

UNITED STATES POSTAL SERVICE REFORM: THE INTERNATIONAL EXPERIENCE

JOINT HEARING
BEFORE THE
SUBCOMMITTEE ON POST OFFICE
AND CIVIL SERVICE
OF THE
COMMITTEE ON
GOVERNMENTAL AFFAIRS
UNITED STATES SENATE
AND THE
SUBCOMMITTEE ON THE POSTAL SERVICE
OF THE
COMMITTEE ON
GOVERNMENT REFORM AND OVERSIGHT
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JANUARY 25, 1996

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UNITED STATES POSTAL SERVICE REFORM: THE INTERNATIONAL EXPERIENCE

THURSDAY, JANUARY 25, 1996

U.S. SENATE, SUBCOMMITTEE ON POST OFFICE AND CIVIL
SERVICE, OF THE COMMITTEE ON GOVERNMENTAL
AFFAIRS, AND
U.S. HOUSE OF REPRESENTATIVES, SUBCOMMITTEE ON
THE POSTAL SERVICE, OF THE COMMITTEE ON GOVERN-
MENT REFORM AND OVERSIGHT,

Washington, DC.

The Subcommittees met, pursuant to notice, at 9:38 a.m., in room SD-342, Dirksen Senate Office Building, Hon. Ted Stevens (Chairman of the Subcommittee on Post Office and Civil Service) and Hon. John McHugh (Chairman of the Subcommittee on the Postal Service) presiding jointly.

Present: Senators Stevens and Pryor; Representatives McHugh, Sanford, Collins, and Green.

Chairman STEVENS. Good morning. I am very pleased to be able to hold this joint hearing of the Senate Subcommittee on Post Office and Civil Service and the House Subcommittee on the Postal Service.

Let me thank our guests, whom I will introduce in a few moments, but it is a pleasure to chair this joint hearing with you, Mr. Chairman. Let me yield to Chairman McHugh of the House Subcommittee to make his statement first, please.

OPENING STATEMENT OF CONGRESSMAN McHUGH

Mr. McHUGH. Thank you very much, Mr. Chairman, Senator Stevens. Let me begin by thanking you for all of your efforts, not just in the case of this hearing but in fact over a good number of years with respect to many issues but certainly, principally among those concerning the Postal Service.

I might say also, as someone who has not been in this town for too terribly long and who does not have a chance to come over to this side of the Congress too often, that this is a nice place you have here.

More importantly, let me echo the sentiments of the good Senator from the great State of Alaska in welcoming you, gentlemen. You have done us a great service, and I think the record should note, at no cost to U.S. taxpayers, but borne by you and your resources. We are tremendously grateful to you for that as well.

I do have a prepared statement, Mr. Chairman, that with your permission I would like entered formally into the record without objection. I do think we have a lot of work ahead of us here this

morning, and I think it would be far more helpful, at least from my perspective, to hear from our valued witnesses this morning.

So I will, with that and my appreciation, yield back to you, sir.
[The prepared statement of Mr. McHugh follows:]

PREPARED STATEMENT OF CONGRESSMAN MCHUGH

Good morning. I too am pleased to help convene this joint hearing this morning with the Senate Subcommittee on Post Office and Civil Service, chaired by my good friend, Senator Ted Stevens. Senator Stevens has long been recognized as a leader on postal issues and I am confident the membership of both subcommittees will stand to benefit from the joint efforts put forth at today's hearing.

This past fall, the House Subcommittee on the Postal Service embarked on an aggressive series of hearings directed at reviewing possible reform initiatives for the U.S. Postal Service. Today's hearing represents the second in that series and I look forward to the testimony presented by our witnesses in order to learn of foreign postal reform efforts, their successes and failures, and the potential relevancy of such reforms to our unique American postal system.

The first panel of witnesses represents four postal administrations which have generally been heralded as the leaders in progressive reform and privatization efforts. All were represented last summer at the Futurepost summit conducted here in Washington and sponsored by the U.S. Postal Service. These postal administrators have been at the forefront of change in transforming their respective postal services. I join Senator Stevens and my colleagues today in welcoming them to our country and I look forward to their testimony detailing the nature of changes which they have overseen.

I am particularly interested in hearing from our guests the successes and failures which they have encountered on what has proven for some countries to be a long and difficult path. (During my Subcommittee's oversight hearings this past year, four issue areas emerged on which a general consensus appeared to favor reform, specifically—the scope of the postal monopoly, labor-management relations, postal ratemaking and product pricing, and the ability for the U.S. Postal Service to introduce new products. While a consensus for change has emerged, the form and shape of those generally accepted changes has yet to be determined. I hope our witnesses can comment today on their respective experiences in addressing their postal reform efforts in these general areas.)

Our second panel is comprised of witnesses representing Price Waterhouse and the General Accounting Office.

Last year, the Postal Service commissioned Price Waterhouse to conduct a study of a number of progressive postal administrations worldwide and report on the status of their reform initiatives. Their report summarized the current state of ten postal administrations at the forefront of a general move towards postal corporatization and deregulation. I look forward to Mr. Waddell's testimony and I hope he can provide updates on this report regarding changes in the status of these countries' efforts to deregulate and corporatize their postal administrations.

Once again, I want to welcome Mr. Mike Motley, accompanied by Mr. Jim Campbell, of the General Accounting Office for their appearance before the subcommittees for this joint hearing. The GAO has performed invaluable work for both of our subcommittees over the years and I look forward to Mr. Motley's testimony in relating GAO's previous and ongoing work regarding postal reform developments in other countries.

Comparing the postal system in the United States to those of other countries can be difficult. No other postal system in the world is utilized to the extent and in the same ways as our Postal Service. And no other postal administration comes close to rivaling the U.S. Postal Service in terms of size, revenue, volume or the many purposes for which Americans use the Service. This is why I am pleased the GAO agreed to accept the subcommittees' invitation to testify today regarding their analyses on the relevancy of such comparisons.

When the House Subcommittee on the Postal Service embarked on this series of postal reform hearings, our intent and purpose was to systematically review the Postal Reorganization Act to determine whether, and in what ways, Congress should consider reform. Yet, the cornerstone of any reform efforts remains the extent to which postal delivery and service can be improved for all postal customers. Clearly, there are lessons to be learned from these and other progressive postal administrations' efforts at reform, lessons which may prove workable here at home. Many postal deregulation and privatization proponents cite the examples of foreign posts as

blueprints for privatization of our postal system. And, today's hearing should highlight those reforms.

Yet, I urge my colleagues to remain mindful that a "one size fits all" approach of applying reform approaches may not prove workable for our complex system.

Again, I want to welcome our witnesses here today and I particularly acknowledge the time, effort, and expense put forth by the witnesses representing the foreign posts in order to be with us this morning. I also want to commend Senator Stevens for extending this invitation for today's House and Senate joint hearing and I look forward to working with him in developing legislation to address the first significant postal reforms since the current Postal Service was created a quarter century ago.

OPENING STATEMENT OF SENATOR STEVENS

Chairman STEVENS. Thank you very much, Mr. Chairman. We know how serious you are about reform of the long-term needs of the Postal Service.

I am delighted to be able to chair this hearing. The Postal Service in our country, gentlemen, is very important to Americans, but it is a lifeline in rural America. In a State such as the one I represent, or even in parts of New York and what we call "the South 48," our people, my Alaskan people, depend on the Postal Service for the necessities of life. The things that many people here go to the corner grocery store or pharmacy to pick up, we have to ship in by parcel post, and it is a continuing problem for us.

Our State is one-fifth the size of the United States and has fewer roads than Cook County in Illinois. It is a very challenging concept to maintain a communication system in that part of our country. So I am personally grateful to you, and grateful to you as chairman of this Subcommittee.

I had the privilege of meeting some of you before, when the Postmaster General had his meeting last year, and that's what gave us the idea of asking you to come here and give us for our record, as we proceed now toward some sort of modernization of the postal system, the experiences that each of you have encountered in your own countries.

So let me just introduce you, and then we'll proceed with my colleagues to see if they have any comments.

Graeme T. John of Australia Postal Corporation; Georges Clermont, of Canada Post Corporation; Elmar Toime of New Zealand Post Limited; Ulf Dahlsten of Sweden Post, who is accompanied by Tommy Persson, the senior vice president of Sweden Post. We do look forward to your comments about what has worked for you in your countries, and I know some of you have opinions as to whether similar reforms can or should be accomplished in our country. We do learn from others' mistakes, we believe, so do not hesitate to tell us if you tried something and it did not work. I think we should not run the same gamut that you have and fail if you had that experience.

A representative of the British Post Office was unable to be here this morning, and I am going to ask that his statement be printed in our record. Copies of that statement will be available to any interested parties.

[The prepared statement of the British Post Office follows:]

PREPARED STATEMENT OF THE BRITISH POST OFFICE

BACKGROUND

The British Post Office remains as part of the public sector. It has been widely acknowledged for a number of years a first class UK company and a benchmark for Post Offices throughout the world. The Post Office includes four main businesses:

- Royal Mail: which handles 69 million items of mail per day and has 170,000 employees
- Parcelforce: which is the country's biggest parcel carrier and has 11,000 employees
- Post Office Counters Ltd: which has a network of Crown Office counters (i.e. main post offices) and franchise post offices totalling 20,000 (bigger than the combined network of banks and building societies)
- SSL: which collects TV licence fees on behalf of the state

The Post Office operates a monopoly system for the delivery of letters. With the exception of a few private operations (such as document exchanges) there is a monopoly for the handling of mail set at £1 (current prices for handling mail are 25p securing 92.5 percent arriving the next day) The Post Office is, however, under threat from other communications which are not subject to a monopoly, particularly telephone/fax, overseas Post Offices and electronic communication methods. Additionally, direct marketing, a huge slice of Royal Mail, competes vigorously with other types of advertisers. Our Counters business also competes vigorously with retailing and banking networks and Parcelforce operates in a completely deregulated market.

Commercial Constraints:

Because of the competitive nature of our business, The Post Office needs to be free to act like any commercial organisation in developing its products, setting its prices and running its business. Under current legislation, this freedom does not exist. The Post Office is not allowed to borrow money for investment in its future, nor is it allowed to decide how much of its profits should be retained for investment, but is forced to invest them in Government securities. The Post Office is not allowed to broaden its range of services into adjacent markets, particularly if these would conflict with services that are already on offer in the private sector. Nor is The Post Office allowed to operate its own pay and incentivisation policy, but has to comply with the government's public sector pay policy which has been operating for 3 years.

Government Review:

In 1992 the Government announced that it intended to sell Parcelforce and move it into the private sector. This was quickly followed by an announcement of a Review of The Post Office which was intended to be completed rapidly. In 1994 the Government issued a Green Paper outlining proposals for the future of The Post Office and recommending, that Counters should remain in the public sector and options for ownership and regulatory control of Royal Mail and Parcelforce.

The Government's preferred option was to sell 51 percent of the shares in Royal Mail and Parcelforce to ensure a continuing partnership between the public, the tax payer, employees and subpostmasters. In the event the privatisation proposals were dropped as the Government was unable to secure an overall majority in the House of Commons.

Commercial Freedom:

Following this decision, The Post Office sought various assurances from the Government about the future of its businesses:

1. That it should be free to reward and incentivise its employees in line with basic commercial practice and its own commercial needs.
2. The Post Office should be able to enter into joint ventures with suppliers or competitors.
3. The Post Office should pay a reasonable commercial dividend set at a fixed percentage of our post tax profits (the normal commercial rate is about 40 percent).
4. The Post Office should be free to raise capital.
5. The Post Office should be able to have greater freedom in deploying new services and products.

In May 1995 the President of the Board of Trade, Michael Heseltine, gave reasonably positive responses on all of those issues with the exception of pay and incentivisation. The assurances have not yet been translated into practice and

whilst we have been successful in getting approval for some new products and services in Post Office Counters, by and large, progress has been slow. Similarly, whilst we were anticipating having a dividend of 40-50 percent of post tax profits, the Chancellor of the Exchequer (in his November Budget) announced that The Post Office would be required to pay an extra 1 billion pounds over the next 3 years. At current profit rates this means that all profits will have to be invested in Government securities. This in itself has now made a price rise almost inevitable.

Conclusions:

The Post Office is not concerned with issues of ownership: it recognises that is a matter for the Government. The Post Office does however feel that it is competing in a commercial environment and needs further freedom to make commercial decisions.

Chairman STEVENS. We will hear from another panel after this one, which will include representatives of the General Accounting Office and Price Waterhouse. Each of those entities has conducted studies on a number of international postal organizations, including some of those represented by our first panel.

Let me first ask if Members of the Committee have a statement. First, let me turn to Mrs. Collins, if I may, as our guest, and then to my friend, the vice chairman.

OPENING STATEMENT OF CONGRESSWOMAN COLLINS

Mrs. COLLINS. Thank you very much, Mr. Chairman.

Chairmen John McHugh and Ted Stevens, Senate Subcommittee Ranking Minority Member David Pryor, I am pleased to join you in convening the first joint hearing before the Postal Subcommittees of the House and Senate.

This is the House Subcommittee on the Postal Services' second hearing on postal reform. As such, our Subcommittee, under the very able direction of Chairman John McHugh, continues to explore and examine alternatives relative to postal reform of the U.S. Postal Service.

I am pleased we could make this particular hearing on foreign postal reform the object of a joint hearing.

As the Ranking Minority Member of the House Postal Subcommittee, I would like to personally welcome and thank our distinguished foreign presenters for taking the time to testify before us. You have travelled a great distance and at great expense to present your views and discuss with us the postal reforms your respective countries have taken to become better providers of postal service.

I am particularly interested in your thoughts and suggestions on how the U.S. Postal Service and Congress might benefit from the steps you have taken which have improved your postal departments. I am especially curious to learn more about how you were able to effect positive and improved changes in labor relations and criteria you utilized for deciding to contract out non-core elements of postal service and delivery.

I look forward to your testimony, and I thank you for the opportunity to dialogue with you on the issue of foreign postal service reform. Thank you very much.

Chairman STEVENS. Thank you very much.
Senator Pryor?

OPENING STATEMENT OF SENATOR PRYOR

Senator PRYOR. Mr. Chairman, I have a statement, and I would ask consent that my full statement be placed in the record.

This is a unique occasion when we the House and the Senate can come together to hear such distinguished guests, who will tell us what they have been able to accomplish with their own postal systems.

I did a rare thing right before we left for our Christmas break, colleagues. I put a statement in the record praising our Postal Service. That is a rare thing to do in this day and time because there is a great deal of criticism of it. People love to make jokes about the Postal Service and politicians; I guess those are the two subjects of most jokes these days, and maybe somewhat deservingly.

I think the Postal Service has done a great job over these years, but I think that we can do a lot more. As my colleague on my right has just stated, one of her main concerns, as is mine, and has been for some time, is the relationship between labor and management. Somehow or another, in our system, that relationship has become extremely fragile, very brittle, very adversarial and, I would say, very distrustful. It is not a healthy relationship, and we need to improve upon that, and we would very much like to hear the testimony of our friends who have come from so many miles away this morning to tell us how they have surmounted some of these challenges.

With that, Mr. Chairman, I thank you for the opportunity of appearing and once again thank our guests.

Chairman STEVENS. You are the former chairman of this Subcommittee, Senator Pryor, and I am delighted to hear that comment of yours about putting a statement in the record. I missed that. I am constrained to say that you have gained great courage since you decided to retire.

Senator PRYOR. I have become a statesman. [Laughter.]

[The prepared statement of Senator Pryor follows:]

PREPARED STATEMENT OF SENATOR DAVID PRYOR

Thank you Chairman Stevens, and welcome Chairman McHugh. It is a pleasure to be here this morning to greet our special guests, representing the postal systems of Australia, Canada, New Zealand, and Sweden. I want to thank these gentlemen for taking the time to be here and share their respective country's experiences with postal reform.

I think it is very helpful for us at this time to be discussing some of the experiences that other nations have had with postal reform. The ongoing debate in the United States has largely focused on theoretical ideas ranging from privatization to commercialization to deregulation. Today's hearing will give us the opportunity to talk about real reform plans, and at the very least, some preliminary results.

Although the topic of postal reform encompasses a number of critical issues, I am particularly interested in the impact that any changes will have on two areas—the important role that our Postal Service plays in our nation's economy and communities, and the Postal Service's already strained labor-management relations.

Scarcely a week goes by that I am not contacted by the residents of a small Arkansas town concerning their post office. Sometimes, I am asked to help prevent a post office from closing. At other times, these towns want my assistance in obtaining a new facility. I also receive letters from people praising their local postal workers. Whatever the issue, these letters are a constant reminder to me of the important role post offices play in small communities throughout the United States.

I believe the most crucial societal function of the U.S. Postal Service is its mandate to provide universal service at a uniform price. Whether they live in rural or

urban areas, Americans have depended on a reliable and inexpensive mail delivery system for over two hundred years.

The fact that we have enjoyed a reliable and inexpensive mail service has been a boon to our economy as well. Without it, business in America would be much different. Direct mail is now a multi-billion dollar industry in this country.

I believe these responsibilities of the Postal Service are still relevant and sustainable. While I am not opposed to giving the Postal Service greater flexibility, I will carefully consider the costs to our communities and economy of any reforms that are proposed. I know our guests here today have a lot of information on rural post offices and universal delivery in their countries, and I look forward to hearing their comments.

The postal administrations represented at this hearing differ significantly with that of the U.S. Postal Service in terms of the size of population served and the amount of mail volume processed. However, like the U.S. Postal Service, their workforces are highly unionized.

It has been my feeling for some time that the U.S. Postal Service will never perform at its best unless it improves its labor-management relations. The current relationship is far too adversarial and distrustful. If any reforms are to be successful, then both labor and management will have to take risks and form a new partnership. I would have to add, that even without major reform, union and management must find a way to a better working relationship.

I hope our guests today will discuss the steps that their organizations took to involve the labor groups in the reform process. It is imperative that we learn from these success stories. I also hope that the leaders of both the Postal Service and the labor groups will be listening closely.

Finally, I also look forward to hearing from the General Accounting Office and Price-Waterhouse this morning. While the members of the second panel have not traveled quite as far to testify, I am sure that their expertise will be a valuable addition to our discussion this morning.

Again, I want to welcome our friends from Australia, Canada, New Zealand, and Sweden. I believe this hearing comes at an important time, and I look forward to this morning's discussion. Thank you, Mr. Chairman.

Chairman STEVENS. Gentlemen, we are honored that you have taken the time to come today, and I appreciate it personally because it was my suggestion to the Postmaster General that he negotiate with you to see if you would come and make a record before the Congress of some of the comments you made in the meetings held last year.

So let me proceed now to receive any opening comments you want to make. It would be my suggestion, unless someone disagrees, that we proceed in the order that I have introduced you, and ask you to make statements, and we will withhold any questions from up here at the Committee table until each of you has finished.

So, Mr. John, would you proceed, please?

TESTIMONY OF GRAEME T. JOHN,¹ MANAGING DIRECTOR, AUSTRALIA POST

Mr. JOHN. Thank you, Mr. Chairman.

I am pleased to respond to your invitation to address this Joint Committee on our experience in significantly improving our postal service. I have provided you with a written submission examining Australia Post's evolution from a bureaucratic department of government to a commercially oriented and customer-focused business enterprise.

This morning, I will outline briefly how we have transformed our culture, lifted our financial performance from break-even to match some of Australia's most successful businesses, built postal revenue

¹ The prepared statement of Mr. John with an attachment appears on page 45.

by "freezing" letter prices, and improving delivery reliability; and are now growing the business further by introducing new services.

We have completed a half decade or so of unprecedented progress. On every financial and operational measure, Australia Post's performance today is the best it has ever been. Profitability has more than quadrupled, from 3.5 percent return on average assets in 1989 to 15.6 percent last year—or a profit of \$331 million on a turnover of \$2.7 billion.

The standard letter rate has not changed since January 1992 and will remain fixed until at least 1997, when we expect it will have brought a real price fall of around 14 percent, or 6 cents over that time.

Our productivity has improved over twice the national rate, up by more than 25 percent at Australia Post since 1990, compared with a national gain of 12 percent. In 1989, lost time strikes averaged 1.5 hours per employee, and in 1995, it was 6 minutes per employee, down almost 95 percent. We are now among one of the best Australian businesses, with only three comparable companies recording stronger profit growth than ours since 1990. Internationally, we are among the Western world's best-performing postal enterprises.

Our customers have also noticed the difference. Our annual independent surveys show we are now more favorably viewed by most private and business customers than Australia's major communications, banking, airline, retailing and transport businesses. Their regard for our staff has lifted 40 percent over the past 4 years. In 1991, only 6 in 10 of our customers felt our staff cared about them and their businesses; today, it is 9 out of 10.

We come from a checkered past, though. Just a short time ago, Australians were far less complimentary about their postal service. In the mid-1980's, labor relations were at breaking point. Delivery performance was very mediocre. Our customers, particularly the business sector, had no confidence in our service, and the Federal Government was concerned with management's inability to fix problems permanently.

Coincidentally, at the same time, the Government was tackling national economic problems emerging in the latter half of the 1980's. It saw microeconomic reform as a part of the broader solution, including corporatization of its business enterprises, one of which was Australia Post.

This determination by the Government to make these enterprises more efficient, to provide improved service to the community, was an important incentive in encouraging Post's management and unions to accommodate their differences and led to recognition of a shared interest—the continued viability and growth of the business.

A Joint Statement of Understanding between Australia Post and the unions acknowledged that viability of the postal service was critically dependent upon our reputation. It established effective dispute-settling procedures and committed the enterprise to participative management.

This acceptance of mutual interdependence and its implications for security of the enterprise and for the jobs of individuals provided the climate for a new, customer-focused service culture. We

have redesigned jobs, giving all our people a say in decisions directly affecting their work, recognized and rewarded performance, and provided our people with the resources, the personal skills and equipment, needed to achieve high standards. Increasingly, we are using all their skills and talents.

We have flattened management structures, removed job tenure for managers and reeducated them to focus on bottom-line outcomes, rather than building bureaucratic empires. Autocratic management is a practice of the past.

Now most of our people feel part of a team, proud of their achievements, proud of the commercial status and performance of Australia Post, and especially proud to work for one of the most successful Australian businesses.

The reasons for our metamorphosis can be found in four key areas.

First, the arm's-length relationship between the corporation and the Federal public service. In the past, day-to-day controls such as contract approvals, land acquisition or disposal, labor rates, and managerial salaries were entirely in the hands of Federal Government departments. Now they are the responsibility of board members and senior management with appropriate experience.

Discipline is brought to this freedom through the corporate plan, quarterly reports to the minister, and our annual report to the Australian Parliament which sets out performance against plan targets.

Controls have been shifted from a past preoccupation with inputs and processes, when Federal Government bureaucrats made key decisions, to a focus on outputs and accountability for performance.

Second, there is the healthy relationship between the corporation's management, our people, and their unions. This is the most significant change brought to the day-to-day functioning of the enterprise. It differs from other cultural change successes because it involves three parties—management, staff and unions. Unlike in some other places, our unions, conscious of the government's micro-economic reform program, have been willing partners in our reform process. Now the maintenance of this relationship is fundamental to the continued achievement of high performance levels that Australians have come to expect from their postal service.

Third, postal regulation is relatively light-handed. In Australia, the public interest in postal matters is protected by a combination of price-capping, increasing reliance on the market, and competitive pressures, and the maintenance of a high-quality, universally-accessible letter service.

Finally, there is our commercial freedom. To operate and grow successfully, the legislators accepted our need for freedom to introduce commercial services compatible with our business, but without reducing the scope and effectiveness of our community service obligation to provide all Australians with a uniform-priced letter service no matter where they live. This freedom meant that we could stem the financial hemorrhage through our network of postal outlets.

Many have been relocated, reconfigured, and reequipped with purpose-built electronic counter technology. A range of postal-relat-

ed products and electronically-accessed financial services, including banking, are now available through them.

With this introduction, our new express post service was immediately competing successfully with overnight courier services, and it continues to grow strongly because we are allowed to introduce new services.

In concluding, Mr. Chairman, the Government leveled the playing field, requiring us to pay all the same Federal, State and local government taxes and charges that apply to any commercial business. All new services must stand alone commercially without subsidy from reserved letter service revenue. And all services are now subject to the competition reform legislation which applies to all business.

While Australia Post is making progress, I recognize that the successful ingredients of reform in one country do not necessarily translate to success in another. Your markets are profoundly larger than ours, and our cultures of politics and regulation have few similarities.

The approach that is working for us stems from the Australian Government's decision in 1989 to give Australia Post its full trust. It set the enterprise the task of delivering a high-quality mail service while operating commercially. It undertook not to interfere in the process. Instead, it put the principal determinants of success or failure in the hands of Australia Post, its management and its people, with the board held squarely responsible for satisfactory performance.

In Australia, an efficient mail service continues to be essential for social and business communications for all Australians, not least for those in rural and remote areas. Importantly, the Government has brought a phased approach to reform, recognizing that any rapid move to postal deregulation might put at risk the delicate balance between successful commercial and noncommercial objectives, or jeopardize the gains we have made through the participative approach. It recognizes that a viable national postal network must be preserved in the interests of social cohesion and national development, and this has implications for the rate of change and degree of reform that can be applied. This "steady change" formula has been a major contribution to our success.

As we face new challenges and rising customer expectations driven by our success, complacency is not an option.

Mr. Chairman, with this framework of trust, freedom, accountability and measured reform, Australia Post is in a stronger position to face these challenges than at any previous time.

I thank you for the opportunity to address the Committee.

Chairman STEVENS. Thank you, Mr. John. We will come back to you.

Mr. Clermont, from Canada.

**TESTIMONY OF GEORGES C. CLERMONT,¹ PRESIDENT AND
DIRECTOR GENERAL, CANADA POST CORPORATION**

Mr. CLERMONT. Thank you, Mr. Chairman. Good morning, ladies and gentlemen.

¹The prepared statement of Mr. Clermont appears on page 83.

It gives me great pleasure, and a great honor it is indeed, to appear before you today to talk about some of the complex issues that we face.

Many would have you believe that national postal services are dinosaurs, relics of a bygone age, totally irrelevant in the world of faxes, e-mail, etc., they say.

Mr. Runyon could perhaps test the relevancy of the U.S. Postal Service by announcing tomorrow that he has decided to deliver mail 3 days a week and close all post offices that serve less than 25,000 customers. I believe that your phones and your in-baskets would measure the relevancy of the postal system today.

I would like to go through a brief history of Canada Post Corporation. Back in 1981, the post office became what we refer to as a Crown Corporation. A Crown Corporation is a creature of statute, subject for the most part to the provisions of the Canada Business Corporations Act, and to all other laws of the land including the antitrust legislation. There are Crown Corporations that have a purely social mandate, and some that have a mixed social and commercial mandate. The latter must be run as a business although it is entirely owned by the Government of Canada.

There were a number of reasons for the Government to move the Post Office Department in that direction, chief amongst them the bureaucratic and political interference in the day-to-day management, the elimination of deficits that ran into the hundreds of millions of dollars, and to eliminate labor strife, which had become so commonplace that Canadians had lost confidence in the postal system.

I believe that these parallel the conditions that a number of postal administrations have found themselves in over the years.

As a first step as a corporation, we concentrated on operational improvements because we had to give the Canadians a reason to believe in the system. It was important, first and foremost, to show them that their postal system could do the job and give them good service.

Having set standards of service, we had our performance measured by an independent auditing firm—we were the first to do so in the world—and this allowed us to measure our progress, quarter by quarter, year by year. This became one of the key determinants for incentive awards to all our salaried employees.

We know that we are doing better now than 10 years ago, for example, as on-time delivery has gone from 85 percent to 97–98 percent.

Having had a good shot at fixing the operation, constraining costs and establishing a sound network of retail outlets, distributed between corporate outlets and franchised outlets, we turned our effort to our customers.

When you have been a monopoly for well over 100 years, it is very difficult to instill a customer-driven culture in an organization. to change the culture is our current challenge—a more difficult task, perhaps, than those we undertook during the first phase. We are now dealing with attitudes and the human mind. When properly trained and motivated, there is no doubt that postal employees are as productive, if not more productive, than any.

While our work force has a right to strike, acquired in the mid-1960's, it knows and we know that after a week or 10 days of strike, the Government will force them back to work and impose arbitration. We do not have an equilibrium of forces in the area of industrial relations.

They also know that they have contractually obtained job security, and that the post office is not about to disappear. A normal business corporation has a choice of shutting down an operation, moving it somewhere else. We do not have that choice, and it is evident in our work force behavior.

Today I can say that we have restored customer confidence in the postal system. We have started measuring customer satisfaction index through an outside firm, of course, and improvement on this index, quarter by quarter, year by year, will become part of our goals, just like we did for service performance and part of our incentive awards.

When dealing with such a large work force, the goals must be simple, clear and measurable. We will set targets for customer satisfaction improvement in increments of 2 or 3 percentage points every year, and nobody can pretend not to participate.

Participation by all is a prerequisite for a successful turnaround. There is no substitute for a work force that is proud of the corporation that it works for.

Our success has allowed us to regain market share in most of our product lines. This progress, of course, has caused considerable unrest amongst our competitors. As can be expected, cries of cross-subsidization soon reverberated. These allegations have been repeated over the last 5 years and have been dismissed every time, the last time by the Bureau of Competition, our watchdog for anti-trust legislation, when it approved our acquisition of a 75 percent interest in Purolator Courier, Limited, the largest courier service in Canada.

Our competitors would like to see us subjected to some form of regulatory regime as is the case in this country. Our Government has so far resisted that, and I believe for good reason.

The basic letter rate is the only one that is not subject to market forces. Even that, as we all know, is facing severe competition. The letter rate is set by Cabinet. Our corporation is otherwise subject to all laws of the land including, as I have said, the Competition Act, which is the perfect remedy for keeping us honest. There is no need, I believe, to force us into a straightjacket, which in the end only benefits the competitors.

Our Government has just appointed a commissioner to review our mandate. The last time it did so was 10 years ago. Its terms of reference are broad. Chief amongst them is the maintenance of some form of exclusive privilege—our monopoly—which gives us the exclusive privilege, subject to 2 pages of exceptions, to deliver letters weighing less than 500 grams. It will also look into our role in the future electronic information transfer media.

Part of the review will focus on definitions of social function. As I stated in the beginning, our corporation has the mix of a social and commercial mandate. Its social mandate is essentially the universality of the service and the single price for a basic letter.

We like to look at those social obligations, however, as a marketing asset. It allows us to put everything we do in a very single focus; we "stick to our knitting." For instance, we got rid of censoring mail; that is none of our business. Law enforcement agencies are there for this purpose. Free mailing for elected representatives is a Government policy, not ours, so we get paid for it.

Most of our non-core operations are contracted out. We do no long-distance transportation, surface or air. We found out that our information technology staff tended to reinvent what was already in the market. We have outsourced all of this function, which frees up capital for processing equipment. The same with our property management function. We are not good at managing real estate, and we have contracted out to the private sector, which results in great savings.

By concentrating on our core business, by focusing on our business like any other corporation, we believe that we can play the game on a level playing field with our private sector competitors.

Playing on a level field means meeting the needs of customers, citizens, business and others; evolving with technology; paying taxes and dividends to your shareholder, whoever he may be; and achieving the commercial freedom that is required to measure up to our goals.

Given these rules, Mr. Chairman, I would suggest that we let the market decide who would be in the game.

Thank you very much.

Chairman STEVENS. Very interesting, Mr. Clermont. Thank you. Mr. Toime, from New Zealand, please.

**TESTIMONY OF ELMAR TOIME,¹ CHIEF EXECUTIVE OFFICER,
NEW ZEALAND POST LIMITED**

Mr. TOIME. Thank you, Mr. Chairman, for the invitation to appear as a witness and the recognition of New Zealand and New Zealand Post implied by the invitation. I am honored to represent the company here this morning.

I have submitted written testimony dealing with the legislative changes in New Zealand which have allowed the business to perform. I will not repeat that testimony now.

I have also provided information on the company's achievements. Measures of which we are particularly proud include the fact that we were nominated New Zealand's company of the year in November 1994; in October of last year, we dropped the price of postage for First Class letter mail by 5 cents; in the 8 years since we were corporatized, the price of that class of mail has fallen by almost 30 percent in real terms; we have been profitable for the 8 years since being corporatized—we were loss-making before then—and in our last financial year, we posted a record profit with key ratios of 32 percent return on shareholder funds, profit before interest and tax to turnover of 17 percent, profit before interest and tax to assets of over 25 percent.

It is my conviction that similar results can be obtained for all postal businesses.

¹ The prepared statement of Mr. Toime appears on page 88.

To be brief and to the point, I believe that there is frequently confusion between what I would call the social obligations required of the Post and commercial behavior. I believe the Post is amenable to market forces. It is a business, and it needs commercial disciplines.

I believe the role of legislators is to decide the social mandate required of the post and then establish an operating environment which as closely as possible allows markets to operate.

In other words, government is responsible for the operating environment and the social policy contract. Once that is defined, the post should be allowed to run like any other business. It will then have responsibilities to its owners—in this case, government on behalf of the people of the United States; it will have responsibilities to social infrastructure—that would be the universal service mandate required by Congress; it will have responsibilities to its customers in efficient service, and it will have responsibilities to employees as a fair employer.

Reform must discover the optimum formula to best achieve these multiple objectives. The state-owned enterprise model pioneered in New Zealand has achieved this.

In dealing with a complex business with a long and valued heritage, both in the minds of the public and in the people who work for the business, reform may be daunting. The desired end objective of all stakeholders cannot be achieved except over time. The natural conservatism of the public, customers, and employees—and no doubt even many managers in the business—will mitigate against rapid change.

Changing the behaviors of people does take time. In thinking about the USPS and reflecting on my own experiences in the turnaround of New Zealand Post, I have suggested a program of change which I believe allows commercial goals to be set while still keeping an equilibrium of sorts among the diverse stakeholders and self-interested parties.

The headings that I would propose under such a reform would include separation of the regulatory and ownership powers in government; second, I would establish a commercial company structure. All operational and commercial decisions within the social obligations framework should be the responsibility of the board of governors. Performance targets need to be reported to Congress, and commercial balance sheets and financial statements need to be established.

And my third point would be to establish the necessary monopoly and regulatory controls which enable maintenance of the universal service obligations.

That represents on my part a very brief summary of how I see reform proceeding.

Thank you.

Chairman STEVENS. Thank you very much, Mr. Toime.

Now we will hear from Mr. Ulf Dahlsten, who is accompanied by Mr. Tommy Persson, of Sweden Post.

TESTIMONY OF ULF DAHLSTEN,¹ PRESIDENT AND CHIEF EXECUTIVE OFFICER, POSTEN AB, LIMITED, SWEDEN; ACCOMPANIED BY TOMMY PERSSON,² SENIOR VICE PRESIDENT, POSTEN AB, LIMITED, SWEDEN

Mr. DAHLSTEN. Thank you, Mr. Chairman and Mr. Co-Chairman. As the others, I am honored to be invited to present to you our experiences.

As perhaps you all know, Sweden has in some ways gone further than the others and actually abolished the letter monopoly. When it happened in 1993, we were one of the first three nations in the world to deregulate the letter market totally.

Just under 10 operators, most of them very small, tried to establish business in letter distribution. Of the active ones, only Svensk Directreklam is now left. This company, originally a distributor of unaddressed mail, is now also involved in the distribution of addressed items.

On the other hand, Sweden's best-known private sector operator, City Mail, has for the second time filed for bankruptcy. According to an independent committee, the company has no prospects for survival within the scope of its current business concept. City Mail may perhaps have been able to compete with the old Sweden Post, but not with the much more efficient Sweden Post of today.

City Mail's business scheme, with sorting conducted manually, cannot become competitive even if volume increases sharply. Even if City Mail is now once more reconstructed, the forecast for the future is thus weak. What many in the postal world now ask themselves is: Does this mean that the deregulation in Sweden has failed? My personal answer to that is no.

There was no doubt that many people who supported deregulation had the main intention to give the private entrepreneurs a chance. However, my own reasons for urging the need for deregulation of the letter market and the conversion of Sweden Post into a limited liability company were different, and so were others.

Our analysis was and still is that the position of letters as a means of communication is seriously under threat by the developments of technology. You have to remember that nearly 90 percent of letter revenue comes from companies, other organizations and the public sector. They use the letters mainly for two purposes. The first is for administrative and financial messages. In this market, electronic systems are gaining market shares day by day—fax, e-post e-mail, EDI, and so on already account for more than half the volume of messages across borders as well as for 20 percent of business communications in a country like Sweden.

The second use of letters is in market communications. Some of you call it junk mail. Here, the letter competes with other media, including the growing area of radio and TV advertising, as well as with press advertising and billboards, etc. Letters have around one-third of the media market in Sweden, and of that share, Sweden Post has in turn two-thirds. Other operators share the remainder.

In this expanding market the letter has maintained its position well.

¹ The prepared statement of Mr. Dahlsten appears on page 135.

² The prepared statement of Mr. Persson appears on page 139.

There were also other reasons for deregulation and privatization. Sweden Post has much more to offer than delivery of letters alone, even if letters represent more than 40 percent of our revenue. Basically, we are in the market for messages, payments and distribution of goods. And the pressure of competition is also growing in other areas than letters.

The Postal Giro Bank that is handling payments is not only responding to a trend in which payments will increasingly be made by electronic means. Furthermore, as a result of the Swedish European Union membership, all banks in Europe are now European banks. This means that international banks specializing in payment processing now have free access to the Swedish market.

The parcel business, too, no longer has domestic competitors alone to deal with. International integrators are increasingly turning their attention to the Swedish market.

The first step toward a deregulated postal market was to take away the monopoly on letters that we had. Although we are free to decide on prices for our services, there is a price cap on letters up to 500 grams. The cap is what is presented in your papers. The real price that customers pay is less and has been in real terms reduced by 10 percent the last 2 years.

We got a Postal Services Act in 1994, and at the same time, Sweden Post became a limited liability company. The monopoly that the Postal Giro had on some State payments was terminated in this context. Today Sweden Post operates on the Swedish market without any monopoly protection at all.

The Government has the responsibility for giving all citizens daily postal service, 5 days a week, wherever they live in Sweden. Sweden Post has taken on these responsibilities in an agreement with Government. This agreement will soon be renegotiated. It is important to underline that we can provide this postal service without any compensation from the Government. In the case of the counter services, mainly cash transactions, there is a certain compensation for rural areas that does not cover costs.

The choice of direction—deregulation and conversion of Sweden Post into a limited liability company, made a couple of years ago, has opened up opportunities for Sweden Post to rise to this challenge, and we have taken our chances. We have adopted four external strategies, the first being efficiency improvements. Three billion Swedish crowns have been saved in 5 years out of a turnover of around 20 billion Swedish crowns. Approximately 75 percent of the work on improving efficiency has now been completed. We once employed almost 75,000 people; now we are under 50,000. One-third of our post office are outsourced. Out of the 500 biggest companies in Europe, Sweden Post last year was ranked as the third most profitable company all over Europe. Our time on delivery on overnight service is now 97 percent, and of course, higher on slower items.

The second strategy was to adapt IT as a friend. Through development of Post Net, among other projects, Sweden Post today is a market leader in Sweden within the field of electronic messages and payments.

The third strategy has been to add value to the customer by combining our range of services in administrative processes and

logistical systems, and by developing the postal outlets into what we call "the best friend of the ordinary businessman." We can enhance the value of the services we offer to the customer.

The fourth strategy is internationalization. By meeting our international competitors aggressively and by applying our knowledge abroad to best effect, we can enhance our earning capacity.

These external strategies have been backed up by intensive work on internal change spanning everything from management systems, new labor agreements, the breakdown of Sweden Post into 1,500 small profit centers where every employee participates in our corporate planning system, to a buildup of enterprise culture around shared visions and values and the development of leadership and proficiency.

We believe that today we represent a National asset. I am aware that this is not, sadly, said about all postal operators in the world. This hearing indicates that the intention of this Congress is to guarantee that this will be said about the USPS in the days to come.

This is contrary to most European countries, where governments seem to have reached the conclusion that their postal operators are incapable of surviving through their own efforts. Indeed, the prevailing view is that they need the protection of a monopoly position.

It is considered that the extra cost has to be borne by the customers. There are examples of countries which, in order to retain the monopoly for the foreseeable future, are prepared to pay a letter rate, excluding VAT, double that accepted in Sweden.

However, there are no certain victories in the future, not even for us in Sweden Post. Hard work and a forward-looking approach will be needed, and developments will have to go our way if we are to succeed.

We believe that if we continue to receive the right support and are able to work under the same conditions as private sector business, we will continue to be able to provide the whole of Sweden with a world class postal service and continue to represent a National asset to our country.

If I may conclude with some remarks on what experiences can be drawn from Sweden and perhaps to the United States, those would be as follows—and I make these comments bearing in mind that each country has its own history and its own tradition that must be respected, and that is certainly the case in your great Nation.

Bearing that in mind, I would say that a first step, given our experiences, would probably be to prepare the USPS for competition. That would be done by changing USPS into a limited liability company still owned by the State in the first step.

The second step, to be decided now, but to take place in, say, 5 years' time, would be to deregulate the market and at the same time introduce a Postal Services Act. This Act could be implemented by a new services commission, perhaps developed on the basis of the present Postal Rate Commission.

As a third step, the USPS could be fully privatized by a sale of shares. In Sweden, that would be a controversial step; with the American tradition, it is probably a necessary one.

The basic question faced here is whether the Postal Service is a part of the market economy where consumers demands are governing or whether it should be looked upon as a part of a country's infrastructure, like highways, to be financed collectively.

To me, the answer is simple. To 95 percent, the posts are a part of the market economy and should be run accordingly.

Thank you.

Chairman STEVENS. Thank you very much, Mr. Dahlsten.

Those were all very interesting comments.

Let me first recognize that Congressman Mark Sanford has joined us. Did you have an opening statement, Mr. Sanford?

Mr. SANFORD. No, I do not, Mr. Chairman.

Chairman STEVENS. Thank you. All of the statements that were referred to in the beginning will be printed in full in the record, and with the concurrence of our guests, we will print all of the material that you have given us in the record.

Pardon me. I do apologize, Mr. Persson. Did you have a comment to make in addition to that of Mr. Dahlsten?

Mr. PERSSON. No, Mr. Chairman.

Chairman STEVENS. Let me turn to Chairman McHugh first.

Mr. MCHUGH. Thank you very much, Senator.

Gentlemen, we appreciate your comments here today. Beyond what you noted for the record in your spoken words today, I think everyone should know that you have collectively provided us with a wealth of information that we are going to take back and try to analyze and utilize as best we can. So we appreciate that rather unseen effort as well.

Let me start with the comments near the conclusion of Mr. Dahlsten's remark. You gentlemen—Mr. Toime, Mr. Clermont and Mr. John—heard his comments about a letter mail monopoly and his feelings about how it is somewhat unnecessary. All of you, as I understand it, if not enjoy, employ, that mail monopoly.

Mr. Toime, in your recommendations to us as to how we might restructure the U.S. Postal Service, you recommend retention of that mail monopoly. I was curious as to how you might respond to Mr. Dahlsten's comments or, more to the point, how you perceive the letter mail monopoly in your jurisdictions.

Mr. John?

Mr. JOHN. Our mail service is going through a transition. We enjoyed a monopoly of 10 times the basic letter rate—our basic letter rate was 45 cents—and also a 500 gram weight break, so anything that was below 500 grams, a competitor had to charge \$4.50. The last round of regulation came about from an industry commission report on Australia Post, and they recommended a reduction of the monopoly structure down to four times and to 250 grams, so there was a very, very considerable reduction in that monopoly.

This was designed to allow us to become more efficient and to open up the market, and \$250 million worth of revenue was opened up to competition within our organization because of that. We believe that maintaining the monopoly and not budget-funding community service obligations is the way to go. While progressively decreasing the monopoly, allowing access to markets has at least decreased by competitors and taken us into a competitive environment—keeping in mind all the time our community service obliga-

tions for a country that is as vast as Australia, particularly in our rural and semi-rural areas.

Mr. MCHUGH. Before we turn to the other gentlemen, let me rephrase the question. Do the three of you feel that the letter mail monopoly is necessary to protect affordable services principally to rural areas, but indeed anywhere in the country?

You heard Senator Stevens' opening comments about the sparse population of his district and his State, and certainly of my district as well. That is a deep concern for many of us, and the letter mail monopoly is traditionally presented as a way by which we can preserve that uniform price, universal service. Do you agree with that approach, or do you think there is a different way?

Mr. JOHN. We certainly agree with universal service for a universal price.

Mr. MCHUGH. Mr. Clermont?

Mr. CLERMONT. Yes, also. Senator Stevens mentioned that his State was one-fifth of the United States. At least 70 percent of our country is like your State, hardly populated. So we need to serve all Canadians, wherever they are, and the only way to do it is through this system. Our monopoly was set at three times the basic letter rate back in 1982 and has not moved.

There are infringers. A number of cities lately have started delivering their utility bills through their surplus employees as they have downsized. We do nothing about it; we do not enforce it because in the end, I think we can satisfy these customers that we will do it better and cheaper. So in the meantime, we do need that monopoly.

Mr. MCHUGH. Mr. Toime?

Mr. TOIME. In New Zealand, it is Government policy to remove the monopoly, and New Zealand Post and I personally support the removal of the monopoly and the deregulation of the post in New Zealand.

However, I think the circumstances and conditions are very different. Setting aside the question of geography, it's a question of 8 years of continuous reform of a postal business where we are match-fit, we are ready for competition, and we know that we can perform very creditably in a deregulated market.

In the case of the United States, I do not think the evidence is available to be able to tell that story, to be able to make a decision about deregulation. Given the magnitude of the changes which are necessary here, I for that reason would not support immediate deregulation of the postal business here. I think that is something that would have to be investigated over time once the postal business here has been able to prove itself as a commercial entity.

Mr. MCHUGH. Thank you very much.

As a related follow-up, I would think you three gentlemen would have a lot in common. You certainly have some powers that would be in some ways envied by our postmaster general, in your opportunities outside the letter mail to commercialize.

Mr. Clermont, you mentioned the recurring charges of cross-subsidization that you have encountered. We are encountering that against our Postal Service already. I have to wonder how, particularly given your high level of commercialization outside the letter mail monopoly, you have been able to prove that you are not cross-

subsidizing. How do you build those walls in a way that is believable?

Mr. CLERMONT. Well, it is extremely technical, but I think that the last time we were at the Bureau of Competition, which is a judicial tribunal there to administer the Competition Act, which is the equivalent of your antitrust legislation, and we made the proof, just like any other companies would, that the combined—two things—that the combined market share of Purolator, the company we were acquiring, and our market share in the courier business would not be detrimental to the competition in that business in Canada; and then, secondly, we opened our books to the Bureau of Competition. We had accountants, we had our auditors come to the Bureau, and in its public decision, the Bureau stated that it was satisfied that the accounting practices of the corporation were such that there was no need to be concerned with cross-subsidization.

Mr. McHUGH. Let me interrupt you, and I apologize. You said you opened your books. Do you have certain data or information that you consider proprietary, and you do not share?

Mr. CLERMONT. Very much so. We have some data that we will not share. We will share with the Bureau of Competition, and we are equal to any other corporation in that sense. There is provision in the antitrust legislation for the Bureau to keep some information confidential if it is commercially sensitive or would give undue advantage to the competitors.

Mr. McHUGH. But all of that information is opened up to an independent panel.

Mr. CLERMONT. Yes.

Mr. McHUGH. I have many other questions, but I would defer back to the good Senator at this time so that others may question you.

Thank you, gentlemen.

Chairman STEVENS. Thank you very much.

Mrs. COLLINS?

Mrs. COLLINS. Thank you very much, Mr. Chairman.

Chairman STEVENS. We are using about a 10-minute, give-or-take rule. Please proceed.

Mrs. COLLINS. Thank you, Mr. Chairman. I have about three or four questions.

Mr. Clermont, what does "long-distance transportation" mean?

Mr. CLERMONT. We mean inter-city or inter-provincial. We have a fleet of stepvans to move mail in the cities, but any other transportation as between Toronto and Montreal or Ottawa and Montreal is contracted out to the private sector. So we are the largest user of transportation services in Canada.

Mrs. COLLINS. So your postal service that the Government owns is only within a city or province?

Mr. CLERMONT. Yes. Otherwise, we move it through—

Mrs. COLLINS. Your transportation is Government-owned isn't it—your railways?

Mr. CLERMONT. No. First of all, we do not use the railways, but this was Government-owned until 3 months ago; it was privatized 3 months ago. Canadian National Railways was privatized.

Mrs. COLLINS. All right. You said you have a state-of-the-art control center in Ottawa that allows you to track every piece of mail.

Mr. CLERMONT. Yes.

Mrs. COLLINS. Even through the private carriers, then?

Mr. CLERMONT. Yes. Well, we track the letter containers in which mail is placed. We track every, single piece of mail of courier, for instance, where the customer buys a track and trace feature. So we know where that piece of mail is at any moment in time.

Mrs. COLLINS. Mr. Chairman, it might be nice to have a CODEL to visit that center in Ottawa.

Mr. CLERMONT. You would be most welcome.

Mrs. COLLINS. I would really like to see that.

Mr. MCHUGH. That is just a few miles from my Congressional District, so no problem.

Chairman STEVENS. Well, I think you have a good idea. It does seem to me that we ought to go on a basis of not only both Houses of Congress, but with the management and labor structure of our country, and go and visit some of these and have some informal conversations to get a better grasp of what has happened in these areas, because they are ahead of us in terms of modernization—not in modernization, but in terms of management reform.

Mrs. COLLINS. Mr. Toime, you said 32.1 percent profit. Is that in 1 year, or is that over the 8 years?

Mr. TOIME. That is in 1 year; it has been profitable over the years, and the average for the last 5 years was 24 percent return on shareholder funds.

Mrs. COLLINS. After tax?

Mr. TOIME. Yes, after tax.

Mrs. COLLINS. That is wonderful.

Mr. John, you mentioned that you flattened the management structure and removed job tenure for managers and reeducated them to focus on the bottom line rather than building bureaucratic empires. I wonder, how long did it take you to resolve that labor-management tension? Was that something that happened in 1, 2, or 3 years, or are you still working on it?

Mr. JOHN. Well, we have gone a long way toward solving that. I would say it is about 80 percent completed. And we have just conducted surveys of our staff, and it is showing that that is in fact the case.

But we certainly did change our method of management. All of our executives had security of tenure in their jobs—and I am going back now to corporatization in 1989—and the management structure was challenged because it was recognized that the style of management, bureaucratic, inward-looking, was not going to take Australia Post where it needed to go to survive.

So five senior positions were advertised, and of those five, three appointments were made externally, and that was either through people applying or, in my case, a headhunter. Then, that process was cascaded down through the senior management positions, some 150–160 management positions. And then, the next two levels of management, which was around 430–450 people, were all taken from security of tenure as well, so that they were then placed on performance contracts, and their salaries were adjusted to take into account their loss of the security of tenure.

Some of those positions were advertised, and some were not, but it meant that there was about a 25 percent change in the management structure throughout the organization, and that was to introduce new culture, which became market-driven rather than operationally inward-looking.

Mrs. COLLINS. You mentioned that most of the major decisions that affect the workers were jointly made between labor and management. Did labor pick their own representatives to work with you on those, or did your postal service pick those representatives?

Mr. JOHN. Our participative management is a style of management, and I will just run through the sort of environment that is created. There is a preamble about the necessity to commit the union and the management toward the viability and continued efficiency and reliability of providing service to the organization.

But briefly, the steps were: that effective local consultative arrangements are to be put in place; middle managers, supervisors and staff are assisted and encouraged to participate in problem-solving decisions at their own workplaces; effective two-way communication with staff is to take place; and first-line middle managers are assisted and encouraged to play a greater role; adequate training is given to management, supervisors and staff in participative groups, to enable them to talk meaningfully to each other and to identify, analyze and resolve problems; the reasons for changes affecting their workplaces are to be clearly explained and discussed with all staff prior to implementation; contentious decisions or implementation difficulties arising out of national agreements are to be referred to higher levels before implementation so that consultation can take place at those levels; the roles and functions of various management levels and union representatives need to be clearly documented and respected. The parties agree that priority needs to be given to putting the above principles into effect, and National and State groups will be established to lead and monitor resultant actions.

The participative culture of Australia Post is what really has changed the whole culture of the organization, and it is the foundation stone of all of our methods of implementing change and maintaining change. We have now moved to quality accreditations and world best practice by using a participative management approach. It involves everybody; even I have been to a 7-day off-campus participative management structure. We are about halfway through training people in the whole of the organization in participative management of the workplace center, but most of them have all had training on the work center in smaller areas.

Mrs. COLLINS. Have all of you had great success in your labor-management relationships?

Mr. DAHLSTEN. If I may answer that question, if you make a big change like most of us have done, there is of course a bit of turmoil around that, and you have to expect it. But we have had the support of the labor unions in all basic changes. They understand that it is a question of survival in the long term, and they cannot hang onto old systems.

The biggest problem was to change the system of wages to a more modern, business-oriented way, with bonuses on the profit center level and so on.

Mrs. COLLINS. Was that an increase in wages?

Mr. DAHLSTEN. No—well, you could put it this way. The fixed wages were reduced, actually, but the incentives were increased. This has worked very well in the long run and has increased efficiency enormously.

So this breaking down into profit centers has also meant that we now have formal boards where union representatives participate. They appoint a couple of the members of those boards that are running those broken-down profit centers and are in that way participating in the corporate planning.

Mr. TOIME. In New Zealand, we have spent a lot of time to ensure that labor unions and employees understand the reasons and background and necessity for the change, what the company is trying to achieve. We have had no lost time. Even though we have implemented some very significant reforms within the business, it has always been explained and understood in the context of the commercial necessity and the need to win in the future. So it is always focused on what is to be achieved in the future.

Mrs. COLLINS. Mr. Chairman, I want to ask one more question about the shareholders. Is that open to the public?

Mr. TOIME. Not in New Zealand. The Government is the sole shareholder, and that ownership is separated quite clearly from the issues of regulation and the social obligations.

Mrs. COLLINS. I see.

Mr. CLERMONT. It is the same thing in Canada.

Mr. DAHLSTEN. The same thing in Sweden.

Mr. JOHN. We refer to our shareholders—even though we are Government-owned—as firstly the people of Australia, and they get a dividend in the area of efficiency in the lower price of the letter. The employees there are shareholders in the business, and they get increased rewards by improving their efficiency through our enterprise bargaining agreements. And the management naturally share in the success, and the legislative people share, and the Parliament who represents the people shares in the success of their ability to come to grips with what needs to be done.

Mrs. COLLINS. Thank you.

Thank you very much, Mr. Chairman.

Chairman STEVENS. Thank you.

Let me welcome Gene Green of Texas. Congressman, did you have an opening statement you would like to make?

Mr. GREEN. Mr. Chairman, I would just like to submit it for the record and thank you for having the hearing.¹

Chairman STEVENS. Thank you very much.

We will now turn to Congressman Mark Sanford.

Mr. SANFORD. Thank you, sir.

One quick question, and in large part this is following up on co-Chairman McHugh's thoughts on the issue of privatization, commercialization, whatever you want to call it—

Chairman STEVENS. Congressman, could I interrupt, please? Pardon me.

Mr. SANFORD. Yes, sir.

¹ See Mr. Green's prepared statement on page 26.

Chairman STEVENS. I see people standing up in the back. These chairs up in front are no longer reserved; so if you would like to come up front, we would be pleased to have you.

Pardon me.

Mr. SANFORD. Yes, sir.

My question is sort of open-ended, and that is, if you were to take New Zealand as being the furthest out there on the competition frontier, are they the only ones on the right track? Some people have argued that changes in technology will take away in time monopolistic control of any mail system. If you look, for instance, at the Atlanta-New York mail route, right now, that is a cash cow for the U.S. Postal Service. However, as technology changes, the cash cow portions of the business will be eroded in terms of market share by electronic mail and by a whole host of other activities, and therefore it is going to be tougher and tougher to do universal service at one price.

Some have therefore argued, go ahead and make the change now so that the Postal Service can be reactive and be prepared to offer at least quasi-universal service at one price, or close to one price, rather than make an abrupt change down the road.

What is wrong with that argument?

Mr. CLERMONT. Personally, I do not think there is anything wrong with this argument. We have to prepare now for the future, and——

Mr. SANFORD. But my question is competition, the way New Zealand has gone, is that the only way to get there?

Mr. CLERMONT. I believe so.

Mr. SANFORD. Would that be contrary to your——

Mr. CLERMONT. Well, New Zealand still has the monopoly. I think it has to be a system of checks and balances. In a country like Canada, there is no question that down the road, the substitution will take its toll. But we see our role in Canada Post Corporation as the one organization that can still, even in an electronic age, offer universal mail service, whether the mail is electronic or otherwise.

We are partners in a test being developed in the Province of Quebec for interactive, universal, bi-directional cable television, with a cable TV company and a phone company and a bank, because we see that this is probably where our future lies.

We will not have a monopoly or any form of monopoly there, of course, and we will have to prove as good as any, and the earlier we can start doing that, the better. I think that at three times the letter rate, as I indicated, our monopoly is very lax—plus a number of exceptions, at least two pages of exceptions, and a policy of not enforcing it. We are almost at the point that Mr. Toime suggested.

Mr. SANFORD. Are there any other thoughts on that?

[No response.]

Mr. SANFORD. If not, I will yield back my time, sir.

Mr. DAHLSTEN. Not to misunderstand my position here. I agree with Elmar Toime that you have to be prepared for competition first, and I do not think that in the present situation, the USPS should be put in a situation where they have to face total deregulation. That would probably be disastrous in the short term, but also in the long term.

So you have to take it in steps. But perhaps you are better off if you decide upon the steps now, saying that you have this timetable, so that everyone knows what to expect, because if you know that, then you prepare yourself. Otherwise, you will just postpone the preparation.

But that is my view, and I still believe that you should deregulate, but you have to take into account that the circumstances should be according to a timetable where USPS step-by-step prepares itself for the new situation.

Mr. SANFORD. Thank you.

I yield back.

Chairman STEVENS. Thank you very much.

Mr. Green?

OPENING STATEMENT OF CONGRESSMAN GREEN

Mr. GREEN. Thank you, Mr. Chairman. I appreciate the opportunity to be here.

Gentlemen, if you cannot tell from my accent, I am from Texas, and there are some comparisons—I know the testimony from Sweden Post is that they handle 4.3 billion pieces of mail each year. In the district that I represent in Houston, we process 1 billion per year just in our facility. And it is a new facility that has been modernized in the last few years, in fact, upgraded, and it is literally state-of-the-art—although, Mr. Chairman, I enjoyed my visit to the North Slope in August, and I would think some of the North Slope in your State would be similar to the northern part of Sweden, where it is difficult to get to, particularly on a daily delivery, but it is done, and I know in Sweden, too.

This is my first term on this committee, and all of us utilize the mail, and we know the problems that we see. After reviewing the testimony, I know that each of you moved from less autocratic management to more employee involvement. And I see the complaints that we get from both employees and managers in our system. Each of you has some type of collective bargaining agreement with your employees, and I know from the history of your countries that you have a long tradition of collective bargaining, so you involve them in the success you have had the profit from. In New Zealand particularly, it is a part of involving your employees in that and using their collective bargaining agreement.

I know my colleague from Detroit probably asked some similar questions, but one of the complaints I receive from the actual line workers, letter carriers, postal workers is that sometimes we have such autocratic management techniques, and I know you reached that hurdle and obviously have had success in overcoming it when you add 10 times or 20 times the number of employees and the number of parcels and items that we deliver.

If you have some suggestions that we could use to involve more—and I know that is also the tone of management, though, in private business, is to involve your employees in your decisionmaking, using the collective bargaining process that each of you have. And so I wonder if you have any comments on that, or on any particular success that you may have had, how you developed that trust between management and your employee groups.

[The prepared statement of Mr. Green follows:]

PREPARED STATEMENT OF CONGRESSMAN GREEN

I would like to thank and commend Chairman McHugh for having the insight to hold these much needed hearings on Postal reorganization within the U.S. Postal Service. In this time of massive reorganization and streamlining of the Federal Government it is timely to hold these hearings.

The U.S. Postal Service handles the largest amount of mail in the world and therefore is very unique, however, it is to our benefit to look at what plans other countries have implemented in their successful reorganization plans.

With the technological advances this country has made it is in our best interest to look at reorganizing the U.S. Postal Service and bringing it in line with today's competitive market.

As always I look forward to hearing from the various witnesses who will testify this morning on how we can make the postal service more responsive to the needs of its customers and more competitive in this world of ever increasing technology.

Again thank you, Mr. Chairman.

Mr. CLERMONT. If I may, Mr. Chairman, what struck me on visiting the U.S. Postal Service and the conversations I have had is indeed, still, the great degree of autocracy that I find here. And perhaps one symptom of this is the importance that the security investigation branch of the postal service still has.

I think that you get what you call for. First of all, the department used to hire a supervisor, give him or her a baseball bat, and then tell him or her walk behind the rows and make sure everybody was there. And that is very true that it was done this way.

We have reduced the number of supervisors by 50 percent. In some offices, we do not have supervision. The unionized work force elect a lead hand, and he is one of them, and they are probably the ones that run best.

We have reduced the role of our security people by 90 percent. The head of security is three levels down in the organization. And I remember that when I first came to Canada Post in 1983, the head of the security to the postal service came back with a lot of good recommendations that he had heard here, and I fired him promptly because that was not the tone that I thought we needed in the organization, and I think it served us well.

It is a cliché the violence in the Postal Service. You see it in comedies and skits. But we do not have that problem, and again, you have to wonder who brought the gun into the workplace in the first place.

Mr. TOIME. Mr. Chairman, if I might just add some brief comments to that, I think this question of autocracy is a major management development issue, and it does take time to address, and I think some of the things we just heard from Canada are very, very applicable.

What I would add in addition is that every manager in New Zealand Post has objectives relating to improvements in employee satisfaction. It is a truism in management that you get what you measure, and really, this has made a significant difference. Managers are being forced to think about what their employees think about them. We have independent surveys three or four times a year which are reported back to the employees and the managers, and that really is making significant differences in the business.

Thank you.

Mr. JOHN. We have approached it very much in the facility basis and in our enterprise agreement, where anybody who works in a particular facility, that facility qualifies under seven different cri-

teria. They actually score themselves, and once they get to a certain level, they get a cash payment—this year, it is \$580—for achieving above the benchmark, and we keep lifting the benchmark in each one of the agreements. So we actually give the people the money, and they form their work groups and their teams to achieve a reduction in absenteeism, better occupational health and safety, better performance regulation. So we are sharing the gains with our people. And then, if the conditions under which they are working in terms of hours and things of that nature are no good, we have the flexibility within our organization and with our union's concurrence to have a separate agreement so that people can come to work any time they like and leave any time they like provided they put in all the hours.

So the people have actually got a buy-in to the community in which they work and the environment and the social reaction, and we have continual programs in innovative ways for people to come to work and spend their time in happier, better environments. We are the leading edge in that in Australia, and our quality service programs are internationally recognized and in fact have been taken up by some of the postal administrations and outside of the postal organizations.

But what it has done is allowed everybody to have a buy-in in their facility, so they are relative to their day-to-day job; they are not part of an enormous bureaucracy, and they are not lost. Every individual is represented and given an opportunity to be a part of a team and to be able to be rewarded through achieving predetermined goals.

Mr. DAHLSTEN. I would also emphasize what has been said here about how you must get there. Targeting on profitability, customer satisfaction and employee satisfaction is essential, because you do what you are targeted on, and you get your bonus.

I would just add one thing. The breaking down of the company into business areas, into subsidiaries, into profit centers that are so small that people can feel part of the unit, is essential. Modern IT technology makes it quite possible to keep a very complicated company together even if you break down the responsibilities into those small profit centers. I believe that to be the way to get real participation.

Mr. GREEN. Mr. Chairman, I noticed in Canada Post in particular, on-time delivery has gone from 85 percent to 97 percent. Again using Houston, we were trumpeting 86 percent overnight in our area, and that is such an improvement. And you still increased to that 97 percent without losing some of the support that you have from your employees, and that is commendable in each of the countries.

Mr. CLERMONT. I think our employees are very much behind us, Mr. Chairman. I wish that their labor leaders were as much behind us as the membership is, but that will come. It is still ingrained in the tradition. But I believe that working and empowering our employees the way we have, and because I spend a lot of time in the plants myself, I hear what they have to say, and they want a change in the leadership of their unions as well.

Mr. GREEN. Thank you, Mr. Chairman.

Chairman STEVENS. Thank you.

Gentlemen, we come from a different constitutional base. Our Constitution requires us to maintain post offices and post roads—an interesting thing that some people forget sometimes.

I wonder, do we all have the same definition of “universal service”? Is it service anywhere in your Nation at a fixed price? Is the postage stamp rate the same throughout the service area? Do we have the same concept of universal service?

Mr. DAHLSTEN. Not fully. In Sweden, we have five times a week, and there is a universal price cap for individual letters—single letters, not for bulks—

Chairman STEVENS. You have different rates for parcel post, then.

Mr. DAHLSTEN [continuing]. But it is overnight, so it has to be overnight all over the country. That, I do not think is the case in any other country.

Chairman STEVENS. You put a time factor in universal service that it must be overnight.

Mr. DAHLSTEN. Exactly; it must be overnight. I think we are the only ones who have that.

Chairman STEVENS. Do any of you have zones for letter service? Is it universal throughout your country?

Mr. TOIME. Throughout the country.

Mr. CLERMONT. We do not, Mr. Chairman, legally have to maintain a post office in every community.

Chairman STEVENS. That was going to be my next question. We do not have that mandate, either, but it has been a tradition in our country that every community has a post office, and we have gone to contract post offices at times.

Do all of you maintain post offices in each community?

Mr. JOHN. Our Act defines it as “access to the postal service anywhere in Australia,” and that access can be through various methods other than a post office. It can be through the community service mailbag and a plethora of different ways of accessing, but that is how it is defined in our Act, as access to the postal network.

Chairman STEVENS. Well, our Congress has mandated 6 days delivery per week. I take it you all work on a 5-day basis; is that correct?

Mr. TOIME. Six days in New Zealand.

Mr. CLERMONT. Five in Canada.

Mr. JOHN. Five in Australia.

Mr. DAHLSTEN. Yes, five.

Chairman STEVENS. Five elsewhere. Was that a change from the time that you went into this deregulatory period? Did you have 6 days before?

Mr. JOHN. No.

Mr. DAHLSTEN. We had 5 days.

Mr. CLERMONT. We had 6 days. This was not legal, Mr. Chairman. It was a policy. It had always been 6 days, so we moved it down to 5 days.

Chairman STEVENS. There has been some concept expressed here about employee relations. I take it from what has been said that some of you have operated under systems where your employees have the right to strike, but it is compulsory arbitration if they do

strike, with the right of the government to call them back during compulsory arbitration.

Is that the case uniformly here?

Mr. DAHLSTEN. No. They have the right to strike without any restrictions. But the real restriction here is that they are afraid of loosing jobs. In Sweden, it is perhaps easier than in many other countries to lay off. Our situation is just like that of a private company; there is no difference. And therefore, they know that if we are not competitive, we will have fewer jobs, and that is the real restriction.

Chairman STEVENS. I see.

In the other countries, is there the right to strike subject to compulsory arbitration?

Mr. TOIME. In New Zealand, once we have an agreed contract for a period of time, there is no right to strike, but you can strike in negotiating for a contract, and then there is no compulsory arbitration. It is absolutely between the employees and the company to resolve all industrial matters.

Chairman STEVENS. But if there is no contract, what happens, Mr. Toime, at the end of a contract?

Mr. TOIME. At the end of the contract, both parties have to come together to attempt to negotiate a new one. It is left to the parties to do that. It has always been achieved.

Chairman STEVENS. You have been successful.

Mr. John?

Mr. JOHN. We have a right to strike, and they do go on strike, and we have an arbitration system which can direct people to return to work, but they do not necessarily have to do that, so then we resort to civil action. We have the capability of doing that.

Chairman STEVENS. Do you have striker replacement? Can you replace people who are on strike?

Mr. JOHN. Under certain conditions, but very, very rarely would that be invoked.

Mr. CLERMONT. We have that ability, Mr. Chairman, to hire replacement workers. We have done it twice.

Chairman STEVENS. You have some interesting retail outlet franchise agreement, in going over the papers that we have gotten. I would be interested if you could tell us how they have worked with regard to staffing and with regard to location of the offices. Are those like our contract post offices, where we contract with an entity to provide the postal service—usually, it is boxes that they provide at a central location within a community—or am I misreading this franchise agreement concept?

What does it mean to you, Mr. Clermont?

Mr. CLERMONT. For us, it is the same as a McDonald's franchise. We have contracted offices. We used to have more of them. We call them sub-post offices. But the franchisee puts up the money up front, then he pays in royalties afterward. He or she has to buy a standard set of equipment, counters, that are to our design, and then operates it with his or her own staff.

The way we choose the franchisee is to go through a locational analysis first—where should the post office be located, at the corner of such-and-such street. Then we see who is interested around

there. Most of them are in drugstores. We have the same conditions as you would see in a McDonald's franchise.

Chairman STEVENS. They can operate other businesses on the same premises?

Mr. CLERMONT. Oh, very much so, very much so, yes.

Chairman STEVENS. Do you have some standard of compatibility? Could you put it in a McDonald's, or can you put it in—

Mr. CLERMONT. Well, we try to choose businesses that are open very long hours and weekends. Drugstores are the most common choice.

Chairman STEVENS. Do you do that, too, Mr. John?

Mr. JOHN. Yes. We were losing an enormous amount of money in our retail networks, and in conjunction with our unions, we came to an agreement that we had to tackle it. And what we did was we said we would convert—where we had three full-time employees in a post office that were losing the bulk of the money, that we would convert those to agency arrangements. So the postmaster was offered, indeed, the purchase of the premises, the purchase of the business, but generally, it could not operate by itself, so if it was unprofitable with us with three people, it was going to be unprofitable with him. So then it became what we call an "in conjunction licensed post office." So they are with news agencies, with pharmacies around the country, and that is the major part of our retail network is licensed post offices. And our franchisees are remunerated on a commission system where they get a commission for selling stamps, they get commissions for doing banking and things of that nature. They also provide lockboxes and security and private—

Chairman STEVENS. Do they charge the customers for the lockboxes?

Mr. JOHN. Yes.

Chairman STEVENS. In New Zealand, do you have similar concepts of franchise or contract operations?

Mr. TOIME. Yes. In New Zealand, we have both franchise and contract operations. Franchises operate exactly as was described in the Canadian case, strict franchises, always in conjunction with other businesses, and we find that the postal element will contribute to the fixed costs of running that business, but will not contribute to profit, so it does require some other business in conjunction with the post. We also have some contract offices.

The whole objective is to convert fixed costs into variable costs. That is the millstone of the post, and the opportunity to contract out post office services really shifts from fixed to variable cost.

Chairman STEVENS. Do you have the same experience in Sweden, Mr. Dahlsten?

Mr. PERSSON. Yes. The Swedish franchise system is normally a grocery shop taking over as a franchisee, and he works on a 50 percent fixed revenue and 50 percent variable revenue. And a successful franchisee in Sweden gets about \$20,000 per year.

Chairman STEVENS. I am delighted, gentlemen, that you are going to join some of us for lunch, and we will have some further conversations about some details. But let me ask you about one detail that is very interesting to me, personally.

I am the Senator who proposed the reformation of our Federal retirement system. We have a new type of retirement system now, and it is available to our postal employees. Is your Government retirement system available to your postal employees, and do you make contributions as an employer to that retirement system?

Mr. JOHN?

Mr. JOHN. Yes. All of our employees have an opportunity to join a retirement fund. It is one of the most generous in the nation. There is a qualifying period; they make contribution, we make contribution, and it is universal to everyone.

Chairman STEVENS. Mr. Clermont?

Mr. CLERMONT. The same thing.

Chairman STEVENS. Mr. Toime, do you have one?

Mr. TOIME. Our employees do not belong to a Government fund; they belong to a company-sponsored fund.

Chairman STEVENS. But is there any contribution from your Government to that system?

Mr. TOIME. No, not at all, no. Totally——

Chairman STEVENS. It is totally privatized now?

Mr. TOIME. Totally privatized in terms of pension schemes.

Chairman STEVENS. Very interesting.

Mr. Dahlsten?

Mr. DAHLSTEN. When we became a limited company, we took over all pension liabilities from the State, which meant a big dip into our equity, actually, but now everything is on our agenda; nothing on the State.

Chairman STEVENS. My last question would go to you, Mr. Dahlsten. You made a comment that in rural areas, your postage rate does not cover the costs, but that you have worked that out. That is a problem in our country and in Alaska in particular. How have you worked out the differential of costs in rural areas?

Mr. DAHLSTEN. First of all, I would say that you have to realize that it is part of the business idea that everyone should reach everyone. If you look upon Federal Express and UPS, private companies, for instance, you can see that they basically try to solve these problems in many ways. Everyone has to reach everyone; that is part of the whole idea.

You could not run a business like this without that concept. You have to bear that in mind. It is not just a question of cost; it is a question of giving service according to what the customers want.

The other thing is that you can do this by being competitive for the business community. If you give them the services in the big cities, the services that the big industries and the big customers want, then you get the revenue and the profitability that will cover the costs for the rural areas.

That is what it is all about. If you are not allowed to really compete where the big money is, then you will never have a chance to pay for the costs for the rural areas.

Chairman STEVENS. Do you get any Government contribution for the excess cost of rural areas, any of you?

Mr. JOHN. That is covered by the universal service rate.

Chairman STEVENS. But in your privatized system, or even semi-privatized system, the postal rate is sufficient to cover the excess cost to rural areas?

Mr. JOHN. Yes. We identify a community service obligation and actually put a value on that on an annualized basis, and it is \$60 million, or it is \$90 million, or it is \$100 million, and that is the community service obligation which is funded by the cross-subsidization of the basic letter price, the basic letter being less than 250 grams. Anything above that has differential pricing. We charge more to go a farther distance than we do for a shorter distance.

Chairman STEVENS. But what about your parcel post system in rural areas? Is it strictly on a cost basis?

Mr. JOHN. That is deregulated; we can charge what we like.

Mr. DAHLSTEN. Totally deregulated. We have a lot of private competitors, although we are market leaders now, and the most profitable one.

Chairman STEVENS. But you do have different rates to rural areas?

Mr. DAHLSTEN. We have the same system with a price cap that is put by ourselves for commercial reasons.

Mr. JOHN. We operate virtually a universal service in our parcels market above the 250 grams because it is a market advantage for us. But the Government from time to time does look at our prices for nonreserved services, and as a matter of fact, that is up to inquiry at the moment.

Chairman STEVENS. I have taken a little more time than I should. Mr. Chairman, do you have any further questions?

Mr. MCHUGH. Mr. Dahlsten, I assume you pay full taxes as any operation or enterprise in your country; true?

Mr. DAHLSTEN. Yes.

Mr. MCHUGH. Mr. Clermont, you mentioned that you do pay taxes on your commercialized enterprises, but do you pay property taxes on your freestanding postal offices, etc.?

Mr. CLERMONT. Yes.

Mr. MCHUGH. So you pay taxes from top to bottom.

Is that true for you, Mr. John?

Mr. JOHN. We pay all taxes as though we were a private enterprise organization.

Mr. MCHUGH. Mr. Toime?

Mr. TOIME. The same.

Mr. MCHUGH. So there is no exemption or attribution for your letter mail monopoly?

Mr. JOHN. None whatsoever.

Mr. CLERMONT. No.

Mr. DAHLSTEN. No.

Mr. MCHUGH. Thank you, Mr. Chairman.

Chairman STEVENS. Mr. Sanford, do you have any further questions?

Mr. SANFORD. No.

Chairman STEVENS. Mr. Green?

Mr. GREEN. No, thank you, Mr. Chairman.

Chairman STEVENS. Gentlemen, thank you very much. We will join you later when you will be our guests for lunch, and if you wish to hear the next two witnesses who will talk about the studies they have made, you are welcome to remain. But we hope that you will join us in about an hour in the Senators' Dining Room. We

look forward to being with you, and thank you very much for your courtesy.

I do think the record should show that these gentlemen have come a long way to be here at our request, and the experiences that they have shared with us for the record and in the materials they have provided to us are going to be very helpful to our Government, both in the Postal Service and here in the executive branch, to try to see if we can move forward in our postal reform.

We are now going to listen to Mr. Michael Motley, who is the associate director of the Government Business Operations Issues for the General Accounting Office. He is accompanied by Mr. James T. Campbell, who is the assistant director of that area for the GAO.

We also welcome James Waddell, a partner in Price Waterhouse, who is accompanied by David Treworgy, who is also with Price Waterhouse.

We will use the same procedure, if you agree, Mr. Chairman.

Mr. MCHUGH. Absolutely.

Chairman STEVENS. We will listen to Mr. Motley and any comments Mr. Campbell wishes to make, and then to Mr. Waddell and Mr. Treworgy, and then we will have some questions.

May we start with Mr. Motley?

TESTIMONY OF MICHAEL E. MOTLEY,¹ ASSOCIATE DIRECTOR, GOVERNMENT BUSINESS OPERATIONS ISSUES, U.S. GENERAL ACCOUNTING OFFICE, ACCOMPANIED BY JAMES T. CAMPBELL, ASSISTANT DIRECTOR, GOVERNMENT BUSINESS OPERATIONS ISSUES, U.S. GENERAL ACCOUNTING OFFICE

Mr. MOTLEY. Thank you, Mr. Chairman.

Chairman Stevens, Chairman McHugh, and Members of the Subcommittees, it is a pleasure for us to be here today. You have already introduced Mr. Campbell, who is in charge of all of our postal operation activities, reviews and investigations for the General Accounting Office as we look into postal activities.

I am going to summarize my statement, of course, and would like it to be put into the record in full.

Chairman STEVENS. They all will be included in the record.

Mr. MOTLEY. We appreciate the opportunity to participate in this hearing today, and we will discuss the experiences of other postal administrations that are particularly relevant to any future decisions by Congress affecting public service obligations such as universal service and uniform rates, the postal monopoly, and regulation of postal prices.

My testimony is based primarily on our past and ongoing work. However, we have done some limited work in other countries, most of which has been concentrated at this point on Canada Post.

Our statement will also refer to postal administrations in seven other countries, many of which have testified just recently.

While we believe that the overall experiences of other countries' postal administrations are relevant to the current discussions of postal reform in the United States, meaningful comparisons of specific operational practices are difficult. Compared to each of the eight other postal administrations, the U.S. Postal Service has at

¹ The prepared statement of Mr. Motley appears on page 148.

least seven times the mail volume and at least twice the number of employees. All eight postal services combined have only one-half of the U.S. Postal Service mail volume and just slightly more than the total number of its employees. The U.S. Postal Service handled about 180 million pieces of mail in fiscal year 1995 and had over 850,000 employees in December 1995.

Notwithstanding the differences in work force size and mail volume, other countries' experiences with granting their postal administrations greater commercial freedom are relevant to current consideration for granting such freedom here in the United States.

For example, in 1992, we issued a report describing how the competition from both private firms and electronic communication, particularly in expedited service mail and package delivery markets, may create the need for statutory change. Similarly, according to Price Waterhouse's February 1995 report, while many factors are driving postal reform in other countries, the increase in competition in the delivery and communications markets has, above all else, driven the changes.

In the past decade, a number of countries have restructured postal administrations from entities subject to close governmental control to entities that are still owned by the government, but with less government control over day-to-day practices.

As we have just heard from Canada, in 1981, they started their Canada Post Corporation, an entity owned by the Canadian Government but freed from many government regulations. And as we heard from Sweden, in 1994, they started, and in Germany in 1995.

The Postal Service in 1970 had its Postal Reorganization Act which created the U.S. Postal Service, and that is the most recent change, or major change, for the U.S. Postal Service here in the United States. So as far as change, we are considerably behind these other countries, and there are opportunities to learn.

Following the reforms in other countries, they reported significant improvements in financial performance and service delivery. We believe that three areas—universal service, the mail monopoly and rate-making—will be among the most challenging for Congress to address in any future reform of the U.S. Postal Service, so we will specifically highlight those today.

However, it is important not to forget the interrelationship of other factors which most likely will be affected during reform. Those include, but are not limited to, the employees of the Postal Service, postal labor-management relations, and quality of service.

Let me briefly discuss universal service. The primary mission of the U.S. Postal Service as it now exists in law, is to provide mail delivery service to persons in all communities and access to the mail system through post offices and other means. The rate for First Class mail must be uniform for delivery anywhere in the United States.

In all of the other eight countries, the postal administrations provided certain services widely to their citizens and at uniform rates before reform and continued to provide them following reform.

However, the definition, which I think you got to quite succinctly at the end, Mr. Chairman, is different and varies from country to country. Some of the countries provide the same level of service for

urban and rural customers, while others have different service standards for urban and rural customers.

For example, Canadian citizens in very remote areas in the far north may receive mail delivery less frequently each week than those in some other areas of Canada.

Accessibility to postal services, which includes maintenance of local post offices in the United States, is also part of the public service obligation of postal administrations in some other countries. The U.S. Postal Service must follow strict legal criteria in determining whether to close post offices.

In New Zealand, the postal administration has negotiated a written agreement with the Government that specifies the minimum number of postal retail outlets. In the Netherlands, Dutch law specifies minimum requirements regarding the density of post offices in urban and rural areas.

Five of the eight countries' postal administrations differ from the U.S. Postal Service in that a majority of the postal retail outlets are privately owned and operated. Except for France, all of the eight postal administrations have some form of franchising policy for postal retail services.

Like the U.S. Postal Service, other postal administrations have also continued to provide certain subsidized services.

Now, turning to monopoly over the mail, it is important to understand that its definition—that is, the definition of monopoly—varies among the countries. The U.S. Postal Service has said that the current universal service obligation and related public service mandates can only be met if its markets continue to be statutorily protected by the private express statutes that provide the Service with the monopoly over letter mail. We plan to issue a report in the coming months that discusses the Postal Service monopoly in detail, including the growth since 1970 of private delivery firms that are competing and will likely compete more strongly in the future for some of the Service's First-Class, Priority, and Third-Class mail.

The postal monopoly is defined differently and varies widely in scope among the eight foreign postal administrations. In this country, the letter mail monopoly helps ensure that the Postal Service has sufficient revenues to carry out public service mandates, including universal service. The U.S. postal monopoly covers all letter mail, with some key regulatory exceptions. Postal Service data indicates that in fiscal year 1995, at least 80 percent of the Postal Service's total mail volume was covered by the postal monopoly.

All but one—Sweden—of the eight countries postal administrations have monopolies over some aspects of the letter mail. Generally, the letter monopolies in other countries are defined according to price, weight, urgency of delivery, or a combination of these factors. For example, in Canada, the postal monopoly covers letters, with a statutory exclusion for "urgent" letters transmitted by a messenger for a fee that is at least three times Canada's regular rate of postage. In Germany, the monopoly covers letters priced up to 10 times the German's standard letter rate.

Australia and New Zealand narrowed the scope of their postal monopolies after reform. For example, in Australia, the monopoly

price threshold was reduced in 1994 from 10 times the basic stamp price to four times the price.

Australia now receives the majority of its revenues from services open to competition, and Sweden has eliminated its postal monopoly—full competition for all postal and courier services.

Finally, a monopoly on mailbox access in the United States is related to the Postal Service monopoly on delivery of letter mail. By law, mailbox access is restricted to the Postal Service. In contrast, none of the eight countries we reviewed has laws that give their postal administrations exclusive access to the mailbox.

Finally, I would like to make a few comments on the greater freedom some countries have in setting postal rates. I would like to first mention that a few months ago, we issued a report on postal rate-making which updated our 1992 report, saying that if the Postal Service is to be more competitive, it will need more flexibility in setting postal rates. In our opinion, legislative changes to the 1970 Act's ratemaking provisions may be necessary in order to give the Postal Service greater flexibility in setting rates. In both reports, we said that Congress should reexamine the 1970 Act to determine whether volume discounting by the Postal Service would be considered a discriminatory pricing policy and clarify the extent to which demand pricing should be considered in postal rate-making.

Postal administrations in the other eight countries appear to have greater freedom to establish and change postal rates than does the U.S. Postal Service. In Canada, only certain rates, mainly those for full-price letter mail and the mailing of publications at government-subsidized rates, must be approved by the Canadian Government. In addition, rate proposals are not subject to an independent regulatory body as they are here in the United States. In Canada, interested parties have an opportunity to provide information, but the rate-setting process is not public, and parties do not have access to costing data or other information underlying postal rates.

In Sweden, the postal administration is free to set all prices except for the standard domestic letter. The Government and the postal administration have agreed to a price cap on the domestic letter rate equal to the standard consumer rate of inflation. Similarly, in New Zealand, the postal administration is free to set prices except for standard letters, which are subject to a price cap of the country's consumer price index minus one percent.

In summary, Mr. Chairman, while we have focused on three complex and interrelated issues of universal service, postal monopoly and postal rate-setting, there are other issues that will also require reexamination in any future reform initiatives. These include the quality of Postal Service labor relations, which has been discussed during this hearing quite extensively, and I think it is good that we have.

We previously reported that Congress may need to reconsider the collective bargaining provisions of the 1970 Act if the Postal Service and its major employee organizations are unable to resolve some longstanding problems.

As the Congress continues its deliberations on postal reform, we believe that it is important to examine the interrelationships of

these issues and how changes addressing them may affect postal operations and related services to the American public and business.

This concludes my statement.

Thank you, Mr. Chairman.

Chairman STEVENS. Thank you very much. Very interesting.

Did you have any statement, Mr. Campbell?

Mr. CAMPBELL. No, sir, I do not.

Chairman STEVENS. Mr. Waddell?

TESTIMONY OF JAMES A. WADDELL,¹ PARTNER, PRICE WATERHOUSE, ACCOMPANIED BY DAVID E. TREWORGY,¹ PRINCIPAL CONSULTANT, PRICE WATERHOUSE

Mr. WADDELL. Thank you, Mr. Chairman, Chairman McHugh, and Members of the Subcommittees. I am Jim Waddell. I am with Price Waterhouse's Office of Government Service. With me here today is David Treworgy, who is also in our office.

The principal reason for our appearance is a report that we issued in February 1995 entitled, "A Strategic Review of Progressive Postal Administrations." That report has been made available to all of you and was distributed outside.

In addition to that, we have done a substantial amount of work with the Postal Service over the years and have come to offer our views on what implications can be drawn from the experiences of other postal administrations.

My intent this morning is simply to summarize the report that you already have before you.

Twenty-five years ago, at the time the Postal Reorganization Act of 1970 was passed, the United States was on the cutting edge of postal organization and regulatory oversight. Since that time, substantial changes have occurred in the market for postal services.

The postal environment now is more competitive, and technology has transformed the nature of the market. An obvious question to ask is whether the reforms adopted in 1970 continue to be relevant in this new environment.

The Postal Reorganization Act envisioned a world largely devoid of competition. One of the principal missions of the Postal Service was, and continues to be, to provide universal service at uniform letter rates throughout the United States. In this environment, the Postal Service was given the exclusive right to deliver letter mail and, in return, the responsibility to serve every address in the country.

The advent of competition has put the Postal Service's market position at risk, particularly in lower-cost markets where profits are earned. The traditional monopoly of the Postal Service has strengthened the unions that represent its employees and made competition ever more attractive.

The regulatory structure created to protect consumers from the monopoly has proven cumbersome, especially as it regulates competitive services. The Postal Service has incurred substantial losses since the passage of the Postal Reorganization Act and is struggling to build its equity to a positive position. In view of these chal-

¹ The combined prepared statement of Mr. Waddell and Mr. Treworgy appears on page 166.

lenges, the goal of universal service may be better served by a different structure or by different operating rules for the postal sector generally.

You have heard a substantial amount of testimony over the last year from various parties regarding the challenges facing the Postal Service. In addition, you have heard proposals for dealing with these challenges. To help you in evaluating this information, I would like to highlight some of the major findings from the "Review of Progressive Postal Administrations" that we have published.

The major trends that emerge from our review of practices in other countries are the following.

First, the monopoly position held by the postal administration is under pressure in many countries. Increased competition is the norm, including competition from other postal administrations.

Second, postal administrations are being corporatized and given greater commercial freedoms. This trend is manifested in greater authority to set prices, introduce new services, acquire subsidiaries, and raise capital. Also noted is an increased accountability for management through incentive systems that reward good performance and penalize poor.

Combined with the greater pricing freedom noted previously is a trend toward the use of price caps. Price caps generally allow the postal system to adjust prices without regulatory review provided that the price increase does not exceed the country's inflation rate or some lower percentage.

In many countries, there is a trend toward increasing efficiency by downsizing the labor force. This trend, of course, can be noted in many different sectors of countries' economies. In the postal sector, downsizing is often a response to increased competition and the increased availability of technology.

Many countries are considering privatization or some partial ownership of the postal system. Only two countries have actually sold shares to the public—the Netherlands and a country that was not reviewed in our report, Singapore. In both cases, the government sold a portion of the shares of its combined telecommunications and postal authority.

Several other countries have held serious discussions toward privatization, most notably the United Kingdom, Germany, and Argentina.

The reforms developed and implemented by the eight countries we reviewed in reaction to pressing business challenges suggests some potential paths to the U.S. Postal Service in creating a business environment capable of withstanding market challenges now and in the future.

Bearing in mind the similarities yet real differences among the countries, I would like to draw on the reforms of the eight administrations we reviewed to suggest three principles of particular relevance for application to the United States.

First, to create a more businesslike organizational structure than is currently found at the Postal Service; second, to increase pricing flexibility, and third, to introduce change incrementally but meaningfully.

I will address each of these principles in turn. To create a more businesslike organizational structure, it is critical that the U.S. Postal Service operate under a structure that is able to make rapid responses to changing conditions such as competition in the market. Many of the foreign postal administrations we reviewed have worked toward achieving these objectives by recasting themselves as businesslike agencies with strong social mandates to provide universal service at uniform letter rates. As such, they exhibit many similarities to commercial enterprises, including a profit orientation, freedom to diversify product lines to meet customer requirements, ability to form joint ventures, sanction to own subsidiaries, and authority to borrow money in the private capital markets.

Internationally, the trend toward commercialization applies to all eight postal administrations we reviewed but can be illustrated especially well by the Netherlands and New Zealand, which have completed dramatic corporatizations and demonstrated substantial benefits to these actions.

For example, the Dutch Government privatized its postal service, PTT Post, along with its telecommunications business, in two public offerings that resulted in over 50 percent ownership of the holding company by the private sector. With a majority of shares held outside the Government, the organization is clearly accountable for its performance. With a strong commercial mandate, PTT Post has become one of the most aggressive players in the international mail market, successfully capturing market share from sister postal administrations, including the U.S. Postal Service. The case of New Zealand was described for us earlier this morning.

For the United States, a businesslike organizational structure could include corporatization of all or part of the Postal Service. This structure would be conducive to promoting a profit orientation throughout the Postal Service and rewarding managers that helped to achieve the goals of the business.

Corporatization would also permit the Postal Service to acquire subsidiaries, form joint ventures, and raise capital.

Against these benefits, there are additional implications from corporatization that may be positive or negative but certainly warrant further consideration. Principally, corporatization could subject the Postal Service to the same laws that apply to other enterprises, unless the new corporation were to be specifically exempted. The laws with the most far-reaching implications would include labor legislation, the tax code, and the antitrust laws. In addition, the corporate governance of the Service would likely change, with a board of directors replacing the Board of Governors.

Second, to increase pricing flexibility. Increasing the commercial orientation of the Postal Service through structural changes raises the issue of how much flexibility management would have in setting the prices of its services. The communications and delivery market is fast-paced, with competitors rapidly deploying new products and pricing structures that adroitly outmaneuver the Postal Rate Commission's 10-month rate process.

For example, earlier this month, United Parcel Service announced a major restructuring of prices, and this restructuring will take effect on Saturday, February 3rd. The Postal Service may re-

quire as long as 2 years to prepare and file a rate case; by then, market conditions are almost certain to have changed several times.

The international record reveals that many postal administrations have greater latitude in rate-setting. In countries where regulators exist, price restrictions tend to cover only monopoly products and take the form of price caps. New Zealand, for example, not only has adhered to its price cap, but actually reduced its prices.

The third principle I established at the outset is to introduce change incrementally but meaningfully. Because the organization is a large enterprise directly affecting over 800,000 workers as well as roughly 250 million customers, change to the U.S. Postal Service should be implemented with care and planned on a long-term basis. While unaggressive reforms that only tinker will overlook fundamental problems, rash initiatives that proceed too quickly could disrupt an institution of far-reaching significance.

The international experience testifies to a record of reaching substantial goals through incremental reform and an articulated, long-term strategy. For example, in a country not represented here today, Germany, the Government has consistently pursued a reform time line that began by separating postal, banking and telecommunications services in 1989. Three years later, Germany commercialized the postal service by making it a public corporation with 100 percent Government ownership. Currently, the Government is preparing outlines for deregulation and eventual privatization in the reform's final phase.

We include in our testimony a suggestion to apply these three principles to the United States. This would include an initial step of reorganizing the Postal Service's competitive businesses—principally, Express Mail, Priority Mail and Parcel Post—into a deregulated, wholly-owned subsidiary. Perhaps a year down the road, selling a small tranche of equity in the public market of this entity would achieve the dual objectives of raising revenue for the Postal Service and of providing management and employees with a real market indicator of the success of the company.

By taking a "go slow" approach that initially affects only 10 percent of the business, the lessons learned by the Postal Service and its constituents could be applied a year or two later in a second planned phase to the other 90 percent of the organization.

Options for this second phase could focus on corporatizing the remainder of the organization into one or more corporations and developing structural and regulatory policies that are consistent with the degree of competition that each of the products and services faces.

Reform of the primary products—First-Class mail and Third-Class mail—could include price cap regulation of these monopoly products. Shares in a fully-corporatized postal organization could be initially held by the Federal Government for potential partial or full sale in the future.

Although on the surface, the delivery of mail may appear to be a simple activity, the diversity of products and customers, the unique aspects of the economics of delivery networks, and the large number of individuals and businesses with a stake in the change

process combine to make reform of the U.S. Postal Service a challenging endeavor.

I thank you for inviting me here today to address the current issues facing the Postal Service.

Chairman STEVENS. Thank you very much, gentlemen.

Let me ask you both an initial question. Is the delay of Congress in getting around to modernizing the 1970 Act in your opinion jeopardizing the total operation of the Postal Service, and are they in a situation where the competition will soon overcome them?

Mr. MOTLEY. Let me start, Mr. Chairman. I do not think the delay at this point has put them in that total jeopardy that you might suggest there. I believe that the kinds of things we are dealing with now and the kinds of things you are dealing with as well, if they do not continue to be dealt with directly, could hinder the Postal Service. Primarily the electronic market that is coming in and starting to erode some of the major First-Class mail volumes in this country.

As you have seen since 1970, they have lost markets to competition that they used to have totally, and I think the electronic market is one that is going to be a tremendous challenge for them. The Postmaster General has said that they have already lost 35 percent of their First-Class mailings as a result of that and suggests that over the next several years, much more will be lost.

Businesses are concentrating in that area more and more, and as the prices of electronics become more available to households, I think you are going to see more people switching to that mode of communication.

Chairman STEVENS. Mr. Waddell?

Mr. WADDELL. I think the lack of flexibility that the Postal Service has to some degree has caused it to lose some of its traditional markets, and I think reform will be necessary so that it can continue to serve its monopoly market well.

Chairman STEVENS. I suggested in the late seventies that the Postal Service go into electronic mail and have a division for electronic mail and set up in each post office the capability for e-mail, both sending and receiving e-mail. That was not pursued.

Are those functions that might have been pursued at that time by the Postal Service and are now provided adequately in the private sector, would that be your conclusion?

Mr. WADDELL. Let me perhaps make a correction. I think that the Postal Service to some degree did pursue the e-mail option, and perhaps highlighting some of our testimony today, it ran into regulatory difficulties in introducing that service. As you know, in the regulatory proceedings, some of the competitors are permitted to appear, and as I recall it, there were some classification hearings held concerning e-mail, and the Postal Service at that point decided to drop the service.

I know that the Postal Service is considering implementing new services associated with e-mail which I think would be distinct from some of the services that are currently provided in the market, so to the extent that they are correct that there is a demand for that service, they certainly think there is a niche there that they could enter.

Chairman STEVENS. We envisioned at the time I made the suggestion the old World War II v-mail concept, where a person would come and present the letter, and the concept of having it transmitted electronically and then delivered in printed form on the other end. That has not been pursued to my knowledge in the Postal Service.

Mr. MOTLEY. Well, I think it is just now that they are starting to pursue that a little bit stronger. I think when it was initially given some thought or pursued by the Postal Service, there were probably a variety of barriers, both internal as well as external, and I do not think in some regards that the community was at that point willing or as enlightened as they are today in some of the electronic media that is available now.

Mr. TREWORY. I think it is also worth noting that, with the definite exception of New Zealand, the price of postage in the United States is substantially less than in Europe and other parts of the world, so that some of the incentive for moving to electronic communication has not been as high as elsewhere due to the fact that the United States does have such a low postage price.

Chairman STEVENS. Have any of you done any studies that indicate if we do go this step toward deregulation and privatization whether that will result in an increased consumer price? The gentlemen preceding you indicated to some extent that their steps have led to a reduction in the cost of postal service. We are already operating on a fairly low unit cost. Is it possible to reduce that cost through additional steps of modernization?

Mr. MOTLEY. I think one of the goals that the Postal Service has always had is trying to reduce those costs through modernization. GAO has reported on several occasions that unfortunately, they have not been able to meet some of those goals. A lot of the money that they put into automation programs has not been able to foster that.

I will mention as well, as I briefly mentioned in the testimony, that we will be reporting shortly on some of our work on the Private Express Statutes, some of the growth that has been taking place since 1970 of private carriers. Also, to the extent we are able, suggest that if you were to lose certain parts of the market—let us say Priority or Express Mail—the kind of impact that might have on the postal system as far as its prices are concerned.

Chairman STEVENS. Well, I am constrained to say, as I said here before in one of these hearings, that I remember when an ice cream cone was 5 cents and the postage stamp was 6 cents. And when I stop off in Salt Lake City and get an ice cream cone now, it is \$1.60, and our postage stamp is 32 cents.

Now, I am not sure that we are at the point that some suggest, that it is so broke that we have got to fix it, but I do think that these gentlemen have given us a lot of things to think about, and we ought to have your assistance to pursue them. And I thank you, Mr. Waddell, for your private cooperation.

Mr. Motley, how soon will you be able to review those other points that you have mentioned to us that were not covered by your report?

Mr. MOTLEY. I would hope that within the next several months, we will be able to issue that report that deals with the private express statutes, Mr. Chairman.

And with regard to the postal employment issues, that is the basis of the report that we had testimony about here about a year and a half ago, and I would sense that the Postal Service will be in a position, hopefully soon, to give that some additional attention now that many of the agreements have been reached with the labor unions.

And the international report I referred to hopefully will be out within a couple of weeks.

Chairman STEVENS. I would hope that we could have those final items soon. We do hope that we will have a second series of hearings on postal reform before the end of March, and that we will also have an opportunity to bring in and have a dialogue with observers and users of the Postal Service.

I would hope that we would be ready to present legislation to the Senate that would take the first step in modernization by at least the first of June. So the problem of your several months could be a problem, Mr. Motley. I would ask you, is it possible to constrain the time frame?

Mr. MOTLEY. Yes, sir. We will do that.

Chairman STEVENS. We would appreciate that very much, and perhaps we will ask you to participate when we do have hearings with the users and observers.

We may have some other questions. My colleagues have been called to a vote in the House, and I must apologize for that and for the fact that since we are not in session today until late, we really do not have great participation in the hearing by Members. That is not new for postal hearings.

We do thank you for your participation. I think we have got to take steps, Mr. Waddell, to meet the challenges you have given us in those three areas. We will work with you on doing that.

Thank you all very much. I appreciate your coming and look forward to further hearings.

[Whereupon, at 11:50 a.m., the joint hearing was concluded.]

A P P E N D I X

AUSTRALIA POST'S REFORM EXPERIENCE

ADDRESS TO THE UNITED STATES CONGRESS

Subcommittee on Postal Service
U.S. House of Representatives

Subcommittee on Post Office and Civil Service
U.S. Senate

BY THE MANAGING DIRECTOR
AUSTRALIA POST
Graeme John

WASHINGTON DC

25 January 1996

INTRODUCTION

Thank you, Mr Chairman.

As Chief Executive of Australia Post, and a member of its Board of Directors, I'm pleased to respond to your invitation to address this joint committee on our experience in significantly improving our postal service.

I have provided you with a written submission examining Australia Post's evolution from a bureaucratic department of government, to a commercially oriented and customer-focused business enterprise.

This morning I will outline briefly how we have transformed our culture; lifted our financial performance from break-even to match some of Australia's most successful businesses; built postal revenue by "freezing" letter prices and improving delivery reliability; and are now growing the business further by introducing new services.

UNPRECEDENTED PROGRESS

We have completed a half decade or so of unprecedented progress.

On every financial and operational measure Australia Post's performance today is the best it's ever been.

Profitability has more than quadrupled - from 3.5% Return On Average Assets in 1989, to 15.6% last year

or a profit of \$331.6m on a turnover of \$2.7bn

The standard letter rate has not changed since January 1992, and will remain fixed until at least 1997 - when we expect it will have brought a real price fall of around 14%, or about 6cents over that time.

Our productivity has improved at over twice the national rate - up by more than 25% at Australia Post since 1990, compared with a national gain of 12%.

In 1989 time lost to strikes averaged 1.5 hours per employee, and in 1995 was 6 minutes per employee - down almost 95%.

And in 1995 we averaged 93.6% on-time delivery of standard letters, nearly five percentage points better than in 1989.

We are now among the best Australian businesses, with only three comparable companies recording stronger profit growth than ours since 1990.

Internationally we are among the ^VWestern world's best performing postal enterprises.

'TRIPLE-A' CREDIT RATING

Standard and Poor's have great confidence in the direction we have taken the enterprise.

In 1994 they awarded us the strongest possible endorsement, a 'triple-A' credit rating; and they reconfirmed it in 1995.

Only eight other Australian corporate and government businesses hold Standard and Poor's 'triple-A' credit ratings.

CUSTOMER RESPONSE

Our customers have also noticed the difference.

Annual independent surveys show we are now more favorably viewed by both private and business customers than Australia's major communications, banking, airline, retailing and transport businesses.

Their regard for our staff has lifted 40% over the past four years. In 1991, only 6 in 10 customers felt staff cared about them and their businesses. Today it's 9 out of 10.

CHEQUERED PAST

Just a short time ago Australians were far less complimentary about their postal service.

In the mid-1980s labour relations were at breaking point. Delivery performance was mediocre. Our customers, particularly the business sector, had no confidence in our service, and the Federal Government was concerned with management's inability to fix problems properly.

Co-incidentally, the Government was tackling national economic problems emerging in the latter half of the 1980s. It saw microeconomic reform as part of the broader solution

including 'corporatisation' of its business enterprises, one of which was Australia Post

This determination by the Government to make these enterprises more efficient, to provide improved service to the community, was an important incentive in encouraging Post's management and unions to accommodate their differences, and led to recognition of a shared interest - the continued viability and growth of the business.

A 'Joint Statement of Understanding' between Australia Post and the unions acknowledged that viability of the postal service was critically dependent on our reputation. It established effective dispute settling procedures, and committed the enterprise to participative management to achieve this.

CULTURAL CHANGE

This acceptance of mutual interdependence, and its implications for security of the enterprise and for the jobs of individuals, provided the climate for a new customer-focused service culture.

We have redesigned jobs, giving all our people a say in decisions directly affecting their work; recognised and rewarded performance; and provided our people with the resources - the personal skills and equipment - needed to achieve high standards.

Increasingly we are using all their skills and talents.

We've flattened management structures, removed job tenure for managers, and re-educated them to focus on bottom line outcomes, rather than building bureaucratic empires. Autocratic management is a practice of the past.

Now most of our people feel part of a team, proud of their achievements, proud of the commercial status and performance of Australia Post, and especially proud to work for one of the most successful Australian enterprises.

KEYS TO METAMORPHOSIS

The reasons for our metamorphosis can be found in four key areas.

- **Firstly, the 'arms length' relationship between the corporation and the Federal public service.**

In the past, day-to-day controls such as contract approvals, land acquisition or disposal, labour rates and managerial salaries were entirely in the hands of Federal Government Departments. Now they are the responsibility of Board members and senior management with appropriate experience.

Discipline is brought to this freedom through the Corporate Plan, quarterly reports to the Minister, and our annual report to the Australian Federal Parliament which sets out performance against plan targets.

Controls have been shifted from a past pre-occupation with inputs and processes when Federal Government bureaucrats made key decisions, to a focus on outputs and accountability for performance.

- **Secondly, there is the healthy relationship between the corporation's management, our people and their unions.**

This is the most significant change brought to the day-to-day functioning of the enterprise.

It differs from other cultural change successes, because it involved three parties - management, staff and unions. Unlike in some other places our unions, conscious of the Government's microeconomic reform program, have been willing partners in our reform process.

Now the maintenance of this relationship is fundamental to the continued achievement of high performance levels that Australians have come to expect from their postal service.

- **Thirdly, postal regulation is relatively 'light-handed'.**

In Australia, the public interest in postal matters is protected by a combination of price capping, increasing reliance on the market and competitive pressures, and the maintenance of a high-quality, universally accessible letter service.

- **Finally, there is our commercial freedom.**

To operate and grow successfully, the legislators accepted our need for freedom to introduce commercial services compatible with our business

but without reducing the scope and effectiveness of our community service obligation to provide all Australians with a uniform-priced letter service no matter where they live

This freedom meant we could stem the financial haemorrhage through our network of postal outlets.

Many have been relocated, reconfigured, and re-equipped with purpose-built electronic counter technology. A range of postal-related products and electronically accessed financial services, including banking, are now available through them.

The postal related products, such as cards and stationery, will this year earn nearly as much as our long-established philatelic sales business. And we expect financial services will generate 40% of postal outlet revenue by the year 2000.

With its introduction our new Express Post service was immediately competing successfully with overnight courier services, and it continues to grow strongly.

Now we are working on services that will meet electronic communication needs, the integrated mail of the future.

CONCLUSION

Mr Chairman.

The Government leveled the playing field requiring us to pay all the same Federal, State and local government taxes and charges that apply to any commercial business.

All new services must stand ~~alone~~ commercially without subsidy from reserved letter-service revenue.

And all services are now subject to the competition reform legislation which applies to all businesses.

While Australia Post is making progress, I recognise that the successful ingredients of reform in one country do not necessarily translate to success in another.

Your markets are profoundly larger than ours, and our cultures of politics and regulation have few similarities.

The approach that is working for us stems from the Australian Government's decision in 1989 to give Australia Post its full trust.

It set the enterprise the task of delivering a high quality mail service while operating commercially.

It undertook not to interfere in the process. Instead it put the principal determinants of success or failure in the hands of Australia Post, its management and its people - with the Board held squarely responsible for satisfactory performance.

In Australia an efficient mail service continues to be essential for social and business communications for all Australians, not least for those in rural and remote areas.

Importantly, the Government has brought a phased approach to reform, recognising that any rapid move to postal deregulation might put at risk the delicate balance between successful commercial and non-commercial objectives

or jeopardise the gains we have made through the participative approach

It recognises that a viable, national postal network must be preserved in the interests of social cohesion and national development, and this has implications for the rate of change and degree of reform that can be applied.

This 'steady-change' formula has been a major contributor to our success.

As we face new challenges - and rising customer expectations driven by our success - complacency is not an option.

Mr Chairman, with this framework of trust, freedom, accountability and measured reform, Australia Post is in a stronger position to face these challenges than at any previous time.

Thank you.



**Australia
Post**

**Postal Reform
in Australia
1975 to 1995**

POST

A Submission to the United States Congress

- Subcommittee on Postal Service, U.S. House of Representatives
- Subcommittee on Post Office and Civil Service, U.S. Senate

January 1996

POSTAL REFORM IN AUSTRALIA 1975 TO 1995

Evidence Provided by

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to the
Subcommittee on Postal Service
U.S. House of Representatives
and the
Subcommittee on
Post Office and Civil Service
U.S. Senate

U.S. CONGRESS
Washington DC

25 January 1996

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FOREWORD

Today, the Postal Service operates in a highly contestable marketplace, in competition with alternative service providers and with substitute products based on advanced telecommunications.

Australia Post is obliged to provide a national letter service. At the same time it derives more than 50% of its revenue from services completely open to competition.

To meet its customers' needs, now and in the future, it is learning to use its two most valuable resources, its people and its network, in a highly efficient and skilled way.

The process of postal reform in Australia has enabled Post, its management and its people, to be the principal determinants of its success.

1. PURPOSE OF DOCUMENT

- 1.1** This paper is presented in response to the invitation extended by the United States Senate and House subcommittees, with jurisdiction over the US Postal Service, for Australia Post's experience to be introduced into the hearing on:

"USPS Reform - the International Experience".

1.2 The paper:

- outlines the course of postal reform in Australia over the past twenty years;
- comments on the main reform measures and their role in achieving good postal performance; and
- provides a basis for further exploration of specific issues during the course of the study of USPS reform, if so desired.

2 AUSTRALIA POST TODAY

- 2.1** Australia Post is a business enterprise wholly owned by the Australian (Commonwealth) Government. It was established as the Australian Postal Commission in 1975, and in 1989, the *Australian Postal Corporation Act* continued the enterprise as the Australian Postal Corporation.
- 2.2** Post operates letter and parcel services within Australia and internationally. Throughout its network of retail outlets it also provides a range of related services, including acting as an agent for other principals such as banks (deposit and withdrawal facilities), utilities, Telstra (the national telecommunications carrier), and the Australian Government, for example in relation to the processing of passport applications.
- 2.3** It is operated commercially, returning a profit, paying all taxes, and providing annual dividends to its owner. Post is subject to the same laws as ordinary commercial corporations.
- 2.4** The enterprise is required to maintain a national letter service, meeting quality and performance standards. This service is to be reasonably accessible to all Australians on an equitable basis. In addition, as part of the letter service, Australia Post is required to price domestic (non bulk) standard letters at a uniform price. As a result of this requirement, a proportion of letter traffic is carried at a price which does not recover its costs. These requirements, together, constitute the legislated social and "community service obligations" (CSO's) of Australia Post.
- 2.5** In recognition of the CSO's, and subject to some exceptions, the domestic letter service is reserved to Australia Post within certain price and weight limits. Where these services have to be delivered at prices which do not recover their cost, there is a CSO cost to Post. Under present government policy, Post must fund this cost by internal cross-subsidy.
- 2.6** Letter prices are subject to review by the Australian Competition and Consumer Commission, under the provisions of the Prices Surveillance Act. The price of basic postage is subject to a price cap of the "CPI - X" type.
- 2.7** Post employs 31600 full-time, and another 4500 part-time and casual staff. It operates a network of 4300 post offices, 3000 of which are licensees or agents, and it handles around 3.8 billion articles per year. Its assets are currently \$2.2 billion, and it has an annual revenue of some \$2.8 billion. For the year ended June 1995, Post reported a profit before tax of \$331.6 million, provided for the payment of a dividend of \$120 million to its owner, the Australian Government, and paid \$254m in taxes and government charges.

3. TWENTY YEARS OF POSTAL REFORM

Pre 1975 - Postmaster General's Department

3.1 Prior to 1975, postal and telecommunications services were provided jointly by the Postmaster General's Department of Government which was widely referred to as the Australian Post Office (APO).

3.2 The performance of the postal service in the 1960's to 1971 had given cause for concern. The Report of the Commission of Inquiry into the Australian Post Office (Vernon-1975) ⁽¹⁾ stated:

"Postal and telecommunications services, which are examined separately (in the report) show widely differing characteristics in respect of capital investment, growth rates, and profitability. In the profit and loss sense, postal services have been a problem area within the APO for a number of years (emphasis added). Consistent losses have largely offset profits derived from the telecommunications services."

3.3 Between 1964/65 and 1974/75, postal operations had been carried out at a loss, every year. The losses range from 5% to 20% of revenue. Over the same period, mail service performance (on time delivery) on an average national basis had fluctuated around 93 per cent. However, performance in New South Wales, the largest State accounting for 35, to 40 per cent of the total had never exceeded 90.5 per cent. Furthermore, for several years, service levels had fluctuated between 75 and 85 per cent. The poor performance in New South Wales had also been accompanied by considerable time lost through industrial disputes.

3.4 The reform which resulted in the creation of Australia Post as a separate, specialised postal entity had its origins in the industry itself. The Vernon Report stated:

"...the unsatisfactory industrial climate at this (Sydney mail) exchange, evidenced by the number of stoppages and black bans, the frequency of meetings between management and staff and the difficulties of making changes in procedures, is unique within the APO service".

"The Commission has no ready solutions to propose. Improvement in the industrial climate at the Sydney exchange will be one of the major tasks for the new management of the postal service as it has been for APO for many years....The achievement of better industrial relations at the Sydney mail exchange appears as one of the major problems which management and the staff organisations will have to pursue assiduously in the public interest of maintaining a reliable and efficient mail service."

(1) Commission of Inquiry into the Australian Post Office 1975. Report. The Government Printer of Australia, Canberra.

1975 - The Australian Postal Commission

- 3.5** The postal enterprise was vested as a separate entity in 1975, the Australian Postal Commission, trading as Australia Post. Its financial objective was to break-even whilst providing not less than 50% of its capital expenditure.
- 3.6** In its first year of operation, 1975-76, volumes fell some 12% as rates were adjusted in order to meet the financial objective. The principal market objective became that of "winning back" business to a revitalised postal organisation intent on meeting customer's needs.
- 3.7** Throughout the late 1970's to mid 1980's postal financial performance was principally on target. This, however, was marred by a climate of management/union conflict and industrial stoppages accompanying the major restructuring of the NSW mail processing network.

1982 - Inquiry into the Letter Monopoly

- 3.8** In 1982, a government-instituted inquiry under the Chairmanship of Mr A E Bradley⁽²⁾ recommended some modifications to the letter monopoly and to the financial arrangements which then existed.
- 3.9** In the event, the only significant change made by the Government in response to that inquiry was the lowering of the hitherto unlimited letter monopoly price barrier (to 10 times the basic postage rate). The main aim was to legalise the activities of private sector couriers which had grown vigorously in numbers and business volumes, unchallenged by law enforcement processes at the time.

1989 Reforms - The Australian Postal Corporation

- 3.10** In contrast to the earlier reform episodes, the driving force in 1989 was national economic policy. The period 1983 to 1986 had been one of relatively unremarkable postal performance: on-time delivery fell significantly in 1984/85 and remained low; days lost through industrial disputation rose significantly; labour productivity had remained subdued overall; and trading performance had continued to be little different from break-even. However, Australia Post did not face strong complaints from the public. The 1989 reforms followed inclusion of Australia Post in "the Government's microeconomic agenda."⁽³⁾
- 3.11** Microeconomic reform in its broadest sense is about making markets work better, improving incentives and enhancing the effectiveness of government operations.

⁽²⁾ Committee of Inquiry into the Monopoly Position of the Australian Postal Commission. 1982. Report. Australian Government Publishing Service. Canberra.

⁽³⁾ Evans, G., 1988. *Reshaping the Transport and Communications Government Business Enterprises*. Statement by the Minister for Transport and Communications, Australian Government Publishing Service, Canberra. pp 2 and 3.

- 3.12** The process involves removing market impediments which discourage or prevent resources being used in the most efficient manner, including restrictions on competition (either domestically or from imports), rigidities in work organisation, or a tax system which distorts incentive. Microeconomic reform is a comprehensive program which involves business and government institutions and processes.
- 3.13** From a national perspective, Australia Post is one of several Australian government business enterprises (GBE's) supplying goods and services. A number of those are assisted by a legislated monopoly. Within the Australian federal system, three levels of government operate, and GBEs are found at the Federal (Commonwealth), State or Local government levels. Under the Australian Constitution, the Commonwealth Government has exclusive power in respect of postal and like services; Australia Post is a Commonwealth GBE.
- 3.14** Since the mid eighties, the Australian Government has made a number of major reforms including: deregulation of financial markets, reduction of tariffs and other forms of protection, introduction of competition in aviation, and telecommunications.
- 3.15** These initiatives are part of the program of **microeconomic reform** aimed at restructuring key industries in the Australian economy and improving its efficiency. The focus of microeconomic reform has been on the structural and institutional factors which inhibit efficient performance. The main changes include corporatisation, abolition of, or reduction in restrictions on competition, and privatisation.
- 3.16** The basic thrust of the 1989 reforms was to improve the efficiency of Post through corporatisation. These reforms had four main elements:
- establishment of new corporate and financial structures;
 - new planning and accountability mechanisms;
 - modification of major strategic controls; and
 - removal of day-to-day controls.
- 3.17** A new relationship was established between Post and the Government. The enterprise was to operate commercially while still meeting defined social objectives. Through a triennial corporate plan, service, efficiency, pricing and profit targets were to be agreed with the Minister, as was the cost of CSO's. These targets are publicly accountable through the annual report.
- 3.18** Post was placed on a fully commercial footing and, in pursuit of *competitive neutrality* objectives, Post became subject to the laws applicable to other corporations, lost its exemption from taxes and was expected to pay dividends on a regular commercial basis.

- 3.19** The 1989 reforms included a number of radical changes. Amongst these were:

3.19.1 *Board of Directors*

Persons with the required commercial skill and experience were appointed to the Board and made accountable for performance. Section 70 of the *Australian Postal Corporation Act* provides for termination of appointment in specified circumstances, including when the performance of the Board or of a particular Director has been unsatisfactory for a significant period of time.

3.19.2 *Executive Appointments and Tenure*

Starting with top management, executives with private sector commercial experience were recruited and employed on contract. Tenure was abolished, and central government restrictions on payment of market rates were removed.

3.19.3 *Clarification of Corporate Objectives*

Social objectives were defined in the legislation and separated from the commercial objectives. Australia Post was required in legislation to operate in accordance with sound commercial practice, achieve a reasonable rate of return on assets, pay all taxes and a reasonable dividend to the government. Periodic revaluation of assets is also mandated. Post was also required to meet legislated "Community Service Obligations" (CSO's) and to comply with specified general government policies notified to it from time to time.

3.19.4 *Corporate Planning Process*

The legislation required Australia Post to prepare three to five year corporate plans. Through the corporate planning process, the Board of Australia Post and the Minister agree on a set of financial, service, and CSO targets over the planning period. The corporate plan which has a three-year time horizon provides the basis for accountability of the Board and top management.

3.19.5 *Government Controls*

Day-to-day controls such as approval of contracts above a specified value, approval of land purchases, or mandatory Parliamentary review of major postal building works were removed. The government also relaxed certain strategic controls, including central coordination of industrial relations matters.

The 1989 reforms reserved for the government strategic controls over Australia Post, but the day-to-day bureaucratic controls exercised by the Government in earlier periods were abandoned.

- 3.20** A major transformation of Post's culture, management and internal processes followed reform. Within the enterprise, more rigorous planning and accountability mechanisms came to govern internal performance. Top management and executive positions were opened to outside appointment, many of which were filled from the private sector.

- 3.21** At the same time as commercial imperatives began to take hold internally, Government oversighting of Post moved from detailed day-to-day controls, to a strategic overview.
- 3.22** Having restructured the enterprise and modified the relationship with the owner, the Government turned its attention to postal market reform, particularly the reserved service.

The 1994 Reforms - The Letter Monopoly ⁽⁴⁾

- 3.23** In December 1993, the Australian Government announced reductions in the legislated monopoly protection provided to Australia Post; these measures were implemented through the *Australian Postal Corporation Amendment Act 1994*. The postal reforms followed a report of the Industry Commission Inquiry completed in October 1992.⁽⁵⁾ The main elements of the reform package were:

3.23.1 *Domestic Letter Monopoly*

The protected letter monopoly prices was reduced from 10 times the basic letter rate to 4 times. Based on the current basic postage rate of 45 cents, the threshold is \$1.80. The weight of protected letters, also, was reduced from 500 gms to 250 gms.

Carriage of letters within document exchanges was deregulated; and the carriage by contractors of an organisation's internal mail is now allowed outside the reserved services.

3.23.2 *International Letter Monopoly*

Outbound international letter traffic was deregulated (but inbound international letters continue to be reserved to Australia Post).

3.23.3 *Downstream Access for Reserved Service (or Interconnection)*

A limited access regime for bulk letters reserved to Australia Post (referred to as "interconnection") is now mandated. Mailers of bulk letters can carry letters to designated mail centres for *delivery intrastate, and benefit from a discount based on average costs avoided by Australia Post through the interconnection.*

- 3.24** The achievements of postal reform are set out in Section 6.

⁽⁴⁾ The letter monopoly is referred to in legislation as a service "reserved" to Australia Post. The terms "monopoly" and "reserved services" are used here interchangeably.

⁽⁵⁾ Industry Commission. 1992. *Mail Courier and Parcel Services*. Report No. 28, Australian Government Publishing Service, Canberra.

4. THE LETTER MONOPOLY

- 4.1** Until 1982, the letter monopoly in Australia had followed somewhat similar lines to the arrangement introduced by Rowland Hill in Britain in 1837. The letter monopoly reserved for Australia Post all letters up to 500 gms in weight except for letters concerned with goods, and carried with those goods and some other minor exceptions.
- 4.2** In 1983, following the report of the Committee of Inquiry Into the Monopoly Position of the Australian Postal Commission (the Bradley Committee, referred to in paragraphs 3.8 and 3.9), the letter monopoly was relaxed to allow *urgent letters* to be carried by other carriers. The legislation exempted from the monopoly letters carried for a fee at least 10 times the ordinary rate for domestic and overseas letters. Letters up to 500 gms in weight generally continued to be protected by the monopoly.
- 4.3** The letter monopoly was reviewed in 1992 by the Industry Commission which recommended that the monopoly be abolished from 1 January 1995; but if immediate abolition was not acceptable then progressive reduction in monopoly protection be effected over five years, at the end of which, remaining monopoly protection be reviewed. In the event, the Government rejected that advice, but decided to make several changes to the regulatory framework including reductions in the levels of monopoly protection (see paragraphs 3.23.1 to 3.23.3). Current legislative provisions as at January 96 regarding the reserved services are summarised in the following sections. A copy of the legislation is at Appendix B.
- 4.4** Section 29 of the *Australian Postal Corporation Act 1989* (the Act), among other things, gives Australia Post the exclusive right to carry letters within Australia, whether the letters originate within or outside Australia.
- 4.5** Outbound international letters are not reserved to Australia Post; however, the delivery in Australia of inbound international letters in the same categories as those reserved if posted from a domestic origin, is reserved to the enterprise.
- 4.6** A letter is defined (section 3 of the Act) as "*any form of written communication that is directed to a particular person or address and includes:*
- *any standard postal article;*
 - *any envelope, packet, parcel, container or wrapper containing such a communication; and*
 - *any unenclosed communication that is directed to a particular person or address."*
- 4.7** But there are several exceptions to the services reserved to Australia Post (section 30 of the Act). The more important exceptions include:

- a letter weighing more than 250 gms;
- a letter within Australia for which the carriage fee is at least 4 times the standard rate of 45 cents;
- a letter carried solely by any electromagnetic or other non physical means;
- the carriage of a letter to an office of Australia Post for delivery under the bulk interconnection service; and
- the carriage of a newspaper, magazine, book, catalogue or leaflet whether or not directed to a particular person or address and whether or not enclosed in any sort of cover.

4.8 Bulk letters under the bulk interconnection service can be lodged at designated mail centres for delivery within the State of destination, at reduced rates.

4.9 The letter monopoly is linked to Australia Post's Community Service Obligations. Under section 27 of the Act, Australia Post is required to maintain a letter service of set characteristics and quality standards. That section further states that the principal purpose of the letter service is to carry letters Australia Post has the exclusive right to carry, and outgoing overseas letters.

5. POST REGULATION - SOME ISSUES

- 5.1** Australia Post is responsible for the operation of the national postal service. It is wholly owned by the Australian (Federal) Government. (No debt is owed to Government - only to private sector lenders). The interface between Australia Post and the government is principally through two Ministers: The Minister for Communications and the Arts is the responsible Minister for postal matters; the Minister for Finance has responsibility for oversight of the Government's investments and assets.
- 5.2** At the enterprise level responsibility for the commercial operation of the enterprise, including achievement of profits and the payment of dividends to the owner, is borne by the Board and Management of Australia Post. The corporate plan is the vehicle for communicating and agreeing with the Government strategies and policies, including those relating to the Community Service Obligations (CSO's), financial, quality of service and other performance targets, and the cost of the CSO's.
- 5.3** Pricing is the responsibility of Australia Post but is subject to a power of "disapproval" available to the Minister *only for the basic postage rate* (the Minister is otherwise unable to issue directions to Australia Post in matters of pricing).
- 5.4** Comments on important regulatory issues relevant to postal services in Australia follow:

Financial Protection

- 5.4.1** **Employee shares:** Current practice in government owned corporations, in effect, prevents the issue of employee shares.
- 5.4.2** **Financial guarantee:** There is no explicit government guarantee on Australia Post's borrowings, although an "implied guarantee" is often believed to exist in financial circles to be available as a last resort.
- 5.4.3** **Government Subsidies:** No **cash subsidies** are paid directly to Australia Post by government for the provision of services to government or to particular groups at prices below cost. (However, the uniform letter rate in Australia entails an internal cross subsidy funded within the postal service).
- A free redirection service is provided to pensioners (revenue forgone). Australia Post sells its services to government departments at market rates (e.g. mail for the blind, Australian Defence Force services).
- 5.4.4** **Pension Liability:** Since 1975, Australia Post has fully funded the cost of all pensions to which its employees are entitled.
- 5.4.5** **Borrowing:** Borrowings by Australia Post have to be approved by government as part of the Loan Council process - the

government requires all borrowings, however, to be raised in the open market, from the private sector.

Financial Independence

- 5.4.6** ***Buying and selling of assets:*** Australia Post is generally free to buy and sell assets on a commercial basis but is subject to government restrictions on heritage property and policy on local industry development.
- 5.4.7** ***Ability to raise capital, incur debt:*** Australia Post cannot raise equity except from the government - it is currently not open to "privatisation". Debt can only be incurred with government approval. Post is free, however, to make investments in accordance with Board powers providing the Minister is duly informed of its intentions.
- 5.4.8** ***Dividends:*** Post is expected to pay dividends to the owner government in accordance with postal legislation and government policy.
- 5.4.9** ***Taxes:*** Australia Post is subject to all Commonwealth, State and Territory laws and pays all taxes.

Independence of Governance

- 5.4.10** Australia Post's staff are appointed by Australia Post. The Board of Directors are appointed by the Governor General on the nomination of the responsible Minister. The Managing Director, who is ex-officio a member of the Board, is appointed by the Board.

Performance Monitoring

- 5.4.11** A quarterly report is provided to the Minister. An annual report, published each year and tabled in Parliament, accounts publicly for performance. An explicit compliance report on Australia Post's Community Service Obligations, included in the Annual Report, is also required.

Public Scrutiny

- 5.4.12** Australia Post is able to protect confidential business information, but Post is subject to Freedom of Information, Ombudsman and Administrative law processes.

Labour Management Practices

- 5.4.13**
- The right to strike - the workforce has the same rights as other workers in Australian businesses.
 - Australia Post is free to negotiate the outsourcing (contracting out) of any of its services or functions. The process is subject to consultations with staff and unions.
 - Currently Australia Post is required to consult with the Department of Industrial Relations in respect of decisions regarding wages and conditions likely to have significant "flow-on" effects for others in the community.

Australia Post's policy is to avoid being a pacesetter on wages and conditions matters.

Market Liberalisation

5.4.14 **Mailboxes:** In Australia, access to the mailbox is not reserved to Australia Post.

5.4.15 **Ability to compete:** There are no specific government initiated measures which prevent Australia Post from integrating backwards or forwards. Australia Post now operates a fulfilment arm, **Sprintpak**, and is a joint owner of **Australian air Express** - an air transport business. However, Australia Post is subject to the Trade Practices Act which deals with competitive conduct and unfair practices.

Commercial Freedoms

5.4.16 **Price:** One price only is subject to Ministerial disapproval - the standard letter rate. Prices of **all reserved services**, however, are subject to price review as part of the government's Competition Policy Reform measures. Australia Post has held its letter prices since January 1992.

5.4.17 **New Products:** Post can and has introduced new products and services (e.g. **EDIPost**: Australia Post's hybrid mail service).

5.4.18 **New Markets:** Australia Post has wide discretion in this regard both within Australia and abroad (wide range of postal related activities) including hybrid, electronic/physical mail. A variety of mechanisms for entry are explicitly available e.g. inhouse, joint venture, acquisition or through any other form of external participation. The Board must notify the Minister of new significant business activities.

6. ACHIEVEMENTS OF REFORM

1975 Reforms

- 6.1** The reforms of 1975 made far reaching structural changes. The first issue was the clear separation of postal services from the affairs of general government by placing postal matters at arms length from the day to day business of government. Second, the mission of the newly created entity was clarified through legislative provision. This greatly facilitated the introduction of the discipline and policies which ultimately led to commercial operation.
- 6.2** The 1975 reforms provided the postal service with a robust structure, a clearer mission, industrial separation from the public service workforce proper, and effective financial disciplines, all of which prepared the foundation for Australia Post's transition to commercial operation.

1989 Reforms

- 6.3** The *Australian Postal Corporation Act 1989* legislated the "corporatisation" of Australia Post. Clearly, these reforms built on the achievements, principles and institutional changes introduced in 1975. The dominant feature of corporatisation was to give Australia Post a commercial charter, albeit in conjunction with parallel non commercial obligations ie Community Service Obligations and specific general government obligations (sections 27 and 28 of the Act).
- 6.4** In the process, Post has achieved high levels of service performance, strong productivity growth and commercially creditable levels of profitability. This has been attended by decreasing real postage prices, sustained mail volume growth and substantial annual dividends paid to the owner, the Australian Government.
- 6.5** "Transparency" in the planning, costing and delivery of CSO's was embedded in the system. Through the corporate planning process, agreement was to be reached between Australia Post and the responsible Minister on the performance target to be met over three years, including the strategies and policies for the delivery of the CSO's and costing them. In return, day to day controls by the government were lifted.
- 6.6** A Board of Directors, selected for their commercial skills and experience, was appointed, executives drawn from the private sector were recruited to top management, and a commercial financial structure put in place.

- 6.7** The regulatory framework, the scope of the letter monopoly and the height of the protective barriers around the reserved services and the role of the regulators were left unaltered.⁶⁹
- 6.8** The 1989 reforms imparted to the enterprise a positive commercial orientation and put further distance between it and the owner government. They strengthened its organisational and financial structures, with a commercial Board and restructured capital in the balance sheet, they opened the door to appointments of executives from the private sector, and redefined the relationship between Australia Post and the Government. Having completed the internal commercialisation of Australia Post, the 1989 reforms cleared the way for future reforms to focus on market regulation and competition.

The 1994 Reforms

- 6.9** These reforms followed the report of the Industry Commission on Mail Courier and Parcel Services of December 1992 which had recommended abolition of the letter monopoly and other radical changes to the market for postal services. That inquiry had been initiated by the Government as part of microreform. It made recommendations for radical changes to market regulation, but in the event, they were adopted only in part.

⁶⁹

Castro Maurice C. 1994. *Deregulation of Australia's Postal Services*, pp 27-40. In *Commercialization of Postal Delivery Services: National and International Perspectives*, Michael A Crew and Paul R. Kleindorfer (ed). Kluwer Academic Publishers. Boston.

7. AUSTRALIA POST'S PERFORMANCE

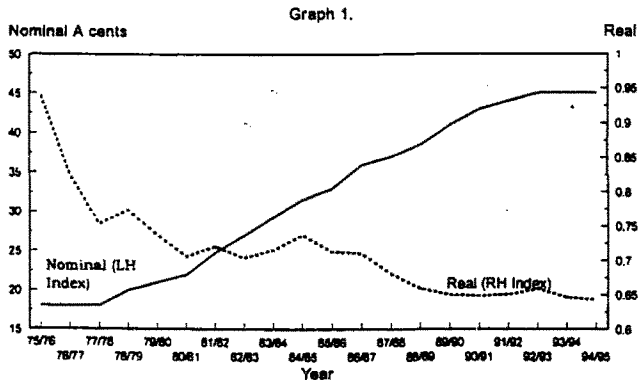
7.1 The performance of Post has shown significant improvement over time, notably so since corporatisation in 1989. This section briefly illustrates the following major aspects of performance.

Price

7.2 Before 1975, the postal service recorded losses for several successive years. In 1975/76, following reform, Australia Post recorded a profit, and only once in subsequent years did it record a deficit. Following 1975/76, and with tight control over costs, the price of basic postage increased significantly less than average community prices.

Graph 1 shows the movements in nominal and real basic postage from 1975/76. A fall of more than one third has occurred since 1975 in the "real" basic postage rate.

Nominal and Real Basic Postage Rate 1975/76 to 1994/95



1- Nominal Basic Postage Rate (NBPR) for a standard letter in Australian (A) cents

2- Real Basic Postage Rate (NBPR deflated by Consumer Price Index)

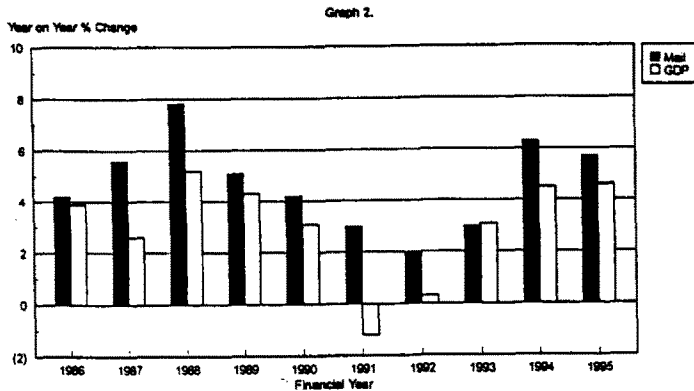
Sources: Australian Bureau of Statistics, Consumer Price Index, Cat. No.6401.0, Various Australia Post publications: Post Charges, MS 11

Mail Volumes and GDP

7.3

Over the years since 1975/76, mail volumes achieved sustained growth, often at rates much higher than economic growth. Graph 2 shows the annual percentage change in mail volumes and GDP from 1985/86 to 1994/95.

Mail Volume and GDP - 1985 to 1995
Year on Year % Change

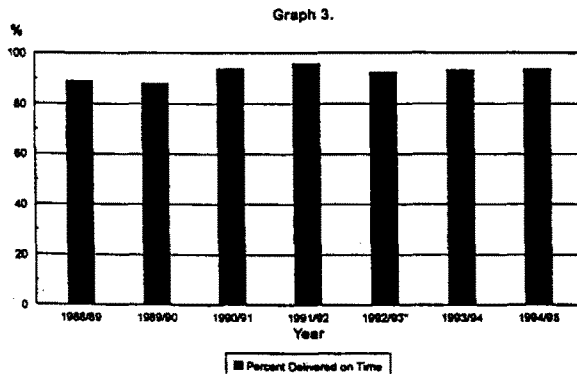


Service Quality

7.4

On time delivery is one of the major indicators of letter service quality. Graph 3 shows on time delivery since 1988. While the measurement of performance was changed in 1992/93 with the introduction of external audit, the results in the table indicate an upward trend in on-time delivery performance over the period.

Delivery Performance 1989 to 1995 - Within Promised Time



Sources: Australia Post, and since March quarter 1993 externally audited performance
*New performance measurement/audit introduced in second half of the year

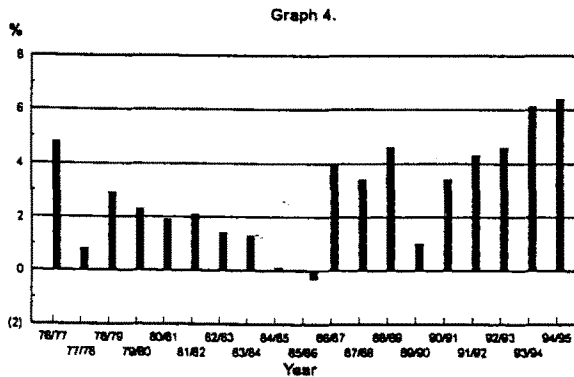
Productivity

7.5

Labour productivity is frequently used as an indicator of efficiency in the delivery of postal services. The postal process is very labour-intensive and labour productivity captures most of the improvements made.

Graph 4 shows annual changes in labour productivity since 1975. Over the period, productivity change has shown consistent, though variable, improvement. Since 1990-91, a significant change in the trend occurred, with the annual rate of change increasing and performance reaching relatively high levels.

Annual Labour Productivity Change %
(Revenue at Constant Prices per Paid Workyear)
1976/77 to 1994/95

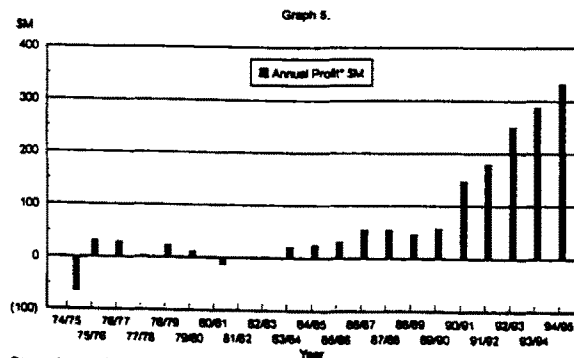


Profitability

7.6

Graph 5 shows Australia Post's profitability since 1975. Profitability trended upwards starting in 1989-90 reflecting the combined outcome of many changes of the reform process.

Corporate Annual Profit 1974/75 to 1994/95

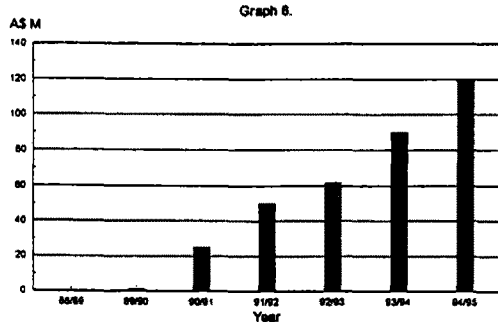


Dividends Paid

7.7

Dividends paid to the Australian Government have increased each year since payments commenced in 1989/90.

Dividends Paid to Government (A\$ M) from 1988 to 1995



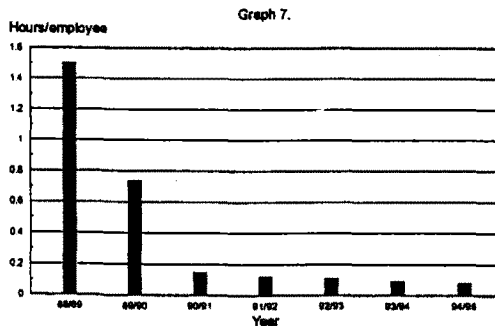
Dividends were not paid to government prior to 1989/90

Time lost through Industrial Disputation

7.8

Graph 7 shows the impact that the changing face of labour relations has had on the incidence of industrial disputes which have led to lost time.

Time Lost Through Industrial Disputes (Hrs per employee)



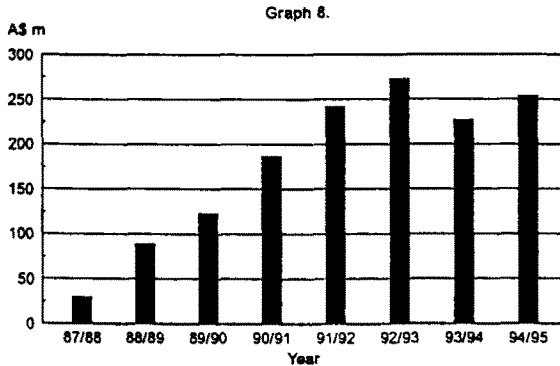
Total Taxes and Government Charges

7.9

Under section 83 of the Postal Services Act 1975, the Australian Postal Commission was exempt from the payment of taxation under any Federal, State or local law. During 1987 - 88 the Commission became subject to fringe benefits tax, sales tax and customs duty. The Commission became subject to State payroll tax from 1 July 1988, other State and local government taxes and charges from 1 July 1989 and corporate income tax from the 1990-91 financial year.

Graph 8 shows the total taxes and government charges paid by Australia Post. In the lead-up to corporatisation, several taxes were introduced progressively to lessen the financial impact of subjecting the postal business to all taxes at one time.

Total Taxes and Government Charges (A\$m)
from 1987 to 1995



Source: Australia Post Annual Reports

7.10

Corporatisation, the product of the 1989 reforms, influenced the achievements of the past five years. Those achievements are reflected in the productivity and profitability of Post, which (before tax) increased sevenfold; the percentage of mail delivered early or on-time, which increased from 88% in 1989 to 93.4% today; the reduction in the real price of its output; and dividends to the Government, which rose to \$120 m in 1994/95 from nil in the first year. Taxes and government charges paid rose dramatically as profits grew, from \$30 m in 1987/88 to \$254 m in 1994/95. Not illustrated in the graphs but fact, nevertheless, is that in recent years Australia Post has repaid \$375 m of capital to Government (of a \$450 m four-year capital repayment programme) and has continued to meet its social obligations as required in its enabling legislation.

8. AUSTRALIA POST'S LABOUR RELATIONS

- 8.1 Corporatisation was both a development milestone and catalyst for many aspects of change at Australia Post including labour relations.
- 8.2 The aim of reform was to improve Australia Post's efficiency; and in such a labour-intensive enterprise, labour relations would naturally command a great deal of attention.
- 8.3 During the mid-1980's, Australia Post went through a period of escalating workplace unrest due in part to an autocratic 'top down' style of management. Local disputes were frequent and labour relations took on an adversarial character. This culminated in the industrial turmoil of the second half of the 1980's.
- 8.4 In the run up to corporatisation, it was realised that as a customer service organisation, **Australia Post relies critically on the motivation and commitment of front-line employees for its business success and competitive advantage.** Several key factors were then identified. These included: workplace and job design; the latitude in decision-making given to employees; rewards and recognition; the adequacy of the services provided to customers; and the standard of equipment available to employees to provide the service.
- 8.5 At the time it was also established that existing processes did not result in constructive labour relations; for example, the dispute resolution processes encouraged abdication of responsibility for solving problems where they occurred, instead of encouraging local management to resolve them. This worked against acceptance of management-mediated solutions. These were regarded as externally imposed, and often not accepted in the workplace.
- 8.6 A 'Joint Statement of Understanding' setting out the process to guide future relations was signed by Australia Post's management and its unions in 1989. The Agreement set the object of establishing Australia Post's reputation for reliability and efficiency in providing customer service and outlined six principles ;and processes of participative management. The Agreement has been closely adhered to. These principles now guide the process of renewal and redevelopment and the on-going relationships between the key players in the business - people, unions, management.
- 8.7 The first step afterwards was to provide opportunities for much greater involvement in the business by employees. This was effected through *Industrial Participation*. *Industrial Participation* has become Australia Post's human resource management philosophy, built around a process of employee involvement in work centre decisions, and placing emphasis on employee's accountability.

- 8.8** *Industrial Participation* has strongly motivated employees. It has broadened their perspective, created more interesting jobs, and given people greater involvement in the business. Since 1989, there has been a dramatic fall in disputes and today they are at a negligible level.
- 8.9** The jobs of most senior managers were declared vacant and were recontested in a thoroughly open field. These positions no longer carry security of tenure; they are filled under contractual arrangement, and they provide for rates of remuneration based on current market prices.
- 8.10** Employee remuneration is now set under Enterprise Agreements which relate expected performance much more closely to rates of remuneration. Australia Post's Enterprise Agreement is widely recognised as a leading edge example of enterprise bargaining and includes provision for:
- union rationalisation
 - quality measurement
 - provision for workplace flexibility; and
 - a commitment to achieving world best practice.
- 8.11** Recognition is also extended to employees in other forms; for example, bonuses for achieving 'quality accreditation' and for meeting productivity targets. These programs are designed to foster a quality culture and provide for tangible recognition where a desired outcome is achieved.
- 8.12** Australia Post's labour experience is setting standards in workplace reform and is emerging as a model for successful change. Its distinguishing features are consultation rather than confrontation; mutual respect rather than mutual mistrust; and incentives for performance, rather than sanctions for poor performance. The successful vehicle for the change has been worker participation.

9. FUTURE POSTAL REFORM

Background

- 9.1 The past twenty years have seen several waves of postal reform in Australia; and it is fair to say that reform has been generally successful. As an enterprise, Australia Post has improved its performance markedly following the changes made to its status, structure, and its relationship with the government in the dual capacity of sole owner and regulator. Furthermore, from a public policy point of view, the social objectives set by the Government have been consistently met, and the retention of national assets in the postal enterprise has been well justified.
- 9.2 While the drivers of postal reform in the 1970's were industry specific, since the late 1980's, postal reform has been part of a national all-industries strategy. Increasingly, therefore, developments in the postal area are being affected by, as well as influencing, reform in other Australian industries.
- 9.3 Government statements and the continuing imperative to improve Australia's international competitiveness indicate strong pressure for change will continue to be felt in all service areas including postal services.

Further Review of the Letter Monopoly

- 9.4 A review of the remaining limits to competition is to be undertaken in 1996-97.

In announcing the Government's 1994 postal reform decisions, the Minister for Communications stated,

"The Government has agreed to proposals for a sensible managed approach to the introduction of further competition for Australia Post...The initial impetus for Australia Post to lift its business performance was given in 1989 when the Government corporatised Australia Post and put in place a commercial charter and board. Australia Post is already the model of government business enterprise reforming itself. Productivity gains, higher staff morale and strong profits have been the result."

"The Review should examine the future arrangements for Australia Post. The Review's terms of reference should be consistent with the Government's determinations on the findings of the National Competition Policy Review. Including its policies on a declared access regime, monopoly pricing, competitive neutrality and regulatory restrictions on competition."

This is consistent with the Government's view that a public monopoly must justify the continuation of its monopoly position."

- 9.5** It seems likely, therefore, that the 1996-97 review will examine the implications of the Industry Commission's proposition that reserved services protection is necessary to ensure the uniform charge for standard letters continues and is funded by cross subsidy from low cost to high cost mail paths.
- 9.6** The extent of monopoly protection may be reconsidered in terms of the weight and price at which competition will be allowed. As well, the scope of the monopoly may be examined in terms of the types of communications to be excluded from the reserved services.

Principles

- 9.7** Future Postal Regulation will be developed in conformity with the Australian Government's National Competition Reform legislation and policies introduced in 1995. Under this general umbrella the National Competition Reform Principles Agreement envisages that legislated restrictions on competition would be removed unless it can be demonstrated that the benefits of such restrictions to the community as a whole outweigh the costs, and that the objectives of the legislation can only be achieved by restricting competition. They further provide that such legislation would be systematically reviewed at least once every ten years, by an appropriate independent body.

Present Government views on the postal service

- 9.8** On behalf of the Labor Government, the then Minister of Communications stated in December 1993 when the last set of reforms were announced that the aims were:
- to safeguard the basic letter service and the uniform postage rate (both of which are currently provided by Australia Post under a legislated community service obligation);
 - to encourage price and service competition in value added services; and
 - to encourage Australia Post to continue to operate at world best practice; and as a 100 per cent publicly owned corporation.

The Minister also stated that the government had rejected the Industry Commission's radical proposals because they might have "destroyed Australia Post's viability", and not ensured continued delivery of the community service obligations. He added, the Industry Commission's failure to estimate with confidence the quantum of monopoly protection necessary to ensure the viability of Australia Post while community service obligations continue to be internally funded was a major reason for the decision of the government to take a moderate first step in 1994 and to review competitive arrangements in 1996-97.

The Hon. Michael Lee, the present Minister for Communications and the Arts stated, in October 1994, when comparing postal reforms to other sectors of industry affected by microreforms:

"We need make no apology for approaching the reform of this industry sector (ie the postal industry) on a responsible and progressive basis. Unlike other industry sectors, we are starting from an internationally competitive base - not playing "catch-up". While that is not grounds for complacency, it argues against a radical pace of reform that might destabilise the necessary balance between commercial objectives and social objectives that makes Australia Post a unique institution in Australian society - much more than just another business enterprise."

10. CONCLUDING COMMENTS

10.1 Australia Post's reform is an outstanding success story - one which is internationally recognised. The indications of performance, all point to financial success.

10.2 The key issues leading to the improved performance include:

- *the "arm's length" relationship between the Corporation and the Australian Government;*
- *the establishment of a healthy working relationship between the Corporation's management, staff and their unions;*
- *light-handed regulation; and*
- *Australia Post's commercial freedom, enabling the introduction of new services to meet customers' needs.*

10.3 From our experience, four fundamental steps have established the framework for successful and profitable postal service:

- *the clear definition of the postal service mission;*
- *the introduction of incentives into the framework to ensure achievement of high financial and operational performance;*
- *the acquisition of new resources and skills; and*
- *a shift from an inward looking operational focus to that of "the customer", focussing on performance, accountability, meeting customer needs and customer satisfaction.*

10.4 Today, Australia Post is equipped to meet the challenges of our dynamic and contestable market place.

**Mr. Georges C. Clermont
President and CEO
Canada Post Corporation**

Good morning, ladies and gentlemen. I take great pleasure in appearing before you today to discuss some of the complex issues facing postal administrations. These are very challenging times indeed for those of us charged with running a twenty-first century postal service.

Some would have you believe that national postal services are dinosaurs, relics of a bygone age. They will tell you that there will be no need for us in the years ahead. They will lead you to believe that today, communication is done by fax, by electronic mail, or through the Internet, not through old fashioned postal services. Get rid of the dinosaurs, will they say, or, at most, let them deliver a few letters from grandma and uncle Harvey.

They will bury you with statistics to demonstrate the growth of other communication media: E-Mail has grown by 100%, business to business mail has fallen by 20 or 25%. etc.

To come to this kind of forum to defend the postal world makes us look like Don Quichote. But did our predecessors not go through the same debates in the late 19th century when communications by telephone were growing by leaps and bounds, set to replace mail as a communication medium?

Postal administrations are not thought of as showplaces for modern technology; our image is one of armies of people wearing green shades and black armbands, sorting letters one by one. The fact that a lot of very high tech equipment was designed and manufactured to allow us to process 30,000 letters an hour does not enter the public's mind.

We have built in Ottawa a state of the art Control Centre that has more of a NASA image than that of a post office. The centre is our most important tool to manage the postal system from a central point -- it allows us to monitor every monotoner of mail, every aircraft or truck carrying these monotoners, the conditions of every major highway, every single piece of mail which the customer has paid for tracking -- but it has also become our most important marketing tool; we bring hundreds of customers through this centre and a customer that's gone through this centre will never doubt our ability to serve.

This, of course is a far cry from the perception that our competition wants to create in the public's mind. Let's recognize that they have a vested interest in making us look irrelevant.

Mr. Runyon could perhaps test the relevancy of the US postal service by announcing tomorrow that he's decided to deliver mail 3 days a week and close all post offices that serve less than 25,000 customers. Your phones and your in-basket would measure the relevancy of the postal system.

We are not blind to the changes around us. We are not for a minute advocating the status quo but we know that we are filling a very real need.

People like mail. It is personal. Someone took the trouble to write to you. It is delivered by a real person. It is tangible. You open it, you read it, you respond to it. It is private and it is secure. People everywhere order huge quantities of products delivered through the mail. Why can one find that the Company delivering your parcel fulfills your needs and not the Post Office?

Postal administrations are mandated to serve the whole country, however remote the area. It is one of those intangible things that forms a nation. No one can claim the same coverage. It is indeed a weighty obligation that we have and our challenge is to turn it into a useful marketing feature. Last summer, here in Washington I had the pleasure to hear Senator Stevens refer to the thousands of communities whose only tie to the main centres of the nation is the postal system. Ask those living in these communities how relevant the Post office is.

But Postal services are no different than other corporations or organizations: to survive they have to be relevant.

Let me tell you, if I may, some of the things we have done and are doing in Canada Post to remain relevant.

In 1981, the Post Office became what we refer to as a Crown Corporation. A Crown Corporation is a creature of statute, subject for the most part to the provisions of the Canada Business Corporations Act, and to all other laws of the land, including the anti-trust legislation. There are Crown Corporations that have a purely social mandate and some that have a mixed social and commercial mandate. The latter must be run as a business, but it is entirely owned by the Government of Canada.

There were a number of reasons for the Government to move the Post Office Department in that direction, chief amongst them the political and bureaucratic interference in the day to day management, the elimination of deficits that ran into the hundreds of millions of dollars in some years, and to eliminate labour strife, which had become so commonplace that Canadians had lost confidence in the postal system. I believe these parallel the conditions that a number of postal administrations have found themselves in at one time or another.

As a first step, we concentrated on operational improvements, because we had to give people a reason to believe in the system. It was important, first and foremost, to show Canadians that their postal system could do the job and give them good service. Having set standards of service, we had our performance measured by an independent auditing firm - we were the first to do so - and this allowed us to measure our progress, quarter by quarter, year by year. This became one of the key determinants for incentive awards to our salaried employees. We know that we are doing better now than ten years ago, for example, as on-time delivery has gone from 85% to 97-98%.

Having had a good shot at fixing the operation, constraining costs and establishing a sound network of retail outlets, distributed between corporate outlets and franchised outlets, we turned our effort to our customers.

When you've been a monopoly for well over 100 years, it is very difficult to instill a customer-driven culture. To change the culture is our current challenge; a more difficult task perhaps than those we undertook during the first phase. We are now dealing with attitudes and the human mind. When properly trained and motivated, postal employees are as productive as any.

While our workforce has a right to strike, it knows and we know that after a week or ten days, the Government will force them back to work and impose arbitration. We do not have an equilibrium of forces in the area of industrial relations. They also know that they have contractually obtained job security and that the Post office is not about to disappear. A normal corporation has a choice of shutting down an operation: we don't have that choice, and it is evident in our workforce's behaviour.

But we have spent a lot of time and money on our human resources; we have tripled our training budget two years ago and have funded the Canada Post Learning Institute, a virtual university through which all our training is executed. This training can go from product knowledge to forklift operation through advanced management courses in our universities. Two faculties of management, Queen's University in Ontario and Ecole des Hautes Etudes Commerciales at the University of Montreal work with us at developing curriculae or special courses. For instance, by the end of this year, we will have every one of our employees through a 2 or 4 day course called "Service Plus", a basic course in understanding who is a customer and the choices that he or she has.

Today, I can say that we have restored customer confidence in our postal system; we have started measuring customer satisfaction index through an outside firm, of course, and improvement on this index, quarter by quarter, year by year, will become part of goals, just like we did for service performance, several years ago. When dealing with such a large workforce, the goals must be simple and clear and measurable. We will set targets for customer satisfaction in increments of 2 or 4% points every year. Nobody can pretend to not participate.

Participation by all is a prerequisite for a successful turnaround. There is no substitute for a workforce that is proud of the Corporation that it works for. In the early stages of the Corporation, our employees, when asked who they worked for, mumbled "the government", so bad was the Post Office department. Today, I can say that our people are proud to work for a well regarded institution and to wear its uniform.

Our success has allowed us to regain market share in most of our product lines. This progress has caused considerable unrest amongst our competitors. As can be expected, cries of cross-subsidization soon reverberated. These allegations have been repeated for the last five years and have been dismissed every time, the last time by the Bureau of Competition, when it approved our acquisition of a 75% interest in Purolator Courier Ltd, the largest courier service in Canada.

Financially, we have not been as successful as we would have liked: we have sought no government funding since 1986 and we have had some years of good profits and some of losses. Our current mandate is to earn a return that is commensurate with that earned by firms of similar size, facing similar risks. Today, we would set that at 10 - 12%.

Our competitors would like to see us subjected to some form of regulatory regime as is the USPS. The Government has so far resisted that, for good reason, it seems. The basic letter rate is the only one that is not subject to market forces; it is set by Cabinet. Our Corporation is subject to all laws of the land, including the Competition Act - equivalent to your anti trust legislation - which is the perfect remedy for "keeping us honest". There is no need to force us into a straight jacket which in the end only benefits our competitors.

Our government has just appointed a commissioner to review our mandate. Its terms of reference are broad; chief amongst them are the maintenance of some form of "exclusive privilege" - our form of monopoly which gives us the exclusive privilege, subject to 2 pages of exceptions, to deliver letters weighing less than 500 grams - and our role in the future electronic information transfer media.

Part of the review will also focus on a clearer definition and cost of our social function. As I stated in the beginning, our corporation has a mix of a social and commercial mandate. Its social mandate is essentially the universality of the service and the single price for a basic letter. We like to look at those social obligations as a marketing asset. It allows us to put everything we do in a very single focus; we "stick to our knitting". Censoring mail, for instance is not ours to do. Law enforcement agencies are there for this. Free mailing for elected representatives is government policy: not ours. We get paid for it. Most of our "non-core" operations are contracted out: we do no long distance transportation, surface or air; we found out that our information technology staff tended to re-invent what was already out in the market: we have outsourced all of this function which frees up capital for processing equipment; the same with our property management function - we are not managers of real estate - and this resulted in huge savings.

By concentrating on our core business, by focusing on our business like any other corporation, we believe that we can play the game on a level field with our private sector competitors.

Playing on a level field means:

- meeting the needs of the customers, citizens, businesses, etc.
- evolving with technology
- paying taxes and dividends to your shareholder, whoever he may be.
- achieving the commercial freedom that is required to measure up to our goals.

Given these rules, let the market place decide who should be in the game and who is best.

New Zealand Post



Testimony

of

ELMAR TOIME

**Chief Executive Officer
New Zealand Post Limited**

Before the Joint Hearing of

The Subcommittee on Post Office and Civil Service

and

The Subcommittee on Postal Services

of the

United States Congress

USPS REFORM - THE INTERNATIONAL EXPERIENCE

25 January 1996



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Senator Ted Stevens
Chairman
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Congressman John McHugh
Chairman
Subcommittee on Postal Service

Members of the Subcommittees

My name is Elmar Toime and I am the Chief Executive of New Zealand Post Limited, a company incorporated in New Zealand and fully owned by the New Zealand Government. New Zealand Post is responsible for the provision of postal services in New Zealand.

Consider the following facts about New Zealand Post:

- ☒ In November 1994 we were nominated as New Zealand's *Company of the Year*.
- ☒ In October 1995 we *dropped* the price of postage for a first class standard letter from 45 cents to 40 cents (US26 cents).
- ☒ In the eight years 1987-95, the *real price* of letter postage has fallen by almost 30%.
- ☒ For our last financial year ended March 1995 we posted a *record profit* after tax of \$72.4 million (US\$47 million) on a turnover of \$644 million (US\$420 million).
- ☒ We have been *profitable* for the eight years since being corporatised in April 1987; we made losses before then.
- ☒ Our key *ratios* are:

Profit after tax to shareholder funds:	32.1% (24.1% five year average)
Profit before interest and tax to turnover:	17.3%
Profit before interest and tax to assets:	25.3%

New Zealand Post is a successful business under any measure. It is my conviction that the same results can be obtained for the United States Postal Service. In the material that follows I have given my views on how I see this may be achieved and I have summarised the measures and reasons for the success of New Zealand Post.

Yours Sincerely

Elmar Toime

New Zealand Post



ATTACHMENT 1

Reform of the USPS

Role of Government

The New Zealand experience suggests that the correct environment must be provided for managers to perform. The Board of Governors and the management team must be given control of as many of the levers as possible to run the business. At the same time a commercial discipline is needed. This means that market forces must be allowed to operate in as close a proxy to the real market as may be possible, given other objectives of Government.

In other words, Government is responsible for the operating environment *and* the social policy contract. Once that is defined, the Post should be allowed to run like any other business. It will have:

- responsibilities to its owners (the government on behalf of the people of the United States);
- responsibilities to social infrastructure (the universal service mandate dictated by Congress);
- responsibilities to its customers (efficient service); and
- responsibilities to its employees (the fair employer requirement)

Reform must discover the optimum formula to best achieve these multiple objectives. The State Owned Enterprise model pioneered in New Zealand has achieved this.

Conservative change

In dealing with a complex business with a long and valued heritage, both in the minds of the public and in the people who work for the USPS, reform may be daunting. The desired end objective of all stakeholders cannot be achieved except over time. The natural conservatism of the public, customers, and employees and no doubt even many managers, will mitigate against rapid change.

Changing the behaviours and attitudes of people does take time. In thinking about the USPS and reflecting on my own experiences in the turnaround of New Zealand Post, I have proposed below a programme of change which I believe allows commercial goals to be set while still keeping an equilibrium of sorts among the diverse stakeholders and self-interested parties

The following structure provides my view of how this can be achieved in the United States.

Summary Overview of Change Programme

1 Separate Regulatory and Ownership Powers in Government

1.1 Ownership is concerned with:

- 1.1.1 business performance (including value creation and profitability)
- 1.1.2 business scope and investment policies
- 1.1.3 dividend and capital structure.

- 1.2 Regulation is concerned with:
 - 1.2.1 social policy requirements
 - 1.2.2 market behaviours
 - 1.2.3 monopoly provisions (letterbox monopoly and universal service)
 - 1.2.4 pricing controls
 - 1.2.5 antitrust behaviour.
- 2 **Establish a Commercial Company Structure**
 - 2.1 Accept Government ownership.
 - 2.2 Board of Directors appointed for commercial skills (not political and geographical balance).
 - 2.3 All operational and commercial decisions within the social obligations framework to be the responsibility of the Board.
 - 2.4 Performance targets reported to Congress.
 - 2.5 Commercial Balance Sheet established which will allow the USPS to trade in its first year (the Government to assume major liabilities if they exist by way of loan, to ensure a sound capital structure).
 - 2.6 Free cash flow dividend policy, in the context of an agreed Business Plan.
- 3 **Establish Monopoly and Regulatory Controls.**
 - 3.1 Maintain the universal service obligations and universal price for the standard letter.
 - 3.2 Continue to protect the standard letter as a reserved service.
 - 3.3 Maintain the sanctity of the mail by preserving the letterbox monopoly.
 - 3.4 Regulate the price of the first class letter at an agreed price for 5 years.
 - 3.5 All other mail services, including volume discounting, to be commercially priced by the business itself.

Offer of Assistance

The foregoing points summarise the New Zealand Post view on a realistic and workable reform package. The discipline of commercial behaviour, allowing the Board and management to control as many of the levers of performance as is possible, will achieve the necessary results of optimal performance.

I would be pleased to elaborate on these points at the hearing or by separate commission.

New Zealand Post has both the strategic and operational achievements to believe it has the ability to assist both Congress and the USPS itself meet its reform targets.

ATTACHMENT 2

Addressing the Future
Creating Benefits for all New Zealanders



New Zealand Post Limited

Presentation : Elmar Toime
CEO
New Zealand Post

The following presentation summarises the record of New Zealand Post since corporatisation and presents its operating principles and reasons for success.

New Zealand Post is presently engaged in helping many other postal businesses around the world achieve similar results.

Contents

- ⇒ Overview
- ⇒ Measures of Success
- ⇒ Delivering the Future
- ⇒ Keys to our Success



These are the key headings of this presentation.

New Zealand Post Limited

- Created from the Post Office which was divided into three separate businesses: Post, Telecom, PostBank.
- New Zealand Post is a limited liability company.
- Clear separation of the powers of the Board (commercial) and powers of the Government (shareholder rights and public policy).
- Its shares are held by the Minister of Finance and the Minister for State Owned Enterprises.
- The State Owned Enterprises Act controls the public accountability requirements.
- The Postal Services Act controls the regulatory environment.



This summarises the structure of NZP.

For all intents and purposes, we operate like any other private company. There is a requirement by law that we operate as a successful commercial company. We pay taxes exactly like any other business. Our postage attracts the general value added tax of 12.5%. Our loans are not guaranteed by the Government.

The Post Office in 1986/87

New Zealand Post Limited took over a postal operation in 1987 that was:

- ⇒ Incurring major losses (\$40 M in its last year).
- ⇒ Overstaffed and burdened with a large fixed cost structure.
- ⇒ Operating inadequate mail processing facilities.
- ⇒ Lacking financial and management systems.
- ⇒ Needing substantial capital investment.
- ⇒ Deteriorating service standards and not meeting customer needs.



Before corporatisation, NZP was a poor operation. It lost money, little had been invested, there was little technology employed, and many of its managers had become administrators. People were demoralised and lacked commercial incentive.

The real losers were the public of New Zealand. They received deteriorating service and subsidised an inefficient operation.

Business Performance

Since corporatisation in 1987, New Zealand Post now operates in 1995:

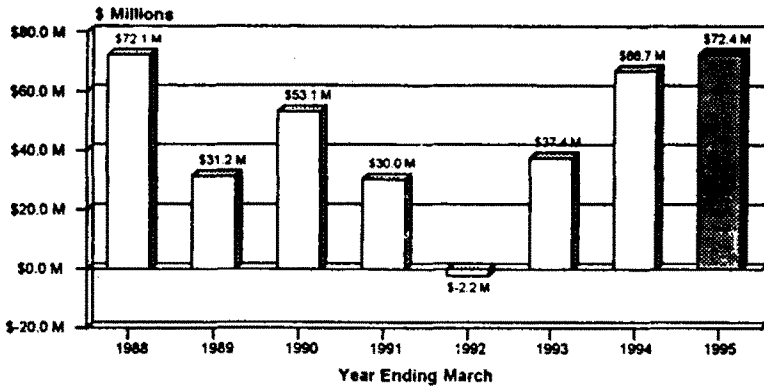
- With 30% more mail to deliver:
 - ... real unit costs 30% less.
 - ... labour productivity up by over 100%.
 - ... at a 97% plus on-time service performance.
- New products and services meeting market needs.
- Modern plant, transport and equipment funded from within the business.
- Paid dividends and taxes of \$445 M.
- Satisfied and involved labour force



Success was achieved over the entire eight years of our life as a corporate entity. We were completely self-funding. The Government received handsome dividends, the public a first rate postal service.

The next few charts record the *key measures of success* as we see them.

Profit after Tax

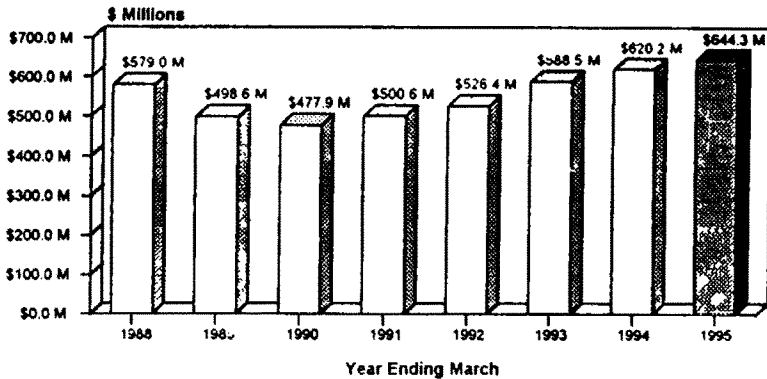


The year before corporatisation recorded a NZ\$40 million *loss* for the postal business. This was turned around in year 1.

In 1988 a subsidy of about NZ\$19 million was paid to keep small rural Post Offices open. This subsidy was withdrawn the following year. There are no subsidies paid to NZ Post.

The loss in 1992 was due to abnormals, including property value writedowns, severance payments to workers made redundant due to restructuring, and expensing a major computer system investment. Normal operating profits were about \$40 million.

Revenue



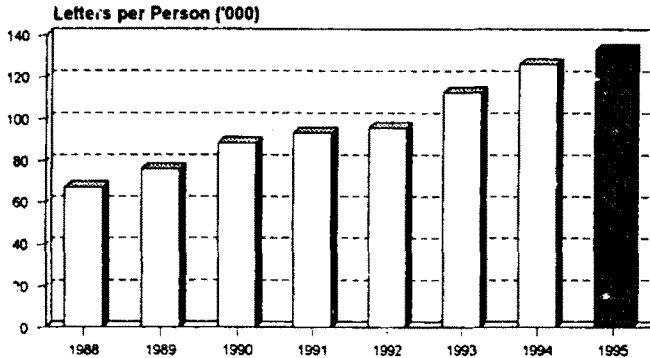
Turnover fell initially as we lost income from banking (formerly conducted at Post Offices, but withdrawn by the now independent and privatised PostBank).

New turnover growth has come from a new courier service, new mail products and services, merchandising sales in Post Shops, agency payment services, and new ventures.

NZ Post is able to acquire and divest businesses and companies to meet core business opportunities.

NZ Post ranks 27th by turnover in New Zealand (and 13th by profit after tax).

Productivity

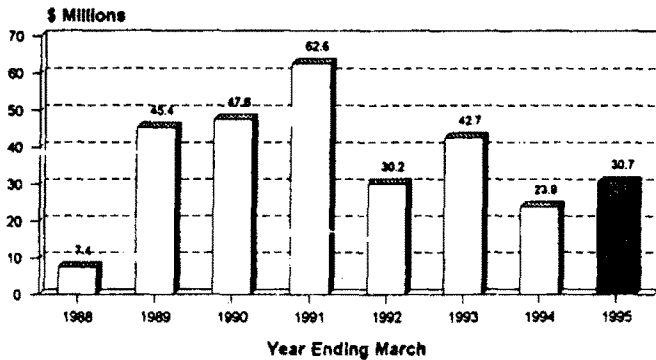


This is a broad measure of labour productivity. The chart shows letters handled per Post employee per annum.

Total factor productivity shows similar trends. Value based management measures also record significant value creation by the business.

The inverse of this chart is the fall in number of employees employed. It is true that we have 40% fewer people (measured by full time equivalents). Because the key workload falls in the evenings and mornings, we now have a large part-time workforce. We have also outsourced or contracted out some of our activities.

Capital Expenditure

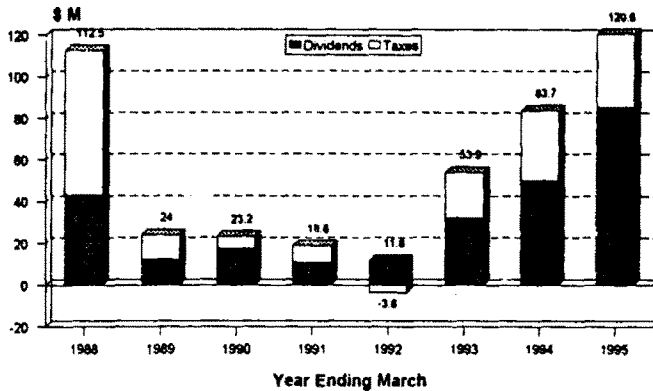


Our capital expenditure has been sourced from retained earnings, sale of surplus assets, or borrowings. We have completely modernised our business - state of the art technology, in-house transport network (including a small air fleet), modern post office premises, computerised.

However, we are exceptionally rigorous in project evaluation to justify capital investment. We take the benefits of management reform before we apply benefits to capital investment projects.

Our investment in subsidiary businesses is included here also.

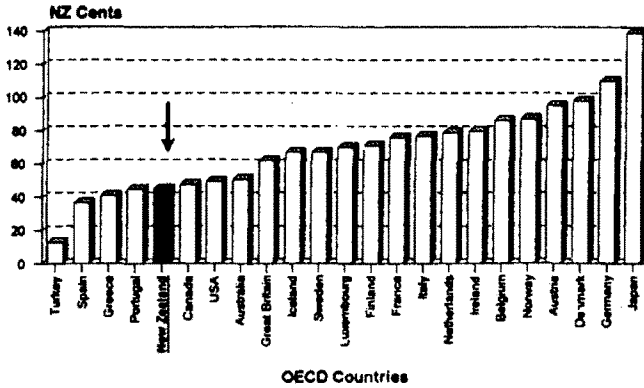
Payments to Government



We have paid substantial dividends to Government (over 70% of profits after tax) as well as corporate tax.

Next year we intend to take on more debt to closer match private companies debt structures. This will allow a capital repayment to be made to Government, our second such restructure.

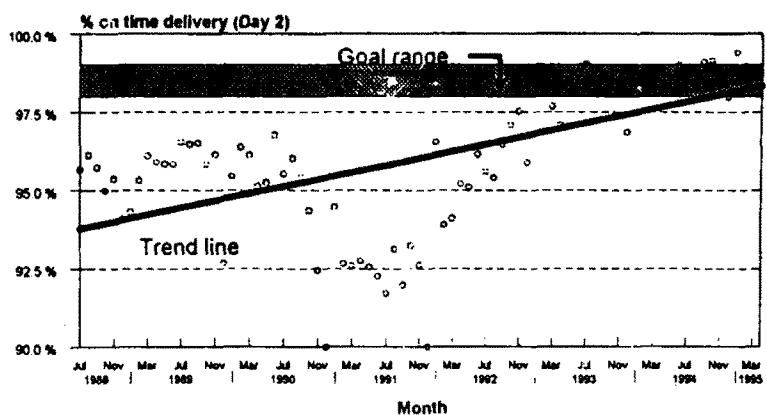
International Letter Prices as at 31 March 1995



This chart shows relative prices (in NZ cents) for first class letter postage. It was prepared before we reduced the price of postage from 45 to 40 cents.

NZ Post has therefore achieved its profitability not through pricing.

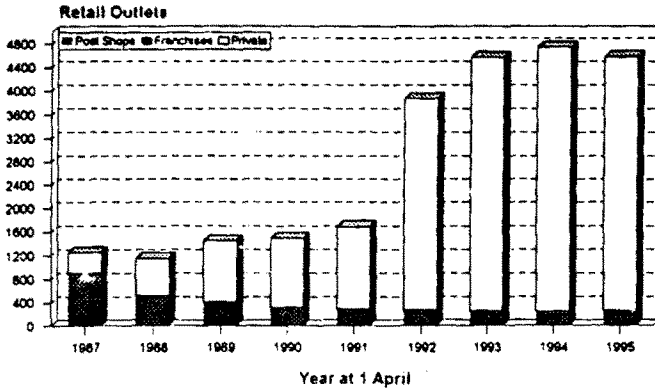
Standard Post Performance



Further, on time performance has continued to improve. We measure performance internally daily, and report the results of independent measures of service performance in our Annual Report.



Retail Network

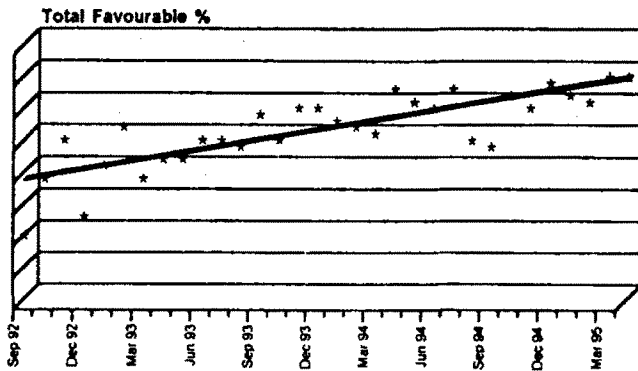


In 1988 we abolished the term “post office” and replaced it with Post Shop. This characterises the commercial attitude we have developed in the business.

Post Shops sell stamps, accept mail, parcels and courier express items, accept payments for a wide variety of financial transactions (for example you may renew vehicle registration or pay road user taxes at a Post Shop). We also sell a range of stationery and related merchandise.

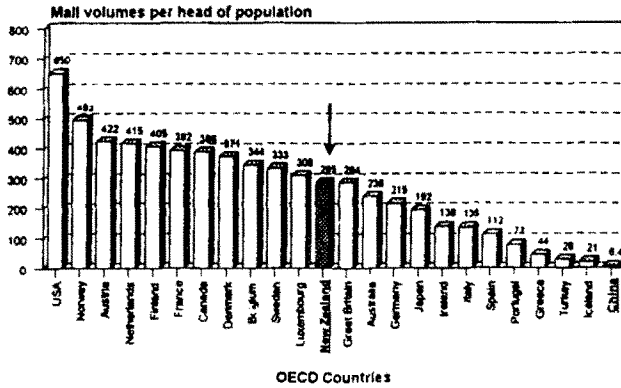
in 1992 we made stamps available to any approved retailer, with a sales commission of 5%. We are now introducing franchises - we have a formal franchise programme and in the last year have begun to increase once again the number of “full service” Post Shops as franchises.

Favourability



We have an external and independent research house measure the public perception of NZ Post monthly. We are now the highest rated utility.

Per capita mail volumes



Mail volumes in NZ are not particularly high. This chart gives us cause for optimism. Our growth has been around 5% per annum for four years. This year will be our highest growth, at nearly 6%.

Good service and cheap prices are the best causes of growth.

Our Social Obligations

- Universal price-equalised service
- Price control on standard letter
- Six day delivery
- Minimum number of retail outlets
- Free rural delivery



We have a contract with Government, called the Deed of Understanding, in which we accept these social obligations. As a state owned enterprise, we must also fulfill our obligations as a key infrastructure service.

The reference to free delivery service is a situation unique to NZ. For 70 years rural customers were required to pay a small fee to have mail delivered. This fee was abolished by NZ Post in April 1995 as part of our continuing to return the benefits of our efficiency gains to our customers.

Business Vision

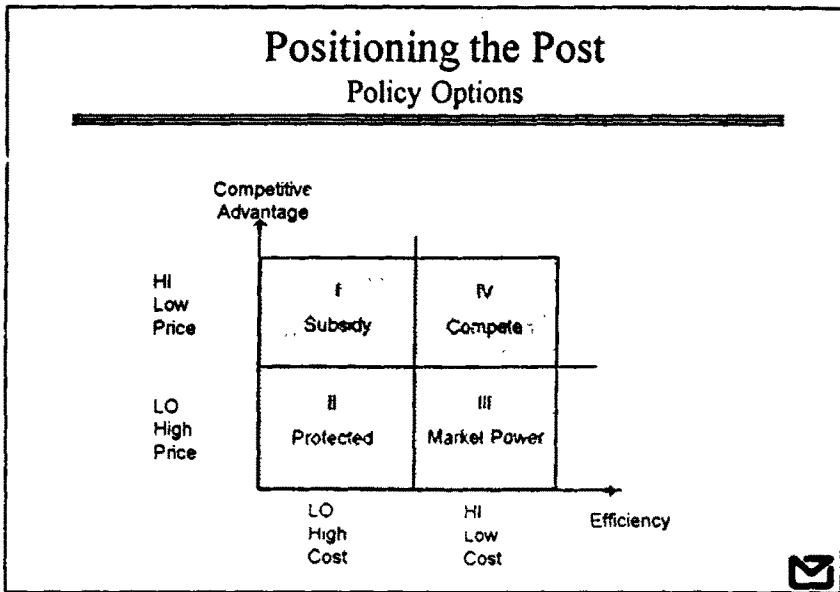
*Our vision is to be recognised by
New Zealanders as the best company in
New Zealand.*

- Sustained Profitability.
- Care for New Zealand by meeting defined Social Obligations.
- Investment which adds Shareholder Value.
- Valuing our People.
- Reliable, efficient services at lowest Cost and Price.



I have established a vision inside NZ Post to target and provide direction to people. This vision is accompanied by a set of five business principles to guide decision making.

The last one is market positioning statement, illustrated in the next chart.



NZ Post targets the 4th quadrant "Compete". We want to be competitors, winning customers because we are good, not because we have a monopoly. It takes many years to reach that positioning.

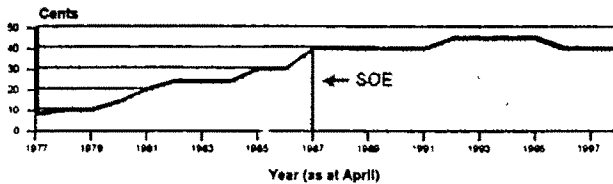
The US Government must set a target for the USPS. Low price and high efficiency (meaning on time service and low unit costs). How to achieve this is of course the issue.

A Major Price Initiative

New Zealand Post reduced the price of the medium-sized standard letter from 45 cents to 40 cents () including GST on 2 October 1995.*

*1.5 minutes of average hourly wages

Standard Letter
Nominal Price



This is the price record for the first class letter in NZ. Remember, the price includes 12.5% GST (Goods and Services Tax or VAT).

Prices are set by NZ Post. This is independent of Government. The Company does have, however, a price ceiling against changes in the Consumer Price Index.

On 2 October 1995 we reduced the price of postage for the standard letter. This means postage is now almost **30% cheaper in real terms** than 8 years ago.

In 1988 we moved away from weight based letter postage to size-based prices. This reflects better the actual processing cost structures and makes life far simpler for the customer.

We also offer very substantial discounts for high volume customers who pre-sort their mail before lodgement. We share cost savings with our customers. This discounting is unregulated and determined solely by the Company (with reference to market pressures of course).

Delivering the Future

⇒ Strategies for success

⇒ Business purpose

*People reaching people through
New Zealand Post for messages,
goods, and payments*

⇒ Farming the Core

⇒ Key Programmes

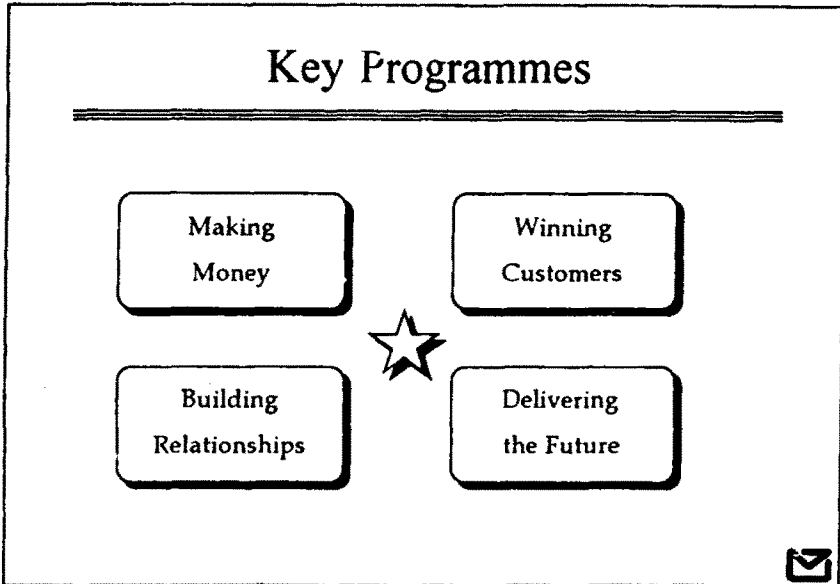


This presentation now turns to the future. What are the strategies being pursued by New Zealand Post to succeed in the future.

Our business purpose statement is : ***“People reaching people through NZ Post for messages, goods, and payments”***.

This defines the scope of the business. We will invest only in these core activities. We agree that as a Government owned business it is inappropriate to diversify.

We call this strategy of confidence in our business scope “farming the core”.



Each manager in NZ Post has objectives against these four Key Result Areas.

Making money is concerned with profitability, productivity growth, margins.

Winning customers is concerned with service performance, measured by customer satisfaction indices and on time mail delivery.

Building relationships is concerned with stakeholder relationships (the public, our employees, labour unions, Government) and we measure performance through public favourability measures and employee satisfaction indices.

Delivering the future deals with investment: whether in capital, people development, systems, or image of the Company.

New Zealand Post

Keys to our Success

- ⇒ Corporatisation
- ⇒ Strategy
- ⇒ People and Organisation
- ⇒ Marketing
- ⇒ Production Control (measurement)
- ⇒ Management Systems

Rethinking traditional performance standards



Turning now to the reasons for NZ Post's success we think about these areas of performance. Each is summarised in the following.

We believe we have "gone outside the box" in rethinking the traditional expectations of the postal business.

Corporatisation

- Separation of ownership (Government) and operational (commercial) matters
- Corporate performance accountability vested in Board and management
- Board and Chairman selected by Minister
- CEO selected by Board
- Social obligations defined by (separate) regulatory arm of Government
- Performance objectives defined in Statement of Corporate Intent (accountable to Parliament)



The corporatisation process provided the correct external stimulus to initiate change.

Postal Strategy

- ⇒ National priorities.
- ⇒ Infrastructure position.
- ⇒ Investment priorities.
- ⇒ Growth: efficiency and service.
- ⇒ Commercial discipline.

The time has come for postal development.



We understand that postal strategy must consider the fact that the Post is a key national infrastructure. It is not exactly like a private business. It is important to proxy the market as best as possible, to give managers the correct performance signals.

There is no reason why the postal business cannot be made into a successful corporate.

People and Organisation

- ⇒ Accept responsibility.
- ⇒ Appropriate organisation structure:
 - for growth,
 - for delegation,
 - for market focus.
- ⇒ Management development.
- ⇒ Best practice.
- ⇒ Teamwork.

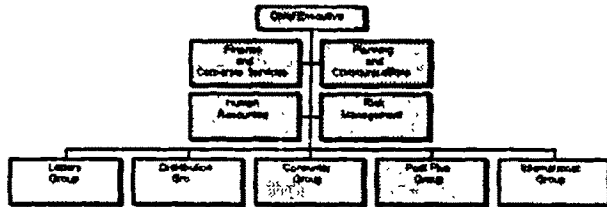


Labour relations and management focus are vital ingredients to success.

Changing attitudes does require a lot of time. For that reason it is unrealistic to implement a radical reform programme. Conservative change in the right direction is preferable - that is why for the US I do not recommend extreme measures such as full market deregulation and privatisation.

Those options may remain for the future, but are not necessary for major change to be achieved now with a more limited programme.

Business Unit Reorganisation



- ⇒ Focus on growth and closer to the customer.
- ⇒ Commitment to our people, our customers and the community.



The present organisation of NZ Post is simple and uncluttered, allowing business divisions to exercise maximum market focus.

Letters is concerned with the letters market: marketing and sales, delivery, mail processing operations.

Distribution is concerned with parcels and express courier, and the linehaul transport network.

Consumer manages the business of Post Shops - the retail network.

Post Plus is concerned with direct mail, stamps, and electronic mail ventures.

International manages the international range of services.

Each business division is autonomous as far as possible and writes its own Profit and Loss.

Marketing

- ⇒ Product knowledge:
 - service performance,
 - volume information,
 - cost structures.
- ⇒ Customer knowledge.
- ⇒ Product development:
 - the importance of simplification.
- ⇒ Marketing planning.
- ⇒ Sales and account management.



We have placed a huge emphasis on marketing and sales.

Production Control

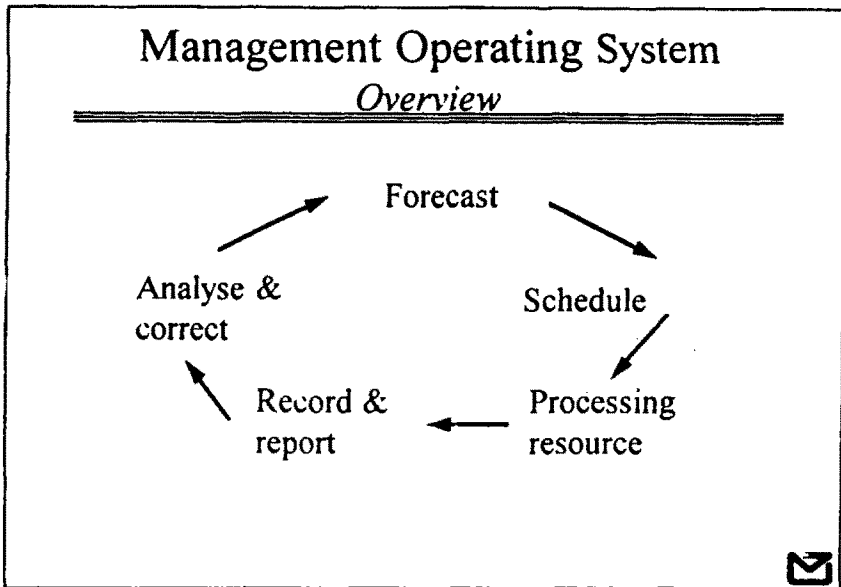
A system of management for mail operations that:

- ⇒ improves service performance,
- ⇒ increase productivity,
- ⇒ achieves greater flexibility,
- ⇒ copes with volume fluctuations.

Puts service performance under control!



Our business efficiency is as a result of proprietary systems implemented in mail service centres. Resources closely match workload. This production control process lies at the heart of our productivity success. The techniques are amenable to any single postal installation - here the comparison in size and complexity between the US and NZ does not matter.



This is a simple schematic for our production control system.

Underlying Benefits

- ⇒ These are fundamental principles involving a new way of managing the postal business - simple, practical, enduring.
- ⇒ Hands-on quantitative management.
- ⇒ Does not require technology - capital is conserved.
- ⇒ Involves staff and produces an environment that fosters improvement and innovation.
- ⇒ Guarantees productivity improvement and capability to handle growth.
- ⇒ Compatible with total quality management.

A unique New Zealand Post business process that can apply anywhere



We would like to assist the USPS in these practical measures.

Management Systems

Developed by New Zealand Post

- Mail processing systems.
- Delivery systems for letter carriers.
- Operations training.
- Transport network control.
- Track and trace - courier and mail shipments.
- Financial and management reporting.
- Business and marketing planning.



Like all businesses, we have worked hard to develop and adapt systems for better management. We are pleased with our achievements in these areas.

New Zealand Post



FROM 'TYRANNOSAURUS' POST TO 'COMPANY OF THE YEAR'

Today's New Zealand Post is a very different company from the one that was founded in 1840.

New Zealand Post is a company that has been transformed into a modern, efficient, and profitable business. It is now a leading company in its field, and its success is a testament to the hard work and dedication of its staff.

It has become an indispensable part of our lives, and we are proud to be part of it. We are committed to providing the best possible service to our customers, and we are confident that we will continue to grow and succeed in the future.

At New Zealand Post, we are committed to providing the best possible service to our customers. We are proud to be a leading company in our field, and we are confident that we will continue to grow and succeed in the future.

For more information, please contact us at 0800 937 937. We are committed to providing the best possible service to our customers, and we are confident that we will continue to grow and succeed in the future.

New Zealand Post
People reaching people



To conclude, we see this as the metaphor for our transformation.

ATTACHMENT 3

Statutory Change and the Post



Elmar Toime, Chief Executive
New Zealand Post Limited

Statutory Change and the Post

The legislative influence on the development of New Zealand Post

Presentation by

Elmar Toime
Chief Executive
New Zealand Post Limited

Washington
13 July 1995

Introduction

Recently, a business paper in New Zealand headed an article discussing management training in the following way:

"Does management reform the economy or the economy reform management?"

The article went on to quote the government of a neighbouring country announcing a new investment in management training as *"the next key step towards a competitive economy"*. The journalist put it rather neatly when she pointed out the belief in New Zealand was the other way around: *"a competitive economy produces management reform"*. I think this rather neatly captures my theme today.

There is a lesson here for those who wish to push for postal reform and bring about the change necessary to bring a postal entity into the competitive real world. There is only so much managers can do. They are a product of their environment.

What is New Zealand Post

New Zealand Post Limited is a government owned enterprise. It holds the franchise in New Zealand for universal mail delivery. Otherwise, it is just like any other company. Importantly, our employees believe in our company status. Having that state of mind helps achieve commercial behaviour. We try hard to get the entire public of New Zealand to also accept this. The language we use (for example, we do not refer now to *post offices*, but to *Post Shops*) and the symbols we have created emphasise the point. Nevertheless, the old institutional, way of thinking endures. That's OK - it can be turned to business advantage, as I will show.

There were no half measures when we were established as a corporate. The government gave us a clean, straightforward balance sheet with no hidden elements or special provisions. The break from government administration was clear-cut.

The change process was not exclusive to New Zealand Post. The enabling legislation which created us as a legal company, defined as a State Owned Enterprise (SOE), served a dozen other government trading entities. We were all commercially set free on the same day. All have succeeded and become profitable. Many have since been sold and trade today as privatised companies. We at Post remain in government ownership.

I have discussed privately how all this came about with the government Ministers of the day who were responsible for the SOE initiative. They tell me they were confident of the *model*, but not of Post itself. They wondered what they would do when (not if!) we failed. I have heard that said in many places around the world since. If there is one lesson from New Zealand experience it is that the Post can and does work as a successful business.

The Measures of Success

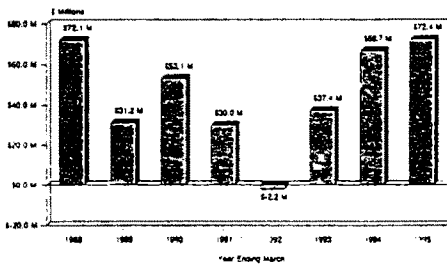


Figure 1: Profit after Tax

Well, we didn't fail. I think the initiative was a resounding success. Why? First: the environment was set up for success. The company was not only told to be commercial, it was given the tools and freedom to be commercial. Pricing policies were ours to make and market positioning was ours to define. Personnel policies were ours to formulate, to ensure we brought staff with us. We were free to hire and fire, and reward at market rates for skills and achievements.

Second: while the Company was denied government guarantees in its borrowings and trading activities, a sound commercial structure was established. This took almost a year to set up before launching as a corporate. Properties were assessed and valued, and assets were identified and assigned to the business. The government decided a postage price to get the Company closer to profitability. Preliminary budgets still had the Company making a loss. The full value added tax of 10% (called GST in New Zealand) was applied to all postage.

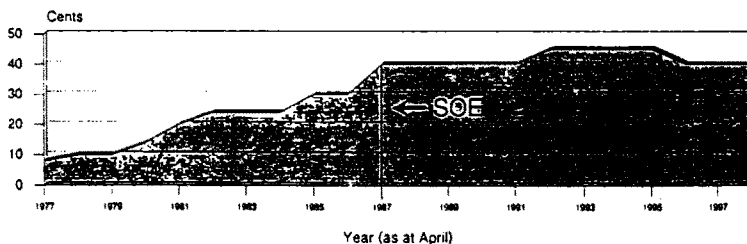


Figure 2: Standard Letter Postage

That postage price of 40 cents established then (about 25 cents US), now including 12.5% GST, applies today! In real terms, the price today is 27 cents, a fall of over 30%.

Third: a leadership structure was established. The government appointed a commercial Board of directors, consisting of leading accountants, lawyers, and entrepreneurs. Strategic skills and purpose were strong. Political affiliation was not a criterion for selection. The Board recruited a strong chief executive (my predecessor and mentor, Harvey Parker, who introduced me to this great business). From the outset it was decided that success, meaning principally profitability, was to be established immediately, in the first year of trading. That became the driving force throughout the business.

The Statutory Environment

I have said that the Post was established as one of a dozen other government trading enterprises. Back in 1987 policy setters did not think it was fundamentally different to any other. I believe that view may have changed for many. It must be acknowledged the Post has a mysterious social position that has endured throughout the years of reform in New Zealand. This is reflected in the complex statutory environment that remains in place for us.

Figure 3: New Zealand Post Limited

- ❑ Created in 1987 from the Post Office which was divided into three separate businesses: Post, Telecom, PostBank
- ❑ New Zealand Post is a limited liability company
- ❑ Clear separation of the powers of the Board (commercial) and powers of the Government (shareholder rights and public policy)
- ❑ Its shares are held by the Minister of Finance and the Minister for State Owned Enterprises
- ❑ The State Owned Enterprises Act controls the public accountability requirements
- ❑ The Postal Services Act controls the regulatory environment

All stakeholder groups have been considered in the legislative framework

• *State Owned Enterprises Act*

The key to understanding is the State Owned Enterprises Act, a statute that defines our objectives. Section 4(1) states:

"The principal objective of every State enterprise shall be to operate as a successful business and, to this end, to be -

- (a) As profitable and efficient as comparable businesses that are not owned by the Crown; and*
- (b) A good employer; and*
- (c) An organisation that exhibits a sense of social responsibility by having regard to the interests of the community in which it operates and by endeavouring to accommodate or encourage these when able to do so."*

This principle and its objectives have been tested in the Courts as various interest groups have sought to modify a number of decisions the Company has made by appealing on the grounds of what is "a sense of social responsibility". The first instance occurred in 1988 when an attempt was made to prevent the closure of uneconomic post offices. Mr Justice Greig decided:

"It is plain in my view, that the over-riding consideration is commercial; the operation of the successful business to be the background and probably the foreground of the company's operations."

A more comprehensive test occurred in 1992 when the rural community attempted to prevent New Zealand Post increasing a special charge for delivery that had existed for 70 years. I quote the following key passage from the judgement of Mr Justice McGechan in the High Court of New Zealand:

"While Section 4, and other surrounding factors impose a duty to deliver, they likewise limit that duty to the commercially realistic. If a service is commercially feasible, it is to be provided - under contract or howsoever - and is not to be withheld as a matter of policy, or arbitrarily or in a discriminatory fashion. However the duty to be a successful business does not in itself oblige New Zealand Post to provide uneconomic services, even within a monopoly, whether or not such were traditional for its departmental predecessor. Indeed, if anything, the duty prohibits the uneconomic and unbusinesslike, unless there are over-riding extraneous commercial factors.."

Two Cabinet Ministers, the Minister of Finance and the SOE Minister are named in the Act as shareholders. Their's is a key role. They exercise responsibilities as shareholders and are concerned with the overall performance of the business and they are responsible to Parliament. Day to day operational matters, including pricing, are solely issues for the Board and management of New Zealand Post. Ministers may only direct the Company in writing to undertake any action, and any such request must be tabled in Parliament. There has been no such request to New Zealand Post in its eight years of existence.

Postal Services Act

This defines our regulatory environment. Policy setters continued to believe that until the business proved itself successful a degree of statutory protection was necessary to ensure a universal service could be provided. This protection was defined to apply only to the standard letter. It was made clear to the Company however that these provisions would be removed in due course. Again, the initial correct incentives were established. I think there is no doubt that the intention to remove the monopoly provided a powerful motivating force inside the business. The Company and its people were marshalled behind the catch-cry of competition.

In the event, government took the view, in conjunction with the Company, that deregulation was to be phased in. This was as much to do with the state of the New Zealand economy at the time (a major recession and property market collapse) as it was to do with concern about the Company's ability to survive.

Last November the government decided it would legislate to remove fully the monopoly protection in 1995, but that has not happened as yet. We have shaped our business plans to expect an open competitive environment.

Our decision to reduce the price of standard letter postage, made with the release of our Annual Report on 27 June 1995, is only partly a competitive reaction to deregulation. It is more to do with our confidence in mail as a communications tool and as a stimulant to growth.

The Company fully supports the present initiative to deregulate the postal market in New Zealand. While it is not within the ambit this paper, I do believe it is the correct future world initiative.

• *Deed of Understanding*

- Universal price-equalised service
- Price control on standard letter
- Six day delivery
- Minimum number of retail outlets
- No rural delivery fee

Figure 4: Defined Social Obligations

New Zealand Post has been a commercially aggressive business. Our quest for efficiency and reform has required us to take a number of difficult and unpopular decisions. This led to some concerns from Parliament that perhaps the Company could reach decisions that compromised the role Government saw necessary for a universal service provider. Government asked the company to commit itself to defined social obligations in exchange for continued statutory protection.

This gave rise to the Deed of Understanding which is a contract between the government, represented by the Minister for Communications, and New Zealand Post. The basic provisions of the Deed cover universal service, an indexed price cap for the standard letter, frequency of mail delivery, and size of the post office network.

The company has committed itself to the Deed even when the market is fully deregulated.

• *Companies Act*

The business also operates under the Companies Act and financial reporting acts, which are codes of legislation pertaining to all companies in New Zealand. The Acts define the responsibilities of the Board, statutory reporting requirements, and so on.

• *Other Legislation*

As a government owned entity there are a number of further constraints on the business. We are subject to an Official Information Act which in principle allows people to seek information about the Company and its decisions. Administrative decisions and refusals to supply information can be reviewed by an Ombudsman (a parliamentary officer) who has power to recommend compliance but not enforcement with his viewpoint. Commercially sensitive information can be withheld, but it is an onerous responsibility to prove its sensitivity.

The Company is audited by the Auditor-General who contracts a private firm of auditors to carry out the audit. This audit is reported to a Select Committee of Parliament who can call Company officers before it to account for its actions during the year. The Annual Report of the Company is tabled to Parliament, as part of the SOE regime which also requires a Statement of Corporate Intent.

Statement of Corporate Intent (SCI)

The SCI provides for the Company to prepare a statement of its broad operating strategies, business targets, and investment policies for tabling to parliament. The statement must be agreed with the Minister. In this way a form of broad control is exercised over the trading activities of the business. It is a public and accountable instrument to allow the shareholder to be involved in strategic decisions which could lead to diversification away from the core. For example acquisitions of other companies or shareholdings over \$1 million require Ministerial approval. I believe this sort of control is appropriate for a shareholder. In particular the Government determines the extent to which it wishes to see its businesses encroach into new private sector activities.

People and Public

New Zealand Post has worked hard at its labour relations. Organised labour participated in the New Zealand reform process. It recognised the need for change in the economy. Today that reformist zeal has slowed down but it was a potent force in the mid to late 1980's. The cost of New Zealand Post's commercial success has been a 40% reduction in the workforce. Part time and shift work employment is a major element of some parts of the business. The efficiency imperative drives all change in the Company.

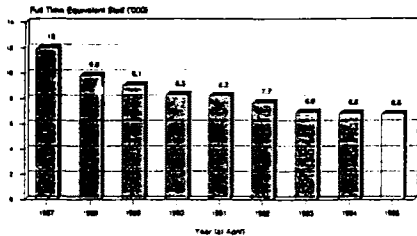


Figure 5: Full Time Equivalent Labour

Simplistically, that is achieved in one of two ways. You can reduce labour input for a given mail volume, or, you can hold labour effort constant while volumes increase. It is a management fallacy in my view to depend on volume growth to solve productivity problems. That dodges the issue. Volume growth is delivered by economic conditions and it is delivered by a postal environment with good service and minimum price. The Post can only be responsible for the latter. Marketing, new niche markets, divergence from core activities are only pretence. They can't disguise what ultimately has to be faced - the efficiency of the workforce itself.

Certainly, make the marketing changes that favour productivity. For example, by simplifying postage rate conditions, it makes it easier to run the business. It makes it easier for customers as well. In New Zealand we do not need a public post or zip code. We have tackled the management options for productivity gains without making demands on the public. Our letter pricing is based on size, not weight, because that's what determines costs. As a result, life is so much easier for our counter people and for our customers.

The following table summarises some of our key performance indicators.

Interest groups have mixed views. To the mind of some, the reforms we have made have gone too far. Generally, there is little public awareness that it is business that pays the way. The uninitiated believe the Post is a community and social service for householders. As a consequence too much weight can be given to the features of the universal service - basic letter post price, post office networks, and delivery frequency.

New Zealand Post now operates in 1995:

- ☑ With 30% more mail to deliver
 - ... real unit costs 30% less
 - ... labour productivity up by over 100%
 - ... at a 97% plus on-time service performance
- ☑ Prices under control, with only one price rise in 8 years for the standard letter
- ☑ New products and services meeting market needs
- ☑ Modern plant, transport and equipment funded from within the business
- ☑ Paid dividends and taxes of \$445 M

Figure 6: Business Performance

If customers are prepared to pay for these services, well and good. The true test is what would happen in a competitive environment. Competition decides what is affordable and what is needed by customers.

As I have mentioned, interest groups have tested the law in the courts to see where commercial behaviour begins, and where the Company must have other, broader social considerations. There was major opposition to our post office conversion process. But no place in New Zealand was left with a lesser *postal* service. Banking was taken away (hardly a Post matter) and agency payment services could no longer be carried out in our franchises. It is undeniable however that many communities felt a community loss with the closure of the local post office.

The rural community was similarly aggrieved when the Company at one stage threatened to withdraw from delivery services to rural addresses. Our solution was to increase a long-standing fee for service, paid by the addressee. This gave birth to a major and enduring lobby which sought political interference to force New Zealand Post to desist. The SOE model was upheld and the Company effected the change.

Today, the company could be seen in one sense to be reversing these unpopular actions. We are increasing the number of full service Post Shops and have removed the controversial rural delivery fee from 1 April 1995. While public opposition was one element to our decision-making, a new set of commercial imperatives have driven us.

With the introduction of counter automation technology and the development of our franchise operation, we can see the benefits of a more commercial solution to the question of public access to our services. And, of course, we can see the commercial benefits of having a universal delivery service, including the rural sector. Rather than charging the addressee, it is better to encourage more mail through a more cost-effective delivery channel. That is what we are doing.

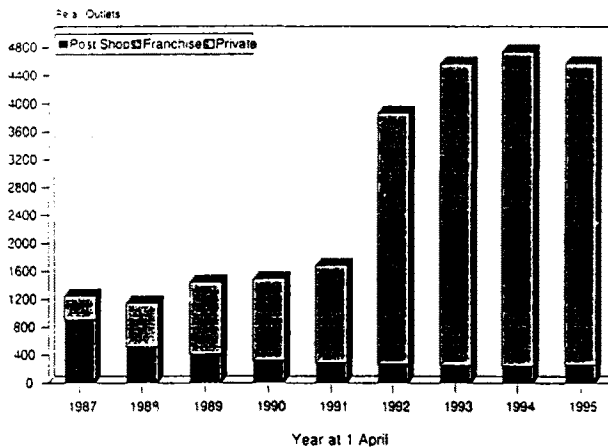


Figure 7: Retail Outlets

These two examples, the Post Office closure lobby and rural delivery, show that there are key interest groups that do have valid points of view. One first decides the commercial priorities. This may require unpalatable solutions, but usually they just have to be made.

Having said that, I do believe the Post is different to ordinary business enterprises because we are a carrier of last resort. The government says that must be so as a matter of public policy. If we weren't there, someone else would have to do it.

One vital interest group comprises the large mailing businesses. These are the companies that either are dependent on the mail for their livelihood, or whose own administrative processes need a viable, vigorous and efficient Post system to exist. Many of these groups are represented in the audience of this conference. Many present may be enjoying the benefits of subsidy or lobbying power. They have a real influence on what happens through the various rating processes. I have a message for you, too. A commercially free Post, able to set its own prices and service offers should not hold any fears, except if you benefit today in an unreasonable manner.

I offer three examples of changes made by New Zealand Post where business customers did not immediately benefit from our efficiency and structural reforms.

Publications Discount.

Like many other postal administrations we used to offer a 50% publications discount. I don't know why. It was the first subsidy we eliminated, and properly so, for mail costs depend on size and weight, not contents! The consequence for some publishers, particularly small non-profit organisations, was to close them down. We are not proud of this, but they had existed because of a historical and unjustifiable subsidy. Hardly the way for them to sustain a viable business. Large customers, who swung a lot of weight, negotiated a phased price change. Some managed to win a five and six year phased removal of the discount. That's great. That's commercial.

Franking Machines

My second example concerns franking machines. It was the practice in New Zealand to sell postage on credit to people using franking machines. There were tens of thousands of customers with effective credit lines of only a few dollars. They were billed monthly and were a major administrative cost to the company.

We introduced a new credit policy and required small business customers to convert their machines to credit locking. This cost them hundreds of dollars. At the same time we introduced a service called BoxLink that did not require stamps or franking, compounding the effect. This devastated the franking machine industry in New Zealand.

Following the announcement of our intentions, the industry asked me to respond to their concerns. I asked how they had factored what New Zealand Post might do into their business plans. This question seemed to catch them by surprise. No-one had thought New Zealand Post was a relevant factor in their strategic planning.

Mailing houses

My third example concerns the mailing house industry. It was the practice that customers who originated the mail paid the mailing house, usually on 7 day terms. Because the old Post Office was such a poor chaser of debts, the mailing houses enjoyed debt-free working capital funded by the Post. Needless to say that changed as we focused on cash flow. We began to contract directly with the major mailers and received payment on 20 day terms. Mailing house cash flow dried up and some businesses folded. Their profitability had depended on a lazy Post.

My observation is this. The Post used to be a sleeping giant. Many rested their heads on its gentle and fat belly. Beware when the giant awakes!

The Future



New Zealand Post
Company of the Year

I want to briefly turn to where I see New Zealand Post going now. Our business vision is to become the best company in New Zealand and recognised as such by ordinary New Zealanders. We are already 1994 Company of the Year in New Zealand! To give effect to The Best Company vision I have defined five business principles to target all our shareholder groups. These are:

- ▷ Sustained profitability
- ▷ Care for New Zealand by meeting defined social obligations
- ▷ Investment which adds shareholder value
- ▷ Valuing our people
- ▷ Reliable, efficient services at lowest cost and price

Figure 8: Business Principles

Our business purpose and direction is firmly based on what we call our *"farming the core"* strategy. We concentrate on the established parts of our business, and extend these only where we can demonstrate clear synergies of operation.

This year we have divested two of our subsidiary activities which we felt were diverging from our core. Instead, we are presently in the process of acquiring two others to prepare a future strategy to lessen the company's dependence on the letter post market. That is commercial freedom. We apply strict internal investment disciplines: shareholder value considerations and relevance to our core key drivers.

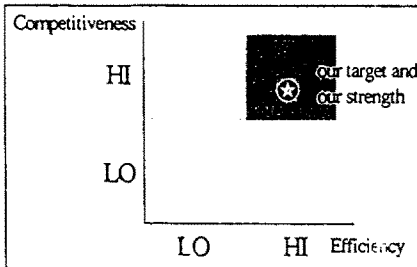


Figure 9: NZ Post market positioning

Our drive for ongoing efficiency continues. We are advising a number of overseas postal administrations on practical and basic productivity projects. If you haven't seen these projects, you will be amazed. I invite my audience to come and observe these changes first hand in New Zealand!

Conclusion: What Advice Do I Give?

I come back to my opening question. Do managers get the environment right, or does the environment produce the right managers? I believe the importance of getting the environment right can't be glossed over. In the case of New Zealand Post the environment was changed first. The law makers established a model for government trading enterprises predicated on a policy view that said it was preferable for government to be small. Their view was that government was a poor investor and could not properly operate a trading entity, because at some point the need to implement social policies would come into conflict with or dominate commercial objectives.

The State Owned Enterprise model was the product of this change. Public policy and commercial activities were clearly separated. A minimal set of social objectives evolved, expressed in the Deed of Understanding, that appears today to satisfy nearly all interest groups. And, there has been some pain.

Difficult decisions cannot be avoided. The Post is too important for that. There are commercial solutions for the problems facing the Post.

If the legislative and commercial environment is put right, what then? Obviously objectives must be set for the business. For New Zealand Post, the business is required by law to be successful on a comparable basis. The governance of the business must be directed to that goal. It means a strong profit ethos. Profitability, and more particularly building the value of the business, drives managers. Rewards and incentives for people must be correspondingly appropriate for the scale of the business. Sensible commercial freedom is necessary.

Public accountability is still possible. Rules for reporting and disclosure exist to ensure public targets are met. None of this means that the operation can't run commercially. Capital investment, whether in plant, technology, or new business ventures must have the appropriate disciplines. This means the business is able to raise capital because it is commercially sound. The changes we have seen in the world in the past few years have reinforced the capitalist model. The Post is not immune.

The challenge before the Postal Service is good service getting better at low costs. Efficiency and business profitability must be the aim. I have no doubt whatsoever that these goals for the Post can be achieved in the United States of America. Complete the change process which has begun.

I close with a quote from Shakespeare's *Julius Caesar*:

*"There is a tide in the affairs of men,
Which, taken at the flood, leads on to fortune;"*

Now is the time!

Testimony by Ulf Dahlsten January 25, 1996 at a hearing organised by the Senate and House subcommittees with jurisdiction over the U.S. Postal Service.
The hearing was entitled "USPS Reform - The International Experience"

Can deregulation work?

Mr Chairman, Mr Co-chairman. As the others I am honoured to be invited to present our experiences. Sweden has gone further than most countries - as you probably know - and totally abolished the monopoly on letter distribution.

Sweden was when it happened in 1993 one of the first three nations in the world to deregulate its letter market. Just under ten operators, most of them very small, tried to establish business in letter distribution. Of the active ones, only Svensk Direktreklam is left. This company, originally a distributor of unaddressed mail, is now also involved in the distribution of addressed items.

On the other hand, Sweden's best-known private sector operator - CityMail - has for the second time filed for bankruptcy. According to an independent committee the company has no prospects for survival within the scope of its current business concept. CityMail may, perhaps, have been able to compete with the "old" Sweden Post, but not with the much more efficient Sweden Post of today. CityMail's business scheme - with sorting being conducted manually - cannot become competitive, even if volume increases sharply. Even if CityMail is now once more reconstructed, the forecast for the future is thus weak. Does this mean that the deregulation in Sweden has failed? My personal answer is no.

There were no doubt many people who supported deregulation with the main intention to give the private entrepreneurs a chance. However, my own reasons for urging the need for a deregulation of the letter market and the conversion of Sweden Post into a limited liability company were different. So were others. Our analysis was - and still is - that the position of letters as means of communications is seriously under threat by developments in technology.

Nearly ninety per cent of letter revenues comes from companies, other organisations and the public sector. They use letters primarily for two purposes. The first is for administrative and financial messages. In this market, electronic systems are gaining market shares day by day. Fax, ePost, eMail, eDI etc. already account for more than half the volume of messages across borders, as well as for 20 per cent of business communications in a country like Sweden. The second use of letters is in market communications. Some of you call it junk mail. Here, the letter competes with other media, including the growing area of radio and TV-advertising, as well as with press advertising, billboards etc. Letters have around a third of the media

market, and of that share Sweden Post has, in turn, two thirds. Other operators share the remainder. In this expanding market the letter has maintained its position well.

There were also other reasons for deregulation and privatisation. Sweden Post has much more to offer than delivery of letters alone, even if letters represent more than 40 per cent of our revenue. Basically we are in the markets for messages, payments and distribution of goods. The pressure of competition is also growing in other areas than letters. The Postgirot that is handling payments is not only responding to a trend in which payments will increasingly be made by electronic means. Furthermore, as a result of Swedish EU membership, all banks in Europe are now European banks. This means that international banks specialising in payment-processing now have free access to the Swedish market. The parcel business, too, no longer has domestic competitors alone to deal with. International integrators are increasingly turning their attention to the Swedish market.

The step toward a deregulated postal market was to take away the monopoly on letters that we had. Although we are free to decide on prices for our services there is a capping on letters up to 500 gr. The cap is the price level that is presented in your documents. The real price paid is less. And has in real terms been reduced with 10 percent the last two years.

We got a Postal Services Act in 1994 and at the same time Sweden Post became a limited liability company. The monopoly the Postgirot had on state payments was terminated in this context. Today Sweden Post operates on the Swedish market without any monopoly protection.

The Government has the responsibility for giving all citizens a daily postal service (5 days a week) wherever they live in Sweden. Sweden Post has taken on these responsibilities in an agreement with government. This agreement will soon be renegotiated. It is important to underline that we can provide this postal service without any compensation from the Government. In the case of the counter services there is a certain compensation for rural areas that do not cover costs.

The choice of direction - deregulation and conversion of Sweden Post into a limited liability company - made a couple of years ago has opened up for opportunities for Sweden Post to rise to this challenge, and we have taken our chances. We have adopted four external strategies.

Efficiency improvements. SEK 3 bn (460 million US dollars) has been saved in five years out of a turnover of around SEK 20 bn. (3.1 bn US dollars). Approximately 75 per cent of the work on improving efficiency has now been completed. 1/3 of post offices is outsourced. Out of the 500 biggest companies in

Europe Sweden Post is ranked as number three in profitability last year. The on-time delivery is 97 percent.

IT as a friend. Through development of PostNet, among other projects, Sweden Post is today a market leader within the field of electronic messages and payments.

Added value for the customer. By combining our range of services in administrative processes and logistical systems, and by developing the postal outlets into what we can call "The best friend of the ordinary businessman", we can enhance the value to the customer of the services we offer.

Internationalisation. By meeting our international competitors aggressively, and by applying our knowledge abroad to best effect, we can enhance our earning capacity,

These external strategies have been backed up by an intensive work on internal change, spanning everything from management systems and the breakdown of Sweden Post into 1500 small profit centres thereby creating participation of all employees in the corporate planning process, to a build-up of enterprise culture around shared visions and values, and the development of leadership and proficiency.

We believe that today we represent a national asset. This is sadly seldom said about all postal operators in the world. This hearing indicates that the intention of this congress is to guarantee that this will be said about the USPS in the days to come. This is contrary to most European countries where governments seem to have reached the conclusion that their postal operator is incapable of surviving through his own efforts; indeed, the prevailing view is that they need the protection of a monopoly position. It is considered that the extra cost has to be borne by the customer. There are examples of countries who in order to retain the monopoly for the foreseeable future are prepared to pay a letter rate (excluding VAT) double to that accepted in Sweden.

However, there are no certain victories in the future - not even for Sweden Post. Hard work and a forward-looking approach will be needed - and developments will have to go our way - if we are to succeed.

If we continue to receive the right support, and are able to work under the same conditions as private - sector business, we believe that we will continue to be able to provide the whole of Sweden with a world-class postal service and continue to represent a national asset to our country.

If I may conclude with some remarks on what experiences that can be drawn from Sweden and perhaps applied to the US those would be as follows. I make those

comments bearing in mind that every country has its own history and own traditions that must be respected. That is certainly the case in your great nation.

The first step to be taken ought in my opinion to be to prepare USPS for competition. That could be done by changing USPS into a limited liability company.

The second step, to be decided now but to take place in say five years time would be to deregulate the market and at the same time introduce a Postal Services Act.

This act could be implemented by a new Postal Services Commission perhaps developed on the basis of the present Postal rate Commission.

As a third step the USPS could be fully privatised by a sale of the shares. In Sweden that would be a controversial step. With the American traditions probably a necessary one.

The basic question faced here is whether the postal services is a part of the market economy where consumers demands are governing or whether it should be looked upon as part of a country's infrastructure - like highways - to be financed collectively. To me the answer is simple. To 95% the Posts are a part of the market economy and should be run accordingly.



FUTUREPOST 95 Conference

Liberalizing the market

Washington, 12-14 July 1995

SWEDEN POST -

PUBLIC OPERATOR ON A DEREGULATED MARKET

Presentation by Mr Tommy Persson,
Senior Vice President, Sweden Post

Introduction

It's a great pleasure for me to be able to talk to this distinguished audience today. The pleasure comes mostly from the simple fact that I represent a country which has already implemented what this conference aims to just discuss, namely the liberalization of the Postal Services. What I will say can be confusing for several of you but the steps towards a deregulated market have been taken without any larger experience of deregulation. Neither from the government nor from Sweden Post.

Some facts about Sweden

Let me just first put you into the Swedish perspective as some of you might not be too familiar with this new member of the European Union.

Sweden is the second biggest country in Europe if we consider only the surface. The distance from North to South is some 2000 km, which is approximately the double of the corresponding distance in Germany or France. Or expressed in another way: if you lay out the same distance from the south of Sweden and southwards you end up in Rome.

If we consider the population, Sweden is on the contrary one of the smaller countries in Europe with less than 9 million inhabitants. This means that the country is sparsely populated and you may have heard that Sweden is sometimes called the last remaining wilderness of Europe.

The two facts I have mentioned - the size and the thinly spread population - would of course in principle make it difficult to run an efficient postal service. However, I will come back in a moment to show you that Sweden Post is actually very successful in doing it despite the obstacles.

Some facts about Sweden Post (Ltd)

Just a few words about Sweden Post, in Swedish Posten AB. This is the limited company which the government has entrusted with operating the universal postal service in the country. It has a turnover of slightly over 20 billion SEK (2.7 billion US\$) and last year yielded a handsome profit of 1.3 billion SEK (180 million US\$). In fact Sweden Post has been profitable every year during this century.

At the end of 1994 staff numbered 45 000, down 8000 since 1992 and down some 15 000 in the last five years.

The business concept is to provide information, goods transport and payment services all over the country and internationally so that everybody is able to reach everybody. In Sweden, Posts and Telecoms were never combined in the same administration and they are now both limited companies. Payment services within the Sweden Post Group are provided by the Postal Giro, which is now also officially a bank. The fact that we are able within the same group to provide information, logistics and payment services gives us a competitive advantage as banks do not provide transport services and delivery companies do not operate banking services themselves. Thereto we also provide the customers with full retail banking services through the branch net work. This is done in cooperation with another bank.

A few words about mail. Last year Sweden Post handled approximately 4.3 billion postal items of all kinds which means some 500 items per inhabitant per year which I think is one of the highest figures in Europe. Normal first class letters are distributed overnight all over this big country. The systems are designed to do it to 100 % and the actual performance is not far away: the last few years it has been a stable 96 % on average, all connections taken into account. The prices have been under European average until just recently when VAT had to be put on top. The parcel division with a turnover of 3 billion SEK (410 mUS\$) has a market share of 70%. The market defined as parcels with a weight of less than 35 kg. The parcel division is since a year ago profitable after years of losses. The girodivision transmits 50% of all payments in Sweden and has also been very profitable. The market share in retail banking is about 10%.

I hope that this brief overview has given you an impression of both my country and my company.

Then I turn to recent events as regards postal liberalization.

The five major postal reforms in Sweden

In the last couple of years we have seen a number of sweeping reforms in the postal field in Sweden. To start with I will just give you the list:

- the postal monopoly has been completely abolished
- a very first Postal Services Act has been promulgated
- the Post has been incorporated as a limited company under private law
- VAT has been introduced on all postal prices except on export of goods

- the Postal Giro has lost its privilege on payments to and from the government.

Those of you who have followed the current debate on European postal policy will have noted that these reforms go far beyond what is contemplated in most other European countries.

I will now comment on each of these five points and finally say a few words about the experiences so far.

Abolition of the postal letter monopoly, 1 January 1993

Sweden Post had always had a monopoly on the handling and delivery of letters. This was of the type which is common in most countries, i.e. covering the regular transmission against a fee of sealed letters and of unsealed mail items containing personal messages.

The last legal text concerning the monopoly dated from 1947 and was just because of that no longer up-to-date. New printing methods and new ways of distributing information, e.g. by means of local and even international courier firms, had in fact eroded the monopoly. The Post furthermore did not pursue those who broke the law for corporate image reasons.

The management of Sweden Post actively supported the abolition of the monopoly mainly for image reasons. In fact the public perception of the Post as a State monopoly negatively influenced our relations to customers and that also in fields where the Post did not operate with monopoly protection, such as in parcels and banking services.

The Government was of the same opinion and furthermore came under some pressure at the beginning of the 1990s as a private company started a letter delivery service in Stockholm. According to the letter of the monopoly law the activity of this company was illegal and subject to public prosecution. But the company claimed that its activity was legal because what they handled, namely computer-produced letters, did not exist in 1947 when the last legal text was drafted.

In order to get a basis for taking a decision about the monopoly the Government ordered an independent consultancy study to be carried out. It was undertaken by the internationally well-known firm of McKinsey and Company. This study showed that the Post on the one hand has to carry extra cost for delivering mail all over the country and some costs of a social character. On the other hand the Post has considerable advantages of scale and scope because of being the only company able to deliver every weekday to every address in the country.

The Government thought that there was no reason to wait for the complete package of reforms and decided to go for deregulation without contributing Sweden Post for the mentioned extra cost. Further on the deregulation was a fact some time before a postal service net was established.

I will come back later to the effects of the abolition of the monopoly but I would like to add a comment to the corresponding discussion in the European context.

In our view the Postal Green Paper and the subsequent announcements from the Commission have a big black hole. In these papers it has more or less been taken for granted that the universal service entails some costs for which the operator has to be compensated. However

no calculation of these extra costs has been made - or at least not published - and the worse is that no mention whatsoever has been made of the income side, that is what I just said about our case, that there are e.g. advantages of scale and scope on which it is possible to put a price tag. In this particular case I think that we tend to agree with some of the third-party comments made in the Green Paper process that it has not been demonstrated that a postal monopoly is economically justified.

As mentioned Sweden Post gets no contribution for the extra costs for nationwide distribution of letters. However Sweden Post has taken on the task of providing the country with daily (5 days a week) and nationwide counter services. In a certain agreement with the Government Sweden Post gets a contribution corresponding to 5% of the total cost for the counter services. This amount is yearly negotiated.

I now have to quickly go on to the next subject which is the Postal Services Act.

Postal Services Act (1 March 1994)

In Sweden we have actually never had any postal law. The few things which during some periods required legal protection, such as the monopoly provisions, were in fact enacted in legal instruments of a lower status than an actual law.

When the postal market was completely liberalized it however became necessary to regulate some basic aspects of this market in a special law. As a difference to the postal laws in other countries, our new Postal Services Act does not apply only to the public operator but to the entire postal market, including also possible private operators.

Although this Act is very short, in fact only some 4 pages of printed text, I have not got time here to comment in detail on it. I will just mention a few interesting facts.

The most ingenious feature of the Act is its opening paragraph by which the Parliament, the law-making body, puts the burden on the Government, the executive branch of the State, to see to it that there is a good postal service in the country. This gives the Government an unlimited freedom to contract with any company on the market which is able to provide a postal service.

The only condition attached to this obligation is that the Act defines the limits of the universal service, by the way quite simply in the same way as the UPU, i.e. letters up to 2 kg and parcels up to 20 kg.

The Postal Services Act furthermore lays the basis for a supervisory authority which has the task of monitoring the application of the Act and to intervene in case of anomalies. This body is now in operation, the National Swedish Post and Telecom Agency. Also in this respect Sweden has gone further than required by the Green Paper, i.e. that we have both separated the operator from the regulator and furthermore separated the two governmental functions of being the owner of the main operator and the regulator of the market in two separate bodies. The owner function is performed by a special section of the Ministry of Transport and Communications.

Operators which intend to start delivering letters have to register with this Agency but there is no need for formal authorization or concession.

The Agency has taken over some tasks of a public authority character both from the Post (such as opening of undeliverable letters) and from the Government, namely to be the signatory of international intergovernmental treaties in the postal field.

Finally I would like to mention that the Postal Services Act says about postage stamps that such stamps designed according to the UPU Convention can only be issued by the operator which has been appointed by the Government to fulfill its obligations according to the UPU Acts. Indirectly this however means that all other operators are free to issue stamps with another type of design if they need to use this means of prepayment of the price of their services. The same goes for putting up mail-boxes in public places. In practice no private operator has as far as I know made use of these possibilities.

Sweden Post (Ltd) - (1 March 1994)

In comparison with the abolition of the monopoly and the change of the legal situation, the transformation of the status of Sweden Post from a commercial state enterprise to a normal limited company was not that dramatic. Or should at least not have been.

In our case the formal change of status just represented the final step in a long development which took place mainly in the 1980s. The Post and other state enterprises with the same status were in fact during this period gradually granted more and freedom of action in areas such as fixing prices and making investments.

In the case of the Post we in fact bought all our assets from the State in the middle of the 1980s and at the same time we were authorized to decide upon and finance all investments ourselves. Also the right to set prices was gradually extended and in the last few years all power of decision in that area was within the enterprise, subject only to a limited price-cap.

The reason why the management of the Post and the Government wanted nevertheless to take the last step to the status of limited company was very briefly that in order to create the level playing field required in a market with several actors the Post had to have the same possibilities and restrictions as private competitors. This concerns e.g. the conditions for paying company tax and for concluding collective labour contracts with employees.

It was also noted that most major customers are limited companies which in fact prefer to deal with other limited companies and feel uncomfortable concluding agreements with a state enterprise with a particular legal status.

So, basically there would not be any problem to take that final step. However, I mentioned at the beginning of my presentation that in the last few years Sweden Post has had to slim its organization by thousands of employees i.e. because of sharply decreasing volumes of transactions at post office counters and of better working procedures in general, including increased mechanization. This led to a general belief among our staff and also in some political circles that the incorporation itself was the root of all the evil.

For this reason there was a big internal and public debate about the proposal to Parliament to incorporate the Post and the decision was finally taken with a rather slim margin in favour.

I have so far deliberately used the word incorporation because as the State retains all the shares in the company there is no privatization in the real meaning of the word. The Government thus appoints the Board of Sweden Post and the Board appoints the President and Chief Executive.

Finally under this heading I would like to mention especially for those who think about incorporation that there are three very crucial difficulties from a financial point of view:

- firstly the question about acquiring your own assets which I mentioned a while ago and in which respect we were lucky because we had already many years ago bought our assets
- secondly the question about how to finance your pension commitments. In this respect our position was bad as we had always only paid pensions to retired employees but not constituted any pension fund for future pension commitments. We expected the Government to find these earlier commitments but in the end it was not willing to do so. Instead we will not be expected to pay any dividend on the State's shares in the company until a sufficient capital base has been built up again.
- thirdly the agreement with the Government about the regional and social services i.e. daily and nationwide distribution of letters and daily and nationwide counter services.

Agreements between the Government and Sweden Post

As I said when I talked about the Postal Services Act the Government is in principle free to contract any postal operator for the universal postal service which it is obliged by Parliament to provide. However, at least now when this option had to be applied for the first time the Government of course in practice had very little choice as there was only one operator able to serve the entire country with high-quality postal services.

The fact that the Government realized that it was also the single owner of that particular company may also have helped it taking the decision.

But more seriously, there were negotiations about the agreement to be signed and the first agreement is only valid for a limited period, i.e. up to the end of 1996, thus less than 3 years. After that the Government has the possibility to reassess the situation and in principle also to appoint another or several other operators.

I cannot go into the details of this first agreement but I just mention some of the aspects it covers:

- the Post accepts to provide a universal mail service without any compensation from the Government. This includes the delivery of newspapers, at present performed at prices under cost
- the universal service is defined on the basis of the Postal Services Act and with further specifications as regards e.g. the number of days per week deliveries have to take place, the quality of service (although not exactly defined) and the principles for pricing of various categories of mail items (including an index-type price cap for individual letters)
- the Post is also to provide a counter service all over the country, with the compensation from the Government mentioned above.

Application of Value Added Tax, VAT (1 March 1994)

European countries normally do not apply VAT on prices for postal services. As regards the EU member countries this is based on the 6th EC VAT Directive which exempts something which is called "public postal services" from VAT.

In Sweden's case, it was quite natural in the new situation with several operators competing on the same market that one of them could not be exempt while the others had to charge VAT. This would have been against all principles of fair competition which we by the way have enshrined in a new law on competition which has been copied from the Treaty of Rome. I might also add that when we introduced VAT we had expected some public debate about the price increase but actually almost no reaction came. Apparently the Swedish public is so accustomed to VAT being applied to almost all goods and services that they found it logic and acceptable.

In order to find out how this could comply with the VAT Directive, the Swedish Government sought clarification from Brussels and got the answer that VAT in our case, operating as a company under private law, did not fall under the mysterious concept of "public postal services" but that we had to apply VAT.

At the same time we also agreed with our tax authorities about the definition of a postage stamp. According once again to the VAT Directive VAT cannot be charged on some "means of payment", including stamps. This is basically a misunderstanding as postage stamps have never had the same function as legal tender for which this regulation is understandable. We now consider stamps as a receipt for prepayment of a postal service and as such it is possible to charge VAT at the moment the stamp is bought.

Our view, which we are going to follow up in our future contributions to the discussion about the European postal policy, is that the 6th Directive is out-dated on both these points, creates market distortions and has to be amended when it anyway will come up for revision in the next future.

Competition on payments to and from the Government (1 July 1994)

I will not say very much about this issue as it is of a more national character.

The Postal Giro service run by Sweden Post has had a favoured position as regards these payments, taxes, VAT, pensions etc, and the interest on the float of such money has contributed to the profit of the Post and thus to support the nation-wide post office network through which many of these payments have been made.

These privileges have been removed and all banks and other financial institutions may now compete for this business. As the Postal Giro is the normal means of payment in Sweden it keeps its very strong position and is still the main payment channel also for payments to and from the Government.

At the same time the Postal Giro service has been incorporated as a limited company under bank law and is now able to operate on more general terms but there are restrictions. The Postal Giro is not allowed, according to the company act, to deal with medium or longterm financing. Neither is the development to a fully assorted retail bank allowed. The strategy is to keep the Postal Giro Bank as a Payment service institution.

Experiences so far

Of course it is yet too early to draw any firm conclusions about the effects of the five reforms I have been talking about. The incorporation is only some 16 months back but the monopoly has been gone almost two years which may make at least some comments possible.

There are at present only three companies registered as operating letter services or combined letter and parcel services. One of them is of course Sweden Post, the second is the company which I have mentioned before which delivers computer-produced letters in the Stockholm city region and the third is a company which has a big market share in the delivery of unaddressed printed matter but which might diversify into addressed mail in the future.

In Stockholm City competition has tried to expand since their activity is now fully legal. That has forced Sweden Post to a new pricing strategy in Stockholm within the business segment of the market. The price-fall in those segments in Stockholm is estimated at approx. 7%. The competition has also created an extra stimulus for improved effectiveness. In this respect the competition has been positive. However the main competitor went bankrupt during the spring. Under pressure from the National Swedish Post and Telecom Agency Sweden Post bought the 75% of the company. We today run it as a completely separate company in order to restructure it. In the meantime a taskforce with representatives from the market actors and authorities discuss a policy for the long term structure of the market.

The conclusion is of course that as long as you keep up your quality and to some extent react on the market prices, then it is very hard for a newcomer with restricted services to succeed even if the prices are very low.

The competition for the Postal Giro has increased heavily. Due to an outstanding payment service product we have however only lost one larger customer (one county administration) since the monopoly on Government payments was abolished. The profitability has dropped somewhat due to the effect on margins caused by the competition.

Remail from Swedish senders has increased as this is now a completely legal activity but it might have grown as much anyway as we postal operators have still not got our internal compensation systems in order and continue to make price arbitrage possible.

We have some indications that other operators are interested in doing something on the Swedish market, i.e. a few of the traditional partner Posts in Europe and the main international integrators. This is a problem which we will have to face in the future: how to be at the same time partners and competitors.

Further on we have to accept that we are no longer protected from scrutiny from media and as a consequence of this type of publicity there has also been an increase in reactions from our own staff in the press.

A positive consequence is that we have noted that new categories of people have taken up an interest in joining our staff, in particular university graduates which we earlier had difficulties to attract. In a recent case we advertized for 25 trainees and got some 1900 candidates which meant that the ones we recruited were extremely qualified.

Conclusion

We are aware of the fact the two northernmost newcomers to the European Union - Finland and Sweden which are in approximately the same situation - attract some attention from the rest of the world as regards the extent to which we have already liberalized our postal markets. I have myself heard reactions varying from pure admiration because we dare to conduct this full-scale experiment to comments that we must be complete fools.

The truth certainly lies somewhere in between. What I can assure you is that it has been an extremely interesting process in which we sometimes have had to find solutions to problems which no one had even tried to solve before.

I am sure that this presentation does not give you all the information you would like to have but I am of course at your disposal if you want to put questions either after this section of the conference or quite informally during breaks today and tomorrow.

United States General Accounting Office

Motley

GAO

Testimony

Before the Subcommittee on Post Office and Civil Service,
Senate Committee on Governmental Affairs; and the
Subcommittee on the Postal Service, House Committee on
Government Reform and Oversight

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U.S. POSTAL SERVICE**A Look at Other Countries'
Postal Reform Efforts**

Statement of Michael E. Motley
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General Government Division



A LOOK AT OTHER COUNTRIES' POSTAL REFORM EFFORTS

SUMMARY OF STATEMENT BY
MICHAEL E. MOTLEY
ASSOCIATE DIRECTOR, GOVERNMENT BUSINESS
OPERATIONS ISSUES

Various parties have called for fundamental changes in the laws and regulations governing the U.S. Postal Service. GAO believes that three areas--universal service, the mail monopoly, and ratemaking--will be among the most challenging for the Congress to address in any future reform of the U.S. Postal Service.

In the past decade, a number of other countries have restructured postal administrations from entities subject to close governmental control to entities still owned by the government, but subject to less governmental control. GAO looked at postal reform efforts of eight other countries: Australia, Canada, France, Germany, the Netherlands, New Zealand, Sweden, and the United Kingdom. The U.S. Postal Service is much larger, having at least seven times the mail volume, than any of the eight. Even so, other countries' experiences in giving postal administrations greater commercial freedom are relevant to current reform issues in the United States.

After reforms of other postal administrations, many of them have reported significant improvements in financial performance. In all of the other eight countries, the postal administrations provided certain services widely to their citizens and at uniform rates before reform and continued to provide them following reform. In some countries, changes in universal service practices, such as access to post office services, have been controversial. For example, after its reform, the New Zealand Post increased a delivery fee for rural service; this decision proved unpopular and the fee was eliminated in 1995.

All but one (Sweden) of the eight countries have monopolies over some letter mail. In Sweden, full competition for all postal services has been allowed since January 1994. Some of the other countries narrowed the scope of the monopoly following postal reform. For example, in Australia, the monopoly price threshold was reduced in 1994 from 10 times the basic stamp price to 4 times the price. In contrast to the United States, none of the eight countries give postal administrations exclusive access to the mail box.

Postal administrations in the other eight countries have greater freedom than the U. S. Postal Service to set postal rates. For example, in New Zealand, the postal administration is free to set prices except for standard letters which are subject to a price cap of the country's Consumer Price index minus one percent. In Canada, only certain rates, mainly those for letter mail and some publications, must be approved by the Canadian government.

Chairman Stevens, Chairman McHugh, and Members of the
Subcommittees:

We appreciate the opportunity to participate in this hearing on how the reform experiences of other countries' postal administrations may relate to ideas and proposals for reform of the U.S. Postal Service. We will discuss experiences of other postal administrations that are particularly relevant to any future decisions by Congress affecting (1) public service obligations, such as universal service and uniform rates; (2) the postal monopoly; and (3) regulation of postal prices.

My testimony is based primarily on our past and ongoing work relating to the responsibility of the U.S. Postal Service to provide uniform service to all communities in an increasingly competitive postal environment, as well as on issues involving the postal monopoly and postal rate setting in this country. We have also done limited work on other countries' postal administrations. To date, we have focused most of our attention on Canada Post. Canada's experience is especially relevant because of its proximity to the United States and its similarities in geographic size, business environment, and market-oriented economic systems. I will also refer to postal administrations in seven other countries on which we obtained data: Australia, France, Germany, the Netherlands, New Zealand, Sweden, and the United Kingdom. These countries, along with Canada, have been described by Price

Waterhouse in a recent study¹ as among the most "progressive postal administrations," and most of them have undergone reforms that changed their structure and operations in the past decade. Our testimony relating to other countries' experiences is based primarily on that study as well as data readily available from the other countries' postal administrations.

While we believe that the overall experiences of other countries' postal administrations are relevant to the current discussions of postal reform in the United States, meaningful comparisons of the specific operational practices followed and performance results can be difficult. Compared to each of the eight other postal administrations, the U.S. Postal Service's has at least seven times the mail volume, and at least twice the number of employees. All eight postal services combined have only one-half of the U.S. Postal Service mail volume, and just slightly more than the total number of its employees. The U.S. Postal Service handled about 180 billion pieces of mail in fiscal year 1995 and had over 850,000 employees in December 1995. By comparison, Canada Post has about 6 percent of the U.S. Postal Service's mail volume and about 6 percent of its number of employees. I have appended to my statement two graphics that illustrate the differences in mail volume and employment between the U.S. Postal Service and the other eight postal administrations.

¹"A Strategic Review of Progressive Postal Administrations: Competition, Commercialization, and Deregulation" (Price Waterhouse LLP, February 1995).

OTHER COUNTRIES' EXPERIENCES ARE RELEVANT
TO POSTAL REFORM IN THE UNITED STATES

Notwithstanding the differences in workforce size and mail volume, other countries' experiences with granting their postal administrations greater commercial freedom are relevant to current consideration for granting such freedom in the United States. For example, in 1992, we issued a report² describing how the competition from both private firms and electronic communication, particularly in the expedited-service mail and package-delivery markets, may create the need for statutory changes. Similarly, according to Price Waterhouse's February 1995 report, while many factors are driving postal reform in other countries, the increase in competition in the delivery and communications markets has, above all else, driven the changes.

Various parties, including some Members of Congress and the Postmaster General, have called for fundamental changes in the laws and regulations governing the U.S. Postal Service. The Postmaster General has said that the Postal Service needs greater freedom to set postage rates, manage the postal workforce, and introduce new products and services. Private delivery firms and U.S. mailers say they want more freedom to deliver letters now protected by the statutory monopoly. In recent hearings, Congress has been

2U.S. Postal Service: Pricing Postal Services in a Competitive Environment (GAO/GGD-92-49, Mar. 25, 1992).

presented with many ideas and some specific proposals for reforming and privatizing the Postal Service.

The 1970 Postal Reorganization Act, which created the U.S. Postal Service, was the most recent major change to the laws governing the structure and operation of the postal administration in the United States. Major change has occurred more recently for some foreign postal administrations. In the past decade, a number of other countries have restructured postal administrations from entities subject to close governmental control to entities that are still owned by the government, but with less governmental control over day-to-day practices. For example, in 1981 Canada established the Canada Post Corporation, an entity owned by the Canadian government but freed from many government regulations. Reform of postal administrations also took place in New Zealand in 1987, in Australia and the Netherlands in 1989, in France in 1991, in Sweden in 1994, and in Germany in 1995.

Following these reforms, postal administrations in many of these countries reported significant improvements in financial performance and service delivery. We will not discuss their performance or the effects of postal reform. However, I will highlight a key common feature--universal service--of the U.S. and other postal administrations after reform. I will also highlight variances in the characteristics of their monopolies and their ability to set postal prices. We believe that these three areas

universal service, the mail monopoly, and ratemaking--will be among the most challenging for Congress to address in any future reform of the U.S. Postal Service.

UNIVERSAL SERVICE REMAINS A COMMON GOAL
AMONG OTHER POSTAL ADMINISTRATIONS

The primary mission of the U.S. Postal Service, as it now exists in law, is to provide mail delivery service to persons in all communities and access to the mail system through post offices and other means. The rate for First Class mail, i.e. letters "sealed against inspection", must be uniform for delivery anywhere in the U.S. The U.S. Postal Service generally offers delivery to both urban and rural addresses six days a week. Any consideration of reforming the U.S. Postal Service will require a careful review of, and no doubt much debate on, how the current universal service mandate will be affected.

In all of the other eight countries, the postal administrations provided certain services widely to their citizens and at uniform rates before reform and continued to provide them following reform. However, the definition of universal mail service varies somewhat from country to country. Some of the countries provided the same level of service for urban and rural customers, while some others had different service standards for urban and rural areas. For example, although Canada Post is required by law to maintain

service that meets the needs of Canadian citizens, the service only needs to be similar for communities of the same size. Canadian citizens in very remote areas in the far north may receive mail delivery less frequently each week than those in some other areas of Canada.

In some countries, changes in universal service practices, involving such areas as the frequency of delivery and access to post office services, have been controversial. For example, in New Zealand, citizens in rural communities were upset when they learned New Zealand Post wanted to discontinue delivery services to rural addresses. The Post then increased a longstanding rural delivery fee for service, paid by the addressee; this decision proved unpopular, and the fee was eliminated in 1995.³ There continues to be no rural delivery fee in New Zealand.

Accessibility to postal services, which includes maintenance of local post offices in the United States, is also part of the public service obligation of postal administrations in some other countries. The U.S. Postal Service must follow strict legal criteria in determining whether to close post offices. In New Zealand, the postal administration has negotiated a written agreement with the government that specifies the minimum number of postal retail outlets. In the Netherlands, Dutch law specifies

³New Zealand Post estimated the 1-year cost of eliminating the rural delivery fee at between \$7 and \$8 million (NZ dollars).

minimum requirements regarding the density of post offices in urban and rural areas.

Five of the eight countries' postal administrations differ from the U.S. Postal Service in that a majority of their postal retail outlets are privately owned and operated, according to the February 1995 Price Waterhouse report. This group includes Australia, Canada, the Netherlands, New Zealand, and the United Kingdom. Except for the French postal administration, all of the eight foreign postal administrations have some form of franchising policy for postal retail services.

Like the U.S. Postal Service, other postal administrations have also continued to provide certain subsidized services. For example, in Canada, the government compensates Canada Post for providing subsidized rates for publications, parliamentary mail, and literature for the blind. In Sweden, the government subsidized certain services, such as free delivery of literature to the blind, while the postal service subsidizes the distribution of certain newspapers and provides discounts on association letters.

We plan to issue a report shortly on the U.S. Postal Service's role in the international mail market, including issues that have been raised by both the U.S. Postal Service and its major competitors, such as Federal Express and DHL Airways. The Postal Service participates in the Universal Postal Union, a specialized agency of

the United Nations that governs international postal services. Its basic purpose is to help postal administrations fulfill statutory universal service obligations on an international level. A total of 189 Universal Postal Union member countries have agreed to accept mail from each other and to deliver the international mail to its final destination.

THE SCOPE OF POSTAL MONOPOLIES VARIES

The Postal Service has said that current universal service obligations and related public service mandates can only be met if its markets continue to be statutorily protected by the Private Express Statutes that provide the Service with a monopoly over letter mail. We plan to issue a report in the coming months that discusses the Postal Service's monopoly in detail, including the growth since 1970 of private delivery firms that are competing and will likely compete more strongly in the future for some of the Service's First-Class, Priority, and Third-Class mail.

The postal monopoly is defined differently and varies widely in scope among the eight foreign postal administrations. In this country, the letter mail monopoly helps ensure that the Postal Service has sufficient revenues to carry out public service mandates, including universal service. The U.S. postal monopoly covers all letter mail, with some key regulatory exceptions being "extremely urgent" letters (generally next-day delivery) and

outbound international letters. Postal Service data indicates that, in fiscal year 1995, at least 80 percent of the Postal Service's total mail volume was covered by the postal monopoly.

All but one (Sweden) of the eight countries' postal administrations have monopolies over some aspects of the letter mail. Generally, the letter monopolies in other countries are defined according to price, weight, urgency of delivery, or a combination of these factors.⁴ For example, in Canada, the postal monopoly covers letters, with a statutory exclusion for "urgent" letters transmitted by a messenger for a fee that is at least three times Canada's regular rate of postage. In Germany, the monopoly covers letters priced up to 10 times German's standard letter rate. The postal monopoly in France covers letters and those parcels weighing less than 1 kilogram (2.2 pounds). In the United Kingdom, the monopoly is defined by price, covering those letters and parcels with postage up to one British pound.

Australia and New Zealand narrowed the scope of their postal monopolies after reform. For example, in Australia, the monopoly price threshold was reduced in 1994 from 10 times the basic stamp price to 4 times the price. Other changes were also made, such as reducing the weight threshold from 500 grams to 250 grams and the excluding of outbound international mail. Australia Post reported

⁴There are various exclusions to the postal monopoly in each country.

in its 1994 annual report that these changes "will reduce the proportion of total business revenue from reserved services from around 60 percent to about 50 percent." It now receives a majority of its revenues from services open to competition. Australia plans a review of the remaining postal monopoly during 1996-1997. In New Zealand, the monopoly price threshold was reduced in phases over 3 years, and the government announced in November 1994 that it would introduce legislation to completely deregulate the postal market. While no final decision has been made, New Zealand Post officials said last year that they had shaped their business plans to expect an open, competitive environment.

Sweden has eliminated its postal monopoly. Full competition for all postal and courier services, including the delivery of letters and parcels, has been allowed in Sweden since January 1, 1994. Sweden Post officials told us that its monopoly offered little protection of postal revenue and enforcement was not cost-effective. The Swedish government, not the postal administration, has the obligation to provide universal mail service.⁵

The U.S. Postal Service and some other postal administrations have made efforts to enforce their postal monopoly. The U.S. postal monopoly has proved difficult to enforce for a number of reasons, including objections by both mailers and competitors to the Postal

⁵The Swedish government currently contracts exclusively with Sweden Post to provide universal service but may extend this arrangement to other competitors if they achieve sufficient scope.

Service's audits and other enforcement actions. We were informed by Canada Post officials that Canada Post also finds its monopoly difficult to enforce. They said that while Canada Post has taken legal action against major violators of its postal monopoly, it prefers to use other means of persuasion to get violators to comply with the law.

Enforcement problems can also be related to the way the postal monopoly is defined. For example, in France, an exclusion limits the letter mail postal monopoly to private correspondences. Since letters are sealed against inspection, thus making it impossible to determine whether they are private correspondences, enforcement is difficult.

Finally, a monopoly on mail box access in the United States is related to the Postal Service monopoly on delivery of letter mail. By law, mail box access is restricted to the Postal Service. In contrast, none of the eight countries we reviewed have laws that give their postal administrations exclusive access to the mail box.⁶

⁶There may be certain types of limited access to mail boxes in some countries. For example, in Canada, if Canada Post owns the mailbox, it is locked, and thus only Canada Post has access to it. This also applies to some centralized apartment mail boxes in secure buildings.

POSTAL ADMINISTRATIONS IN SOME COUNTRIES
HAVE BEEN GIVEN GREATER FREEDOM TO SET POSTAL RATES

We issued a report late last year on postal ratemaking,⁷ which updated our 1992 report, saying that, if the Postal Service is to be more competitive, it will need more flexibility in setting postal rates. In our opinion, legislative changes to the 1970 Act's ratemaking provisions may be necessary in order to give the Postal Service greater flexibility in setting rates. In our 1992 report, we said that Congress should reexamine the 1970 Act to (1) determine whether volume discounting by the Postal Service would be considered a discriminatory pricing policy and (2) clarify the extent to which demand pricing should be considered in postal ratemaking. In our latest report, we reiterated these points and also discussed alternatives which Congress could consider for improving the ratemaking process.

Postal administrations in the other eight countries appear to have greater freedom to establish and change postal rates than does the U.S. Postal Service. In Canada, only certain rates, mainly those for full price letter mail and the mailing of publications at government-subsidized rates, must be approved by the Canadian government. In addition, rate proposals are not subject to an independent regulatory body as they are in the United States. In

⁷U.S. Postal Service: Postal Ratemaking in Need of Change (GAO/GGD-96-8, Nov 15, 1995).

Canada, interested parties have an opportunity to provide information, but the rate-setting process is not public, and parties do not have access to costing data or other information underlying postal rates.

In Sweden, the postal administration is free to set all prices except for the standard domestic letter; the government and the postal administration have agreed to a price cap on the domestic letter rate equal to the standard consumer rate of inflation. Similarly, in New Zealand, the postal administration is free to set prices except for standard letters, which are subject to a price cap of the country's Consumer Price index minus one percent.

The Australian postal administration sets its own prices. The government can "disapprove" of the basic postage rate proposed by Australia Post. In addition, Australia Post must notify an independent authority of proposed increases in the prices of monopoly services. The authority has only an advisory role and in the past has instituted inquiries into proposed increases lasting up to 3 months.

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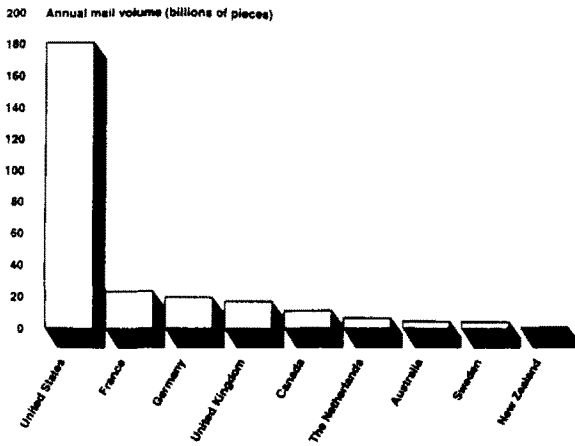
Finally, while we have focused on three complex and interrelated issues of universal mail service, the postal monopoly, and postal rate setting, there are other issues that will also require

reevaluation in any future reform initiative. These include, but are not limited to, the quality of the Postal Service's labor relations. We previously reported⁸ that Congress may need to reconsider the collective bargaining provisions of the 1970 Act if the Postal Service and its major employee organizations are unable to resolve some long-standing problems. As the Congress continues its deliberations on postal reform, we believe that it is important to examine the interrelationships of these issues and how changes addressing them may affect postal operations and related services to the American public and business.

This concludes my prepared statement. I would be happy to respond to your questions.

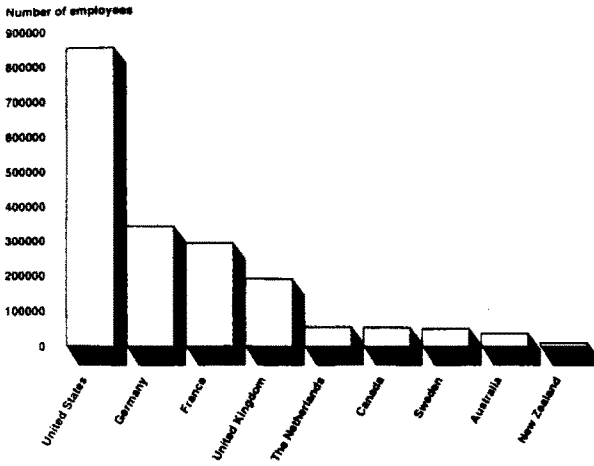
⁸U.S. Postal Service: Labor-Management Problems Persist on the Workroom Floor (GAO/GGD-94-201 A and B, Sept. 29, 1994).

Figure 1: Mail Volume for U.S. Postal Service and Postal Services in Eight Other Countries



Source: U.S. Postal Service, foreign postal administrations, February 1995 Price Waterhouse report: A Strategic Review of Progressive Postal Administrations.

Figure 2: Employment of U.S. Postal Service and Postal Services in Eight Other Countries



Source: U.S. Postal Service, foreign postal administrations, February 1995 Price Waterhouse report: A Strategic Review of Progressive Postal Administrations.

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Price Waterhouse LLP

**STATEMENT OF JAMES A. WADDELL, PARTNER
PRICE WATERHOUSE LLP**

and

**DAVID E. TREWORGY, PRINCIPAL CONSULTANT
PRICE WATERHOUSE LLP**

before the

SUBCOMMITTEE ON POST OFFICE AND CIVIL SERVICE

**Committee on Governmental Affairs
United States Senate**

and the

SUBCOMMITTEE ON THE POSTAL SERVICE

**Committee on Government Reform and Oversight
United States House of Representatives**

January 25, 1995

HEARING ON USPS REFORM — THE INTERNATIONAL EXPERIENCE

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Mr. Chairmen and Members of the Subcommittees:

I am grateful for the opportunity to participate in this hearing on the experiences of foreign countries in reforming their postal systems. My name is James A. Waddell, and I am a partner with Price Waterhouse LLP. Since 1982 I have participated in a variety of consulting assignments for the United States Postal Service, primarily in the areas of cost analysis, strategic assessment, and delivery performance. I have testified before the Postal Rate Commission regarding the Postal Service's requests for rate changes in three different proceedings. Over the last ten years I have been very actively involved in planning and implementing privatization activities around the world, and since 1991 have served as Executive Director of Price Waterhouse's International Privatization Group. With me today is David E. Treworgy, a Principal Consultant with Price Waterhouse. David has focused on consulting assignments for the Postal Service since 1988. He was the lead investigator on a number of projects that are relevant to today's hearing, including the report we issued in February 1995, entitled "A Strategic Review of Progressive Postal Administrations: Competition, Commercialization, and Deregulation." That report forms the basis for our testimony today. A more complete statement of our qualifications is attached to this statement.

Twenty-five years ago, at the time the Postal Reorganization Act of 1970 was passed, the United States was on the cutting edge of postal organization and regulatory oversight. Since that time substantial changes have occurred in the market for postal services. Traditional competitors, such as the United Parcel Service (UPS), Federal Express, and DHL, have proliferated, and new forms of

electronic competition through facsimile transmission and electronic mail have been commercialized and become widespread. New products and services have been developed by postal administrations offering to meet a variety of service standards. New technologies have emerged to help the Postal Service and its competitors to provide service, such as optical character readers, bar code sorters, and remote bar coding systems. In short, the postal environment is more competitive and technology has transformed the nature of the market. An obvious question to ask is whether the reforms adopted in 1970 continue to be relevant in this new environment.

The Postal Reorganization Act (PRA) envisioned a world largely devoid of competition. One of the principal missions of the Postal Service was, and continues to be, to provide universal service at uniform rates throughout the United States. In this environment, the Postal Service was given the exclusive right to deliver letter mail and, in return, the responsibility to serve every address in the country. The advent of competition has put the Postal Service's market position at risk, particularly in lower cost markets where profits are earned. The traditional monopoly of the Postal Service has strengthened the unions that represent its employees and made competition ever more attractive. The regulatory structure created to protect consumers from the monopoly has proven cumbersome — especially as it regulates competitive services. The Postal Service has incurred substantial losses since the passage of the PRA and is struggling to build its equity to a positive position. In view of these challenges, the goal of universal service may be better served by a different structure or different operating rules for the postal sector generally.

The challenges faced by the United States in the postal sector are similarly found in many other countries. Like the United States, these countries are concerned whether competition will provide a mechanism to reduce costs and improve efficiency within the government's postal administration or whether competition will skim the cream off the postal administration's business and threaten its ability to ensure universal service. Many of these countries have taken steps to address the issues in the postal sector by increasing the scope of competition, increasing management's authority and accountability, or in other ways.

You have heard a substantial amount of testimony over the last year from various parties regarding the challenges facing the Postal Service. In addition, you have heard proposals for dealing with these challenges. To help you in evaluating this information, I would like to highlight some of the major findings from a report that we published last year, entitled "A Strategic Review of Progressive Postal Administrations." This report, which has been provided to the subcommittees previously, examines policy developments in eight countries that are facing similar pressures on their postal administrations as we face in the United States. The Annex to this testimony provides a brief summary of major findings in each country, as well as an update on developments during 1995.

The major trends that emerge from our review of practices in other countries are the following:

- The monopoly position held by the postal administration is under pressure in many countries. Increased competition is the norm, including competition from other postal administrations.

- Postal administrations are being corporatized and given greater commercial freedoms. This trend is manifested in greater authority to set prices, introduce new services, acquire subsidiaries, and raise capital. Also noted is an increased accountability for management, through incentive systems that reward good performance and penalize poor.
- Combined with the greater pricing freedom noted above is a trend toward the use of price caps. Price caps generally allow the postal system to adjust prices without regulatory review, provided that the price increase does not exceed the country's inflation rate (or some lesser percentage reflecting the ability to improve efficiency).
- In many countries, there is a trend toward increasing efficiency by downsizing the labor force. This trend, of course, can be noted in many different sectors of countries' economies. In the postal sector, downsizing is often a response to increased competition and the increased availability of technology.
- Many countries are considering privatization or some partial ownership of the postal system. Only two countries have actually sold shares to the public, the Netherlands and a country which was not reviewed in our report, Singapore. In both cases, the government sold a portion of the shares of its combined telecommunications and postal authority. While the governments of the Netherlands and Singapore are the only two that have sold shares to the public, several other countries have held serious discussions toward that end, most notably the United Kingdom, Germany, and Argentina.¹

The principal findings of our review of government policies toward postal administrations are summarized in Exhibit 1. We have also included a column representing the current policies of the United States with respect to the issues presented. As you can see, the United States Postal Service is different in several significant respects from other administrations. In three dimensions the US Postal

¹ The United Kingdom Government published a green paper on Post Office privatization in June of 1994 that recommended selling off 51 percent of the equity in Royal Mail and Parcelforce. While the plan was shelved in the following months as a result of internal discord within the conservative party, Prime Minister John Major plans to reintroduce the legislation should he win reelection.

Germany is actively committed to privatization of Deutsche Post AG as part of a multi-year plan to privatize both the telecom and postal sectors. The telecom sector is planning for a sale of shares in 1996; the postal service is scheduled to follow in 1998.

Argentina's Senate approved a bill in November 1994 to privatize the state postal service by the end of 1995. Details of the privatization are currently being debated by the full Congress. At present, it appears that if the outstanding issues are successfully resolved, a 30-year postal concession would be sold in mid-1996.

Service is unique: its employees do not have the right to strike, it retains a monopoly over patrons' mailboxes, and it is not permitted to hold subsidiaries.

The reforms developed and implemented by these eight countries in reaction to pressing business challenges suggest some potential paths to the United States Postal Service in creating a business environment capable of withstanding market challenges now and in the future. In the balance of my remarks, I would like to take the opportunity to outline the major themes of postal reorganization that can be identified among these countries that have the most relevance to the United States.

Comparison of the United States postal sector with that of other countries offers valuable lessons, though the exercise must be completed with some care and recognition of differences in industry structures across nations. While the postal system in the United States is similar in many fundamental respects, such as basic product and service offerings, operational processes, and technology, certain characteristics do set it apart. For example, in terms of sheer volume, the United States Postal Service handles roughly twice as many letters each year than all the eight postal administrations *combined*. While size does not necessarily change the impact of many policy prescriptions, in the sense that the postal sector accounts for approximately the same percent of GDP in each country and the United States is simply a larger economy, the magnitude of the United States Postal Service in terms of volume and geography does give rise to certain significant differences. For example, a major element of planned reform in the European Community is elimination of the monopoly on cross-border mail. In Europe, this reform is significant because cross-border mail can account for a substantial portion, up to

five, ten, or more percent of a nation's mail by virtue of the relatively small sizes of the countries in terms of population and geography. In the United States, by contrast, international mail accounts for only one-half of one percent of total mail volume; hence, such as reform would have little impact on the organization.

Bearing in mind the striking similarities, yet real differences, I would like draw on the reforms of the eight progressive postal administrations to suggest three principles of particular relevance for application to the United States:

1. Create a more businesslike organizational structure
2. Increase pricing flexibility
3. Introduce change incrementally but meaningfully

These three principles are important to bear in mind in evaluating potential postal reform. I will address each briefly as it relates to the United States.

1. Create a more businesslike organizational structure

As competition from traditional and electronic sources increases, it is critical that the United States Postal Service operate under a structure that is able to make rapid responses to changing conditions. Only in this way can it fulfill its goals of providing universal service within a financially viable organization and meet its service commitments to customers. Many of the foreign postal administrations we reviewed have worked toward achieving these objectives by recasting themselves as what might be characterized as businesslike agencies with strong social

mandates to provide universal service at uniform letter rates. As such, they exhibit many similarities to commercial enterprises, including profit orientation, freedom to diversify product lines to meet customer requirements, ability to form joint ventures, sanction to own subsidiaries, and authority to borrow in the private capital markets. ^{money}

Internationally, the trend toward commercialization applies to all eight postal administrations we reviewed, but can be illustrated especially well by the Netherlands and New Zealand, which have completed dramatic corporatizations and demonstrated substantial benefits to these actions.

For example, the Dutch government privatized the postal service, PTT Post, in two public offerings that resulted in over 50 percent ownership of the holding company, Royal PTT Nederland NV (KPN), by individuals or private institutions. With a majority of shares held outside the government, the organization is clearly accountable for its performance. With a strong commercial mandate, PTT Post has become one of the most aggressive players in the international mail market, successfully capturing market share from sister postal administrations, including the United States Postal Service. PTT Post has actually opened offices in several foreign countries, including the United States. The U.S. Postal Service has no such offices abroad.

In New Zealand, the government transformed New Zealand Post (NZ Post) into a "State-Owned Enterprise" in 1987. The reform allotted 120 million shares of NZ Post's equity to the Ministers of Finance and State-Owned Enterprises. Following share allotment, NZ Post dramatically restructured its organization and product

lines. Efficiencies gained through restructuring permitted NZ Post to *lower* postage rates once in 1989 and a second time in 1995. Moreover, NZ Post paid the government a dividend of 21 cents (NZ) per share for the most recent fiscal year.

For the United States, a businesslike organizational structure could include corporatization of all or part of the Postal Service. This structure would be conducive to promoting a profit orientation throughout the Postal Service and rewarding managers that helped to achieve the goals of the business.

Corporatization would also permit the Postal Service to acquire subsidiaries, form joint ventures, and raise capital. Against these benefits, there are additional implications from corporatization that may be positive or negative but certainly warrant further consideration. Principally, corporatization could subject the Postal Service to the same laws that apply to other enterprises unless the new corporation were to be specifically exempted. The laws with the most far-reaching implications would include labor legislation, the tax code, and the antitrust laws. In addition, the corporate governance of the Postal Service would likely change with a Board of Directors replacing the Board of Governors. We have not examined in detail the effects these changes would have.

2. Increase pricing flexibility

Increasing the commercial orientation of the Postal Service through structural changes raises the issue of how much flexibility management would have in setting the prices of its services. Currently, prices are regulated by the Postal Rate Commission. The communications and delivery market is fast-paced, with competitors rapidly deploying new products and pricing structures that adroitly outmaneuver the Postal Service's ten-month rate case process. For example, earlier this month United Parcel Service announced a major restructuring of prices that will take effect next week on Saturday, February 3. The Postal Service may require as long as two years to prepare and file a rate case; by then market conditions are almost certain to have changed several times.

The international record reveals that many postal administrations have greater latitude in rate setting. In Sweden, price increases are subject to a price cap, but not review by an independent regulatory body. The New Zealand, Dutch, and French postal services are subject to statutory guidelines that cap rate increases for monopoly products, but, as with Sweden, do not face independent regulatory commissions. Unique among the countries we surveyed, Canada Post adjusts prices with neither the constraint of a price cap nor the oversight of a regulatory body (though the ministry approves certain letter and publication rates). In countries where they do exist, price restrictions tend to cover only monopoly products and take the form of price caps. New Zealand, as I previously mentioned, not only has adhered to its price cap but actually reduced prices.

Price caps have proven to be an effective means of regulating prices in other industries and in the postal systems of other countries. Price caps increase management's flexibility relative to traditional cost of service regulation, and increase the speed of price adjustment, which is important in competitive markets. Consumer protection is not abandoned, since prices will remain constant or even decline, relative to inflation. Adoption of price caps or another form of pricing flexibility should be considered for the Postal Service.

3. Introduce change incrementally but meaningfully

Because the organization is a large enterprise directly affecting over approximately 800,000 workers as well as roughly 250 million customers (both mailers and consignees), change to the United States Postal Service should be implemented with care and planned on a long-term basis. While unaggressive reforms that only tinker will overlook fundamental problems, rash initiatives that proceed too quickly without being carefully thought out could disrupt an institution of far-reaching significance.

The international experience testifies to a record of reaching substantial goals through incremental reform and an articulated, long-term strategy. In the United Kingdom, the government gradually reformed the Post Office over a ten year period. Early steps involved spinning off telecom operations and subsequently removing banking services. Barring political interference, the final phase of reform would have culminated in offering majority stakes of Royal Mail and Parcelforce to the public.

In Germany, the government has consistently pursued a reform timeline that began with "Postreform I" in 1989. This early initiative separated postal, banking, and telecommunication services. Three years later, "Postreform II" commercialized the postal service by making it a public corporation, with 100 percent government ownership. Currently, the government is preparing outlines for deregulation and eventual privatization in the reform's final phase, "Postreform III."

A potential application of principles to the United States Postal Service

In applying these three principles — businesslike organizational structure, pricing flexibility, and incremental change — to the United States, I might suggest an initial step of reorganizing the Postal Service's competitive businesses — Express Mail, Priority Mail, and Parcel Post — into a deregulated, wholly-owned subsidiary. (Note that transfer prices charged for services provided by the parent would still have to be regulated to ensure no cross-subsidization of competitive products by monopoly products.) This action would create a commercialized environment, both in terms of a businesslike organizational structure and pricing and product flexibility, that would allow the company to compete on a level playing field in the marketplace. The change would be incremental in the sense that the subsidiary would represent only ten percent of the Postal Service's \$55 billion in revenues. Yet, the change is substantial because even ten percent is still a \$5 billion business of sufficient magnitude to compete with private sector organizations. Perhaps a year down the road, selling a small initial tranche of equity in the public market would achieve the dual objectives of raising revenue for the Postal Service and of

providing management and employees with a real market indicator of the success of the company.

By taking a "go slow" approach that initially affects only ten percent of the business, the lessons learned by the Postal Service and its constituents could be applied a year or two later in a second, planned phase to the other 90 percent of the organization. Options for this second phase could focus on corporatizing the remainder of the organization into one or more corporations and developing structural and regulatory policies that are consistent with the degree of competition that each of the products and services faces. Reform of the primary products — First-Class Mail and third-class mail — could include price cap regulation of monopoly products. Shares in a fully corporatized postal organization could be initially held by the federal government for potential partial or full sale in the future.

Although on the surface, the delivery of mail may appear to be a simple activity, the diversity of products and customers, the unique aspects of the economics of delivery networks, and the large number of individuals and businesses with a stake in the change process combine to make reform of the United States Postal Service a challenging endeavor. I commend you for taking these first steps toward responding to current issues facing the Postal Service.

This concludes my prepared statement. I would be happy to respond to your questions.

Autobiographical Sketches

James A. Waddell is a partner with Price Waterhouse LLP (hereafter Price Waterhouse), located at 1616 North Fort Myer Drive in Arlington, Virginia. From 1977 to 1979, Mr. Waddell was a Field Examiner with the National Labor Relations Board. In 1979, he joined Price Waterhouse and was promoted to partner in 1988.

Mr. Waddell currently serves as partner in charge of Price Waterhouse's Finance and Economics Consulting Group, which includes the International Privatization Group. Mr. Waddell has 15 years of experience in infrastructure finance and privatization, including projects in the postal, electric utilities, telecommunications, transportation, and water and waste sectors.

Since 1982, Mr. Waddell has conducted extensive work for the United States Postal Service in the areas of cost analysis, strategic assessment, and delivery performance. He testified before the Postal Rate Commission on behalf of the United States Postal Service in Dockets R84-1, R87-1, and R90-1. Mr. Waddell also served as director of the USPS External First-Class Measurement System (EXFC), an independent quality assessment project designed to quantify inter- and intra-city domestic mail performance for the United States. In addition, he serves as project partner for strategic planning projects Price Waterhouse conducts for the U.S. Postal Service. Mr. Waddell has also conducted work internationally in the postal sector for Post Danmark and Zambia Post and Telecommunications Corporation.

Mr. Waddell holds a B.A. in economics with Highest Distinction from the University of Virginia, an M.S. in industrial and labor relations from Cornell University, and a M.A. in economics from Georgetown University.

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Mr. Treworgy has conducted substantial financial and economic analysis in the area of transportation costs for the Postal Service, including testifying before the Postal Rate Commission in Docket MC95-1. In addition, he conducts market research and new product development work for promising potential service offerings. In the area of strategic planning, he has conducted benchmarking and financial forecasting work for the Postal Service.

Mr. Treworgy has given presentations at several international postal conferences, including one which resulted in publication of the paper, "Postal Service and Developing Countries." Also internationally, he has been involved in work for several foreign postal administrations, most recently in 1995 in a strategic review for the board of directors of An Post, the Irish national postal service.

Mr. Treworgy holds a B.A. with honors in Economics from Williams College and an MBA from the Graduate School of Business Administration at Harvard University.

Annex

Since publication of the "Strategic Review of Progressive Postal Administrations" in February 1995, new developments have altered the postal administrations of many countries. The following analysis identifies important developments and summarizes the key attributes of each nation's policy environment with respect to postal services.

Australia

The Australian government has actively liberalized Australia Post (AP) as part of a larger attempt to deregulate and commercialize the public sector. The government's first phase of deregulation occurred in 1989, when the *Australian Postal Corporation Act* established AP as a "Government Business Enterprise." The next stage of government review, originally scheduled for 1996-1997, may occur as early as July 1996. The outcome of the review is uncertain though it seems likely to continue gradual erosion of the postal monopoly.

Australia Post is free to set prices, with the exception of monopoly products, which are constrained by a price cap equal to the price index less a productivity factor. Though the government has not yet defined the productivity factor, AP has agreed to freeze rates until 1997, at which time the government will revisit the issue. Whenever increasing rates, AP consults the Prices Surveillance Authority (PSA). While the PSA serves an advisory role and does not have the authority to prohibit

rate increases, its inquiries nonetheless prolong rate increases and can result in recommendations that are politically difficult to ignore.

One of AP's more ambitious recent endeavors has targeted the financial services sector. In 1995, Australia Post launched a multi-user electronic banking network that allows customers from a consortium of banks to use postal outlets as banking sites. The venture highlights Australia Post's attempt to leverage its retail presence by broadening existing products in the financial services market.

Canada

In 1981, the former Post Office Department of the Canadian government became Canada Post Corporation (CPC), a federal Crown corporation with significant commercial freedoms. The Canadian government announced in November 1995 that it would conduct a review of Canada Post's mandate. Now underway, the review aims to define the long term mission of Canada Post as well as assess the organization's ability to react in an increasingly competitive environment.

CPC has significant pricing freedom relative to other postal administrations. Though CPC gives interested parties an opportunity to submit appeals when setting rates for letter mail and certain categories of publication mail, the organization establishes prices without official review by an independent regulatory body (rate increases on letter mail are subject to final approval by the ministry).

France

The French postal service, La Poste, separated from its telecommunications counterpart and from the central French Administration in 1991; it currently operates as a government-owned corporation. Though there is no statutory limit on rate increases, an agreement between La Poste and the Ministries of Industry and Finance caps increases through 1997 at the retail price index.

In the absence of a regulatory commission that oversees pricing, competitors have filed legal suits that allege unfair competition. Accusations of cross-subsidy and anti-competitive practice are gaining credibility with the European Court, which in September re-opened a case filed against La Poste that had previously been settled in La Poste's favor. Despite complaints, La Poste continues to introduce new financial products, including life insurance and deposit accounts, and announced plans to automate its financial services network.

Germany

In Germany, the government has systematically pursued phased deregulation of its postal, telecommunication, and banking sectors. The first phase, Postreform I, gave organizational independence to formally joined postal, banking, and telecommunication services in 1989. Postreform II followed in 1995, turning the German postal service, Deutsche Post AG (Deutsche Post), into a fully owned government corporation. Postreform III, scheduled to take place within the next few years, will result in a share offering of Deutsche Post. Despite planned

liberalization, Deutsche Post's tariff increases are still subject to rigorous oversight from the federal Ministry for Post and Telecommunications.

In preparation for deeper reform, the postal minister recently unveiled an outline of legislation which would begin deregulating the postal market in 1998 and introduce full competition in 2003. Prior to the outline's publication, Deutsche Post's chairman indicated in March 1995 that the organization should be able to float shares on the stock exchange in 1998.

A hurdle that Germany was required to overcome in order to develop postal sector privatization plans was the issue of the postal administration's large unfunded pension liability, estimated at over DM 60 billion (\$40 billion US). As a solution to this problem, Deutsche Post will be required to contribute payments to the pension fund at a rate typically experienced by the private sector, while the government will meet any shortfall.

In the face of upcoming deregulation, Deutsche Post is attempting to acquire its former sister organization, Deutsche Postbank AG (Postbank). The two organizations were formally united as a single government entity until 1989, when government reforms gave each managerial autonomy. By acquiring Postbank, Deutsche Post hopes to promote financial transactions in its retail network and preserve its long term presence in the financial services market.

The Netherlands

The Dutch postal service, PTT Post BV (PTT Post), is a subsidiary of holding company Koninklijke PTT Nederland NV (KPN). KPN became a wholly government-owned corporation on January 1, 1989 and its stock currently trades on public exchanges in Amsterdam and New York. Through an initial public offering in June 1994, the government lowered its ownership stake to approximately 70 percent; in October 1995, KPN's second stock offering lowered the government's stake below 50 percent.

PTT Post's rate setting is free of regulatory oversight, with the stipulation that rate hikes not exceed increases in the Dutch national wage index. Competitor complaints of unfair pricing have recently complicated PTT Post's price setting latitude. In response to complaints from PTT Post's competitors alleging unfair pricing, a Dutch government ministry is trying to remove bulk reductions and VAT exemptions given by PTT Post to mail order companies.

Competitive threats to the monopoly increased further when Algemene Postdienst Nederland (APN), a Dutch alternate delivery firm, announced plans to begin delivering bulk mailings in the Netherlands. APN plans to undercut the PTT Post's rates and deliver as many as one million items per week. To expand its market presence in an increasingly competitive environment, PTT Post recently purchased two expedited carrier firms and has plans to increase the number of franchised postal outlets. PTT Post also plans to decrease its work force by 9,000 employees over the next five years (current employment stands at 55,263 staff).

New Zealand

The postal service of New Zealand became a State-Owned Enterprise in 1987 and ever since has operated with the stated goal of being as profitable and efficient as a private sector business. New Zealand Post Limited (NZ Post) establishes most tariffs without regulatory interference; when setting rates for standard letters, NZ Post must abide by the Deed of Understanding which stipulates that postage increases for letter mail may not exceed growth in the Consumer Price Index minus one percent.

In the period following corporatization, NZ Post has aggressively implemented personnel and organizational restructuring. In 1995, efficiency improvements gained through restructuring permitted the organization to lower postage rates from 45¢ to 40¢ (NZ). The government of New Zealand is currently contemplating legislation that would completely eliminate the letter monopoly. Although the proposal has the full support of NZ Post, political factors have handicapped speedy legislative action.

Sweden

The Swedish government removed monopoly protection for Postverket (Sweden Post) in 1993. During the past three years of unrestricted competition, Sweden Post's primary competitor has been CityMail, a household delivery firm operating in Stockholm and Lidingö. On April 20, 1995, Sweden Post acquired 75 percent of

CityMail. At the time of the acquisition, Sweden Post agreed to enter an on-going consultation process with the government that would establish clear-cut guidelines for future competition. CityMail executives accepted the acquisition, arguing that since CityMail would operate as an independent subsidiary of Sweden Post, no operational changes would result from the sale. After recording a loss of SEK 29 million (\$4 million) on sales of SEK 28 million (\$7 million) for the first nine months of 1995, CityMail entered into liquidation in December 1995, leaving uncertain the future of competition in the Swedish sector.

One important aspect of Sweden Post's relationship with CityMail concerned tariffs. CityMail often accused Sweden Post of predatory pricing in areas where CityMail competed against the former state monopoly. No regulatory agency oversees Sweden Post's rate setting behavior; instead, the government and Sweden Post have agreed to a price cap for the domestic letter rate equal to the standard consumer rate of inflation.

United Kingdom

Originally, the Post Office operated jointly with banking and telecommunication operators. After the government privatized the telecom in 1986 and banking services in 1990, the government in 1992 announced it was reviewing the possibility of privatizing the Post Office and Parcelforce. Political opposition from Members of Parliament who feared a reduction in service eventually halted the privatization initiative in 1994.

In May 1995, the President of the Board of Trade, Michael Heseltine, revisited postal reform by announcing new commercial freedoms for the Post Office. Though the reforms fall short of genuine privatization, they include relaxed limits on capital spending and the ability to enter joint ventures with private sector firms. The Post Office embraced these reforms while calling for deeper reform and renewed interest in privatization. Prime Minister John Major has publicly stated he will reopen the issue of privatization if re-elected.

Currently, the Post Office must seek government approval for tariff increases and its price changes are monitored by the Department of Trade and Industry. Debate regarding future Post Office reforms suggests the Post Office may receive a more structured approach to tariff setting and introduction of a price index formula as a cap on rate increases.

Though substantial reforms have not taken place, the Post Office has exercised its new freedoms to partner with private sector firms and introduce a range of new products, including hybrid mail, money wire transfer, travel insurance, and currency exchange. While expanding its product range, the Post Office is seeking to improve the efficiency of retail operations by installing an automated system for welfare disbursement. Once installed, the system will provide an electronic network of potentially 20,000 computer-linked outlets.

Argentina

As part of an economy-wide initiative to increase efficiency and government revenue, the Argentine government is planning to privatize the state-owned postal administration (Correo Argentino). In November 1994, the Argentine Senate approved a bill that proposed selling a 30-year concession to run the nation's postal service and regulate the private mail sector. Critics of the bill complained that it puts senseless restrictions on new private companies wanting to enter the market and makes a single organized crime figure the only person qualified to bid for the concession. Political disputes surrounding the bill have stalled progress towards privatization.

Despite the slow movement towards privatization, Correo Argentino has moved quickly to improve the efficiency and service quality of its operation. In 1993, new management entered the organization and reduced the workforce from 27,000 to approximately 20,000 staff. Following the restructuring, employees received rigorous training and post offices underwent major remodeling that included introduction of new technologies. Gradually, Correo Argentino has succeeded in slowing the decline in its mail volume and regaining former customers.

Denmark

Denmark's postal sector has recently experienced legislative reform that opens the way for monopoly deregulation and fosters a commercial outlook at the postal administration. Passed in 1995, the *Postal Activities Act* fixes the reserved area at

250 grams or six times the price of a 20 gram letter for items weighing less than 250 grams. The act could potentially open the monopoly as it gives the minister responsible for postal matters the authority to alter the reserved area, including the authority to remove the monopoly in international mail.

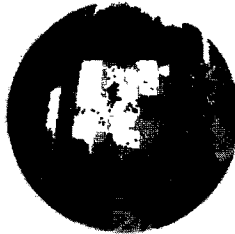
Another 1995 bill, the *Post Danmark Act*, officially transformed Denmark's postal organization from a government department to a semi-autonomous corporation fully owned by the government. Renamed Post Danmark, the postal administration has greater flexibility and an unambiguous commercial mandate. The new organization reports directly to the Board of Trade and Industry and assumes its own liability.



**A Strategic Review of Progressive
Postal Administrations**

Competition Commercialization and Deregulation

February 1995



Price Waterhouse LLP

OMEGA
PARTNERS



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Executive Summary

This document summarizes the major findings of a report describing the current status of ten postal administrations at the forefront of a general move towards postal corporatization and deregulation. The postal administrations (PAs) included in this study are Australia Post, Canada Post Corporation, La Poste in France, Deutsche Post AG in Germany, PTT Post BV in the Netherlands, New Zealand Post Limited, Sweden Post, The Post Office in the United Kingdom, Correo Argentino, and the Danish Post.

In most of the ten countries surveyed, significant legislative reform has occurred in the last six years. As a result, most of these postal operators are mandated to earn a profit and are given considerable freedom to conduct financial transactions. Most also participate in joint ventures and own subsidiaries which provide non-monopoly services. In spite of corporatization and increasing pressures to liberalize postal markets, all of these PAs, except Sweden Post and Argentina Post, have maintained a monopoly over letter mail services. The monopoly is generally defined by weight, price, or both. Even with these statutory monopolies, all of the postal administrations surveyed have considerable latitude in setting prices, particularly for non-monopoly services. While all of these PAs are highly unionized, most believe that their wage rates are not significantly above private sector levels.

Ownership, Structure, and Organization

In all of the countries studied, major postal reorganizations have occurred, usually as a result of a combination of wider government reform programs and strong postal leadership.

In most cases, "corporatization" has not led to privatization. All of the postal administrations in this study are 100 percent government owned except the Netherlands Post, which recently conducted a public offering of shares equal to 30 percent of the equity of the company (with a plan to offer an additional 30 percent in 1996 or 1997). Although the governments of Argentina and Germany have announced their intentions to privatize their postal administrations, there has been little public pressure in any of these countries (with the

exception of Argentina) to "sell off" the postal administrations.

One area in which a form of privatization has occurred is in the retail, or counters, network. In the Commonwealth countries (the U.K., Canada, Australia, and New Zealand), a majority of the retail outlets are in private hands. Except La Poste, all of the postal administrations studied have some form of franchising policy for retail services.

Most of these postal administrations have, in recent years, begun to operate under an explicit goal of profitability and with set targets for returns on their investments. This changing approach to financial management has been a critical element of the reform process.

The move towards a government-owned corporate status has also brought a change in the structure of many postal administrations. In the U.K., Germany, Sweden, and New Zealand, for example, the PAs are organized around product lines (e.g., letter mail, parcels, and international mail) as opposed to functional areas. Many PAs have also added a variety of new services. Sweden Post offers a number of electronic messaging and hybrid services; Australia Post and Canada Post Corporation provide hybrid mail services; and Argentina Post sells tax and money transfer services.

Social Responsibility

All postal administrations in the study have non-commercial social obligations to the government and its citizens. Increasingly, these obligations are explicitly stated, either in the acts of incorporation or in contracts between the postal administrations and the governments. Sweden Post and Australia Post estimate and publish the annual cost of these non-commercial obligations, which equal less than five percent of their annual expenditures.

A recent phenomenon has been the move to define the social obligations of the postal administrations not through statutes but through a negotiated contract between the government and the postal administration. New Zealand Post's Deed of Understanding and the Netherlands Post's

exclusive rights agreement are examples of these contracts. Sweden Post's agreement is a variation of this practice in which the government, not the postal administration, has the obligation to provide postal services. The government currently contracts exclusively with Sweden Post to provide these services but may extend this arrangement to other competitors if they achieve sufficient scope.

A universal service requirement is an element of the postal statutes or the postal administrations' agreements with the governments in all ten countries. In some cases, the statute requires a uniform letter rate; in other cases, uniform rates are included in the contract with the government. Regardless of the law, all of these postal administrations maintain uniform rates for their retail letter services.

The required frequency of delivery varies across PAs as does the flexibility in the definition of uniform delivery. Australia Post, for example, is not required to deliver to the most rural addresses with the same frequency as to the rest of the country.

The requirement to maintain a universal retail network is a sensitive political issue in all of these countries. In Sweden and France, for example, the closing of post offices is regulated by the government. Some administrations have been successful at rationalizing their retail network either through closures (e.g., Germany, Argentina, and Australia) or through franchising (e.g., Canada, New Zealand, and Australia).

Scope of the Monopoly

All of the postal administrations in the survey have some form of monopoly protection except Sweden Post and Argentina Post. The New Zealand government's recently announced plan to eliminate the letter monopoly in 1995, supported by New Zealand Post Ltd., has run into problems from the opposition party and from some in the government. In France and Germany, the monopolies extend beyond letters. Unaddressed advertising mail is usually outside the scope of the monopoly but addressed advertising mail is generally treated as part of the letter mail monopoly.

The method used to define the scope of the letter monopoly varies across countries. Some letter monopolies are defined by weight (e.g., Netherlands, up to 1.1 pounds), others by price (e.g., Germany, ten times the standard letter price and Canada, three times the letter price), others by a combination of weight and price (e.g., Australia, four times standard letter price and up to 8.8 ounces). In New Zealand and the U.K., the letter monopolies are quite narrow, allowing competition above approximately \$0.51 U.S. and \$1.60 U.S., respectively. Once the threshold values are in place, they may be narrowed over time as a way to increase competition in a controlled process.

Some administrations are required to perform services even though those services are not protected by a statutory monopoly. Canada Post must deliver parcels and the Netherlands Post must deliver all mail up to 22 pounds.

Pricing Freedom

Only Argentina has absolute freedom to set postal rates. All others are regulated to some degree, although none face regulation by an independent regulatory body. In all but two of the other countries, price regulation is limited to the monopoly services, not to services that face direct competition. Competitive services are, however, generally subject to commercial antitrust rules that restrict predatory pricing. Hybrid mail services and financial services have been the subject of antitrust complaints in some of the countries surveyed.

For most PAs, rate increases in monopoly markets require approval by a government body (usually either the ministry that "owns" the PA or a separate regulatory body). In Australia, the government can only "disapprove" rates. New Zealand's letter rates are defined in a formal contract between the government and the PA. Increasingly, rates for monopoly services are regulated using a price cap formula (e.g., pegged to the rate of inflation in the Netherlands and France and to a price index less one percent in New Zealand).



Managerial Freedom

Most of the postal administrations in this study are permitted to purchase goods and services, enter into joint ventures, and establish subsidiaries like a private sector firm. Canada Post, for example, recently purchased 75 percent of Purolator Courier Ltd., a large express company. Canada Post is also a member of a consortium testing the use of cable television to sell goods and services in 34,000 homes. Five postal administrations are members of a joint venture with TNT to provide international expedited mail and remail services. The Netherlands Post and La Poste also have a large number of subsidiaries and participate in a number of joint ventures to provide, for example, transportation services, warehousing and order fulfillment, and direct mail services.

Employment

All postal administrations studied are heavily unionized with collective bargaining as the basis for wage negotiations. In all of these postal administrations, some or all of the employees have the right to strike if agreement cannot be reached on the terms of their contracts. In general, however, significant labor unrest and work stoppages in postal administrations in the Netherlands, Australia, and Canada in the 1980s have given way to improved labor relations in the 1990s (Germany's postal strike in 1994 is an exception to this trend). Many argue that the confrontational approaches of the past will continue to fade as the postal administrations transform themselves into modern service businesses. Canada Post, however, believes that the strikes in the 1980s resulted in business lost to competitors. The postal strike in France in 1974 was also viewed as particularly debilitating.

Work force reductions have been significant in many of these postal administrations. This is especially true in New Zealand (40 percent over seven years), Canada (12 percent over six years), Australia (11 percent over five years), and Sweden (11 percent over two years). In many cases, work force reductions were achieved through voluntary action of employees and/or incentive packages.

Most postal managers surveyed do not believe that wage premiums exist in their postal administrations, although other types of premiums, such as job security, are present. Canada Post, for example, believes that over the 14 year period since corporatization, through difficult and often acrimonious labor relations, it has eliminated the premium in postal wages.

In the Netherlands, employees were given incentives to participate in the Post/Telecom's share offering last year. It is not known, however, what percent of the publicly traded stock is held by postal employees.

Financial Information

All PAs in the survey except Canada, Germany, and Argentina reported a pre-tax profit in their latest fiscal year. All of these postal corporations currently pay federal income taxes except the German postal service, which will be required to do so beginning in 1996. Of the postal administrations researched, only Sweden Post pays the European Union Value Added Tax.

Some of these PAs have a pension fund that is separate from the government. Only the German and French postal administrations reported large unfunded pension and medical liabilities. Sweden Post inherited a relatively small pension liability when it became corporatized. Sweden Post agreed to pay off this liability in exchange for an understanding that it would not pay dividends to the government for the first few years of operation.

Most of these postal corporations are able to access capital markets like a commercial enterprise, without requesting government permission. However, planned borrowing and investments are generally included as part of the strategic package presented to the Ministries that "own" the postal administrations. The Post Office's lack of financial flexibility was one of the major reasons cited for the U.K. Post's recent support for privatization.

Introduction

The last decade has been a period of significant change for postal administrations around the world. There are many factors driving this change, including the election of conservative governments in a number of countries, the separation of posts and telecoms, the move to deregulate the telecom markets, and, above all else, the increase in competition in the delivery and communications markets. Competition from traditional sources, such as expedited carriers, remailers, document exchanges, and private postal stores, has increased the pressure to reduce the scope of the posts' protective monopolies. Competition from new forms of communications, such as faxes and electronic data exchanges, has significantly weakened the value to the postal administrations of these statutory monopolies.

Although there are significant differences across countries, the most successful postal administrations have followed similar reform paths including two critical elements – corporatization and deregulation. In many of the ten countries included in this study, postal statutes have been modified or rewritten to create government-owned postal corporations. These statutes both require that postal corporations act like businesses (e.g., pay taxes and compete fairly) and provide them with the managerial freedoms (e.g., the ability to access capital markets) to do so.

1.1 Objective and Scope

This study describes the current status of ten of the most progressive postal administrations. The purpose of the study is to identify best practices and lessons learned in the areas of commercialization, deregulation, and privatization in the postal sector.

The ten countries included in this report are Australia, Canada, France, Germany, the Netherlands, New Zealand, Sweden, the United Kingdom, Argentina, and Denmark. For each country, the following issues were researched: ownership structure and organization, social responsibility, scope of the monopoly, competition, regulation, managerial freedom, employment, and financial information.

1.2 Approach

Data collected for this study consisted of a mix of primary and secondary information. Secondary sources were used first to address the study issues and, where appropriate, primary research, such as interviews with senior postal officials, was conducted.

Profiles have been written for each of the countries researched. Countries are presented in alphabetical order, except for Argentina and Denmark which are presented last due to their limited relevance to the USPS. Exhibit A on the following page summarizes in a cursory fashion some of the major findings of this report.



Comparison of Organizational and Financial Characteristics Progressive Postal Administrations

	Australia	Canada	France	Germany	The Netherlands	New Zealand	Sweden	United Kingdom
Owner	Govt	Govt	Govt	Govt	Govt & Private	Govt	Govt	Govt
Last Major Reform	1989	1981	1991	1995	1994	1987	1994	1840 ¹
Stamp (U.S.)	35¢	30¢	53¢	66¢	47¢	29¢	50¢ ²	43¢
Staff	31,130	54,000	300,000	360,000	56,000	8,670	50,213	183,000
Volume (billions)	4.3	11.0	23.0	19.0	6.3	0.7	4.2	17.0
Revenue (billions of U.S.)	\$1.9	\$2.8	\$14.3	\$14.7	\$3.2	\$0.4	\$2.9	\$7.7
Franchises Most Post Offices	Yes	Yes	No	No	Yes	Yes	No	Yes
Borrows Private Capital Without Government Approval	No	Yes	Yes	No	Yes	Yes	Yes	No
Pays Federal Income Tax	Yes	Yes	Yes	No	Yes	Yes	Yes	Yes
Joint Ventures	Yes	Yes	Yes	No, but allowed	Yes	Yes	Yes	No
Subsidiaries	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Financial Mandate	Profit	Break-even	Break-even	Profit	Profit	Profit	Profit	Break-even ³
Scope of Monopoly	4 times standard rate, 8.8 oz.	3 times standard rate	Up to 2.2 pounds	10 times standard rate	Up to 1.1 pounds	51¢ and 7 oz.	No monopoly	Up to \$1.60
Monopoly Price Cap	Yes	No	Yes	No ⁴	Yes	Yes	Yes	No ⁵
Mail Box Monopoly	No	No	No	No	No	No	No	No
Non-Monopoly Prices Regulated	No	No	No	Yes	No	No	No	Yes
Right to Strike	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes

¹ - Recent reforms at the Post Office have been limited to specifics of telecommunications and banking services.

² - Includes 20 percent VAT.

³ - In practice, the Post Office is given revenue targets above break-even to fund withdrawals by the government.

⁴ - The government is considering the introduction of a price cap.

⁵ - The Post Office wants to use a price index formula introduced and historically, increases have been below the rate of inflation.



Australia

 Australia Post
A. Corporate Profile

Australia Post (AP) is a federal "Government Business Enterprise" serving 17.5 million Australians. In 1993-94, AP collected and processed 4.3 billion mail items for delivery to 7.5 million delivery points, an increase in volume of 3.8 percent over 1992-93. AP owns 1,203 retail outlets and 38 mail processing sites, and also serves customers through an additional 2,789 post office "agencies" in the retail network. AP employs a total of 31,130 full-time staff — down from 35,107 five years ago.

For the year ended June 30, 1994, AP's revenues were Aust. \$2,568 million (\$1,978 million U.S.),¹ with a net pre-tax profit of Aust. \$287 million (\$221 million U.S.). Australia Post has total assets of Aust. \$2 billion (\$1.54 billion U.S.).

The standard addressed letter mail postage is Aust. 45¢ (35¢ U.S.) for delivery anywhere in Australia.

B. Ownership, Structure, and Organization**Corporatization**

Australia Post is a "Government Business Enterprise" owned by the Commonwealth of Australia. There is no formal share structure. Instead, Australia Post operates under the *Australian Postal Corporation Act*, paying an annual dividend to the Commonwealth.

Prior to 1989, AP operated as the Australian Postal Commission, with no commercial remit and numerous bureaucratic controls over day-to-day operations. The 1989 corporatization was part of the Labor government's program of micro-economic reform.

There is currently no political or private pressure for privatization. A 1992 Industry Commission study did propose privatization by 1997, but the government rejected this proposal. The current

Minister for Communications and the Arts has recently restated the government's commitment to public ownership. Moreover, the leading (conservative) opposition party has never proposed postal privatization, despite its pro-business stance. Neither the business community nor AP's senior management is seeking privatization. The government, the unions, and the public all feel that privatization would lead to lower standards of service.

While it is possible that a government review of the Post scheduled for July 1997 may reopen the question of ownership, the main political debate over AP surrounds the degree and speed of future deregulation.

Financial mandate

Before 1989, AP was required to recover costs and fund at least half of its capital expenditures.

The 1989 *Australian Postal Corporation Act* requires that AP operate commercially, including achieving a "reasonable rate of return on assets" (undefined in the legislation), payment of all taxes and dividends to government, and periodic revaluations of assets. In 1993-94, AP paid a record dividend to the Commonwealth government of Aust. \$90 million (\$69.3 million U.S.), made a capital repayment to the Commonwealth government of Aust. \$200 million (\$154.1 million U.S.), and earned a return on assets of 14.5 percent.

Management structure and board oversight

The Minister appoints the Board of Australia Post which is responsible and accountable to the Minister as owner. Through the corporate planning process, the Minister for Communications and the Arts and the Minister of Finance participate with the Board in setting the targets for financial performance, service quality, and various "Community Service Obligations" (CSOs) over a three-year planning period.

The Minister for Communications and the Arts deals with postal matters, while the Minister for Finance oversees the government's investments and assets. There is no separate postal regulator.

¹ Based on January 25, 1995 exchange rate of \$0.7703 (U.S.).

outside the Ministry for Communications and the Arts. After a recent review of the CSOs, the government asked the House of Representatives' Standing Committee on Transport, Communications, and Infrastructure to annually review the performance of AP on the CSOs. AP must also report any proposed price increases to the Prices Surveillance Authority. The Authority may state its opposition to a change, but only the Minister has the power to block an increase.

The Board, which can consist of up to nine Directors, appoints the Managing Director (MD). Currently, the MD is responsible for operations and the retail network, and the General Managers in the State Profit Centers report directly to the MD. Directly under the MD is a Deputy Chief Executive who has responsibility for various business units, including Letters and Parcels. The next most senior manager is the Chief Manager, Finance and Services, with responsibility for all central finance and information technology functions.

Range of business

Australia Post's core business is postal and delivery services, which account for approximately 85 percent of revenues. In addition to traditional letter and parcel services, AP offers assistance with direct mail and address checking and has developed a hybrid mail business branded as EDIPOST.

Retail network

AP's retail network is currently being restructured and modernized. The key to this reform program is a significant change to the contractual relationship between AP and the "Agents" that manage the postal outlets.

For the past 50 years, two-thirds of AP's retail outlets have been managed by these Agents on behalf of AP according to contracts negotiated nationally with an Agent's Association. In 1993, a new contractual arrangement was established that removed bureaucratic barriers and provided incentives for growth. Agents were provided incentives to become "Licensed Post Offices" through "income safety nets" that have a sunset date. Two-thirds of the 2,977 post offices have

made the transition. There are now "Postshops" (public retail outlets) and "Business Centers" (business retail outlets) within the network.

Financial transaction services remain a relatively small business area for AP. While AP is actively seeking to increase the number of financial transactions handled through the network, and is signing partner agreements with banks, it says it has no plans to develop "post bank" services like some European postal administrations.

C. Social Responsibility

The 1989 *Australian Postal Corporation Act* explicitly separates social obligations from commercial objectives. The former are referred to as the "Community Service Obligations" or CSOs. In the Act, the list of CSOs includes:

- the provision of domestic and international letter services;
- the provision of a domestic standard letter service available at a uniform price;
- a letter service which is reasonably accessible to all Australians on an equitable basis; and
- performance standards for the letter service which reasonably meet the social, industrial, and commercial needs of the Australian community.

However, since some of these obligations are profitable, there is a separate group known as noncommercial CSOs, whose costs are directly measured.

Specific CSO targets are set during the corporate planning process. Such targets include the number of outlets where customers can buy stamps, the maintenance of convenient hours of operation nationwide, and the maintenance of the network measured in terms of the number of delivery points and delivery frequency.

Australia Post actively seeks public consultation on its CSOs and reports its performance against

these targets annually. In AP's 1993 fiscal year, the company estimated the cost of its noncommercial social obligations at Aust. \$46 million (\$35.4 million U.S.). There is some debate between AP and the government regarding how the CSOs should be measured.

The government may also direct Australia Post to follow various general government policies such as those relating to wages and industrial relations.

Rural delivery and delivery frequency

AP employs 3,300 contractors to deliver mail in rural areas. Some 346,000 households in remote areas receive only roadside delivery service, while 157,000 households receive no residential delivery.

Australia Post aims to provide five day a week delivery service to approximately 99 percent of all delivery points, including 80 percent of the 364,000 most remote households.

Community Post Offices

While there is no written restriction on the number of postal outlets, closure rates have been low due to political sensitivities and the requirement to open all such decisions to detailed public consultation. The strategy to reduce the unit cost burden of the network involves increasing the number of transactions handled by retail outlets and transferring agency-based outlets to a new contractual form known as Licensed Post Offices.

Obligations to government

Apart from the CSOs and the usual obligations of an Australian Corporation to the federal government (such as paying taxes), AP has no other duties. However, it performs a number of tasks for government under commercial contract such as tax collection, passport interviews, and distribution of information.

D. Scope of Monopoly

According to the 1989 Australian Postal Corporation Act "AP has the exclusive right to carry letters within Australia."

The domestic letter monopoly is set at a price threshold of Aust. \$1.80 (\$1.39 U.S.), or four times the basic postage rate, with a weight threshold of up to 250 grams (8.8 ounces). This monopoly no longer includes the carriage of letters within document exchanges or within an organization. Addressed domestic mail is considered by AP to be in the monopoly, but a recent amendment to the 1989 Act changing the definition of catalogues and leaflets that may be delivered by competitors has left some doubt about the extent of the monopoly over advertising mail. The international letter monopoly is limited to inbound letters. There is no monopoly over parcels or publications.

The scope of the monopoly (often called the "reserved area") was last changed in July 1994 and will be reexamined again in 1996-97. The recent change reduced the monopoly price threshold from 10 times the basic stamp price to four times the basic stamp price. The Minister announced the recent measures, saying "The government has agreed to proposals for a sensible managed approach to the introduction of further competition for Australia Post...."

AP has no legal obligation to deliver products other than "letters that are standard postal articles." However, in practice, AP management believes that it must provide all basic postal services throughout Australia.

Mailbox exclusivity

AP has no exclusive right to deliver to a mailbox.

E. Competition

Presence of competition

Australia Post has a number of competitors for the delivery of catalogues, annual reports, and courier and express items, and faces competition from other media such as electronic communication. AP does not provide data on market share but cites several competitors and services. Progress Press offers an extensive unaddressed letter and targeted catalogue delivery service. Streetfile employs sophisticated computer systems in conjunction with a new print technology to offer a

targeted delivery service. Its main clients are advertisers. Saimat delivers publications addressed to businesses and households and has links to a mailing house called Automail.

The recent reduction in the monopoly and the introduction of downstream access pricing have not led to any immediate change in competitive pressure, probably because the destination entry discount is small.

There have been no recent antitrust complaints against AP.

Presort discounts

Discounts for bulk mailers are available and vary by category of letter, weight, and level of presorting. For example, a small letter of up to 125 grams (4.4 ounces) sorted into direct bags or trays receives an Aust. 7¢ (5¢ U.S.) discount.

The 1994 reforms allowed, for the first time, a degree of downstream access for letters, or "interconnection." Bulk mailers can now carry mail between major cities to designated mail centers and interconnect with Australia Post's delivery network. A common discount is provided based on average avoidable transport costs. However, this discount is relatively small, on average approximately one cent.

F. Regulation/Managerial Freedom

Pricing and regulatory oversight

Australia Post sets its own prices. The government can only "disapprove" of the basic postage rate sought by Australia Post.

AP's pricing freedom is somewhat constrained by a price cap regime. From 1994-95, increases in the basic letter rate may not exceed the price index less "X". The "X", often referred to as a "productivity factor," has not yet been determined, and in the meantime AP has agreed to freeze rates until 1997. The Minister has said he will look at this experience and rule on the future price cap regime for AP in 1997.

The only other regulatory influence on Australia Post's pricing decisions is the Prices Surveillance Authority (PSA), which Australia Post must notify regarding proposed price increases for monopoly services. While the PSA has only an advisory role, it has in the past instituted inquiries into proposed increases lasting up to three months. The Board is not required to accept the findings of the PSA's inquiries, but in practice it is politically difficult to ignore the recommendations.

Day-to-day government control over the operation of the Post disappeared with the 1989 reforms. The Ministries' direct control is limited to their involvement in the corporate planning process.

In principle, management freedom is constrained only by the corporate plan and the powers granted the executives under the 1989 Act. The 1989 Act states that the Corporation may undertake any business or activity, either in Australia or overseas, which relates to its principal function — supplying a service for the carriage of letters.

Authority to purchase suppliers, competitors, and customers

The federal government would expect any purchase of a large supplier, competitor, or customer to have been detailed within the Corporate Plan. As the government could object, there is no absolute freedom for such takeovers, and AP has so far not attempted any acquisitions.

Antitrust

AP is subject to antitrust claims brought before the Trade Practices Commission (TPC), the general regulator for competition. The government's general economic policy is to strongly regulate anti-competitive behavior, and AP has an active TPC compliance program throughout its organization.

Procurement flexibility and oversight

Since corporatization, AP's procurement policy has been set by the Board, not the government.

Contracts of Aust. \$10 million (\$7.7 million U.S.) or more must go to the Board for approval. The head of procurement at AP's headquarters can approve up to Aust. \$5 million (\$3.9 million U.S.), with a range of approval levels below that.

The main criterion is value for money, and managers are encouraged to take the "commercial option." Managers are not required to tender for competitive bid in all cases, for example, if they seek to establish a long-term supply relationship. AP feels it has achieved a high degree of flexibility in procurement, with the main existing deficiency being the need to introduce electronic data interchange systems.

Government, in theory, influences procurement policy through its policy of encouraging "local preference" (i.e., Australian) in public procurement. In practice, AP does not feel this policy has affected purchase decisions.

Joint ventures and subsidiaries

Australia Post has developed two joint ventures to date. It has a 50/50 joint venture with Qantas called Australian airExpress to provide air express services. With Geospend, AP is providing direct marketing expertise.

Australia Post has one subsidiary, Sprintpak, which provides quality assurance and secure finishing for the production and packaging of stamps, philatelic products, and collectibles.

G. Employment**Wage settlement**

AP's current wage negotiation process is the result of two major influences: the Australian Industrial Relations Commission's (AIRC) guidelines for "enterprise agreements" (company wage negotiations) and a Joint Statement of Understanding signed with the postal unions in 1988. The AIRC sets a framework for the process of negotiations for unions and management, while the

Joint Statement of Understanding provides a new start for labor relations after a number of damaging postal disputes.

Wages are now settled under an "Enterprise Agreement" which takes approximately six months to negotiate. There are two main unions who negotiate with management as a single bargaining unit on behalf of all unions within AP. In addition to basic pay, agreements have covered incentives, numbers of part-time staff, and the sharing of information such as the corporate plan. The first AP Enterprise Agreement ran from October 1992 to April 1994, and the second operates for 18 months to April 1996.

This structure has promoted consensus in recent years, but if the parties were unable to reach agreement, they could seek the help of the AIRC. A dispute over an Enterprise Agreement would be handled under a dispute settlement clause under which the parties agree to arbitration by the AIRC.

Job protection

AP has an agreement with the unions called "Redundancy, retraining, and redeployment" for managing staff levels. This agreement accepts compulsory redundancy of staff if certain criteria are met. However, reductions in staff levels in recent years have mostly been made through voluntary redundancies. AP does not have any targets for staff reductions and believes in an open, consultative approach to reducing staff numbers. AP does not make agreements with the unions on staffing levels, except in relation to a limit on the number of part-time staff it will hire.

Wage premiums

AP is not generally regarded as paying above market rates, although jobs are seen as fairly secure.

H. Financial**Pensions and the balance sheet**

All pensions are fully funded, and there are no outstanding large medical liabilities.



In recent years, AP has maintained a positive balance sheet and is projected to maintain a healthy financial position in the foreseeable future. Management knew of no special procedures for dealing with a negative balance sheet and assumed the government would have instituted managerial changes before the situation arose.

Taxation

Since corporatization in 1989, AP has paid the same taxes as would any other Australian corporation. In FY 1993-94, its tax bill was Aust. \$280 million (\$216 million U.S.), made up largely of income, payroll, and sales taxes. It is also liable for excise duties, withholding taxes, and land taxes. The main lesson of AP's tax experience involves the transition from being tax privileged to becoming a normal taxable company in 1989. The transition was made easier by the change in accounting procedures prior to 1989. AP's management believes that the financial reforms needed to fulfill the new "corporate" mandate have had significant positive effects by focusing the company on profitable investments and on maintaining a healthy balance sheet.

Access to capital markets

AP can borrow only with the permission of the federal government's Loan Council. Last year, AP's Board requested Aust. \$50 million (\$38.5 million U.S.) from the Loan Council, and this has been accepted. AP is forbidden by statute from going directly to the private markets. However, once government/Loan Council permission is granted, AP calls a tender for borrowing.

Requests to the Loan Council could, in theory, be turned down. However, after prior consultation with the Minister, it is unlikely a request would be rejected.

Until March 1994, AP had previously borrowed only small amounts of money and had accumulated a cash portfolio of between Aust. \$300 million (\$231.0 million U.S.) and Aust. \$400 million (\$308.1 million U.S.).

Control of treasurer over investments

The policy for the postal Treasurer is determined by the Board, with a manual describing the basic procedures. The policy is conservative; for example, any funds invested over 12 months must seek a floating rate. Investments in derivatives are allowed, but can only be for the purpose of hedging, not speculation. The Treasury function does not operate as a profit center, and its mandate is to maintain capital value and achieve a reasonable return on funds.

I. Best Practices/Lessons Learned

The main lesson from the Australian experience is the importance of overall federal government policy in enabling postal reform. The 1989 corporatization followed a 1988 document called "Reshaping the Transport and Communications Government Business Enterprises," which also dealt with state owned companies in the airline, telecommunications, and railroad industries. This document was itself part of a general program of microeconomic reform. Thus, postal reform was part of a much larger effort to "corporatize" government enterprises. Similarly, the importance of political leadership can be seen in the success of AP's handling of employee relations over this period.

The Australian experience indicates a number of significant lessons:

- Reform can be assisted by outside government bodies making bold proposals. The 1992 Industry Commission Report and the forthcoming 1997 review have served the purpose of pressuring management to consider significant reforms.
- The freedoms won for management within the Government Business Enterprise structure have enabled innovation and the development of long-term strategies. The EDIPOST product is an example.



- AP has implemented change, increased productivity, and increased profits while maintaining the basic stamp price and service quality (93 percent on-time delivery rating within Australia).

It could be argued that AP has been fortunate in implementing postal reform (e.g., government support, partial deregulation instead of full-scale privatization, and a strong balance sheet). However, AP's performance improvements since corporatization reveal the extent of changes that are possible given the freedom to manage.



Canada

MAIL ➤ POSTE**A. Corporate Profile**

Canada Post Corporation (CPC) is a federal Crown corporation that serves 28 million Canadians and 900,000 businesses and public institutions. CPC collects and processes 11 billion pieces of mail annually for delivery to 12 million addresses. CPC has 19,000 retail outlets, 22 major mail processing plants, and 5,500 vehicles and engages 7,000 transportation contractors. CPC employs 54,000 full- and part-time employees — down from 63,000 six years ago.

For the year ended March 26, 1994, CPC's revenues were \$3.9 billion Canadian (\$2.8 billion U.S.);² the net loss was \$259 million Canadian (\$183.0 million U.S.).

The standard addressed letter mail postage (up to 1.1 ounces) is 43¢ Canadian (30¢ U.S.), excluding the seven percent federal Goods and Services Tax.³ The rate is uniform throughout Canada. Some private retailers sell stamps at a discount as a sales promotion for other products or services. Significant discounts from the standard rate are also available to bulk mailers who prepare letter mail to facilitate processing by CPC.

B. Ownership, Structure, and Organization**Corporatization**

CPC is a federal Crown corporation whose only shareholder is the government of Canada. Prior to 1981, CPC was a government department known as the Post Office Department.

A total of 75 percent of CPC's 19,000 retail outlets are operated by private businesses. This shift to private businesses occurred after the 1981 reforms.

CPC was made a Crown corporation in order to free the post office from government administrative practices that restricted the organization's ability to function effectively in a commercial environment. Since corporatization, public discussion about selling Canada Post to private owners has been infrequent.

CPC recently acquired a 75 percent interest in a major domestic courier company (Purolator Courier Ltd.), expanding the role of public ownership in postal services.

Financial mandate

The legislation incorporating Canada Post requires CPC to conduct its operations on a self-sustaining financial basis while providing a uniform standard of service and rates to all Canadians. CPC's financial statements are prepared in accordance with generally accepted accounting principles. CPC is subject to federal income taxation.

Management structure and board oversight

The government appoints a Board of Directors as well as the Chairman of the Board and the President. According to the legislation incorporating Canada Post, the Board directs and manages the affairs of CPC. Canada Post, however, must comply with directives from the Minister Responsible for Canada Post Corporation.

Range of business

CPC provides traditional postal services such as the delivery of letter mail, parcels, advertising material, money orders, and publications. The corporation is also a major participant in the courier market. As an alternative to courier and regular mail, Canada Post recently introduced an express service, XPRESSPOST, for time-sensitive packages and documents. XPRESSPOST is part of CPC's move to brand marketing — focusing marketing efforts on unique products or service identifications (e.g., Tide) rather than on marketing Canada Post.

CPC provides electronic mail services. Messages and customer lists are provided electronically to Canada Post. CPC prints, folds, inserts into envelopes, and delivers the messages.

² Based on January 25, 1995 exchange rate of \$0.7063 (U.S.).

³ A national sales tax.

Canada Post is also part of a consortium testing the use of cable television networks for the electronic provision of goods and services to 34,000 homes. The corporation operates Direct Marketing Resource Centers to promote the use of advertising mail. Postal vending machines are being tested. Canada Post Systems Management Limited is the technology center of the corporation that markets management systems and postal technology to other postal administrations.

C. Social Responsibility

Social obligation defined

Canada Post's social responsibility is defined in the 1980 *Canada Post Corporation Act*. The act requires that CPC maintain "a standard of service that will meet the needs of the people of Canada and that is similar with respect to communities of the same size." It also requires Canada Post to maintain "basic customary postal service" and "fair and reasonable" rates.

CPC is required by the act to comply with directives from the Minister Responsible for Canada Post Corporation. However, the Minister rarely uses his directive power, choosing instead to issue public statements regarding changes CPC should make to its policies. The Minister's recent announcement that rural post offices should no longer be closed and that urban post office closings should be the subject of a public consultation was an example of this less direct approach.

Universal service

Canada Post provides universal service, although the nature of the service varies, reflecting the managerial flexibility granted to Canada Post by the *Canada Post Corporation Act*. Universal service is understood by CPC to mean nondiscriminatory service. Depending on the circumstances, people in some communities pick up mail at community mailboxes near their homes, while others receive mail at their residences.

Uniform rates

CPC offers universal service at a uniform rate for letter mail. However, uniform rates are not a requirement of the postal statutes.

Delivery

Delivery is generally five days per week (Monday to Friday). Canada Post courier delivery is available on Saturday. In some areas, unaddressed advertising mail is delivered by an alternate postal delivery force on weekends.

Social policy subsidies

During the last decade, Canada Post has phased out mailers' subsidies for Canadian publications, Parliamentary mail, literature for the blind, and the shipment of food and similar items to the North. These subsidies still exist but are now provided by the federal government, taking social policy out of the post office. In fiscal year 1994, the federal government compensated CPC \$114.9 million Canadian (\$81.2 million U.S.) for foregone revenues from these sources.

D. Scope of Monopoly

Extent of monopoly

According to the *Canada Post Corporation Act*, Canada Post "has the sole and exclusive privilege of collecting, transmitting, and delivering letters to the addressee thereof within Canada." However, several important exceptions to this exclusive privilege exist in the legislation, including:

- newspapers, books, magazines, goods, and catalogues;
- letters delivered to a friend;
- letters of "an urgent nature" that are transmitted by a messenger for a fee at least equal to an amount that is three times the regular rate of postage; and
- letters "in the course of transmission by any electronic or optical means."

Canada Post has the power to define a letter. The definition must be approved by the federal



government after an opportunity has been given to interested parties to make representations to the government about the proposed definition.

Although Canada Post has on occasion relied on the *Canada Post Corporation Act* to assert its monopoly over letter delivery, CPC has generally accepted that, for practical purposes, the corporation must function in a competitive environment. The monopoly would be difficult to enforce in the dynamic and competitive Canadian communications environment and attempts to enforce the monopoly would not be welcomed in the marketplace, because they would create an unfavorable image of Canada Post. A recent Canada Post publication noted that a taxi company was competing with CPC in Calgary and Edmonton for delivery of letters. The taxi company delivers standard mail for 35¢ (25¢ U.S.); CPC's rate is 43¢ (30¢ U.S.). CPC's latest annual report states: "Letter mail volumes showed minimal growth as transition to alternative communication methods continues to escalate."

Mailbox exclusivity

Only Canada Post generally delivers directly to locked mailboxes. Rural mailboxes located along roads are not locked; they are accessible to anyone. For security reasons, mailboxes in apartment lobbies are normally accessible only to CPC. Letter slots or mailboxes at residential homes are not considered exclusive to CPC use.

Mandatory services

The *Canada Post Corporation Act* requires CPC "to establish and operate a postal service for the collection, transmission, and delivery of messages, information, funds, and goods." This requirement presumably means that Canada Post must provide parcel service and postal money orders.

E. Competition

Presence of competition

Competition is a major factor in the provision of Canadian postal services, reducing mail volumes, changing service delivery, and driving the development of new Canada Post services such as electronic mail. CPC was made a Crown corpora-

tion to allow the postal service more operational flexibility in a commercial environment.

CPC perceives that flyer companies, some of which are owned by newspapers, are a competitive threat. The newspaper connection is relevant because CPC feels that it is unfairly targeted as the "junk mail bad guy." CPC often points out that newspapers typically include flyers (i.e., junk mail). CPC's recent initiative to hire a separate work force to deliver unaddressed advertising mail is an attempt to respond to competition by providing a low cost alternative to the flyer companies and the newspapers. The pay scales for these workers are considerably below those of regular carrier.

Presort discounts

Significant discounts from the standard rate are available to bulk mailers who prepare letter mail to facilitate processing by CPC. Canada Post has encouraged the practice of discounts to reflect customer capabilities and reduce CPC costs.

F. Regulation/Managerial Freedom

Pricing and regulatory oversight

Canada Post has been granted significant latitude in setting postage rates. Only certain rates, primarily regular letter mail and certain categories of publication mail, must be approved by the federal government. An opportunity is given to interested parties to make representations to the government about proposed rate changes. The rate proposals are not subject to review by an independent regulatory body. Since the rate setting process is not public, interested parties do not have access to the costing studies and other information underlying the rates. Some competitors allege that standard letter mail rates cross-subsidize competitive services such as courier and parcel services. According to Canada Post, the competitors' allegations are unfounded.

Canada Post can and does enter into discount agreements with bulk mailers seeking government approval of the discounts. In addition, CPC can offer experimental services for three years without seeking government approval of rates.

Authority to purchase suppliers, competitors, and customers

Subject to the federal government's concurrence, Canada Post can purchase suppliers, competitors, and customers. For example, Canada Post recently acquired 75 percent of a major Canadian courier company, Purolator Courier Limited. Acquisitions are subject to review by the Bureau of Competition Policy — Canada's competition watchdog.

Joint ventures, subsidiaries, companies purchased

As noted above, Canada Post has purchased Purolator Courier Limited. CPC is also a partner in a consortium called UBI, with Le Groupe Vidéotron Ltée, Hydro-Québec, National Bank of Canada, Loto-Québec, Vidéoway Communications Inc., and Hearst Corporation. UBI is conducting a residential information highway trial, providing interactive services to 34,000 homes over a cable television network. Canada Post also has an alliance with the Canadian Imperial Bank of Commerce to provide automatic teller machines in certain corporate retail outlets.

CPC has also entered into partnerships to sponsor some commemorative stamps — for example, advertising has appeared in the selva of some issues. A recent booklet stamp commemorating a Canadian department store was sponsored by several companies. Although the stamp and its selva bore no advertising, the booklet acknowledged the sponsors. The corporation has sponsored contests in partnership with Air Canada. To participate in a contest for free airline tickets, one had to enter by mail, necessitating the purchase of postage.

G. Employment

Wage settlement

Ninety percent of CPC's employees are subject to collective bargaining agreements. CPC has had a history of costly strikes since the Crown corporation was created. Undoubtedly, strikes, or situations when strikes are likely, have resulted in business lost to competitors.

The collective bargaining process involves a number of stages. First, if collective bargaining is not successful, the Minister may appoint a conciliation officer with a deadline to prepare a report for the Minister. If the conciliation officer is unsuccessful, the Minister may appoint a conciliation board. The board prepares a report that is submitted to both parties and may be made public. The parties may agree in advance that this report will be binding on both sides. If still no agreement is reached, parties may strike or lock out seven days after parties receive the board's report. Binding arbitration cannot take place unless both parties agree. Differences related to the interpretation, application, or alleged violation of an existing collective agreement are settled without work stoppage by arbitration or other methods.

CPC's willingness to push negotiations to the limit has undoubtedly led to lower wages than if CPC had settled quickly. In addition, some of the past labor troubles were related to technology issues rather than wages. Canada Post's ability to use high speed sorting machines and other technology has benefited CPC. On the negative side, CPC's tough bargaining may have hurt employee morale by negatively impacting productivity. For example, Canada Post's unions are notorious for filing large numbers of grievances. According to recent media reports, approximately 150,000 grievances (about three per employee) are outstanding.

The labor situation has improved significantly since the 1980s. The Canadian Union of Postal Workers (CUPW) represents 38,000 of CPC's 54,000 employees. CUPW and CPC apparently have negotiated a new agreement prior to the expiration of the existing agreement — an unheard of development in recent years at CPC.

Job protection

All unionized employees have job security (i.e., no layoffs). Incentive buyout programs have been used to reduce the labor force. Buyouts have been an important factor in the reduction of the labor force to 54,000 employees from 63,600 six years ago.



According to Canada Post, during the past 10 years, mail processing efficiency has increased from 242 pieces per hour paid to 321 pieces per hour paid. In the same period, letter carrier efficiency has increased from 43.9 points of delivery per hour paid to 54.1 points of delivery per hour paid.

CUPW and Canada Post have a Service Expansion and Workplaces Development Committee. CPC will provide \$3 million Canadian (\$2.1 million U.S.) for the use of the committee. The committee's mandate is to identify ways of enhancing customer satisfaction, business growth, and opportunities to create additional positions for the union's members.

Wage premiums

Premiums had become inherent in the post office wage structure for three reasons: (1) monopoly, (2) essential service, and (3) government management. According to Canada Post, the premium in basic wage rates has been eliminated; wages now meet industry norms. On average, letter carriers are paid \$16.07 per hour (\$11.25 U.S.), motorized mail drivers are paid \$16.51 per hour (\$11.66 U.S.), and mail handlers are paid \$16.50 per hour (\$11.65 U.S.).

The reduction in the wage premium was a gradual process over the 14 years following creation of the Crown corporation. The process was characterized by complex and difficult labor negotiations, resulting in work stoppages and acrimonious labor relations. According to Canada Post, only some non-wage premiums still exist, regarding working conditions (e.g., cleanup time) and work rules that deal with overtime and part-time and casual labor.

Compensation

With respect to compensation, the collective agreements are national with no regional disparities. Incentive plans do not exist for employees subject to collective agreements because the unions do not favor the plans. Some sales employees and management groups are on an incentive plan. The incentives relate to corporate performance, individual performance, and quality of service.

The Act permits employee ownership of up to 10 percent of issued shares of the Corporation. However, there has been no issuance of shares to date and none are expected in the near future.

H. Financial

Pensions

CPC's employees are part of the Canadian federal government's pension plan. From CPC's perspective, any unfunded liability is an obligation of the federal government.

An Employee Termination Benefit Fund exists. Employees are entitled to specific termination benefits based on salary levels at the time of termination, as provided under collective agreements and conditions of employment. The CPC liability at this time is \$400 million Canadian (\$282.5 million U.S.); the obligation is funded.

The balance sheet

CPC has been a financially self-sufficient Crown corporation since 1988. Canada Post has no access to government funds or capital for operating shortfalls. The corporation plans for a positive balance sheet. Canada Post's corporate plan is formulated in accordance with the *Financial Administration Act*, the *Canada Post Corporation Act*, and other federal acts and regulations. Borrowing limits are approved by Parliament. The borrowing plan, within the limit, is approved by the Minister of Finance.

CPC pays dividends to the government when it earns a positive net income. The last time it paid a dividend was in FY 1992-93. The corporate goal is a 14 percent return, which is similar to other regulated industries in Canada.

Taxation

As noted above, CPC is subject to federal income taxation. Canada Post is not subject to provincial taxes. CPC pays grants in lieu of taxes to municipalities with respect to local property taxes.

Access to capital markets

The federal government can lend money to CPC. In addition, CPC may borrow private capital on the

credit of the corporation, CPC's status as an agent of the federal government allows CPC to obtain the interest rates available to the government of Canada. Currently, CPC has long term debt payable to the federal government (\$80 million Canadian, \$56.5 million U.S.) and \$55 million Canadian (\$38.8 million U.S.) in bonds maturing in 2016.

Control of treasurer over investments

The Board of Directors has considerable latitude with regard to its investment policy. However, CPC is not permitted to invest in publicly traded stocks. (Its purchase of Purolator involved some creative steps to get around this limitation).

I. Best Practices/Lessons Learned

CPC's experience is particularly relevant to the US Postal Service. Both administrations provide postal services in North America, both face similar business, social, and cultural environments. Alternatives to traditional postal services are rapidly emerging in both countries, creating a powerful need for the Canadian and U.S. postal administrations to be flexible and responsive to emerging market developments.

In light of the Canadian experience, lessons learned and best practices with respect to corporatization and deregulation are:

- **Privatization is not essential.** However, more corporate freedom than is typically associated with a government department is critical. In Canada, the Crown corporation appears to serve this purpose without creating the controversy that can flow from transferring what is often perceived to be a public service to the private sector.
- **Tactically privatize some operations.** Although Canada Post is owned by the government, 75 percent of CPC's retail outlets are operated by private businesses. In addition, CPC offers discounts to encourage bulk mailers to prepare letter mail for processing. The tacit privatization of some operations reduces the controversy associated with privatization.
- **Operate on a self-sustaining financial basis.** This imposes discipline on corporate managers, particularly when there is a limit imposed by competitors and public opinion on rate increases.
- **Prepare financial statements in accordance with generally accepted accounting principles.** This provides a universal benchmark for judging whether or not operations are self-sustaining.
- **Rate regulation should not be onerous.** In a competitive and rapidly changing communications environment, the postal administration should not be hamstrung by a lengthy regulatory process. In addition, competitors should not have access to commercially sensitive information through the regulatory process. Canada Post has the flexibility to negotiate discounts outside the government's rate review process for bulk mailers who prepare letter mail for processing. Although a timely and flexible rate review process is key, rates must also be seen as fair and reasonable in light of the postal administration's monopoly powers and market dominance for certain services.
- **Accept competition as a fact of life.** Rather than trying to prevent competition through heavy-handed enforcement of the monopoly provisions, postal administrations should adapt to the competitive marketplace. For example, most of CPC's retail outlets are operated by private businesses, providing more convenience for customers. In addition, Canada Post has developed new services to meet the marketplace's demand for time-sensitive delivery.
- **Embrace new communications and mail processing technology.** Postal administrations must become efficient and productive to meet the challenge of alternative communications methods. For example, Canada Post offers "hybrid" mail service — a combination of electronic and traditional hard copy mail.



France

A. Corporate Profile

Etablissement Public La Poste (La Poste) is the French national postal service and is one of the ten largest organizations in France. In 1991, the French postal service separated from its telecommunications counterpart and left the French Administration to become an Etablissement Public. La Poste employs 300,000 staff and handles approximately 23 billion pieces of mail per year.

In FY 1994, total revenues of La Poste were FF 75 billion (\$14.3 billion U.S.),⁴ of which FF 55 billion (\$10.5 billion U.S.) was generated by Mail Services and FF 20 billion (\$3.8 billion U.S.) by Financial Services. Financial Services includes banking deposits and insurance sales. Net income was FF 60 million (\$11.5 million U.S.).

The standard letter mail rate is FF 2 80 (53¢ U.S.).

As a result of the 1991 reorganization of La Poste as an Etablissement Public, the organization is "off budget," allowing La Poste additional freedom to manage its own finances. The French state, however, is the sole owner of the corporation and generally maintains closer control over its activities than in many other countries surveyed.

In spite of the wave of privatizations sweeping through France's state-owned industries, there has been little talk of privatizing La Poste.

B. Ownership, Structure, and Organization

Corporatization

La Poste is managed by a Board of Administration. The Board includes seven representatives appointed by government, seven "qualified" representatives, and seven representatives from the work force. Qualified members are designated by the government based upon their specific skills

and typically include business executives (e.g., the CEO of a bank or insurance company).

Although its reorganization as an Etablissement Public separated it from the central French Administration, La Poste remains under the oversight of two French ministries: the Ministry of Industry and the Ministry of Finance.

The Ministry of Industry, through its Direction Générale des Postes et Télécommunications, exercises the regulatory role. The Finance Ministry retains considerable control over financial performance. Financial performance is determined through ratio targets (e.g., debt/equity ratio) defined in a "Contract Plan" signed between La Poste and the French Budget Department. Compared with a number of other postal services throughout Europe, La Poste is controlled quite restrictively by government. There are no plans to liberalize the existing regulatory structure.

C. Social Responsibility

Social obligation defined

La Poste must provide basic mail delivery service throughout France at a uniform price. As a public service provider, it is required to show no discrimination between users. Any new Financial Services must be provided universally.

France has rural regions with low population density. Despite a number of attempts to limit the number of postal counters within rural districts, La Poste is still obliged to maintain rural deliveries and a minimum number of community post offices.

As elsewhere in Europe, the issue of community post offices generates much public interest. Public opinion in France strongly supports the maintenance of the status quo. The Prime Minister has made personal statements guaranteeing commitments to community post offices. Nonetheless, the obligation to maintain community post offices has been diluted in some areas by a reduction in the hours of rural post offices and the delivery of postal services from agents based at home.

⁴ Based on January 25, 1995 exchange rate of \$0.1910 (U.S.).

La Poste's retail network, including the number of outlets, has not changed significantly in the last 10 years.

Mail delivery is required to be provided six days per week.

The obligations of La Poste can be traced through to the French constitution which requires equal treatment for all citizens by the French state. Through a number of court decisions, this constitutional obligation has been interpreted to require that La Poste provide good quality postal services at prices that reflect the costs of providing these services. A 1990 law explicitly defined the social obligations of the public postal service provider. The three year plan ("Contract Plan"), which La Poste negotiates with the French Budget Ministry, sets out these obligations in qualitative and financial terms.

D. Scope of Monopoly

The monopoly is defined by law and applies to letters and parcels weighing less than one kilogram (2.2 pounds). Newspapers and unaddressed advertising mail are not included in the monopoly.

The monopoly over letter mail is limited to "private correspondences." However, since letters are sealed against inspection, it is impossible to determine whether or not the contents are private correspondences. La Poste has complained that this loophole in the statutes has made enforcement of the monopoly difficult and has led to the (possibly illegal) entry of international and domestic competitors.

In response to competitive entry, La Poste formed Chronopost in 1986, a partnership with a private sector airline (TAT European Airlines) which is now the leader in express mail with revenues of FF 1.7 billion (\$324.7 million U.S.). La Poste is the main shareholder with 66 percent of equity. This partnership between the public and private sectors has allowed the joint venture company to operate largely free from administrative rules regarding

financing and personnel. The joint venture has been a commercial success.

La Poste has a monopoly in its use of postal network counters (retail outlets). The exception to this rule is Chronopost who may also use La Poste's retail network for its express mail collection and delivery.

Mailbox exclusivity

There is no mailbox exclusivity.

E. Competition

Presence of competition

The arrival of international couriers in the mid-1980s obliged the French authorities to open up first the international express delivery market and then the domestic express market, although the one kilogram (2.2 pound) monopoly limit still applies to parcels.

The competition which has emerged over the last ten years comprises:

- international competitors like DHL, Federal Express and UPS (which has also acquired a number of domestic French delivery agents);
- French delivery and transportation companies in parcel delivery over the 2.2 pound limit; and
- competition from alternative forms of communication. La Poste estimates that revenues of FF 2 billion (\$382.0 million U.S.) are lost each year to the use of faxes.

Presort discounts

Within the reserved service area, reduced tariffs are available from La Poste for companies that presort their mail. La Poste and France Telecom also lease address lists and customer lists to private sector companies.



F. Regulation/Managerial Freedom

Pricing and regulatory oversight

Tariffs for monopoly services (letters and parcels up to 2.2 pounds) must be consistent with the objectives defined in the Contract Plan and authorized by the Ministry of Industry (DPT).

There is no regulation defining limits on prices charged for monopoly services, however, under the current agreement with the Ministries of Industry and Finance, increases in these rates will be pegged to the retail price index through 1997. Tariffs for non-monopoly services are not regulated; however, the two ministries must be advised of price changes.

La Poste admits to the existence of cross-subsidies from the protected letter market to the competitive newspaper delivery service. Competitors in the expedited delivery industry also argue that La Poste does not charge its joint venture, Chronopost, all of the true costs of providing express mail services (i.e., the transfer prices are "cooked"). La Poste disputes these claims. La Poste has also faced an antitrust complaint regarding the issuance of insurance policies. The complaint was rejected by the EC in January 1995.

Major management initiatives must be included within the Contract Plan and are therefore effectively subject to review and agreement with the government. Purchasing is subject to public sector rules requiring a process of open bidding. Purchases above a certain level must be done through a competitive process.

Joint ventures, subsidiaries, and companies purchased

While there are considerable restrictions on La Poste's management freedoms, the service has nonetheless been able to participate in a number of joint ventures. Chronopost is the most significant example. La Poste is also a member of Global Distribution Express Worldwide (GDEW), an international express and remail company which is a joint venture between five postal administrations and TNT.

Other joint ventures have been undertaken with a mix of private sector and public sector companies including:

- Mediapost - direct mail marketing through mail databases in partnership with GMF (an insurance company);
- Sompost - distribution of postal equipment and export of postal technology;
- Sogepost - financial products and management of mutual funds; and
- Dynapost - an integrated processor of corporate mail.

G. Employment

Wage settlement

La Poste employs 300,000 people throughout France and its overseas territories. The rural and urban post office retail outlets are staffed by La Poste employees, which inflates the numbers considerably relative to other postal administrations who have franchised out their domestic retail network.

Most of these employees are civil servants subject to all public sector rules regarding terms and conditions and salaries. There are some incentive programs that are uniquely available to postal employees, including performance premiums and commissions on the sale of financial and insurance-based products.

La Poste employees can strike as a last resort if labor negotiations fail. A particularly damaging postal strike in 1974 substantially interrupted the economic life of the country over a period of several months and is still uppermost in the minds of decision makers when there are any negotiations on pay.

Job protection

Employees of La Poste are viewed as having job security.

H. Financial

Pensions

Pensions for employees of La Poste are the responsibility of the State and there is no separate pension fund. La Poste is charged the current cost of pensions (approximately 27 percent of total salary expenses), rather than the charge being based on a funding of current and future commitments.

The unfunded balance of pensions has not been estimated but would be substantial. It could not possibly be absorbed within La Poste's balance sheet without creating considerable negative net equity.

There is a specific private fund for medical liabilities shared between La Poste and the telecoms company, but the bulk of medical liabilities falls within the national social security system.

Balance sheet

La Poste is not profitable, having registered negative net earnings in two of the last three years. The financial services aspect of the business is particularly unprofitable. The mail side of La Poste's business is now (1993-94) generating relatively small profits, but not sufficient to balance the losses encountered by Financial Services.

There is no provision for the payment of dividends to government.

Taxes

La Poste is liable for income taxes, but has not historically paid any significant amounts due to its financial losses. La Poste must also pay local taxes — real estate taxes and a "professional tax" related to the industrial activity of the company.

Postal and financial services are not subject to the Value Added Tax (VAT) in accordance with current EC guidelines.

Access to capital markets

La Poste is able to access private capital markets to manage its significant cash flow fluctuations.

I. Best Practices/Lessons Learned

Although there have been moves to transfer power from central government to the postal agency, in practice the influence of the government over major managerial decisions remains strong.

The scope of the reserved area is quite large (up to 2.2 pounds), but La Poste's statutory protections are limited by the practical difficulties of enforcing a monopoly only on private correspondences.

The French government has taken a generally conservative approach to liberalization of the postal sector and to reductions in the bureaucratic controls over its postal operator. Interestingly, the government has, however, allowed La Poste to pursue an aggressive policy of responding to competitive entry, particularly in the expedited services market. La Poste has formed a number of joint ventures with private sector firms which have been permitted to operate freely. Chronopost, in particular, has become the market leader in express services.



Germany

A. Corporate Profile

On January 1, 1995 the German postal service was commercialized and renamed Deutsche Post AG (Deutsche Post). Deutsche Post is the largest employer in the German service sector employing more than 360,000 people. In 1993 its predecessor, the Deutsche Bundespost Postdienst (Postdienst), handled 18,946 million items of mail including 646 million parcels and 8,385 million letters. Postdienst maintains 20,000 post office retail outlets.

In 1993 Postdienst recorded an operating loss of DM 173 million (\$114 million U.S.),⁵ due mainly to losses in the new federal states which joined post unification in 1990. The loss is increased substantially to DM 1.7 billion (\$1.12 billion U.S.) when account is taken of the special turnover tax (a contribution to the federal budget) of 10 percent. Though details on the performance in 1994 are not yet released, the chairman has indicated that there have been improvements in turnover and costs which are expected to result in a "good" operating profit.

The letter monopoly currently covers all letters and postcards charged less than 10 times the standard letter rate, which is currently DM 1 (66¢ U.S.). A standard letter is defined by size and must not weigh more than 20 grams (0.7 ounces).

B. Ownership, Structure, and Organization

Corporatization

The German postal service is undergoing a period of fundamental organizational change.

The first reform initiative, which was launched under the heading "Postreform I" in 1989, resulted in the organizational separation of postal services, postal banking, and telecommunications. The operational management was delegated to the

newly created entities which remained, however, part of the federal administration.

After Postreform 1, a new Board of Directors with a number of new members from the private sector initiated the movement towards financial accountability, with private sector management and accounting practices.

A number of commercial reforms have occurred. Deutsche Post AG has been reorganized into four groups: letters, cargo, post offices, and new business segments. A significant reclassification effort simplified the letter service offerings. A new parcel network, including 33 break bulk facilities and 480 delivery bases, is currently being built. Post offices are now allowed to offer a wider range of products. In a recent pilot project, 500 postal agencies were opened in grocery shops and gas stations.

At the beginning of 1995, "Postreform II" transformed Postdienst into Deutsche Post AG, a public corporation which, for now, is 100 percent government owned. The explicit aim of the government is to prepare Deutsche Post AG for privatization, which could occur as soon as 1997.

The commercialization of Deutsche Post required a two-thirds vote of the German Bundestag to modify the Constitution. The new wording of the Constitution guarantees the provision of universal postal services which are appropriate and sufficient. Clarification of this and other policies governing postal activities is found in the *Law for the Restructuring of the Postal Service and Telecommunication*.

At least until 1997, the main responsibility for regulating Deutsche Post remains with the federal Ministry for Post and Telecommunications (BAPT).

Retail Outlets

All of the 20,000 post offices in the retail network are owned by the Deutsche Post AG. Due to a reduction in the demand for retail services (estimated at 30 percent from 1990 to 1993), the postal administration has been gradually closing post offices for some time. However, it stated

⁵ Based on January 25, 1995 exchange rate of \$0.6614 (U.S.).

policy is to ensure that the radius for each post office will be no greater than 2 kilometers (1.2 miles). Deutsche Post has also begun testing postal franchises, for example those in grocery stores and gas stations, to reduce the cost of the retail network.

C. Social Responsibility

Social obligation defined

The universal service obligation is included in the Constitution and defined by federal law which requires Deutsche Post to ensure equal access to postal services for customers in both rural and urban areas.

All monopoly services must be offered at a uniform rate. However, prices for these services must, to the extent possible, reflect market conditions.

The BMPT defines all other social responsibilities of Deutsche Post. Currently these include delivery six days per week and special rates for books and blind persons. The only mandatory, non-reserved service is acceptance of parcels at all post offices.

D. Scope of Monopoly

The definition of the reserved area (the monopoly) has historically been fairly broad by international standards, covering virtually all mail delivery except parcels. In part due to the efforts of the European Commission, it has been narrowed in recent years. Although private sector couriers have operated in both the international and the domestic markets for many years (UPS's strongest foothold in Europe is in Germany), they were only legally recognized in the late 1980s. Armed with the Treaty of Rome and other European laws that restrict anti-competitive activity, these companies have worked for many years to pry open the lucrative German postal market. Due to their efforts, and to the efforts of the European Commission, the scope of the monopoly has been narrowed somewhat in recent years. Deutsche Post has fought to maintain its monopoly protections. In fact, the corporation recently filed a suit against a number of companies (Federal Express, DHL, some postal administrations, and

others) to protect what it views as its monopoly on outbound international mail. The suit also named GDEW, of which Deutsche Post is a founding member. Thus, Deutsche Post is, in effect, suing itself for violation of the monopoly.

The current monopoly includes the delivery of all letters and postcards priced up to 10 times the standard letter rate (DM 1, 66 ¢ U.S.). Parcel deliveries are not protected.

Direct mail

The Minister for Post and Telecommunication can grant licenses for private companies to offer services within the reserved area. In late 1994, the BMPT for the first time licensed private companies to deliver advertisements and printed matters (bulk mail) pieces that weigh more than 250 grams (8.8 ounces). The action opened approximately one-quarter of the estimated DM 3 billion (\$2 billion U.S.) market in bulk printed matter to competition. There has also been talk of lowering the minimum weight threshold to 100 grams (3.5 ounces) in 1996. This would expose approximately 10 percent of Deutsche Post's revenues to competitive entry.

Mailbox exclusivity

Access to mailboxes is not restricted in Germany.

E. Competition

Presence of competition

The liberalization of bulk mail was a result of the lobbying of the delivery warehouses (Versandhäuser) which now hold the licenses. However, additional pressure has been exerted by the remaining activities of international carriers and neighboring postal services, mainly the Netherlands and some east European countries. As a reaction to this increased competition and in anticipation of the liberalization, Deutsche Post has already begun to offer generous discounts to its biggest mailers.

Cross-subsidization from the reserved services to the competitive services is allowed as long as it does not undermine competition as a result of long term and significant pricing below costs. In the latter case, BMPT can instruct that appropriate



changes are made to the tariff and may ultimately refer the issue to the Federal Antitrust Commission.

Direct competition in the postal core business has previously been limited as there was (and still is) no downstream access for private carriers.

Deutsche Post does however see a major threat in alternative forms of communication. In 1993, an estimated one million fax machines sent approximately three billion faxes. This compares to a delivery volume of nine billion letters and postcards. With the accelerating liberalization in the telecommunications sectors, other services, such as e-mail, video conferencing, and voice telephone, will become more sophisticated and cheaper, further eroding the postal service's market share.

F. Regulation/Managerial Freedom

Pricing and regulatory oversight

As regulator, BMPT defines the reserved service and the infrastructure obligation and approves tariffs. There is no clear pricing policy in place, with the Ministry currently considering the introduction of a price cap.

While BMPT has the main responsibility for regulation of Deutsche Post, BAPT controls the ownership rights and is responsible for organizing the transition to the private sector. BAPT was created and is supervised by BMPT and is the body which would be responsible for any capital market transactions of Deutsche Post. It also negotiates with the unions. Hence, in terms of employment and wage setting, Deutsche Post is not yet completely independent.

Authority to purchase suppliers, competitors, and customers

In terms of procurement, mergers, and acquisitions, Deutsche Post may act as though it were a private sector company. It is not clear yet how boldly this freedom will be used in the future. To date there have been no acquisitions and the only strategic move has been the formation of EMS Kurierpost which now competes with private courier services.

Deutsche Post AG uses open bidding processes for procurement. However, it is not subject to governmental procurement policies.

G. Employment

Wage settlement

The responsibility for industrial relations currently lies with the Agency for Post and Telecommunications. Civil servants are not allowed to strike. Other employees, however, can and have.

The power of the unions in the postal sector has traditionally been strong. Even after the separation of the postal service, the telecom, and postal banking, the postal union continued to represent all three companies' employees.

Overall, employees have secured a high level of benefits since Postreform II. The unions used strikes and political pressure on the opposition party, the Social Democrats, to achieve this aim.

H. Financial

Pensions

The German postal administration has a large unfunded pension liability, estimated at over DM 60 billion (\$40 billion US). If all the pension liabilities of Deutsche Post were to be put on its balance sheet, the postal service could not have become a public company due to a significant negative net asset position. To solve this problem, separate funds have been created which are liable for pension payments and support payments. The funds will be financed by dividends and proceeds from privatization. After a transitional period, Deutsche Post will have to contribute payments at a rate which is capped by the rate of payments typically experienced in the private sector. The government ultimately guarantees the payment of pensions and support by the Fund.

Taxation

Beginning in 1996, the special tax (10 percent of turnover) will be abolished and normal taxation of profit will apply. However, the postal service is not subject to the Value Added Tax (VAT) and, under

present European Commission legislation, is unlikely to be subject to VAT in the foreseeable future.

sheet of carrying the unfunded liability, is a particularly interesting feature of the restructuring.

Access to capital markets

The company can access funds on the capital market but its actions are subject to agreement by the annual General Assembly. The post's subsidy from Deutsche Telecom AG will be eliminated in 1996.

Dividends

In principle, Deutsche Post AG will earn a profit and pay dividends like any other public company. However, for the foreseeable future, the corporation will commit any profit it earns to finance its pension and support liabilities.

Antitrust

The postal service in Germany has not been challenged by the German antitrust agency. However, extensive lobbying by the European Commission and industry associations in Germany has put pressure on the Ministry for Post and Telecommunication to liberalize.

1. Best Practices/Lessons Learned

There have been substantial changes in Germany over the past six years. Pressure for change has come from increasing competition resulting from improved and innovative telecommunication services, the re-mail activities of private operators and neighboring postal services, and through pressure from the European Community.

Despite the uncertain environment, the German postal service has been considerably restructured and the management is endeavoring to transform the biggest German service company from an organization of civil servants into a private company. The new regulatory structure is not clear and is a compromise, resulting from the required broad consensus needed for changing the constitution.

The use of a special pension fund, to avoid the significant impact on Deutsche Post's balance



The Netherlands



A. Corporate Profile

The Dutch Postal Service, PTT Post BV, is one of two divisions (the other being PTT Telecom BV) of the holding company Koninklijke PTT Nederland NV ("KPN"). Currently, the government owns 70 percent of KPN's shares. The other 30 percent of the shares are traded on the Amsterdam Stock Exchange.

PTT Post BV maintains a monopoly over the delivery of letters via its exclusive concession with the government. Approximately 55 percent of PTT Post's revenues are earned from services outside the scope of the exclusive concession.

Total revenues of PTT Post increased from NLG 4,700 million (\$2,774 million U.S.)⁶ in 1991 to NLG 5,400 million (\$3,187 million U.S.) in 1993. In the same period, operating income and net profit increased from NLG 355 million (\$210 million U.S.) and NLG 260 million (\$153 million U.S.) to NLG 460 million (\$271 million U.S.) and NLG 370 million (\$218 million U.S.), respectively.

The number of employees decreased by 4,000 full time equivalents to 56,000 in 1993. Total mail volume increased from 6,150 million items in 1991 to 6,225 million in 1993. The basic rate for a domestic letter of up to 20 grams (0.7 ounces) is NLG 0.80 (47¢ U.S.).

B. Ownership, Structure, and Organization

Corporatization

KPN became a wholly government-owned corporation on January 1, 1989. In June 1994, the corporation issued shares equal to 30 percent of equity on the Amsterdam Stock Exchange. The Dutch postal service is the first postal administration in Europe to be partially privatized. A further issue of approximately 30 percent is due in 1996-97, reducing state ownership to less than 50

percent. The government has stated that it plans to hold at least 30 percent of the shares in PTT Post until 2005. The government also retains an option to acquire preference shares in order to retain a majority of the voting rights.

Financial mandate

PTT Post is a profit-making corporation. However, its ability to earn profits is to some extent limited by a cap on monopoly (concession) prices equal to the increase in the Dutch national wage index.

Management structure and board oversight

The Board of Directors consists of five persons and the supervisory Board comprises seven to nine persons. The Minister of Transport has the right to appoint three members, of which one is to be appointed in agreement with the Minister of Finance and one in agreement with the Minister of Economic Affairs. The other members are elected by the government appointees. PTT Post reports annually to the Ministry of Transport on its execution of concessionary activities.

Retail outlets

There are two kinds of retail outlets: official post offices and representative offices (small offices often located inside shops). All outlets are organized in a joint venture called Postkantoren BV. The joint venture is owned by PTT Post (50 percent) and the Postbank (50 percent), a 100 percent subsidiary of a leading Dutch financial institution, ING. The small representative offices are operated on a franchise basis.

Cooperation between PTT Post and Postbank dates back to when both companies were fully state owned. Postbank was privatized in 1986 and merged with the NMB Bank in 1989 into NMB Postbank which merged with the Dutch insurer Nationale Nederlanden into Internationale Nederlanden Groep (ING) in 1993.

Postkantoren BV receives a fee for each transaction according to the added value it provides. Apart from Postbank (50 percent of all transactions) and PTT Post (30 percent), government departments are important contributors to transactions (e.g., car

⁶ Based on January 25, 1995 exchange rate of \$0.5902 (U.S.).



registrations). The two shareholders supply a fixed sum as an infrastructure fee.

The joint venture was set up as a separate entity to allow for a more market-oriented management approach. Recently, there have been efforts to upgrade the post offices by improving the interiors and adding more functions (e.g., travel agencies).

C. Social Responsibility

Social responsibilities are set out in the general rules for PTT Post. These responsibilities include the provision of universal service at uniform tariffs and domestic delivery six days a week. These social obligations are explicitly defined in the concession agreement.

Obligations to investors are defined by the general rules of the Amsterdam Stock Exchange.

D. Scope of Monopoly

Extent of monopoly

Dutch law defines specific mandatory services assigned to the postal administration. These include:

- the obligation to carry all postal items up to 10 kilograms (22 pounds), including those from and to other countries;
- public services should be offered on the same conditions and tariffs nationwide;
- minimum requirements regarding the density of post offices and boxes in urban and rural areas;
- delivery every day except Sundays; and
- next day delivery for domestic mail.

The exclusive (monopoly) rights, which are granted under the terms of the concession, include:

- the carriage of letters up to 500 grams (1.1 pounds);
- the installation of post boxes on public grounds; and
- the issuance of stamps with the portrait of the monarch and the word 'Nederland'.

Courier services are excluded from the concessionary benefits and exempted from the mandatory obligations in order to comply with European Community competition rules.

Direct mail is not part of the monopoly.

Mailbox exclusivity

There is no exclusivity regarding delivery to mailboxes by PTT Post.

E. Competition

Like other postal administrations, PTT Post BV faces significant competition from traditional and electronic services. However, PTT Post is generally viewed as an aggressive competitor, particularly in the international market, probably the most aggressive of all European postal administrations. In fact, PTT Post has been vocal in its support for other remailers' and express carriers' attempts to pry open the European international mail market.

Currently, PTT Post faces competition in several areas:

- Letter Mail - Above the concession threshold (500 grams, 1.1 pounds), PTT Post faces competition from so called City Mail companies. These companies have also attempted to bypass PTT Post's exclusive concession by delivering lighter weight pieces. The government has responded with lawsuits that have effectively reduced the market share of City Mail companies to approximately two percent.
- Direct mail and periodicals - PTT Post faces competition from local delivery companies who also deliver newspapers door-to-door. PTT Post's market share in direct mail is only 15-20

percent but this type of mail accounts for less than 15 percent of total mail volume. PTT Post's market share in periodicals is 60 percent. Most remaining periodicals are delivered by a subsidiary of a large publishing company (VNU).

- **Parcels** - PTT Post's market share in parcels up to 30 kilograms (66 pounds) is 40 percent. A competitor services approximately 30 percent of the market. In the long run, competition from non-Dutch competitors is expected.
- **Courier services** - Competition is fragmented, with more than 1,000 companies active. PTT Post's market share is 40 percent.
- **Logistics** - PTT Post owns a warehousing and fulfillment company. This subsidiary faces competition from a number of other logistics companies.

Further liberalization of the market by the government will lead to a reduction in the tariff level above which rival companies are allowed to offer courier services — from approximately NLG 11 90 (\$7.02 U.S.) to about NLG 7 50 (\$4.43 U.S.). The European Union may also introduce more competition into cross-border mail traffic in the medium term.

F. Regulation/Managerial Freedom

Pricing and regulatory oversight

The following restrictions on PTT Post's concession apply:

- **Tariff-control system** - Price increases may not exceed increases in the Dutch national wage index. Within this limit, PTT Post can set prices freely.
- **Announcement of general conditions** - Changes in the general postal conditions are subject to consultation with a committee, which comprises representatives of consumer, employee and employer organizations as well as representatives of large customers.

- **No cross-subsidizing** - Prices charged for concession (i.e., monopoly) services may not subsidize non-monopoly services. PTT Post is also subject to European Union antitrust legislation.
- **Universal service delivery** - Postal services must be offered at a uniform rate across the Netherlands. Volume discounts are permitted as well as discounts to individual large users. PTT Post is obliged to operate a network of post offices throughout the Netherlands. An agreement has been drawn up with the Ministry of Transport regarding the spread and density of this network.
- **Post concession reporting** - Every year PTT Post must supply the Ministry of Transport with a report regarding the activities executed concerning the concession. Every two years PTT Post supplies the Ministry with the prospects for the next five years.

Authority to purchase suppliers, competitors, and customers

The liberal regime in the Netherlands provides few if any restrictions on the activities of PTT Post. It can act like any other private company with respect to purchasing. PTT Post is also allowed to purchase suppliers, competitors, and customers. Below is a partial list of joint ventures and subsidiaries currently held by PTT Post:

- **Courier services** - City courier Nederland BV; Wini Traffic Couriers (100 percent); Geldnet BV (50 percent) (money transport); GD Net BV (18 percent); and Global Distribution Express Worldwide (9 percent).
- **Parcels** - Leerdoms Vervoers Centrum BV (100 percent).
- **International mail handling** - PTT Post Caribbean NV (100 percent); Interpost Group of Comp BV (50 percent); and International Mail Handling (60 percent).



- Postoffices - Postkantoren BV (50 percent): joint venture with Postbank, a subsidiary of ING Bank.
- Market Research - Geo-marktprofiel (35 percent).
- Direct Mail - Independent Mail BV (35 percent) and Mailprofs BV (50 percent).
- Logistics - Logistiek (100 percent).

G. Employment

Wage settlement

Prior to its commercialization, wages within PTT Post were set by the government at relatively high levels compared to industry norms. The working conditions and wage levels were not affected by the commercialization. The pension fund was transferred in the commercialization from the governmental Algemeen Burgerlijk Pensioenfonds (ABP) to a new corporate pension fund. The pension fund is fully funded and is external to the parent company.

KPN is the largest employer in the private sector and its wage increases are an unofficial benchmark in the Netherlands. Large companies in the Netherlands operate under Collective Labor Agreements (CLA), for which the management bargains with unions. A total of 99 percent of the workers are covered by this CLA.

In the event labor negotiations fail, a strike may occur. The employer can go to court and ask the court to force the workers back to work. Historically, the courts rule in favor of the employees' right to strike but they can force the parties to reenter negotiations.

Job protection

Labor relations in the Netherlands are based on a much higher degree of consultation between management and unions than is the case in, for example, the U.K. or the U.S. In general, the record of relations with unions is good, although the company did suffer a strike among postal workers in December 1989. There are no regional variations

in compensation. Employees were offered shares in the 1994 public offering but the take up is not publicly known.

Compensation

A stock option plan for the Board of Directors and a number of senior managers has been in place since June 1994. A maximum of 1 million options for ordinary shares can be distributed among these officials.

The KPN employees were granted the possibility to subscribe to convertible bonds up to NLG 10,000 (\$5,902 US) per employee in the June 1994 public offer. The bonds could be converted immediately thereafter into ordinary shares.

H. Financial

Services provided by PTT Post are not subject to the Value Added Tax (VAT), but PTT Post is subject to income tax. On January 1, 1996 PTT Telecom, the other main subsidiary of KPN, will be subject to VAT.

Investment decisions are made by management. The Dutch government can only exercise control through its Supervisory Board members' influence.

The management board of KPN can issue shares but needs approval of the Supervisory Board and the shareholders.

Dividends

The dividend payout ratio was 50 percent in 1993 (40 percent in 1992). The company has stated this level will be maintained or may even increase further in the future.

Antitrust

No antitrust measures have taken place

I. Best Practices/Lessons Learned

PTT Post is recognized as being one of the most commercial and competitive postal administrations in Europe. Privatization, albeit only partial so far and under the umbrella of a joint telecom and

postal holding company, has allowed PTT Post to enjoy commercial freedoms which have few equivalents in Europe. These freedoms have helped PTT Post aggressively pursue and capture remail business in neighboring countries.

It is not entirely clear why the postal and telecommunication businesses were not separated as has been the case in most PTTs in Europe. However, keeping the two together has certainly increased the speed of commercialization and privatization of the postal service. In Europe, telecommunications reform is significantly ahead of postal reform (e.g., Deutsche Telecom will become private well before Deutsche Post).



New Zealand

New Zealand Post



A. Corporate Profile

New Zealand Post Limited (NZP) is a State-Owned Enterprise (SOE) serving 3.4 million New Zealanders. In FY 1993-94, NZP collected and processed 724 million letters for delivery to 1.4 million delivery points, an increase in volume of 5.9 percent over 1992-93. NZP owns 245 "Post Shops" (retail outlets) and postal services are also available from an additional 644 Post Center franchises. NZP employs 8,670 people full-time and part-time, a reduction of 40 percent since 1987.

For the year ended March 31, 1994, NZP revenues were NZ \$620 million (\$399.8 million U.S.),⁷ with net pre-tax earnings of NZ \$99.7 million (\$64.3 million U.S.). NZP has total assets of NZ \$425 million (\$274.0 million U.S.).

The standard letter price is NZ 45¢ (29¢ U.S.) for delivery anywhere in New Zealand. Standard letters of larger size cost NZ 80¢ (52¢ U.S.), and envelopes above 1 kilogram (2.2 pounds) in weight are classified as parcels.

B. Ownership, Structure, and Organization

Corporatization

New Zealand Post Ltd. is a "State-Owned Enterprise" (SOE) with shares held by two Ministers of the Crown, the Minister of Finance and the Minister of State-Owned Enterprises. Ministers cannot sell or allot any of the 120 million \$1 shares (64¢ U.S.). It operates as a limited company under the 1955 *Companies Act*, the 1986 *State-Owned Enterprises Act* (SOEA), the 1987 *Postal Services Act* (PSA), the *Commerce Act*, and the *Fair Trading Act*, as well as its own Articles of Association.

Prior to the 1987 corporatization, NZP was classified as a Trading Department, was combined with telecommunications and banking operations, and was highly regulated. The 1987 reform was

part of the Labor government's microeconomic reform program.

Currently, there appears to be little pressure from any political party to privatize NZP. There has been discussion of privatization in recent years, particularly in connection with the government's "assets sales program." However, the NZ government announced in November 1994 that it has absolutely no intention of privatizing NZ Post. Indeed, the 1980s liberalization moves appear to be losing momentum, with the recent government announcement of full postal deregulation being contested both by the opposition and by members of the government.

NZP's objectives derive from the 1986 *State-Owned Enterprises Act*, which states that the principal objective of an SOE "shall be to operate as a successful business and, to this end, to be:

- as profitable and efficient as comparable businesses that are not owned by the Crown;
- a good employer; and
- an organization that exhibits a sense of social responsibility by having regard to the interests of the community in which it operates and by endeavoring to accommodate or encourage these when able to do so."

A "good employer" is only defined in terms of a fair personnel policy and good working conditions, not in terms of wages or employment levels.

Financial mandate

The financial mandate is to be profitable. In the 1994 annual Statement of Corporate Intent, required under the SOEA, performance targets are set for three measures of profitability:

- operating earnings (after tax) to average shareholder funds (22 percent target);
- operating earnings (before interest and tax) to total tangible assets (17 percent target); and

⁷ Based on January 25, 1995 exchange rate of \$0.6448 (U.S.).



- Operating earnings (before interest, tax and depreciation) to turnover (16 percent target).

In 1994, the return on assets was 30 percent. Targets for the next three years are envisioned to drop off to approximately 17 percent in 1997. NZP pays dividends to the federal government.

Management structure and board oversight

The Ministers of Finance and of State-Owned Enterprises appoint the Board's Directors, who number between five and nine. NZP must report to the Ministers biannually, and in practice provides Ministers with quarterly reports. NZP is also required under the SOEA to provide a "Statement of Corporate Intent" to Ministers outlining the corporation's three-year strategy. The SOE structure is designed to provide the Board with considerable autonomy in operational decision-making.

A third ministry, the Minister of Communications, is the regulator, with responsibility for administering the 1987 *Postal Services Act*.

The Board sets the strategic direction for NZP and appoints the Chief Executive Officer. Approximately 50 percent of senior management in NZP now comes from the private sector.

NZP has had four management structures since corporatization. Initially, a functional structure was developed with four geographical regions reporting to the head office. This structure gave prominence to new areas of strategic and business planning, finance, and marketing and helped drive the initial cost reduction exercise. Then a "divisionalized" structure was used, with "Letters," "Commercial Services," and "Property" Divisions. This assisted during the main phase of rationalizing the property portfolio. The third structure was a "matrix organization," with three cost centers (letters, sales and retail, couriers and parcels) and two marketing groups, with the purpose of making the organization market-driven. From January 4, 1995, NZP will have a profit center structure based on five business units: letters, "consumer" (retail), "distribution" (parcels), international, and "Post Plus" (e.g., electronic services).

Retail outlets

NZP's 245 Post Shops are wholly owned by NZP. They have been renamed (from Post Office) as an attempt to change their image. Post Shops are experimenting with a wider range of products (e.g., traveler's checks and mailing labels) and have established a service standard that 95 percent of customers wait no longer than two minutes in line.

A second tier of NZP's retail network is made up of 644 privately owned outlets, franchised by NZP. NZP has been extending the Post Shop computer network into this privately-owned network and has provided assistance through training. The third tier of the network is made up of stamp retailers and stamp booklet outlets, which are totally private.

Over the last five years, there has been a small decrease in NZP-owned Post Shops, a small decrease in franchises, and a large increase in the number of stamp retailers (from less than 1,000 to over 3,000 in five years). The number of Post Shops and franchises are defined in the Deed of Understanding.

C. Social Responsibility

NZP's social responsibilities are described in general terms in the SOEA and in a "Deed of Understanding" which NZP negotiates with the government in return for a continued level of monopoly protection. The Deed of Understanding sets out the requirements that NZP should:

- operate a universal letter service in NZ;
- charge a uniform price for a standard ("medium") letter throughout New Zealand;
- maintain specific delivery services (e.g., six days per week to 95 percent of households); and
- maintain its retail network at certain specified levels (e.g., the Deed requires at least 240 "postal outlets" and 880 "Post Centers" and postal delivery centers).

The Deed of Understanding also covers prices and delivery standards.

The initial idea behind the Deed was that it would make transparent NZP's obligations and also act as a device for reducing political interference and political reaction to unpopular decisions. NZP's management believes that the Deed has served its purpose. They also state that the agreement has not imposed any obligations on the corporation that it would not otherwise seek to fulfill for business reasons.

However, it should be noted that the Deed has been renegotiated on a number of occasions. While this risks the return of political interference, NZP feels it gives them a voice.

One characteristic of the Deed stressed by NZP is its legal status. It is a contract, but one that is only enforceable by the government. If private individuals or businesses wish to challenge NZP about their services, judicial review of NZP is only against statutory obligations (e.g., in the SOEA).

D. Scope of the monopoly

Extent of the monopoly

NZP's monopoly is restricted to letters below 200 grams (7.1 ounces) in weight and below NZ 80¢ (51¢ U.S.) in price. This price threshold is quite low by international standards. It has been reduced in phases over three years, beginning at NZ \$1.75 (\$1.13 U.S.).

Within this letter category, there are three key exemptions from the monopoly:

- "delivery by an employee of the sender";
- unaddressed direct mail; and
- legal document exchanges.

The government announced in November 1994 that it would introduce legislation to completely deregulate the postal market. NZP has welcomed this proposal. The legislation is expected to be introduced in Parliament in late February 1995 and to be implemented by July 1, 1995. However, there is strong political opposition, and the government

only has a majority of one. As in the U.K., it is possible that backbenchers may prevent further liberalization.

Unaddressed direct mail is not included in the monopoly. Addressed direct mail below the threshold is included in the monopoly.

Although there are no other mandatory services, NZP believes that, in practice, it would not be possible to withdraw its parcels service (and it would not want to as it is profitable).

Mailbox exclusivity

There is no mailbox exclusivity.

E. Competition

Presence of competition

NZP has a number of competitors and deregulation has certainly encouraged this competitive presence.

In the express documents and parcels market, international courier companies such as DHL and TNT are active, as are local companies such as the Freightways Group.

Companies taking advantage of the monopoly exemptions include "NZ Document Exchange," several contract delivery companies, and "Circular Distributors." Various local government authorities and utilities also deliver their own mail.

NZP is preparing for the entry of competition into its core markets. They believe costs of entry are low, and that existing delivery companies can easily move into traditional mail services.

Presort discounts and downstream access

NZP offers a number of presort discounts for bulk mailers. Interestingly, however, to limit competition, NZP will not offer discounts to consolidators who combine mailings from more than one source.

Downstream access is not currently allowed, although there is some pressure for this to be permitted.



F. Regulation/Managerial Freedom

Pricing and regulatory oversight

NZP is free to set prices for all services, except the price for standard letters which is subject to a price-cap rule set in the Deed of Understanding. The price cap is the Consumer Price Index minus one percent. Since 1987, the price of a standard letter has increased 12.5 percent, including a tax rise of 2.5 percent, while the price index has increased by 31 percent.

Authority to purchase suppliers, competitors, and customers

NZP is free to invest and acquire other companies, although shareholder (i.e., government) approval is needed to buy more than 20 percent of another company.

The Statement of Corporate Intent states that "the company may invest in the shares of another business when the shares acquired are consistent with the nature and scope of NZ Post's business and considered likely to bring added value to the business of the company." NZP may also "invest in shares of another business operating outside the nature and scope of NZ Post's business. In these circumstances, specific endorsement by the Shareholding Ministers will be sought."

In 1988, NZP acquired shares in Datanet Ltd., which owns and operates a digital network. NZ Post has also acquired a wholly-owned subsidiary company, Synet, to develop business in value-added services. Synet operates a multimedia network offering electronic messaging facilities.

Antitrust

NZP is governed by the Commerce Commission under the Commerce Act. The New Zealand regulatory regime was described as "light-handed." While NZP has been accused of predatory pricing and cross-subsidizing by competitors, to date there has been no investigation or prosecution.

Procurement flexibility and oversight

Procurement policy guidelines are drawn up by NZP's Chief Financial Officer and agreed to by the Board.

Capital expenditures tend to go to the Board, although the CEO and senior managers have set authorization limits.

Oversight is provided by an internal audit team and ultimately by the Board, plus reviews at a company-wide level by the Auditor-General and the Crown Company Monitoring Unit.

Joint ventures and subsidiaries

NZP is free to enter into joint ventures and operate subsidiary companies. For example, it has a joint ownership, 50/50 venture with Gallagher Mailing Services, Ltd. in a company called GMS Fulfillment Services which provides inventory and warehousing services and just-in-time delivery services for corporate clients.

G. Employment

Wage settlement

Wages for most employees are negotiated in a collective agreement on an annual basis. The 1994 agreement, however, is for two years. This agreement is binding and is registered with New Zealand's Labor Court. Industrial relations have generally been good, and there have been no strikes for many years.

Compensation and wage premiums

Before the recent wage negotiation, NZP undertook a survey of "market rates," comparing the wages of its employees with employees in similar jobs in other firms, and will gradually aim to adjust its salaries to these market rates.

A delivery carrier ("postie") earned approximately NZ \$23,200 (\$14,959 U.S.) in 1994, which is approximately NZ \$3,000 (\$1,934 U.S.) less than the market rate. A teller in a Post Shop earned NZ \$26,400 (\$17,023 U.S.), around NZ \$1,500 (\$967 U.S.) above the market rate. A driver was paid NZ \$23,700 (\$15,282 U.S.), around the market rate. Incentives exist for superior performance, though



they are being reformed. Currently, anyone who is judged to have performed well may be promoted two steps on the pay scale in a year, rather than one. There is also a company-wide profit-related bonus.

Senior managers have individual contracts. When specialists were brought in after 1987, some salaries were tied to market rates, but, in general, management pay levels are still below private sector levels. Bonus schemes are tied to a formula.

Job protection

The main employment change after corporatization came in employment numbers rather than wage rates. NZP has shed approximately 40 percent of its labor force since 1987.

NZP avoided disputes by seeking voluntary redundancies and by providing incentives for early retirement and various other attractive redundancy packages. It also consulted closely with the unions, who saw change as inevitable, and blamed the government rather than the management.

Before corporatization, employees were public servants, with some job protection. There is no permanency of tenure in the new NZP contracts.

H. Financial

Pensions and negative balance sheet

NZP has no unfunded pension or medical liabilities. Its balance sheet is healthy.

Dividends

The Statement of Corporate Intent specifies a dividend target level for NZP each year. The dividend is payable to the government. In 1994 the total dividend payment was NZ \$50 million (\$32.2 million U.S.). This represents 75 percent of operating earnings after tax and is significantly higher than the 50 percent target level in the Statement of Corporate Intent.

Taxation

NZP pays the same taxes as any company. In 1993-94 it paid NZ \$33.7 million (\$21.7 million U.S.) on the year's earnings.

Access to capital markets

NZP is free to raise capital and borrow at commercial rates and on commercial terms. It has lines of credit with four banks, and can even issue equity bonds.

Control of Treasurer over Investments

NZP's Chief Financial Officer recommends the guidelines for treasury policy and managing cash flow to the Board.

I. Best Practices/Lessons Learned

NZP's experiences in postal reform indicate that an appropriate political climate can be an important driving force for change.

Postal liberalization in New Zealand must be seen in the context of the economic policy of the government at the time of corporatization in 1987. It was a government with a clearly defined and radical program of economic reform, and NZP was simply one element of that reform program.

As part of this reform program, the *State-Owned Enterprise Act* drew up the framework for all the corporatizations of government-owned organizations in New Zealand. This framework enabled postal reform to be pushed through quickly within a favorable political environment.

After the Act was passed, Ministers appointed a top class, commercially minded Board, with an ambitious Managing Director. With political interference at a minimum during the first years, management was able to introduce a program of rationalization and to be innovative in all aspects of the business.

Thus, the key ingredients of success were the external political environment and the quality of management.



Outside the political context, the lessons learned from the NZP experience include:

- Seek to operate as a commercial organization (e.g., accounting principles, pricing competition) even if wholly owned by government.
- Deregulation may not be a threat if management freedoms come with it, and if management is allowed several years to reform prior to deregulation. Plans for future deregulation are a useful tool for promoting change.
- Rate regulation and other forms of regulation will be counterproductive if a postal administration is allowed to act commercially. The NZP experience indicates that rates are best kept low through commercialization rather than direct regulation.
- Major change need not be done through privatization.
- Social obligations may not be as onerous as originally believed by management, once the freedom to manage is established.
- Cost control is a priority in the early days of reform. Changes to work force size may be easier than changes to wage rates and will be borne more stoically if wage rates are maintained or improved.
- Innovations in the basic product/service portfolio can assist the process of change by signaling a new confidence.

Sweden



A. Corporate Profile

The Swedish postal administration, Postverket, was changed from a public corporation into a state owned corporation on January 1, 1993. Sweden Post (Posten AB) is the largest service and communications organization in Sweden. In 1993 Sweden Post's revenues were £2 billion UK sterling (\$3.2 million U.S.)⁸ from volume of 4.2 billion mail items. Customers can deposit their mail at 1,900 post offices, 40,000 letter boxes, and 350 private retailers. Posten AB employed 50,213 employees in 1993, a decrease from 56,415 in 1991.

In the financial year 1992-93, Sweden Post's profit was SEK 1,363 million (\$183.1 million U.S.), down from SEK 1,413 million (\$189.8 million U.S.) in 1991-92. Total revenues decreased from SEK 22,096 million (\$2,967.5 million U.S.) in 1991-92 to SEK 21,644 million (\$2,906.8 million U.S.) in 1992-93.

The price of a standard letter for domestic delivery weighing less than 50 grams (1.8 ounces) is SEK 3.70 (50¢ U.S.), which includes a Value Added Tax (VAT) of 25 percent (changed from 12 percent after Sweden joined the EU). The rate is uniform throughout Sweden.

Discounts are available to bulk mailers and are negotiated on an individual basis, but under Sweden's competition law, they can only be given in relation to explicit criteria, even if these discounts are not published.

B. Ownership, Structure, and Organization

Corporatization

Sweden Post is a public limited company. The company's only shareholder is the State of Sweden. The owner's requirements are that Posten AB shall operate commercially under market

conditions and generate a return on capital comparable with that of major well-managed Swedish companies in similar industries. The postal market is completely deregulated, after the abolition of the monopoly on standard letters on January 1, 1993.

Financial mandate

The Postal Law does not state any formal financial mandate for Sweden Post. Prior to corporatization, it was required to be profitable, finance its own investments, and survive on its own resources. An internal management objective is for a 5 percent return on sales to cover future investments.

Management structure and board oversight

The government appoints a 10 member Board of Directors which consists of a Chairman of the Board, three representatives from the unions, a civil servant, and five members from the private sector. The Board appoints the senior management.

Organization

Sweden Post is made up of six business areas: Postgirot, Sweden Post Banking and Counter Services, Sweden Post Letters, Sweden Post Parcel, Postnet, and Sweden Post International.

Postgirot handles payment transmissions and is responsible for the nationwide cash handling service. Post Banking and Counter Service is responsible for Sweden Post's counter network, offering the entire range of mail services to private individuals and small businesses as well as banking services. Sweden Post Letters delivers individual and mass-produced messages, newspapers and periodicals throughout Sweden. Sweden Post Parcel is responsible for standardized, nationwide transport services for packages up to 35 kilograms (77 pounds). Sweden Post International is responsible for marketing and distribution of letters and parcels destined for delivery outside Sweden's borders, customs clearance, and distribution of all letters and parcels arriving in Sweden from abroad. Postnet provides electronic messaging and information services to corporate customers and consumers.

⁸ Based on January 25, 1995 exchange rate of \$0.1343 (U.S.).



Each business area is responsible for products, sales, production, and profitability within its area of accountability. Posten AB is the holding company.

Range of business

Posten AB provides traditional postal services, such as delivery of letters and parcels, as well as banking and electronic messaging services. Posten AB is the market leader in hybrid mail services, currently with 10 percent of all transactions mail originating as electronic mail.

C. Social Responsibility

Social obligation defined

Posten AB's social responsibility is defined in the *Postal Service Act* of January 1, 1993. An overview of these obligations is provided below.

Universal service

The new Postal Act guarantees the general public a universal service at a uniform price. The state has a contract with Sweden Post for the Post to provide that universal service. This will be reviewed in a few years and, if competition has advanced sufficiently, other operators will also have an obligation to provide universal service.

The cost of this social commitment (loss realized by providing the services) amounted to SEK 400 million (\$53.7 million U.S.) in 1993 and was partly covered by government payments. The loss results from the distribution of certain newspapers, discounts on association letters, free delivery of literature to the blind, defense planning, and services in low population areas for the elderly and the disabled. (No compensation is paid by the State with regard to the deficit on newspaper delivery and discounts for associations' letters.)

Delivery frequency

For the most part, letters and parcels are delivered five days per week. However, Sweden Post is not required to maintain this delivery frequency to the most remote areas in Sweden, although in practice it does.

Retail network

Sweden Post is not required to maintain a specific number of retail outlets. Posten AB is free to close postal outlets in remote areas, although it is recognized that Posten AB has a duty to manage the process carefully. The regulator (National Postal and Telecom Agency) does monitor Posten's policy regarding post office closings. In practice, Posten has adopted a policy of franchising post offices.

Sweden Post provided retail service in 1,878 post offices in 1994. This is down from 2,169 in 1989. Retail outlets include Posten AB wholly-owned post offices (1,341), fully franchised outlets owned by individuals (363), "trial" post offices such as mobile outlets (92), and franchises with limited services (82).

D. Scope of Monopoly

No monopoly on delivering letters and parcels to addresses has existed in Sweden since January 1, 1993.

A new authority, the National Postal and Telecom Agency (Post- och Telestyrelsen), has been established to regulate competition and service quality. The regulator will be responsible for overseeing the activities of all letter delivery companies, not only Posten AB.

Mailbox exclusivity

There is no mailbox exclusivity.

E. Competition

The *Postal Services Act* allows for full competition in postal and counters services. For now, however, Posten AB is the only operator required by contract to provide universal letter service.

Competition prevails in the market for the distribution and transportation of goods (market share data is collected but considered confidential). In this sector, main rivals are ASG and Blispedition haulage companies. However, in the distribution of parcels up to 35 kilograms (77



pounds), Sweden Post Parcels is the dominant player. In the distribution of letters, Posten AB's biggest competitor is CityMail. In unaddressed Direct Mail, competitors include SDR and several smaller, regionally based companies.

F. Regulation/Managerial Freedom

Pricing and regulatory oversight

Posten AB is free to set all its prices, except for the standard domestic letter. The government and Posten AB have agreed to a price cap on the domestic letter rate equal to the standard consumer rate of inflation. The charge to private individuals for delivery of a letter up to 500 grams (1.1 pounds) may be increased by a maximum of the average change in the net price index over a three-year period.

While the price cap on letter mail is not itself unique, it is interesting to note that, even though Sweden Post has no monopoly over letters, letter rate increases are still limited by an agreement with the government.

Authority to purchase suppliers, competitors, and customers

Posten AB is free to acquire and invest in other companies. Posten operates an open bidding process for many purchases, but there is discretion, especially when managers are developing long-term links with suppliers.

Joint ventures and subsidiaries

Posten AB is free to enter into joint ventures and form subsidiaries. For example, Sweden Post International has formed Nordic Postgroup BV and, through this subsidiary, participates in a joint venture with four other postal organizations and TNT.

Sweden Post Parcels has several subsidiaries including Hultbergs Inrikes Transporter AB, which operates as a sales company for nationwide deliveries of newspapers, magazines and spare parts, and Posten Express AB which produces and sells express services and operates a messenger service in Stockholm.

Antitrust

Posten AB is governed by the normal competition laws of Sweden. Sweden Post has been the subject of antitrust complaints. A competitor successfully argued that ePost (hybrid mail service) was engaging in unfair competition through cross-subsidization. A court required that Sweden Post charge a higher price and alter its accounting practices for ePost services.

G. Employment

Wage settlement, compensation, and premiums

The number of employees has fallen from 56,500 in 1989 to 50,200 in 1993. Posten AB worked closely with the two unions during this period.

The annual wage negotiation process involves two steps. First, there is a central collective bargaining process between the government and a body representing the two unions. This step decides general public sector wage rates. Second, there is negotiation between individual unions and management.

If collective bargaining fails at the national level there is the possibility of a strike. Outside arbitrators may be used to broker a settlement but this process is not binding. Strikes are forbidden if collective bargaining fails in the second step.

The wage structure of Posten AB is analogous to industry norms of companies of comparable market orientation. There is scope for performance-related pay and incentives relating to corporate performance, individual performance, and quality of service. Minimum pay for an employee of 18 years of age is SEK 9600 (\$1,289 U.S.) per month. Posten employees are regarded as earning approximately five to ten percent above the market average.

Job protection

Employees in Posten AB have no job security and can be laid off at any time. However, 3,000 employees are still covered by the public corporation employment law, and will automatically be guaranteed a new job if made redundant in their present position in Posten AB. Beginning July 1,



1995, Posten AB's conditions of employment will be regulated by a new employment code specifically formulated to suit the new role of the State Owned PLC.

H. Financial

Pensions

Posten AB employees were previously covered by government pension plans, but Posten has now established its own plans. During the recent transition, Posten AB agreed to take on pension liabilities for its employees. In return, Posten AB will not have to pay a dividend to the government for several years.

Balance sheet

Posten AB has no access to government funds or capital for operating shortfalls. In recent years, Sweden Post has been profitable (see Corporate Profile section) and its balance sheet has been improving.

Dividends

Posten AB will eventually pay dividends, but will not do so until the equity/assets ratio improves. The current ratio is weak, owing mainly to the pension commitments taken on by Posten AB.

Taxation

Posten AB is subject to income taxation as laid down by the Company law. As part of the transformation into a commercial corporation, exemption from the duty to charge VAT on letter, newspaper, and parcel deliveries ceased. The standard universal VAT rate on all services amounts to 25 percent.

Access to capital markets

Posten is free to borrow in commercial markets. Despite 100 percent public ownership, Sweden Post no longer enjoys a government guarantee and can raise money on a fully commercial basis.

I. Best Practices/Lessons Learned

Posten AB is one of two postal administrations in the European Union (the other being Finland Post)

that has absolutely no statutory monopoly. As such, it is watched with interest by other postal administrations facing deregulation. Although it is too early to assess the extent of competition in the letter market, there are lessons to be learned from this case. Sweden Post has faced competition in its letter market from CityMail, a private delivery firm that operates primarily in Stockholm and handles only presorted, low cost pieces. In spite of lower prices, CityMail has not yet earned significant market share. Even with competition in its core market, Posten AB believes that full deregulation has not damaged its ability to compete.

The threat of competition has certainly created an incentive for Sweden Post to diversify into new markets. Posten AB is a leading producer of hybrid and fully electronic services, with 10 percent of its transactions mail originating in electronic form. Posten AB offers electronic mail services, ePost, enhanced fax services, and electronic stock market data. It participates in joint ventures and owns subsidiaries.

Posten AB believes that deregulation is not possible without corporatization. Without the managerial flexibility to compete, the company would not be able to survive entry from new competitors.



United Kingdom



A. Corporate Profile

The Post Office is a statutory corporation serving 58 million people in the United Kingdom. The Post Office collects and processes 17 billion pieces of mail annually for delivery to almost 25 million addresses in England, Scotland, Wales, and Northern Ireland. The Post Office has 19,000 retail outlets, over 100 major mail processing centers, and employs 183,000 full time equivalents.

For the year ended March 31, 1994 the Post Office's revenues were £4.8 billion (\$7.7 billion U.S.)⁹ and operating profits were £280 million (\$44.7 million U.S.). The Post Office's financial statements are prepared in accordance with U.K. and international generally accepted accounting principles.

The standard letter mail postage for domestic delivery, weighing up to 60 grams (2.1 ounces), is 27 pence (43¢ U.S.). The rate is uniform throughout the United Kingdom. Significant discounts from the standard rate are available to bulk mailers who prepare letter mail to facilitate processing by the Post Office.

The Post Office is structured into three operating divisions: Royal Mail (letters), Parcelforce (parcels), and Counters (post office retail outlets). Counters is a subsidiary of the Post Office.

B. Ownership, Structure, and Organization

Corporatization

The Post Office is the world's first postal administration (established 1657). Originally, the Post Office was a department of the government and included the telecom operator; the latter was privatized in 1986. Banking services provided through the retail outlets were also separated from the Post Office and privatized in 1990.

In 1992, the government announced that it was reviewing the potential to privatize the Post Office and Parcelforce in two separate sales.

The original plan proposed by the Department of Trade and Industry (DTI) was to sell 40 percent of the Post Office (minus Counters, which would remain government-owned) in an initial public offering. This plan faced considerable opposition, particularly from "backbenchers" in Parliament who feared a reduction in rural service. The unions also opposed the privatization plan. As opposition mounted, DTI proposed an alternate plan that would have included a sale of shares to employees. Eventually, opposition to DTI's proposal grew too strong and it was withdrawn.

Financial mandate

The Post Office therefore remains a government-owned statutory corporation. Principle features of a statutory corporation are

- it prepares and publishes financial statements to the same standard as major listed companies;
- it pays taxes like a normal commercial company;
- the Chairman and Board members are appointed by the government, but responsibility for running the Post Office rests with the Board in its corporate capacity; and
- the government can and does require withdrawal of cash from the business and expenditure by the Post Office is counted within the Public Sector Borrowing Requirement.

C. Social Responsibility

Social obligation defined

In return for the monopoly, two social obligations are currently required by the Post Office. These are confirmed in government policy documents (Citizens Charter) rather than as statutory law.

⁹ Based on January 25, 1995 exchange rate of \$1.5962 (U.S.).



The two obligations are:

- uniform postal rates across the country; and
- nationwide collection and delivery of mail (six days a week)

In addition, when announcing plans to privatize Parcelforce (now abandoned) the government made it clear that it regards universal service in the carriage of parcels as an obligation. In practice, therefore, the Post Office offers universal service up to a weight limit which is practical for collection — around 30-40 kilogram (66-88 pounds) in larger collection centers.

Other obligations

There are other self-imposed obligations which would be difficult for the Post Office to withdraw such as two deliveries each working day and a requirement to publish delivery standards. In 1993-94 the target for delivery of first class letters next day was 91 percent (achieved 91.2 percent). The delivery standards for first and second class mail are independently audited and published with the annual accounts. (In the U.K. second class mail is not publications mail but deferred letter mail).

While there is no formal requirement to maintain retail counters (community post offices) there would be political opposition to significant reductions in the network. There is substantial cross-subsidization, mostly from the urban post offices and mail collection recharges to rural post offices.

Retail outlets

With the exception of 800 larger urban branches which are fully owned, retail branches are franchised out — typically to small grocery storekeepers who operate the Post Office Counter as only one part of their retail businesses.

Approximately 75 percent of retail revenues at franchise post offices comes from non-mail services, for example fees from handling government checks.

D. Scope of Monopoly

Extent of monopoly

Under national law, the Post Office has an exclusive "privilege" over the carriage of letters, although the government could license others to carry letters and could suspend or limit the Post Office's privilege. The monopoly is value limited rather than weight limited (i.e., up to £1 or \$1.60 U.S.). Letters and parcels with a value in excess of £1 (\$1.60 U.S.) are outside the monopoly but within the universal service obligation.

Direct mail

Addressed direct mail is within the monopoly. Private companies are permitted to do a general door to door delivery of unaddressed mail — although generally this is accomplished by enclosing advertisement leaflets within local free newspapers delivered by schoolchildren.

There are no proposals to reduce the monopoly limit, although this would have been considered as part of privatization. Indeed, the management of the Post Office had volunteered during the privatization debate that the monopoly limit could be reduced to 50 pence (80¢ U.S.) as part of a trade-off to maintain the network and a basic letter monopoly intact.

Mailbox exclusivity

There is no mailbox exclusivity.

E. Competition

Presence of competition

As noted above, there is effectively no competition at price levels below £1 (\$1.60 U.S.). Above this limit there are highly competitive markets in the following:

- International courier mail. The Post Office's products struggle to compete against heavily advertised offerings from the likes of DHL. The Post Office's market share is minimal.



- Domestic packets and parcels. Parcelforce operates in a price competitive market in which most operators suffer losses. While it has a one-third share of the "later than next day market", its share of express domestic parcels is considerably less than this.
- Domestic couriers (typically business letters and packets). This is a highly competitive and fragmented market with national and international players and many hundreds of local bike courier firms. The Post Office's share of this market is minimal.
- a requirement to approve the Corporate Plan including the cash withdrawal target for the year;
- a requirement to approve major capital expenditure items;
- restrictions on contracting freedoms. As a broad generalization, the Post Office must submit purchasing and service related contracts above a certain value (about \$100,000 U.S.) to competitive tender; and
- restrictions on the range of activities imposed by government. The Post Office is basically restricted to postal-related activities

The Post Office has suffered from the remail activities of the Dutch Post, which has established itself in the U.K. and attracted large corporate customers. The Post Office is not presently permitted to respond by opening for business in other countries. Recently proposed increases in terminal dues may gradually erode the threat of remail.

Presort Discounts

There is no right of downstream access for other mailers to Royal Mail or Parcelforce. But discounts are available to high volume mailers who presort or who can send their product to specialized presort distribution centers.

F. Regulation/Managerial Freedom

Pricing and regulatory oversight

The Post Office is regulated by its ownership government department, the Department of Trade and Industry. There has been discussion of separating the ownership and regulatory functions and creating a semi-independent postal regulator, but there are no formal proposals.

In practice, day-to-day operations are left to the Board. The principle interventions by government come through:

- a requirement to seek government approval for tariff increases;
- a structured agreement on cash withdrawn into government funds to peg withdrawals to profits, rather than a discretionary take (which is unpredictable);
- relaxation on control over the range of activities particularly to permit joint ventures with the private sector and an ability to market remail services overseas;
- relaxation of capital investment limits; and
- a more structured approach to tariff setting with perhaps a price index formula

There is no set approach to agreement on tariffs and there have been occasions when increases above the rate of inflation have been allowed to finance a greater cash withdrawal by government from the business. Government, in most cases, seeks to restrict tariff increases to below the rate of inflation and the Post Office has had to rely on volume increases to finance new investment.

G. Employment

Wage settlement

The Post Office is one of the largest employers in the U.K. and is heavily unionized. Unions in general had their powers curbed by the Thatcher government in the 1980s and there has been little militancy or strike loss in the last 15 years.

There is a government sponsored independent review body to which both sides can refer disputes for binding arbitration. Both sides, however, must agree to refer. The government can also announce an independent inquiry into sector pay levels. Its findings would be strongly advisory but not binding.

The union's success in fighting off recent privatization efforts appears to have increased its confidence. It is notable that strikes in the postal sector have shut down some postal areas in the last three months.

Wage premiums

Postal workers are generally poorly paid relative to the industry, having suffered from government inspired sub-inflation wage increase pressures. Much of the postal private sector is however also generally low skilled/low paid. On the other hand, Post Office pensions are relatively high by private sector standards.

H. Financial

Pensions

Pensions are fully funded in a separate and independent pension fund. There is no provision for future medical liabilities but postal retirement medical benefits are not provided and private health care is limited to the most senior executives.

The balance sheet

The Post Office has a strong balance sheet. Having been profitable for several years, the organization has no debt and significant cash and deposit balances. The Post Office pays all income and real estate taxes that an equivalent commercial organization would bear. Postal services are,

however, exempted from VAT by virtue of European Community Law.

Dividends

The government takes cash out of the Post Office by a mechanism called the "external finance limit". Essentially, the Post Office is required to deposit surplus funds or repay borrowings to the Treasury. There is no share capital and no mechanism for a dividend to be paid without a change in the law.

Access to capital

Freedom to raise capital and control investments is strictly limited. Basically, little can be done without Treasury (the Finance Ministry) approval.

The Post Office is not able to raise debt capital (there is no equity capital) without the approval of government. The government has encouraged state owned corporations to identify private sector partners who would take on project risks and private risk debt capital for major investment projects. This new policy is known as the Private Finance Initiative. It is not yet clear whether the Post Office will take advantage of these developments for mail services, but, within the retail business, a private finance project for the development of a new information technology network to deliver social benefit payments is under contract negotiation.

Antitrust

There have been no antitrust or other competition authority investigations in modern times. Private sector carriers continually complain about the monopoly power of the Post Office but they appear to be a relatively ineffective lobby.

I. Best Practices/Lessons Learned

The UK has been in the forefront of the trend to privatize state industries and privatization of the Post Office would have been a natural progression. Senior management of The Post Office was keen to transfer to the private sector to get away from what they saw as a greedy Finance ministry and overly restrictive sponsoring ministry.



Privatization failed because the unions ran a good campaign against it, focusing on fears in the population that service levels would be reduced. Government has ridden over similar public concerns in the past when forcing through unpopular privatization but their parliamentary majority, in this instance, was too weak to risk a political defeat which would have prompted an election.

It is not clear what happens next. The Post Office desperately wants greater commercial freedoms, and needs to quickly catch up in technology use (e.g., electronic mail is well behind postal administrations in Sweden and Italy). The Minister responsible for the Post Office does not believe in public organizations competing with the private sector and the Finance minister probably will not allow greater financial freedom. In short, there appears to be an impasse within the government.

Argentina



A. Corporate Profile

Correo Argentino (CA), also known as ENCOTESA, has been a government-owned corporation since 1993. The government has announced plans to privatize CA, through a 100 percent sell-off, later this year. CA serves 33 million Argentines in competition with over 270 private postal operators.

In 1993 CA delivered 312 million letters (standard and registered), out of a total basic mail market of 433 million items. It also delivered 170 million other pieces, including express mail and parcels. CA has 5,480 post offices and 20,000 employees. Its annual revenue in 1993-94 was 450 million pesos (\$418.5 million U.S.).¹⁰

The basic stamp price for a "carta simple" is 75¢ (U.S.). A number of possible discounts can be applied which different levels of management can determine. With a large customer, the Board may ask to grant the maximum discount of 40 percent.

B. Ownership, Structure, and Organization

Corporatization

The legislation to privatize CA will appear before Parliament when it reopens in March 1995. The original schedule was for the sell-off to take place in June, but CA believes that it may not now occur until the end of the year, although the Ministry of Economy is pushing for the sale as soon as possible.

The main debate regarding privatization surrounds the provisions to prevent the formation of a private monopoly. There is a real danger in Argentina's liberalized market because, while there are four private postal operators of significant size, they are actually owned by one individual.

Financial mandate

The current financial objective in the run-up to privatization is to reverse large historical losses and to make a profit. The deficit was halved in the current year, and CA is projected to be profitable in 1995.

Management structure and board oversight

Currently, a Board of five members operates CA. Eight regional managers report directly to the Board. There are several central departments covering national areas such as Operations, Marketing, and Technology. These are organized as Strategic Business Units (SBUs). In addition, there is an SBU for "corporate customers."

Assuming the provisions to prevent a controlling shareholder emerging are successful, it is expected that this basic structure will survive the sell-off. However, the Board of Directors would then have the power to decide upon any new structure.

Range of business

CA offers traditional mail delivery services plus services such as tax and money transfers.

C. Social responsibility

CA must provide a universal letter mail service at a uniform price. It also must deliver the government's mail. In addition, it must supervise the distribution of ballot boxes during elections. In return for these social obligations, the government currently covers CA's losses. Financial losses will not be covered after privatization.

Retail outlets

No limit is put on the number of postal outlets that CA must maintain. Its policy in recent years has been to reduce the network it runs directly using franchising and agencies (e.g., making postal services available through local libraries).

¹⁰ Based on February 15, 1995 exchange rate of \$0.9300 (U.S.).



D. Scope of Monopoly

Extent of the monopoly

CA has no monopoly in delivery services. The Argentinean mail market was completely deregulated in 1979 by a system of licensing. In order to become a licensed deliverer of letters, a firm must buy a license from the National Commission of Postal and Telegraph Services, the regulator of CA and the postal industry, for 5,000 pesos (\$4,650 U.S.).

Mailbox exclusivity

There is no mailbox exclusivity.

E. Competition

Presence of competition

There are over 270 licensed postal operators, though only four of any size: OCA, Andreani, Autobuses, and OCASA. These four main private operators tend to concentrate on higher-value letters, that is, where proof of delivery is given to the sender. While they could legally undercut the high stamp price of CA, they appear to have made no serious attempt to do so.

Mailing practices and traditions in Argentina may partly explain the demand for registered letters: people prefer to have acknowledgment that their letter was actually delivered. This practice may relate to problems of reliability and integrity in the past.

F. Regulation/Managerial Freedom

Pricing and regulatory oversight

CA has the freedom to set its own prices in a totally competitive market. After privatization, it is assumed that all the freedoms of a normal commercial company will apply.

G. Employment

No detailed, reliable information was received. CA has recently reduced staff numbers from 27,000 to 20,000.

H. Financial

CA has never operated its own pension plan, and employees have relied on the government-run plan.

The government has funded CA's losses in the past.

I. Best Practices/Lessons Learned

Argentina's postal privatization will be the first 100 percent postal sell-off in the world. Unique conditions such as low mail volumes, the high stamp price, national mailing practices, highly deregulated markets, and the presence of a potential monopolist make Argentina a particularly unusual case, and it is not clear whether its experience is directly relevant to postal administrations such as the USPS.



Denmark

**A. Corporate Profile**

Denmark is a relatively small country (population of five million) but recent developments in the Danish Post provide an interesting perspective on commercialization within the public sector.

Danish Post forms the remaining public sector part of Danish PTT. Telecommunications companies and postal bank services have already been privatized.

The basic stamp price is Dkr 3.50 (59¢ U.S.)¹¹ for first class mail.

B. The Move to Commercialize

Danish Post has faced the same restrictions which have frustrated many of the world's postal administrations.

- approvals are needed for new services and investments in new ventures, often requiring Parliamentary authority;
- investments are severely restricted by government with no access to external finance;
- constrictive employment rules and civil service collective bargaining;
- setting of tariffs requires Parliamentary approval;
- cumbersome decision making processes; and
- surplus funds are taken away by government.

As a separate issue, the distinction between the postal service provider and regulator has not been clear. Resolutions passed by the European Commission have made non-separation increasingly untenable.

After years of debate, there has been no clear political mandate in Denmark to corporatize, much less privatize. It has, however, been recognized that the postal service needs greater freedom in order to survive in an increasingly competitive communications market. Accordingly, in October 1994, a political agreement was reached to create a hybrid entity within the public sector that shares many of the freedoms enjoyed by private sector companies.

Distinguishing features of the new Post Danmark are:

- an independent publicly owned entity, not included within the national budget;
- Board appointments by the Minister of Transport but with some employee appointed representatives;
- crucial aspects of the delivery of postal services, including profitability, quality of service and basis for tariffs are set in a new concession;
- substantial freedom to act in a commercial manner including the introduction of new services (in practice Post Danmark would inform/consult the government on all major decisions);
- a move towards a predefined price cap model for tariff setting;
- direct mail, if the content is not personalized, can be delivered outside the monopoly;
- preparation of financial statements along fully commercial lines;
- the government Minister approves the financial statements and receives the five year plan, but budgets and business plans are the Board's responsibility;

¹¹ Based on January 25, 1995 exchange rate of \$0.1679 (U.S.).



- Post Danmark moves to an income taxpaying basis;
- no change in civil service employment terms;
- dividends are predetermined as a formula of profit after tax or on a return on investment approach, rather than at government discretion;
- capital can be raised outside of government; and
- investment and alliances up to DKK 100 million (\$16.8 million U.S.) are allowed without government approval.

Retail outlets

Five years ago all retail branches were owned by Post Danmark. Following a process of commercialization which is ongoing, approximately half are now typically franchised out to grocery store owners. Financial viability of the retail network is difficult to determine, because it relies on cost allocations between the postal and retail business and there are no separate accounts for the retail business. In general terms, urban retail outlets are thought to be profitable and rural outlets unprofitable.

Antitrust

There has been a recent antitrust complaint to competition authorities. Post Danmark set up an operation which collects electronic mail for assembly and delivery. Private sector operators have complained to the Competition Council that this service is being cross-subsidized by monopoly products. A decision on the complaint is pending.

Labor relations

A total of 70 percent of postal employees are civil servants, for whom strike action is illegal. Nonetheless, the remaining 30 percent may strike and they are, therefore, used as a negotiating tool. There is a separate independent arbitration body for dispute settlement and it is generally accepted within Denmark that unresolved disputes should go to arbitration. The findings of the arbitration body are not mandatory but must be put to a vote

among members of the employers councils (industry sector wide rather than postal specific) and employees (postal and general transport workers unions). The recommendation of the arbitration body can only be turned down if more than 50 percent of all members on both sides vote against the result. In practice this makes it difficult (through no-shows) to resist the final recommendation.

C. Commentary

It is too early to judge how these new freedoms will work out in practice but Denmark offers an interesting alternative to privatization in a political environment where the final step to private sector ownership is unacceptable.

The dividend formula, access to private capital, and investment alliances are particularly interesting and are not common features of state enterprises.



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Price Waterhouse LLP



March 13, 1996

The Honorable John M. McHugh
Chairman, Subcommittee on the Postal Service
Committee on Government Reform and Oversight
United States House of Representatives
Washington, D.C. 20515

Dear Chairman McHugh:

Enclosed are answers to the 13 questions regarding postal reform you asked of us in your letter of February 7.

Please let me know if any areas need clarification or elaboration.

Sincerely,

James A. Waddell
Partner

Enclosure

1. Of the ten progressive postal administrations that you have studied, which model would most suit the needs of the U.S.A.? Does Price Waterhouse have a comprehensive reform proposal?

Price Waterhouse LLP does not have a comprehensive reform proposal. However, what can be viewed as "best practices" on the parts of the progressive postal administrations that we studied suggest possible avenues for reform for the U.S. Postal Service.

The ten postal administrations have not progressed in different directions with respect to reform; rather, generally speaking, they tend to be at different points along the same path. In considering the continuum along which postal administrations fall, those administrations that offer the best models to the United States are those countries which are furthest along in various areas. Most notable in offering suggestions would be Germany, the Netherlands, New Zealand, Sweden, and the United Kingdom. These organizations are instructive in the areas of deregulation of monopoly, pricing, insurance of universal service, and ownership.

Deregulation of the monopoly. Sweden has proceeded the furthest by completely abolishing the monopoly. While eliminating the monopoly is probably not a good idea for the United States in the short term, the theme of reducing the scope of the monopoly has tended to pressure postal administrations to perform better, as in the case of the United Kingdom, where the Department of Trade and Industry limited the monopoly only to items valued at one pound sterling or greater. An appropriate model for the United States might be that of the European Union (EU) overall, which has proposed that, beginning January 1, 2001, the monopoly will be limited to letters weighing 350 grams (12.5 ounces) or less. After January 1, 2001, direct mail and incoming cross-border mail will be eliminated from the monopoly.

Pricing. New Zealand and others present an interesting model for pricing, one based on price caps. Price caps achieve two benefits: they protect mailers from abuse of the monopoly through overly high price increases and allow the postal operator maximum flexibility in adjusting prices to best meet market needs.

Universal service. Sweden, the Netherlands, and others provide a possible model. In these countries, the government grants a concession to a postal operator, giving a monopoly over letters in return for providing universal service at a uniform letter rate. Sweden Post and PTT Post BV of the Netherlands currently have the monopoly concession in their respective countries; this concession comes up for review periodically. Conceivably, it could be granted to another party if the government were to become unhappy with the level of adherence to the agreement. The important element, however, is that the postal operator receives the monopoly in return for providing universal service at a uniform letter rate. The arrangements are crafted on the basis of balance; the monopoly is a clearly a benefit granted to the operator but in return must adhere to a "contract" with the government to provide specific services. The costs and benefits of the arrangements need to be carefully balanced so that the contract between the postal operator and the government is a fair one.

Ownership. Germany and the Netherlands are highly progressive in the area of ownership, the Netherlands government having sold a majority of shares in the postal administration's holding company and Germany planning privatization for 1998. The United Kingdom planned to privatize Royal Mail and Parcelforce, but the sale was halted at the last minute due to incomplete political support. While wholesale privatization of the U.S. Postal Service may be too aggressive a change in the short term, a clear move in that direction through means such as partial privatization of the competitive services (through a subsidiary owned partially by the USPS and partially by the private sector) and corporatization of the monopoly services (corporation with stock owned by the United States government) could be beneficial in focusing management on minimizing costs and maximizing service to customers.

2. Would you comment on whether the financial mandates of "break-even" and "profit" have an effect on the various postal administrations which are operated under one of those guidelines? Is one more efficient or productive than the other?

Of the eight major postal administrations reviewed, a "profit" mandate tends to go hand-in-hand with corporatization. That is, if the postal operator is a "corporation" then its objective is to earn profits. Those administrations with a profit mandate are: Australia, Germany, the Netherlands, New Zealand, and Sweden. With the exception of Germany, which only corporatized recently, all these operators are financially healthy. The remaining three administrations, those of Canada, France, and the United Kingdom, do not have profit mandates. These, arguably, have been less successful financially.

We have not explicitly studied the correlation between mandate and "efficiency" or "productivity"; this task would be fairly time-consuming and should consider not only financial results but also service performance and other measures of quality to customers. With the exception of Germany, which only recently corporatized, those administrations with a profit incentive tend to be regarded as the most successful both financially and with respect to providing innovative, value-added services to customers.

3. The ten administrations studied by Price Waterhouse do not have a mail box monopoly. They appear to be unaffected by this. Would this open mailbox monopoly work in our country? How would you suggest that this be addressed? (For instance, a sticker on the box indicating open or restricted mailbox, restricting access to locked mailboxes, a poll of customers, etc.)

The ten administrations we studied may appear to be "unaffected" by not having a mailbox monopoly largely because, in most cases, the majority of their revenues are drawn from products that are protected by product monopolies rather than mailbox monopolies.

To evaluate how an open mailbox monopoly would work in the United States, each of six general types of mailbox must be considered. Of these six, the only type of mailbox which would be significantly affected by a rule change is the last, unlocked mailboxes at curbside or attached to a house or business.

Business with employee or mailroom designated to receive mail. Competitors always have had access to businesses with a receptionist or mailroom available to receive mail. Suspending the mailbox monopoly would have no effect on such businesses without mailboxes.

Post Office box. Competitors do not have access to Post Office boxes in the United States or in other countries, so adopting the no-mailbox monopoly rules found in other countries would have no effect in the United States.

Mail slot on door. Competitors in the United States already have access to mail slots, which are not considered subject to the mailbox monopoly, so a rule change again would have no effect.

Locked mailbox with a slot for access. While common in parts of Europe, these do not exist in significant numbers in the United States.

Locked mailbox without a mail slot. This type of mailbox is not common outside the United States. In areas where it does exist, such as Canada, competitors generally are not given keys by the owners of the mailboxes (the apartment buildings) on the grounds of security. If the United States were to suspend the mailbox monopoly, the same result as in Canada is likely to follow, with apartment buildings being reluctant to issue keys to organizations other than the U.S. Postal Service, resulting in little competitor access to these mailboxes. Thus, a rule change likely would have little effect.

Unlocked mailbox at curbside or attached to structure (house or business). This is the only type of mailbox in which suspension of the mailbox monopoly policy would have much bearing for the U.S. Postal Service. These probably account for less than one fourth of delivery points in the United States. There could be a variety of ways to address this issue, including allowing individual customers to handle mailbox access as they see fit. Many postal customers, as daily newspaper customers, already have demonstrated an interest in permitting alternate delivery companies access to their dwellings by constructing a second, and sometimes a third, mailbox alongside their monopoly-restricted postal mailboxes. These types of customers are probably capable of proactively deciding for themselves how they would wish to treat their postal mailboxes in an environment without a mailbox monopoly.

In summary, suspension of the mailbox monopoly in the United States likely would have little effect except for those customers with unlocked mailboxes at curbside or attached to structures, a minority of delivery points. Because these customers own their own mailboxes, and in many cases have permitted access by alternate delivery companies, they may be in a good position to determine how to react to a suspension of the mailbox monopoly.

4. Generally, the progressive administrations have been able to implement labor/management reforms. What was the common denominator? How much employee input was considered?

The precise ingredients of successful management/labor reform in any given country vary depending on the specific history of labor relations. One shared ingredient among postal administrations that have successfully implemented reform is the government's willingness to clearly define the postal authority's long-term mission. Postal operators require the impetus of an unambiguous commercial mandate from their governments in order to motivate meaningful reform in labor/management relations. In New Zealand and Australia, the governments' explicit legislative agendas recast both postal administrations as commercialized entities that should compete much like private sector firms. With the commercial framework clearly defined, management in both nations took bold steps to improve management/labor interaction. New Zealand Post embarked on an aggressive restructuring plan and encouraged managers to mirror the entrepreneurial outlook of private sector counterparts. Australia Post enacted progressive self-assessment procedures for employees and pursued management/labor partnership.

The United Kingdom's experience provides a sobering example of how legislative ambiguity can erode worker morale and cloud management's entrepreneurial outlook. Beginning in 1992, Post Office management began preparing Royal Mail and Parcelforce for privatization. The government reversed its decision to privatize in November 1994, as a result of political discord within the ruling conservative party. Since John Major's January 1996 announcement that he would pursue privatization if re-elected, the uncertainty surrounding the Post Office's future mandate and organization has increased still further. This uncertainty has deprived management of the incentives and foresight needed to enact visionary labor/management reform. The abrupt shift of policy also may have contributed to weakened worker morale, explaining at least in part the 1995 labor strikes that occurred in Scotland.

5. Of the postal administrations you surveyed, which were products of reform efforts initiated due to political or social crisis situations? Ideally, reform of public institutions such as the Post should occur outside of crisis situations - do you agree?

With the possible exception of Argentina, postal reform in surveyed countries has not resulted from crisis situations, whether political, social, or otherwise. While "crisis" *per se* has not been the cause of postal reform, there have existed distinct catalysts. In most countries surveyed, reform proposals have resulted from the government's commitment to greater efficiency in the general economy. In the case of European nations, the need for European Member States to comply with the EC Treaty has also contributed to progress in reform efforts.

In Australia and New Zealand, the governments made legislative commitments to remove the structural and institutional factors that inhibited efficient performance in key industries, including aviation, telecommunications, and financial services. Reform in the postal sector coincided with these economy-wide deregulatory efforts.

In Europe, adherence to Article 86 of the EC Treaty is driving many reform proposals. Article 86 of the EC Treaty prohibits economic activity within the common market by, "one or more undertakings that involves an abuse of a dominant position..." While the European Commission has attempted to establish guidelines that would apply Article 86 to the postal sector, the process has been stymied by special interests—particularly labor, who view efforts to deregulate the postal sector as threatening job security. As Europe migrates towards greater integration, enforcement of the EC Treaty implies that Member States will eventually erode monopoly protection, tax exemption, and other non-competitive practices.

In Argentina, the government's determination to avoid economic crisis is motivating reform. The Argentine government has committed itself to an austere fiscal package that requires revenue from the sale of state owned industries, including the state postal operator. Postal privatization is one component of the government's overarching movement towards lower government involvement in the nation's economy.

As a backdrop to these reform efforts, many postal administrations are increasingly aware of the competitive threat posed by electronic media. Most postal executives view deregulatory initiatives as needed to afford postal operators the flexibility to compete in the modern communications sector.

Reform of public institutions, especially an institution of the Postal Service's magnitude, should occur outside of crisis situations. Crisis situations rarely afford policy makers the opportunity to thoughtfully craft long-term solutions to complex problems. Instead, crisis mentalities encourage band-aid solutions that may overlook fundamental issues.

6. Last November, the Subcommittee on Postal Service initiated its reform hearings by receiving testimony by proponents of legislation which would transform the Postal Service into a fully private entity wholly owned by its employees. Are you aware of any postal administration which operates with this type of ownership model?

We are not aware of any postal administration that operates with this type of model. Canada Post Corporation (CPC) does have an employee share ownership plan which was authorized by the Canada Post Corporation Act but has not yet been implemented. This plan permits CPC to sell up to ten percent of shares to employees. In its February 15, 1996 submission for the mandate review, CPC expressed its interest in exercising the employee share ownership option.

Examples of privatization by transferring ownership in industrialized enterprises to employees has occurred mostly in Eastern Europe and the former Soviet Union, rather than in the West. This model tends to be used in situations where the objective is to quickly return equity held (and often originally seized) by the state to private individuals in such a way that widely distributes shares to the citizenry to help build an economic foundation of capitalism that generates popular support for a Western-style, democratic government. To the best of our knowledge, even in these countries, postal administrations have not been privatized by giving the equity to employees or others.

7. Labor costs account for approximately 83 percent of the operating costs for the U.S. Postal Service. How do these costs compare in relation to other posts? Could you describe the efforts made by the foreign posts you surveyed in addressing labor costs?

Price Waterhouse conducted a survey of postal labor costs as a share of total operating expenses in the eight major countries we studied. The results of this survey, conducted in December 1995, are attached.

The attached figures indicate that all postal operators studied have significantly lower labor expenses than the U.S. Postal Service. Many postal administrations have taken steps to lower the share of expenses attributable to labor, either by decreasing wage premiums or eliminating positions. Canada has pursued gradual reduction of the wage premium since 1981 through difficult labor negotiations and has also reduced staff by 10,000 over the last seven years. Other operators also have focused on streamlining employment, including Australia Post, which reduced staff by 6,000 over the last six years; New Zealand Post, which has cut 5,000 positions over the last nine years; the Dutch postal service, which has lowered employment by 4,000 over the last three years and recently announced another 9,000 in upcoming cuts; Argentina's postal operator, which decreased employment by 7,000 since 1993; and Sweden Post, which lowered employment by 6,000 between 1991 and 1993.

Table 1
Comparison of Labor Expenditures
for International Postal Administrations

(as a share of total operating expenses)

	Unadjusted		Adjusted ¹	
	Labor	Non-labor	Labor	Non-labor
Australia	59%	41%	63%	37%
Canada ²	(figures not available)		(figures not available)	
France ³	76%	24%	76%	24%
Germany ³	77%	23%	77%	23%
The Netherlands ⁴	56%	44%	56%	44%
New Zealand ⁵	52%	48%	(figures not available)	
Sweden	45%	55%	46%	54%
United Kingdom	63%	37%	70%	30%

Notes:

December 12, 1995

Comparison of Labor Expenditures for International Postal Administrations

Methodology

Unadjusted percent labor figures are calculated, for each postal administration, by dividing labor and associated costs by total operating costs. The unadjusted non-labor figures equal one minus this result.

Many postal administrations contract out substantial portions of their retail networks. In these cases, the unadjusted labor figures understate true labor costs because wages and benefits paid to employees of the outsourced retail operations are considered non-labor, rather than labor, costs from the standpoint of the postal administration. To improve the consistency of figures across organizations, the unadjusted figures are modified to reflect actual labor expenditures.

Postal administrations that outsource retail operations normally procure these services by paying an explicit franchise fee. To calculate true labor costs, this amount is divided between labor and non-labor based on the estimated comparable figure for the United States. The outsourced retail labor amount is added to postal administration labor and subtracted from postal administration non-labor; the adjusted percent labor figures are calculated using these revised figures.

Calculations are based on the most recent financial results reported by each postal administration, usually for fiscal year 1994 or 1995. In most instances, clarifications and additional information were obtained from sources at the postal administrations.

It is important to note that these postal administrations have been selected due to their characterization as "progressive" in terms of competition, commercialization, and/or deregulation. They should not be considered a representative sample of any kind.

8. The Clinton Administration recently included in its most recent budget proposal a deficit reduction provision requiring the U.S. Postal Service to prefund its retiree health benefits. Since the Postal Service is an off-budget entity, this requires the Postal Service to transfer approximately \$9.85 billion to the U.S. Treasury. Have other foreign posts been used as similar agents of deficit reduction?

Use of postal revenue as a deficit reduction source has also occurred in countries where the postal administration generates revenue in excess of costs. The most striking example of this practice occurs regularly in the United Kingdom, where the Post Office pays the government a 33 percent income tax on all profits in addition to an after-tax levy of profits. The magnitude of the after-tax levy varies, depending upon negotiations between the government and Post Office management. In fiscal year 1995, the income tax amounted to £158 million (\$240 million) and the profit levy amounted to another £226 million (\$344 million), or 71 percent of after-tax profit. Post Office executives have been highly critical of these *ad hoc* levies on the grounds that they deprive the Post Office of needed revenue for capital investments and inflate postage rates. In November 1995, the Chancellor of the Exchequer's budget called for the Post Office to pay an additional £1 billion (\$1.52 billion) over the next three years, prompting Post Office executives to predict future rate increases.

9. How much competition do the "reform posts" actually face in light of the fact that Sweden and Canada, for example, have acquired ownership of their competition?

The amount of competition faced by "reform posts" must be gauged in each specific product market. Most face substantial competition in the expedited mail and ground parcel markets. Many, such as the Netherlands, face substantial competition in the area of magazines. In the case of direct mail, most countries have not lifted the monopoly yet.

Sweden is the only country studied (except Argentina, where competition for letters is intense) that has abolished the monopoly on letters. In the Swedish case, the competitor, CityMail, entered the market by offering prices substantially below those of Sweden Post in a single market, Stockholm. Sweden Post responded by matching CityMail's prices in those markets. CityMail argued that Sweden Post's prices were predatory and below cost, subsidizing Stockholm mail prices with higher-priced volume from the rest of the country. Due in large part to a price war, CityMail experienced severe losses and was acquired by Sweden Post for reasons that Sweden Post has not made fully clear.

Some have suggested that CityMail's bankruptcy resulted from unsophisticated antitrust procedures on the part of the government that failed to result in a speedy, favorable ruling for CityMail. This argument would suggest that, if CityMail was correct in alleging that Sweden Post was engaged in predatory pricing, a comparable competitor in the United States would not be at risk to similar anticompetitive behavior, provided the U.S. Postal Service were subject to traditional antitrust laws.

In mail, a major difference between the American and European markets is density. The U.S. Postal Service delivers the most mail per capita of any country in the world, and double that of many European postal operators. For example, the U.S. Postal Service's 670 annual items per inhabitant compares with 299 in the United Kingdom and 230 in Germany.¹ The higher density increases the probability of healthy competition in a deregulated market.

Another difference between the United States mail industry and those of other countries studied is the degree to which downstream access discounts have been made available by the U.S. Postal Service and the degree to which customers have taken advantage of those discounts by contracting to private presort bureaus and transportation companies. These companies, which generally do not exist in similar size and number outside of the United States, have developed strong expertise and have the potential to act as formidable competitors to the U.S. Postal Service should the monopoly be reduced.

¹ Source: Statistique des Services Postaux, Universal Postal Union, 1994.

10. What has been the actual experiences of those posts which allow their employees the right to strike? If such a right is exercised, can the post hire replacement workers?

The actual experience of postal services allowing workers the right to strike varies. In countries such as Australia, the Netherlands, New Zealand, and Sweden, postal administrations have operated with little significant labor unrest despite the fact that workers have the right to strike. In other countries, labor relations have been far more contentious. Canada Post faced labor stoppages in the past decade while trying to negotiate lower wage premiums. Over the past year, the United Kingdom's Post Office confronted labor unrest in Scotland. In France, workers went on strike for extended periods to protest government welfare reform and automation programs threatening job security. In early 1996, management at the French postal service announced that postage rates would increase in the near future as a consequence of financial losses induced by labor stoppages.

While strike periods have proven difficult for postal customers in the affected countries, they can be argued to have served as necessary means for the postal administration and the union to adjust to changing market conditions. The alternative, no strike with labor agreements enforced by the government itself or, as in the case of the U.S. Postal Service, by an independent, binding arbitrator, can provide greater stability for postal customers in the short-term but can also have the effect of enforcing a status quo in labor agreements that fail to adjust to an evolving marketplace. If such a status quo eventually becomes outmoded, the resulting imbalances could ultimately prove harmful to labor, management, and customers.

In considering the ability of management to hire replacement workers, a distinction must be made between permanent and temporary replacement workers. While postal administrations in most countries do not have the authority to permanently replace striking workers (including Australia, the Netherlands, France, Germany, and the United Kingdom) in some countries, such as Germany, the postal administration operates with a provision for temporary replacement of workers during labor stoppages. Such a provision strengthens the ability of management to withstand a strike.

11. The U.S. ratemaking system with an independent Postal Rate Commission appears to be unique. Our PRC is charged with both rate and classification responsibilities. How do foreign posts address the issues of different classes of mail? Do foreign posts engage in reclassification efforts?

Most foreign posts are subject to some sort of regulatory or oversight agency; however, the degree to which these operators are regulated is far less than the U.S. Postal Service is by the U.S. Postal Rate Commission. In general, if a postal administration wishes to introduce a new product or change a price for an existing product, the organization discusses the proposals informally with the ministry that regulates it. The ministry may suggest modifications to the product or price changes based on the informal discussions. When both parties (the operator and the regulator) have reached an agreement, the operator implements the changes.

This situation can be seen in two major countries in Europe, the United Kingdom and Germany. The Post Office in the United Kingdom is responsible to the Department of Trade and Industry (DTI). If one of The Post Office's business units wishes to restructure or reprice a product, it submits a proposal to DTI. The Post Office and DTI then discuss this proposal informally, without any specified regulatory process; if DTI agrees, then The Post Office is free to implement the proposal following a three month period during which the Post Office Users National Council (POUNC) has an opportunity to comment, but not materially affect, the proposal. For example, in January 1996 Royal Mail proposed a one penny increase in the price of a first class stamp from 25 pence to 26 pence. Assuming that DTI approves this increase, the price change will be put into effect following the three month comment period.

Similar to the United Kingdom, in Germany, Deutsche Post AG is responsible to its own regulatory ministry. The ministry must approve any product or pricing changes Deutsche Post desires; however, there is no formal regulatory process.

Given this situation, foreign posts do not engage in American-style "reclassification efforts." Generally, if a foreign postal administration wishes to introduce new classes of mail that better serve the needs of customers, it simply proceeds with implementation following informal approval by its oversight ministry. However, no long, cumbersome process as exists in the United States can be found in the reviewed postal administrations.

12. In your prepared statement, you discuss reorganizing the Postal Service's competitive businesses into a deregulated, wholly-owned subsidiary. What role do you see for a regulator in this arrangement to ensure no cross-subsidization between competitive and monopoly products? How would institutional costs shared by the Postal Service and this new entity be allocated? Would the Postal Rate Commission be the regulator?

The regulatory problems that would be facing the Postal Service if it were to reorganize its competitive lines of business into separate, deregulated subsidiaries are not unlike those faced by companies in a variety of rate-regulated industries both in the U.S. and overseas. For example, regulators in the United States telecommunications and electric utility industries at both the federal and state levels have had to face these challenges for several years as companies have diversified into competitive lines of business.

Regulators have addressed this problem through a variety of measures. The most progressive regulatory agencies in both the United States and overseas (particularly in the telecommunications sector) have implemented alternative regulatory frameworks that deal with the cross subsidization problem that you address in your question. Frameworks such as "price caps" or "RPI-X" divide the company's services into different "baskets" (often regulated and non-regulated service baskets) and allow the company to change prices in the regulated services baskets as long as the changes do not exceed the rate of price inflation (RPI) in the economy as a whole minus some productivity factor (X). Detailed cost studies are required to set the initial prices for the various baskets (thus protecting against cross subsidization), but once these initial prices are set (and reviewed periodically), price cap regulation provides several benefits:

- incentives for increased efficiency by the regulated company because it is allowed to keep all profits;
- reduced regulatory costs because of reduced administrative requirements by the regulator; and
- increased ability by the regulated company to change prices quickly to address changing market conditions.

In terms of the allocation of institutional costs across regulated and non-regulated lines of business, once initial prices are set, there is much less need to perform detailed cost allocation studies under price cap regulation. As long as initial prices are subsidy-free and the price cap formula is updated periodically to reflect different market and cost conditions, regulated and non-regulated rates should be subsidy-free.²

It is unclear whether the Postal Rate Commission would remain the Postal Service's regulator under various alternative regulatory frameworks. If such frameworks were adopted, however, the requirements of the regulator would be reduced dramatically, as one of the primary benefits of these frameworks is their relative administrative ease and decreased need for extensive studies and hearings.

For these reasons, alternative regulatory frameworks have been embraced by regulators in a variety of industries that have been looking for an efficient, easy-to-administer form of regulation that both discourages anti-competitive behavior and addresses the problems inherent in regulating a diversified company.

Many postal administrations overseas have recognized the advantages of alternative regulatory frameworks in general, and price caps in particular.

² The development of initial prices and periodic updates may require detailed cost studies.

13. One of the responsibilities of our PRC is to insure against cross subsidization of one class of mail by other classes of mail. How do foreign postal administrations insure against monopoly classes subsidizing competitive classes?

In countries without a regulatory body, the government usually charges an executive ministry with oversight responsibility for the postal administration. The ministry hears complaints of cross-subsidy from competitors and investigates cases as necessary to assure fair competition. In the Netherlands, for example, the transport minister overseeing the Dutch postal service is prodding that organization to remove bulk exemptions given mail order companies because competitors have alleged predatory pricing. The process is generally less public and less drawn-out than rate cases in the United States. The judicial system also resolves complaints of cross subsidy, as occurred in the Netherlands when the Dutch postal service protested the findings of the transport minister regarding pricing.

In European countries, the European Commission serves as the ultimate authority on competition and cross subsidy. It investigates private sector complaints alleging unfair competition and rules on competition issues. Interestingly, the European Commission's recently published draft Directive addresses the issue of cross-subsidy between competitive and non-competitive products. The Commission calls for greater transparency of accounting to guard against cross-subsidy and suggests that governments transfer oversight responsibility from ministries to regulatory agents.

The proposal that we suggested in our January 25, 1995 advocates separating the competitive and monopoly businesses of the U.S. Postal Service as a solution to precisely this cross-subsidization problem. One the one hand, management gains the freedom to pursue profitable non-monopoly products that provide high value to customers. On the other hand, the monopoly products are protected against being used to cross-subsidize non-monopoly activities.

GAO

United States
General Accounting Office
Washington, D.C. 20548

General Government Division

April 5, 1996

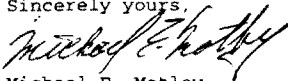
The Honorable John M. McHugh
Chairman, Subcommittee on the
Postal Service
Committee on Government Reform
and Oversight
House of Representatives

Dear Mr. Chairman:

As requested, enclosed are our responses to the ten questions relating to the Subcommittee's hearing of January 25, 1996.

If you have any questions regarding our responses, please call me at (202) 512-8387.

Sincerely yours,



Michael E. Motley
Associate Director, Government Business
Operations Issues

Enclosure

GAO RESPONSES TO QUESTIONS OF FEBRUARY 7, 1996,
FROM THE CHAIRMAN, SUBCOMMITTEE ON THE POSTAL SERVICE,
HOUSE COMMITTEE ON REFORM AND OVERSIGHT, RELATING
TO JANUARY 25, 1996, HEARING

Question

1. GAO reported in its Report to Congress "Labor-Management Problems Persist on the Workroom Floor" that the Kappel Commission found deplorable conditions, "a poor work environment, antiquated personnel policies, limited career opportunities and training, inadequate system for supervision and unproductive labor-management relations." Upon reaching these conclusions and other findings, the Kappel Commission in June 1968 recommended that the Post Office Department be replaced. These findings echo what we are hearing today. Is the time right for a reform/reorganization now?

Response

We believe that it is time for Congress to begin examining those specific provisions of the 1970 Act that may create obstacles to more harmonious labor relations in the Postal Service and consider provisions that may encourage and facilitate efforts of both management and unions to improve employee working conditions. Our belief is based on the conditions we reported to Congress about 18 months ago and the lack of any apparent progress in significantly improving the Service's labor relations since that time. These developments include (1) a significant growth in the number of grievances filed by employees and unions against Postal Service management, (2) the inability of three of the four major unions to reach agreement in the most recent contract negotiations, and (3) the continued dissension and conflict between the two largest unions and Service management over recent initiatives, e.g., **Customer Perfect!** training and employee opinion surveys, to improve organizational and employee performance.

Our September 1994 report dealt primarily with noneconomic issues such as autocratic management styles, poor employee attendance, difficulties in administering employee discipline, and operating inefficiencies that affect customer service. However, Postal Service management and unions often disagree over both economic, e.g., pay and benefits, and noneconomic, e.g., dependent care and grievance arbitration procedures, and sometimes refer all issues to arbitrators for resolution. For example, in their most recent contract negotiations, the Service and the National Association of Letter Carriers could not agree on any of the 80 economic and noneconomic issues at the bargaining table, and all were referred for binding arbitration.

To effectively address both economic and noneconomic issues, Service management and labor unions will need to reorient their relationships from a "we-they" posture in negotiations to a more cooperative, "win-win" approach that balances the overall, long-term interests of postal employees, unions, and management. We said in our report that management and unions in some other organizations, e.g., TVA, Saturn, Ford, were able to implement, at the factory floor level, a cooperative approach after top-level union and company leadership agreed to make some fundamental changes in perspectives, values, and relationships. Our recommendation for a long-term (at least 10 years) framework agreement by the National Leadership Team for demonstrating improvements in the workroom climate was based in part on the positive labor relations experiences of these other organizations.

A number of alternatives exists that could potentially stimulate stronger management-union cooperation and more frequent agreement on issues at the bargaining table in the Postal Service. A criticism sometimes made of the current legislative provisions is that binding interest arbitration tends to drive the parties apart rather than bring them together because, reportedly, arbitrators tend to "split the difference" in their awards and allow, to some degree, both parties to win. Thus, as the argument goes, current binding arbitration provisions can promote uncompromising behavior because each party may hold out for the largest concession from the other party, knowing that the negative consequences of failing will be minimal--perhaps even rewarding.

Alternatives to these binding arbitration provisions of the 1970 Act include the Kappel Commission's 1968 recommendation that, when voluntary mediation and binding arbitration have failed, collective bargaining disputes be referred to the President. The Commission's report said that "The President would be free to establish whatever ad hoc methods he chooses to resolve the matter. The uncertainties for both parties built into the final stages of this procedure make for more meaningful bargaining and are, in our view, a source of strength."

Another form of binding arbitration, "final offer", has also been suggested. We are looking at the experiences of some governments and unions at state and local levels that have used this form of arbitration, and we will provide the results of our work to the Subcommittee. Still another option, which has been used in one state (Massachusetts), is an independent joint labor-management committee to settle contract negotiation disputes. The joint committee can select from a number of options for resolving the disputes. Another technique used at the state and local levels is to require that all arbitration awards be approved by a state or municipal governing entity, such as the state legislature or mayor.

Finally, it may be useful to note that the 1970 Act does not provide any criteria that outside parties, such as mediators or

arbitrators, are to consider when resolving collective bargaining disputes. This is an interesting contrast to detailed criteria of the act for setting postage rates. The act prescribes nine specific criteria that must be considered by the Service and the Postal Rate Commission for setting postage rates and resolving differences between the Service, the Commission, and various third-parties who intervene in rate proceedings.

Question

2. We have heard a variety of interesting approaches to reform of postal systems, although we all know that the U.S. mail system is unique in many ways. What would you say are the most unique features of the U.S. system that create challenges for following the path of other countries in reform? On the other hand, what aspects of our system, if any, are similar to the features of most other countries' systems?

Answer

Perhaps the most unique feature of the U.S. mail system is its size. Significant differences exist in the populations served, and thus the mail volumes and revenues generated, by the U.S. Postal Service compared to the other postal administrations that we reviewed. The Service's larger size would not appear to create any particular challenges in following the path of other countries in reform. However, because of the widely-dispersed U.S. population, issues surrounding the extent and quality of universal mail service, e.g., delivery to all communities 6 days a week, could surface in this country as they have in some other countries. There is also the question of how the practices of a reformed and market-aggressive Postal Service might affect competitors, particularly smaller firms offering mail delivery and mail-related services, given the Service's immense size and potential for economies of scale.

The U.S. mail system, when compared to those of some other countries, also appears to be somewhat unique in the restrictions imposed by law and regulation on the private delivery of mail. More than 80 percent of the Postal Service's mail volume is protected against private delivery under the Private Express Statutes. Information that we gathered and information presented in the February 1995 report by Price Waterhouse indicate that postal administrations in some, if not most, of the other eight countries have much less statutory protection of their mail volumes and revenues. For example, in Canada, about half of the total mail stream is protected against private delivery. A few countries have eliminated the protection altogether.

In addition, many foreign postal services have used their commercial freedom to acquire subsidiaries, participate in joint ventures, and contract out some functions that the U.S. Postal Service handles itself. For example, according to Price Waterhouse, a number of foreign postal services operate a majority of their post offices through private franchises.

Any postal reform initiatives in this country that would give the Postal Service greater commercial freedom to price and market current or new services will likely raise difficult policy issues regarding the Private Express Statutes. Some private delivery firms and mailers may urge a change in the Private Express Statutes to allow private delivery firms greater access to now protected letter mail delivery markets. Also, Congress will likely want to know how universal mail service and the Service's current revenue and rates might be affected by any substantive change in the Statutes. In this regard, we plan to issue a report soon that will include estimates of the changes in the Service's revenue and postage rates if the Statutes are relaxed.

There are a number of similarities between the U.S. systems and those of the other countries that we reviewed, particularly as regard to public service mandates and changes in operating environments. All of the other countries require some form of universal service. Even those countries described as the most progressive in postal reform, such as New Zealand and the Netherlands, have continued to require mail services to all communities.

Another similarity is the challenge of competition from private delivery firms and electronic technology that face the Postal Service and the other postal administrations. According to the Price Waterhouse report, this competition has been a driving force for postal reform initiatives of other countries in the past 15 years. Responding to the changing technology, other postal administrations are already offering new electronic-based services, such as fax services and hybrid mail (a combination of electronic and hard copy message delivery service). Toward that end, the Postal Service is currently devoting considerable market and product research to identifying how it can offer electronic services and is seeking greater statutory freedom to price and market such services.

Questions

3. Given that we have only heard testimony from a few countries, could you expand upon what we have heard by describing how other advanced nations addressed postal monopoly and privatization issues?

A. Last month, GAO's Budget Issues Area issued a report on privatization and divestiture practices in other nations. To what extent, if at all, do you believe that the findings of this report are applicable to the postal arena?

Answers

In addition to those represented at the hearing, we reviewed the postal administrations in four countries: Germany, The Netherlands, the United Kingdom, and France. In answering this question, we use the term privatization to mean a change in ownership from the government to private investors.

The Netherlands have taken steps toward privatization and are currently considering narrowing or eliminating their postal monopolies. The German postal administration has been implementing postal reform in stages, with privatization and deregulation planned for the near future. Under "Postreform I," started in 1989, separate entities were established for the postal administration, postal banking, and telecommunications. Under "Postreform II," the German postal service was commercialized on January 1, 1995. Under "Postreform III," further deregulation and privatization is planned. Deutsche Post said in its 1994 annual report that "the company's privatization will be completed when it goes public in 1998." Germany's postal monopoly was narrowed in 1995, when licenses were granted to private companies to deliver bulk advertising and printed matter weighing more than 250 grams. The German postal minister has outlined legislation to begin deregulating the postal market in 1998 and introduce full competition in 2003, according to Price Waterhouse.

The majority interest in the postal administration of the Netherlands is owned by private investors, and the Dutch government currently owns a 45 percent share of Koninklijke PTT Nederland NV (KPN), the holding company of the postal administration, PTT Post. KPN shares are traded on the Amsterdam and New York Stock exchanges. This is the only postal administration in Europe to have been partially privatized. In the Netherlands, the government's Department of Transport began a review last year of the scope of universal service obligations and the postal monopoly. The Dutch postal administration expects the review to be completed in 1997.

Regarding the other two postal administrations, the British government proposed privatizing their postal administration, but this failed to win the support of Parliament and was withdrawn in late 1994. Our limited information on postal developments in France does not indicate that any actions have been taken toward privatization or narrowing the postal monopoly in that country.

Regarding the GAO report you mentioned (Budget Issues: Privatization/Divestiture Practices in Other Nations, GAO/AIMD-96-23, Dec. 15, 1995), several findings discussed in that report are

relevant to postal reform. The report discusses privatization meaning, for the purposes of that report, divestiture or the transfer of ownership from the government to the private sector. The GAO review focused on the divestiture experiences involving various industries--such as manufacturing; transportation and public utilities; and finance, insurance, and real estate--of five countries: Canada, France, Mexico, New Zealand, and the United Kingdom.

The report says that goal of privatization in some other countries, such as the United Kingdom and New Zealand, was grounded, entirely or in part, in the belief that the private sector could generally operate commercial enterprises more efficiently than the public sector. A form of Postal Service privatization, i.e., transfer of ownership to postal employees, is proposed in H.R. 210, which was discussed at the Subcommittee's November 15, 1995, hearing. It should be noted that the December 1995 GAO report did not include an evaluation of the success in achieving national privatization goals of the other countries.

The GAO report discusses factors that the other countries considered when deciding how and what to privatize, such as the presence or absence of competition and whether the enterprise exhibits natural monopoly characteristics.¹ Some of the countries that sold monopolies either (1) tried to create competition by eliminating the monopoly statutes that had prevented competitors from entering the market, or (2) broke up monopolies, thereby injecting competition. We said that the governments in France and New Zealand will not privatize monopolies. France does not sell monopolies because the government believes that certain public functions, such as the provision of public utilities, require a monopolistic structure to ensure equal access to high quality service. New Zealand will not sell natural monopolies because the government believes that they are economically inefficient. New Zealand will sell statutory monopolies once the legislation that created the monopoly has been removed and the entity has been restructured to allow competition in the industry. The United Kingdom has sold natural monopolies, but in each case it established a regulatory body with the responsibility of preventing abuse of monopoly powers.

Relating to the emphasis placed by other countries on competition, the United States also has varying levels of competition for message (or letter) and merchandise delivery. Expedited letters

¹As defined in our December report, a natural monopoly arises when the entire output of an industry can be most efficiently produced by a single firm, for example, when the firm has significant economies of scale. For this reasons natural monopolies are often regulated or government run. Statutory monopolies are monopolies where an exclusive right to sell is granted by law, and may include natural monopolies.

and parcel delivery services are highly competitive markets and not covered by the Statutes. The delivery of letters to residential customers is subject to the Statutes, and whether such delivery has natural monopoly characteristics is often debated among economists. Notwithstanding the extent of competition or coverage of the Statutes, the rates for all domestic mail services are subject to review and approval by the Postal Rate Commission.

Question

4. The U.S. Postal Service has repeatedly complained that the current ratemaking process allows its competitors access to sensitive and often-times proprietary information. Is this a common complaint by other postal administrations?

Answer

The information we gathered on other countries indicates that their postal ratemaking policies and processes are very different from those followed in the United States. However, in a number of countries, including the United States, there is the issue of how to best balance two seemingly conflicting needs: to protect proprietary rate data, and to ensure that postage rates are not unfair to some customers or predatory toward competitors.

Regarding the need to protect proprietary data, some other countries have given postal administrations freedom to set postage rates without the level of scrutiny by a regulatory body and intervening parties that typifies postage ratesetting in this country. Because of this relative freedom, concerns about protecting commercially-sensitive information from competitors does not appear to be as common in the other countries as in the United States.

As regards the need to ensure fair pricing, it is not clear how the various other governments have done this. In particular, the Subcommittee may want to explore how some other governments provide assurance to the general public and postal competitors that the rates charged by those postal administrations with both statutory monopolies over letter delivery and relatively little independent rate review do not engage in unfair or predatory pricing practices. In this regard, we are aware that competitors of some postal administrations have made allegations of unfair pricing practices. Moreover, Sweden Post was reportedly found in 1993 and 1994 to have engaged in unfair pricing.

To provide some better insight into ratemaking by foreign postal administrations, we are looking at Canada's ratesetting structure for both competitive (nonregulated) and noncompetitive (regulated) services and will be briefing the Subcommittee on our results.

Question

5. In your November 1995 report to the Subcommittee on the Postal Service, you emphasized your support for the Postal Service to be able to utilize volume discounting and demand pricing principles. Do other posts utilize these principles in their respective ratemaking processes?

Answer

We do not have specific information on the pricing principles used by the postal administrations in all of the other eight countries. However, it appears that each of these countries has the flexibility to use market-based pricing methods, including volume discounting and demand pricing, because there is little or no outside review or approval of proposed prices in those countries by a regulatory body similar to the Postal Rate Commission.

As to whether the countries employ volume discounting and demand pricing, Australia Post informed us that it does not use demand pricing methods such as "Ramsey pricing"². Some other foreign postal administrations told us that they use a variety of pricing principles and criteria in formulating postal rates and that demand is only one of a number of factors considered. For example, New Zealand Post said it does not use demand pricing methods such as "Ramsey pricing", explaining that "New Zealand Post does not use rigid formulas to calculate its prices. While market demand will be a factor in assessing price, other factors including competitor activity, cost, and product maturity are also considered." Similarly, PTT Post in the Netherlands also said PTT Post did not use demand pricing methods such as "Ramsey pricing" alone in setting postal rates, adding that "Ramsey pricing is but one of several pricing techniques and principles used in the Netherlands."

Australia Post reported that it did not offer volume discounts in addition to worksharing discounts. In contrast, PTT Post said it offers published volume discounts and has unpublished discounts for very large customers. Canada Post also negotiates some postal rates with large customers. The area of rates negotiated with large customers is complex because volume discounts can be linked to worksharing and thus cost savings. Specifically, it is not clear as to the limitations on the Service's authority to use volume discounts that are cost-based, meaning that the rates vary on the basis of cost savings that result from handling larger volumes of mail. The Postal Rate Commission has indicated that such cost-based rates might be justified under the act. Further, United Parcel Service claimed that some of the Service's

²Under Ramsey pricing, an agency would set prices so that, in each market segment, the percentage markup would be inversely proportional to the elasticity of demand in that segment.

international mail rates were improperly reduced through volume discounts, but the court decided that those rates complied with the 1970 Act.

Question

6. Some foreign posts operate pursuant to a "for-profit" mandate, as opposed to the U.S. statutory mandate to "break-even." Would a profit mandate be prudent for the U.S. postal system? Given the fact that the Postal Service has been viewed as a source of deficit reduction in the past, and most recently by Administration (e.g. the retiree health benefit prefunding issue), what impact would this profit mandate have on postal operations?

Answer

A for-profit mandate may warrant consideration by Congress, particularly if the mandate is part of an overall Postal Service reform initiative that includes some degree of privatization, i.e. a change of ownership. Such an initiative would presumably give the Service the flexibility to set prices and otherwise manage itself like a private business, while also continuing to provide certain basic mail services to all communities. Also, it would require that the Service make business forecasts as a basis for setting prices and controlling cost in order to provide both a reasonable return on investment to owners and a reinvestment of profits in increasing or maintaining future earnings capacity.

Further, it has been argued that, if the Service is to compete with private firms, it should do so on a level playing field. This would appear to require that the Service set prices sufficient to return a profit, as its competitors must do, not to just break even. Similarly, the Service is planning major investments in new products that are to compete in electronic communications markets. If the products are profitable, they could help to restrain the growth of postal rates. However, to the extent that the Service's ventures into the electronic arena are not profitable, all mailers may incur higher mail costs through higher postage rates, most of whom have no choice but to use the Service.

Whether profits generated from a reformed Postal Service should be used as payments to the Treasury for deficit reduction or other purposes is a question to be decided by Congress. We have not determined how such a policy might affect the Service's operations. We are aware of one case--the Tennessee Valley Authority (TVA)--where such payments were established and rationalized as a return of the government's investment. In 1959, Congress amended the TVA Act of 1933 to require that TVA operate on a financially independent basis by, among other things, issuing public debt to finance its electric power program. One provision of those amendments was the requirement that TVA make annual

payments to the U.S. Treasury as a return on the government's net investment in the TVA power program.

Question

7. One of the significant aspects of the Australian postal reform experience is the amicable labor-management relations which Australia Post enjoys. Mr. John testified regarding a "Joint dispute settling procedures" and committed the organization to participatory management practices. What prevents the USPS management and labor organizations from entering into a similar agreement?

Answer

By way of background, Australia Post has reported that an autocratic, top-down style of management contributed to their labor problems in the 1980s. Australia Post credits an independent advisory commission known as the Industry Commission for intervening after disputes had escalated. After a truce was declared, union representatives, workers, and managers at one mail center met to discuss their problems. A number of other local meetings followed and then a national agreement was reached between the government and the main postal union, which set out the process to guide future relations.

A barrier to an agreement between the U.S. Postal Service and its labor organizations was said to be ongoing contract negotiations, including binding arbitration proceedings. It was only after the Subcommittee's recent inquiry about the status of such an agreement that some progress appears to have been made toward getting the two largest unions (the National Association of Letter Carriers and American Postal Workers Union) to agree to meet and begin discussing a framework agreement for improved relations. The Subcommittee's continued monitoring of this critical issue might help to encourage the parties to make some fundamental changes in their relations.

A reason for the lack of any substantial change in Postal Service labor-management relations over many years may be the lack of sufficient incentives for change. Mail volume continues to grow, and the Service continues to obtain approval of rate increases every 3 to 4 years. In this growth environment, neither cooperative or hard-nosed approaches by the current and previous Postmasters General appear to have resulted in improved labor-management relations.

As we reported in September 1994, if the problems we reported still remain after 2 years, Congress may want to reexamine relevant provisions of the 1970 Act that may constitute barriers to improvement.

Question

8. Many of the postal administrations surveyed cited that their reasons for reform were that their current respective systems faced serious bureaucratic and political interference, postal deficits were draining national treasuries, and labor-management problems were leading to a profound distrust of the post's ability to perform its functions. This sounds like the atmosphere which led to the creation of the Postal Reorganization Act. In reviewing reform initiatives, did any of these countries consider the current U.S. model?

Answer

We have little information on this question because our review of foreign postal administrations focused on the current status of postal reforms. One report³ on Canada Post said that the idea of transforming the Canadian Post Office Department was "given further momentum" when the United States set up the U.S. Postal Service." (Canada Post was established as a Crown corporation about a decade after the 1970 act that created the U.S. Postal Service.) The author of that report noted that "The Canadian situation was unlike that in the United States, where the idea of a postal Crown corporation did not have to be sold to the postal community; outside of immediate government circles, no postal constituency was opposed."

To better respond to your question, we recently submitted the following question to foreign postal administrations identified in our testimony: Are there any features of the U.S. postal system or the U.S. Postal Service that have been used as a model for postal service in your country? Three postal administrations, Australia Post, New Zealand Post, and PTT Post in the Netherlands, all answered "no". We will provide the Subcommittee with other responses that we receive.

Question

9. GAO refers to the difficulties of making meaningful comparisons between the U.S. Postal Service and other postal administrations. The Service has compared its postage rates to other countries' rates, stating the rates in the U.S. Postal Service is operating more efficiently than other postal administrations, including those recently reformed?

³Robert M. Campbell, The Politics of The Post: Canada's Postal System from Public Service to Privatization, (Canada: Broadview Press, 1994).

Answer

When comparing the U.S. system with mail systems of other countries, it is important to keep in mind that detailed comparisons of operating characteristics, efficiencies, prices, and productivity can be misleading. Postage rates in the United States are said to be among the lowest in the world, but this does not necessarily mean that the U.S. mail system is operating more efficiently than some other postal administrations. The lower rates in this country might be explained, in part, by differences among countries and postal administrations in the overall mail volumes delivered. The volume of mail handled in the U.S. mail system is twice the combined mail volume of all eight countries we reviewed. This difference would appear to offer economies-of-scale advantages of the Postal Service compared to other postal administrations.

Other differences might also affect detailed comparisons among countries such as variations in the shape, size, and weight of the mail delivered; the geographic density of customers; and, perhaps of greatest importance, the degree to which postal customers themselves prepare, e.g., presort and prebarcode letters, and transport mail before it is accepted by the postal administrations for delivery. In this country, the vast majority of the mail delivered to homes and businesses has been presorted (and often transported) to some degree by mailers.

Question

10. GAO does not identify any particular change made for other postal administrations that could be incorporated into the U.S. mail system. Are there any changes in universal service, the mail monopoly, or ratemaking that GAO believes would be appropriate for this country? Are there specific cautions that you would offer the Congress when considering postal reform in this country?

Answer

Regarding universal service, some other postal administrations--such as Canada Post Corporation--have used franchises quite extensively to provide certain retail mail services to communities. The experience in Canada and possibly some other countries with franchised postal retail operations might be explored in terms of customer/community acceptance, quality of service, and economies achieved.

Some other countries have redefined and narrowed their mail monopolies. We are currently looking at the basis for the current scope of the U.S. mail monopoly, i.e., the Private Express Statutes, and expect to issue our report in the near future. At present, the monopoly covers about 83 percent of the Service's total mail volume. Because the purpose of the Statutes is to

protect the Service's revenue base so that it can provide universal service, it is important to know, when considering whether to change the Statutes, how the Service's revenue will be affected by such change. Our report will include a range of estimates of the effects of relaxing or repealing the Statutes on the Service's revenue, cost, and postage rates.

Regarding ratemaking, some other postal administrations are reported to have more flexibility than the Postal Service in setting postal rates. We have previously reported that one of the areas in need of change is the ratemaking criteria and process prescribed in the 1970 Act. The Service is constrained by the act in quickly responding to changes in market conditions because all of its proposed changes in domestic postage rates are subject to extensive outside review by competitors and various other parties and ultimately approval by the Postal Rate Commission. Because most (over 80 percent) of the Service's mail volume is protected from competition by the Private Express Statutes, there is a need to ensure, as provided in the 1970 act, that all of the Service's prices are sufficient to cover direct and indirect cost and other reasonably assignable cost and that the Service does not engage in anticompetitive practices. However, there may be alternatives to the current review process and criteria for achieving that end. As mentioned previously, we are examining the approach followed in Canada for setting postage rates and, particularly, for assuring that the rates are fair to all customers and meet statutory requirements in Canada's Competition Act, which prohibits cross-subsidization and unfair competition for all Canadian companies.

As just one caution regarding changes in the 1970 Act, many of the provisions of the act and the associated policies and practices that have since evolved are very complex and interrelated. It is important, therefore, that the possible effects on the overall systems be considered when proposing any particular legislative change. Specifically, universal service, ratemaking, and the monopoly are all interrelated. According to the Postal Service, universal service is not possible without the current scope of the statutory monopoly. One of the principal reasons for the current provisions of the act on ratemaking is to help ensure that the Service does not abuse the statutory monopoly. Consequently, reducing the Postal Rate Commission's role in reviewing proposed postage rates, without also reducing the scope of the monopoly or in some way ensuring that the monopoly is not abused, would likely increase claims by competitors of anticompetitive practices and concerns among customers about the fairness of postage rates. Similarly, reducing the monopoly without giving the Service greater flexibility in deciding how it will provide universal rates, e.g., allowing the Service to select more efficient methods of providing access to services and to pay competitive labor rates, will likely increase postage rates to a greater extent than otherwise might be the case.



**Australia
Post**

POST

14 March 1996

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Mr John M McHugh
Chairman
Subcommittee on the Postal Service
Congress of the United States
2157 Rayburn House Office Building
Washington DC 20515-6143
UNITED STATES OF AMERICA

Dear Mr McHugh

I refer to your letter of 6 February 1996 which reached me only on February 21.

In the Attachment to this letter, I have provided responses to the written questions appended to your letter. Please do not hesitate to contact me if you need clarification of any outstanding issue.

Best wishes on your endeavour.

Yours sincerely

Graeme John

ATTACHMENT**RESPONSES TO QUESTIONS FROM THE HONORABLE JOHN M McHUGH**

Q1 In your prepared text you discuss the services Australia Post provides through its retail outlets, including the processing of passports. Is the Australian Postal Corporation dependent on non-traditional postal business to break even/make a profit. Do postal and nonpostal product lines cross subsidize one another? Similarly, would you expand on your comments regarding the Australian Post *selling* its services to Government Departments?

A The Australian Postal Corporation trading as Australia Post derives most of its revenue and profits from traditional postal business. In 1994/95, the latest complete financial year, Mail Services, Philatelic Products and the Postal Money Order Services generated 92 percent of corporate revenue, and a commensurate proportion of profits.

While Australia Post operates its letter service under legislation which gives it exclusive rights of carriage over a defined product range, it is otherwise subject to the requirements of competition policy, and in particular to the Trade Practices Act. In short, Australia Post is not permitted to, nor does it engage in legislatively proscribed anti-competitive conduct, including cross subsidisation from "reserved" to "non reserved" services.

Apart from the carriage of letters reserved to Australia Post, Government Departments purchasing is generally subject to competitive tendering. In this way, Australia Post has to compete with other local producers with respect to the supply of services to Government. Examples of sales in this category include the supply of courier services, unaddressed mail and agency (billpay) services.

Q2 You mention that many of these reforms were born of the Industry Commission Inquiry which was completed in October 1992. Would you expand a little about this Commission, its make-up and mandate, and offer your thoughts on whether an independent Commission study is necessary before reform can be achieved?

A The Industry Commission is a long established Australian institution. It began in the 1920's as the Tariff Board when its focus was customs tariffs and tariff protection. In 1972 it became the Industries Assistance Commission and its focus was expanded to cover industry assistance in general. In 1989 its focus was again widened to cover economic efficiency in a wider sense, and was renamed the Industry Commission.

Currently, the Industry Commission operates under the Industry Commission Act 1989. The functions of the Commission are "...to hold inquiries and make reports to the Minister in respect of such matters relating to industry as are referred to it by the Minister...". The General policy guidelines for the Commission in section 8 of its enabling Act principally are:

"(1) In the performance of its functions, the Commission must have regard to the desire of the Commonwealth Government:

- (a) to encourage the development and growth of Australian industries that are efficient in their use of resources, self-reliant, enterprising, innovative and

internationally competitive; and,

- (b) to facilitate adjustment to structural changes in the economy and to ease social and economic hardships arising from those changes; and
- (c) to reduce regulation of industry (including regulation by the States and Territories) where this is consistent with the social and economic goals of the Commonwealth Government; and
- (d) to recognise the interests of industries, consumers and the community, likely to be affected by measures proposed by the Commission."

For the past twenty five years, the Industry Commission and its forebears have consistently adopted a pro-competitive stance, advocating the removal of restrictions to competition as the major driver for economic efficiency improvement.

The Industry Commission is an independent advisory statutory body. Its members are appointed for fixed terms. While the Commission has no executive powers, it has enjoyed considerable influence over policy making, notably in the 1970s. It has developed major competence in quantitative economic analysis and modelling, and continues to be an important source of policy advice in Australia.

In response to your question on an independent Commission study, I believe such a study would be generally helpful in eliciting facts and data, and reinforcing public perceptions of objectivity, especially if the processes of consultation and inquiry used are public and encourage interested parties to express their views. Further than that however, the success of reform, in my view, depends on carefully designed solutions which incorporate incentives to stimulate the required behaviour.

Q3 You say there are no cross-subsidies, then state the uniform letter rate entails an internal cross-subsidy funded within the Post. Would you expand on this exchange and comment on whether it is necessary to monitor the amount of the cross -subsidy?

A First, it is necessary to clarify the position. Australia Post makes every effort to attribute costs to products and services on an **objective causal basis**, across all postal activities. Thus costs are recorded separately for reserved and non reserved services, and for their component services.

With regard to non reserved services, as already indicated above Australia Post operates in generally competitive markets, and postal prices are set commercially in this sector. As already stated above, Post is always careful not to engage in legislatively proscribed competitive behaviour, including cross subsidisation.

In regard to reserved services, the legislated social obligations (including the obligation to price uniformly) lead to prices being set on the basis of **average costs**, and inevitably, some services do not recover their actual costs. To this extent therefore, there are cross-subsidies **within the reserved services**.

Second, I would suggest that the quantification and monitoring of the cross subsidy

increasingly will be required for the processes if government. For the evaluation and efficiency of delivery of social programs (such as those part of the postal service's mission), benefits and costs will need to be measured and matched on an ongoing basis.

I should add however, that where the postal service is operated on a commercial basis,, the evaluation of the cross-subsidy should allow for the fact that some loss making activities are undertaken for valid commercial reasons - accordingly, the losses on such activities, should be excluded from the aggregate cross-subsidy.

Q4 As you know, sanctity of the mail is a major U.S. concern and this is typified by restricted access to a customer's mail receptacle. You do not have this restriction and I am very interested in having your comments on how you have handled this, particularly, as it related to theft of mail or fraud. Would you comment on this? Are outside commercial carriers allowed access to deliver to those boxes or receptacles located in postal facilities?

A In Australia, the customer's mail receptacle has always been available to Australia Post for **delivery purposes** (but **not** used for mail to be collected by postal staff) on a non-exclusive basis. Other carriers (eg carriers of unaddressed mail), other organisations (eg utilities) and private individuals also have access to those receptacles. Of course, some parcels carried by Post could not fit into the receptacle, and are delivered to the door or made available for delivery at a post office counter.

Australia Post, like the USPS, has always believed in the sanctity of the mail, and has organised its own processes to ensure that high standards of security apply.

Our experience is that the incidence of theft or fraud has not been affected by our practices.

With regard to private boxes/bags (the receptacles located in postal facilities), Australia Post retains exclusive access.

En affaires pour vous servir.

In Business to Serve

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March 5, 1996

Mr. John M. McHugh
Chairman, Subcommittee on the Postal Service
2157 Rayburn House Office Building
Washington, DC 20515-6143
USA

Dear Mr. McHugh:

On behalf of Canada Post Corporation, I would like to thank you for inviting me to take part in the joint House and Senate hearing on reform initiatives for the United States Postal Service. I certainly appreciate the profound interest your country continues to demonstrate towards our postal administration. I hope you find our answers helpful as you continue your examination on postal reform initiatives for the United States.

I wish you the greatest success in your role as Chairman of the House Subcommittee on the Postal Service.

Sincerely yours,


Georges Clermont

1. Operations Improvements

As you accurately stated, Canada is the largest country in land size in the western hemisphere and its population density is far less than the United States. In spite of the need to travel longer distances to deliver mail, Canada Post Corporation (CPC) was able to improve our on-time delivery from 85% to 97-98% in a decade. These on-time delivery improvements can be attributed to a management group determined to improve customer service by motivating its employees.

In 1987, CPC became the first postal administration in the world to implement and publish the results of external, independent tests of domestic lettermail delivery performance. These independent tests gave employees an opportunity to objectively evaluate and improve their performance levels. In 1994/95, Ernst & Young reported that CPC achieved on-time delivery 97% of the time for properly prepared, local, provincial and national domestic lettermail between major urban centres. Since 1989-90, CPC has consistently maintained that lettermail delivery performance at or above 96%.

As well, a National Control Centre was created to monitor service performance. Through this Centre and five linked regional control centres - the most sophisticated mail monitoring system in the world - CPC uses the best available telecommunications and computer-based technology to monitor every aspect of mail movement on a continuous basis.

While improving on-time delivery, the Corporation also focuses its efforts on operational improvements. Surveys performed throughout the world by the International Postal Organization show that Canada has the most automated postal administration. Since 1982/83, CPC has used two broad standards to measure productivity: pieces of mail processed/hour paid, which is a measure of processing productivity; and letter carrier points of delivery/hour paid, which is a measure of delivery productivity of the letter carrier operation. For 1982/83 to 1994/95, processing productivity has improved 65%, primarily as a result of the implementation of advanced processing equipment and other technology. This has been achieved despite the significant constraints of work rules in CPC's collective agreements. Work rules relating to collection and delivery also restrict CPC's ability to achieve productivity gains. However, in the same period and while points of delivery increased nearly 30%, overall delivery productivity improved 24% largely through the introduction of community mail boxes and other similar equipment.

Therefore, most productivity gains have resulted from the following initiatives: an equipment replacement program to improve lettermail processing; a program for downsizing of management and administrative employees; the introduction and expansion of new delivery equipment, particularly community mail boxes; restructuring of CPC's retail network through franchising; and a program to reduce absenteeism.

2. Learning Institute

In conjunction with Queen's University and l'École des Hautes Études Commerciales (HEC), affiliated with the University of Montreal, CPC created the Learning Institute in June 1994. This \$56 million annual training expenditure represents an investment of approximately \$1,000 per employee. This investment continues to play an important role in CPC's "In Business to Serve" program by enhancing customer service and strengthening CPC's contributions to the business and social infrastructure of the country.

The training is being offered in the workplace or at existing facilities, such as community colleges and universities. The courses are delivered by Queen's School of Business, HEC and in-house trainers, assisted by private-sector specialists.

Although it is difficult to quantify, the return on the increased investment in learning is reflected through the strengthening of our competitive abilities in three key areas. First, the Learning Institute helps employees develop a better understanding of the Corporation in the context of our markets and the challenges the Corporation is facing. Second, the Learning Institute's programs maintain a strong emphasis on customer service, which is a vital element for the Corporation's future. Third, leadership training and development is perhaps the most important qualification for employees who aspire to promotion and career progression within the Corporation. By helping people to prepare for other career possibilities, both the employee and the Corporation gain long-term benefits.

The Corporation's commitment to the Learning Institute clearly demonstrates that we are determined to invest in our most important asset: our people. To a great extent, we can buy technologies and systems. But people - with the new skills, attitudes and understanding - make our business operate efficiently and will determine our success in the future.

3. Rate Setting Process

The establishment of rates for products and services offered by CPC is conducted within a complex array of external and internal authorities, policies and process. As noted in my written testimony, the basic letter rate is indeed set by Cabinet. Specifically, the setting of rates can be further explained by examining statutory and regulatory authority.

Statutory and Regulatory Authority

Canada Post Corporation Act

The *Canada Post Corporation Act* ("the Act") has specific provisions with respect to the establishment of postal rates. The Act obliges the Corporation to have regard to the need to be self-sustaining financially while providing a service that is similar to communities of similar size. CPC can make regulations with approval of the Governor in Council (GIC) prescribing rates of postage. In addition, the Act states that such rates of postage shall be fair and reasonable and consistent so far as possible with providing a revenue, together with any revenue from other sources, sufficient to defray the costs incurred by the Corporation in the conduct of its operations under this Act

The Act defines the external process for approval of modifications of rates established by regulation. All proposed rate regulation changes (including proposed removal of certain rates from regulation to be set by the Corporation) must be published in the *Canada Gazette* Part I for a period of 60 days inviting interested parties to make representations to the Minister Responsible for CPC on the proposed changes. The Corporation reviews these representations and seeks its Board of Directors' approval of the final form of the proposed rate regulations. The final form of the proposed regulations is submitted by the Corporation to the Minister who must forthwith submit these proposals to GIC for their consideration. The GIC has 60 days in which to accept or reject the proposed rate regulations (it cannot vary the proposed rates). If GIC does not make a decision within 60 days, the proposed rate regulations are deemed approved.

The authority under the Act to establish rates of postage by regulation is permissive as opposed to obligatory. The Corporation has over time sought and received GIC approval for the removal of numerous rate categories from regulations thereby reserving the formal, more complex external rate regulation approval process primarily for letter mail products that fall within the corporation's exclusive privilege and that do not involve incentives for mail preparation. This practice recognizes that the rates outside of regulations are those subject to competition or which represent operational incentives/discounts from letter rates set by regulation. It should be noted that the Act explicitly provides that CPC may prescribe rates of postage outside of regulation through customer agreements for bulk mailing, additional customer mail preparation that facilitates processing, receiving additional services, or for experimental services for any period not exceeding three years.

Corporate Plan

Section 122 of the *Financial Administration Act* states that each parent Crown corporation shall annually submit a corporate plan to the appropriate Minister for the approval of the Governor in Council on the recommendation of the appropriate Minister and, if required by regulations, on the recommendation of the Minister of Finance and, in practice, the Treasury Board.

The Corporate plan is perhaps the most important factor related to rate making. It is a continuous activity of review and analysis to ensure that CPC is on course to achieving its goals. The Corporate Plan expresses how the Corporation intends to meet its objectives with respect to products offered, service performance, customer access, employee welfare, and financial performance over the coming five-year period. Through the target modelling process, the Corporate objectives and profitability goals are translated into functional targets (both revenue and cost). To meet its financial objectives, the Corporation in its plans attempts to balance its financial requirements among efficiency, business growth, and pricing.

The Corporation prepares its five-year Corporate Plan and submits it to the Board of Directors for approval. The Corporation then submits the Plan to GIC for approval on the recommendation of the Minister and, in practice, of Treasury Board. Included in the Corporate Plan is a summary of proposed general rate increases by major product area for the five-year period including specific references to the basic domestic letter rate.

U.S. Ratemaking Process

The regulatory environment in the United States has been characterized by conflict, political intervention and substantial influence by direct competitors of the U.S. Postal Service. The existing system is burdensome, rigid, political and highly contentious. This system has affected dramatically, and detrimentally, the continuing ability of the Postal Service to compete effectively. The current system generates barriers that constrain the Postal Service from pricing correctly, offering new products and providing enhanced services. This has led to a decline in the market share of the Postal Service in a number of competitive markets.

Hearings before the Postal Rate Commission typically involve interventions from customers and competitors of the Postal Service; both groups criticize the pricing and costing methodologies of the Postal Service, albeit for different reasons. Customers, for instance, oppose rate increases and frequently argue that the costs attributable to products they purchase or utilize are below the amounts calculated by the Postal Service. Direct competitors of the Postal Service, such as UPS and Federal Express, have a vested interest in hampering the ability of the Postal Service to compete by causing it to charge high prices. For these reasons, competitors typically produce studies in Commission hearings that show the Postal Service's attributable costs to be above those calculated by the Postal Service. Competitors such as UPS and Federal Express intervene in virtually all proceedings before the Commission and argue persistently for much higher levels of attribution of costs to products that have been proposed by the Postal Service. The result of this position can be to require the Postal Service to charge artificially high prices for its products or services and render the Postal Service unable to compete effectively on a price basis.

The existing regulatory structure in the United States has had an adverse impact on the ability of the United States Postal Service to compete effectively in the markets it serves. The current system virtually precludes the Postal Service from using pricing to define market niches. In most industries, correct pricing is an iterative process in which prices adjust to the changing realities of the marketplace. Pricing is also used to identify particular groups of customers who are interested in a specific part of a firm's product offering. The rigidities inherent in the existing regulatory system in the United States, however, have led to the result that prices cannot be changed any more rapidly than every three years. This severely handicaps the ability of the U.S. Postal Service to compete.

The existing process also limits the ability of the Postal Service to offer new products or services. This is the case because the Postal Service requires prior approval from the Postal Rate Commission before offering new product or services. Such approval cannot be obtained without providing to the Commission extensive prospective cost and market information which, in the case of new products, is virtually impossible to obtain or provide. Competitors can utilize the regulatory process to achieve the purpose of blocking the introduction of new products, and to cause the Postal Service to charge prices that are too high to make the product feasible. The process requires the Postal Service to disclose details concerning proposed new products to its direct competitors before those products are brought to market. The process enables direct competitors to acquire proprietary information concerning existing and new or proposed products of the Postal Service. There have even been some indication that competitors have attempted to use the Commission's discovery process to demand the production of confidential data or information which has little or no bearing on the case at hand.

The above position taken by our Rate Economics Department and I supports several of the comments Professor Michael D. Bradley, from George Washington University, has expressed in his study, "The Effects of Regulation on the Competitive Position of United States Postal Service" (November 17, 1995).

4. Labour-Management Relations

The unionized employees of Canada Post Corporation are organized into four bargaining units represented by four different unions. The largest bargaining unit consists of 38,700 employees of CPC working in its operational networks and is represented by the Canadian Union of Postal Workers (CUPW). The 7,000 employees working in rural offices are represented by the Canadian Postmasters and Assistants Association (CPAA). CPC's 3,000 unionized administrative, technical and professional employees are represented by the Public Service Alliance of Canada (PSAC). The Association of Postal Officials of Canada (APOC) represents CPC's 2,800 operational supervisory employees. CPC has separate collective agreements with each of these four unions.

When CPC was incorporated in 1981 as the successor to the Post Office Department (the POD), one of the primary objectives of both the federal government and the POD employees and unions was improved labour relations. In the 14 years of CPC's operations, labour matters have continued to be of great importance. In the late 1960's and the 1970's, the POD experienced its most unsettled period of labour relations, which culminated in a strike by CUPW in 1975 that lasted a record 42 days. Precipitated principally by union opposition to the implementation of mechanized mail processing, the 1975 strike ended with a settlement that made major modifications to the previous CUPW collective agreement in the form of work rules that restricted the operational flexibility of the POD. CPC's current collective agreements still contain many of these restrictive work rules, as well as others that were added subsequently. The 1975 strike was settled through mediation, reflecting the POD's inability to conclude a collective agreement without third party assistance. Of the 14 rounds of collective bargaining with CUPW and the Letter Carriers' Union of Canada (LCUC) alone in this final period of the POD, only one was completed without third party assistance from mediators, conciliators or arbitrators. On one of those occasions, a collective agreement was reached only after back to work legislation and binding arbitration.

When CPC was created in 1981, the implementing legislation prevented both the renegotiation of the POD's collective agreements and changes to its bargaining units, which would otherwise have been permitted at that time. In doing so, the legislation deviated from the recommendation of the final government report that had preceded conversion of the POD into a Crown corporation, which had analyzed organizational issues arising on the conversion. When CPC's mandate was first reviewed in 1985, the Marchmont Committee recognized the adverse effects of the inheritance by CPC and its employees of the labour relations of the POD and recommended that CPC's bargaining units be consolidated and that CPC negotiate to eliminate restrictive work rules impeding operating efficiency.

Although the consolidation into four bargaining units took place in 1988, its practical effect was not felt until the 1989-1992 round of negotiations - eight to eleven years after CPC's incorporation. In addition, restrictive work rules have remained in collective agreements through five rounds of negotiations between CPC and its unions. While the 1994 round produced a collective agreement one month before the expiry of the existing one, previous CPC rounds involved three strikes and a continued pattern of reliance on third party assistance for concluding collective agreements. In 1987 and 1991, back to work legislation and binding arbitration were required.

Since 1991, labour strife - as measured by the decline in the backlog of grievances and other factors - has, however, been reduced. In that period, CPC has ensured continuity of service to its customers through negotiated, rather than imposed, collective agreements and has avoided both strikes and threats of strikes. Other improvements in labour and employee relations have been achieved, particularly through the establishment of joint labour - management mechanisms for the consideration of workplace issues.



March 6, 1996

Mr. John M. McHugh
Chairman of Subcommittee on
the Postal Service
Congress of the United States
House of Representatives
Committee on Government Reform
and Oversight
2157 Rayburn House Office Building
Washington, DC 20515-6143
USA

Dear Sir

I highly appreciated the opportunity to meet you and your distinguished colleagues in the Committee on Postal Services and the kind hospitality I met during my stay. It is truly an honour for me and Sweden Post to have been invited and to inform the Committee about our experiences and ideas. We are of course pleased to answer any additional question that may arise. With reference to your letter I would like to give the following comments.

1) The system in Sweden has always been based on individually owned maildrops or mailboxes, without any exclusive rights concerning access for Sweden Post or any other operator. We have no significant negative experience of this system.

The sanctity of the mail is protected by legislation. The legislation in that context does not make any difference between Sweden Post and other operators.

2) On 1 March, 1994, the Sweden Post Public Service Corporation - the Government administration - was transformed into a limited liability company. The procedure chosen for conversion was that first *the assets and liabilities of the business were transferred at book value* to Postbolagen AB (formerly a subsidiary of the public service corporation), which was then renamed Posten AB. The operations of Postgiron were transferred at book value to a newly established limited liability bank, Postgiron AB, wholly owned by Posten AB.

All operations are now conducted within a limited liability group whose parent company is Posten AB. The Parent Company is 100 per cent owned by the Swedish State.

Since the middle of the 1980's Sweden Post has showed good economic results. The equity has increased from \$ 460 million in 1987 to \$ 1 700 million six year later. At the conversion the former public service corporation's pension liability - \$ 1 200 million - was booked as a liability directly against the equity.

3) Although Sweden Post meets competition on all markets, new technology is the key factor to the decline in volumes of transactions at postal counters and the decrease in mail volume. With the new technology transactions can be performed electronically which make private customers and companies less dependent on post and bank offices. This process will no doubt continue. There are no way back. Our strategy is then to reduce the number of post offices and to develop a new service concept based on co-operation with private entrepreneurs. Instead of maintaining unprofitable post offices, Sweden Post can offer their customers a basic service through selected shops in co-operation with private shop-owners.

Sweden Post sees the new technology and the IT development as a friend. We make use of the technology in all our services also including the traditional letter business. It is not competition from new operators that is challenging the letter. The position of the letter as means of communications is seriously under threat by developments in technology. In this market, electronic systems are gaining market share day by day. As I stated in my testimony, fax, ePost, eMail, eDI etc. already accounts for more than half the volume of messages across borders, as well as for 20 per cent of business communications in a country like Sweden.

4) It seems that the quotation you are referring to is from Mr Persson's presentation. My interpretation of the text is that the abolition of the monopoly also confirmed that the company is on the market without any administrative safeguards. The basic reason for advocating abolition of the monopoly was that the monopoly no longer represented an effective instrument. As we were facing real competition from new technology on the market for messages, a monopoly legislation would be inadequate.

We are now totally dependent on our own skill and strength to keep Sweden Post's position on the market. The abolition of the monopoly legislation - made it absolutely clear to our own staff and to customers that we have no one to rely on but ourselves.

Sincerely yours,



Ulf Dahlsten

New Zealand Post

*Elmar Toime*

CHIEF EXECUTIVE

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29 February 1996

Mr John M McHugh
 Chairman
 Sub-Committee on the Postal Service
 Committee on Government Reform and Oversight
 House of Representatives
 Congress of the United States
 2157 Rayburn House Office Building
 Washington DC 20515-6143
 USA

Dear Mr McHugh

Thank you for your letter of 6 February 1996. I appreciated the opportunity to address the Joint Committee Hearing as I believe that there is a lot to be learnt from the shared international experience in postal reform. As you know, I am keenly interested in postal reform and look forward to the eventual recommendations from the Committee.

Q.1: Labour Management Reform

I agree with the sentiment evident in your first question that improving employee productivity lies at the heart of achieving successful postal reform. My reference to conservative change referred to the regulatory environment - the letter monopoly and the exclusivity of the mail box. I formed this view based on my knowledge and understanding of the postal market in the USA.

To change the regulatory environment at the same time as you might change the business and commercial structure of the USPS would be too threatening. Customers and employees of the USPS could be expected to resist because of the uncertainty so posed.

My concept is to hold firm for a given time period (eg three to five years) on the regulatory environment, but introduce real change into how the USPS is managed as a commercial company.

In New Zealand Post, management and Board created a sense of urgency through the Government-led expectation of deregulation within three years. The monopoly was significantly relaxed at that point, but essentially still remains today, nine years later.

In contrast to my views on slower regulatory reform, major change with people needs to be done quickly.

Labour management reforms cannot be separated from other areas of commercial reform.

I would suggest that first and foremost a prescription is required to establish the USPS as a corporate entity - the United States Postal Corporation (USPC). Upon vesting day, through an Act of Congress, postal employees will be deemed to be employees of the USPC, with broadly similar conditions of employment. Pension liabilities would be frozen for existing employees, and future liabilities written into the balance sheet. This is obviously a complex area, but the aim would be to create, over time, a pension structure to match corporates in the private sector.

The USPC would become responsible for negotiating its collective employment contracts. It would use a mandate to be profitable as the lever to reach settlement with its own employees.

You should not underestimate the potential for managers, who have been given full responsibility to operate the business, to reach negotiated settlements in the mutual interests of the business and its stakeholders.

Given these full responsibilities, the language of business comes to the fore: variable costs, not fixed; productivity (labour and capital); flexible work practices; customer satisfaction; competition; employee satisfaction; incentive rewards systems; and so on.

In New Zealand three factors come to mind which have contributed to our ability to make fundamental change in this area of employee contribution. These are:

- having final responsibility for labour management practices resting within the Company;
- management (and, in time, employee) reward systems which emphasise commercial success;
- having a mandated commitment to growth and commercial freedom.

So, for example, if productivity growth leads to a decline in employment levels, there are nevertheless business mechanisms in place targeting future growth and therefore, eventual better job security.

Make no mistake, labour reform is as much about attitudinal change as it is about working conditions. Congress may be able to influence the latter, but it cannot directly attack the first. The best it can do is put the business environment for change in place.

Q.2 Rates

You have asked about New Zealand Post's authority to set prices. As I explained in my evidence New Zealand Post is free to introduce new products and to establish the prices for those products without reference to any Government agency. Pricing decisions are decisions for the Board and are not subject to supervision.

There is one exception. That relates to a service known as the standard letter service which provides one to three day delivery for letters throughout New Zealand. There is a price cap relating to this product. It is the only product regulated in this way. The price cap mechanism which is established in a contract between New Zealand Post and the Government (Deed of Understanding) enables New Zealand Post to increase the price of the standard letter service according to a formula (the movement in the Consumer Price Index since the last price increase minus 1%). The last price increase for the standard letter service was in 1992. At that time the price increased from NZ\$0.40 cents to NZ\$0.45 cents. Movements in the Consumer Price Index since that date would enable New Zealand Post should it wish to, to increase the price of the standard letter service to NZ\$0.50 cents. In fact in October 1995 New Zealand Post reduced the price of this service to NZ\$0.40 cents. This reflected our determination to ensure that letters remain a cost effective means of communication for business mailers. The decision - which was extremely well received by New Zealand Post's customers - has stimulated increased letter volumes since its introduction.

Pricing decisions are often made quickly. They need to be to enable the Company to respond to movements in the dynamic and competitive markets in which we operate. There is no prescribed process which we require people to go through to establish a new price. The Board gives final approval for key price changes.

You would be surprised at the rapidity with which New Zealand Post can make pricing decisions. The longest process may well be the gap between announcement and effective implementation. As a policy, we provide for a minimum of one month notice for a price change. For our recent price reduction, we allowed for a three month advice period, to allow the public to work through stamp stock levels.

Q.2b "To Be Successful"

New Zealand Post was established under the State Owned Enterprises Act 1986. This means that it is a company incorporated under New Zealand company law which has as its shareholders two Ministers of the Crown, the Ministers of Finance and State Owned Enterprises. The State Owned Enterprises Act establishes the objectives for these types of Crown trading enterprises. Section 4 of that section provides:

"Principal objective to be successful business - (1) The principal objective of every State enterprise shall be to operate as a successful business and, to this end, to be -

- (a) As profitable and efficient as comparable businesses that are not owned by the Crown; and*
- (b) A good employer; and*
- (c) An organisation that exhibits a sense of social responsibility by having regard to the interests of the community in which it operates and by endeavouring to accommodate or encourage these when able to do so."*

Balancing these competing requirements is not easy. However the Courts have recognised the importance of State Enterprises taking a broad commercial focus in decision making. Although some Company decisions - such as the restructuring of the network of post offices in 1987 - have been challenged on the basis that the Company has failed to "exhibit a sense of social responsibility" as required under Section 4(2)(c) of the Act the Courts have rejected those challenges on the basis that the wider obligation to achieve success has required these difficult decisions to be taken.

New Zealand Post does however take its social responsibilities seriously. These are recorded in the Deed of Understanding referred to above. I have attached a copy of that Deed and of the State Owned Enterprises Act to this submission for your information. We believe that our continued success will be built around service, price and product innovation.

Q.3 The Legislative Change Process

The third question which you have posed accurately describes the environment in which the State Enterprise reforms were introduced as being "a crisis atmosphere". That does not understate the position. The New Zealand economy was performing poorly. There was high inflation. Productivity was low and living standards had declined. The need for radical reform was understood by most of the population. It is probably not too sensational to say that the economy either needed to be radically reformed or it faced collapse. It is true that this environment made it easier for New Zealand Post to communicate the need for change - which is perhaps an ingredient in successful labour reform. However, having said that, it is appropriate to acknowledge that the politicians in Government at that time were prepared to take risks to achieve radical reform greater than any which has been introduced in New Zealand since the Second World War.

Much of the credit for the improvement in the performance of State sector trading enterprises and of the New Zealand economy as a whole must be attributed to those political leaders. New Zealand Post was established with a legislative framework which enabled (indeed dictated) success.

However, I do feel confident in saying that the State Enterprise model upon which New Zealand Post is based, whether fortuitously or by grand design, is particular well suited to achieving the aims of structural reform. Crisis produced the model, but we can all adopt the model.

Q.4 Board

As you recognise in your fourth question leadership is a critical factor in achieving corporate change. The Board of New Zealand Post has played a central role in providing that leadership. They are not an honorary board. They carry exactly the same responsibilities as are faced by the directors of other companies. Given the responsibilities placed on them they are remunerated for their services. We have no difficulty with this.

- 5 -

It is critically important that we have as Board members people with a broad commercial experience. We will not attract appropriately qualified people if we cannot pay them for their services. Remuneration levels are broadly comparable to private sector rates. Incidentally, no executives sit on the Board as Directors. All Directors are part-time - that is they come together only for Board or Committee meetings.

I trust that the above answers the questions you have posed. If you would like any further information or if you, or any member of your Sub-committee wish to discuss any of these issues please do not hesitate to contact me. I would be very pleased to receive a commission to provide resources to work in more detail or in a consultancy mode with your advisors.

I have sent a copy of these papers to Mr Marvin Runyon.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Elmar Toime', written in a cursive style.

Elmar Toime
CHIEF EXECUTIVE

cc: Mr Marvin Runyon

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