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U.S. POSTAL SERVICE

Challenges to Sustaining
Improved Performance

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U.S. Postal Service: Challenges to Sustaining Improved Performance

GAO's testimony addresses the challenges that confront Congress and the Postal Service as they consider how to sustain its performance and maintain a competitive role in providing mail service to the American public in the future.

The Postal Service reported that fiscal year 1996 represented the second year in a row that its financial performance was profitable and operational performance improved. The Postal Service's 1996 net income was \$1.6 billion and it delivered 91 percent of overnight mail on time. Additionally, for fiscal year 1996, the Postal Service's volume exceeded 182 billion pieces of mail and generated more than \$56 billion in revenue.

While these results are encouraging, other performance data suggest that some areas warrant closer scrutiny. Last year's delivery of 2-day and 3-day mail—at 80 and 83 percent respectively—did not score as high as overnight delivery. The concern among customers is that the Postal Service's emphasis on overnight delivery is at the expense of 2-day and 3-day mail. Additionally, although its mail volume continues to grow, the Postal Service is concerned that customers increasingly are turning to its competitors or alternative communications methods. In 1996, mail volume increased by about one-half of anticipated increase in volume. Containing costs is another key challenge that GAO has reported on previously. For example, last year's operating expenses increased 4.7 percent compared to a 3.9 percent increase in operating revenues. GAO has also found several weaknesses in the Postal Service's internal controls that contributed to increased costs. The Postal Service's continued success in both financial and operational performance will depend heavily on controlling operating costs, strengthening internal controls, and ensuring the integrity of its services.

The prospect that pending postal legislation may place the Postal Service in a more competitive arena with its private sector counterparts has prompted congressional consideration of some key reform issues. These issues include how proposed changes to the Private Express Statutes may affect universal mail service, postal revenues, and rates. Another reform issue is the future role of the Postal Service in an increasingly competitive, constantly changing communications market.

Congressional oversight remains a key tool for improving the organizational performance of the Postal Service. One of the most important areas for oversight is labor-management relations. Despite the initiatives that have been established to address them, the long-standing

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labor-management relations problems GAO identified in 1994 remain unresolved. The Government Performance and Results Act (GPRA) provides an important avenue for addressing such problems. Also, the Postal Service's automation efforts will continue to require the attention of both the Postal Service and Congress to ensure that increased productivity and an adequate return on investments are realized.

U.S. Postal Service: Challenges to Sustaining Improved Performance

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. My testimony will (1) focus on the performance of the Postal Service and the need for improving internal controls and protecting revenue in an organization that takes in and spends billions of dollars each year and (2) highlight some of the key reform and oversight issues that continue to challenge the Postal Service and Congress as they consider how U.S. mail service will be provided in the future. I will also provide some observations from our ongoing work relating to labor-management relations at the Postal Service and other areas. My testimony is based on our ongoing work and work that we completed over the past year.

Improving Internal Controls and Revenue Protection Remains a Concern

First, I would like to discuss both the reported successes and some of the remaining areas of concern related to the Postal Service's performance. Last year, the Postal Service reported that it had achieved outstanding financial and operational performance. Financially, the Postal Service had the second most profitable year in its history. According to the Postal Service's 1996 annual report, its fiscal year 1996 net income was \$1.6 billion. Similarly, with regard to mail delivery service, the Postal Service continued to meet or exceed its goals for on-time delivery of overnight mail. Most recently, the Postmaster General announced that, during 1996, the Postal Service delivered 91 percent of overnight mail on time or better. Additionally, during fiscal year 1996, the Postal Service's volume exceeded 182 billion pieces of mail and generated more than \$56 billion in revenue.

While these results are encouraging, other performance data suggest that some areas of concern warrant closer scrutiny. For example, last year's delivery of 2-day and 3-day mail—at 80 and 83 percent respectively—did not score as high as overnight delivery. Such performance has raised a concern among some customers that the Postal Service's emphasis on overnight delivery is at the expense of 2-day and 3-day mail. Additionally, although its mail volume continues to grow, the Postal Service is concerned that customers increasingly are turning to its competitors or alternative communications methods. In 1996, mail volume increased by about one-half of anticipated increase in volume.

Containing costs is another key challenge that we reported on previously. In the area of expenditures, the Postal Service's 1996 annual report

showed that its 1996 operating expenses increased 4.7 percent compared to a 3.9 percent increase in operating revenues. Labor costs, which include pay and benefits, continued to account for almost 80 percent of the Postal Service's operating expenses, and the Postal Service expects that its costs for compensation and benefits will grow more than 6 percent in 1997. Moreover, controlling costs will be critical with regard to capital investments in 1997, as the Postal Service plans to commit \$6 billion to capital improvements. Over the next 5 years, the Service plans to devote more than \$14 billion in capital investments to technology, infrastructure improvements, and customer service and revenue initiatives.

The Postal Service's continued success in both operational and financial performance will depend heavily on its ability to control operating costs, strengthen internal controls, and ensure the integrity of its services. However, we found several weaknesses in the Postal Service's internal controls that contributed to unnecessary increased costs.

We reported in October 1996¹ that internal controls over Express Mail Corporate Accounts (EMCA) were weak or nonexistent, which resulted in the potential for abuse and increasing revenue losses over the past 3 fiscal years. Specifically, we found that some mailers obtained express mail services using invalid EMCAs and that the Postal Service did not collect the postage due. Consequently, in fiscal year 1995, the Postal Service lost express mail revenue of about \$800,000 primarily because it had not verified EMCAs that were later determined to be invalid.

Since our report was issued, the Postal Service has developed plans to address these deficiencies. The Postal Service is revising its regulations to require an initial deposit of \$250, up from \$100, to open an EMCA. It also plans to issue a memorandum requiring that district managers ensure that employees perform the necessary express mail acceptance checks so that the correct postage amounts can be collected. Finally, the Postal Service plans to install terminals in mail processing plants to allow Express Mail packages that are deposited in collection boxes or picked up at customers' locations to be checked for valid EMCA numbers before they are accepted into the mail system.

¹U.S. Postal Service: Revenue Losses From Express Mail Accounts Have Grown (GAO/GGD-97-3, Oct. 24, 1996).

Similarly, we reported in June 1996² that weaknesses in the Postal Service's controls for accepting bulk business mail prevent it from having reasonable assurance that all significant amounts of postage revenue due are received when mailers claim presort/barcode discounts. We reported that during fiscal year 1994, as much as 40 percent of required bulk mail verifications were not performed. Bulk mail totalled almost one-half of the Postal Service's total revenue of \$47.7 billion in fiscal year 1994. At the same time, we found that less than 50 percent of the required follow-up verifications to determine the accuracy of the clerk's work were being performed by the supervisors. In response to our recommendations, the Postal Service is developing new and strengthening existing internal controls to help prevent revenue losses in bulk mailings. For example, the Postal Service plans to improve the processes used in verification of mail, including how units are staffed, how verifications are performed, and how results of acceptance work are reported and reviewed.

To avoid additional unwarranted costs, the Postal Service also needs to better ensure the overall integrity of its acquisitions and services. We concluded, in our January 1996 report³, that the Postal Service did not follow required procedures for seven real estate or equipment purchases. We estimated that these seven purchases resulted in the Postal Service's expending about \$89 million on penalties, unusable, or marginally usable property. Three of the seven purchases involved ethics violations arising from the contracting officers' failure to correct situations in which individuals had financial relationships with the Postal Service and with certain offerors. We also pointed out that the Office of Government Ethics was reviewing the Postal Service's ethics program and reported that all areas of the program required improvement. The Office of Government Ethics subsequently made a number of recommendations designed to ensure that improvement of the Postal Service's ethics program continues through more consistent oversight and management support.

Since our January 1996 report, the Office of Government Ethics has completed three reviews to follow up on its open recommendations. Recently, the Postal Service developed guidance for avoiding conflicts of interest and filing financial disclosure reports as well as established procedures to ensure that the Office of Government Ethics is notified about all conflict-of-interest violations that are referred to the Department

²U.S Postal Service: Stronger Mail Acceptance Controls Could Help Prevent Revenue Losses (GAO/GGD-96-126, June 25, 1996).

³Postal Service: Conditions Leading to Problems in Some Major Purchases (GAO/GGD-96-59, Jan. 18, 1996).

of Justice. As a result of these actions, the Office of Government Ethics closed its remaining open recommendations.

Additionally, strengthening program oversight is essential to effective mail delivery. We found that the Postal Service did not exercise adequate oversight of its National Change of Address (NCOA) program.⁴ We reported that the Postal Service took a positive step toward dealing with the inefficiencies of processing misaddressed mail. However, at the same time, we found that the NCOA program was operating without clear procedures and sufficient oversight to ensure that the program was operating in compliance with the privacy provisions of federal laws. Accordingly, we recommended that the Postal Service strengthen oversight of NCOA by developing and implementing written oversight procedures. In response to our recommendation, the Postal Service developed written oversight procedures for the NCOA program.

Most recently, we issued a report⁵ that describes how the Postal Service closes post offices and provides information on the number closed since 1970—over 3,900 post offices. We also provided information on the number of appeals and their dispositions, as well as some information about the communities where post offices were closed in fiscal years 1995 and 1996. Generally, the Postal Service initiated the closing process after a postmaster vacancy occurred through retirement, transfer or promotion, or after the termination of the post office building's lease. In each case, the Postal Service proposed less costly alternative postal services to the affected community, such as establishing a community post office operated by a contractor or providing postal deliveries through rural routes and cluster boxes.

Key Reform Issues

The second area I would like to discuss is the pending postal legislation. This legislation may place the Postal Service in a more competitive arena with its private sector counterparts and has raised some key reform issues for consideration. One such issue relates to proposed changes to the Private Express Statutes. These Statutes were set up to ensure that the Postal Service has enough revenue to provide universal access to postal services to the general public and that certain mail, such as First-Class,

⁴U.S. Postal Service: Improved Oversight Needed to Protect Privacy of Address Changes (GAO/GGD-96-119, Aug. 13, 1996).

⁵U.S. Postal Service: Information on Post Office Closures, Appeals, and Affected Communities (GAO/GGD-97-38BR, Mar. 11, 1997).

will bear a uniform rate. In our September 1996 report,⁶ we emphasized the importance of recognizing the Statute's underlying purpose and determining how changes may affect universal mail service and uniform rates. Most important among the potential consequences is that relaxing the Statutes could open First-Class mail services to additional competition, thus possibly affecting postal revenues and rates and the Postal Service's ability to carry out its public service mandates. However, at the same time, the American public could benefit through improved service. It will be important to take into account the possible consequences for all stakeholders in deciding how mail services will be provided to the American public in the future.

Another key reform issue is the future role of the Postal Service in the constantly changing and increasingly competitive communications market. For example, the use of alternative communications methods such as electronic mail, faxes, and the Internet continues to grow at phenomenal rates in the United States and is beginning to affect the Postal Service markets. At the same time, the Postal Service's competitors continue to challenge it for major shares of the communications market. According to the Postmaster General, the Postal Service has been losing market share in five of its six product lines. It seems reasonable to assume that these alternative communications methods are likely to be used more and more. In addition, international mail has become an increasingly vital market in which the Postal Service competes. In our March 1996 report,⁷ we pointed out that, although the Postal Service has more flexibility in setting international rates, it still lost business to competitors because rates were not competitive and delivery service was not reliable. We also identified several issues surrounding the Postal Service's role in the international mail arena that remain unresolved. Chief among them is the appropriateness of the Postal Service's pricing practices in setting rates for international mail services.

We also reviewed postal reform in other countries to learn about their experiences. Recently, we issued a report⁸ on Canada's efforts since 1981 to reform its postal service, the Canada Post Corporation (CPC). Although CPC retained basic letter mail services at a uniform rate, it also reduced the

⁶Postal Service Reform: Issues Relevant to Changing Restrictions on Private Letter Delivery (GAO/GGD-96-129A/B, Sept. 12, 1996).

⁷U.S. Postal Service: Unresolved Issues in the International Mail Market (GAO/GGD-96-51, Mar. 11, 1996).

⁸Postal Reform in Canada: Canada Post Corporation's Universal Service and Ratemaking (GAO/GGD-97-45BR, Mar. 5, 1997).

frequency of mail delivery to some businesses, as well as in urban and rural areas. CPC uses a regulatory rate-making process that includes the opportunity for public comment and government approval for basic domestic and international single-piece letters. However, postage rates for other mail services can be approved by CPC without issuing regulations or obtaining government approval. Some of the key concerns that have been raised by CPC customers include CPC's closure of rural post offices and its conversion of others to private ownership. In addition, CPC's competitors have expressed concern about whether CPC is cross-subsidizing the prices of its courier services with monopoly revenues. The Canadian government has responded to these concerns by continuing its moratorium on post office closings and directing CPC to discontinue delivery of unaddressed advertising mail. The government is also considering a call for additional government oversight of CPC.

Mr. Chairman, as you are aware, we also have a number of ongoing reviews related to postal reform. For example, in concert with your focus on the future role of the Postal Service, we are currently reviewing the role and structure of the Postal Service's Board of Governors in order to determine its strengths and weaknesses. The Board of Governors is responsible for directing and controlling the expenditures of the Postal Service, reviewing its practices, participating in long-range planning, and setting policies on all postal matters. In addition to obtaining the views of current and former Board members, we will provide information on the role and structure of Boards in other types of government-created organizations. Another issue important to postal reform that we are reviewing involves access to mailboxes. More specifically, we plan to provide information on (1) public opinions on the issue of mailbox restrictions; (2) views of the Postal Service and other major stakeholders; and (3) this country's experience with mailbox security and enforcement of related laws, compared with the experiences in selected other countries.

Oversight of the Postal Service Remains Important

Congressional oversight remains a key to improving the organizational performance of the Postal Service. One of the most important areas for oversight is labor-management relations. As the Postal Service focuses on the significant challenges it faces to compete in today's communications marketplace, unresolved labor-management relations disputes continue to hinder efforts to improve productivity. Generally, the long-standing labor-management problems we identified in 1994 still remain unresolved,

despite the initiatives that have been established to address them.⁹ For example, the number of grievances requiring formal arbitration has increased almost 76 percent, from about 51,000 in fiscal year 1993 to over 90,000 in fiscal year 1996. These difficulties continue to plague the Service primarily because the major postal stakeholders (the Postal Service, four major unions, and three management associations) cannot agree on common approaches for addressing their problems. We continue to believe that until the major postal stakeholders develop a framework agreement that would outline common objectives and strategies, efforts to improve labor-management relations will likely continue to be fragmented and difficult to sustain.

The Government Performance and Results Act (GPRA) provides a mechanism that may be useful in focusing a dialogue that could lead to a framework agreement. GPRA provides a legislatively based mechanism for the major stakeholders, including Congress, to jointly engage in discussions that focus on an agency's mission and on establishing goals, measuring performance, and reporting on mission-related accomplishments. GPRA can be instrumental to the Postal Service's efforts to better define its current and future role. As results-oriented goals are established to achieve that role, the related discussions can also provide a foundation for a framework agreement. Successful labor-management relations will be critical to achieving the Postal Service's goals. The Postal Service and Congress will need results-oriented goals and sound performance information to most effectively address some of the policy issues that surround the Postal Service's performance in a dynamic communications market. Recognizing that the changes envisioned by GPRA do not come quickly or easily, sustained oversight by the Postal Service and Congress will be necessary.

Finally, several other areas will continue to require the attention of both the Postal Service and Congress. One such area is the Postal Service's automation efforts. The Postal Service has spent billions of dollars to ensure that an increase in productivity and an adequate return on planned investments are realized. Another area is the Postal Service's 5-year capital investment plan for 1997-2001. It calls for investing \$14.3 billion, of which \$3.6 billion is designated for technology investments. Also included is \$6.6 billion for planned infrastructure improvements such as maintaining and improving over 35,000 postal facilities and upgrading the vehicle fleet of more than 200,000 vehicles. In addition, customer satisfaction at both

⁹U.S. Postal Service: Labor-Management Problems Persist on the Workroom Floor (GAO/GGD-94-201A/B, Sept. 29, 1994).

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the residential and business levels will continue to be a critical area as the Postal Service strives to improve customer service in order to remain competitive.

The Postal Service has made considerable progress in improving its financial and operational performance. Sustaining this progress will be dependent upon ensuring that the key issues we identified, such as controlling costs, protecting revenues, and clarifying the role of the Postal Service in an increasingly competitive communications market, are effectively addressed by the Postal Service and Congress.

Mr. Chairman, this concludes my prepared statement. I have attached a list of our Postal Service products issued since January 1996. I would be pleased to respond to any questions you or members of the Subcommittee may have.

GAO Postal-Related Products Issued Since January 1, 1996

U.S. Postal Service: Information on Post Office Closures, Appeals, and Affected Communities ([GAO/GGD-97-38BR](#), Mar. 11, 1997).

Postal Reform in Canada: Canada Post Corporation's Universal Service and Ratemaking ([GAO/GGD-97-45BR](#), Mar. 5, 1997).

U.S. Postal Service: Revenue Losses From Express Mail Accounts Have Grown ([GAO/GGD-97-3](#), Oct. 24, 1996).

Postal Service: Controls Over Postage Meters ([GAO/GGD-96-194R](#), Sept. 26, 1996).

Inspector General: Comparison of Certain Activities of the Postal IG and Other IGs ([GAO/AIMD-96-150](#), Sept. 20, 1996).

Postal Service Reform: Issues Relevant to Changing Restrictions on Private Letter Delivery ([GAO/GGD-96-129A/B](#), Sept. 12, 1996).

U.S. Postal Service: Improved Oversight Needed to Protect Privacy of Address Changes ([GAO/GGD-96-119](#), Aug. 13, 1996).

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

U.S. Postal Service: Unresolved Issues in the International Mail Market ([GAO/GGD-96-51](#), Mar. 11, 1996).

Postal Service: Conditions Leading to Problems in Some Major Purchases ([GAO/GGD-96-59](#), Jan. 18, 1996).

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