (2) the difference in settlement charge claims. These costs are incremental to international service as a whole, i.e., eliminating any one individual service or any group of services would have no effect on the amount of these costs.

1/ The Postal Service did not provide separate cost data for these services, but it did provide separate revenues and volumes. The revenues and volumes for ValuePost/Canada cannot be separated between surface periodicals and all other surface AO. Therefore, the costs, revenues, and volumes for ValuePost remain in surface periodicals and all other surface AO. The revenues and volumes for Bulk Letter Service to Canada can be separated from the data for Air Letters. Since the costs for Bulk Letters to Canada would remain in the cost for Air Letters, the unit cost, contribution, and cost coverage for Air Letters would be misstated. For this reason, the data for Bulk Letters to Canada remains in the Air Letter category.

2/ The revenue amount reflects Internal Air Conveyance Dues and Transit revenue, corresponding costs are included in inbound costs by service.

It shows that of the fourteen outbound services for which the Commission received separate cost data, at least four are noncompensatory:[8] (1) Surface Printed Matter and Small Packets; (2) Surface Periodicals; (3) Global Priority Mail; and, (4) Global Package Link. During FY 1998, Surface Printed Matter and Surface Periodicals experienced cost coverages of 83 percent and 84 percent, respectively. According to the Postal Service, the contribution was positive for Fiscal Years 1993 to 1995, but was slightly negative in FY 1996, correlating with the increase in terminal dues that went into effect in the second quarter. The negative contribution continued in FY 1997 and FY 1998. The Postal Service acknowledged that because of these poor results, it planned an average increase of about 15 percent for these services. The increase became effective May 30, 1999. The Postal Service also stated that it might have to raise these rates still more in the future. Source 7, Response to Item 12.

Global Package Link had a cost coverage of 88.7 percent in FY 1998 with attributable costs exceeding revenues by $3 million. The Service reported that the businesses using this service were adversely affected by the downturn of the global economy and the corresponding decrease in value of some foreign currencies. The economic slowdown hurt the Postal Service's business customers because there were substantially fewer overseas orders and, accordingly, fewer packages were mailed. The Postal Service believes that revenue will cover cost in FY 1999 because (1) it has increased rates by about 9 percent on average; and, (2) it expects to achieve cost reductions in this area. The Postal Service did not provide any specific information on the expected cost reductions. Source 7, Response to Item 12.

Global Priority Mail shows a cost coverage of 77.8 percent for FY 1998. The Postal Service observes that revenues covered volume variable costs but not the

[8] The Postal Service did not provide separable data for Bulk Letter Service to Canada and ValuePost/Canada. However, based on FY 97 results it implemented rate increases that did not become effective until well into FY 99.

combination of volume variable and product specific costs. Revenues fall short of costs by $8.6 million when product specific costs are included. The Postal Service believes the contribution to institutional costs will improve because of expected reductions in advertising expense that accounted for $16 million of the $19 million product specific cost in FY 1998 and because of the 14 percent average rate increase that was effective in December, 1998. Source 7, Response to Item 12.

ValuePost/Canada and Bulk Letter Service to Canada are services with very little volume. The Postal Service provided ValuePost/Canada's share of the revenue and volume of Surface AO overall, but did not provide ValuePost/Canada's share of the revenue and volume of Surface AO's component parts (periodicals and all other). The revenues and volumes of Bulk Letter Services to Canada remain subsumed within the revenues and volumes that the Postal Service provided for Air Letters. The Postal Service did not provide separate attributable cost estimates for either of these services.

Early in the § 3663 information gathering process, the Commission asked the Postal Service to identify the FY 1998 costs attributable separately to ValuePost/Canada and Bulk Letter Service to Canada. See Order No. 1226 at 3 and Attachment. The Postal Service stated that it did not track costs separately for these services. Comments of the United States Postal Service on Order No. 1226, filed January 29, 1999, at 3. Subsequently, the Postal Service indicated that it bases rates for these services on costs estimated separately for each service. See Appendix A, Source 7. Twice, the Commission requested the FY 1998 attributable cost estimates for each of these services that the Postal Service would use to set rates for those services. Order No. 1240, Item 3; Order No. 1244, Item 6. Twice, the Postal Service did not directly respond. See Source 3, Item 3, filed May 17, 1999, and Source 8, Item 6, filed May 27 1999.

In Order No. 1251, the Commission described specific calculations that it suspected the Postal Service applied to FY 1997 data to estimate the attributable costs

for ValuePost/Canada and Bulk Letter Service to Canada that the Postal Service used when it designed the rate increases for those services that took effect May 30, 1999. The Commission asked the Postal Service to confirm that it used the calculations described, and to provide equivalent calculations for FY 1998. The Postal Service's response to Order No. 1251 confirmed that it used the method of calculating FY 1997 costs that the Commission described, but said that the data needed to perform equivalent calculations for FY 1998 were not available. For this reason, the Commission has not been able to report separate attributable cost estimates for these services for FY 1998, and therefore can not compute cost coverages for these services.

(2) Inbound Mail

As shown on Table IV-2, inbound mail, as a whole, had a cost coverage of 98.2 percent in FY 1998 with revenue falling short of attributable cost by over $5 million. The losses are directly traceable to Surface LC/AO and Air LC/AO. These services combined to lose $33 million. The difference in cost coverage is a result of how settlement charges (terminal dues, etc.) are established.

UPU terminal dues rates are based on global average cost and are noncompensatory for the U.S. Postal Service. The U.S. Postal Service has entered into separate agreements with Canada and the European Bilateral group, presumably, to obtain rates that cover costs. However, the remaining UPU countries account for 42 percent[9] of inbound LC/AO and the Postal Service still did not achieve a compensatory cost coverage for inbound LC/AO as a whole. The Commission was not able to satisfactorily disaggregate costs by terminal dues regime because the costs provided by the Postal Service are averaged across regimes.

[9] Based on Postal Service Response to Order No. 1236, Item 15.

Unlike terminal dues, inward land charges for parcel post and imbalance charges for EMS are not based on a global average, but reflect country-specific costs. For parcel post, each country publishes annual rates reflecting a per-piece and per-kilogram rate. The U.S. Postal Service also has bilateral agreements with ten countries. As Table IV-2 shows, the unit revenues exceed the unit attributable costs for both categories of parcel post. Surface parcel post and air parcel post show cost coverages of 167.7 percent and 171.1 percent respectively. Achieving a positive outcome for EMS should not pose a problem as the Postal Service is free to enter into bilateral agreements with other countries in which rates can be cost based. In fact, the U.S. Postal Service has agreements with 188 countries. Source 9, pp. 5 and 6. The cost coverage for inbound EMS is 101.3 percent.

(3) Other Comments

The Postal Service provided the distribution of the major categories of outgoing international mail between Household and Non-Household mailers. Table IV-3 arrays this information along with revenue and cost data.

TABLE IV-3
COMPARISON OF REVENUE AND COST DATA
AND PERCENTAGE DISTRIBUTION OF ORIGINATING VOLUME
FOR SELECTED INTERNATIONAL MAIL CATEGORIES

Mail Categories	Percentage Non-Household (1)	Distribution: Household (2)	Revenue ($) (3)	Attributable Cost ($) (4)	Cost Coverage (5)
Mostly NHH					
EMS	91%	9%	125,363	78,366	160.0%
ISAL	100%	0%	116,120	111,739	103.9%
IPA	100%	0%	39,219	22,101	177.5%
Air AO	65%	35%	194,833	139,277	139.9%
Air CP	60%	40%	124,029	97,897	126.7%
Surface AO	90%	10%	126,076	151,034	83.5%
Subtotal			725,640	600,414	120.9%
Mostly HH					
Air LC	45%	55%	483,242	295,643	163.5%
Surface CP	11%	89%	57,607	48,107	119.7%
Subtotal			540,849	343,750	157.3%

NHH = Non-Household; HH = Household
Source: Postal Service Response to Second Notice, Item 21 & Table IV-2

The weighted average cost coverage for the two categories with the highest proportion of Household mail is 157.3 percent. For the six categories of mail with the highest proportion of non-household mail, the cost coverage is 120.9 percent. The largest volume category, Air Letters and Cards, which contains 55 percent household mail (315 million pieces),[10] has the second highest cost coverage at 163.5 percent. The second largest volume category is ISAL mail (164 million pieces), which contains no household mail. It has a cost coverage of 103.9 percent.

[10] 573 million pieces from Table II-1 times 55 percent from Table IV-3.

Appendices

LIST OF APPENDICES

Appendix A	List of Reference Sources
Appendix B	Outbound International Services
Appendix C	Measuring the Costs, Revenues and Volumes of International Mail
Appendix D	Derivation of Approximations for Attributable Cost Per Piece (ACP) and Its Coefficient of Variation (CV)
Appendix E	Outbound Regional Data
Appendix F	The Postal Service's Revised Treatment of International Air Transportation Costs and the Settlement Difference
Appendix G	Reference Material – Postal Service Views

LIST OF REFERENCE SOURCES

Source No.	Reference Documents
1	Workpaper 1B, International Cost and Revenue Analysis, FY 1998, Summary Description and Documentation, Volume 2, Technical Description
2	Exhibit 3C, SIRVO – MIDAS Interface, Training Guide, February, 1996
3	USPS Response to Third Notice of International Mail Data Requirements, Order No. 1240
4	Exhibit 3B, System for International Revenue and Volume/Inbound, Reference Manual, February, 1994
5	Workpaper 1E, International Cost and Revenue Analysis, FY 1998, Summary Description and Documentation, Appendices – Part 3 of 6
6	File: ICRAPRC4.XLS; Sheet: TRACS Input; Cells B1 to CK38.
7	USPS Response to Second Notice of International Mail Data Requirements, Order No. 1236
8	USPS Response to Fourth Notice of International Mail Data Requirements, Order No. 1244
9	Billing, payment, and Accrual Process for Terminal Dues and International Transportation Cost (Paper attached to FY 1998 International Cost and Revenue Analysis Report – Postal Service Version)
10	Workpaper 1H, International Cost and Revenue Analysis, FY 1998, Summary Description and Documentation, Appendices – Part 6 of 6
11	USPS Response to Fifth Notice of International Mail Data Requirements, Order No. 1246
12	Cohen, et al., A Cross Sectional Comparison and Analysis of Productivity for 21 National Postal Administrations, Printed in Managing Change in Postal and Delivery Industries, edited by Crew and Kleindorfer, Kluwer Academic publishers, 1997

13 USPS electronic workpapers, File: ICRA98IB.XLS, Sheets IPK981 and IPK982

14 Postal Operations Council of the Universal Postal Union, World Round Table on Terminal Dues, Geneva, 3 and 4 February 1999, page 18 (CEPT TR 1999.1-Doc2)

OUTBOUND INTERNATIONAL SERVICES

SURFACE

Printed Matter and Small Packets (AO)

Printed matter includes regular printed matter such as advertising circulars and catalogues, small packets (gifts, samples, merchandise), books and sheet music, and publishers' periodicals. Printed matter has two levels of service — surface and air. Surface printed matter is a non-priority service. Rates are based on weight. There are separate rates to Canada, Mexico, and the rest of the world, reflecting differences in terminal dues and other settlement regimes, and transportation costs. Surface printed matter has different rates for three subcategories— Regular Printed Matter, Books and Sheet Music, and Publishers Periodicals.

Publishers' Periodicals

Publishers' Periodicals is offered only to publishers and registered newsagents for mailings that would qualify for the domestic publishers' periodicals classification if destined within the United States.

International Surface Airlift (ISAL)

ISAL is a bulk mailing service for the delivery of publications, advertising mail, catalogs, directories, other printed matter, and small packets. Mailers must meet a 50-pound minimum mailing requirement and presort mail by country. ISAL costs less than airmail, but is much faster than surface AO. Per-piece and per-pound rates are charged. There are different rates for the full service, gateway, and direct shipment

options. Under the full service option, ISAL receives air transportation to the domestic gateway city, where it is flown to the destinating country and entered into that country's surface mail system for delivery. Under the gateway option, customers receive a reduced rate for entering ISAL shipments at designated U.S. acceptance cities. An ISAL mailer with a minimum of 750 pounds addressed to each destinating country may receive a direct shipment rate if direct transportation from a gateway city can be arranged ahead of time. Rates differ by region, reflecting differences in terminal dues regimes and transportation costs.

ValuePost/Canada

Value/Post Canada is an ISAL-equivalent service that reflects the terminal dues that apply to mail exchanged with Canada Post. There are distinct rates for letters, and for flats. There is a per-piece charge for letters up to one ounce, and for flats up to five ounces. Above these thresholds, both piece and pound charges apply.

Parcel Post

International parcel post is similar to domestic parcel post. Generally, anything other than personal correspondence may be mailed parcel post. Surface parcel post is a non-priority service comparable to domestic zone-rated parcel post. There is a maximum weight limit that varies from 11 to 70 pounds depending on the destinating country. Single-piece rates are charged. There are different rates for mail destined to Canada, Mexico, and five country groups, reflecting differences in transportation costs and inward land charges.

M-Bag Service

M-Bag service allows a mailer to prepare a direct sack of printed matter weighing between 11 pounds and 66 pounds to a single address. A reduced terminal dues rate of 0.653 SDR/kg applies that reflects its reduced sorting costs.

AIR

Air Letters and Cards

Air LC consists of personal correspondence, statements of account, and other business-oriented transactions mail. Mailers are typically individuals, households, and small business enterprises. Single-piece rates are charged. Air LC is offered as a universal service. Rates are weight-based and unzoned, but there are different rates to Canada, Mexico, and the rest of the world. Air letters receive First-Class Mail service in the United States, travel by the most expeditious transportation mode available, and receive airmail or priority treatment in the destinating country.

Aerogrammes and Post Cards

An aerogramme consists of a single page that folds into a light-weight, self-sealing envelope. It is designed for personal correspondence. Post cards are not sealed. They are designed for business and personal correspondence. A per-piece rate applies to both. The aerogramme rate is universal. There are different card rates to Canada, Mexico, and the rest of the world.

International Priority Airmail (IPA)

IPA is a bulk air service for LC/AO mail. Per-piece and per-pound rates are charged. Rates differ by region, reflecting differing terminal dues regimes and transportation costs. Under the non-presort option, mailers must meet a minimum ten-pound volume requirement. Under the presort option, mail must be presorted to destinating country. There are three rate groups. A presorted mailing must have a minimum of ten pounds destined to a specific rate group.

Printed Matter and Small Packets (AO)

Air printed matter is a priority service. Rates are based on weight. Rates reflects differences in settlement charge regimes and transportation costs. There are different rates to Canada, Mexico, the rest of the western hemisphere, Asia and Africa, and the Pacific Rim.

Bulk Letter Service to Canada

This is a bulk letter service to Canada. Five hundred pieces weighing three ounces or less are needed to qualify for this service. In addition, mailers are required to tray their mail and apply a Canadian post code to each piece. The rates for this service represent a fixed reduction from the Air LC single-piece rate.

Parcel Post

Air parcel post is a priority service comparable to domestic priority mail. There are maximum weight limits that vary by destinating country. Single-piece rates are charged. There are different rates for mail going to Canada, Central America, and the rest of the world.

Express Mail International Service (EMS)

International EMS may consist of almost any type of document or merchandise. It is the fastest of the international services offered by the Postal Service. EMS receives priority handling in the destinating country, by either the local postal administration or by private courier. There are two levels of service — Custom Designed and On Demand. Custom Designed service follows a prearranged schedule. On Demand service does not. Service is provided to 180 countries. Postage is based on weight. There are distinct rates for Canada, Mexico, Great Britain, China, Japan, and five other rate groups.

INITIATIVES

Global Package Link (GPL)

GPL is a bulk mailing system that provides international delivery of packages containing merchandise. GPL is designed to make it easier and less costly for mailers to export goods. The Postal Service provides GPL on a destination country-specific basis to Brazil, Canada, Chile, China (People's Republic of), France, Germany, Hong Kong Special Administrative Region, Japan, Mexico, Singapore, and the United Kingdom.

To qualify for GPL service, a mailer must enter into a service agreement with the Postal Service and send a minimum of 10,000 packages a year. In addition, the mailer must link its information system to that of the Postal Service so that the Postal Service can automatically extract information about each package needed to produce customs forms and package labels and to provide tracking and tracing.

GPL offers premium, standard, and economy service. Service enhancements offered are merchandise return, insurance, customs forms and clearance, and payment of customs duties.

Global Priority Mail (GPM)

GPM is an expedited airmail letter service providing delivery of all items mailable as letters or merchandise up to 4 pounds. GPM items receive priority handling in the United States and in destination countries. Single-piece and volume rates are available. Separate rates are available for small envelope, large envelope, boxes, and Variable Weight Service. Variable Weight Service has a single-piece and a bulk rate. For single-piece rates, the mailer must have a minimum of five or more pieces to one or more GPM countries. To qualify for bulk rates, the mail must be separated by geographic rate zone (Western Europe, Pacific Rim, and Canada).

GPM single-piece variable weight option pieces, GPM flat-rate envelopes, and GPM flat-rate boxes with postage affixed may be deposited wherever Express Mail is accepted. On-call or scheduled pickup service is available in cities where GPM is accepted. GPM pieces mailed at volume rates must be deposited at a business mail acceptance unit authorized to receive GPM.

Global Direct Service

Global Direct Service to or from Mexico, Canada, Brazil, and Great Britain is available only pursuant to a service agreement between the Postal Service and a qualifying mailer. The mailer tenders to the Postal Service items meeting the applicable makeup and preparation requirements for domestic mail in the country of destination. The Postal

Service transports the items to the destination country for entry into its domestic mail system.

To qualify for Mexico Direct, a mailer must have operations in both the United States and Mexico. In addition, the mailer must agree to send at least 10,000 Mexico Direct items during a 60-day period. The charge for this service is $1.01 per pound or fraction of a pound (plus the applicable Mexican domestic postage). To qualify for Global Direct - Canada Admail, a mailer must enter a minimum of 25,000 identical printed matter items that meet the applicable eligibility, makeup, and preparation requirements for Canadian Post domestic Addressed Admail service. The size, weight, and level of sortation of the items being mailed determine the rate of postage.

Global Parcel Services (GPS)

GPS is an inbound parcel delivery service being tested with a limited number of foreign postal administrations. It is described as an inbound mail order fulfillment service. The mail is entered directly into the domestic mailstream, generally as Priority Mail. In FY 1998 GPS was received from only one country.

International Customized Mail (ICM)

ICM service is available only pursuant to an ICM service agreement between the Postal Service and a mailer meeting volume and postage requirements. The mailer must be capable, on an annualized basis, of (1) tendering at least 1 million pounds of international mail to the Postal Service, or (2) paying at least $2 million in international postage to the Postal Service. There are no published rates for ICM.

Several services are available on ICM terms. They are International Surface Airlift (ISAL), ValuePost, and Express Mail Service (EMS). Discounts are negotiated on an individual customer basis. For costing purposes, the ICM portions of each of these services are presented collectively as ICM costs in the initiatives section of the ICRA.

MEASURING THE COSTS, REVENUES AND VOLUMES OF INTERNATIONAL MAIL

This appendix addresses the underlying data sources and the methodology the Postal Service uses to calculate the revenue, pieces, weight, and attributable cost (PRC version) for international mail. The section is organized as follows: (1) outbound revenue, pieces, and weight (RPW); (2) inbound RPW; (3) the attributable costs of standard services; (4) the attributable cost of initiatives; and (5) International Mail Service Incremental Costs. Standard services is a descriptive term used in this appendix to differentiate the traditional or standard international mail services, *e.g.*, air letters and cards, from the new service offerings the Postal Service refers to as initiatives. While the revenues and volumes for the initiatives are collected through the Permit system and other similar census-based systems, their attributable costs are developed using a variety of sources and calculation procedures. The Postal Service also has presented costs it considers to be incremental to International Mail service as a whole. The nature of these costs is discussed in subsection (5) of this Appendix. Responsibility for these costs is discussed in Section IV.

(1) Outbound Revenue, Pieces, and Weight

The Postal Service develops estimates of revenue, pieces, and weight for outbound mail using five different systems: (1) the Permit system; (2) the Electronic Marketing Reporting System (EMRS); (3) the International Business Information System (IBIS); (4) the Corporate Business Customer Information System (CBCIS); and (5) the System for International Revenue and Volume/ Outbound (SIRV/O). Of the five systems, the first four collect census information as part of the Postal Service's accounting process. In FY 1998, they captured 33 percent of all international outbound volume. Source 1, pp. 7-6 to 7-8 and Table C-1. The fifth system, SIRV/O, is a

statistical sampling system designed to collect revenue, pieces, and weight for international mail not incorporated into the Postal Service's accounting systems. SIRV/O, in turn, is supported by the Military and International Accounting and Dispatch System (MIDAS). Source 1, p. 7-3. This is an operating system that tracks all outbound mail. Source 1, p. 7-1. It provides the weight of mail by UPU class, destination country, and transportation mode. MIDAS, therefore, provides a control weight figure for adjusting the sample (SIRV/O) volume to coincide with a direct measure of the actual weight of International Mail. Source 1, p. 7-1 and Source 2, p. 1. SIRV/O accounted for 67 percent of all international outbound mail in FY 1998. Table C-1.

Because some mailers enter their mail at offices that do not have the Permit system in place, the Service supplements its data systems by obtaining census data on revenue, pieces, and weight from special Postmaster reports and from postage statements and account activity reports. Source 1, p. 9-1. The table below shows the distribution of piece volumes by mail category and data source.

Table C-1

DISTRIBUTION OF OUTBOUND VOLUME
BY INTERNATIONAL MAIL CATEGORY AND DATA SOURCE

International Mail Category	Data Source	Piece Volume (000) (1)	Percent Distribution of Volume (2)
OUTBOUND MAIL			
Surface			
Printed Matter & Small Packets, excl. ISAL & Per.	SIRV/O	28,215	2.9%
Periodicals	Permit	65,082	6.7%
Parcel Post	SIRV/O	2,312	0.2%
Int'l Surface Airlift	Permit	163,587	16.8%
ValuePost/Canada	Permit	-	
Subtotal, Surface		**259,196**	26.7%
Air			
Letters and Letter Packages	SIRV/O	510,053	52.5%
Postcards, Postal Cards, and Aerogrammes	SIRV/O	63,010	6.5%
Printed Matter and Small Packets (AO)	SIRV/O	45,017	4.6%
International Priority Airmail Service	Permit	52,843	5.4%
Bulk Letter Service to Canada	Permit	-	
Parcel Post	SIRV/O	4,240	0.4%
Express Mail International Service	EMRS	4,694	0.5%
Subtotal, Air		**679,857**	69.9%
Initiatives			
Global Priority Mail	IBIS/CBCIS	4,219	0.4%
Global Package Link	Permit+	1,513	0.2%
Direct Entry/Inbound	Permit	17,138	1.8%
International Customized Mail	Postage St+	10,433	1.1%
Subtotal, Initiatives		33,303	3.4%
Total Outbound		**972,356**	100.0%
Volume from Sample		652,847	67.1%
Volume from Census Information		319,509	32.9%
Total Outbound		**972,356**	100.0%

Source: FY 1998 ICRA, pp. A-1, A-2, and A-3 and Source 1, pp. 7-6 to 7-8.
Note: Permit + equals Permit system & Postmaster Reports Postage St + equals Postage Statements & Account Activity Reports

Census Information. Table C-1 displays volume data for the 16 outbound international services for which revenue, cost, and volume data are analyzed in this report. These 16 services account for all outbound mail. Census data are gathered on ten of the 16 services that accounted for 319.5 million pieces in FY 1998. Table III-1 shows that the Permit system is used to track seven of those services: (1) Periodicals, (2) ISAL, (3) IPAS, (4) ValuePost/Canada, (5) Bulk Letter Service to Canada, (6) Global Package Link (except for a small portion of the volume), and (7) Direct Entry. These categories account for 94 percent of the census data. The other three services, International Express Mail, Global Priority Mail and International Customized Mail are tracked by other accounting systems that are similar to the Permit system in that they directly collect mailer information on revenue, pieces, and weight on a census basis. Express mail data are collected in the EMRS. GPM data come from the IBIS and CBCIS. The IBIS houses information on four of the five GPM services: small envelope, large envelope, boxes, and variable weight. The Variable Weight Service is composed of a single piece service and a bulk service. The IBIS collects the total RPW data for variable weight service, while the CBCIS collects only the bulk service portion. The single-piece service portion is obtained by subtracting the bulk service totals from the combined service totals. Source 1, p. 7-8.

Most of the volume and revenue data for GPL are contained in the Permit system; however, during FY 1998, there were some customers who entered their mail at postal facilities without the Permit system. For this reason, the Postal Service assembled the revenues and volumes from the Postmaster Reports at the applicable facilities. The same problem arose for the mailers using ICM during FY 1998. The revenues and volumes for this service are developed using postage statements from the specific-facility and account activity reports maintained in the International Business Unit (IBU). Source 1, p. 9-1.

Sample Data. The SIRV/O collects data on the lion's share of total outbound mail volume (652.8 million pieces in FY 1998). Table C-1. It collects RPW data for the

other six services shown in Table C-1: (1) Surface Printed Matter, (2) Surface Parcel Post, (3) Air Letters and Letter Packages, (4) Air Cards and Aerogrammes, (5) Air Printed Matter, and (6) Air Parcel Post. Source 1, p. 7-7. The SIRV/O also collects RPW data for Periodicals, ISAL, and IPAS. The SIRV/O data is used to develop country-specific information, not total outbound volume for these services. These come from the Permit system, as noted earlier. Source 1, p. 7-7.

The SIRV/O is a random sampling system stratified as follows: (1) destination country or country group; (2) Origin Exchange Office (OEO) group; (3) transportation mode (Surface, Air, ISAL); (4) MIDAS container type (*e.g.*, bags, letter trays, flat trays); (5) MIDAS mail category (LC, AO, CP); and, (6) weight. The Postal Service selects a cluster sample within the stratum for measuring revenue, pieces, and weight. Clusters are defined as mailflow days where a mailflow represents a unique combination of destination foreign city, U.S. origin exchange office, transportation mode, MIDAS container type, and Midas mail category. Source 1, p. 7-3.

MIDAS is the primary component of SIRV/O. It is a network computer system with nodes in all U.S. offices dispatching international mail. Source 1, p. 7-5. It is an automated dispatching system that produces a billing record for the payment of air and surface carriers. It yields a census count of the gross weight (*i.e.*, weight of mail + weight of container) of outbound international mail by country, transportation mode, and UPU class. Source 1, pp. 7-1, 7-3, 7-6, 7-7. The weights recorded in this manner, when summed to country, transportation mode, and class, form control totals for the SIRV/O estimates. The control totals are used to expand sampled revenues, pieces, and weight to the universe. Source 1, p. 7-7. MIDAS also identifies the active mailflows for the cluster samples, and automatically selects mail containers for sampling, based on the Postal Service's testing schedule and the expected total weight of the mailflow day. The ultimate sample is a container of mail. Source 1, p. 7-3.

MIDAS collects data on all outbound international mail. The SIRV/O supplements the MIDAS system in three important ways. First, MIDAS does not collect

information on the number of pieces. Second, MIDAS treats LC and AO mail as a combined total, while the Postal Service needs separate volumes for LC and AO mail for costing and pricing purposes. Third, MIDAS measures the gross weight of mail, *i.e.*, it includes the weight of the mail container in its estimate. The SIRV/O sampling system identifies the weight of the mail and of the container separately. The Postal Service, therefore, is able to adjust the final volume estimates to correct for the difference between the gross weight and the net weight of mail.

The Postal Service uses an auxiliary sampling system independent of the SIRV/O to estimate the GPM volume distribution by country. The data residing in the IBIS and CBCIS do not contain information on destination country. Source 1, p. 7-8. The sampling process is similar to the SIRV/O process. The strata are defined as the origin exchange office and destination country. The ultimate sample unit is a container of outbound GPM. GPM is always transported in its own container to ensure expedited handling. Source 1, p.7-8. The sample data on revenue, pieces, and weight is expanded to the universe on the basis of the sampling fraction and the control totals from the IBIS and CBCIS. Source 1, p. 7-8. The Postal Service uses the resulting volumes for each GPM service, and the applicable GPM rate schedule, to develop the revenues. Source 1, p. 7-8.

(2) Inbound Revenue, Pieces, and Weight

The Postal Service's International Accounts Branch (IAB) routinely collects volume information on inbound international mail from the manifests that accompany the mail. Source 1, p. 6-1 and Source 8, Response to Item 2. The data are used to compute settlement charges, which are the revenues the Postal Service receives for delivering inbound mail. Source 1, p. 3-5. Through the manifest process, the Postal Service collects piece and weight data for parcel post, international express mail, and M-bags. For LC/AO mail (including inbound ISAL), it collects only the weight of the

mail. To develop the number of pieces of inbound LC/AO, the Service estimates the average number of pieces per kilogram by transportation mode, and country or terminal dues regime. Then, it multiplies the total weight of inbound LC/AO mail for each country by the applicable pieces per kilogram. Source 1, p. 8-2 and 8-5. This estimate is derived from the System for International Revenue and Volume/Inbound (SIRV/I). As the table below shows, the SIRV/I estimate of pieces per kilogram is used to calculate piece volumes for 98.6 percent of inbound mail.

TABLE C-2

SUMMARY OF INBOUND VOLUME BY DATA SOURCE

Mail Category	Data Source	Calculation Method	Piece Volume (000) (1)	Percent Distribution of Volume (2)
Surface LC/AO	SIRV/I	Kg x p/Kg	46,735	7.3%
Surface CP	IAB	N/A	2,142	0.3%
Air LC/AO	SIRV/I	Kg x p/Kg	587,926	91.3%
Air CP	IAB	N/A	2,192	0.3%
Express Mail	IAB	N/A	3,763	0.6%
Global Parcel Svc	IAB	N/A	1,049	0.2%
Total	Sum of Lines 1 thru 6		643,807	100.0%
SIRV/I	L.1 + L.3		634,661	98.6%
IAB	Sum of Lns. 2, 4, 5, & 6		9,146	1.4%
			643,807	100.0%

Source: Table III-5, Summary of Revenues, Volumes, and Attributable Cost

The SIRV/I is based on a stratified random sampling system. The strata are defined as foreign origin country, U.S. destination exchange office, and transportation mode (Surface, Air, and ISAL). Source 1, p. 8-1. Each combination of these three characteristics defines a mailflow for sampling purposes. Sampling fractions differ between surface and air transportation. When the Service selects a mailflow day, a

systematic sample of inbound mail containers is selected at the destination exchange office. The data technician records the gross weight and the tare weight of the container, the number of pieces in the container, and for each piece, whether it is a letter, a flat, a packet, or a parcel. The technician also records the number of containers available for sampling that day. Source 1, p. 8-1.

Using the expanded[1] piece and weight data from the SIRV/I, the Service estimates pieces per kilogram (based on gross weight) by country and transportation mode. This produces a measure of pieces per kilogram for (1) Surface LC/AO; (2) Air LC/AO; and, (3) ISAL. These estimates align with lines 1 and 3 of Table C-2 where ISAL is included in Surface LC/AO. To develop the annual piece volumes by country and transportation mode, the Postal Service multiplies the total kilogram weight of inbound mail for each foreign origin country and transportation mode by the corresponding estimated pieces per kilogram. According to the Postal Service, this is a standard method for calibrating a sample estimate to the universe that takes advantage of the positive correlation between weight and pieces. Source 1, p. 8-4. In the case of countries with very small sampled volumes, the Postal Service uses the UPU or the EURB average pieces per kilogram, as applicable, rather than the specific country estimate. Source 1, p. 6-2 and Source 5, pp. 52 and 53.

Having described how the Postal Service estimates annual volumes for LC/AO, parcel post, international express mail, and M-bags, a discussion of the development of inbound revenues follows. This process is conceptually straightforward since the rates are known for terminal dues (LC/AO and M-bags), inward land charges (parcel post), and imbalance charges (EMS). However, the rates for LC/AO differ between Canada, UPU countries, and the European Bilateral countries. For parcel post, each country publishes its own inward land charges annually. For EMS, the U.S. Postal Service maintains bilateral agreements with other countries. Further, since all the rates for

[1] Raw sample estimate divided by the sampling rate or sampling fraction to obtain the estimate for the entire population.

terminal dues, etc., are in terms of SDRs (Special Drawing Rights), the Postal Service must use the applicable exchange rate to convert SDRs to U.S. dollars. To calculate the revenue for inbound mail, the Postal Service aligns the applicable volumes with the applicable rate for terminal dues, etc., with the applicable exchange rate, and multiplies the three numbers. Source 1, p. 6-1.

The agreement with Canada for LC/AO mail contains separate rates for letters and flats. To accommodate this agreement, the U.S. Postal Service maintains a separate system for accumulating Canadian revenue and volume information. The system also covers parcel post. The development of revenue for inbound Canadian mail follows the same calculation procedure described above. Source 1, pp. 6-1 and 6-3.

Since this procedure provides imputed values for inbound revenues, the Postal Service adjusts the revenues for each UPU service so that, in aggregate, they match the total revenues included in the Domestic RPW Report. Source 1, p.6-3.

Finally, the aggregate revenues for air conveyance dues and transit fees are obtained from the Postal Service's revenue accounts. Source 1, p. 6-3. Air conveyance dues are the revenues the Postal Service receives for transporting inbound mail by air to its destination. Transit fees are the revenues the Postal Service earns for forwarding mail from one foreign country to another.

(3) The Development of Attributable Costs for the Standard Services based on the PRC Costing Methodology

There are six generalized components for international mail costs: (1) mail processing; (2) delivery (in-office and street), (3) domestic transportation; (4) international transportation; (5) settlement charges; and, (6) "all other" costs (primarily costs that piggyback on the directly variable costs). This categorization accounts for all cost elements in the Domestic Cost Segments and Components Report and the Domestic CRA, which has a line item for international mail.

Outbound services incur domestic mail processing, domestic transportation, international transportation, terminal dues (the cost of delivery in the destination foreign country), and applicable "all other" costs. Outbound services do not incur domestic delivery costs. Inbound mail incurs domestic mail processing, domestic transportation, delivery, and applicable all other costs. Inbound mail does not incur settlement charges or international transportation costs.

Mail Processing Costs. Mail processing costs are based on Management Operating Data System (MODS) activity costs and In-Office Cost System (IOCS) distribution keys. The MODS system organizes mail processing costs into specific activity pools for which there are corresponding IOCS distribution keys. The distribution keys are used to allocate the MODS activity costs to each international service. In the ICRA, PRC Version, the Postal Service applied the cost variability factors utilized in the Commission's most recent recommended decision (Docket No. R97-1). In Docket No. R97-1, the Commission concluded that the variability factor for mail processing cost should be 100 percent. Differences in variability estimates and distribution keys distinguish the Commission's costing methodology from the Service's. For ease of presentation, the ICRA includes some costs under the heading "process" that are not traditionally incorporated there. These costs include all the costs of supervision (Cost Segment 2) and the remaining clerk and mailhandler cost that is not related to mail processing (Cost Segment 3).

Delivery Costs. The in-office carrier costs and street costs (city and rural) also follow the Commission's recommended costing procedure. The Commission's approach includes volume variable cost and the incremental cost that arises when only one subclass of mail is delivered to a business or residence. In contrast, the Postal Service prefers to assign only the volume variable cost.

Domestic Transportation Cost. Both inbound and outbound mail incur domestic transportation costs. These costs come from the applicable expense categories in the Book of Accounts. Source 1, p. 2-1. The Service's transportation cost system, TRACS,

is used to develop distribution keys to distribute the Book of Accounts' expenses among the domestic subclasses and the international mail services. TRACS collects volumetric data on both outbound and inbound mail in sufficient detail for most expense categories. See Source 6. Where the volumetric data are insufficient for the distribution of attributable cost to international mail categories, the Service develops a distribution key using data from the SIRV/O and the SIRV/I in combination with the density data (pounds per cubic foot) underlying the Domestic RPW report. In these instances, the ultimate distribution key is cubic feet of mail. Source 1, p. 2-1.

According to the Postal Service, with the exception of Canada, sample size limitations prevent it from obtaining reliable figures by which attributable domestic transportation costs can be separated by foreign origin or destination countries. Source 1, p. 2-1. Thus, there is no breakdown of domestic transportation cost by country or country group.

The Postal Service also determined that, with respect to Express Mail and Global Priority Mail, the TRACS system had sampling limitations related to TRACS Passenger, the Eagle network, and the Western network, all of which handle expedited mail. Accordingly, the Service used information from SIRV/O and RPW to distribute the costs among the appropriate categories. Source 1, pp. 2-2 and 2-3. The Postal Service believes this approach provides more accurate reporting and reflects the similarity in transportation costs between International Express Mail and Global Priority Mail. Source 1, p. 2-2.

International Transportation Cost. The costs for transporting mail from U.S. Postal Service dispatching points to foreign countries are kept in the Book of Accounts and apply only to outbound mail. Source 1, p. 4-1. The International Accounts Branch (IAB) maintains international transportation costs and kilograms by country. According to the Postal Service, it develops cost by mail category and country groupings in four steps. First, using the IAB data, the Service develops unit cost (*i.e.*, cost per kilogram) by country and mail category. Second, unit costs are multiplied by category volumes for

each country to develop total cost. Third, country totals are grouped into the appropriate rate groupings, as applicable. Fourth, the group totals are adjusted to match the book of account totals. Source 1, p. 4-1.

Highway costs for Canada and Mexico are developed separately using analogous domestic unit costs. The Service also uses assumptions concerning the proportion of mail destined to Canada and Mexico. The Service assumes that for mail to Canada, 75 percent of the surface mail and 10 percent of airmail moves by highway. For Mexico, it assumes that 100 percent of surface mail and 0 (zero) percent of airmail moves by highway. Source 1, p. 4-4.

Settlement Costs. Settlement costs apply only to outbound mail. The costs represent payments to foreign countries for delivering U.S. Mail. The settlement charges for LC/AO mail are referred to as *terminal dues*. For parcel post, the term is *inward land charge*. For Express Mail, the term is *imbalance charge*. For air LC/AO and air parcel post, there is an additional charge referred to as *air conveyance dues*. This change applies to mail receiving air transportation in the destination country. There is also a *transit fee* that applies to mail originating in one country and moving through a second country for destination in a third country. Source 1, pp. 5-1 and 5-2.

U.S outbound LC/AO mail is subject to three terminal dues regimes: (1) UPU countries, (2) EURB, and (3) Canada. The EURB terminal dues rates have per-piece and per-kilogram elements. The UPU rate is a per-kilogram rate. The Canadian rates are shape based. Source 1, 5-3.

Inward land charges, air conveyance dues and transit rates for parcel post vary by country and are independent of UPU and EURB groupings. The rates are on a per-piece and per-kilogram basis. The UPU specifies the allowable charges for Air conveyance dues and transit fees for LC/AO mail. Source 1, 5-2, 5-3 and 5-9.

EMS imbalance charges also vary by country. Some of the rates are reciprocal, i.e., the U.S. Postal Service pays the foreign postal administration the same rate the foreign postal administration pays to it. The reciprocal rates for some countries reflect a

two-tier system that differentiates between documents and merchandise. According to the Postal Service, this distinction corresponds to customs arrangements. The two-tier system also applies in some countries where private couriers, rather than the Postal Administration, deliver EMS. The remainder of imbalance charges vary widely by country. Source 1, p. 5-4.

The Service's methodology for computing settlement charges requires the outbound volumes by country, mail category (LC/AO, Parcel Post, and EMS), transportation mode, the applicable settlement charge, and the appropriate exchange rate. Multiplying the volumes for each country by the applicable settlement charge and exchange rate yields settlement cost. Source 1, pp. 5-1 and 5-2. Except for EMS, the outbound volume data are obtained from the SIRV/O. They not only support the calculation of settlement costs, but are also used for calculating international transportation costs discussed earlier. Source 1, p. 5-1 and 5-4.

Settlement costs, calculated as described above, are imputed costs. The Postal Service does not attempt to reconcile the imputed cost to the Book of Accounts cost because the accounting procedures are not well suited to the task. Source 1, p. 5-1. In FY 1998, the total booked settlement cost amounted to $547,738.5 (000); while the imputed costs amounted to $477,496.7 (000). Thus, the booked costs exceeded the imputed costs by $70,242 (000). In a response to a Commission inquiry, the Postal Service stated that the imputed costs are based on FY 1998 volumes and reflect the different conversion rates in effect for calendar years 1997 and 1998. In contrast, the booked costs reflect five items that are not the result of FY 1998 volumes or rates: (1) prior year adjustments; (2) a fixed conversion rate; (3) the difference between the fixed conversion rate and the current rate is assigned to general ledger accounts; (4) some settlement payments are provisional; and (5) accruals are conservative to avoid underestimating expenses. For these reasons, the Postal Service treats these

costs as incremental to all international mail as whole.[2] Source 7, Response to Item 10. This will be discussed further below.

"All Other" Costs. "All other" costs include all attributable costs not included above. These are mostly cost items that both the Service and the Commission treat as varying in proportion to directly variable cost. These costs include the costs of some lower level regional and headquarters administration, rents, fuels, utilities, supplies and services, and other support costs. There are also supervisor costs and clerk and mailhandler costs for window service and administrative support included here.

(4) The Development of Attributable Costs for the Initiatives

The cost allocations for International initiatives, with the exception of GPM, are derived from data gathered outside of the Postal Service's main data collection systems. The Postal Service has indicated that the initiatives are seldom observed in the data collection systems used for the higher-volume international mail products. This section describes the Postal Service's costing methodology for each of the initiatives.

Global Package Link. The GPL model used by the Postal Service to track cost and revenue information consists of a series of linked spreadsheets. The model was developed to determine the institutional cost contribution of GPL. Calculating GPL's contribution requires calculation of the product's attributable cost for each postal accounting period (AP) using existing sources of data for GPL revenue, pieces, and weight. Source 10, p. 275.

Costs are allocated to GPL based on an engineering approach. Each step "involved in processing, transporting and delivering mail is mapped out. Each step is

[2] On June 7, 1999, the Postal Service submitted a new FY 1998 ICRA Report - Postal Service Version. The report contained a revised methodology for calculating international transportation cost and a different treatment of the difference between imputed settlement charges and the settlement charges in the book of accounts. Because of time constraints, the Commission has not been able to evaluate the merits of the changes. For this reason, the attributable costs in this report reflect the FY 1998 ICRA Report – PRC Version.

classified as variable with piece, with volume, or with some other criterion, or fixed with respect to volume. Then, costs for each step are summed." Source 3, Response to Item 9. The attributable cost components included in the GPL model are: verification labor, domestic shipping, processing labor, facilities and equipment, international transportation, international settlement, IBU contractors, IBU administrative, and other charges and expenses. Excluded costs are institutional costs not attributable to specific postal products. These include headquarters general and administrative expenses. Source 10, p. 275.

The model uses volume data from the Postal Service's Revenue, Pieces, and Weights system. Costs are manually input, based on reports from Postmasters at the facilities where GPL is processed. Source 10, p. 282. "Customer verification rate is the average hours spent per shipment verifying GPL." Source 3, Response to Item 7. Contract highway service costs are obtained by contacting postmasters or GPL account representatives. Domestic shipping rates are per minute costs for vehicle service drivers and per mile costs for contract highway routes that are not dedicated to GPL. These costs are determined by separate analyses. International transportation rates are calculated in the GPL model using the highest international airmail rates for Express GPL and the Surface Airlift Rates for Standard and Economy GPL. Source 3, Response to Item 7.

In addition to the volume variable cost, the Postal Service also included product-specific costs in the amount of $6,151 (000). These expenses are causally related to GPL, but do not vary with marginal volume changes. They include advertising and promotional activities and other related business expenses. Source 7, Response to Item 9.

Global Priority Mail. GPM costs are estimated "by using In Office Cost System (IOCS) tallies, domestic transportation information and other elements of the process used for most other categories of international mail, including the identification of product-specific costs." Source 3, Response to Item 9. As in the case of GPL, there

are product-specific costs associated with GPM in the amount of $18,913 (000). They include the expense of advertising and promotion, supplies and other related business activities. Source 7, Response to Item 9.

Global Direct Services (Direct Entry/Inbound). The costing methodology for Global Direct Services varies by country, reflecting the operational specifics of the service that is provided to each customer. The Postal Service provided service to or from three countries during FY 1998:

Canada. Mail going to Canada can have either of two different rates for terminal dues. The terminal dues rate is either taken from the mailing statements or is calculated at a fixed rate, which is then converted from Canadian to U.S. currency and multiplied by pieces. For domestic transportation, the highway contract rate is used. The standard Department of Transportation (DOT) international airmail rates are used for the international air transportation cost. An acceptance clerk cost per piece taken from the 1997 CRA report in Cost Segment 3.2 under the Window Service Category is added. Source 1, p. 9-5.

Brazil. The IBU provides the settled terminal dues by mailing. Domestic transportation is based on a highway truck rate per mile multiplied by the distance between the domestic acceptance site and the international mail facility. The standard DOT international airmail rates are used for the international air transportation cost. An acceptance clerk cost, identified from an international mail processing study, is also added. Source 1, pp. 9-4 and 9-5.

Great Britain. Costs for Direct Entry Great Britain are attributed based on the cost segment distribution of Standard Mail (A) Regular from the 1997 CRA. For Cost Segment 14, a weight per piece ratio is used in order to determine a weight-based cost for transportation. Source 3, p. 9-4.

These services consist of both outbound (US origin) and inbound (foreign origin) mail. The following table shows the breakdown of the two types of mail for FY 1998.

TABLE C-3

GLOBAL DIRECT MAIL

Category	Revenue $(000)	Cost $(000)	Contribution $(000)	Pieces (000)	Weight (lbs) (000)
Outbound (US Origin)	3,351	3,115	236	16,837	840
Inbound (Foreign Origin)	116	23	93	301	79
Total	3,467	3,138	329	17,138	919

Source: Source 11, Response to Item 1.

The volume is predominantly outbound mail. The small numbers in the inbound entries in Table C-3 illustrate the difficulty of using the Postal Service's major data collection systems for tracking the costs of initiatives.

Global Parcel Services. The GPS volume and revenue report is in a database maintained by the International Accounting Branch (IAB). The dispatch data are entered daily and the accounting period report is based on this information. Specific revenue data are taken form the Financial Accounting Cost Tracking System (FACTS). The data are sent from International Finance to the IAB on an accounting period basis. Source 1, p. 9-1.

Costs for GPS are determined by using a proxy. The volume characteristics of GPS are applied, on an accounting period basis, to the unit cost for Domestic Priority Mail as identified in the 1997 Cost and Revenue Analysis (CRA) report for costs excluding transportation. For transportation, calculations are based on a unit cost, and adjusted for the difference in the weight per piece ratio between Domestic Priority and GPS. Source 1, p. 9-5.

International Customized Mail. In FY 1998, ICM service ofered access to five existing services: ISAL, IPAS, EMS, ValuePost, and Air/Surface Parcel Post on terms adapted to specific customers. Generally, the costs associated with service specific ICM customers are developed using the average costs of the applicable service (ISAL,

etc.) for settlement costs, international transportation charges, and processing costs. In some cases, only an acceptance cost is used rather than full processing costs to reflect the specific operations of the particular ICM service. Source 1, p. 9-3 and 9-4.

The lone exception to this methodology is the cost incurred by ICM customers that use the Postal Service's Air or Surface Parcel Post. For these customers, the Postal Service develops costs using the cost coverage for the standard Air and Surface Parcel Post categories. Source 1, p. 9-4.

(5) International Mail Service Incremental Costs

The Postal Service has included costs that it views as incremental to International Mail as whole. The cost has two components. The first component reflects the difference in settlement charges between imputed costs used in the ICRA as attributable settlement cost and the booked cost in the system of accounts. This cost amounted to $52,203 (000) in FY 1998 and was discussed in the earlier section on the development of settlement cost. The second component reflects expenses for the IBU that amounted to $70,242 (000) in FY 1998. ICRA Report, p. A-1, footnote 1. The reported amount includes the salaries and benefits for IBU personnel, supplies and services, rents, utilities, and other related expenses. Source 3, Response to Item 4. Together, these expenses amount to $122,445 (000).

These costs cannot be causally related to specific international mail services on the basis of current information, but can be causally related to international services as a whole.

DERIVATION OF APPROXIMATIONS FOR ATTRIBUTABLE COST PER PIECE (ACP) AND ITS COEFFICIENT OF VARIATION (CV)

The Attributable Cost per Piece (ACP) for a domestic subclass or international category of mail is derived by the United States Postal Service for its annual Cost and Revenue Analysis (CRA) and International CRA (ICRA) reports using a formula that combines in a nonlinear way estimates of volume-variabilities, distribution key shares and mail volumes produced by a number of postal data systems and special econometric studies. In most Postal Service material ACP is referred to as Unit Volume-Variable Cost (UVVC). Individually, the coefficients of variability for these estimates (the standard deviation of the error of the estimate divided by the estimate) are often a product of the sampling process or econometric fit that produced the estimate and are known to the Postal Service. Furthermore, there is little interdependence between Postal Service data systems and/or special studies so the errors that arise in estimates of volume-variabilities, distribution key shares and mail volumes, as they appear in the formula for a single subclass or category, can be expected to be uncorrelated and approximately normally distributed. In the absence of non-sampling errors, the expected value or mean of the errors will also be zero. These assumptions are nearly identical to the assumptions made by the study team in the recently concluded study of the quality of several principal Postal Service data systems.

The purpose of this Technical Appendix is to derive and to apply formulas to calculate accurate approximate values for expected ACP and its coefficient of variation (CV) under these assumptions and using no more information than the estimates of volume variability, distribution key shares, and mail volumes, and the estimates of the CVs of these variables, as provided by the Postal Service. The formulas are approximations for five reasons. First, the derivation uses a second-order Taylor series expansion of the formula for ACP; thus the effect of third and higher-order terms in the Taylor series is presumed to be negligible. Second, virtually all of the errors in the

estimates found in the formula for ACP are lower-bounded; however, the normal distribution is not. Consequently, the normal distribution is only an approximate description of the error-generating process, although the approximation should be very good for variables with moderate CVs (0.5 or less). Third, the assumption that the errors in the estimates of the variables found in the formula are independently distributed is too heroic. There are some connections between Postal Service data systems and special studies that could produce correlations between the errors. However, there exist no estimates of these correlations that could be used in approximations derived under the assumption that the correlations are known. Fourth, the derived approximation for the CV of ACP contains terms that are very small and have no appreciable affect on the approximations. These terms can be ignored as a practical matter in applying the approximation formula. Fifth, the derivations assume that there are no non-sampling errors in Postal Service estimates of volume-variabilities, distribution key shares and mail volumes, although it is widely suspected that unknown non-sampling errors exist. Fortunately, non-sampling errors in the form of additive biases will have little effect on the approximations. If the amounts of the biases become known, they can be simply subtracted to correct the estimates with little effect on the calculated CVs. In effect, there is little interaction in the approximations between simple biases and the CV of ACP when non-sampling errors are discovered and corrected.

The derivation proceeds, first, for a general function $y = F(x)$ having continuous first- and second-order partial derivatives with respect to the elements x_i of the vector of variables x. An estimate $\hat{x}$ of x is assumed to have been obtained such that the errors $e_i = x_i - \hat{x}_i$ are normally distributed and independent random variables with zero means. The derivation makes use of the following expected values for independent normal errors with zero means:

1. $E[e_i] = 0$ Zero mean (no bias in $\hat{x}_i$).

2. $E[e_i^2] = \sigma_i^2$ Variance of e_i.

3. $E[e_i e_j] = 0$ for all $i \neq j$ independent errors

4. $E[e_{i...} e_j] = 0$ for any expression $e_{i...} e_j$ in which one or more of the errors appears alone unsquared, e.g., $E[e_1] = 0$ and $E[e_1 e_2] = 0$, $E[e_1^2 e_2] = 0$, $E[e_1 e_2^3] = 0$.

5. $E[e_i^2 e_j^2] = \sigma_i^2 \sigma_j^2$ if $i \neq j$. Also because of independent errors.

6. $E[e_i^3] = 0$ Third moment about the mean of the normal distribution.

7. $E[e_i^4] = 3\sigma_i^4$ Fourth moment above the mean of the normal distribution.

Only 6 and 7 make use of the normality assumption and 6 is also true for any symmetric distribution.

The second-order Taylor series expansion of the function $y = F(x)$ is taken around $\hat{y} = F(\hat{x})$: $y = \hat{y} + \sum_i F_i e_i + \sum_i \sum_j F_{ij} e_i e_j / 2$ where $F_i = \partial F / \partial x_i$ and $F_{ij} = \partial^2 F / \partial x_i \partial x_j$. All partial derivatives are evaluated at $x = \hat{x}$.

The expected value of y is obtained by taking the expected value of its components. $E[y] = \hat{y} + \sum_i F_i E(e_i) + \sum_i \sum_j F_{ij} E[e_i e_j]/2$. The term $\sum_i F_i E[e_i^i] = 0$ because $E[e_i] = 0$ (1). All of the terms in the double summation for which $i \neq j$ also vanish because $E[e_i e_j] = 0$ for $i \neq j$ (3). In the remaining terms $\sum_i F_{ii} E[e_i^2]/2$, substitute $E[e_i^2] = \sigma_i^2$ (2)

8. $E[y] = \hat{y} + \sum_i F_{ii} \sigma_i^2 / 2$

This expression (8) reveals that $\hat{y}$ is likely to be a biased estimate of y unless the function $F(x)$ is linear or in the unlikely circumstance that there are exactly affecting terms in the expression $\sum_i F_{ii} \sigma_i^2$.

The CV of y is defined as: $C_y = \sqrt{E[(y - E[y])^2]} / E[y]$. This definition uses $E[y]$ rather than the biased estimate $\hat{y}$ to normalize the standard deviation of the error $y - E[y]$, which is also measured from $E[y]$ rather than $\hat{y}$. Therefore, the approximation for C_y derived here requires a bias correction to obtain $E[y]$ from $\hat{y}$ as shown in (8).

The error $y - E[y]$ is approximated by combining the Taylor series for $y = F[x]$ and the result obtained for $E[y]$: $y - E[y] = \sum_i F_i e_i + \sum_i \sum_j F_{ij} e_i e_j / 2 - \sum_i F_{ii} \sigma_i^2 / 2$.

$E[(y - E[y])^2]$ is the variance of the error in the bias-corrected estimate $E[y]$ of y. Substituting for $y - E[y]$ and squaring the resulting expression produces:

$$E[(y - E[y])^2] = E[(\sum_i F_i e_i)^2 + (\sum_i F_i e_i)(\sum_i \sum_j F_{ij} e_i e_j)$$
$$- (\sum_i F_i e_i)(\sum_i F_{ii} \sigma_i^2) + (\sum_i \sum_j F_{ij} e_i e_j)^2 / 4$$
$$- (\sum_i \sum_j F_{ij} e_i e_j)(\sum_i F_{ii} \sigma_i^2) / 2 + (\sum_i F_{ii} \sigma_i^2)^2 / 4].$$

The expression is reduced by evaluating the expected value of each component using 1-7 above and then combining the results.

$$E[(\sum_i F_i e_i)^2] = \sum_i \sum_j F_i F_j E[e_i e_j]$$
$$= \sum_i F_i^2 \sigma_i^2 \; because \; E[e_i^2] = \sigma_i^2 \text{ (2) and}$$
$$E[e_i e_j] = 0 \; for \; all \; i \neq j \text{ (3).}$$

$E[(\sum_i F_i e_i)(\sum_i \sum_j F_{ij} e_i e_j)] = \sum_h \sum_i \sum_j F_h F_{ij} E[e_h e_i e_j] = 0$ because any expectation of the product of three errors $e_h e_i e_j$ either involves at least one unsquared e_i alone (4) or is e_i^3. $E[e_i^3] = 0$ by (6).

$$E[(\sum_i F_i e_i)(\sum_i F_{ii} \sigma_i^2)] = (\sum_i F_{ii}) \sum_i F_i E[e_i] = 0 \; because \; E[e_i] = 0 \text{ (1).}$$

$$E[(\sum_i \sum_j F_{ij} e_i e_j)^2] = E[\sum_h \sum_i \sum_j \sum_k F_{hi} F_{jk} e_h e_i e_j e_k]$$

$$= E[\sum_i F_{ii}^2 e_i^4] + E[\sum_i \sum_{j \neq i} (F_{ii} F_{jj} + 2F_{ij}^2) e_i^2 e_j^2]$$

$$+ E[terms\ e_h e_i e_j e_k\ with\ one\ unsquared\ e_i\ alone]$$

$$= \sum_i F_{ii}^2 E[e_i^4] + \sum_i \sum_{j \neq i} (F_{ii} F_{jj} + 2F_{ij}) E[e_i^2 e_j^2]$$ because expected

values of products with one e_i term all are zero (4).

$$= \sum_i 3F_{ii}^2 \sigma_i^4 + \sum_i \sum_{j \neq i} (F_{ii} F_{jj} + 2F_{ij}) \sigma_i^2 \sigma_j^2$$ because $E[e_i^4] = 3\sigma_i^4$ (7),

and $E[e_i^2 e_j^2] = \sigma_i^2 \sigma_j^2$ when $i \neq j$ (5).

$$= \sum_i \sum_j (F_{ii} F_{jj} + 2F_{ij}) \sigma_i^2 \sigma_j^2$$

$$E[(\sum_i \sum_j F_{ij} e_i e_j)(\sum_i F_{ii} \sigma_i^2)] = (\sum_i F_{ii} \sigma_i^2) \sum_i \sum_j F_{ij} E[e_i e_j]$$

$$= (\sum_i F_{ii} \sigma_i^2)^2$$ because $E[e_i^2] = \sigma_i^2$ (2) and

$E[e_i e_j] = 0\ for\ i \neq j$ (3).

Recombining the components $E[(y - E[y])^2] = \sum_i F_i^2 \sigma_i^2 + \sum_i \sum_j (F_{ii} F_{jj} + 2F_{ij}^2) \sigma_i^2 \sigma_j^2 / 4$

$$- (\sum_i F_{ii} \sigma_i^2)^2 / 2 + (\sum_i F_{ii} \sigma_i^2)^2 / 4$$

$$= \sum_i F_i^2 \sigma_i^2 + \sum_i \sum_j F_{ij}^2 \sigma_i^2 \sigma_j^2 / 2$$ because

$$\sum_i \sum_j F_{ii} F_{jj} \sigma_i^2 \sigma_j^2 = (\sum_i F_{ii} \sigma_i^2)^2.$$

Therefore, the CV of y is found from the approximation formula.

9. $$C_y = \frac{\sqrt{\sum_i F_i^2 \sigma_i^2 + \sum_i \sum_j F_{ij}^2 \sigma_i^2 \sigma_j^2 / 2}}{\hat{y} + \sum_i F_{ii}^2 \sigma_i^2 / 2}$$

In practical applications the term $\sum_i \sum_j F_{ij}^2 \sigma_i^2 \sigma_j^2 / 2$ is frequently small and can be ignored without materially affecting the accuracy of the calculated value of C_y. The term

$\sum_i F_{ii}^2 \sigma_i^2 / 2$ in the denominator may also be small enough to be ignored in many applications. In other words, the bias correction to $\hat{y}$ may sometimes be omitted without materially affecting the results.

Applying (8) and (9) to ACP is straightforward. The formula used by the Postal Service to compute ACP for the CRA and ICRA is:

$$u = \sum_j T_j E_j d_j / V \qquad \text{ACP of a single subclass/category}$$

The summation is taken over all cost pools $_j$. T_j denotes the annual total cost in pool $_j$ and is assumed to be known certainly from Postal Service financial accounts. The other terms in the formula are either assumed values or are estimated in one way or another. These terms are: E_j, the volume variability of costs in pool $_j$; d_j, the distribution key share for the subclass in pool $_j$; and, V, mail volume for the subclass.

The CRA or ICRA estimate of u is:

$$\hat{u} = \sum_j T_j \hat{E}_j \hat{d}_j / \hat{V}$$

The $\hat{E}_j$, $\hat{d}_j$ and $\hat{V}$ are all assumed to be unbiased estimates of the E_j, d_j and V with errors that are independent and normally distributed. The CVs are defined as $C_{Ej} = \sigma_{Ej} / \hat{E}_j$, $C_{dj} = \sigma_{dj} / \hat{d}_j$ and $C_V = \sigma_V / \hat{V}$. Estimates of these CVs are assumed to be available. It simplifies the notation somewhat to define $\hat{u}_j$ as the $_j$ th component of the summation that produces $\hat{u}$, i.e., $\hat{u}_j = T_j \hat{E}_j \hat{d}_j / \hat{V}$.

The partial derivatives of u, evaluated at $E_j = \hat{E}_j$, $d_j = \hat{d}_j$ and $V = \hat{V}$ are:

$$\frac{\partial u}{\partial E_j} = \frac{\hat{u}_j}{\hat{E}_j}, \frac{\partial u}{\partial d_j} = \frac{\hat{u}_j}{\hat{d}_j}, \frac{\partial u}{\partial V} = -\frac{\hat{u}}{\hat{V}}, \frac{\partial^2 u}{\partial E_j^2} = \frac{\partial^2 u}{\partial E_j \partial d_j} = \frac{\partial^2 u}{\partial d_j^2} = 0$$

$$\frac{\partial^2 u}{\partial V^2} = \frac{\partial \hat{u}}{\hat{V}^2}, \frac{\partial^2 u}{\partial V \partial E_j} = -\frac{\hat{u}_j}{\hat{E}_j \hat{V}}, \frac{\partial^2 u}{\partial V \partial d_j} = -\frac{\hat{u}_j}{\hat{d}_j \hat{V}}$$

Inserting partial derivatives in equation 8 provides an approximation for $E[u]$, the expected value of ACP:

$$E[u] = \hat{u} + \frac{2\hat{u}\ \sigma_v^2}{\hat{V}^2\ 2}$$

$$E[u] = \hat{u}(1 + C_v^2) \text{ since } \sigma_v^2 / \hat{V}^2 = C_v^2.$$

10. As a proportion: $E[u]/\hat{u} = 1 + C_v^2$.

This shows that the CRA and ICRA estimates of ACP are biased downwards by an amount that is related to the square of the CVs of the volume estimates. In most instances, this bias is small since the CVs of the volume estimates are close to zero.

Inserting partial derivatives in equation 9 provides the estimate of the CV of u, denoted C_u.

$$C_u = \frac{\sqrt{\sum_j \left(\frac{\hat{u}_j}{\hat{E}_j}\right)^2 \sigma_{ej}^2 + \sum_j \left(\frac{\hat{u}_j}{\hat{d}_j}\right)^2 \sigma_{dj}^2 + \left(\frac{\hat{u}}{\hat{V}}\right)^2 \sigma_v^2 + \left(\frac{2\hat{u}}{\hat{V}^2}\right)^2 \frac{\sigma_v^4}{2} - 2\sum_j \left(\frac{\hat{u}}{\hat{E}_j \hat{V}}\right)^2 \frac{\sigma_{Ej}^2 \sigma_v^2}{2} - 2\sum_j \left(\frac{\hat{u}_j}{\hat{d}_j \hat{V}}\right)^2 \frac{\sigma_{dj}^2 \sigma_v^2}{2}}}{\hat{u}(1 + C_v^2)}$$

$$C_u = \frac{\sqrt{\sum_j \hat{u}_j^2 (C_{Ej}^2 + C_{dj}^2) + \hat{u}^2 C_v^2 + 2\hat{u}^2 C_v^4 - \sum_j \hat{u}_j^2 C_v^2 (C_{Ej}^2 + C_{dj}^2)}}{\hat{u}(1 + C_v^2)}$$

11. $$C_u = \frac{\sqrt{\sum_j (\hat{u}_j / \hat{u})^2 (C_{Ej}^2 + C_{dj}^2) + C_v^2 + [2C_v^4 - \sum_j (\hat{u}_j / \hat{u})^2 C_v^2 (C_{Ej}^2 + C_{dj}^2)]}}{(1 + C_v^2)}$$

The term in the brackets [ ] under the square-root sign can be ignored without materially affecting the calculated value of C_u since the terms C_v^4 and $C_v^2(C_{Ej}^2 + C_{dj}^2)$ are all

quite small and enter the formula in a way that tends to be offsetting. Therefore, the approximating formula for C_u can be reduced with no appreciable loss in accuracy to the much simpler expression:

12. $$C_u = \frac{\sqrt{\sum_j (\hat{u}_j/\hat{u})^2 (C_{Ej}^2 + C_{dj}^2) + C_v^2}}{1 + C_v^2}$$

This is the formula that has been used to calculate the CVs for International Mail.

Finally, consider the possibility that a non-sampling error is discovered in the form of an additive bias β_i in one of the components $\hat{x}_i$ of $\hat{x}_j$, that is $\hat{x}_i = E[x_i] + \beta_i$. It can easily be shown that if one simply corrects the bias by replacing $\hat{x}_i$ with $\hat{x}_i - \beta_i$ when $\hat{y}$ and all of the partial derivatiives F_i and F_{ij} are computed, then the mathematics used to derive $E[y]$ (8) and C_y (9) continues to be valid. Although the use of $\hat{x}_i$ rather than $\hat{x}_i - \beta_i$ will provide biased estimates of $E[y]$ and C_y, correcting for the bias requires no essential change in the application of formulas 8, 9, 10, 11 or 12.

Note also that correcting an additive bias in an $\hat{E}_j$, $\hat{d}_j$ or $\hat{V}$ is not likely to have much of an impact on a C_u calculated according to formula 12. The bias correction affects C_u primarily by changing the ratios $(\hat{u}_j/\hat{u})$ and thus reweighting the summation of terms in $\sum_j (\hat{u}_j/\hat{u})^2 (C_{Ej}^2 + C_{dj}^2)$. The CV of the biased variable would also change from $\sigma_i/\hat{x}_i$ to $\sigma_i/(\hat{x}_i - \beta_i)$. Except for a bias in the volume estimate $\hat{V}$ and its effect on C_v, such a change would probably have only a small impact on C_u.

The Postal Service has never proposed a method for computing the overall CVs for the ACPs it annually estimates for domestic and international mail in the CRA and

ICRA reports. However, it appears that the Service retains sufficient information about the CVs of the components of its ACP formula to make possible either a simulation or an approximate calculation of the overall CVs using (12). A calculation or simulation of the CVs of ACP would be a helpful addition to the Service's annual CRA and ICRA reports and would be useful to the Commission and others if supplied by the Postal Service in its submissions for rate proceedings.

Table D-2 displays approximate values of the CVs for the ACPs of the major categories of inbound and outbound International Mail. The calculated values depend upon Unit Volume-Variable Costs (UVVCs), volumes and other information provided by the Postal Service in "International Cost and Revenue Analysis (ICRA) Report – PRC Version Fiscal Year 1998", upon CVs for distribution shares and volumes provided in the Service's responses to Commission Orders 1236 and 1244, and upon a small amount of information taken from the 1998 CRA (PRC Version) for domestic mail and the National Consolidated Trial Balance for FY 1998.

Some of the CVs of the variables appearing in equation 12 are missing from the Service's responses to the Commission's information requests. In particular, there are no coefficients of variation for any cost pool volume-variabilities. These volume-variabilities are all assumed to be equal to one and their CVs are assumed to be zero. It is frequently the case that the CVs for distribution key shares and mail volumes are reported for aggregations of more than one category of International Mail, or in other ways that do not exactly match the formula. Also, the cost pool definitions used to report UVVC in the ICRA do not exactly match the cost categories for which the Service has reported CVs for the IOCS distribution keys. These and other defects in the data have been overcome by using proxies and by making other assumptions as needed to use whatever data has been supplied. Any differences in the Service's use of UVVC in the ICRA and the definition of ACP used by the Commission have been ignored in the application of the approximation formula.

The overall CVs for the fifteen major categories of inbound and outbound International mail are shown in Table D-2 in the column labeled "CV of ACP" These overall CVs are derived directly from CVs for the various cost components and volume as shown in the other columns of the table. The formula also involves cost proportions. These proportions, shown as percentages, are derived from the ICRA and appear in Table D-1. Some of the ICRA cost categories have been combined or redistributed for the CV calculations as described below.

The specific assumptions that have been made to overcome the various omissions and defects in the data are as follows:

1. The CVs of the volume-variabilities (E_j) are all taken to be zero. For most cost components, the CRA and ICRA rely upon volume-variabilities with an assumed value of one. This means that the cost component is completely volume-variable. When a volume-variability is an assumed value, its associated CV is zero.

2. Several mail categories have been combined in Table 1 "Estimated IOCS Cost CVs for International Mail Categories, FY 1998" from the Service's response to Commission Orders 1236 and 1244. Where this has occurred the same CVs have been used for the components. Inbound Surface and Air LC/AO both use the CVs reported for Inbound LC/AO; Inbound Surface and Air Parcel Post both use the CVs for Inbound Parcel Post. Outbound Surface Publishers Periodicals use the CVs for Outbound Surface AO. The CVs for Outbound Global Priority Mail have been assumed to apply to all outbound international priority mail.

3. The Service was able to supply a CV for mail volume for only one category of inbound International Mail, inbound Air LC/AO. For all other categories of inbound mail the volume CV was assumed to be the same as the volume CV of the corresponding category of outbound mail.

4. A somewhat more aggregate set of mail categories has been used in the Service's Table 2 "TRACS CVs PQ1-4, FY 98" from the Service's response to Commission Orders 1236 and 1244. In addition to the assumptions made above (2) it was assumed that Post Cards and Postal Cards have the same domestic transportation CVs as Letters and Letter Packages.

5. The Postal Service provided CVs for Clerks and Mailhandlers broken down by Mail Processing, Administrative, and Window Service. These were recombined into a single CV for Clerks and Mailhandlers under the assumption that the three subcategories have independent errors. The formula is:

$$C_p = \sqrt{(P_1C_1)^2 + (P_2C_2)^2 + (P_3C_3)^2}$$

C_p = CV for mail processing

C_1, C_2, C_3 = CVs for Clerks and Mailhandlers
(1) Mail Processing, (2) Administrative, and (3) Window Service

P_1, P_2, P_3 = Proportions of costs for Clerks and Mailhandlers

Values for the proportions appearing in the formula were taken from the 1998 CRA (PRC Version) "Cost Segments and Components Report, Segment 3". The proportions are .758 for mail processing, .120 for administrative and .122 for window service. The results of applying the formula were used as the CVs for the ICRA non-transportation cost category "Process."

6. The ICRA non-transportation cost category "Delivery" was assumed to have the CV reported by the Postal Service for "City-Carrier In-Office" in Table 1.

7. No CVs were reported by the Postal Service that appeared to apply directly to the ICRA non-transportation category "Other." In fact, this category is a collection of capital-related and overhead costs that are customarily apportioned in the annual CRA by a method called "piggy-backing." That is, they are apportioned in the same way as

related labor costs and can be expected to have similar errors. Consequently, they have been redistributed back to the other domestic cost categories in applying the approximation formula. This redistribution follows the proportions in the ICRA for Process, Delivery and Domestic Transportation.

8. No CVs were reported directly for any of the non-domestic ICRA cost categories. These categories are "International Transportation," "Terminal Dues," "Transit" and "International Air." However, most of the costs in these categories are charges that are based upon weight. Therefore, these charges were combined and assigned the CV reported by the Postal Service for weight. This assumption may cause a minor violation of the assumption that the errors in the components of ACP are uncorrelated since weight and volume are measured in ways that are sometimes related. Fortunately, the CVs for weight are all quite small so the effect any correlation with volumes should be small.

9. The Postal Service's response to PRC Order No. 1236 provided CVs for eight separate modes of domestic transportation and for each postal quarter of FY 1998. These were combined in two stages into the single set of CVs for Domestic Transportation for 1998 used in the approximation formula. First, the CVs for the four postal quarters were combined by assuming that the CVs were drawn from up to four independent, equal-sized samples with the same mean. Where no CV was reported for a quarter, it was assumed that no sample had been drawn for that quarter. The formula for combining the quarterly CVs under these assumptions is:

$$C_y = \sqrt{(C_1^2 + C_2^2 + C_3^2 + C_4^2)/N}$$

C_y = Annual CV

$C_1, C_2, C_3 C_4$ = CVs for quarters 1-4

N = The number of quarters for which the Postal Service reported a nonzero CV.

10. The annual CVs for the eight modes of domestic transportation were then combined into a single CV for each international mail category using the assumption that the errors in the distribution key shares for these pools are independent. This assumption is an extension of the assumption of independent errors underlying the derivation of the approximation formula.

$$C_t = \sqrt{\sum_{j=1}^{8} (P_j C_j)^2}$$

C_t = CV for all modes of domestic transportation
C_j = CV for domestic transportation mode $_j$
P_j = Proportion of domestic transportation cost attributed to mode $_j$

The formula for combining the eight CVs requires the proportion of total domestic transportation cost for each mode. A single set of proportions was used based upon the cost of all categories of international mail reported in the 1998 CRA Report. The proportion for each mode is the cost attributed to international mail for the mode in the "National Consolidated Trial Balance, FY 1998", Accounting Period 14, Year-to-date. The proportions are: Passenger Air .4810, Highway Intra-SCF .0003, Highway Inter-SCF .0016, Highway Intra-BMC .1605, Highway Inter-BMC .1516, Eagle Network .1429, Passenger Rail .0419, and Western Air .0203.

TABLE D-1
PERCENTAGE DISTRIBUTION OF COSTS BY COST GROUPS

International Mail Category	Mail Processing	Delivery	Other	Domestic Transp.	Int'l Transp.	Terminal Dues	Transit	Int'l Air
Outbound:								
Letters and letter packages	26.77%	0.56%	10.97%	1.30%	14.31%	45.54%	0.00%	0.56%
Postcards, postal cards	31.48%	0.62%	11.73%	0.31%	5.25%	50.62%	0.00%	0.00%
International Priority Airmail	4.55%	0.24%	2.39%	2.39%	36.36%	53.11%	0.00%	0.96%
Air AO	16.67%	0.36%	6.28%	3.62%	31.36%	40.78%	0.00%	0.94%
Air Parcel Post	14.78%	0.64%	5.22%	4.24%	42.80%	31.73%	0.00%	0.58%
Express Mail International Service	12.16%	0.21%	6.51%	7.15%	22.30%	50.70%	0.00%	0.96%
Surface AO	23.32%	0.45%	10.23%	2.85%	5.18%	57.97%	0.00%	0.00%
Surface Publishers Periodicals	14.19%	0.48%	7.50%	0.72%	2.23%	74.88%	0.00%	0.00%
International Surface Airlift	0.88%	0.29%	1.02%	1.90%	33.09%	62.81%	0.00%	0.00%
Surface Parcel Post	25.08%	1.19%	11.29%	9.36%	7.30%	44.72%	1.05%	0.00%
Inbound:								
Surface LC/AO	58.62%	13.14%	24.31%	3.93%	N/A	N/A	N/A	N/A
Surface Parcel Post	49.63%	5.04%	17.46%	27.86%	N/A	N/A	N/A	N/A
Air LC/AO	60.33%	11.80%	24.59%	3.28%	N/A	N/A	N/A	N/A
Express Mail International Service	34.32%	40.86%	17.72%	7.11%	N/A	N/A	N/A	N/A
Air Parcel Post	55.55%	5.19%	21.95%	17.31%	N/A	N/A	N/A	N/A

TABLE D-2
PERCENTAGE COEFFICIENTS OF VARIATION BY COST GROUPS 1998

International Mail Category	Mail Processing	Delivery	Domestic Transp.	All Other Int'l Costs	Volume	CV of ACP	ACP Coverage	Coverage t-value
Outbound:								
Letters and letter packages	5.29%	70.70%	39.00%	1.04%	2.01%	3.00%	164.68%	21.53
Postcards, postal cards	13.13%	0.00%	39.00%	1.04%	2.01%	6.00%	153.40%	8.89
International Priority Airmail	19.27%	95.23%	41.77%	0.00%	0.00%	1.80%	177.51%	43.12
Air AO	11.40%	0.00%	48.84%	2.00%	2.57%	4.50%	140.06%	8.91
Air Parcel Post	13.46%	0.00%	38.84%	2.93%	3.20%	5.07%	126.83%	5.29
Express Mail International Service	18.25%	0.00%	12.67%	0.00%	0.00%	3.20%	160.05%	18.78
Surface AO	12.33%	0.00%	55.04%	5.04%	6.67%	8.63%	83.04%	-1.96
Surface Publishers Periodicals	12.33%	0.00%	0.00%	0.00%	0.00%	2.60%	84.05%	-6.13
International Surface Airlift	31.80%	0.00%	0.00%	0.00%	0.00%	0.37%	103.95%	10.61
Surface Parcel Post	11.65%	97.48%	63.61%	3.40%	2.65%	9.42%	119.98%	2.12
Inbound:								
Surface LC/AO	8.70%	8.55%	38.42%	N/A	6.67%	9.76%	70.06%	-3.07
Surface Parcel Post	17.10%	0.00%	54.92%	N/A	2.65%	21.35%	168.41%	3.20
Air LC/AO	8.70%	8.55%	38.42%	N/A	2.50%	7.70%	91.15%	-1.15
Express Mail International Service	16.45%	106.90%	16.31%	N/A	0.00%	53.54%	101.70%	0.03
Air Parcel Post	17.10%	0.00%	54.92%	N/A	3.20%	17.49%	171.88%	4.11

OUTBOUND REGIONAL DATA

The Postal Service provided volume, cost, and revenue data by terminal dues regime. Although terminal dues apply to only LC/AO mail, the Service provided the terminal dues regime separation for all services. There are three regimes: (1) Canada; (2) European Bilateral Countries; and, (3) UPU countries. Although Mexico is part of the UPU country group, the Postal Service has reported data for it separately.

There is no reporting of the data for the initiatives on a regime basis. Also, the Postal Service cannot separate the cost for ValuePost/Canada between periodicals and all other printed matter; therefore, those costs are included in the data for Surface printed matter.

TABLE E-1 (Revised 6/11/99)
OUTBOUND INTERNATIONAL MAIL
SUMMARY OF FY 1998 INTERNATIONAL VOLUMES, REVENUE,
ATTRIBUTABLE COST AND COST COVERAGE
BY INTERNATIONAL MAIL CATEGORY AND TERMINAL DUES REGIME 1/

International Mail Category	Volume (1)	Revenue ($) (2)	Attributable Cost ($) 2/ (3)	Contribution ($) (4)=(2)-(3)	Cost Coverage (5)=(2)/(3)
Surface					
Printed Matter and Small Packets (AO), Excluding Periodicals and ISAL					
Canada	15,954	14,611	12,824	1,787	113.9%
Mexico	214	745	1,129	(384)	66.0%
European Bilateral Group	3,972	12,541	13,791	(1,250)	90.9%
UPU Countries	8,075	29,564	41,581	(12,017)	71.1%
Periodicals					
Canada	21,581	18,245	11,097	7,148	164.4%
Mexico	1,556	1,624	2,668	(1,044)	60.9%
European Bilateral Group	14,457	16,944	18,428	(1,484)	91.9%
UPU Countries	27,487	31,802	49,515	(17,713)	64.2%
Parcel Post					
Canada	300	4,718	3,678	1,040	128.3%
Mexico	33	939	695	244	135.1%
European Bilateral Group	761	16,429	14,797	1,632	111.0%
UPU Countries	1,218	35,521	28,937	6,584	122.8%
International Surface Airlift (ISAL)					
Canada	N/A	N/A	N/A	N/A	N/A
Mexico	5,162	2,201	1,817	384	121.1%
European Bilateral Group	43,871	24,331	19,866	4,465	122.5%
UPU Countries	114,554	89,588	90,057	(469)	99.5%
Valuepost Canada 3/	-	-	-	-	-
Total Surface	259,195	$ 299,803	$ 310,880	(11,077)	96.4%
Airmail					
Letters and Letter Packages					
Canada	165,026	106,300	102,273	4,027	103.9%
Mexico	31,018	18,632	12,429	6,203	149.9%
European Bilateral Group	124,219	128,534	72,037	56,497	178.4%
UPU Countries	189,790	198,477	88,427	110,050	224.5%
Postcards, Postal Cards, & Aerogrammes					
Canada	7,999	3,175	3,391	(216)	93.6%
Mexico	966	386	181	205	213.3%
European Bilateral Group	33,663	17,237	13,036	4,201	132.2%
UPU Countries	20,382	10,500	3,869	6,631	271.4%

Footnotes and sources are on Table E-1 (continued).

TABLE E-1 (CONTINUED)
OUTBOUND INTERNATIONAL MAIL
SUMMARY OF FY 1998 INTERNATIONAL VOLUMES, REVENUE,
ATTRIBUTABLE COST AND COST COVERAGE
BY INTERNATIONAL MAIL CATEGORY AND TERMINAL DUES REGIME 1/

International Mail Category	Volume (1)	Revenue ($) (2)	Attributable Cost ($) 2/ (3)	Contribution ($) (4)=(2)-(3)	Cost Coverage (5)=(2)/(3)
Airmail (Continued)					
Printed Matter and Small Packets					
Canada	13,441	27,423	27,720	(297)	98.9%
Mexico	2,334	3,400	4,483	(1,083)	75.8%
European Bilateral Group	11,330	59,877	33,747	26,130	177.4%
UPU Countries	17,911	104,134	73,327	30,807	142.0%
Parcel Post					
Canada	1,265	18,217	14,532	3,685	125.4%
Mexico	111	2,811	2,616	195	107.5%
European Bilateral Group	1,052	35,075	25,785	9,290	136.0%
UPU Countries	1,813	67,926	54,965	12,961	123.6%
International Priority Airmail Service					
Canada	N/A	N/A	N/A	N/A	N/A
Mexico	1,241	627	282	345	222.3%
European Bilateral Group	17,227	10,397	7,062	3,335	147.2%
UPU Countries	34,376	28,194	14,756	13,438	191.1%
Bulk Letter Service to Canada 3/	-	-	-	-	-
Express Mail International Service					
Canada	359	7,671	4,354	3,317	176.2%
Mexico	690	12,833	10,198	2,635	125.8%
European Bilateral Group	652	20,232	13,121	7,111	154.2%
UPU Countries	2,992	84,628	50,693	33,935	166.9%
Total Air	679,857	$ 966,686	$ 633,284	$ 333,402	152.6%
Initiatives					
Global Priority Mail	4,219	30,265	38,886	(8,621)	77.8%
Global Package Link	1,513	23,630	26,635	(3,005)	88.7%
International Customized Mail	10,433	9,061	7,720	1,341	117.4%
Direct entry	16,837	3,351	3,115	236	107.6%
Total Initiatives	33,002	$ 66,307	$ 76,356	$ (10,049)	86.8%
Grand Total Outbound	972,054	$ 1,332,796	$1,020,520	$ 312,276	130.6%

1/ Mexico is part of the UPU terminal dues regime.

2/ Volume variable cost + product-specific cost

3/ See Table IV-2 for caveat

Source: FY 1998 ICRA Report, June 11, 1999, Pages A-3,A-4, A-5, A-7 ; Attributable cost for EURB/UPU split from pages B-4 & B-5, unit cost times volume, as applicable

THE POSTAL SERVICE'S REVISED TREATMENT OF INTERNATIONAL AIR TRANSPORTATION COSTS AND THE SETTLEMENT DIFFERENCE

The Postal Service submitted an FY 1998 ICRA Report – USPS Version on June 7, 1999. It reflected a revised methodology for calculating international air transportation costs and a revised treatment for the difference between imputed settlement costs and booked costs (the settlement difference). The change in the treatment of the latter cost only affects the calculation of incremental costs.

Settlement treatment. In the original ICRA submission, the Postal Service treated the settlement difference as an incremental cost of providing international mail service as a whole. In adjusting this treatment the Postal Service emphasized that the settlement difference was the result of a conservative approach to accruing settlement costs. The Postal Service continues to believe that the imputed values represent the cost consequence of current international volumes but it now apparently concludes that the booked values are less accurate measures of settlement costs than the imputed values, and therefore the booked values can be ignored. This treatment eliminates a component of incremental cost and would reduce the total incremental cost for international mail by $70 million (from $122 million to $52 million).

International air transportation costs treatment. In the original ICRA — PRC Version, submitted on March 15, the Postal Service cross-multiplied outbound volumes by unit air transportation costs, based on IAB cost information, to calculate an imputed value for international air transportation costs. The calculation produces an imputed value because it does not reflect the corresponding value in the Book of Accounts. For this reason, the Postal Service adjusted the imputed value to the level of the Book of Accounts' accrued value for international air transportation cost. Since the Book of Accounts figure was larger than the aggregate imputed value, the adjustment increased the imputed value.

In the Postal Service version filed June 7, 1999, the Postal Service adjusted the imputed value to the level of the actual payments. This is a level between the imputed value and the booked value. The imputed value of payments to carriers and the actual payments to air carriers differ from accrued expenses because international air transportation costs are accrued using the historical level of payments as a basis. Although the imputed value reflects the expected payment to carriers, sometimes the actual payment differs because of adjustments to the bill resulting from a change in routing or other differences. Accordingly, the Postal Service now believes that using the actual payments as the benchmark for the imputed value is the most accurate method for estimating the international air transportation cost of specific international mail services.

Table F-1 calculates the differences in attributable cost, contribution to institutional cost, and cost coverage for the standard services resulting from the revised Postal Service treatment of air transportation costs. Unit attributable costs that incorporate the revised approach are calculated in Table F-2 for the standard services. The corresponding adjustment of the Initiatives' cost is calculated in Table F-3.

Because of time constraints, the Commission did not ask the Postal Service to produce a PRC Version of the ICRA with the Postal Service's revised treatment. However, in Table F-2, the unit cost for standard services reflecting the revised approach was obtained by adjusting the total unit attributable costs from the revised ICRA — PRC Version submitted June 11, 1999, to reflect the Postal Service's revised international air transportation. The June 11 revised ICRA — PRC Version does not incorporate the two methodology changes discussed in this appendix.

Of the initiatives, only GPM was affected by the revised approach. In Table F-3, the attributable costs for GPM are adjusted, based on underlying Postal Service electronic workpapers, to reflect revised international air costs. Tables F-4 and F-5 calculate the effects of the change on attributable costs, contribution to institutional cost, and cost coverage.

TABLE F-1
COMPARISON OF REVENUE, ATTRIBUTABLE COST, CONTRIBUTION TO INSTITUTIONAL COST AND COST COVERAGE
FOR OUTBOUND SURFACE AND AIR INTERNATIONAL MAIL USING PRC METHODOLOGY UNADJUSTED
AND ADJUSTED FOR THE USPS' NEW METHODOLOGY FOR INTERNATIONAL AIR TRANSPORTATION COST
(Amounts in Thousands)

		PRC Total Attributable Costs			Contribution to Institutional Costs			Cost Coverage		
	Revenue (1)	Unadjusted (2)	Adjusted (3)	Adjusted minus Unadjusted (4)=(3)-(2)	Unadjusted (5)=(1)-(2)	Adjusted (6)=(1)-(3)	Adjusted minus Unadjusted (7)=(6)-(5)	Unadjusted (8)=(1)/(2)	Adjusted (9)=(1)/(3)	Percent Change (10)=(9)/(8)-1
OUTBOUND MAIL										
Surface										
1 Printed Matter & Small Packets, excl. ISAL & Per.	$ 57,461	$ 69,326	$ 69,326	$ -	$ (11,865)	$ (11,865)	$ -	83%	83%	0%
2 Periodicals	$ 68,615	$ 81,708	$ 81,708	$ -	$ (13,093)	$ (13,093)	$ -	84%	84%	0%
3 Parcel Post	$ 57,607	$ 48,107	$ 48,107	$ -	$ 9,500	$ 9,500	$ -	120%	120%	0%
4 Int'l Surface Airlift	$ 116,120	$ 111,739	$ 111,739	$ -	$ 4,381	$ 4,381	$ -	104%	104%	0%
5 ValuePost/Canada 1/	$ -	$ -	$ -	$ -	$ -	$ -	$ -	-	-	-
6 Subtotal, Surface	$ 299,803	$ 310,880	$ 310,880	$ -	$ (11,077)	$ (11,077)	$ -	96%	96%	0%
Air										
7 Letters and Letter Packages	$ 451,943	$ 275,166	$ 266,248	$ (8,918)	$ 176,777	$ 185,695	$ 8,918	164%	170%	3%
8 Postcards, Postal Cards, and Aerogrammes	$ 31,299	$ 20,477	$ 20,163	$ (314)	$ 10,822	$ 11,136	$ 314	153%	155%	2%
9 Printed Matter and Small Packets (AO)	$ 194,833	$ 139,277	$ 129,469	$ (9,808)	$ 55,556	$ 65,364	$ 9,808	140%	150%	8%
10 International Priority Airmail Service	$ 39,219	$ 22,101	$ 20,080	$ (2,021)	$ 17,118	$ 19,139	$ 2,021	177%	195%	10%
11 Bulk Letter Service to Canada 1/	$ -	$ -	$ -	$ -	$ -	$ -	$ -	-	-	-
12 Parcel Post	$ 124,029	$ 97,897	$ 88,904	$ (8,993)	$ 26,132	$ 35,125	$ 8,993	127%	140%	10%
13 Express Mail International Service	$ 125,363	$ 78,366	$ 74,020	$ (4,346)	$ 46,997	$ 51,343	$ 4,346	160%	169%	6%
14 Subtotal, Air	$ 966,686	$ 633,284	$ 598,884	$ (34,400)	$ 333,402	$ 367,802	$ 34,400	153%	161%	6%
15 Total Surface and Air	$1,266,489	$ 944,164	$ 909,764	$ (34,400)	$ 322,325	$ 356,725	$ 34,400	134%	139%	4%

1/ See caveat inTable IV-2, footnote 1

Source: Cols.1 & 2 from Table IV-2, Col. 2 or 5, as applicable; Col. 3 from Table F-2, Col.6.

TABLE F-2
DEVELOPMENT OF FY 1998 ATTRIBUTABLE COST FOR INTERNATIONAL MAIL USING PRC COSTING METHODOLOGY
WITH USPS REVISED METHODOLOGY FOR CALCULATING INTERNATIONAL TRANSPORTATION COST
(Amounts in Thousands)

U.S. Total International Mail Category	Volume (1)	PRC Unit Cost (2)	PRC Int'l Tp Unit Cost (3)	Int'l Tp Unit Cost (4)	Adjusted PRC Unit Cost (5)	Adjusted PRC Total attrib Cost (6)	Revenue (7)	Adjusted Cost Coverage (8)=(7)/(6)	Unadjusted Cost Coverage (9)
OUTBOUND MAIL									
Surface									
1 Printed Matter & Small Packets, excl. ISAL & Per.	28,215	$ 2.457	$ 0.127	$ 0.127	$ 2.457	$ 69,326	$ 57,461	82.9%	82.9%
2 Periodicals	65,082	$ 1.255	$ 0.028	$ 0.028	$ 1.255	$ 81,708	$ 68,615	84.0%	84.0%
3 Parcel Post	2,312	$ 20.808	$ 1.517	$ 1.517	$ 20.808	$ 48,107	$ 57,607	119.7%	119.7%
4 Int'l Surface Airlift	163,587	$ 0.683	$ 0.226	$ 0.226	$ 0.683	$ 111,739	$ 116,120	103.9%	103.9%
5 ValuePost/Canada 1/	-	$ -	$ -	$ -	-	-	-	-	-
6 Subtotal, Surface	259,196	-	-	-	-	$ 310,880	$ 299,803	96.4%	96.4%
Air									
7 Letters and Letter Packages	510,053	$ 0.538	$ 0.077	$ 0.061	$ 0.522	$ 266,248	$ 451,943	169.7%	164.2%
8 Postcards, Postal Cards, and Aerogrammes	63,010	$ 0.324	$ 0.017	$ 0.013	$ 0.320	$ 20,163	$ 31,299	155.2%	152.8%
9 Printed Matter and Small Packets (AO)	45,017	$ 3.090	$ 0.969	$ 0.755	$ 2.876	$ 129,469	$ 194,833	150.5%	139.9%
10 International Priority Airmail Service	52,843	$ 0.418	$ 0.152	$ 0.114	$ 0.380	$ 20,080	$ 39,219	195.3%	177.5%
11 Bulk Letter Service to Canada 1/	-	-	-	-	$ -	$ -	$ -	-	-
12 Parcel Post	4,240	$ 23.064	$ 9.872	$ 7.776	$ 20.968	$ 88,904	$ 124,029	139.5%	126.7%
13 Express Mail International Service	4,694	$ 16.681	$ 3.722	$ 2.810	$ 15.769	$ 74,020	$ 125,363	169.4%	160.0%
14 Subtotal, Air	679,857	-	-	-	-	$ 598,884	$ 966,686	161.4%	152.6%
15 Total Surface and Air	939,053	-	-	-	-	$ 909,764	$ 1,266,489	139.2%	134.1%

1/ See caveat in Table IV-2, footnote 1

Source: Col.1 from Table IV-4; Cols.2 & 3 from FY 1998 ICRA Report-PRC Version, p.B-1; Col.4 from FY 1998 ICRA Report-USPS Version, p.B-1;
Col.5 = Col.2-Col.3+Col.5; Col.6 = Col.1 x Col.5; Col.7 from Table IV-2; Col. 9 from Table IV-4.

TABLE F-3
DEVELOPMENT OF ATTRIBUTABLE COST FOR GLOBAL PRIORITY MAIL USING THE 6/11/99 ICRA REPORT-PRC VERSION AND THE POSTAL SERVICE'S NEW METHODOLOGOGY FOR INTERNATIONAL AIR TRANSPORTATION COST
(Amounts in Thousands)

	Cost Segments/Components	Source	PRC Version (3/15/99) (1)	USPS Version (6/7/99) w/ new int'l Air Trans Cost (2)	PRC Version (6/11/99) w/ new Int/l 1/ Air Trans Cost (3)
1	Total Cost Segement Costs excluding CS 1	Sheet: Cost Segment, Cell X19	$ 8,863	$ 6,004	$ 8,904
2	Domestic Rail Cost	Sheet: Domestic Trans, Cell AV47	$ 324	$ 326	$ 326
3	Domestic Other Transprtation Cost	Sheet: Domestic Trans, Cell AB183	$ -	$ -	$ -
4	Domestic Highway Cost	Sheet: Domestic Trans, Cell P138	$ 181	$ 181	$ 181
5	Domestic Water Cost	Sheet: Domestic Trans, Cell P 227	$ 3	$ 3	$ 3
6	International Air Transportation Cost	Sheet: Intl Trans & Adj., Cell G217	$ 5,608	$ 4,219	$ 4,219
7	Terminal Dues	Sheet: Intl Trans & Adj., Cell L217	$ 4,883	$ 4,883	$ 4,883
8	Transit&Air Conveyance costs	Sheet: Intl Trans & Adj., Cell M217	$ 70	$ 70	$ 70
9	Subtotal,	Sum of Lines 1 thru 8	$ 19,933	$ 15,686	$ 18,586
10	Product-Specific Cost	ICRA Report, p.A-1	$ 18,913	$ 18,913	$ 18,913
11	Total Attributable Cost	L.10 + L.11	$ 38,846	$ 34,599	$ 37,499
12	Reconciliation Total	ICRA Report, p.A-7	$ 38,845	$ 34,599	N/A
13	Reconciliation Difference	L. 12 - L. 11	$ (1)	$ (0)	N/A

Note on Sources: For USPS, Sheet references are for File ICRAusp3.XLS
For PRC (3/15/99), Sheet references are for File ICRAPRC5.XLS

1/ Line 1 costs are obtained from the international cost segments and components report accompanying the FY 1998 ICRA Report-PRC Version, 6/11/99. All other costs come from column 2.

TABLE F-4
DEVELOPMENT OF ATTRIBUTABLE COST
FOR OUTBOUND MAIL- STANDARD SERVICE AND INITIAITVES -
ADJUSTED TO REFLECT THE NEW USPS METHOD FOR
INTERNATIONAL AIR TRANSPORTATION COST
(Amounts in Thousands)

Outbound Categories	PRC Version (6/11/99) (1)	PRC Version (6/11/99) w/ new Int/l 1/ Air Trans Cost (2)	Reduction in Attributable Costs (3)=(2)-(1)
1 Standard Services	$ 944,164	$ 909,764	$ (34,400)
Initiatives			
2 Global Priority Mail	$ 38,886	$ 37,499	$ (1,387)
3 Global Package Link	$ 26,635	$ 26,635	$ -
4 Direct Entry/Inbound	$ 3,115	$ 3,115	$ -
5 International Customized Services	$ 7,720	$ 7,720	$ -
6 Subtotal, Initiatives	$ 76,356	$ 74,969	$ (1,387)
7 Total Outbound	$ 1,020,520	$ 984,733	$ (35,787)

Sources:
Line 1 -- Table E-1, L.15, Col. 2 or Col. 3, as applicable.
Line 2 -- Col. 1 from Table IV-2, L.15, Col. 5.
Col. 2 from Table F-3, L. 11, Col. 3.
Lines 3, 4, & 5 from Table IV-2, Col. 2, Lines 16, 17, or 18, as applicable.
Line 6 = Sum of Lines 2 thru 5.
Line 7 = L. 1 + L. 6.

TABLE F-5
COMPARISON OF REVENUE, ATTRIBUTABLE COST, CONTRIBUTION TO INSTITUTIONAL COST AND COST COVERAGE
FOR INTERNATIONAL MAIL - STANDARD SERVICES AND INITIATIVES - USING PRC METHODOLOGY UNADJUSTED
AND ADJUSTED FOR THE USPS' NEW METHODOLOGY FOR INTERNATIONAL AIR TRANSPORTATION COST
(Amounts in Thousands)

		Attributable Costs			Contribution to Institutional Cost			Cost Coverage		
Outbound Categories	Revenue (1)	PRC Version (6/11/99) (2)	PRC Version (6/11/99) w/ new Int/l 1/ Air Trans Cost (3)	Reduction in Attributable Costs (4)=(2)-(3)	PRC Version (6/11/99) (5)=(1)-(2)	PRC Version (6/11/99) w/ new Int/l 1/ Air Trans Cost (6)=(1)-(3)	Increase in Contribution (7)=(6)-(5)	PRC Version (6/11/99) (8)=(1)/(2)	PRC Version (6/11/99) w/ new Int/l 1/ Air Trans Cost (9)=(1)/(3)	Percent Change (10)=((9)/(8))-1
Standard Services	$ 1,266,489	$ 944,164	$ 909,764	$ (34,400)	$ 322,325	$ 356,725	$ 34,400	134.1%	139.2%	3.8%
Initiatives										
Global Priority Mail	$ 30,265	$ 38,886	$ 37,499	$ (1,387)	$ (8,621)	$ (7,234)	$ 1,387	77.8%	80.7%	3.7%
Global Package Link	$ 23,630	$ 26,635	$ 26,635	$ -	$ (3,005)	$ (3,005)	$ -	88.7%	88.7%	0.0%
Direct Entry/Inbound	$ 3,351	$ 3,115	$ 3,115	$ -	$ 236	$ 236	$ -	107.6%	107.6%	0.0%
International Customized Service	$ 9,061	$ 7,720	$ 7,720	$ -	$ 1,341	$ 1,341	$ -	117.4%	117.4%	0.0%
Subtotal, Initiatives	$ 66,307	$ 76,356	$ 74,969	$ (1,387)	$ (10,049)	$ (8,662)	$ 1,387	86.8%	88.4%	1.8%
Total Outbound	$ 1,332,796	$1,020,520	$ 984,733	$ (35,787)	$ 312,276	$ 348,063	$ 35,787	130.6%	135.3%	3.6%

Source: Col.1 = Table IV-2, Col.2, L.6+L.14; Col.2 = Table IV-2, Col.5, L.6+L.14; Col. 3 = Table F-4, Col.2, as applicable.

The effects of these revised unit attributable costs on aggregate and individual international mail services are developed in Tables F-6, F-7, and F-8 of this appendix. In Table F-6, settlement differences in the amount of $70 million are excluded from the incremental cost in accordance with the Postal Service's revised treatment. The remaining incremental costs are equal to the IBU overhead cost in the amount of $52 million. Both figures are obtained from the ICRA Report – PRC Version submitted June 11, 1999 at page A-1, Footnote 3.

Table F-7 displays the impact of revised attributable air transportation costs on the cost coverages of individual international mail products.

Table F-8 is a summary of FY 1998 revenue and attributable costs for international mail, similar to Table IV-1 in the body of this report except that it reflects both the air transportation and settlement cost methodologies now favored by the Postal Service.

TABLE F-6
EFFECT OF USING THE POSTAL SERVICE'S METHOD FOR CALCULATING INTERNATIONAL AIR TRANSPORTATION AND SETTLEMENT COSTS
(Amounts in Thousands)

Category	Reduction in Attributable Cost ($) (1)	Increase in Contribution to Institutional Cost ($) (2)	Unadjusted Cost Coverage (3)	Adjusted Cost Coverage (4)
Outbound Mail	(35,787)	35,787	130.6%	135.3%
Inbound Mail	-	-	98.2%	98.2%
Subtotal	(35,787)	35,787	123.5%	127.0%
Int'l Mail Incremental Cost	-	70,242	-	-
Grand Total	$ (35,787)	$ 106,029	112.9%	122.0%

Source: Line 1 from Appendix F, Table F-5, Line 7; Line 2 = No effect on inbound mail; Line 4 = Table IV-1, L.4 - Table F-8, L.4. Reflects ICRA Report released 6/11/99.

TABLE F-7
EFFECT OF USING THE POSTAL SERVICE'S METHOD
FOR CALCULATING INTERNATIONAL AIR TRANSPORTATION COSTS
ON INTERNATIONAL ATTRIBUTABLE COST

	Reduction in Attributable Cost ($) (1)	Increase in Contribution to Institutional Cost ($) (2)	Unadjusted Cost Coverage (3)	Adjusted Cost Coverage (4)
OUTBOUND MAIL				
Surface				
Printed Matter & Small Packets, excl. ISAL & Per.	-	-	82.9%	82.9%
Periodicals	-	-	84.0%	84.0%
Parcel Post	-	-	119.7%	119.7%
Int'l Surface Airlift	-	-	103.9%	103.9%
ValuePost/Canada 1/	-	-	-	-
Subtotal, Surface	-	-	96.4%	96.4%
Air				
Letters and Letter Packages	(8,918)	8,918	164.2%	169.7%
Postcards, Postal Cards, and Aerogrammes	(314)	314	152.8%	155.2%
Printed Matter and Small Packets (AO)	(9,808)	9,808	139.9%	150.5%
International Priority Airmail Service	(2,021)	2,021	177.5%	195.3%
Bulk Letter Service to Canada 1/	-	-	-	-
Parcel Post	(8,993)	8,993	126.7%	139.5%
Express Mail International Service	(4,346)	4,346	160.0%	169.4%
Subtotal, Air	$(34,400)	$34,400	152.6%	161.4%
Initiatives				
Global Priority Mail	(1,387)	1,387	77.8%	80.7%
Global Package Link	-	-	88.7%	88.7%
Direct Entry/Inbound	-	-	107.6%	107.6%
International Customized Services	-	-	117.4%	117.4%
Subtotal, Initiatives	$(1,387)	$1,387	86.8%	88.4%
Total Outbound	$(35,787)	$ 35,787	130.6%	135.3%

1/ See caveat in Table IV-2, footnote 1
Source: For surface & air use Appendix F, Table F-1, Cols. 4, 7, 8, & 9, as applicable;
for initiatives, use Appendix F, Table F-5, Cols. 4, 7, 8, & 9, as applicable.

TABLE F-8
SUMMARY OF FY 1998 REVENUE AND ATTRIBUTABLE COST
FOR OUTBOUND AND INBOUND INTERNATIONAL MAIL
USING USPS NEW METHOD FOR ESTIMATING
INTERNATIONAL AIR TRANSPORTATION COST AND SETTLEMENT COST
(Amounts in Thousands)

Category	Revenue ($) (1)	Attributable Cost ($) (2)	Incremental Cost ($) (3)	Total Attributable Cost ($) (4)	Contribution ($) (5)=(1)-(2)	Cost Coverage (6)=(1)/(4)
Outbound Mail	1,332,796	984,733	-	984,733	348,063	135.3%
Inbound Mail	282,311	287,379	-	287,379	(5,068)	98.2%
Subtotal	1,615,107	1,272,112	-	1,272,112	342,995	127.0%
Int'l Mail Incremental Cost	-	-	52,203	52,203	$ (52,203)	-
Grand Total	$1,615,107	$1,272,112	$ 52,203	$1,324,315	$ 290,792	122.0%

Note: The attributable costs reflect the FY 1998 ICRA Report - PRC Version, submitted 6/11/99.

Source: Table IV-2, except Line 1, Col.2 = Appendix F, Table F-4, Col.2, L. 7 and Line 4, Col. 3 is from the FY 1998 ICRA Report - PRC Version, June 11, 1999, p.A-1, footnote 3.

REFERENCE MATERIAL – POSTAL SERVICE VIEWS

This appendix provides two Postal Service documents for reference: a chart that relates international domestic services; and the Postal Service description of how it develops international mail rates.

Response to Question 23 of the Second Notice of International Mail Data Requirements, Order No. 1236.

23. For each of the international categories shown in the list of appended to Order No. 1228, please indicate what the Postal Service considers to be the most closely analogous subclass of domestic mail and discuss the reasons for these conclusions.

    See the following attachment.

International Outbound Product	Like Domestic Product	Characteristic	Weight	Options	Competition
etters & Letter Packages (LC)	First-Class Mail	LC contains personal handwritten or typewritten communictions having the character of current correspondence and AO which is like First-Class Mail	International ranges from 0 to 4 pounds while domestic goes to 11 ounces.	Domestic has presorted and automation rates while international is only single piece.	Domestic has a monopoly while international is under direct competition
nternational Priority Airmail Service (IPA)	First-Class Mail	Any item of the LC or AO classification can go IPA which is the same as First-Class Mail	International has a 4 pound maximum for LC and an 11 pound maximum when AO is included while domestic goes to 11 ounces.	IPA is a bulk service requiring a sort to country and minimum number of pieces while the various levels of presort requirements are more severe.	Domestic has a monopoly while international is under direct competition
Bulk Letters to Canada	First-Class Mail	Any letter of the LC or AO classification can go Bulk Letters to Canada which is the same as First-Class Mail	International has a 3 ounce maximum while domestic goes to 11 ounces.	Bulk letters to Canada requires 500 three ounce letters or more and sorted to the providences in Canada similar to presort at its highest level.	Domestic has a monopoly while international is under direct competition
Global Priority Mail (GPM)	First-Class Mail	Any item of the LC or AO classification can go GPM which is the same as First-Class Mail	International ranges from 0 to 4 pounds while domestic goes to 11 ounces.	Domestic has presorted and automation rates while international is only single piece.	Domestic has a monopoly while international is under direct competition
Postcards & Aerogrammes	Post Cards	same as domestic Postcards	same	same	Domestic has a monopoly while international is under direct competition
r Other Articles (AO)	Standard A & Periodicals	Contains printed matter, books, sheet music, publishers periodicals. This mail can not be considered personal correspondence.	International this mail can go to 11 pounds while domestic 1 pound Domestic there is a flat rate for the first 3 ounces	International this mail flies while domestic standard A is a surface product which can require deposit at a destinating office.	Both domestic and international face competition except international is faced with other Posts operating acceptance offices and processing plants in this country accepting and sorting US origin mail going to other countries
Surface Other Articles (AO)	Standard A & Periodicals	same as above	same as above	This mail goes by boat to the destination	same as above

International Outbound Product	Like Domestic Product	Characteristic	Weight	Options	Competition
Letters & Letter Packages (LC)	First-Class Mail	LC contains personal handwritten or typewritten communictions having the character of current correspondence and AO which is like First-Class Mail	International ranges from 0 to 4 pounds while domestic goes to 11 ounces.	Domestic has presorted and automation rates while international is only single piece.	Domestic has a monopoly while international is under direct competition
International Priority Airmail Service (IPA)	First-Class Mail	Any Item of the LC or AO classification can go IPA which is the same as First-Class Mail	International has a 4 pound maximum for LC and an 11 pound maximum when AO is included while domestic goes to 11 ounces.	IPA is a bulk service requiring a sort to country and minimum number of pieces while the various levels of presort requirements are more severe.	Domestic has a monopoly while international is under direct competition
Bulk Letters to Canada	First-Class Mail	Any letter of the LC or AO classification can go Bulk Letters to Canada which is the same as First-Class Mail	International has a 3 ounce maximum while domestic goes to 11 ounces.	Bulk letters to Canada requires 500 three ounce letters or more and sorted to the providences in Canada similar to presort at its highest level.	Domestic has a monopoly while international is under direct competition
Global Priority Mail (GPM)	First-Class Mail	Any item of the LC or AO classification can go GPM which is the same as First-Class Mail	International ranges from 0 to 4 pounds while domestic goes to 11 ounces.	Domestic has presorted and automation rates while international is only single piece.	Domestic has a monopoly while international is under direct competition
Postcards & Aerogrammes	Post Cards	same as domestic Postcards	same	same	Domestic has a monopoly while international is under direct competition
Air Other Articles (AO)	Standard A & Periodicals	Contains printed matter, books, sheet music, publishers periodicals This mail can not be considered personal correspondence	International this mail can go to 11 pounds while domestic 1 pound Domestic there is a flat rate for the first 3 ounces	International this mail flies while domestic standard A is a surface product which can require deposit at a destinating office	Both domestic and international face competition except international is faced with other Posts operating acceptance offices and processing plants in this country accepting and sorting US origin mail going to other countries
Surface Other Articles (AO)	Standard A & Periodicals	same as above	same as above	This mail goes by boat to the destination	same as above

International Outbound Product	Like Domestic Product	Characteristic	Weight	Options	Competition
nternational Surface Airlift ISAL)	Standard A & Periodicals	same as above	same as above	ISAL is airlifted to the destination and then surface	same as above
Valuepost to Canada	Standard A & Periodicals	same as above	International there is a 2 pound weight limit for a piece. You must have 50 pounds of letters or 100 pounds of flats.	This mail is trucked the same as standard A.	same as above
Express Mail	Express Mail	No service guarantee for Express International. Customs is a hugh difference for international merchandise. A separate agreement with each country is required.	Maximum weights could be different for each country		Competition for parcels is probably about the same
Air Parcel Post	Priority Mail	Customs is an issue. A different delivery rate for each country.	Maximum weights could be different for each country		Competition for parcels is probably about the same
Surface Parcel Post	Standard B	Customs is an issue. A different delivery rate for each country.	Maximum weights could be different for each country		Competition for parcels is probably about the same
Global Package Link (GPL)	Express Mail & Priority Mail	This product includes special software to provide customs preadvice. There is a large overhead for this. It is restricted to a few countries. A different delivery rate for each country	Maximum weights could be different for each country		Competition for parcels is probably about the same
International Customized Mail (ICM)	Nothing	These are contract with specific customers going to certain countries with a known product. To qualify you need to have a minimum amount to mail.			
Direct Entry	Nothing	This service uses the domestic rates at the destinating country for delivery charges.			
Canada Admail	Nothing	This product is one of the direct entry products.			
International Special Services	Special Services	same as domestic except for requirements within destinating country			

Response to Question 18 of the Second Notice of International Mail Data Requirements, Order No. 1236.

18. Please provide the information on rate design described at page 6 of order No. 1228. (See the first full paragraph of page 6.)

Page 6 of PRC Order No. 1228 asks that the Postal Service provide the Commission enough documentation to allow the calculation and reporting of the cost coverage for each subclass of international mail. Material has already been furnished by the Postal Service to allow such calculations to be made by the Commission. In addition, Order No. 1228 also discusses rate design information necessary to demonstrate how the Postal Service designs the rate for each constituent rate category. The information should allow the Commission to determine whether the difference between the category rate and the base rate for the subclass to which it belongs reflects its added or avoided costs. The information below addresses this request.

General

The following discussion outlines the assumptions and approach underlying the development of international rate levels and the structure specific to each international mail class, subclass, and rate category.

Classification of Mail

Mail class is identified according to the nomenclature and definitions described in the Convention Agreements of the Universal Postal Union (UPU). The *International Mail Manual* provides further descriptive information. There are three basic classes of international mail:

Letters & Cards (LC):	Items weighing up to 2 kilograms (64 ounces).
Printed Matter (AO):	Items consisting of printed papers, literature for the blind and small packets. Weight limits are 2 kilograms for small packets, 5 kilograms for printed papers, and 7 kilograms for literature for the blind.
Parcels:	Parcel post is similar to domestic Standard (B) mail. Merchandise is permitted, but written communications having the nature of current and personal correspondence are not permitted.

These three classes of international mail service are also delineated by air and surface modes of transportation where the transportation mode equates roughly to priority and non-priority levels of service.

Within these three classes, subclasses/rate and product categories can be identified. Within the LC class, these include post cards, aerogrammes, Global Priority Mail, international priority airmail and bulk letters to Canada. Within the AO class, regular printed matter, publishers' periodicals, books and sheet music, international surface airlift (ISAL), and Valuepost Canada are defined.

Within parcels, a distinction is made by mode of transportation; namely, surface and air, and by geographic region.

In addition to these three major classes of mail, the Postal Service also offers an expedited service simply named International Express Mail Service.

Basic Principles

The development of international rates conforms to the statutory criteria of 39 U.S.C. 101 and 403. Factors used to develop international mail rates in some respects parallel those used in domestic rate setting; namely, international mail must cover its direct and indirect costs; international mail must make an appropriate contribution to all other costs, and derivation of

International mail rates must consider the environmental conditions of the market it serves. In general, the following principles are followed when setting international mail rates.

1. Outbound rates are based on outbound costs.
2. Costs are estimated in a manner similar to domestic cost estimation.
3. Rate development follows a bottom up approach. Unlike domestic rate development where base rates are reduced by a cost avoidance/cost savings factors, International rates are set by establishing markups and cost coverage targets.
4. Markups are applied to estimates of unit cost.
5. Unit costs are developed by component and identified according to three basic categories: non-transportation, transportation, and settlement charges.
6. Markups are based upon market factors and recognition that all outbound services are subject to competitive forces and substitute services.
7. Rate differences are a function of cost differences and the markups applied to unit costs.

Rate Design

As a brief historical note, it had been the practice, through the February 1985 international change in rates, to configure outbound international postage rates on total combined inbound/outbound international costs. This had the effect of burdening outbound ratepayers with the cost of delivery of foreign-origin inbound international mail. With the suspension of the Private Express Statutes in September 1986, the subsequent change in international postage rates in April 1988 departed from pooling inbound and outbound costs. It should be understood that since April 1988, outbound international postage rates have been designed solely on outbound costs. There has been no exception to the approach over the past eleven years.

International rates are predicated on specific cost drivers identified with providing outbound international mail service. The costs that are taken into account for each category of mail include domestic handling and domestic transportation, international transportation, and the cost of delivery in each country of destination. Domestic handling and domestic transportation are factors pertinent, for example, in the development of ISAL and IPA gateway rates. International transportation is a cost driver which, in conjunction with foreign delivery costs, contributes to the construction of rate groups for ISAL, IPA, EMS, printed matter, and air parcels. Transportation costs conform to Department of Transportation (DOT) rates for U.S. flag carriers. ISAL transportation costs, however, are contract rates and are generally lower than DOT rates. Transportation and delivery charges are also primary factors in considering the development of country specific rates.

There are three basic types of delivery charges, each of which can contribute to the design of a particular rate structure, and influence the construction of rate groups. *Terminal dues* apply to the distribution and delivery of LC and AO categories of international mail. *Imbalance charges* apply to the distribution and delivery of EMS items; while *inward land rates* apply to parcel post items.

Terminal dues are promulgated by the Universal Postal Union (UPU). Currently there are three structures that UPU members can invoke: (i) a flat rate set at 3.427 SDR/kg, (ii) a revision mechanism rate set at 0.14 SDR/item plus 1.0 SDR/kg, and (iii) a bulk mail option whose rate may not be higher than those calculated on the basis of 67% of the charge for a 20 gram domestic letter rate or exceed 0.204 SDR/item plus 1.46 SDR/kg. A separate, lower rate of 0.653 SDR/kg applies to M-bags. The UPU does permit administrations to enter into bilateral or multilateral payment agreements to settle their terminal dues accounts. The UPU establishes terminal dues rates at Congress, which is held once every five years. However, the Postal Operations Council of the UPU can amend terminal dues rates between Congresses. Such amendments have generally applied to revisions in the rates for the bulk mail option.

Imbalance charges for EMS items are set by each individual postal administration. Likewise *inward land rates* for parcel post items are determined by each UPU member and can be revised annually.

Important parameters to measure with respect to applying all possible terminal dues options are the total weight and the number of items per kilogram (IPK) exchanged with major mail trading partners. Estimates of IPKs are statistically determined.

Changes in the structure and level of terminal dues, imbalance charges, and inward land rates contribute to the definition of rate groups, rate structure, and mail acceptance procedures. Delivery structures that have an explicit item component and weight component have, for example, driven the rate design for IPA and ISAL from weight-based (rate/pound) to a rate per item plus a rate per pound.

Market factors are also relevant considerations in setting international rates. Both markups and mail preparation schemes are taken into account. Development of the Air LC rate provides a good illustration of how these two factors were used to alter its link with domestic First-Class Mail rates. Prior to 1988, the first half-ounce Air LC rate was set at twice the domestic first ounce rate. This rule of thumb, together with the charge for the additional weight increments, had the effect of over-pricing international air letters. This practice was abandoned in April 1988. Had it remained in effect, the first half-ounce Air LC rate, effective May 30, 1999, would be changing to 66 cents. The Postal Service believes that this change in methodology contributed to the reversal of the downward trend in international mail volume and revenue through fiscal year 1988, and was responsible for the growth in international volume and revenue for the period 1989 through 1996.

A description of each mail offering follows.

Air LC: Consists of personal correspondence, statements of accounts, and other business oriented transactions posted at single piece rates. Mailers are typically individuals, households, and small business enterprises. Air letters receive First-Class Mail service in the United States, are dispatched by the most expeditious transportation available, and receive airmail or priority treatment in the country of destination. The rate structure is weight-based and is currently unzoned. Air LC is offered as a universal service. Consistent with moderating the institutional cost burden on this category of mail, the May 1999 international rate change does not increase Air LC from those implemented on July 9, 1995. Separate rates are developed for Canada, Mexico, and rest of the world.

International Priority Airmail (IPA): IPA is a bulk air letter product. It provides business mailers with a service that is as fast or faster than regular airmail. Mailers must meet a minimum ten-pound volume requirement. The current rate design provides for both a presort and non-presort option. The presort option requires separation by country of destination. The rate levels for 1998, however, are not the result of applying cost avoidance factors to the single piece Air LC rates.

Bulk Letter Service to Canada: This service was introduced for business mailers mailing quantities of bulk letters to Canada. A minimum of 500 pieces weighing three ounces or less is required to qualify for this service. Mailers are also required to tray their mail and apply a Canadian post code to each mail piece. The rates for this service represent a fixed reduction from the single piece rate. The reduction was determined on the basis of cost coverage and not on cost avoidance.

Aerogrammes and Post Cards: Aerogrammes are designed for personal correspondence. An aerogramme consists of a single page that folds into a self-sealing envelope. Aerogrammes are very light weight and have little rigidity. Post cards are a non-sealed medium for personal and business communications similar to domestic post cards, with the exception that different size standards apply to international cards. Both services are offered with a flat per item rate. The

aerogramme rate is universal, while a separate card rate applies to Canada, Mexico, and the rest of the world.

(AO) Printed Matter and Small Packets: Printed matter has two levels of service. Surface printed matter is a non-priority service. It includes regular printed matter, books and sheet music, and publishers' periodicals. The long-term trend for surface printed matter has been down. Separate surface printed matter rates apply to Canada, Mexico, and the rest of the world. Rate increases to Mexico and the rest of the world are being implemented in phases to mitigate hardship on the publishing industry. Air printed matter is a priority service whose overall long-term trend has shown steady growth in revenue, pieces and weights. As a priority printed matter service, its cost coverage has been sufficiently high so as not to be impacted by the terminal dues changes which have impacted surface printed matter. Air printed matter is priced according to geographic regions taking into account transportation costs and terminal dues differences.

Publishers' Periodicals: Publishers' Periodicals is one of the three subclassifications of surface printed matter. The service is offered only to publishers and registered newsagents for mailings that would qualify as periodicals under the domestic classification. Similar to other surface offerings, Publishers' Periodicals have experienced a decline in revenue, pieces, and weight since postal reorganization. The rate design recognizes separate rates to Canada, Mexico, and the rest of the world according to terminal dues regime and transportation expense. Changes in UPU terminal dues have resulted in a phased implementation of Publishers' Periodical rates to Mexico and the rest of the world. The UPU convention allows Publishers' Periodical rates to be reduced up to 50% from regular printed matter rates.

International Surface Air Lift (ISAL): ISAL is a bulk mailing service for the delivery of publications, advertising mail, catalogs, directories, other printed matter, and small packets. Mailers must meet a 50-pound minimum mailing requirement. ISAL requires mailer presort by country. Like IPA, ISAL rate design recognizes geographic regions based upon terminal dues and transportation characteristics. The geographic regions are the same for both services. ISAL receives air treatment within the United States, and air transportation to its overseas destination. Surface transportation is provided at destination. ISAL rate design provides for threshold volume discounts for large mailers. The threshold incentives are similar to IPA. When ISAL rates were revised in February 1998, ISAL sustained a rate increase because of a terminal dues change affecting printed matter categories.

ValuePost/Canada: ValuePost Canada is a bulk mailing service for the delivery of regular printed matter, books and sheet music, publishers' periodicals, and small packets. It was introduced as an ISAL equivalent service taking particular account of the terminal dues applicable to mail exchanged with Canada Post Corporation. The rate design recognizes shape, namely, letters and flats. Within shape, a per item rate applies to letters weighing up to one ounce, and a per item rate applies to flats weighing up to five ounces. An item plus pound rate applies to letters and flats exceeding the one ounce and five ounce thresholds, respectively.

M-Bag Service: M-Bag service allows a mailer to prepare a direct sack of printed matter weighing between 11 pounds and 66 pounds to a single address. A reduced terminal dues rate of 0.653 SDR/kg applies and recognizes reduced delivery cost because the M-bag does not require sortation to multiple addresses. The rate design is a simple weight-based charge.

Global Priority Mail (GPM): Global Priority Mail is an expedited airmail letter service providing fast, reliable delivery of all items mailable as letters and merchandise up to four pounds. The service is targeted to specific countries based on market considerations. Rate design provides both a flat rate for small and large envelopes, and single piece weight-based rates. LC terminal dues rates apply to the delivery of GPM, however, the level of service is better since its Expres endorsement accords it special delivery treatment in the country of destination.

Global Package Link (GPL): Global Package Link is a bulk mailing service that provides fast, economical international delivery of packages containing merchandise. A customs pre-advisory option offers convenience and affordability to parcel mailers. GPL is the only bulk parcel service offered internationally by the Postal Service. The rate design is country specific due to the different delivery charges assessed by the countries participating as GPL partners. The rate levels were initially set with a target cost coverage of 130%, however, the world economic slowdown has adversely impacted the volume growth, thus causing fixed costs to be distributed over fewer pieces. GPL rates were increased 9% last December with the expectation of achieving breakeven in the face of declining volumes.

Express Mail Service (EMS): International EMS is the fastest delivery service offered for the delivery of international items by the Postal Service. EMS items may consist of documents and merchandise. The service is offered to approximately 180 countries. EMS expedites urgent letters, small packages, and documents to the country of destination where they are handled and delivered on a priority basis by either a local postal administration or private courier. Rate design considerations have recognized both geographic regions and country specific markets.

Parcel Post: International surface parcel post is comparable to domestic zone-rated parcel post in that it is a non-priority service. It is appropriate for mailing merchandise, printed matter or other items not required to be mailed at letter rates. Written communications having the character of personal correspondence may not be enclosed in parcel post packages. The maximum weight limit for parcel post varies from 11 to 70 pounds, depending on country of destination. International air parcel post is a priority service that can be compared to domestic priority mail service. Weight limitations also apply as specified by the country of destination. Both services are designed as single piece offerings. Anomalies between surface and air parcel rates, however, are a function of the non-transportation costs estimated for each of the two parcel categories.

Mr. MCHUGH. General Henderson, we thank you for your time. I think we've established, if nothing else, we have some very significant challenges in front of us. There are obviously differing opinions as to how those challenges should be met, what role both you and the Congress should play. If nothing else, I hope we've taken a step closer to the realization that this is not theory any longer, that the Postal Service that tens of millions of Americans rely upon each and every day is entering a new era, as we've heard, and that associated with that is going to have to come some sorts of changes. Depending on the eye of the beholder, it may be beautiful or otherwise, but something needs to be done that is different than status quo.

Toward that end, and I know I can speak for all of the members on this subcommittee, both sides of the aisle, we want to engage with you in an honest and open and, we hope, productive dialog on how we can make those changes happen so that communications in America are continued to be conducted under an umbrella of confidence and reliability on postal services provided for some 200 plus years in this country, and we thank you for your effort. We particularly thank the postal workers, the folks we see on the streets every day and who sort and route the mail. They do a tremendous job.

We will be submitting questions for the record. You've kindly offered to provide some information to some of the Members. We welcome your response on that as well.

With that, the hearing is adjourned.

[Whereupon, at 12:45 p.m., the subcommittee was adjourned.]

○