



# Testimony

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The Postal Service  
Committee on Government Reform  
House of Representatives

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## U.S. POSTAL SERVICE

# Sustained Attention to Challenges Remains Critical

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# U.S. Postal Service: Sustained Attention to Challenges Remains Critical

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The Postal Service faces an uncertain future. Although the Service has slightly improved its overnight First-Class Mail delivery performance this year, improved productivity, and implemented cost-cutting measures, it has encountered increasing financial difficulties as mail volumes have grown more slowly than expected and as postal costs have been difficult to restrain. The Service has reported that it faces significant threats from electronic substitution and is planning for declining mail volumes, especially in First-Class Mail, in the coming years. Although it is difficult to predict the timing and magnitude of further mail volume diversion and potential financial consequences, the Service states that it is working to address this challenge by aggressive cost-cutting to achieve breakthrough productivity and by new revenue generation.

A key oversight issue for the Service, Congress, and the American people is whether the Service is heading for financial shortfalls that could, in the long run, hinder its ability to carry out its mission of providing affordable, universal postal services that bind the nation together. Key questions facing the Service in the long term include the following:

- Can the Postal Service maintain and, where necessary, improve on the quality of mail delivery service?
- Can the Service continue to provide affordable postal rates?
- Can the Service remain self-supporting through postal revenues?
- Can the Service continue in the long term to provide the current level and scope of universal postal service?

Several continuing challenges facing the Service include improving productivity, controlling costs, enhancing revenues, and improving labor-management relations. Long-term increases in productivity will be essential for the Service's future success. The Service recently reported to us that its productivity for fiscal year 2000 through mid-August had increased 2.2 percent. Although this would be the largest increase since 1993, it would translate into a cumulative increase of only 1.5 percent over the past decade. Questions for continued oversight include how and when the Service expects to achieve breakthrough productivity. Another issue is whether the Service, unions, and management associations will be able to find common ground to address long-standing problems in the workplace that may impede the Service's ability to improve its productivity.

GAO also has continued concern about the quality and transparency of the Service's performance information. GAO's recent reports contain specific recommendations for further improvements in this area.

# U.S. Postal Service: Sustained Attention to Challenges Remains Critical

Mr. Chairman and Members of the Subcommittee:

We are pleased to be here today to participate in the Subcommittee's oversight hearing on the U.S. Postal Service (the Service). In my testimony, I shall briefly discuss the Service's overall performance during the past year as well as the challenges that persist as mail volume growth continues to slow and competition from the private sector increases. The Service provided us with updated performance information that is included in this statement. Also, I will discuss work that we have completed over the past year and provide information on our ongoing work. A list of our reports and testimonies related to postal matters issued since October 1999 is included in the attachment to this statement.

## The Service's Performance and Future Challenges

The Service has slightly improved its overnight First-Class Mail delivery performance this year, improved productivity, and implemented cost-cutting measures. However, the Service has encountered increasing financial difficulties as mail volumes have grown more slowly than expected and as postal costs have been difficult to restrain.

Moreover, the Service faces an uncertain future, in view of its expectation that mail volumes will decline in the coming years. A key oversight issue for the Service, Congress, and the American people is whether the Service is heading for financial shortfalls that could, in the long run, hinder its ability to carry out its mission of providing affordable, universal postal services that bind the nation together. Key questions facing the Service in the long term include the following:

- Can the Service maintain and, where necessary, improve on the quality of mail delivery service?
- Can the Service continue to provide affordable postal rates?
- Can the Service remain self-supporting through postal revenues?
- Can the Service continue in the long term to provide the current level and scope of universal postal service?

The Service's recently approved 5-Year Strategic Plan for Fiscal Years 2001 through 2005 stated that the changes in competition challenge the Service's traditional mission and raise questions about its public service obligations that do not have easy answers. The Postmaster General recently said that the Service is at a crossroads with regard to its ability to continue to provide affordable universal service. Earlier this month, the Chairman of the Postal Rate Commission (PRC) also raised the possibility that the nature of universal postal service, specifically delivery to every address 6 days each week, may need to be reconsidered at some point if

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competition leads to large declines in the Service's mail volume. Other stakeholders have also raised concerns about the potential effect of competition on universal postal service. In my testimony, I will provide an update on the Service's recent accomplishments, key trends affecting the Service, and how the Service plans to respond to the formidable challenges it is facing.

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**The Service's Delivery Performance and Customer Satisfaction**

Over the past fiscal year, the Service has slightly improved its overnight First-Class Mail delivery service performance. In its fiscal year 2000 performance plan, the Service established targets of 93 percent on-time delivery of overnight First-Class Mail. The Service reported that it delivered about 94 percent of overnight First-Class Mail on time in the first 3 quarters of fiscal year 2000. If this performance were sustained for the fourth quarter, it would represent a record level of annual performance since the Service began its current measures in the early 1990s. The Service also established a target of on-time delivery for 2/3-day First-Class Mail—which accounts for more than half of First-Class Mail volume—of at least 87 percent, with at least 1-percent improvement over the previous fiscal year. For the first 3 quarters of fiscal year 2000, the Service reported that on-time performance for 2/3-day First-Class Mail was about 85 percent, compared with about 86 percent for all 4 quarters of fiscal year 1999.

In addition, the Service recently reported that 92 percent of residential customers surveyed by the Gallup Organization rated its overall service as excellent, very good, or good, including 29 percent who rated their overall service as excellent, 42 percent as very good, and 21 percent as good.

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**The Service Faces an Uncertain Future**

We testified last year before this Subcommittee that the Service may be nearing the end of an era as it faces growing challenges from competition, notably from private delivery companies and electronic communications alternatives such as the Internet. The Service and some stakeholders agree that growth in the Service's core business of delivering First-Class Mail has already been affected by the rapid growth of the Internet, electronic communications, and electronic commerce. Service officials expect that competition will lead to declines in First-Class Mail volume in the next decade and a consequent loss of revenues.

The Service achieved its best ever financial and service performance over the past 5 years. However, according to the Postmaster General, the Service has encountered increasing difficulties in meeting this year's goal of \$100 million in net income. The Service recognizes that it faces challenges from a dynamic and versatile marketplace, changing customer

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demands, and more alternative delivery options that provide greater choices for customers.

As an example of trends that have affected the Service's mail volumes, at the federal level, government agencies are mandated to move as quickly as possible to reduce paperwork and to adopt electronic billing and payment. Of the 880 million Social Security checks, tax refunds, and other payments sent by the Department of the Treasury in fiscal year 1999, 68 percent were sent electronically rather than mailed. According to the Service, this resulted in \$180 million in lost First-Class Mail revenue. Further, according to a postal operations survey conducted by the American Bankers Association, the banking industry reduced its mail volume in 1999 by almost 18 percent compared with its 1996 level.

In fiscal year 2000, the Service's total mail volume has grown by 2.7 percent through accounting period 12 (August 11, 2000) compared to the same period in fiscal year 1999, which has been less than the 3.8 percent called for in the Service's Integrated Financial Plan for fiscal year 2000. This difference has contributed to a shortfall in the Service's revenues compared with what it had originally budgeted for, and thus made it more difficult for the Service to achieve its target of \$100 million in net income for fiscal year 2000. Earlier this month, the Deputy Postmaster General testified before Congress that it is unprecedented for mail volume to grow at such a slow rate given the strong growth in the general economy, which has been associated with faster mail volume growth in the past.

As figure 1 shows, for fiscal year 2000 through accounting period 12, the Service's mail volume growth rate had not reached its projected growth rate for fiscal year 2000<sup>1</sup>—which ended on September 8, 2000—for its major mail categories:

- First-Class Mail volume increased at a 1.3- percent rate in fiscal year 2000 through accounting period 12, compared with the same period in fiscal year 1999. The Service had projected a 2.5 percent growth rate for First-Class Mail in its Integrated Financial Plan for Fiscal Year 2000.
- Standard A (primarily advertising) mail volume increased by 4.9 percent during this period, which was somewhat less than the 5.7 percent rate projected for the full year.

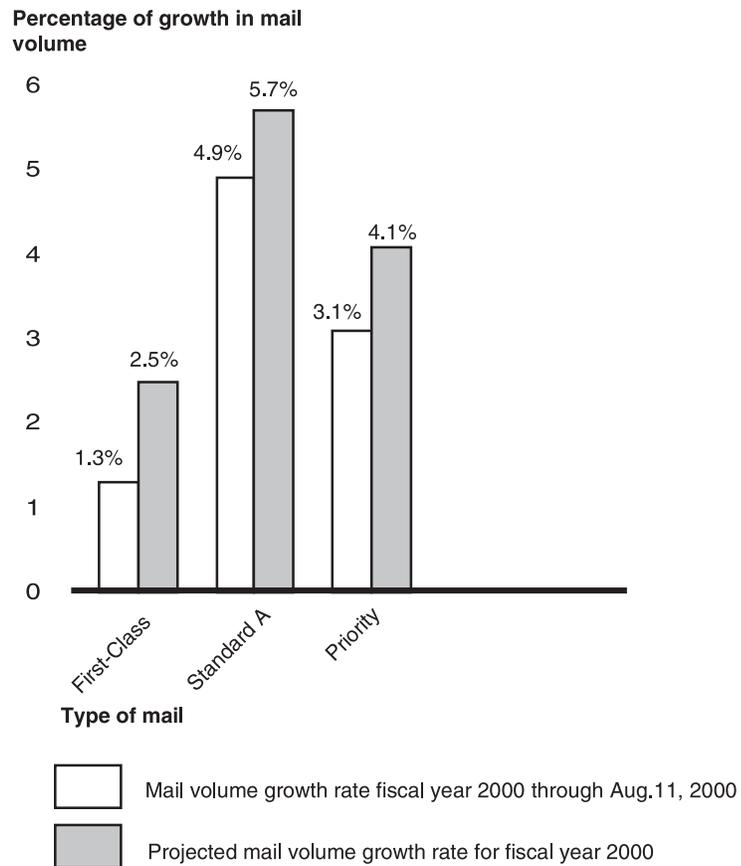
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<sup>1</sup> The dates that Service fiscal years end vary by year and conform to the Service's 13-period accounting year. Accounting period 12 ended on Aug. 11, 2000, and accounting period 13 ended on Sept. 8, 2000.

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- Priority mail volume increased by 3.1 percent during fiscal year 2000 through accounting period 12. The Service's plan had projected a 4.1 percent increase for fiscal year 2000.

**Figure 1: Fiscal Year 2000 Mail Volume Growth Rate Has Been Less Than Projected**

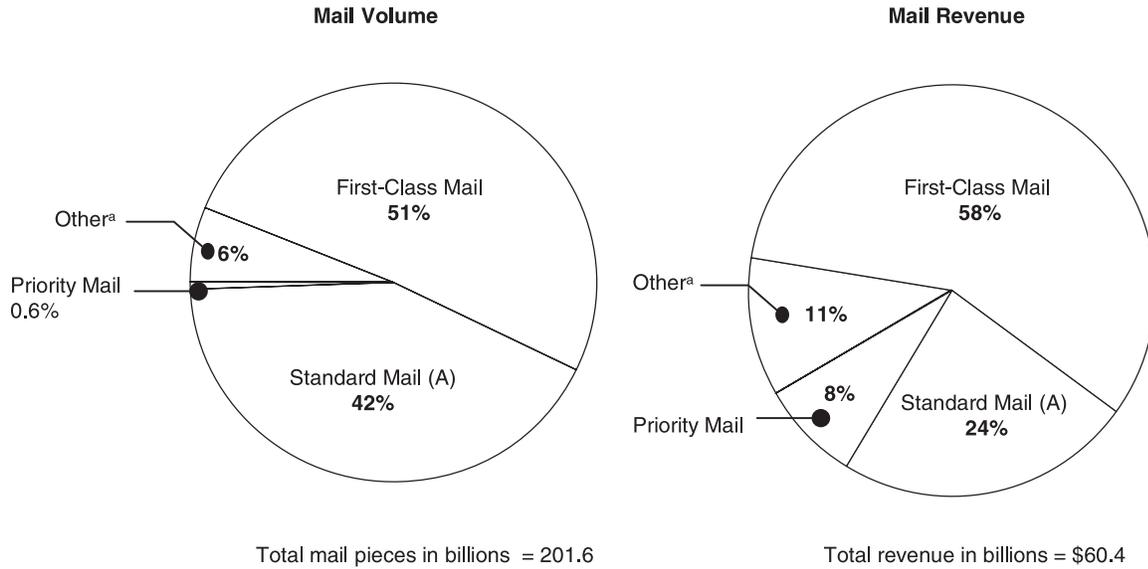


Source: Postal Service Financial and Operating Statements, fiscal year 2000 through accounting period 12 (August 11, 2000), and Fiscal Year 2000 Integrated Financial Plan.

To put these results into context, First-Class Mail, Standard A mail, and Priority mail accounted for the vast majority of the Service's total mail volume, total revenues, and total contribution to pay for institutional costs (see figures 2 and 3).

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**Figure 2: Composition of Service Mail Volume and Corresponding Revenues, Fiscal Year 1999**



Note 1: International mail revenue includes foreign postal transaction revenue.

Note 2: Percentages may not add to 100 due to rounding.

<sup>a</sup>Other includes Express Mail, periodicals, international mail, Standard mail (B), U.S. Postal Service mail, free mail for the blind and handicapped, and mailgrams.

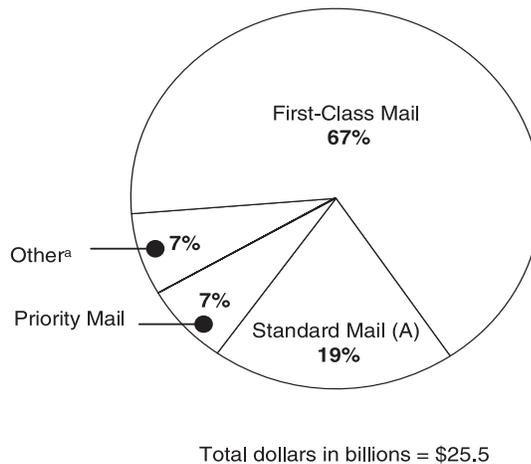
Source: Service's 1999 Annual Report.

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**Figure 3: Net Contribution to Overhead, Fiscal Year 1999**



Note: Percentages may not add to 100 due to rounding.

<sup>a</sup>Other includes Express Mail, periodicals, international mail, standard mail (B), U.S. Postal Service mail, free mail for the blind and handicapped, and mailgrams.

Source: Service documents, fiscal year 1999.

Looking ahead, the Service's 5-Year Strategic Plan for Fiscal Years 2001 through 2005 stated that the substitution effect from new technology on the Service's mail volume is expected to have a significant impact on contribution (or margin). The Strategic Plan reported that the expected declines are likely to be in the categories of mail that the Service handles most efficiently—First-Class bills and payments.

The Strategic Plan stated that for the first time, the Service has adopted a planning assumption that the long-term close relationship between the growth of the economy and mail volume will change in the future, leading to declining mail volumes for First-Class Mail and eventually even Standard A mail. The Service's assumption for its baseline scenario is based on its expectation of "moderate diversion" of First-Class Mail to substitutes such as Electronic Bill Presentment and Payment and e-mail. The baseline scenario presented in the Service's Strategic Plan is somewhat more pessimistic than the baseline scenario that the Service reported to us last year and that was included in our testimony before your Subcommittee. The current baseline scenario calls for total mail volume to increase less, start to decline 1 year sooner, and to decline to a greater extent than last year's baseline scenario.

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However, the Service is also considering the possibility that mail volume may decline even sooner and faster than it does in its revised baseline scenario. The Strategic Plan reported that most external experts suggest a “rapid diversion scenario” where diversion would occur more rapidly, and also impact Standard A mail volumes as interactive Internet advertising reduces traditional targeted advertising mail and catalogs.

The Strategic Plan noted that, like many organizations, the Service was unable to predict the speed at which the Internet has changed the American economy. The Strategic Plan stated that there is broad agreement that the Service will face significant threats from electronic substitution, and that mail volumes, especially in First-Class Mail, are likely to decline in the near future. However, as the plan recognized, there is considerable uncertainty about the timing and rate of diversion, as well as whether the Service can or should do anything about it.

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## The Implications of Mail Volume Trends for the Service

Although it is difficult to predict the timing and magnitude of further mail volume diversion and potential financial consequence, the Service has begun to plan how it would address a range of such scenarios. The Service’s Acting Chief Financial Officer told us that because of the uncertainty concerning future mail volume trends, the Service considers it prudent to develop a range of scenarios and do contingency planning for them. He told us that it takes time for an organization as large and as complex as the Service to plan and prepare for the major operational changes that would likely be necessary in the event of substantial declines in the Service’s mail volume. He also noted that the Vice-Chairman of the Service’s Board of Governors said earlier this month that because the Service does not know how fast or how much the Internet will change the Service’s business model, the stakes are high and the Service cannot wait to be certain before it acts.

The Service’s basic strategy is a combination of aggressive cost-cutting and new revenue generation. The Service’s Strategic Plan stated that the Service expects that if electronic diversion does not shift into high gear, leading to more rapid volume decline, then it can sustain its viability over the next 5 years by dramatically cutting costs and seeking new revenue sources within the current regulatory structure. However, the Strategic Plan noted that if postal markets change over the next 5 years faster than currently anticipated, postal management and stakeholders will need to address a number of issues, including

- the definition of universal postal service,
- the potential realignment of service standards, and

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- the configuration of current operations and infrastructure.

The Strategic Plan warned that historic increases in productivity and aggressive management of the size of the Service workforce already are anticipated. Therefore, according to the Strategic Plan, if the volume decline is as drastic as some experts have forecast, especially in critical mail categories currently carrying the burden of contribution to institutional overhead, postal rates are likely to increase dramatically for the remaining mail volume. Further, other categories of mail would also be affected. Although the Strategic Plan noted that any prediction of the impact of mail volume 5 years in advance is almost certain to be flawed, the Service anticipates the need for a “structural transformation” that is to include, among other things, achieving “breakthrough productivity.”

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## Recent Productivity Changes and the Challenge of Achieving Breakthrough Productivity

The Service reported to us that the increase in its overall productivity for fiscal year 2000 through accounting period 12, as measured by Total Factor Productivity (TFP), was 2.2 percent.<sup>2</sup> If this increase were sustained for the full fiscal year, it would represent the fifth-largest annual increase in postal productivity since 1970, and the largest increase since fiscal year 1993. Nonetheless, since postal productivity declined in 5 of the last 6 fiscal years (from 1994 through 1999), a 2.2 percent productivity increase in fiscal year 2000 would translate into a cumulative productivity increase of only 1.5 percent from fiscal year 1990 to fiscal year 2000. Further, postal productivity would thereby increase by only 12.2 percent since 1970—despite the vast changes in postal automation and postal operations that have occurred in the past 3 decades.

In addition, a 2.2-percent increase in postal productivity would be less than the 3.1-percent increase that was incorporated into the Service’s Performance Plan for Fiscal Year 2000. The Service told us on September 7, 2000, that “Because of the Postal Service’s financial and operational success in FY 1999, the actual productivity improvement estimated to be required to achieve its FY 2000 net income plan of \$100 million was revised to 2.1 percent.” However, it is unclear whether such a productivity improvement would be sufficient for the Service to meet its net income goal. As reported in the press, the Postmaster General said at the end of August that the Service could record a deficit up to \$300 million for fiscal year 2000.

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<sup>2</sup> TFP measures the changes in the relationship between the Service’s outputs and resources expended in producing those outputs. The Service’s main outputs are mail volumes and servicing an expanding delivery network. By tracking outputs and resource usage, TFP provides a measure of historical performance.

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As the Service and key stakeholders have recognized, long-term increases in its productivity will be essential to its future success. For example, the Mailers Council, a coalition of mailers and mailing associations, reported this March that increasing competition, operating and cost management constraints—some imposed by outside entities—as well as the consequences of management decisions, have influenced a decline in the Service’s productivity in past years.<sup>3</sup> The report stated that: “As a result of these factors, at a time when every competing technology is becoming less expensive, the cost of using the nation’s mail system is becoming more expensive. To ensure the Service’s survival, therefore, the Mailers Council believes postal management must focus its considerable skills and resources on those factors it can control, and thereby generate needed productivity gains.” The report noted the need for the Service to reduce its costs and become more efficient to achieve productivity gains.

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## The Challenge of Maintaining Financial Viability

As we testified last year, the Service’s ability to maintain financial viability by controlling costs, improving productivity, and enhancing revenues presents a continuing challenge. We have reported that the Service’s continued success will depend heavily on its ability to control operating costs, and that the Service has recognized that it needs aggressive cost management to avoid unwarranted costs. The Service has made some progress this year in controlling costs through reducing the number of workhours. For fiscal year 2000 through accounting period 12, the Service reported it had reduced the total number of workhours compared to the same period in fiscal year 1999 while, at the same time, increasing the number of delivery points in the postal network.

In his March 20, 2000, speech at the National Postal Forum, the Postmaster General said that the Service intends to reduce expenses by at least \$4 billion by 2004. He estimated that about \$700 million a year would come from “breakthrough productivity” in the mail processing system, while about \$100 million annually would come from overhead reductions, about \$100 million annually from reducing transportation costs, and about \$100 million annually from more efficient paperwork and purchasing. However, on August 11, 2000, the Service told the PRC that: “The amounts from the PMG’s speech represented an aggressive challenge to the organization rather than a blueprint for specific cost savings.” The Service said that it expected to achieve only \$744 million in cost savings in the “test year” (i.e., the year after the proposed rate increase would go into effect), largely because it expected to achieve only \$466 million of the called-for \$700 million in cost savings in mail processing and other operations. The

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<sup>3</sup> Postal Service Productivity: Real Improvements Needed Now, Mailers Council, Mar. 8, 2000.

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Service said that it “recognizes the difficulty in achieving the aggressive cost reductions in fiscal year 2001, the first year of the Breakthrough Productivity Initiative.” Given this response, questions for continued oversight include the following:

- What does the Service consider to be breakthrough productivity?
- How does the Service expect to achieve breakthrough productivity?
- When does the Service expect to achieve breakthrough productivity?

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**Continuing Disagreements  
in Labor-Management  
Relations**

We continue to believe that the Service and its major postal labor unions and management associations need to focus on common approaches for addressing persistent labor-management relations problems, thereby improving the Service’s work environment and helping it maintain its competitive position. The August 2000 Report of the Postal Service Commission On A Safe and Secure Workplace noted that “A sea change in attitudes of all of the parties—and an environment of trust—will be required to slash the number of grievances and reshape compensation systems. This will require a sustained effort.” The report said that in order to eliminate sources of friction, postal management, unions, and management associations must work together.

Further, the report noted that the Service had an enormous backlog of more than 126,000 grievances, and that more than 6,300 grievances were arbitrated in fiscal year 1999. By way of comparison, in the entire automobile industry, with about 400,000 bargaining employees, only 11 grievances reached arbitration in 1998, according to the report. Several federal agencies contacted by the Commission also reported only a few arbitrations a year. Further, the report said that the Service has procedures similar to some other organizations that do not have such unusually large numbers of complaints. The report said that the annual cost of postal grievances was recently estimated at \$217 million, with a small industry of more than 300 arbitrators handling postal cases. At the same time, the report recognized that many grievances in the backlog are related issues grieved separately, such as 40,000 grievances filed by the American Postal Workers Union in a dispute over wash-up time in the New York district.

The Service reported to us that, as of the end of fiscal year 1999, out of about 708,000 bargaining unit employees, about 114,000 grievances were awaiting arbitration at the regional level, up slightly from 112,000 a year ago. However, the Service also reported that about 97,000 grievances had

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been appealed to step 3<sup>4</sup>, down from about 112,000 a year ago. In addition, the Service's General Counsel told us that the Service's Resolving Employee Disputes, Reaching Equitable Solutions Swiftly (REDRESS) program had helped to reduce the number of Equal Employment Opportunity (EEO) complaints, reversing the past trend toward more EEO complaints.

Although any progress in this area is encouraging, we are concerned that continuing disagreements in labor-management relations may impede efforts to achieve improvements in postal productivity. As some stakeholders have noted, keeping the Service financially viable while maintaining the level and scope of universal postal service is expected to become increasingly difficult. A recognition that similar survival issues were at stake helped lead to major improvements in labor-management relations in the auto industry. Thus, a key question for oversight is whether the Service, its labor unions, and its management associations share the same sense of urgency in improving labor-management relations and finding common ground to address long-standing problems in the workplace.

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### The Need for Complete and Reliable Information on Postal Performance

In another key area for congressional oversight, we believe that complete and reliable performance data will be essential for the Service, Congress, and stakeholders to monitor the Service's progress towards meeting its goals. The Service has recognized the need for more accurate and complete information on postal performance. In its Strategic Plan, the Service stated that it will invest in a new "Information Infrastructure" to achieve three goals: streamline interaction with customers; provide more timely, accurate, and relevant information to effectively manage operations and reduce costs, improve service performance and sustain quality; and provide more timely, accurate, and relevant information to allocate costs and improve productivity. The Service said that it plans to spend about \$2 billion on various information systems over the next 5 years and to develop an "Information Platform" to help it manage its resources more effectively and efficiently.

While we encourage the Service to continue its efforts to improve its performance information, we remain concerned about the quality and transparency of the Service's performance information. We have reported on, and are continuing to monitor, opportunities for improvement in the Service's performance information. Specifically:

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<sup>4</sup> Step 3 grievances are grievances that have been appealed by the unions to the area level because they could not be resolved at the plant or district levels.

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- In our testimony last year before this Subcommittee, we highlighted the need for the Service to take action to address long-standing issues related to the quality of data used in ratemaking and recommended that the Postmaster General report to congressional oversight subcommittees on the actions taken and planned in this area.<sup>5</sup> The Service pledged to periodically report on progress in implementing the recommendations of a study that was initiated by your Subcommittee on the quality of data used by the Service in setting rates. In its latest report to your Subcommittee in July 2000, the Service documented actions taken and planned to improve the quality of rate-setting data. The report also contained much useful information on the status of each of the outstanding recommendations as well as the resources devoted to improving data quality.
  - Our recent report on the Service's e-commerce initiatives found deficiencies in the financial information the Service provided for the e-commerce activities that raised concerns about the accuracy and completeness of the financial reporting for e-commerce activities.<sup>6</sup> We do not believe the e-commerce financial data that the Service provided was sufficiently complete and reliable to be used to assess its progress toward meeting its overall financial performance expectation, which is that revenues generated by e-commerce products and services in the aggregate are to cover the Service's direct and indirect costs as well as make a contribution to overhead. The Service agreed with our recommendation that it provide complete and accurate information on costs and revenues for the financial data on e-commerce initiatives and said it is instituting a standard financial reporting procedure in this area. Actions the Service has reported taking are important and need to be effectively implemented.
  - On November 6, 1998, the Service reported to your Subcommittee that: "We recognize the need to provide our customers with specific measures of delivery performance for all our products and services." The Service said it intended to use a phased approach to develop measures as soon as possible for products such as Periodicals. However, the Service's 5-Year Strategic Plan for fiscal years 2001 through 2005, which was approved by the Board last month, stated that "Currently, an internal system is used to measure delivery within requested windows for only a small portion of Standard A and Periodicals mail. The need to build a better indicator is clearly necessary if we are to satisfy the need of our advertising and

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<sup>5</sup> U.S. Postal Service: Challenges to Sustaining Performance Improvements Remain Formidable on the Brink of the 21<sup>st</sup> Century (GAO/T-GGD-00-2, Oct. 21, 1999).

<sup>6</sup> U.S. Postal Service: Postal Activities and Laws Related to Electronic Commerce (GAO/GGD-00-188, Sept. 7, 2000).

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periodical customers in the future . . . . Over the next several years, technology will enable the USPS to develop service performance measurement systems for all major categories of mail and for any new services introduced to the market.” Thus, the Service has recognized the need for improvement in its performance measures for mail delivery but this task will remain incomplete for some time to come. As we reported in January 1999, it will be important for the Service to develop results-oriented measures for its critical functions and program areas, as intended by the Government Performance and Results Act of 1993 (GPRA).<sup>7</sup>

In addition, we are releasing today our report that discusses the Service’s fiscal year 1999 performance report and the fiscal year 2001 preliminary performance plan that are required under GPRA. In our report we identified some positive aspects, however, we are concerned that the Service’s performance plans and performance reports may not have been as useful to Congress, postal managers, and others as they could have been. As we reported, we believe that in preparing future performance plans and performance reports, the Service needs to focus more acutely on providing and presenting information that is clear and understandable. Accordingly, we made recommendations for improvements so that interested parties would be able to more easily determine how well the Service is improving performance and achieving its goals, as intended by GPRA.

Although we recognize that this was the first year that the Service published a performance report, we have some concerns regarding the way information was presented. For example, we believe it was misleading for the Service’s fiscal year 1999 performance report to highlight that the Service exceeded its targets for overnight and 2/3 day on-time deliveries, particularly when there was not an accompanying acknowledgement that less than a full year’s performance was used in making that determination. The Service’s fiscal year 1999 performance plan established 93 and 87 percent targets for on-time delivery for overnight and 2/3 day First-Class Mail, respectively; and portrayed these as annual targets. When all 4 quarters of fiscal year 1999 performance data were aggregated, the Service met, but did not exceed, its goal of 93 percent on-time delivery of overnight First-Class Mail. It also delivered 86 percent of the 2/3-day First-Class Mail on time—1 percentage point less than the established target of 87 percent. The Service’s performance for all 4 quarters of fiscal year 1999 either met, or came close to meeting the established targets. Therefore, we question why the Service chose to

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<sup>7</sup> Major Management Challenges and Program Risks: U.S. Postal Service (GAO/OCG-99-21, Jan. 1999).

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highlight information that did not include performance for the full fiscal year, including its performance during its heaviest volume period—the holiday mailing season.

We also assessed the Service's fiscal year 2001 preliminary performance plan. Some of the positive aspects of this plan included additional performance indicators and targets for selected subgoals, such as targets for (1) overall customer satisfaction (residential and business); (2) resolving employee complaints (Resolving Employee Disputes, Reaching Equitable Solutions Swiftly--REDRESS); and (3) the Voice of the Employee survey—which is the vehicle used by the Service to improve its understanding of employee issues and concerns. However, several subgoals, indicators, and targets that were included in the Service's fiscal year 2000 performance plan were dropped from the fiscal year 2001 preliminary performance plan. Dropped subgoals included (1) keeping price increases at or below the rate of inflation, (2) controlling costs by achieving productivity gains, and (3) restoring equity. The preliminary performance plan did not fully explain why these three subgoals, indicators, and targets were dropped. In May 2000, the Board of Governors stated that it had decided to restore Total Factor Productivity as a national-level results indicator. However, if the Service does not set a goal concerning price increases, it will be more difficult to hold the Service accountable for its performance in this area.

Our report makes recommendations to the Postmaster General regarding specific opportunities for improvement concerning both the Service's fiscal year 2001 preliminary performance plan and its fiscal year 1999 performance report. In commenting on our draft report, the Service generally agreed with the facts and said it planned to implement the report's recommendations.

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## **Our Work Related to Other Postal Issues**

I would now like to provide you with a brief summary of work we have completed on other postal issues since the fall of 1999. This work resulted in reports and/or testimony on (1) the Service's electronic commerce activities, (2) diversity in the Service, (3) the Breast Cancer Research Semipostal Stamp, (4) acceptance controls for business mail, and (5) the Department of State's implementation of its international postal responsibilities. In addition, we have ongoing work related to supervisory pay differentials.

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## Electronic Commerce

On September 7, 2000, we testified<sup>8</sup> and issued a report<sup>9</sup> on the Service's electronic commerce initiatives. We reported that the Service is in the early stages of implementing an electronic commerce (e-commerce) program. It has taken steps this year to develop and implement e-commerce activities, including developing a definition of its e-commerce initiatives, identifying e-commerce and related initiatives, and establishing a process for approving these initiatives. The Service identified seven e-commerce initiatives involving products and services meant to facilitate the movement of messages, merchandise, and money in ways that require the use of the Internet and generate revenues for the Service. The Service also outlined overall e-commerce goals and strategies and developed some performance targets for its e-commerce initiatives. However, we identified three problem areas relating to the Service's management of its e-commerce area:

- inconsistencies in identifying e-commerce and related initiatives and in reporting the status of these activities that made it difficult for us to ensure we had a complete and accurate picture of the Service's e-commerce activities;
- inconsistencies in following the required process for reviewing and approving its e-commerce initiatives, which raised questions as to whether the initiatives were appropriately planned and reviewed; and
- deficiencies in the financial information the Service provided for the e-commerce activities that raised concerns about the accuracy and completeness of the financial reporting for e-commerce activities.

To help ensure more effective management and oversight of the Service's e-commerce activities, we recommended that the Postmaster General (1) take appropriate actions to help ensure that e-commerce and related initiatives are appropriately identified and maintain accurate and complete information related to the status of these initiatives; (2) follow processes and controls that have been established for developing and approving e-commerce initiatives; and (3) provide complete and accurate information on costs and revenues for the financial data on e-commerce initiatives. The Service endorsed our recommendations and reported that it is taking action to implement them.

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<sup>8</sup> U.S. Postal Service: *Electronic Commerce Activities and Legal Matters* (GAO/T-GGD-00-195, Sept. 7, 2000).

<sup>9</sup>GAO/GGD-00-188.

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In the legal area, the Service provided its views on how various laws and regulations apply to its e-commerce activities. The Service said that its unique status as an independent establishment of the executive branch gives it broad legal authority and discretion to offer e-commerce products and services in ways that the Service finds appropriate to its assigned functions and in the public interest. The Service, some competitors, and others have conflicting views on the extent of the Service's legal authority to offer e-commerce products and services and under what circumstances it should offer such services.

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## Diversity

During the past year, we issued two reports to Congressman Chaka Fattah, the Subcommittee's Ranking Minority Member, concerning employee diversity and Equal Employment Opportunity (EEO) issues. Specifically, we issued a report in March 2000, on the representation of women and minorities in the Postal Career Executive Service (PCES),<sup>10</sup> and in June 2000, a report on diversity in district management-level positions.<sup>11</sup>

In our March 2000 report, we provided information on the representation of women and minorities in PCES, which includes officers and executives. Among other things, we determined that at the end of fiscal year 1999, women and minorities represented about 35 percent of the PCES executive workforce compared to their representation of about 58 percent in the Service's overall workforce. We also found that women and minority representation among the Service's PCES executive workforce was about 35 percent compared with about 32 percent in the federal government's career Senior Executive Service (SES), excluding the Department of Defense (DOD).

The Service reported that it had various efforts under way or planned that related to increasing diversity among its PCES executives. For example, in November 1998, the Service required that its PCES merit performance evaluation process address diversity-related activities in individual executive performance objectives and that executives be accountable for the accomplishment of those objectives. The Service also reported that it had developed management training programs to help employees better manage their careers, and had established a diversity oversight group to oversee corporate diversity initiatives.

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<sup>10</sup> U.S. Postal Service: Diversity in the Postal Career Executive Service (GAO/GGD-00-76, Mar. 30, 2000).

<sup>11</sup> U.S. Postal Service: Diversity in District Management-Level Positions (GAO/GGD-00-142, June 30, 2000).

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Our June 2000 report focused on diversity among 83 postal districts located throughout the United States.<sup>12</sup> More specifically, it provided information on the representation of women and minorities (in the Service's districts) in levels 16 through 26 of the Service's Executive and Administrative Schedule (EAS).<sup>13</sup> The report also provided more detailed information on the representation of women and minorities in EAS levels 16 through 26 for the Chicago, IL, and Akron, OH, postal districts; initiatives implemented to promote diversity; and lessons identified by district officials that related to increasing diversity in those two districts.

At the end of fiscal year 1999, women and minorities in the Service's districts represented a district average of about 49 percent of the EAS 16 through 26 workforce compared with their average representation of about 56 percent across all district workforces (excluding EAS levels 16 through 26). Women and minority representation in EAS levels 16 through 26 in the Service's 83 districts ranged from a low of about 22 percent in the Middlesex-Central district office to a high of 95 percent in the Los Angeles district office. Concerning the representation of women and minorities in the Chicago and Akron district offices, at the end of fiscal year 1999, in Chicago, women and minorities represented about 93 percent of the EAS 16 through 26 workforce compared with their overall workforce representation of 92 percent. In Akron, for this period, women and minorities represented about 41 percent of the district's EAS 16 through 26 workforce compared with their overall workforce representation of about 46 percent.

Both districts implemented several diversity-related initiatives, such as various training programs, including national programs to increase the representation of women and minorities in EAS levels 16 through 26. In addition, to improve other aspects of diversity, both districts were using REDRESS (Resolve Employment Disputes, Reach Equitable Solutions Swiftly), a national alternative dispute resolution program, to facilitate discussion between managers and employees on individual EEO complaint issues. Locally, Chicago and Akron officials had also developed their own individual initiatives and had identified several lessons related to increasing diversity in their districts' EAS 16 through 26 workforces, which included (1) management must demonstrate its commitment to diversity;

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<sup>12</sup> The Service has 85 districts. We did not include two district offices—San Juan and Honolulu—in our report because they were missing significant amounts of data on sex and /or race/ethnic origin.

<sup>13</sup> The EAS workforce consists primarily of employees in EAS levels 11 through 26 positions. EAS management-level positions generally start at EAS 16 and include such positions as postmaster, manager of customer services, and manager of postal operations.

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(2) training and career development programs must be made available to provide opportunities for women and minorities to ascend to supervisory and management-level positions; and (3) an environment that encourages communications and cultural appreciation between management and employees must be established.

Regarding the alleged EEO concerns at the Youngstown, OH, postal site, although the number of EEO complaints had increased between fiscal years 1997 and 1999, it was not clear whether the complaints stemmed from alleged discrimination, lack of communications, or labor/management problems. District records showed that the number of EEO complaints in Youngstown increased in fiscal year 1999. However, as of May 2000, 51 of the 57 complaints filed were closed. Of these, one resulted in a finding of discrimination. According to some district and union officials, EEO complaints in Youngstown were based little, if at all, on discrimination, but rather on poor communications among managers, supervisors, and employees or poor labor/management relations.

In our June 2000 report, we recommended that the Service reassess the EEO situation in Youngstown to determine what the issues were with respect to the workplace environment, such as discrimination, communications, or labor/management relations; and what additional actions need to be taken. The Service concurred with our recommendations and told us that they intended to implement them.

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**Breast Cancer Research Stamp**

In April 2000, we reported on the Service's Breast Cancer Research Semipostal (BCRS) stamp.<sup>14</sup> We also participated in a hearing on the BCRS of the Senate Subcommittee on International Security, Proliferation, and Federal Services, Committee on Governmental Affairs, in May 2000.<sup>15</sup> The Stamp Out Breast Cancer Act of 1997 directed the Postal Service to establish a special stamp—known as a semipostal—to raise money for breast cancer research. The BCRS was to be available for sale through July 28, 2000—2 years from the date it was issued. The BCRS was the first stamp ever issued by the Service to raise money for nonpostal purposes. The BCRS costs 40 cents, and is valid for the 33-cent First-Class postage rate, leaving 7 cents as surcharge revenue. The act provided that the Service was to deduct from the surcharge revenue the reasonable costs it incurred in carrying out the act, including those attributable to the

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<sup>14</sup> Breast Cancer Research Stamp: Millions Raised for Research, but Better Cost Recovery Criteria Needed (GAO/GGD-00-80, Apr. 28, 2000).

<sup>15</sup> Breast Cancer Research Stamp: Millions Raised for Research, but Better Cost Recovery Criteria Needed (GAO/T-GGD-00-137, May 25, 2000).

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printing, sale, and distribution of the BCRS, as determined under regulations it shall prescribe. The Service was to remit the remaining net proceeds from the surcharge revenue to the National Institutes of Health (NIH) and DOD for breast cancer research. Seventy percent of the net proceeds were to go to NIH, with the remaining 30 percent to go to DOD's medical research program.

In reviewing the BCRS, we concluded that it has been an effective fundraiser. It has raised millions of dollars and, at the same time, has been convenient and voluntary. In addition, the public and most of the key stakeholders we spoke with believed it appropriate to use semipostals issued by the Service to raise funds for special, nonpostal purposes.

Throughout our review, however, we were concerned that the Service had not formalized its criteria for determining what costs would be recouped from the surcharge revenue generated by the BCRS. Additionally, we were concerned that the Service was not consistently applying its informal criteria for making such determinations to all costs being tracked. We recommended that the Postmaster General promptly issue regulations that clearly state the Service's criteria for determining which costs are to be recouped from the BCRS surcharge revenue and ensure that the criteria are consistently applied to all costs. In response to that recommendation, the Service recently issued regulations formalizing its criteria for making the required reasonable cost determinations associated with the BCRS.

In July 2000, Congress expressed its satisfaction with the BCRS by sending legislation to the President to extend the BCRS sales period for 2 years and grant the Service the authority to issue semipostals. The President signed that legislation into law on July 28, 2000 (Public Law No. 106-253). As of July 28, 2000, the Service reported that the BCRS had raised about \$15 million for breast cancer research.

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## Acceptance Controls for Business Mail

In November 1999, we reported on Service changes to improve acceptance controls for business mail.<sup>16</sup> We did this work to determine whether the Service had made changes we recommended in 1996 and whether those changes were working.<sup>17</sup>

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<sup>16</sup> U.S. Postal Service: Changes Made to Improve Acceptance Controls for Business Mail (GAO/GGD-00-31, Nov. 9, 1999).

<sup>17</sup> U.S. Postal Service: Stronger Mail Acceptance Controls Could Help Prevent Revenue Losses (GAO/GGD-96-126, June 25, 1996).

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The Service discounts postage rates to customers who barcode and presort their business mail before submitting it in bulk quantities to the Service for acceptance processing. The discounted postage rates compensate customers for performing work that otherwise would have to be done by the Service and recognize the Service's lower cost of processing such mail on automated equipment.

We reported in June 1996 that the Service did not have adequate controls over the acceptance of business mail. The Service could not ensure that customers had properly prepared their business mail and were therefore eligible to receive the discounted postage rates. As a result, the Service did not have reasonable assurance that all significant amounts of revenue due from bulk business mailings were correctly identified and received.

Our follow-up review found that the Service had made changes to its controls over the acceptance of business mail that were generally in line with the recommendations we made in 1996 and that should help prevent revenue losses. For example, the Service (1) developed and implemented a risk-based approach for verifying the eligibility of high-risk customers to receive discounted postage rates and (2) made changes to its presort verification, supervisory review, and documentation requirements to help provide more assurance that these functions are performed.

Notwithstanding these actions, however, we could not determine whether all of the changes were working servicewide because data needed to make such a determination were not available. Further, we found evidence that supervisory reviews of revised business mail acceptance procedures were not always performed at the locations we visited. The Inspection Service also found that required verifications were performed properly at some locations but not at others, and that business mail acceptance-unit employees needed additional training at some locations but not at others. We concluded that there was sufficient evidence that the Service still did not have assurance that supervisory reviews of required mail verifications are performed. In addition, we stated that the Service had not fully addressed our recommendation that it develop information for evaluating the adequacy of its business mail acceptance controls.

We recommended that the Postmaster General direct Service officials to develop and implement approaches for providing reasonable assurance that (1) required supervisory reviews of presort verifications are done and (2) business mail acceptance controls are working as intended to prevent improperly prepared mailings from entering the mail stream at reduced postage rates and to minimize the rework required by the Service to

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correctly process and deliver such mail. In response to our recommendations, the Service told us that it has implemented a service-wide reporting requirement each accounting period on the number of supervisory reviews of presort verifications conducted and developed a number of tools and acceptance control procedures that will allow the Service to help mailers achieve a consistently high level of presort accuracy for their mailings.

While we are encouraged by the Service's ongoing efforts to improve its controls over business mail acceptance, we remain concerned by continuing problems. For example, the Postal Service's Office of the Inspector General (OIG) recently conducted an audit to determine the validity of mailers' concerns about the identification, adjudication, and collection of revenue deficiencies. Among other things, OIG reported that mail acceptance personnel were not fully knowledgeable of overly complex rate standards, and that the Service lacked a comprehensive management information system for the revenue assurance process, reliable revenue deficiency data, and thresholds for assessing deficiencies.

We believe that postal management must, for the foreseeable future, remain vigilant in monitoring and maintaining the controls over all facets of business mail acceptance. As we noted in our November 1999 report, in fiscal year 1998, business mail accounted for 49 percent of the Service's \$58 billion in total mail revenue and 66 percent of the nearly 200 billion mail pieces handled by the Service. Accurately determining and collecting postage for business mail are critical to the overall financial health of the Service.

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## The Department of State's International Postal Responsibilities

In January 2000, we reported on the Department of State's implementation of its international postal responsibilities.<sup>18</sup> Public Law 105-277, enacted October 21, 1998, amended 39 U.S.C. 407 to give the Department of State primary responsibility for the formulation, coordination, and oversight of policy regarding United States' participation in the Universal Postal Union (UPU). The UPU is a specialized agency of the United Nations that governs international postal service. The major changes resulting from the 1998 act that related to the UPU included (1) transferring primary responsibility for U.S. policy regarding the UPU from the Service to the Department of State and (2) requiring the Department of State and the Service to consult with private providers and users of international postal services, the general public, and such federal agencies and other persons

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<sup>18</sup> Postal Issues: The Department of State's Implementation of Its International Postal Responsibilities (GAO/GGD-00-40, Jan. 31, 2000).

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that each considers appropriate in carrying out its respective international postal responsibilities.

In our report, and in subsequent testimony before the Subcommittee,<sup>19</sup> we noted that the Department of State had made progress in implementing its UPU responsibilities by taking steps to consult with the Service, other federal agencies, postal users, private providers of international postal services, and the general public. We also recognized the progress made by State in its first year of responsibility for UPU matters and identified opportunities for the Department to improve its process for developing U.S. policy on these matters and the institutional continuity and expertise of its staff working in this area. We identified some shortcomings relating to the timing and notification for public meetings, and the distribution of documents discussed at these meetings, that may have limited the opportunities for stakeholders to provide meaningful input. We also found that State's policy development process on UPU matters resulted in little public record of agency or stakeholder positions, which could make it difficult for Congress and others to fully understand the basis for U.S. policy positions. Further, staff turnover made it more difficult for State to develop the institutional continuity and expertise to fulfill its leadership responsibilities.

We made recommendations to State that addressed these areas. The Department of State has since reported that it has taken a number of specific actions to address the procedural shortcomings we identified. We agree that the Department of State has improved the timeliness and accessibility of information it provides and its efforts to solicit input from interested stakeholders.

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## Supervisory Pay Differentials

Next, Mr. Chairman, I would like to discuss our ongoing Postal Service work on supervisory pay differentials. At your request, Mr. Chairman, we have begun a review of the complaints, primarily from postmasters, that many of the employees they supervise earn more than they do. Our primary objective is to determine whether any employees earn more than their postmasters do and, if so, why (e.g., overtime, shift differential, etc.). As you know, current Service policy calls for certain postmasters and other postal supervisors to be paid at a higher salary rate than they might otherwise be entitled to if they supervise two or more full-time equivalent craft employees. Because the supervisory pay policy is relevant to the broader concerns addressed in Congresswoman Morella's Bill (H.R. 3842,

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<sup>19</sup> [Postal Issues: The Department of State's International Postal Responsibilities](#) (GAO/T-GGD-00-63, Mar. 9, 2000).

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the “Postmasters Fairness and Rights Act),” we agreed with your office to limit our initial review to postmasters and analyze the pay for other postal supervisors in a subsequent review. Due to the Service payroll system's complexity, size, and lack of documentation, our analysis of postmaster pay has taken longer than anticipated. We have been working with the Service's payroll system officials and expect to resolve these problems shortly and begin our analysis of postmaster pay.

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Mr. Chairman, this concludes my prepared statement. I have included a list of our Postal Service products issued since October 1999 in the attachment. I would be pleased to respond to any questions you or the Members of the Subcommittee may have.

**Contact and Acknowledgments**

For further information regarding this testimony, please contact Bernard L. Ungar, Director of Government Business Operations, on (202) 512-8387. Individuals making key contributions to this testimony included Teresa L. Anderson, Kenneth E. John, Charles F. Wicker, and Hazel J. Bailey.

# GAO Postal-Related Products Issued During Fiscal Year 2000

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U.S. Postal Service: Enhancements Needed In Performance Planning and Reporting (GAO/GGD-00-207, Sept. 19, 2000).

U.S. Postal Service: Electronic Commerce Activities and Legal Matters (GAO/T-GGD-00-195, Sept. 7, 2000).

U.S. Postal Service: Postal Activities and Laws Related to Electronic Commerce (GAO/GGD-00-188, Sept. 7, 2000).

U.S. Postal Service: Diversity in District Management-Level Positions (GAO/GGD-00-142, June 30, 2000).

Breast Cancer Research Stamp: Millions Raised for Research, but Better Cost Recovery Criteria Needed (GAO/T-GGD-00-137, May 25, 2000).

Breast Cancer Research Stamp: Millions Raised, but Better Cost Recovery Criteria Needed (GAO/GGD-00-80, Apr. 28, 2000).

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Postal Issues: The Department of State's International Postal Responsibilities (GAO/T-GGD-00-63, Mar. 9, 2000).

Postal Issues: The Department of State's Implementation of Its International Postal Responsibilities (GAO/GGD-00-40, Jan. 31, 2000).

U.S. Postal Service: Changes Made to Improve Acceptance Controls for Business Mail (GAO/GGD-00-31, Nov. 9, 1999).

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