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THE U.S. POSTAL SERVICE'S UNCERTAIN FINANCIAL OUTLOOK, PARTS I AND II

HEARINGS

BEFORE THE

COMMITTEE ON GOVERNMENT REFORM

HOUSE OF REPRESENTATIVES

ONE HUNDRED SEVENTH CONGRESS

FIRST SESSION

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THE U.S. POSTAL SERVICE'S UNCERTAIN FINANCIAL OUTLOOK, PART I

WEDNESDAY, APRIL 4, 2001

HOUSE OF REPRESENTATIVES,
COMMITTEE ON GOVERNMENT REFORM,
Washington, DC.

The committee met, pursuant to notice, at 10:05 a.m., in room 2154, Rayburn House Office Building, Hon. Dan Burton (chairman of the committee) presiding.

Present: Representatives Burton, Gilman, Morella, Shays, McHugh, Horn, Scarborough, LaTourette, Barr, Ose, Lewis, Putnam, Otter, Schrock, Waxman, Maloney, Norton, Cummings, Kuchinich, Davis, Turner, Allen, Schakowsky, and Clay.

Staff present: Kevin Binger, staff director; Daniel R. Moll, deputy staff director; David A. Kass, deputy counsel and parliamentarian; Mark Corallo, director of communications; John Callender and Randy Kaplan, counsels; Sarah Anderson, staff assistant; Robert A. Briggs, chief clerk; Robin Butler, office manager; Michael Canty, legislative assistant; Josie Duckett, deputy communications director; John Sare, deputy chief clerk; Danleigh Halfast, assistant to chief counsel; Corinne Zaccagnini, systems administrator; Phil Schiliro, minority staff director; Phil Barnett, minority chief counsel; Denise Wilson, minority professional staff member; Ellen Rayner, minority chief clerk; Jean Gosa and Earley Green, minority assistant clerks; and Lorran Garrison, minority staff assistant.

Mr. BURTON. The Committee on Government Reform will come to order. We expect a vote on the floor on the Journal probably in about 15 minutes. So, we will get started with opening statements. After that, we will probably have to break for the vote, but we will only be gone for about 10 minutes.

A quorum being present, the Committee on Government Reform will come to order. I ask unanimous consent that all Members and witnesses written opening statements be included in the record.

Without objection, it is so ordered.

I ask unanimous consent that all articles, exhibits and extraneous or tabular material referred to be included in the record.

Without objection, it is so ordered.

I want to welcome everyone to this hearing of the Government Reform Committee. We are here today to examine the current financial condition of the Postal Service.

As part of the reorganization of our committee structure for the 107th Congress, postal issues will be handled at the full committee level.

As most of you know, I am a veteran of the old committee on Post Office and Civil Service. I have been extremely active on postal issues for many years.

Representative John McHugh, the former chairman of the Postal Subcommittee, did an outstanding job for 6 years working on postal reform. I intend, along with Mr. Waxman, to conduct a vigorous oversight of the Postal Service and through that oversight we will work to assure affordable, universal postal service.

The Postal Service is the only government agency that touches the lives of virtually every household and every American in this country. In other words, every citizen has a stake in the future of the Postal Service.

The Service employs over 900,000 people to deliver more than 668 million pieces of mail every day.

At the outset, let me say that I am concerned about the news coming out of the Postal headquarters. They are predicting a $2 to $3 billion loss this fiscal year, the same year that they just raised postal rates.

My first reaction was disbelief, especially in view of the fact that in the last couple of years there has been a surplus. My second reaction was grave concern when I was informed that the Postal Service intends to file for another rate increase in just a few months.

In the past I have been critical of the Postal Service because their first response to every financial shortfall appears to be to raise rates. An increase of the magnitude proposed between $6 and $8 billion total revenue, is astronomical. That represents a 10-percent increase in over all revenues.

This kind of increase would drive businesses away from the Postal Service. Some mailers would be forced to seek alternative means of communication. Others very well could be driven into bankruptcy. I view this as a slippery slope for the Postal Service.

This rate increase, combined with the revenue drain being caused by the information technology revolution spells long-term trouble for the Service. The alternative to raising rates is to do what every private sector business does when its sales decline: cut costs and increase quality of service.

You know, if General Motors or Chrysler has financial difficulties and their sales drop, they don't raise the cost of the car to make up for the deficiency. They try to figure out ways to streamline, to economize and to make sure that they are going to be competitive in the marketplace. That same principle should be applied to the Postal Service.

The alternative to raising rates, as I said, is to do what every private business does when its sales decline. That is to cut costs and increase service quality.

Today, I hope to hear a specific plan from the Postmaster General about what steps are being taken to reduce expenses. The Postal Service has announced plans to immediately freeze capital commitments for improvements to postal facilities. This will reportedly save about $1 billion. More cost containment options must be examined. Nothing should be off of the table. Another rate increase should be the last option and not the first.

Today, I am calling on the Postal Service to work together with all stakeholders to examine all possible ways to cut costs. I am confident that we can find the savings without affecting the quality of mail service.

If we can succeed with significant cost containment, this will allow the Postal Service to push back the filing for the next rate increase or to eliminate it entirely. The current economic slowdown adds to the dire financial straits in which the postal service finds itself.

However, the larger, long-term problem is the regulatory model that is nearly three decades old. It does not provide the Postal Service with the flexibility needed to succeed in a rapidly changing market.

Again, I want to pay tribute to my colleague, John McHugh. John labored for years trying to develop legislation to fix the Postal Service before the crisis hit. Well, John, it looks like you are the only guy in this room who has the right to say, "I told you so."

I think this situation is akin to the current energy crisis occurring in California. Nobody took the steps necessary to fix the problems early on. Now, we have rolling blackouts and price spikes.

We are in the early stages of a similar crisis in the Postal Service. If we take the necessary steps now to fix the problems, maybe we can avoid a full-blown crisis over the next few years. I am sure there are some naysayers in this room who believe that the information technology revolution in not real, that advertisers are not moving over to the internet, that consumers are not going to pay their utility bills on line, that none of this supposed change will have an impact on the Postal Service and their revenues.

These folks remind me of people who said the entertainment industry would never replace silent movies with the newfangled talkies.

Today we will be hearing from a number of distinguished witnesses to examine the current financial problems at the Postal Service. Our first witness is the head of the General Accounting Office, the watchdog for the legislative branch, Comptroller General David Walker. General Walker has had a team of experts working to help this committee analyze the data we are receiving from the Postal Service.

Our second witness is a man I want to pay a special tribute to, Postmaster General Bill Henderson. General Henderson is completing his tenure at the helm of the Postal Service. He has presided over a period of great turmoil, a time of some detours, a few potholes, but also much progress. I want to thank you, Bill, for your 30 years to service to the country.

Our last panel will consist of five members of the Board of Governors of the Postal Service. In addition to directing and controlling the expenditures of the Postal Service, the Board has the difficult task of selecting the new Postmaster General.

I welcome all of our witnesses and look forward to their testimony.

Before I yield to Mr. Waxman, let me say I have discussed briefly with him the need to work out a bipartisan solution to this crisis. He has extended his hand in friendship to me and we are going to

try our best to see if we can't come up with a bill that will solve the problems that we are facing.

I believe he feels this is a necessity as well as I do. Hopefully, with bipartisan support, we can reach agreement. Toward that end I would like to suggest that all segments, and this is very important, I hope everybody listens to this part because we as legislators can't do this by ourselves.

Toward that end, it would like to suggest that all segments of the postal community sit down together and make recommendations to Mr. Waxman and myself as to how this problem can be solved. That is going to take some compromise. Everybody is going to have to sit down together, the postal unions, the postmasters, the people who do a lot of mailing, the mass markets, the magazine publishers, all of you have to sit down, the packet deliverers, and try to find out where you have some commonality so we can get a product that we can get through the Congress.

If they make recommendations to Mr. Waxman and myself on how to solve this problem, then we think we can get it solved. This process will hopefully lead to a legislative proposal that can pass the House, the Senate and be signed by the President.

Compromise, as I said, is clearly necessary. Those who do not realize this and fail to participate in the process do so at their own peril. The reason I say that is if you stay out of the mix and we come up with a solution to this problem with which you do not agree and you have not participated in the process, Mr. Waxman and I may draft a bill.

It may pass the House with both Democrat and Republican support and pass the Senate and get to the President and something you feel is necessary in the bill may have been left out.

So, please appoint somebody from your area to work with other members of the community to come up with a proposal that you can present to Mr. Waxman or myself that we can work with. If we do that, I think we can come up with a product we will be happy with and the American people will be satisfied with.

With that, Mr. Waxman, do you have an opening statement?

[The prepared statement of Hon. Dan Burton follows:]

Statement of Dan Burton (R-IN), Chairman
Committee on Government Reform
Hearing on the "The Postal Service's Uncertain Financial Outlook"
Wednesday, April 4, 2001,

Good morning and welcome to this hearing of the Government Reform Committee. We are here today to examine the current financial condition of the Postal Service.

As part of the reorganization of our Committee structure for the 107th Congress, postal issues will be handled at the full Committee level. As most of you know, I am a veteran of the old Committee on Post Office and Civil Service. I've been extremely active on postal issues for many years. Rep. John McHugh, former chairman of the postal subcommittee, did an outstanding job for six years working for postal reform. I intend to conduct vigorous oversight of the Postal Service and through that oversight I will work to ensure affordable, universal postal service.

The Postal Service is the only government agency that touches the lives of virtually every household in America. In other words, every citizen has a stake in the future of the Postal Service. The Service employs over 900,000 people to deliver more than 668 million pieces of mail each day.

At the outset, let me say that I am concerned about the news coming out of postal headquarters—they are predicting a two to three billion dollar loss this Fiscal Year—the same year that they raised rates. My first reaction was disbelief. My second reaction was grave concern when I was informed that the Postal Service intends to file for another rate increase in just a few months. In the past I have been critical of the Postal Service because their first response to every financial shortfall appears to be to raise rates. An increase of the magnitude proposed—between $6 and $8 billion total revenue--is astronomical. That represents a 10 percent increase in overall revenue. This kind of increase would drive business away from the Postal Service. Some mailers would be forced to seek alternative means of communication. Others may be driven to bankruptcy. I view this as a slippery slope for the Postal Service. This rate increase, combined with the revenue drain being caused by the information technology revolution, spell long-term trouble for the Service.

The alternative to raising rates is to do what every private sector business does when its sales decline: cut costs and increase service quality. Today I hope to hear a specific plan from the Postmaster General about what steps are being taken to reduce expenses. The Postal Service has announced plans to immediately freeze capital commitments or improvements to postal facilities. This will reportedly save one billion dollars. More cost containment options must be examined. Nothing should be off the table. Another rate increase should be the last option, not the first.

Today I'm calling on the Postal Service to work together with all stakeholders to examine all possible ways to cut costs. I'm confident that we can find savings without affecting the quality of mail service. If we can succeed with significant cost containment, this will allow the

Postal Service to push back the filing for the next rate increase or eliminate the necessity entirely.

The current economic slowdown adds to the dire financial straits in which the Postal Service finds itself. However, the larger, long-term problem is the regulatory model that is nearly three decades old. It does not provide the Postal Service with the flexibility needed to succeed in a rapidly changing market. Again, I want to pay tribute to my colleague, John McHugh. John labored for years trying to develop legislation to fix the Postal Service before the crisis hit. Well John, it looks like you are the one guy in this room who has the right to say, "I told you so." I think this situation is akin to the current energy crisis occurring in California. Nobody took the steps necessary to fix the problems early on. Now we have rolling blackouts and price spikes. We're in the early stages of a similar crisis in the Postal Service. If we take the necessary steps now to fix the problems, maybe we can avoid a full-blown crisis in the next few years.

I am sure there are some naysayers in this room who believe that the information technology revolution is not real, that advertisers are not moving over to the Internet, that consumers are not going to pay their utility bills on-line, and that none of this supposed change will have an impact on postal revenues. These folks remind me of people who said that the entertainment industry would never replace silent movies with the new fangled talkies.

Today we will be hearing from a number of distinguished witnesses to examine the current financial problems at the Postal Service. Our first witness is the head of the General Accounting Office--the watchdog for the legislative branch--Comptroller General David Walker. General Walker has had a team of experts working to help this Committee analyze the data we are receiving from the Postal Service. Our second witness is a man I want to pay a special tribute to, Postmaster General Bill Henderson. General Henderson is completing his tenure at the helm of the Postal Service. He has presided over a period of great turmoil, a time of some detours, a few potholes, but also much progress. I want to thank you Bill for your 30 years of service to your Country. Our last panel will consist of five members of the Board of Governors of the Postal Service. In addition to directing and controlling the expenditures of the Postal Service, the Board has the difficult task of selecting the Postmaster General. I welcome all of our witnesses and look forward to their testimony.

Before I yield to the Ranking Member, Mr. Waxman, let me say that I have discussed briefly with him the need to work out a bipartisan solution to this crisis. I believe he feels it is a necessity as well. Hopefully, with bipartisan support we can reach agreement. Toward that end I would like to suggest that all segments of the postal community sit down together to make recommendations to Mr. Waxman and myself, as to how this problem may be solved. This process will hopefully lead to a legislative proposal that can pass the House, the Senate and be signed by President Bush. Compromise is clearly necessary. Those who do not realize this and fail to participate, do so at their own peril. I hope and believe that Mr. Waxman and the Democrats working with myself and the Republicans, can come up with a product we can all be proud of.

Mr. WAXMAN. Well, Mr. Chairman, I am going to hold my opening statement because Mr. Gilman has a meeting with President Mubarak of Eqypt. I want to allow him to go first. Peace in the Middle East is a very high priority. Peace in the Postal Service is a secondary priority.

Mr. GILMAN. Thank you, Mr. Waxman, for yielding. Mr. Chairman I want to thank you for conducting this hearing this morning.

Along with Chairman Burton, as a long-time because of our former Postal Committee and now the inactive Postal Subcommittee, I am pleased that our full committee is going to now devote time and attention to this important issue facing our U.S. Postal Service.

It is important that we examine all of the factors leading up to the Postal Service current financial projections. We have all read the news reports and the memos and have met with our local Postal Supervisors, Postmasters, and labor leaders concerning the $3 billion of debt that the Postal Service now finds itself confronting.

In fact, in my own Congressional District in New York at the new City Post Office, I have been hearing of manpower shortages which already exist, and now we are learning that the Postal Service may have to cut jobs even more in order to help control costs.

Accordingly, I am left to wonder how the Postal Service will maintain the core mission of universal service. There are many reasons we can point at to answer just how the Postal Service has found itself in these troubled waters today.

Continued decline in volume, insufficient revenues, electronic communication are just some of the problems confronting the Postal Service. However, these factors have all been foreshadowed by our colleague, Congressman John McHugh over the past two Congresses as he worked diligently to try to bring postal reform before the committee and before the Congress.

We cannot now throw up our hands in dismay and wonder how the Postal Service has arrived at this point when in fact we have known for some time that these factors do exist. The Postal Service must also be prepared to take responsibility for the difficult economic times they are now experiencing.

The Postal Service has known for some time the problems and inefficiencies in the postal system which do exist. Both the GAO and the Postal Service's Inspector General has repeatedly testified before our Postal Subcommittee on the difficulties that the Service has had in realizing opportunities on savings.

Accordingly, Mr. Chairman, I am hopeful that today's hearing will provide our committee with the consensus needed to move forward on postal reform, as well as to provide the Postal Service with the understanding that in order to survive and perform its core mission changes in management practices are going to have to be made to implement and be adhered to.

I want to thank Mr. Waxman again for yielding.

Mr. Chairman, thank you for holding this hearing.

Mr. BURTON. Thank you, Mr. Gilman. Give President Mubarak our regards.

Mr. Waxman.

Mr. WAXMAN. Thank you, Mr. Chairman. I want to commend Mr. Gilman on his statement and wish him well in his meetings.

I thank you, Mr. Chairman, for calling this hearing and putting this issue on the agenda with a sense of priority, which you have articulated so well.

I look forward to working with you because I think reforms in this area should be bipartisan. As a Member of Congress, we all know too well the enormous undertaking that postal employees do every day. In good weather and bad, postal workers haul and deliver our letters and packages and we thank them for their efforts.

But some serious challenges confront the Postal Service. Two months ago the U.S. Postal Service Board of Governors reported the Postal Service will suffer a $2 to $3 billion deficit for fiscal year 2001. Since that announcement, the Board has called for an immediate freeze on capital commitments and is looking at reducing mail delivery service to 5 days and consolidating Post Offices. Some say the Postal Service is in the midst of a crisis.

Well, I look forward to learning more about these problems from today's hearing and the presentations of the witnesses that we have scheduled. I also look forward to learning more about these issues through the activities of the Postal Caucus, which is chaired by Representative Danny Davis.

I encourage all members on our committee to study these issues and join our Postal Caucus.

I am committed to sensible postal legislation. Last year, with the support of many of my colleagues, I introduced H.R. 2535, the Postal Service Enhancement Act. It operated from the premise that the Postal Service performs a valuable service that should be strengthened and enhanced. The legislation provided ratemaking flexibility, negotiated service agreements, and phased-in postal rates. It also established a Presidential Commission to identify waste and inefficiency in the Postal Service and provided enhanced authorities for the Postal Rate Commission. Unfortunately, the measure was not considered by this committee.

In the face of calls for postal legislation, we need to analyze the Postal Service's financial condition. We need to determine an accurate projection of postal revenues and losses and examine the procedures the Postal Service uses to track its actual costs and savings from productivity initiatives. We need to know the causes of postal deficits and identify structural or operational issues that could impact the Service's ability to provide affordable universal postal service.

We also need to make sure that the Postal Service is acting responsibly. For example, the freeze on construction of new facilities is dramatic action. We need to examine whether the freeze is justified by the facts. If it is simply an attempt to garner headlines and pressure Congress, the action will create ill will and be counterproductive.

I know the chairman is interested in working on these important issues in a bipartisan fashion. I welcome his initiative and look forward to working with him and all of our colleagues on this committee on how to reform the Postal Service, deal with its fiscal problems, and serve the needs of the American people.

Thank you, Mr. Chairman.

Mr. BURTON. Thank you, Mr. Waxman.

We have about 5 minutes before we have to leave for the vote. Do any other Members at this time have opening statements?

Mr. McHugh, we will go to you and then we will come back to Mr. Davis.

Mr. MCHUGH. Thank you, Mr. Chairman. I will try to be brief. Everyone was saying such nice things about me, I couldn't help but be reminded of a quote attributed to Mickey Mantle, one of my heroes, when he said, "If I knew I was going to live this long I would have taken better care of myself."

If I had known I was going to be so right, I probably would have worked harder. I do appreciate the kind things that have been said.

I would like, Mr. Chairman, to submit for the record my complete statement that is available here for anyone who might be interested, and just say a few words in summary, not the least of which is to express my personal gratitude to you, Mr. Chairman.

You were kind enough to say I was the only person in the room who had the right to say, "I told you so." With all due respect, I disagree. I think there are a number of people in this room, and it starts with you, Mr. Chairman, and extends to the good people who served on both sides of the aisle in the Postal Service Subcommittee, including Mr. Davis, Mr. Fattah in his ranking membership, and others who did work hard and who recognized this problem.

Unfortunately, I think they are not too surprised by the developments that we have seen over the past several months. Beyond those good people, I have to pay particular tribute to the Postmaster General, Bill Henderson, who took incredible leadership, and I suspect, not a small amount of criticism from amongst his peers for the rather daring positions that he took.

I want to join with you, Mr. Chairman, in wishing him all the best in the future. He has certainly earned whatever good things will come to him. Although we will miss him, I know he will be a great addition to whatever efforts he dedicates himself to in the future.

We do have some folks here with us today, too, that have been very, very supportive of the subcommittee's efforts over the past 6 years to identify these problems: the GAO, the Inspector General, the Congressional Research Service. They have said to us repeatedly that, in fact, the Postal Service is at the end of an era. Those were the words used by the GAO in 1999.

As I noted during our last Postal Subcommittee hearing some 7 months ago, "Folks, we are fooling ourselves if we think that the growing pressure of declining revenues and increased costs at the base of the Postal Service does not require Congress to act and at long last to begin to address this very, very serious situation."

We did have a base bill—a base bill that I am pleased to say was reported unanimously twice with Republican and Democrat support from the subcommittee. But, because of the reality of Washington where on far too many occasions the urgent overcomes the merely important, the bill was not able to be advanced further.

We now have a crisis. The time to delude ourselves to the contrary is past. The statistics, the proposals that we have heard over the past several weeks, I think, underscore that—a $2 to $3 billion operating deficit for this current fiscal year.

The Service will reach its statutory debt limit of $15 billion by October 1st of this year. The Postal Service is running out of cash and has already cut capital spending by some $1 billion; 800 postal facilities due for construction or rehabilitation in every district and every community in this country will be put aside.

There was an announcement yesterday that the Postal Service is seriously considering the possibility of terminating Saturday deliveries. This is only the beginning.

I agree fully with the chairman that the Postal Service has to draw upon every option as the first direction in trying to meet this challenge. Rate increases are something we would like to see avoided at all possible costs. But at the end of the day, I would say to my colleagues: This is Congress' responsibility.

When all of the efforts are made and whatever failures or successes might come, it is each Member of the 435 Member House that has to go home and tell his or her constituents why it is that the Postal Service is not able to perform its core function, because Congress failed to act.

I want to add my voice to those of the chairman, Mr. Waxman, Mr. Davis and others who stand ready to work on a bipartisan basis because this is not a matter of politics. It is a matter of policy. It is a matter of service to the people of this country. We owe it to them to work within our abilities to at long last bring about meaningful postal reform that meets all of the concerns of the incredibly diverse universe that is the Postal Service.

So, Mr. Chairman, I am looking forward to that effort. Thank you for your leadership. I am looking forward to the comments here today.

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

OPENING STATEMENT OF CONGRESSMAN JOHN M. McHUGH
COMMITTEE ON GOVERNMENT REFORM
POSTAL OVERSIGHT HEARING
APRIL 4, 2001

Good morning. I would like to thank the Chairman for calling this hearing on the Postal Service's financial problems. It is indeed a timely hearing. I would also like to welcome General Walker. The General Accounting Office (GAO) is on the front lines as America's postal watchdog, and during my tenure as Chairman of the Postal Service Subcommittee, they proved to be valuable partners with the Congress in evaluating a broad range of postal operations.

Unfortunately, for folks like me and Chairman Burton who have been focused for more than six years on trying to modernize our nation's outdated postal laws, the Postal Service's problems come as no surprise. Objective parties such as the GAO, the Inspector General, and the Congressional Research Service have testified consistently for the last several years that the Postal Service is at the "end of an era," as the GAO stated in 1999. And as I noted at the last hearing of the Postal Service Subcommittee seven months ago, we are fooling ourselves if we think that with the growing cost pressures and shrinking revenue base of the Postal Service, Congress can continue to delay addressing postal reform.

I have always feared that rather than undertaking reasonable and gradual change as we tried to accomplish through last Congress's Subcommittee-approved Postal Modernization Act – a well-refined bill endorsed by a wide array of postal employee organizations, nonprofit and commercial mailers, community newspapers, and several legislators including Senate Democratic Leader Tom Daschle – Congress would await a worsening crisis and be left with choices of desperation in its duty to provide universal mail delivery that binds the nation together.

And let's not kid ourselves. The crisis is upon us. For those who proudly proclaimed for the last several years that the Postal Service "ain't broke, don't fix it," or who gleefully

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obstructed any substantive postal reform legislation from moving forward, or for those who simply decided to take a pass on all things postal and enjoy the status quo, **it's time for a reality check:**

- A looming deficit: *The Postal Service estimates a $2 billion to $3 billion deficit for fiscal year 2001*;
- Barred from borrowing: *The Service expects to reach its statutory debt limit of $15 billion in fiscal year 2002, which begins October 1*;
- A cash crunch: *The Postal Service is running out of cash, and has already cut capital spending by $1 billion*;
- Another rate hike: *The Service plans to file another rate increase, probably averaging more than 10 percent.*

Because of our careful work to advance postal reform the past six years, we fortunately don't have to start from scratch. Those efforts resulted in the Postal Modernization Act – twice passed by the Subcommittee in a bipartisan manner with the inclusion of all amendments offered by the Minority. As opposed to the severe constraints the Postal Service faces from outdated governing laws, the Postal Modernization Act provided the Service and its employees true pricing and managerial tools to confront the serious decline in revenue. The Postal Modernization Act substantively addressed the demands of the American mailing consumer for rate stability and service quality. And, the Postal Modernization Act met the concerns of small business and private sector competitors who need strong rules to protect the public interest from unfair competition.

Mr. Chairman, I want to reiterate to all Committee Members our willingness to work with anyone, on any side of the aisle, to enact substantive postal reform in 2001. The Postal Service, its 850,000 dedicated employees, and the 281 million American citizens who depend on universal service at affordable rates are counting on us.

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Rep. John McHugh (R-NY) served as Chairman of the Subcommittee on the Postal Service from 1995-2000 -- until Congressional term-limits forced him to step aside at the end of the 106th Congress. Postal issues are now within the jurisdiction of the full Government Reform Committee, chaired by Rep. Dan Burton (R-IN). Rep. McHugh remains Congress' most outspoken advocate for reform to preserve our nation's mail system.

For additional information, please contact Dana Johnson at 202-225-4611.

Mr. BURTON. Thank you for your leadership, Mr. McHugh. We will start with Mr. Davis when we come back.

We will stand in recess to the call of the gavel.

[Recess.]

Mr. BURTON. The Chair now recognizes the ranking member on the former Post Office and Civil Service Subcommittee, Mr. Davis.

Mr. DAVIS. Thank you, Mr. Chairman. Mr. Chairman, I am pleased to join with you today at the first full committee hearing devoted solely to the U.S. Postal Service. Although this is not a general postal oversight hearing, it is timely given the recent developments in the financial status of the Postal Service.

As a member of the former Subcommittee on the Postal Service for a number of years, I can personally attest to the importance of the Postal Service, the service that it provides to the American people across this Nation.

Postal clerks, mail handlers, letter carriers, police inspectors and others are engaged on a daily basis in the delivery, processing and protection of our mail system.

As a member of the former subcommittee, I can also speak first hand to the efforts of Representative John McHugh and his staff to change the structure and operation of the Postal Service. This change is embodied in H.R. 22, the Postal Modernization Act, which was unanimously voted from the subcommittee in April 1999.

This bipartisan action taken 2 years ago was an acknowledgement of the insight and the hard work of Representative McHugh. It also allowed us the opportunity to further define and refine postal legislation in the full committee setting.

Unfortunately, while many in the postal community wanted change, agreement on just what that change should look like and how far it should go proved illusive. In July 1999, ranking member, Henry Waxman and Representative Chaka Fattah, former ranking member of the Postal Subcommittee, introduced legislation, H.R. 2535, the Postal Enhancement Act. This, too, was in response to those wishing for change, although on a much narrower scope than the Postal Modernization Act.

Since then and now the Postal Service continues to push for change in the area or people, prices, and products. In addressing the people portion, the Board of Governors recently sent letters to the Hill pointing out that the 1970 Postal Reorganization Act establishes, "a system of collective bargaining followed by compulsory arbitration that mitigates against a negotiated settlement and which, moreover, has often placed some 80 percent of our total costs in the hands of a third-party arbitrator with neither understanding of nor the responsibility for our role and mission."

The Board has gone on to say that current postal law does not provide a mechanism to control wage rates. Relative to prices and products, the Board want to adjust postage rates quickly and offer new products in response to market changes and needs.

This hearing is timely because it allows us to pick up where we left off in the last Congress, with one exception. The Postal Service is now predicting a deficit of somewhere between $2 and $3 billion and a crisis is apparently at hand.

To its credit, the Postal Service and Board have begun to take steps to stabilize the situation. The Postal Service has warned us that their ability to deliver universal service is at risk without postal reform.

The Board has called for an immediate freeze on capital commitments. The Postmaster General has just announced that it will cut $2.5 billion in costs, eliminate 75,000 jobs and create a new mailing industry task force to assess the role and value of hard copy mail and identify opportunities for future growth.

Of course, just yesterday the Board directed management to study cost savings associated with reduction in the delivery of service to 5 days and consolidate postal facilities.

Mr. Chairman, I look forward to working with you and ranking member, Henry Waxman, Representative McHugh and others as we seriously examine the Postal Service's financial status. As the newly elected chair of the newly created Bipartisan Congressional Postal Caucus, I invite all of my colleagues and urge them to join so that we will have many opportunities to engage in discussion relative to the current state of the Postal Service.

I believe that this medium would be an excellent chance to really seriously understand, as well as further hammer out possibilities as we deal with the realities of our situation.

I thank you, Mr. Chairman, for your leadership. I look forward to our seriously tackling this problem. I thank you very much and yield back the balance of my time.

Mr. BURTON. Thank you, Mr. Davis.

Mr. Barr.

Mr. BARR. Thank you, Mr. Chairman. I would like to echo the comments of Mr. Davis. I thank you for your leadership on this issue. I think the U.S. Postal Service is clearly important enough so this ought to be a topic for our full committee.

I appreciate, as always, your taking the leadership on key issues.

As have many Members of Congress, I have lived and worked overseas. I know, through having suffered through postal services in other countries, how fortunate we are here in America to have the finest postal service anywhere in the world. As probably most Members do, I work very closely with our post offices in our district. I work very closely with our Postmasters, as well as the men and women who perform the vital service of delivering our mail.

That being said, Mr. Chairman, I am very disturbed by the recent reports of financial difficulties in the Postal Service. I think it is very timely that we look very, very carefully and comprehensively at what has caused what appears to be a very, very sudden turn-around.

I am also very concerned about reports that we continue to receive about excessive bonuses, excessive reimbursement for relocating employees, limousines, lavish parties. Hopefully, all of those reports that we are getting and all of the discussions that we get from business of the Postal Service are all wrong in those regards. Maybe we can clear the record on that here today.

If they are not completely made up, though, we do have some serious problems with how moneys are being spent. Also, I am extremely concerned about reports that are now surfacing that the Postal Service wants to cut out Saturday delivery. I think that

would be the worst thing possible that they could do for themselves.

There is nothing that would hasten people's interest in pursuing other forms of delivering mail than that sort of "cut off your nose to spite your face" activity or proposal by the Postal Service. Hopefully, we will get this cleared up today and the Postal Service leadership will tell us that those reports are completely inaccurate, that the Postal Service will be proud to continue delivering mail to the American people and American businesses 6 days a week, Mr. Chairman.

If those reports are not completely false and if we hear from the Postal Service today that they are indeed even contemplating that, then I think that we will be in a situation of looking at dramatically changing the authority that the Postal Service has. I think that they will put themselves in a box that will result in American businesses and citizens looking for alternative means of having their mail delivered. This would be one of the most self-defeating proposals that I have ever heard in my life, Mr. Chairman.

I think your hearing today could not be more timely. I appreciate the witnesses coming forward. I look forward to a very, very productive hearing, not only today, but as you continue to exert leadership on this issue.

Thank you, Mr. Chairman.

Mr. BURTON. Thank you, Mr. Barr.

Who was here first? Why don't we go to that lovely lady? Yield to Mrs. Maloney.

Mrs. MALONEY. I would be delighted to yield to Mr. Kucinich, since he has seniority over me.

Mr. KUCINICH. Please go ahead.

Mrs. MALONEY. What a gentleman. Thank you.

First of all, I want to be associated with the comments of many of my colleagues. I certainly agree with Congressman McHugh from the great State of New York, and the chairman that this is a bipartisan issues; it is a policy issue, one that we should all care about and all work on.

I agree with Mr. Barr, we do have the best Postal Service in the world and one that should continue 6 days a week.

I would like to summarize my remarks and put my full comments into the record. I am very glad that this hearing is being held. I want to really express the distress that I had earlier in a former year when the Postal Committee was abolished and really merged into the Government Reform and Oversight Committee and this year the Postal Subcommittee was eliminated.

Certainly, a quality universal Postal Service is incredibly important to every American. I was very distressed when the subcommittee was eliminated. I am glad that my colleague, Mr. Davis, along with friends on the other side of the aisle have formed a Task Force on Postal Service, of which I am a member. I applaud them for taking that leadership role.

I think that everyone in this room has got to be upset by the revenue estimates generated by the Postal Service in recent months. What makes the situation even more confusing is that the estimates generated by the USPS are so entirely different from their own projections as recently as last year.

Now, I just want to say that one of the things that happened last year was the rate increase. Now, this rate increase was supposed to ensure that the USPS would not repeat last year's financial problems.

But now, just a few months later, the Postal Service tells us that we are looking at a $2 to $3 billion loss.

My main question today is really a management question. How in the world did this change so much and so quickly? Now, the Postal Service hearings said that they would like more flexibility. They would like more flexibility to run the Post Office more like a private business.

But I have to say, what business in this country would even dream of succeeding with such poor planning and projections?

So I think we really have to look at the management. Even with these unclear, uncertain financial projections, the USPS has basically shouted from the rooftops about their problem, the situation that they face. You know, the sky is falling, we are in a terrible situation. They are saying that the only thing that can save the Post Office is radical postal reform.

Now, indeed everyone needs to reform every year. We need to reform the Post Office and all of our agencies for a 21st century operation. But we cannot forget that the Post Office was created to serve all Americans in a convenient and affordable manner and we have to make sure that continues.

We cannot make radical policy decisions based on unclear projections. Just last month, the Post Office and the Postal Service stopped all work on all capital projects across the Nation.

Yesterday, in a move that I believe was timed to raise the profile of this hearing, the Post Office announced that it was considering eliminating Saturday service and closing postal facilities.

Now, believe me, we are all concerned about the Post Office's financial situation, but we cannot even begin to identify solutions to these problems if we do not have a clear picture and view of where we are going, if we don't have clear planning.

I am very pleased to see Mr. Walker here, the General Accounting Officer. I know that he will speak about some of the reforms they believe the Post Office should pursue, including better tracking of costs, expenses and capital assets. I am very eager to hear their views and gain a better perspective on how accurate USPS projections are and just what is needed to ensure their future financial stability.

I am also interested to learn from the Postal Service why their projections have changed so dramatically and whether they have implemented some of the efficiencies they have previously claimed would save $700 million a year.

So, hopefully today's hearing will shed some light on these and other issues surrounding the operation of the Post Office and help us guarantee that the Postal Service remains a modern and effective organization for the 21st century and beyond.

Thank you very much for having this hearing, Mr. Chairman.

[The prepared statement of Hon. Carolyn B. Maloney follows:]

Opening Statement
Government Reform Committee
Rep. Carolyn Maloney
April 4, 2001

I would like start by saying how pleased I am that this committee has taken the time to look at postal issues today.

I was extremely alarmed when I learned that the Postal Subcommittee was being eliminated earlier this year, and I certainly hope that this committee is willing to continue examining postal issues as thoughtfully and comprehensively as possible.

The Postal Service is one of the most important functions of our government and I think New Yorkers and all Americans understand how important quality, universal postal service is.

In the digital age, we need to make sure that today's postal service does not end up like yesterday's pony express. Today's hearing should be one of many steps this congress takes to ensure that the Postal Service is a strong, viable organization through and beyond the 21st century.

I think all of us in this room have been upset by the revenue estimates generated by the Postal Service in recent months.

What makes the situation even more confusing is that the estimates generated by USPS are so entirely different from their own projections as recently as last year.

The recent rate increase was supposed to ensure that the USPS would not repeat last year's financial flop. Now, a few months later, the Postal Service tells us they are looking at a 2-3 BILLION dollar loss.

Why the sudden change? I frequently hear from my constituents who work for the Postal Service. They work hard, take a lot of pride in what they do, and they are extremely upset with the latest projections and the uncertainty that these numbers have created.

The Post Office has said before that they would like the flexibility of a private business. But what business would succeed with such poor planning?

These sudden accounting changes and the drastic and immediate policy changes USPS is considering sends the wrong signal to postal employees and it sends the wrong signal to postal customers across the country.

Still, despite these unclear and uncertain financial projections, USPS has shouted from the rooftops about their situation. In their view, the sky seems to be falling week after week and the only thing that will save the Postal Service is radical postal reform.

Indeed, postal reform is needed. The Post Office should be a 21st century operation. But we cannot forget that the Post Office exists to serve **all** Americans in a convenient and affordable manner.

We cannot and should not make radical policy decisions based on unclear projections. Last month, the Postal Service stopped all work on capital projects across the nation.

Yesterday, in a move apparently timed to raise the profile of this hearing, the Post Office announced that it was considering eliminating Saturday service and closing postal facilities.

We are all concerned about the Postal Service's financial situation. But we cannot even begin to identify solutions to these problems if we do not have a clear picture of what is really going on.

I understand the General Accounting Office is here today to talk about some of the reforms they believe the Post Office should pursue, including better tracking of costs, expenses, and capital assets. I am very eager to hear their views and gain a better perspective on how accurate USPS projections are, and just what is needed to ensure future financial stability.

I am also interested to learn from the Postal Service why their projections have changed so dramatically and whether they have implemented some of the efficiencies they have previously claimed would save $700 Million a year.

Hopefully, today's hearing will shed some light on these and other issues surrounding the operation of the Post Office and help us guarantee that the Postal Service remains a modern and effective organization for the 21st century and beyond.

Thank you.

Mr. BURTON. Thank you, Mrs. Maloney.

Mrs. Morella.

Mrs. MORELLA. Thank you, Mr. Chairman and also Ranking Member Waxman for holding this critical hearing on the uncertain financial future of the U.S. Postal Service. I do also associate myself with the comments of my colleagues on both sides of the aisle.

After 5 years of operating at a surplus and comparably minor loss in fiscal year 2000, the Postal Service's announcement of a potential $2 to $3 billion deficit in fiscal year 2001 is quite disconcerting. Such a dismal national projection and reports of yet another increase in postal rates has taken my constituents and me by surprise after only recently becoming accustomed to the recent 1-cent stamp increase.

In fact, in January of this year the Postal Service increased rates an average of 4.6 percent. While it was not the 6 percent increase the service sought, at that time it was believed to be sufficient.

Today I am interested in learning what has caused the Postal Service to abruptly fall into such a state of disrepair that they would be projecting losses in the same calendar year that they raised rates.

To the defense of the Postal Service, I understand how difficult it must be to operate like a self-supporting business, as intended by Congress, without the flexibility of price control and within the framework of an antiquated piece of legislation.

However the constraints of the Postal Reorganization Act of 1970 are not new challenges for the Postal Service and therefore do not sufficiently explain such a dramatic reversal of financial fortune over this past fiscal year.

In addition, this committee is well aware that increased competition from private delivery companies and electronic communication alternatives such as the Internet, have led to substantial declines in the Service's first class mail volume.

These challenges will only grow over the next decade as broadband Internet access is extended to each residence. I hope that our witnesses will be able to inform this committee as to what action has been taken to better compete during this ever-evolving information age and how successful these actions have been.

For instance, what success has the Postal Service experienced with its e-commerce ventures, e-bill pay and online bill paying service and postal CS and electronic delivery service?

Finally, I am also concerned with some of the Postal Service's short and long-term strategies to address its financial frustrations. Today the media reports that the Postal Service Board of Governors has directed management to study the cost savings associated with reducing delivery service to 5 days a week.

I feel that this cost cutting approach will compromise the Postal Service commitment to universal service and its renowned reputation for customer service. We do think the number of delivery days will have a devastating impact on our economy and should in no way be pursued as a viable option.

Our reliable and affordable Postal Service is the hallmark of our Nation's infrastructure. In many neighborhoods, the post office plays a more active role in the fabric of the community than simply providing a facility for the dissemination of mail.

For instance, in my district, Garrett Park, the postmaster, the postal workers and the facility provide a healthy environment for local residents to meet, discuss issues of concern as they pick up their mail.

Whatever action is taken to resolve this financial crisis, we urge the Postal Service to preserve this, which has become the last remaining vestige of our great American culture.

I look forward to a bipartisan resolution of this. I thank you, Mr. Chairman.

Mr. BURTON. I thank the gentlelady.

Mr. Kucinich.

Mr. KUCINICH. Thank you very much. Mr. Chairman and members of the committee. The new 34-cent stamp, U.S. postal stamp, has a depiction of the Statue of Liberty. I think it is appropriate at this time in our deliberations about the Postal Service that we reflect on this stamp. Yes, it costs 34 cents and for that 34 cents people have reliable service, service that is accountable.

But more than that, this 34 cents and this stamp representing the Statue of Liberty speaks to the Postal Service in another way and that is that the Postal Service is connected to a basic freedom that the people of this country have, an ability to communicate with one another, that for 34 cents you can send a message across the country.

You don't have to own a computer. You can send a message to anywhere in the country. You can send a message from Cleveland, OH where I live, to a small town in Alaska, where only a few hundred people live. You can enable people to communicate with each other all around this country, and with the help of the Postal Service all over the world.

So, the U.S. Postal Service is really about freedom as much as it is about a service. The U.S. Postal Service has for countless years provided a universal service.

We have to step back and think about the purpose of government here. Government certainly exists to provide a service. We hope that government doesn't lose money in doing that, but sometimes that happens.

The Honorable Inspector General stood before one of our subcommittees recently and told us that the Department of Defense, which provides a service, cannot reconcile $2.3 trillion of accounting entries. We are talking about billions of dollars; they were talking about $2.3 trillion in accounting entries.

Would anyone suggest that we go to mercenaries as opposed to a Department of Defense in order to somehow have better service? No, we try to solve the problems that we have with the defense budget.

In Social Security, there were projections that Social Security was going to have a shortfall. The forces for privatization marched into Congress and said, "Well, now we must turn Social Security over to the stock market."

Would anyone suggest that today? Because everyone knew the truism that what goes up must come down. The market went down. People are saying prayers of thanksgiving that the money was not invested in the stock market.

Years ago, prior to the privatization of Medicare, we saw people getting service, the best service they could get, through the help of the Federal Government, the Medicare Program, but the privatization of Medicare through Medicare HMOs resulted in service going down and costs going up.

So, let us look at our Postal Service, the universal service, the government service, this public service which provides the same service for everyone, no matter what social or economic class, no matter whether they live in the city, the suburb or rural areas, a service which is accountable to this Congress. That is why we have this hearing here today. A service where someone can call us if they are not satisfied with us and a Member of Congress can find out why not.

We understand that there are individuals interested in privatization, who look at the Post Office not as a service to be rendered to the American people, but as an opportunity for making profit. We understand that. This is a great country that provides everyone an opportunity to make money. That is one of the great things about America.

But we are talking about a government service here. We are talking about a public responsibility that we have to make sure the American people can communicate to everyone.

So, as we move forward with these deliberations, let us not forget the excellent work that is being done by the men and women of the U.S. Postal Service. Let us be grateful for a service that we have had that has enabled Americans to communicate with each other.

Let us not forget the responsibility that we have to keep this service intact, to get it through its current financial difficulties and put it on the path where it can continue many more generations of serving the American people.

I thank the chairman for holding this hearing.

Mr. BURTON. Thank you, Mr. Kucinich.

Mr. Shays.

Mr. SHAYS. Thank you, Mr. Chairman.

Aging and anachronistic infrastructures pose an ominous threat to our economic well being. The President eloquently and passionately decries the human and fiscal cost of a public education system hobbled by low expectations and poor performance.

Energy consumers are just beginning to pay the price demanded by long-neglected energy production and conservation systems.

Interstate commerce is slower and most costly due to crumbling highways and railroad bridges.

Today, we discuss the decay besetting another national economic pipeline, the U.S. Postal Service, the USPS. With increased competition from economic, electronic mail, Faxes, the Internet and unregulated shippers, both foreign and domestic, the USPS appears to have entered a death spiral.

Cost controls and productivity increases remain limited and elusive. Required by law to raise rates to meet costs, each price increase drives more consumers away. It wasn't meant to be this way.

The current statutory structure reformed a 1970's Post Office unquestionably dominant and financially capable of providing universal service. Never intended to operate as a competitive enterprise,

the USPS we see today was designed to operate as a government service and entry-level employer.

But the world has changed much in three decades. The laws governing postal operations, human capital management and rate setting have not. As a result, today's Postal Service is a lumbering behemoth, a dinosaur forced to raise gazelles.

I am concerned that we as custodians of this national economic asset seem able only to tinker at the margins of the problem while the need for fundamental structural reform of the postal delivery system goes unmet.

I hope this hearing and those that will surely follow will move us toward a modern, efficient, and affordable postal system that will empower, not impede, national economic well being.

Thank you, Mr. Chairman.

[The prepared statement of Hon. Christopher Shays follows:]

Statement of Rep. Christopher Shays
April 4, 2001

Aging, anachronistic infrastructures pose an ominous threat to our economic well being. The president eloquently and passionately decries the human and fiscal costs of a public education system hobbled by low expectations and poor performance. Energy consumers are just beginning to pay the price demanded by long-neglected energy production and conservation system. Interstate commerce is slower and more costly due to crumbling highway and railroad bridges.

Today we discuss the decay besetting another national economic pipeline – the United States Postal Service.

With increased competition from electronic mail, faxes, the Internet and unregulated shippers, both foreign and domestic, the USPS appears to have entered a death spiral. Cost controls and productivity increases remain limited and elusive. Required by law to raise rates to meet costs, each price increase drives more customers away.

It wasn't meant to be this way. The current statutory structure "reformed" a 1970s post office unquestionably dominant and financially capable of providing universal service. Never intended to operate as a competitive enterprise, the USPS we see today was designed to operate as a government service and entry-level employer.

But the world has changed much in three decades. The laws governing postal operations, human capital management and rate setting have not. As a result, today's postal service is a lumbering behemoth, a mastodon forced to race gazelles.

I am concerned that we, as custodians of this national economic asset, seem able only to tinker at the margins of the problem while the need for fundamental structural reform of the postal delivery system goes unmet. I hope this hearing, and those that will surely follow, will move us toward a modern, efficient and affordable postal system that will empower, not impede, national economic well-being.

Mr. BURTON. Thank you, Mr. Shays.

Ms. Schakowsky.

Ms. SCHAKOWSKY. Thank you, Mr. Chairman. I want to welcome our distinguished witnesses here today to discuss the Postal Service's financial standing. I look forward to their testimony.

I would like to associate myself with Mr. Kucinich's remarks and I, too, want to acknowledge the importance and the generally excellent work of the Postal Service and the postal workers and letter carriers.

That being said, news of financial problems at the Postal Service concerns me and my constituents. Postal issues rate among the highest concerns of my constituents in the Chicago area.

There are over 1,200 postal employees working in the Ninth Congressional District. I am repeatedly informed by some letter carriers that our postal workers have to work long hours and sometimes double and triple shifts.

I hear that from constituents, that letter carriers work routes with which they are not familiar as substitutes leading to a less timely and accurate delivery of the mail.

Finally, Mr. Chairman, I am aware that the Postal Service has put a halt to all capital commitments. This decision has put a stop to two projects in my district, one in Skokie and one in Edgebrook. In Illinois, there are a total of 25 projects scheduled for 2001 that are currently on hold.

We all need to look very seriously at the reasons for halting these projects that could improve service to consumers and the various proposals for improving this system so that postal workers and postal customers are fairly treated and served.

I thank you, Mr. Chairman. I hope our GAO and Postal Service witnesses can address some of these issues for the committee today.

Mr. BURTON. Thank you, Ms. Schakowsky.

Mr. Otter.

Mr. OTTER. Thank you, Mr. Chairman. Mr. Chairman, I am going to shorten my remarks considerably so we have more time for questions. I think there is going to be a lot more to gain because of what the other Members have already said relative to the Postal Service today.

Mr. Chairman, a lack of accountability and oversight has given the U.S. Postal Service free rein to stray from its core mission of delivering the mail. The Postal Service has an unfair competitive advantage over the private sector because of its monopoly in revenues and in privileges.

As a result, private competitors and taxpayers are economically disadvantaged and the mail users are forced to pay ever-increasing stamp prices. The Postal Service brings in $50 billion every year from its monopoly on letter mail. Yet, it continues to seek other sources of revenue.

Recently the Postal Service lost $85 million, it was reported, to try to create new market ventures for things such as phone cards, videos, TV, tee shirts, baseball caps, stationary, greeting cards, ties, and also by selling advertising on its vehicles.

The Postal Service has maintained a $300 to $500 million annual advertising budget, despite the fact that it has no competition in

the first class monopoly. The Postal Service has used this advertising money to directly compete with companies who must necessarily operate in the private sector without all of the perks of a government agency like the Postal Service.

The U.S. Postal Service productivity has increased only 11 percent over the last three decades, even with all the advantages that we have seen in technology.

Time and again the Postal Service has said it will work on reducing costs and increasing productivity. Taking a look at one item, twice the Postal Service has paid for studies that were done for an annual cost for processing undeliverable as addressed mail.

It appears that the Postal Service has not significantly changed the way that it deals with undeliverable as addressed mail because it continues to lose $1.5 billion annually on that alone.

From 1995 to 1999, the Postal Service has budgeted $8.5 billion on capital investment in automation and mechanization equipment. However, it only spent $5.2 billion. The Postal Service portrays the image that it is not concerned with productivity or enhancing their efficiency. This is of great concern. Yet they still want another postal rate increase.

Mr. Chairman and members of the committee, with the projections of this year's deficit at $2.3 billion, the Postal Service needs to refocus their mission on delivering the first class mail. Stop using taxpayer money to compete with the private sector and start making sound business decisions and ultimately need a thorough review by this committee and this Congress.

Thank you, Mr. Chairman.

Mr. BARR [assuming Chair]. I thank the gentleman.

The chair recognizes the gentleman from Missouri, Mr. Clay, for 5 minutes.

Mr. CLAY. I will forego any opening statement and will wait for questions.

Mr. BARR. Thank you. The gentleman yields back.

The gentleman from Virginia, Mr. Schrock, is recognized if he has an opening statement.

Mr. SCHROCK. Thank you, Mr. Chairman. I really do not have an opening statement except to say that I agree with almost everything I have heard from my colleagues here. At the appropriate time and after we have heard from our witnesses, I, too, have five or six questions I would like to ask.

Thank you, Mr. Chairman.

Mr. BARR. Thank you, sir.

The chair recognizes the gentleman from Maryland, Mr. Cummings.

Mr. CUMMINGS. Thank you very much, Mr. Chairman. I am glad we are holding this hearing on the Postal Service's current financial position and the impact postal loss projections will have on the ability of the agency to fulfill a statutory mission under the Postal Reorganization Act of 1970.

Before I go on, I just want to thank all the men and women of the Postal Service who deliver the mail 6 days a week and do a very good job in my district and, I am sure, across the Nation.

We all want a stable and strong Postal Service. The Postal Service processes about 208 billion pieces of mail a year or about 680 million pieces of mail every day.

Additionally, the Postal Service delivers mail to over 5,600 new addresses a day. It generates $65 billion in operating revenues and operates 38,000 Post Offices, stations and branches.

For several years postal reform has been a big issue before this committee and Congress. In the 106th Congress, Congressman McHugh introduced H.R. 22, the Postal Modernization Act. And Congressman Waxman introduced H.R. 2535, the Postal Enhancement Act.

The Subcommittee on the Postal Service held hearings on both of these reform items. There is widespread agreement that reform is needed for the Postal Service. This committee has the oversight responsibility to explore exactly what type of reform is needed.

The Postal Service must develop a long-range strategic plan that truly assesses postal reform. I look forward to hearing the testimony of our witnesses, David M. Walker, William J. Henderson, and S. David Fineman. I hope they will be able to help us examine postal losses and revenues, postal rate increases, deficit and mail volume projections, competition, information technology and budget forecasting.

Thank you very much, Mr. Chairman.

Mr. BARR. I thank the gentleman.

The chair recognizes the gentleman from California, Mr. Horn.

Mr. HORN. Thank you, Mr. Chairman. I know we need to get to the excellent witnesses. But I just want to mention a few things. One is, I don't think any of us have any problem with the letter carriers and clerks we know. I have spent 30 years in Long Beach. I have never had a problem with anybody behind a counter or anybody walking the mail. That started when I was a little kid on a farm. Mr. Cagney, the rural carrier, was not only a newspaper for the rest of the county, but also sent our mail around the world.

But what I do have a problem with is some of the supervisors and some of the central operations here in Washington.

Let me give you an example. I talked to 100 injured Federal workers one afternoon. Sixty of them came out of the Postal Service. One of them, after the truck had fallen on his foot or something, he asked for the form to file under the Federal Workers' Compensation law. The Postal supervisor wouldn't give him that.

Why? Because that supervisor, is performance is that you don't have these things happening. Apparently, that is the way the system works. Well, I think it is a lousy way to work when it does that. Until the supervisors start helping people and the central Postal administration here starts thinking about people, we are never going to get anywhere with the Postal Service.

I guess when I heard that Postmaster General Runyon had $100,000 spent on his farewell dinner and all, I must say, I get a little upset, as one who cares about the taxpayers' money, to say the least, and any agency's money.

We finally got a Post Office person in Long Beach that started things moving. His name was Mr. Shapiro. He will probably be punished now that I have said that. After all, somebody in the line is helping people. What do you know?

The fact is that the city of Long Beach, half a million people, surrounds the city of Signal Hill with 10,000 people. We want a zip code for them. Why? Because all their insurance rates go up when they use the zip codes coming from the inner city of Long Beach, CA.

I think that is just outrageous, not to get a decent zip code for the city. Now, they can make laughter down there and all the rest of it. But I would say the Post Office, when it starts acting like a humane institution, I will have more respect for it. But right now, with the management of the Postal Department, I am not happy about it.

I want them to know about it and get off their seats and start getting something done.

So, I thank you, Mr. Chairman, and I look forward to the witnesses.

Mr. BURTON [resuming Chair]. Thank you, Mr. Horn.

Ms. Norton.

Ms. NORTON. Thank you, Mr. Chairman. I have just a few remarks.

I hope we are not at another low point for the Post Office. We encountered such a point in the early 1990's when there was a great deal of oversight from this committee. We may recall that mail delivery times around the country were terrible, none worse than here in Washington, DC, where official mail as well as residential mail was delivered at times that were among the worst in the country.

To their credit, the Post Office improved extraordinarily in delivery mail times. I am not sure what it is today, but there was cosmic improvement after some oversight here and management focused on the problem.

That leads me to believe that if management focuses on the problems that have arisen today, they, too, can be solved. I don't agree with my friends on the other side that the Post Office can still deliver mail at low rates and not become more market oriented.

Certainly they are going to have to compete with the private sector if they are going to keep the cost of mail down for the average person who must depend on the mail. They, unlike Members of Congress, except for the frank, which is paid for, do not communicate by FAX or e-mail or any of the other gadgets.

We cannot have it both ways. In fact, the Post Office was criticized for not becoming more competitive. Well, they have gone and done some of that. I am not sure they have done enough of it. I am not worried about the private sector. We have extraordinary privatized services and, of course, they don't have the same burden of keeping the cost of the average letter down the way we insist, justifiably so, that the Postal Service do.

I do want to raise one concern that I have. There is a pejorative term that has come into our language, "going postal." This comes from the fact that there have been a fair number of violent incidents involving Postal workers.

The question has been raised over and over again about the stress that is associated with mechanization and automation of services and perhaps with improved management that forces workers into patterns that are more rigid than before.

I am very concerned with how labor relations are handled with the increasing pressure on the Post Office to deliver mail at lower costs and compete with the private sector.

I went out with a Postal worker here in the District of Columbia. I asked the postmaster to just give me a worker to go with at random. I was astounded by what I saw. He was often the only person that residents saw. He had an extraordinary relationship with his neighborhood. It was in Adams Morgan. He climbed steps over and over again. He must have been in the best shape.

I want to learn more today about how management is coping with its cost problems and I want to learn more today about how management is coping with its labor management problems.

Thank you, Mr. Chairman.

Mr. BURTON. I thank the gentlelady.

Mr. Walker, I think we are ready now to have you sworn.

[Witness sworn.]

Mr. BURTON. I assume you have an opening statement.

STATEMENT OF DAVID M. WALKER, COMPTROLLER GENERAL OF THE UNITED STATES, GENERAL ACCOUNTING OFFICE, ACCOMPANIED BY BERNARD UNGAR, DIRECTOR, PHYSICAL INFRASTRUCTURE TEAM, U.S. GENERAL ACCOUNTING OFFICE

Mr. WALKER. I do have an opening statement. As you have already noted, the entire statement, I know, will be in the record. If I could summarize it now, I would appreciate it.

I am pleased to be here today to participate in this committee's hearing on the U.S. Postal Service. The Postal Service plays a vital role in our economy. It links people together and helps to bridge the growing digital divide.

Overall, the Service, however, faces major challenges that collectively call for a structural transformation in order for it to remain viable in the 21st century.

The last major reform of the Postal Service occurred in 1970. The world has changed fundamentally since 1970. It will change even more in the coming 31 years.

The Service's projected financial losses have increased significantly during the past 4 months. Over the past 2 years we have raised concerns about a range of financial, operational and human capital challenges that threaten the Postal Service's ability to continue to provide affordable, high quality and universal postal service on a self-financing basis.

Moreover, the Service's financial outlook has worsened more quickly than expected. It is not clear how the Service will address its mounting financial difficulties and other challenges. These challenges include, as chart one will show, which is also slide one in your packet: The Service's net income has declined over the past 5 years. The Service currently projects a fiscal 2001 deficit of between $2 billion and $3 billion, up from a projected loss of $480 million just 4 months ago.

It is my understanding that the two primary reasons for the change in the projection were No. 1, a postal rate increase that was $800 million lower than they expected to get, and No. 2, a decline in the economy and the resulting effect on volume.

In my opinion, Mr. Chairman, as the Social Security and Medicare trustees do, and I was a trustee of Social Security and Medicare for 5 years, in general I think it is not a good idea to project rate increases unless you know for a fact that they are going to occur.

Therefore, I think one of the reasons for the variance is because there was a projected rate increase that in fact had not been approved. That is $800 million. That is a lot of money.

Further, in fiscal 2002, the Postal Service estimates that its deficit will be in the $2.5 to $3.5 billion range, assuming no further rate increases.

If I can refer you now to chart two, costs have been growing at a faster rate than revenues over recent years.

Now we will go to chart three, which is figure five, I believe. The Service has experienced a net increase in outstanding debt at the end of each fiscal year since 1997. Its total outstanding debt reached $9.3 billion at the end of fiscal year 2000.

Service official expects that they could reach the $15 billion statutory debt limit by the end of fiscal year 2002, assuming no additional increases in postal rates. In addition, the Service does not have a plan to reduce its debt burden. Depending on future events, the Service may face a cash shortage in fiscal years 2002 or 2003.

The next chart, which would be slide No. 6, I believe, shows the Service faces increasing competition from both domestic and foreign-based entities. It also expects certain electronic diversion of existing mail will be caused by greater use of the Internet that will cause a substantial decline in first class mail volume in the next decade, and thus place the Service under, in its own words, "extreme financial pressure."

Although the Service has plans to cut its costs by $2.5 billion by 2003 through increasing productivity and improving human capital programs, it has historically had great difficulty in achieving its planned outcome.

The Service has also had periodic conflicts with some of its key stakeholders, including the postal unions and the Postal Rate Commission. We have noted longstanding labor-management relations problems that have hindered improvement efforts, including the fact that three major labor agreements expired in November 2000, which collectively cover over a half a million of the Postal Service's work force.

In addition, the Postal Service and the Postal Rate Commission have had longstanding disagreements concerning pricing decisions, and they continue. The Service is subject to statutory and other restrictions that seem to limit its ability to transform itself.

A lot of these provisions were put in place in the last reform in the 1970's and some preexist that.

Finally, two key leadership positions need to be filled related to critical postal operations and rate setting, namely the Postmaster General. Postmaster General Henderson has announced that he will be leaving next month. In addition, former Chairman Ed Gleiman is no longer chairman. He resigned recently.

Based upon all this information, Mr. Chairman, we believe that the Service's deteriorating financial situation and the contributing structural challenges call for prompt aggressive action, particularly

in the area of cutting costs and improving productivity, including considering existing legislative provisions that serve to limit the ability of the Postal Service to transform itself.

Accordingly, we are adding the Postal Service's transformation efforts to our high-risk list, effective immediately, so that we and others can focus on its financial, operational, and human capital challenges before the situation reaches truly crisis proportions where the options for action may be more limited.

Let me emphasize, we are not putting the entire Postal Service on our high-risk list. Management and employees at the Postal Service do some things right, and in fact on-time delivery has improved significantly over the last several years.

Rather, we are focusing on the challenges associated with the transformation effort and the related obstacles that must be addressed in order to enable the Postal Service to truly transform itself for the 21st century.

In our view, we believe that the following actions need to be taken. First, the Postal Service should develop a comprehensive plan in conjunction with Congress and its other key stakeholders, such as the postal unions and management associations, customers, and the Postal Rate Commission, that would identify the administrative and legislative actions needed to address the Service's financial, operational and human capital challenges and that would establish a timeframe and specify key milestones for achieving desired results.

Second, the Service should provide summary financial reports to the Congress and the public on a quarterly basis. These reports should present sufficiently detailed information for the stakeholders to understand the Service's current and future projected financial condition and how its outlook may have changed since the previous quarter and its progress toward achieving the desired results specified in its comprehensive plan.

Last, but certainly not least, GAO will work with the Congress and the Service to identify and analyze possible improvement options and will continue to analyze and report to the Congress on the Service's ongoing financial condition.

In consultation with other postal stakeholders, including the Postal Service Office of the Inspector General, postal unions and management associations, the Postal Rate Commission and customers, GAO will review the Service's financial results and future outlook, progress in cost-cutting and productivity efforts, other countries' experiences in dealing with related challenges and the options for addressing the Service's short-term and long-range challenges.

Mr. Chairman, that concludes my prepared remarks. I would be more than happy to answer any questions that you or any other members of the committee may have.

[The prepared statement of Mr. Walker follows:]

United States General Accounting Office

GAO

Testimony

Before the Committee on Government Reform
House of Representatives

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U.S. POSTAL SERVICE

Transformation Challenges Present Significant Risks

Statement by David M. Walker
Comptroller General of the United States

GAO-01-598T

Mr. Chairman and Members of the Committee:

We are pleased to be here today to participate in the Committee's hearing on the U.S. Postal Service (the Service). Overall, the Service faces major challenges that collectively call for a structural transformation if it is to remain viable in the 21st century. In my testimony, I will briefly review the Service's growing financial, operational, and human capital challenges in an increasingly competitive environment; discuss the Service's financial outlook; and make suggestions on what needs to be done to address the challenges facing the Service.

The Service's projected financial losses have increased significantly during the past 4 months. Over the past 2 years we have raised concerns about a range of financial, operational, and human capital challenges that threaten the Postal Service's ability to continue to provide affordable, high-quality universal postal service on a self-financing basis. Moreover, the Service's financial outlook has worsened more quickly than expected, and it is not clear how the Service will address its mounting financial difficulties and other challenges. These challenges include:

- The Service's net income has declined over the past 5 years, and the Service currently projects a fiscal year 2001 deficit in the $2 billion to $3 billion range, up from a projected loss of $480 million just 4 months ago. About $1.8 billion in projected losses are based on results for the first 2 quarters and revised estimates for losses in the last 2 quarters of fiscal year 2001. Based upon its judgment, the Service is also projecting that the slowing economy will further lower net income by $300 million to $1.3 billion. Further, in fiscal year 2002, the Service estimates that its deficit will be in the $2.5 billion to $3.5 billion range, assuming no further increases to postal rates.
- The Service has experienced a net increase in outstanding debt at the end of each fiscal year since 1997, and its total outstanding debt reached $9.3 billion at the end of fiscal year 2000. Service officials expect the Service could reach its $15 billion statutory debt limit by the end of fiscal year 2002, assuming no additional increases in postal rates. At the same time, the Service has curtailed capital investment to conserve cash in fiscal year 2001. In addition, the Service has no plan to reduce its debt. Depending on future events, the Service may face a cash shortage in fiscal years 2002 and/or 2003.
- The Service faces increasing competition from both domestic and foreign-based entities. It also expects electronic diversion—such as greater use of the Internet—to cause substantial declines in First-Class Mail volume in the next decade and thus place the Service under "extreme financial pressure."
- Although the Service has taken steps and plans to cut costs by $2.5 billion by 2003, increase productivity, and improve human capital programs, it has historically had great difficulty achieving desired results in these areas. For example, numerous reports, including some by us and the Postal Service Office of Inspector General (OIG), have noted inefficiencies in the postal system and difficulties the Service has had in realizing opportunities for savings.
- The Service has also had periodic conflicts with some of its key stakeholders including postal unions and the Postal Rate Commission. We have noted longstanding labor-management relations problems that have hindered improvement efforts, including three labor agreements that expired in November 2000. In addition, the Postal Service and the Postal Rate Commission have had longstanding disagreements concerning pricing decisions.

- The Service is subject to several statutory and other restrictions that serve to limit its transformational efforts (e.g., binding arbitration requirement, a cost-based rate-setting process, and facility closure restrictions).
- Finally, two key leadership positions need to be filled relating to postal operations and rate setting (Postmaster General and Chairman of the Postal Rate Commission.)

We believe that the Service's deteriorating financial situation calls for prompt, aggressive action, particularly in the areas of cutting costs and improving productivity. Accordingly, we are adding the Postal Service's transformational efforts and long-term outlook to our High-Risk List, effective immediately, so that we and others can focus on its financial, operational, and human capital challenges before the situation escalates into a crisis where the options for action may be more limited. In this regard, we believe the following actions need to be taken:

- The Service should develop a comprehensive plan, in conjunction with Congress and other stakeholders, such as the postal unions and management associations, customers, and the Postal Rate Commission, that would identify the actions needed to address the Service's financial, operational, and human capital challenges and establish a timeframe and specify key milestones for achieving positive results.

- The Service should provide summary financial reports to Congress and the public on a quarterly basis. These reports should present sufficiently detailed information for stakeholders to understand the Service's current and projected financial condition, how its outlook may have changed since the previous quarter, and its progress toward achieving the desired results specified in its comprehensive plan.

- GAO will work with Congress and the Service to help identify improvement options and will continue to analyze and report to Congress on the Service's ongoing financial condition. In consultation with other postal stakeholders including the Postal Service Office of Inspector General, postal unions and management associations, the Postal Rate Commission, and customers, we will review the Service's financial results and future outlook, progress on cost-cutting and productivity efforts, other countries' experiences, and options for addressing the Service's short-term and long-term challenges.

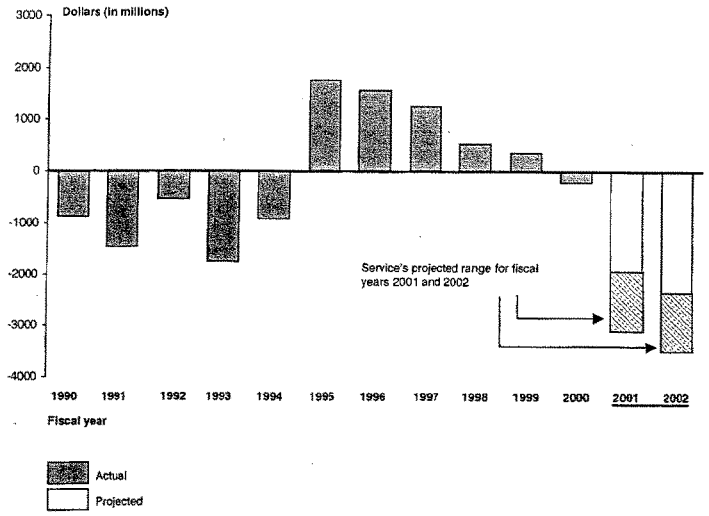
Historical Perspective on the Service's Financial Outlook

The $2 billion to $3 billion deficits estimated by the Service would be unprecedented, although the Service did experience financial difficulties in the early 1990s. The Service's financial position in the early 1990s was adversely affected by the 1990-1991 recession. Also, in 1990, legislation made the Service responsible for funding all health benefits and COLAs for its retirees since July 1, 1971. The Service reported that its financial turnaround in the mid-1990s was aided by rising mail volume, a rate increase that averaged approximately 10 percent in 1995, and a "moderate" increase in expenses. In addition, in the late 1990s, the Service improved the timely delivery of First-Class Mail.

As figure 1 shows, the Service's financial turnaround occurred in fiscal year 1995. The Service raised the price of the First-Class stamp from 29 cents to 32 cents on January 1, 1995. The Service's net income has declined in every year since fiscal year 1995 despite general rate

increases that raised the First-Class stamp price to 33 cents on January 10, 1999, and to 34 cents on January 7, 2001.

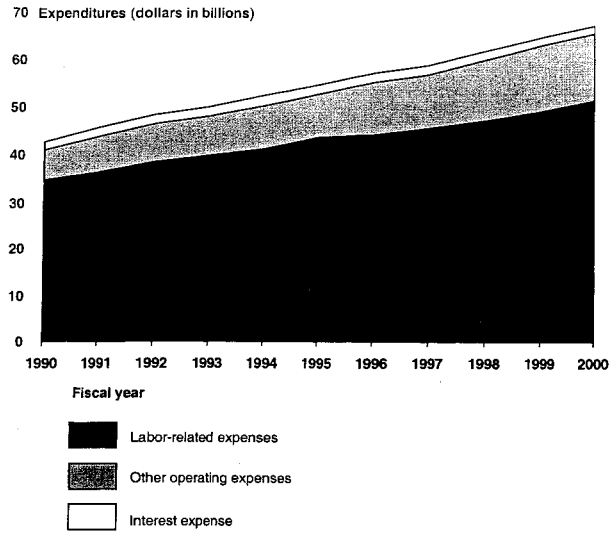
Figure 1: Postal Service Net Income From Fiscal Year 1990 Through 2002



Source: U.S. Postal Service.

One reason for the declining net income has been continued growth in postal expenses (see fig. 2). The Service's delivery network continues to grow at a rate close to 2 million new household and business deliveries each year. Labor-related expenses continue to account for more than three-quarters of the Service's total operating expenses, despite multibillion-dollar expenditures for automation. Other operating expenses have also grown.

Figure 2: Trends in Postal Service Expenses From Fiscal Year 1990 Through 2000



Source: U.S. Postal Service.

The Service Faces Growing Challenges

The Service faces growing challenges in an increasingly competitive environment as it seeks to fulfill its mission: bind the nation together through the correspondence of the people; provide access in all communities; offer prompt, reliable, and efficient postal services at uniform prices; and be self-supporting and break even financially over time. In October 1999, we testified that the Service might be nearing the end of an era and confronting increasing challenges from competition, notably from private delivery companies and electronic communication alternatives such as the Internet.[1] The Service told us that it expected First-Class Mail volume to decline substantially in the next decade, assuming that the diversion of mail to electronic communications alternatives would accelerate in a new and vastly different environment in which the Service would be required to operate.

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

In September 2000, we testified that the Service continued to face an uncertain future in an increasingly competitive environment.[2] We reported that the Service believed that growth in its core business had already been negatively affected by the rapid growth of the Internet, electronic communications, and electronic commerce. We noted that 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 services that bind the nation together. We also reported that the Service had experienced increasing difficulties in meeting its goal of $100 million in net income for fiscal year 2000. Based on its annual financial statements, the Service experienced a net loss of $199 million for fiscal year 2000, its first deficit since fiscal year 1994.

In January 2001, we reported to Congress on the potential consequences if the Service incurred a series of large deficits. These could include increases in postal rates, declines in service quality, consolidation or closure of some facilities, or reconsideration of postal operations or even the scope of postal services.[3] We also noted that fundamental issues concerning the Postal Service's role and authority have been raised in Congress, and various stakeholders have called for changing its legal and regulatory framework. We concluded that to be successful, the Service would need to address formidable performance and accountability challenges in five key areas, which can be posed as the following questions:

1. Can the Postal Service remain self-supporting while providing affordable, high-quality universal service?
2. Can the Service become more efficient by controlling its costs and improving productivity?
3. How will the Service address critical human capital issues, such as maintaining continuity and service in the face of the impending retirement of many postal employees, rapidly rising retirement and other personnel-related costs, and persistent labor-management problems?
4. Does the Service have reliable performance and cost information to effectively manage postal operations, identify inefficiencies, and track progress toward realizing anticipated cost savings?
5. What changes may be needed in the current legal and regulatory framework governing the Postal Service's role and mission so that it can remain self-supporting and provide affordable universal service in an increasingly competitive environment?

In the balance of my testimony today, I will focus on the first three questions. First, I will discuss the Service's short-term financial outlook and assess the Service's increasingly dire financial projections for this fiscal year. Second, I will discuss the Service's financial trends and issues relating to its cash and debt position. Third, I will focus on selected key long-term challenges, including human capital challenges, and conclude with some specific suggestions for action.

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[2] *U.S. Postal Service: Sustained Attention to Challenges Remains Critical* (GAO/T-GGD-00-206, Sept. 19, 2000).

[3] *Major Management Challenges and Program Risks: U.S. Postal Service* (GAO-01-262, Jan. 2001).

The Service's Short-term Financial Outlook Has Deteriorated

The Service is projecting significant losses over the next 2 years, although the full extent of the losses is uncertain. The Service currently estimates that its fiscal year 2001 deficit will range from roughly $2 billion to $3 billion—a sum that far exceeds the $480 million deficit built into the Service's budget that was approved last November. About $1.8 billion of this projected deficit is based on reported losses in the first 2 quarters and revised estimates for losses in the last 2 quarters. Depending on the economic situation for the rest of fiscal year 2001, the Service believes that losses could be much higher. Further, in fiscal year 2002, the Service estimates that its deficit will be in the $2.5 billion to $3.5 billion range, assuming no further increases to postal rates.

An important caveat: Our current assessment of the Service's financial outlook for this fiscal year is based on a preliminary review of the financial data and projections that the Service recently provided to us and on interviews with Service officials, including the Chief Financial Officer. The Service's financial situation is complex, and we are still assessing the validity of key data and assumptions that support the Service's financial projections. In addition, the Service is in the process of updating some of its key projections, such as projections of its revenues for the second half of this fiscal year. We will continue to review the Service's financial condition and will report again to Congress on this matter.

Factors Leading to the Service's Expected Deficit in Fiscal Year 2001

To understand the factors affecting the Service's financial outlook for this fiscal year, I will discuss where the Service stands today with results from the first 2 quarters and what it expects to happen during the last 2 quarters of the year. I will also discuss how the Service's net income projections have changed since the beginning of the fiscal year according to a series of adjustments the Service has made to its projected revenue and expenses. (See fig. 3.) Finally, I will discuss other factors that have not been included in the Service's projections but could affect the Service's financial results for this year, such as the Service's ability to achieve budgeted savings and revenues from new initiatives.

Figure 3: Changes in the Postal Service's Financial Outlook for Fiscal Year 2001

	Budgeted	Current
Reported Net Income: Quarters 1 and 2	$200 M	-$260 M
Originally Budgeted Net Income: Quarters 3 and 4	-$680 M	-$680 M
Expense Adjustments to Net Income: Quarters 3 and 4		-$320 M
Revenue Adjustments to Net Income: Quarters 3 and 4		-$500 M
Subtotal		*-$1.8 B*
Other Revenue Adjustments to Net Income: Soft Economy-Quarters 3 and 4		-$300 M to -$1.3 B
Net Income	-$480 M	-$2.1 to -3.1B
FY 2001 Revised Deficit $2.1 to $3.1B		

Legend: Dollars in millions (M), billions (B).
Source: GAO presentation based on U.S. Postal Service estimates, which are subject to change.

The Service's financial outlook for fiscal year 2001 can be divided into the following categories: (1) $260 million in reported losses for the first half of the fiscal year, (2) $680 million in budgeted losses for the balance of the fiscal year, (3) $320 million in expenses higher than estimated for the last 2 quarters, (4) $500 million in revenues lower than budgeted for the last 2 quarters due to lower-than-requested increases in postal rates, and (5) $300 million to $1.3 billion in revenues lower than budgeted for the last 2 quarters due to the slowing economy and its impact on mail volume and revenues. The uncertainty of the impact of the economy for the remainder of the fiscal year is the largest single factor in the Service's projections that may impact its expected losses for fiscal year 2001, and the estimated range is based on the Service's judgment.

Reported Losses for the First Half of Fiscal Year 2001

As figure 3 shows, the Service reported that its loss for the first 2 quarters of this fiscal year was about $260 million. This reported amount is not audited and is subject to change. It is important to note that historically, the Service's financial performance tends to be stronger in the first part of the fiscal year, which includes the busy holiday mailing season. The $260 million loss during its typically strongest earnings period is a further sign of the Service's financial difficulties. The Service had budgeted for $200 million in net income for the first half of the fiscal year; so, thus far it is running $460 million behind its budget targets. Further, the Service achieved nearly $1 billion in net income in the first half of last fiscal year – a year in which it ended with a $199 million loss.

Additional Losses Built into the Service's Fiscal Year 2001 Budget

In its fiscal year 2001 budget, the Service estimated that it would incur a $680 million deficit for the last 2 quarters of the fiscal year. When this amount is added to the $260 million deficit incurred in the first half of the fiscal year, the Service would lose nearly $1 billion in fiscal year 2001. This estimated loss does not include a number of developments that could have a negative impact on the Service's net income this year, which are detailed below.

Additional Unbudgeted Expenses

The Service currently projects that its expenses for the remaining 2 quarters of this fiscal year will be $320 million greater than budgeted, and gave us supporting information for these estimated expenses. For example, the Service told us that it is experiencing greater transportation expenses because of increases in fuel costs and cost passthroughs from its transportation contractors, among other factors. International mail expenses are also expected to be higher than budgeted because of recent increases in "terminal dues" paid to foreign postal administrations to deliver outbound U.S. international mail. Workers' compensation expenses are also expected to be greater than budgeted and to reach $1.1 billion for the full fiscal year – a significant increase from last year and the late 1990s.

Additional Revenue Shortfalls Relating to Postal Rates and New Revenue Initiatives

The Service projected revenues for the last 2 quarters of fiscal year 2001 to be $500 million below its budgeted targets due to the gap between the requested rates and those implemented in January. The Service's budget for fiscal year 2001 assumed that the Service would receive the full increase in postal rates that it had requested in the 2000 rate case. However, the Postal Rate Commission recommended a rate increase that averaged 4.6 percent—more than 2 percent lower than the requested amount. These rates were put into effect this January and included a 1-cent increase in the price of a First-Class stamp to 34 cents.

Additional Revenue Shortfalls Attributed to the Slowing Economy

The Service further lowered its revenue projections for the second half of fiscal year 2001 by $300 million to $1.3 billion on the basis of the Service's judgment of a "continued soft economy" and the resulting negative impact on mail volume and revenues. The $1 billion range reflects the Service's uncertainty associated with the length and severity of the economic slowdown and its impact on postal revenues. The Service told us it is in the process of updating its mail volume and revenue forecasts for the rest of fiscal year 2001.

Other Factors May Add to the Service's Deficit for Fiscal Year 2001

The Service's expenses could be higher than it currently estimates because it is not on track to achieve some cost-reduction targets. For example:

- The Service planned to decrease its work hours by 1.5 percent from last year's level—which would translate into a reduction of 13,200 work years for the full fiscal year. Although the

Service reported that work hours declined in the first 2 quarters of fiscal year 2001 compared to the first 2 quarters of last fiscal year, the decline was only about half of its target.

- The Service planned for decreasing overtime work hours by about 6 percent in the first 2 quarters from last year's level. However, the Service reported that overtime increased in the first 2 quarters and is running about 13 percent higher than the budgeted targets so far this fiscal year, although some recent progress has been made in reducing overtime.
- The Service's planned reductions in total work hours assume efficiency gains in most aspects of its operations. An estimated 60 percent of the savings is related to greater efficiencies in handling flat mail, such as catalogs and periodicals, and from machines sorting mail for carriers in the sequence it is to be delivered. However, these budgeted savings will be difficult for the Service to fully realize. First, Service officials told us that it takes three to six employees to prepare flat mail to be loaded into its new sorting machines, thus diminishing cost efficiency, although the Service noted it is working with mailers to address this issue. Second, the Service has reported that carrier costs exceeded budgeted targets by $130 million for the first 2 quarters of this fiscal year. Carrier costs were reportedly affected by greater-than-expected volumes of low-margin advertising mail; the worst winter weather in a decade; and difficulty in finding and retaining replacements for rural carriers, which resulted in higher overtime costs.
- The Service expected efficiency gains to result in reductions through attrition. The number of career employees has been declining, while at the same time there have been increases in the number of non-career workers. The Service has said that it might be necessary to offer voluntary early retirements in some cases, or possibly move into isolated reductions-in-force.

Strategies to Improve Net Income

To improve its net income situation in fiscal year 2001 and 2002, the Service will need to increase revenues and/or cut costs and improve productivity. Adding to this challenge will be maintaining the quality of service. The Service is currently making efforts in these areas. The following is a brief discussion of the Service's short-term potential for making further progress.

- Cut operating costs and improve productivity: We have repeatedly emphasized that this should be a priority area for the Service; however, progress historically has been difficult to achieve. Service officials have emphasized some key barriers, such as restrictions on closing unprofitable post offices or limited flexibility in changing workforce deployment, have contributed to the difficulty of making progress in this area. The Service's overall productivity has increased only about 11 percent in the past 3 decades despite vast changes in automation and information technology. The Service has recognized that it needs to make progress in cutting its costs and improving productivity and is currently taking steps to do so. Last week, the Deputy Postmaster General announced that the Service is committed to cutting costs by $2.5 billion by 2003. He said that over the next 5 years, the Service plans to cut 75,000 work years, reduce administrative costs by 25 percent, and cut transportation costs by 10 percent. The Service has not yet specified, however, how these cuts would be achieved. The Service improved productivity in fiscal year 2000 by 2.5 percent and its budget for fiscal year 2001 calls for a 0.7 percent productivity increase. Service officials are also planning for a 2-percent increase in fiscal year 2002, and a 1-percent increase the year

after that—a set of positive productivity increases over 4 consecutive years that they noted would be unprecedented.

- Generate more revenues from new products and services: We believe that it will be difficult for the Service to generate significant revenues from new products and services in the next few years. Historically, as our 1998 report showed, the Service's new product and service initiatives underway during the mid-1990s generally were not profitable.[4] Further, the Service's 5-Year Strategic Plan for fiscal years 2001 through 2005, dated September 30, 2000, stated that no significant new revenue is forecast from new products and services during the next 5 years. The Service has not achieved its revenue targets from its new initiatives for the first half of this fiscal year. Recently, the Service has made downward revisions in its projected revenues from its new revenue initiatives for the second half of fiscal year 2001.

- Raise postal rates: To the extent that operating costs are not contained or reduced, or revenues are not generated from new products and services, the Service will likely need to raise rates to maintain service and to meet its break-even mandate, at least in the short term. The Deputy Postmaster General recently said that the Service may not be able to avoid raising postal rates; but he added that at present, the Service does not know the timing, size, or details of the next rate case. Some stakeholders have expressed strong concern that the Service could request a rate increase of as much as 10 to 15 percent in the near future. However, the Service has also said that "This [option] would worsen the competitive position of the Postal Service and cause substantial disruption to key customer segments with little or no minimal direct substitutes for postal services, such as the publishing industry." In the long run, raising rates may drive postal customers to increase their use of other alternatives, thereby affecting mail volumes and revenues.

The Service Has Growing Cash Flow and Debt Challenges

The amount that the Service borrows on an annual basis is largely determined by the difference between its cash flows from operations and the amount it spends on capital investments. As shown in figure 4, the Service's cash flows from operations are typically significantly greater than its net income. The primary reason for the difference is because net income is calculated on the accrual basis of accounting[5] and includes accrued expenses, such as depreciation expense, that do not use cash.

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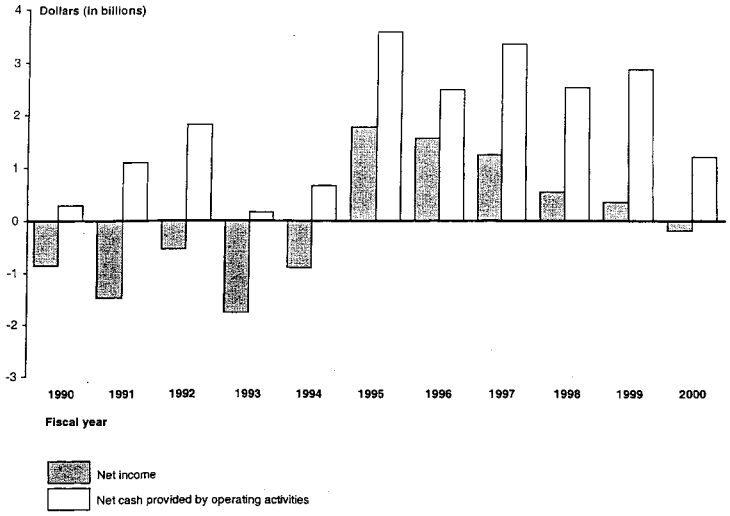
[4] *U.S. Postal Service: Development and Inventory of New Products (GAO/GGD-99-15,Nov. 24, 1998).*

[5] Under the accrual basis of accounting, revenues are recorded when earned and expenses are recorded when incurred, even if these activities are not concurrent with the related receipt or outlay of cash.

Figure 4: Postal Service Net Income and Cash Flows From Operations

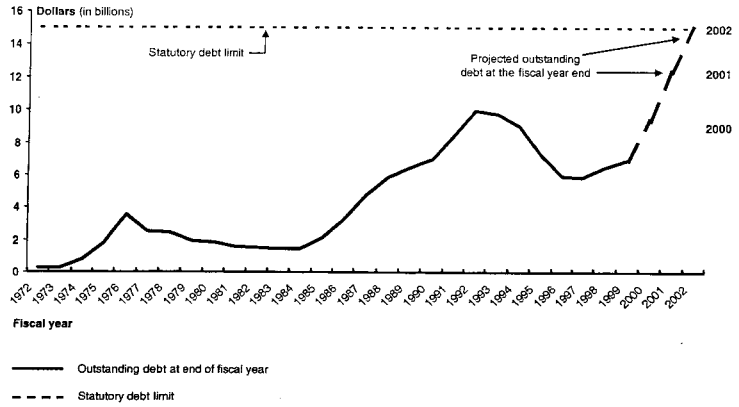


Source: U.S. Postal Service.

Beginning in 1998, the Service's cash outlays for capital expenditures exceeded its cash flows from operations. The Service's debt increased from $5.9 billion at the end of fiscal year 1997 to $9.3 billion at September 30, 2000. The Service anticipates that its projected operating deficit for the full fiscal year 2001 will weaken its cash flows from operations. By way of background, the Service has a statutory borrowing limit of $15 billion and also has an annual limit of increasing its outstanding obligations by $3 billion (that includes a $2 billion limit for capital improvements and a $1 billion limit to defray operating expenses).

Service officials told us that assuming the Service's financial outlook is on target and there are no further changes in postal rates in fiscal years 2001 or 2002, the Service may reach its $15 billion statutory borrowing limit by September 30, 2002 (see fig. 5). Under this scenario, the Service would have no additional borrowing authority at the beginning of fiscal year 2003. Once the Service reaches its statutory borrowing limit, it can pay its bills only through its cash on hand plus additional cash generated from operations until outstanding debt declines. The Service typically generates a cash surplus in the first part of the fiscal year. However, depending on the Service's income and cash from operations, the Service may face a cash shortage in fiscal years 2002 and/or 2003.

Figure 5: Trends in Postal Service Debt



Source: U.S. Postal Service

To avoid a cash shortage during fiscal year 2001, the Service has placed a freeze on capital commitments that will affect more than 800 facility projects. Last year the Service had planned capital commitments of $3.6 billion for fiscal year 2001, but Service officials recently announced reductions in this area and told us they now anticipate a reduction to $2 billion in capital commitments this fiscal year. Preliminary budget plans for fiscal year 2002 would reduce capital investment from $3.7 billion to $2.4 billion. However, reducing needed capital investments serves only to defer capital improvements and associated efficiency gains.

Major Long-Term Performance Challenges Facing the Service

As difficult as the Service's short-term financial outlook may be, we are also concerned about its long-term prospects, given the trends toward increasing competition and its implications for postal revenues, coupled with continued upward pressure on postal costs, and human capital challenges. Therefore, unless the Service makes much more rapid progress in cutting costs and improving productivity, it will face increasing difficulty maintaining its position as a self-supporting provider of universal postal service at reasonable rates. The Postal Service and postal stakeholders have been debating for years whether major changes are needed in the legal and regulatory framework governing the Postal Service, but reaching consensus among the diverse stakeholders has been difficult to achieve.

To address the Service's long-term outlook, a fundamental reassessment of the Service's financial options and operating plans is in order. Better information may also be needed about recent changes in the dynamic postal and delivery sector, as well as on the short and long-term effects of postal rate changes on mail volumes, revenues, and costs. Further, an assessment is needed of the full range of actions that the Service can take under current law and identifying

areas where actions are needed. In making such a reassessment, which should also include identifying areas where statutory changes may be needed, the Service should consult with its stakeholders including unions and management associations, customers, and the Postal Rate Commission.

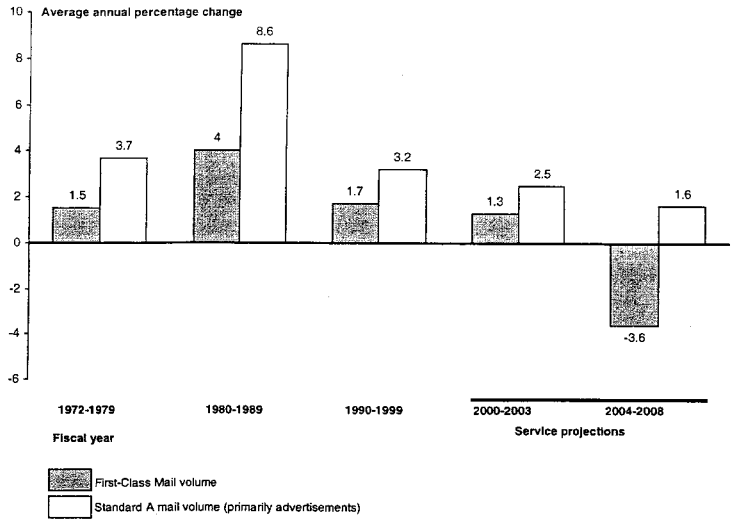
The Service's Viability to Fulfill Its Historic Mission

The Service faces greater competition and expects electronic diversion to cause substantial declines in First-Class Mail volume in the next decade which, according to the Service's most recent 5-year Strategic Plan, would place the Service under "extreme financial pressure." In this event, the Service, like many of its foreign counterparts, would likely face unprecedented challenges to its primary mission of providing universal postal service at reasonable rates while remaining self-supporting from postal revenues. The growing challenges are as follows:

- The Service would face the challenge of responding to any volume declines or changes in the mail mix by attempting to reduce mail processing, personnel, and other costs that have traditionally been considered to vary with changes in mail volume. Labor-related expenses continue to account for more than three-quarters of total postal service operating expenses and have reportedly been difficult to cut quickly in response to less-than-expected mail volumes and revenues. This fiscal year, the Service reported it has experienced continuing difficulty cutting costs when expected mail volumes and revenues did not materialize.
- If First-Class Mail volume declines and the revenue loss is not offset in other areas, rates would need to rise for any mail categories that take on a larger burden of supporting postal institutional costs. The Service maintains a delivery and retail network that includes more than 235,000 city and rural delivery routes; more than 38,000 post offices, stations, and branches; and more than 350 major mail processing and distribution facilities.
- Even if First-Class Mail volumes do not decline, Service officials expect that cost reductions may not be sufficient to keep future rate increases below the rate of inflation.
- Adding to rate pressure, postal infrastructure costs continue to grow. The Service has been adding many new delivery points to new households and businesses—a projected 1.8 million in fiscal year 2001.

Competition is already increasing from private delivery companies, foreign postal administrations accepting outbound international mail from within the United States; and electronic communications alternatives, such as the Internet. As an example of trends that have already affected the Service's mail volumes, federal agencies are mandated to move as quickly as possible to reduce paperwork and to adopt electronic billing and payment. Two-thirds of the 880 million Social Security checks, tax refunds, and other payments that were sent by the Department of the Treasury in fiscal year 1999 were sent electronically. Further, the banking industry's mail volume was almost 18 percent lower in 1999 than it was in 1996. According to the Service, longer term projections suggest that about half of the bills and payments that are currently mailed will eventually be replaced with electronic billing and payment alternatives. It is difficult to predict the timing and magnitude of further mail volume diversion to electronic alternatives and the potential financial consequence. Based on anticipated electronic diversion, the Service's baseline forecast in its 5-Year Strategic Plan calls for total First-Class Mail volume to decline at an average annual rate of 3.6 percent from fiscal years 2004 through 2008 (see fig. 6).

Figure 6: Postal Service Projects Decline in First-Class Mail Volume



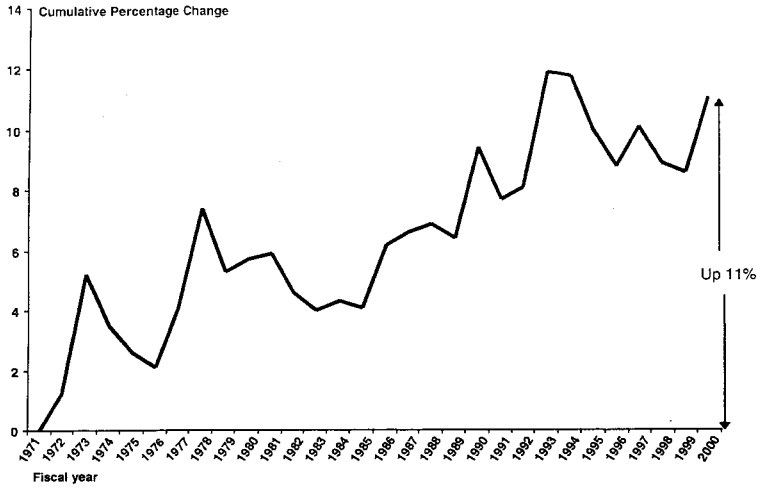
Source: U. S. Postal Service.

The Postal Service has raised the possibility that its financial problems may lead to cutting back universal postal service. A postal official recently said that the Service might ultimately reduce mail delivery from 6 to 5 days each week to remain financially sound. Can the Postal Service continue to maintain the scope and quality of its retail and delivery services? The answer, at least in the short term, is "yes" – but in the long term, the Service's prospects are uncertain.

Control Costs and Improve Productivity

We have previously reported that the Service's continued success will depend heavily on its ability to control operating costs and improve productivity. Postal productivity—the relationship between the Service's outputs of delivering mail to an expanding delivery network and resources expended in producing them—increased only about 11 percent in the past 3 decades, despite vast changes in automation and information technology (see fig. 7). As the Postal Service and key stakeholders have recognized, long-term increases in its productivity will be essential to controlling costs and thus keeping postage rates affordable. However, numerous reports, including some by us and the Postal Service OIG, have noted inefficiencies in the postal system and difficulties the Service has had in realizing opportunities for savings. The OIG has recently identified potential cost savings and is working to identify further opportunities.

Figure 7: Postal Service Productivity Growth Since Fiscal Year 1971

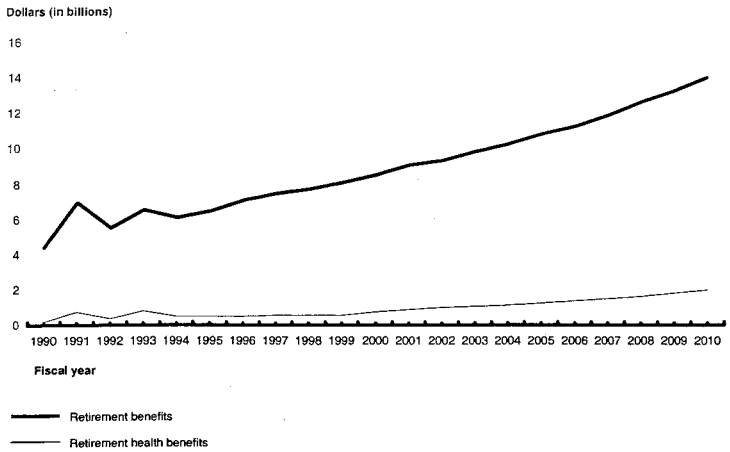


Source: U. S. Postal Service.

The Service's ability to improve productivity and control costs is constrained by a number of factors, such as its requirement to provide postal services to all communities and the requirement that postal wages be determined by binding arbitration when the Service and its labor unions cannot reach agreement. The Service has also reported that extensive work rules and other regulations hamper its flexibility and innovation. In addition, the Service has a self-imposed moratorium on closing post offices and by statute, it cannot close small post offices solely for operating at a deficit. Further, fiscal year 2001 appropriation legislation specifies that the Service cannot close small or rural post offices in fiscal year 2001. The Service estimated several years ago that about half of all post offices do not generate sufficient revenues to cover their costs.

In addition, some employee-related expenses are rising and are difficult to control, such as retirement-related expenses. The Postal Service's retirement-related expenses—that is, the payments the Service makes each fiscal year—have increased in recent years, and these trends are expected to continue (see fig. 8). According to the Service, its retirement expenses are estimated to increase by $554 million in fiscal year 2001 to $9.1 billion and are projected to reach $14.0 billion in fiscal year 2010. In addition, the Service has estimated that its retiree health benefit premium expenses will increase by $114 million in fiscal year 2001 to $858 million, and the Service has projected that these expenses will reach about $2.0 billion in fiscal year 2010.

Figure 8: Postal Service Projects Increases in Retirement-Related Expenses



Source: U. S. Postal Service.

The Service recognizes that it needs aggressive cost management, and the Postmaster General has called for achieving "breakthrough" productivity savings of $1 billion annually, mainly in mail processing, transportation, and administrative areas. However, the Service's fiscal year 2001 budget called for saving only $550 million through such productivity initiatives. The Service is making ongoing efforts to standardize and improve work processes to reduce significant variations in quality, productivity, and costs across the system. The Service is also planning to implement activity-based costing in certain processing facilities to enable it to track activity costs and rates that can be compared across facilities for benchmarking, performance measurement, and budgeting purposes. Another example of potential cost savings that the Service is working to address includes manual processing of mail, which reportedly accounts for half of all labor mail processing costs.

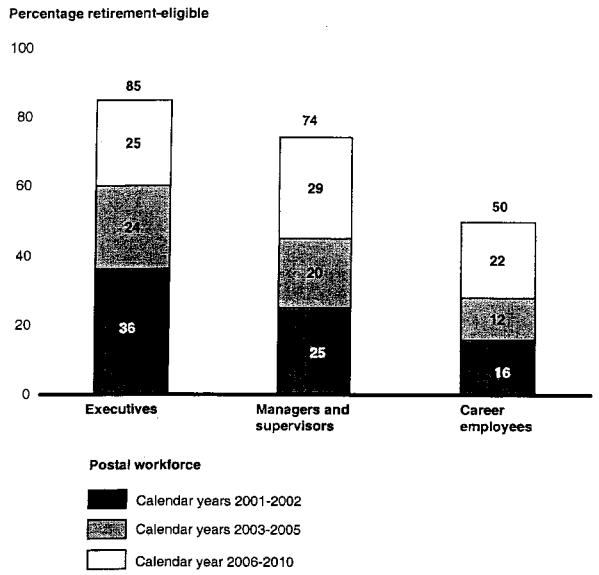
Human Capital Challenges

The Service's Strategic Plan stated that the expected decline in postal workload—in part due to automation and the implementation of information technology—"will inevitably result in both restructuring and a reduction in the workforce." Some of the planned reductions are to be accomplished through eliminating staff vacancies and the work associated with them. We believe that these reductions should be done in a carefully planned manner to avoid negatively impacting the workplace environment, operations, and service quality. In addition, with a large percentage of the postal workforce nearing retirement eligibility, the Postal Service has the opportunity to reduce the size of its workforce; but the Service will be increasingly challenged to deal with human capital issues related to succession planning, maintaining continuity, and the associated

cost issues. The Service will need to maintain the continuity of service to customers as many experienced managers and workers retire and the Service restructures its workforce.

The Service has projected that among its current employees as of October 2000, in calendar years 2001 and 2002 about 130,000 postal employees are already eligible, or are projected to reach eligibility, for regular retirement. This projection includes 36 percent of executives, 25 percent of managers and supervisors, and 16 percent of the career workforce. By calendar year 2010, 85 percent of postal executives, 74 percent of postal managers and supervisors, and 50 percent of the career workforce will reach retirement eligibility, according to Service projections (see fig. 9).

Figure 9: A Large Percentage of the Postal Workforce Is Nearing Retirement



Source: U. S. Postal Service.

The Postal Service faces additional difficult human capital challenges that must be successfully addressed to maintain organizational effectiveness and improve the workplace environment as well as control workforce costs. These challenges include (1) restructuring the postal workforce of about 900,000 career and non-career employees and reducing the number of employees, and (2) ameliorating persistent problems in the workplace that have been exacerbated by decades of adversarial labor-management relations. The Postal Service's human capital problems can be seen as part of a broader pattern of human capital shortcomings that have eroded mission

capabilities across the federal government. The Service and its major unions and management associations need to resolve long-standing labor-management problems that have hindered improvement efforts, including efforts to cut costs and increase productivity. In addition, the Service has recognized the need to provide its employees with the tools and incentives necessary to allow effective participation in planning and implementing improvements.

Actions Needed

We are placing the Service's transformational efforts and long-term outlook on our High-Risk List, effective immediately. The Service is at growing risk of not being able to continue providing universal postal service vital to the national economy, while maintaining reasonable rates and remaining self-supporting through postal revenues. A structural transformation of the Service is called for. The Service's financial outlook has deteriorated significantly since last November and it now projects $2 billion to $3 billion in expected losses in fiscal year 2001 and an even higher deficit in the next fiscal year if there is no additional rate increase. The Service has been increasing its borrowing and is approaching its $15 billion debt ceiling without any debt reduction plan. The Service recently deferred capital investment to conserve cash, thus delaying needed improvements and associated gains in efficiency.

In addition, in March 2001, the Postal Service's Board of Governors wrote the President and Congress asking for a comprehensive review of postal laws. The Board said "We have unanimously concluded that the present statutory scheme puts at serious risk our ability to provide consistent and satisfactory levels of universal service to the American people, generally recognized as delivery to every address every day, at uniform, affordable rates." Further, the Service anticipates substantial losses in First-Class Mail volume over the next decade that would create "extreme financial pressure." If the Service experiences a series of large financial deficits, universal postal service could ultimately be threatened, prices would likely increase at a much faster rate, and other options would need to be explored.

While the Service has announced some steps to address its growing challenges, it has no comprehensive plan to address its numerous financial, operational, or human capital challenges. Inclusion of the Postal Service's transformational efforts and long-term outlook on our High-Risk List will focus needed attention on the dilemmas facing the Service before the situation escalates into a crisis where the options for action may be more limited.

The significant shift in the Postal Service's financial outlook in the last 4 months came as a surprise to a variety of key stakeholders. In order to understand the Service's financial and human capital problems, Congress and postal stakeholders need to have frequent, transparent, and reliable information on the Service's current and projected financial situation, the Service's plans to address its growing challenges, and what progress the Service is making. Therefore, we believe the following actions need to be taken:

- The Service should develop a comprehensive plan, in conjunction with Congress and other stakeholders, such as the postal unions and management associations, customers, and the Postal Rate Commission, that would identify the actions needed to address the Service's financial, operational, and human capital challenges and establish a timeframe and specify key milestones for achieving positive results.

- The Service should provide summary financial reports to Congress and the public on a quarterly basis. These reports should present sufficiently detailed information for stakeholders to understand the Service's current and projected financial condition, how its outlook may have changed since the previous quarter, and its progress towards achieving the desired results specified in its comprehensive plan.

- GAO will work with Congress and the Service to help identify improvement options and will continue to analyze and report to Congress on the Service's ongoing financial condition. In consultation with other postal stakeholders including the Postal Service Office of Inspector General, postal unions and management associations, the Postal Rate Commission, and customers, we will review the Service's financial results and future outlook, progress on cost-cutting and productivity efforts, other countries' experiences, and options for addressing the Service's short-term and long-term challenges.

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

Contact and Acknowledgments

For further information regarding this testimony, please contact Bernard L. Ungar, Director, Physical Infrastructure Issues, on (202) 512-8387. Individuals making key contributions to this testimony included John H. Anderson Jr., Teresa L. Anderson, Hazel J. Bailey, Joshua M. Bartzen, Michael J. Fischetti, Jeanette M. Franzel, Melvin J. Horne, Kenneth E. John, Roger L. Lively, Albert E. Schmidt, and Charles F. Wicker.

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U.S. Postal Service

Transformation Challenges Present Significant Risks

David M. Walker
Comptroller General
of the United States
April 4, 2001

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Postal Service Net Income From Fiscal Year 1990 Through 2002

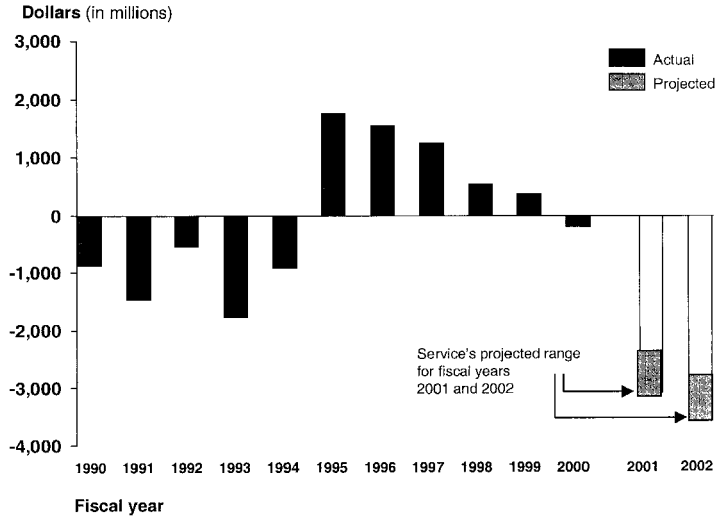

Figure 1

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Trends in Postal Service Expenses From Fiscal Years 1990 Through 2000

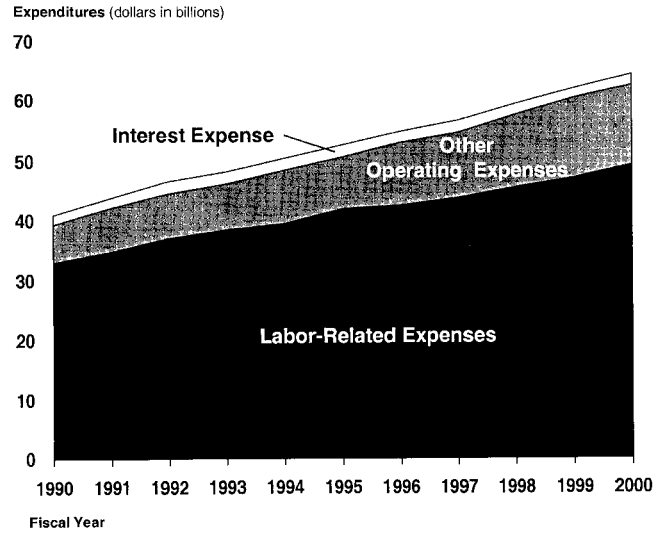

Figure 2

Changes in the Postal Service's Financial Outlook for FY 2001

	Budgeted	Current
Reported Net Income: Quarters 1 and 2	$200 M	-$260 M
Originally Budgeted Net Income: Quarters 3 and 4	-$680 M	-$680 M
Expense Adjustments to Net Income: Quarters 3 and 4		-$320 M
Revenue Adjustments to Net Income: Quarters 3 and 4		-$500 M
Subtotal		*-$1.8 B*
Other Revenue Adjustments to Net Income: Soft Economy-Quarters 3 and 4		-$300 M to -$1.3 B
Net Income	**-$480 M**	**-$2.1 to -3.1B**

FY 2001 Revised Deficit $2.1 to $3.1B

Figure 3

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Postal Service Net Income and Cash Flows From Operations

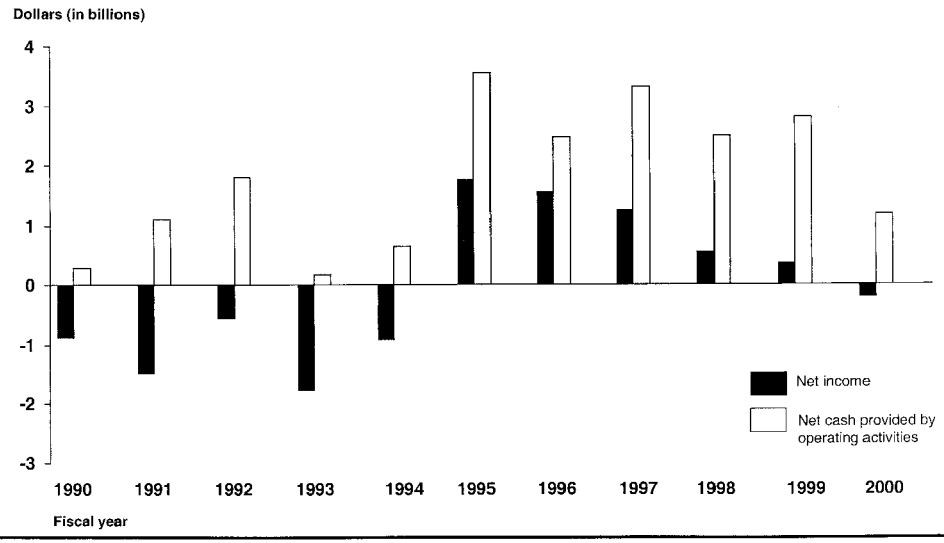

Figure 4

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Trends In Postal Service Debt

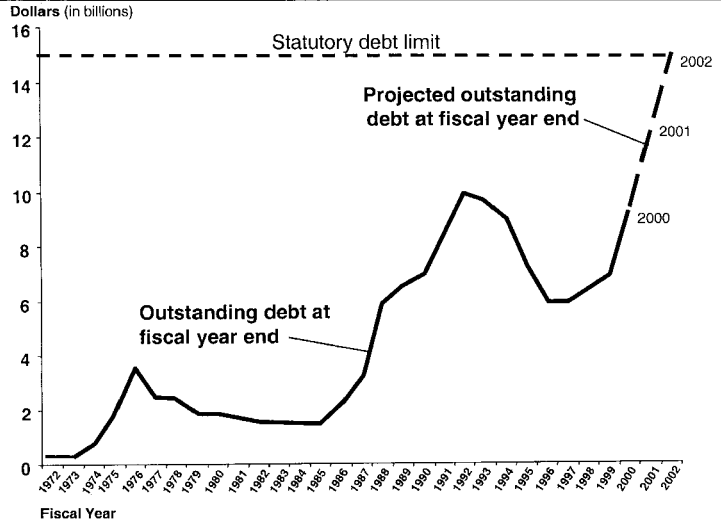

Figure 5

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Postal Service Projects Decline in First-Class Mail Volume

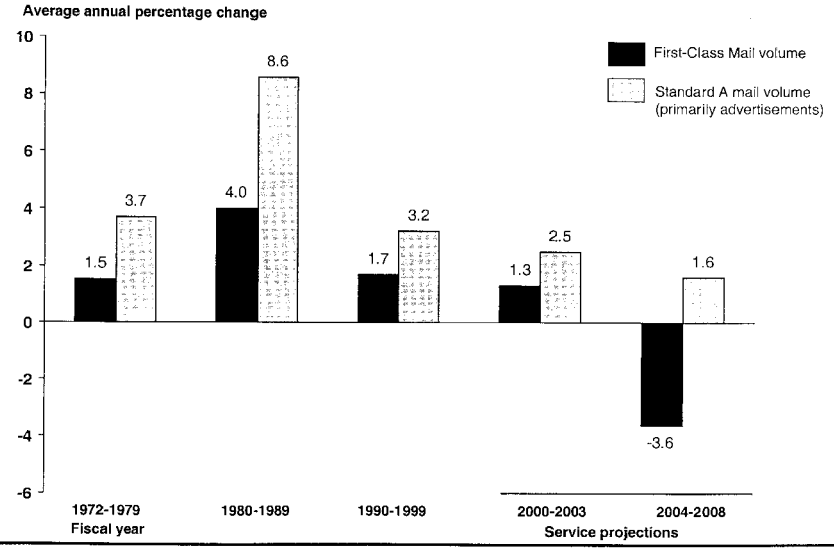

Figure 6

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Postal Service Productivity Growth Since Fiscal Year 1971

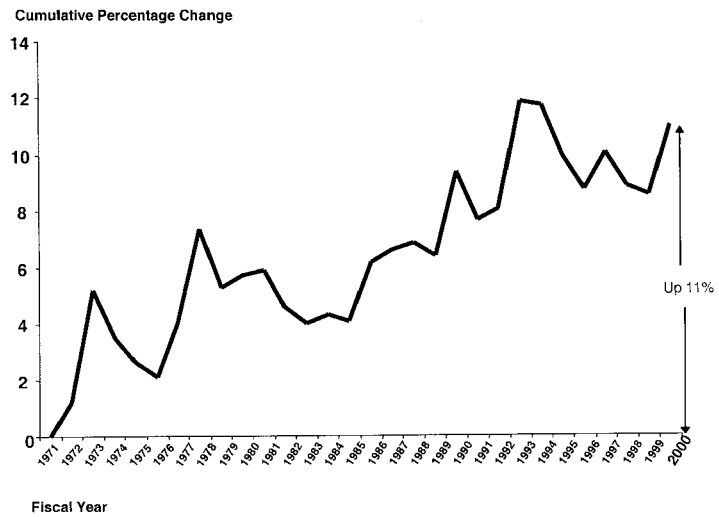

Figure 7

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Postal Service Projects Increases in Retirement-Related Expenses

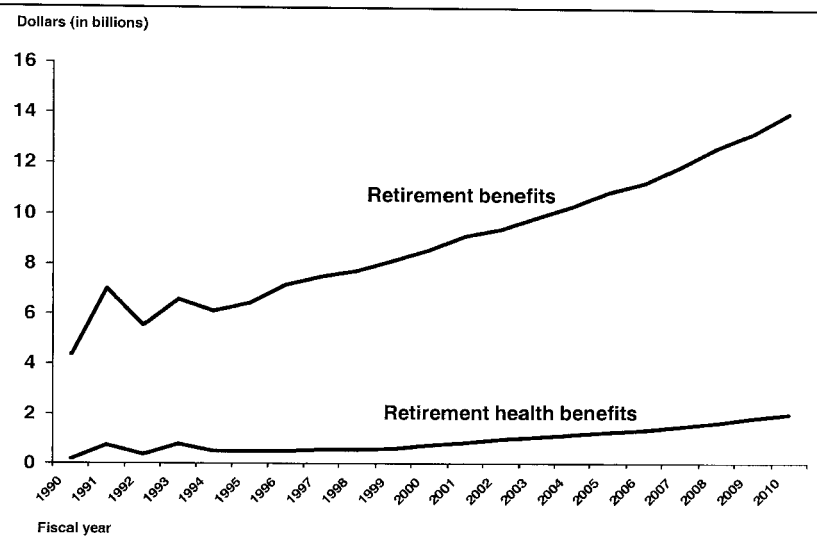

Figure 8

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A Large Percentage of the Postal Service Workforce is Nearing Retirement

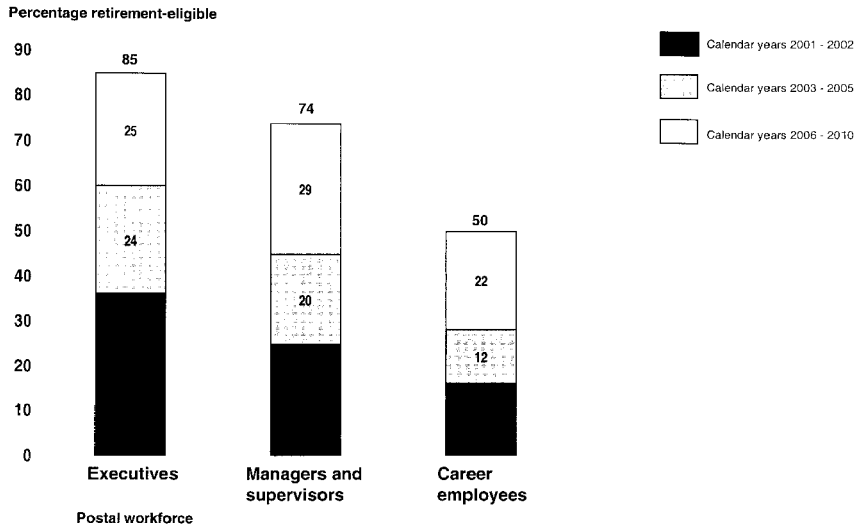

Figure 9

Mr. BURTON. Thank you, General Walker.

You reported just a moment ago that the Postal Service is being added to the GAO's high-risk list. I have a couple of questions on that. Maybe I will just give them all to you at once and you can answer them collectively.

What factors do you take into consideration when determining an agency or program should be placed on the high-risk list? That is No. 1.

Is it unusual for an agency or program to be added to the high-risk list during a congressional session? I mean immediately. We didn't know about this until just recently and then, boom, all of a sudden it just hit us.

Third, what would it take for the Postal Service to be removed from the high-risk list? If you can start off with that question, I would appreciate it.

Mr. WALKER. I would be happy to, Mr. Chairman. They are all excellent questions.

First, what are the factors that we consider? Last year, in calendar 2000, we published for notice and comment the factors that we use in determining when a function or program is deemed to be high risk, and No. 2, what it takes to get off.

Some of the factors that are relevant for considering when a program goes on include: Is the program of national significance? I think we can all agree that the Postal Service has a program that is of national significance.

Does the challenge relate to a key management function that deals with its performance and accountability? Does the risk relate to a systemic or structural problem? Does it involve $1 billion or more of taxpayer funds?

Have there been corrective measures identified? What is the progress toward addressing those? Based upon applying these criteria in our professional and independent judgment, we believe that the Postal Service's transformation effort meets these criteria.

In other words, that transformation effort is at high risk; not the entire Postal Service.

There are several significant subsequent events that have occurred since we made our determination about the January 2001 list. We made that determination in early November 2000, in order to finalize it and to publish it in January 2001.

The significant subsequent events, for example, have been a significant deterioration in the projected financial condition of the Postal Service, escalating from an approximate $480 million anticipated loss for this year to $2 to $3 billion and further escalating in the future.

Second, mounting debt without a debt repayment plan.

Third, a continued conflict over rate setting.

Fourth, key leadership voids. The Postmaster General announced that he was not going to seek reappointment and the chairman of the Postal Rate Commission resigned during this period of time.

In addition, three major labor agreements have expired and are now set for binding arbitration, covering over half of the Postal Service's work force.

Finally, last but certainly not least, the Board itself has stated that it is at serious risk of not being able to achieve its statutory mission.

Mr. Chairman, we could have waited on the 2-year cycle, but I think if there had been subsequent events and the facts dictate that it meets our high risk criteria, if it is a important enough program, and I would argue the Postal Service transformation effort is important, and the Postal Service clearly is, then I think we have a responsibility to act.

In these times, we can't necessarily wait 2 years before we end up adding critical areas to the high-risk list.

As far as what it will take to get off, Mr. Chairman, which I think was your third question, there must be a plan, a specifically identified plan dealing with both operational as well as legislative challenges, to try to address these issues. There must be commitment on behalf of the parties to do it. It must be implemented to some extent and we must see some meaningful results. We must be convinced that it is on a sustainable path to deal with some of the major structural problems in order to get it off the list.

I might add that there is an analogous situation, and it may not sound analogous, but I think there is an analogous situation that occurred earlier in the 1990's. I used to be head of the Pension Benefit Guarantee Corp. PBGC is a government corporation that is intended to be self-financing, that was experiencing a deteriorating financial condition and had certain operational problems as well as certain legislative challenges.

GAO put it on its high-risk list, the single insurance program in the early 1990's. Through a combination of management actions and legislative actions, it was removed from the list several years later.

I think it is a decent analogy, even though that program was in a totally different line of business.

Mr. BURTON. Let me ask one more question real quickly. I think you alluded to the fact that the Postal Service will reach the statutory borrowing limit of $15 billion sometime in the next year or two. What will that mean for Postal operations when they reach that limit? Will the Postal Service run out of cash?

Mr. WALKER. Well, it will then depend on what the projected cash-flows are. Right now the Service is using this borrowing authority for two things, for modernization, for construction activities, as well as to cover operating losses, any cash-flow problems from operations. By law, as you know, the service can only borrow $2 billion a year for construction and improvement and only $1 billion a year to cover negative cash-flows associated with operations.

I think it would be better to ask the Service what projects its cash-flows to be in 2003. But they are deteriorating and we expect right now, if the Service doesn't get a postal rate increase, that it could hit the debt limit in 2002.

By the way, the answer is not simply to raise rates. It is a more fundamental, structural issue that we need to look at here, because you could simply raise rates and deal with the short-term problem. That is dealing with the symptom rather than dealing with the disease. We need to deal with the disease, I think.

Mr. BURTON. Mr. Davis.

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

Mr. Walker, you indicated that if the Service is to reach a break-even point, in all probability, that is going to occur through a rate increase, although you have indicated that you would suggest or hope that would be the last thing that would happen or that every effort should be made to minimize that occurrence.

You also indicated that one of the ways of generating new revenue or additional revenue is through services and products. But we note that the Postal Service has had a difficult time generating real money with services and products.

Given those facts, do you see any way other than perhaps through a rate increase that the situation can be reversed?

Mr. WALKER. I think we need to look at a range of options. I think we need to look at opportunities for cutting costs, for enhancing productivity. I think that the Congress needs to consider looking both on the rate-setting side as well as some of the restrictions that are imposed on the Postal Service with regard to automatically going to binding arbitration and some of the issues that affect its cost structure.

What you can do to provide reasonable flexibility to the Postal Service to allow it to try to transform itself, working with its stakeholders while providing appropriate accountability for results.

I think there are opportunities for economies, for cost cutting, for productivity improvement. But at the same point in time, I think there are some structural impediments that the Service faces that are going to have to be addressed in order to try to enable it to pursue certain things.

You are right, also, Mr. Davis that historically, at least based on our experience, many of the efforts that the Postal Service has made to try to get into different products and services have not resulted in additional margin. They have not resulted in helping the situation and in some situations have hurt.

Mr. DAVIS. You know that in almost any business situation when we start talking about how to come out of a dilemma, immediately we think of cutting costs, that is reducing the requirements for operating.

Do you think we can cut costs and at the same time continue to provide the high quality of service that we have heard some Members allude to that they have been able to receive and benefit from?

Mr. WALKER. Well, clearly, the Postal Service, I think, has done a good job. It has improved its on-time delivery over the past several years. Customer service, in general, customer satisfaction rates have generally been positive and generally have been moving in the right direction, if you will.

So, I think we want to try to minimize postal rate increases and maintain quality and reliability of the Service. I do think, however, that we need to look at more market-oriented approaches to things like rate setting, considering price elasticity a lot more than has been the case.

In other words, obviously, to the extent that you end up raising rates on certain types of postage, in some cases it could have a very serious effect on the volume and in other cases it won't have a serious adverse effect on the volume.

On the other hand, if you look at the cost side, I think we also have to look at what benchmark is being used to set labor wage rates. What is the benchmark that is being used to determine that those rates are fair? To what extent is it based on skills, knowledge and performance? To what extent is it not based on those factors?

I think we also have to look at things compared to other countries and other systems because everything in the world is relevant. We have to learn from them. What are some of the things that they did in order to try to minimize costs while maintaining reliable service? We are doing some work in that area. I think it can help this committee tremendously in trying to deal with some of these issues.

Mr. DAVIS. Finally, if I could, why do you think the Service has had not as much success as desirable in generating large amounts of revenue with its new products or services?

Mr. WALKER. I don't know how much market testing there has been. You might want to ask the Postmaster General that question. But it is not clear to me that there has been a significant amount of concept testing, market testing in advance of some of these products and services that normally you would see in the private sector, that would occur.

Mr. DAVIS. Thank you very much, Mr. Chairman. I am just wondering if sometimes we are not really whistling in the wind in terms of reaching for what is not there when we try to come up with other approaches and other ways.

Thank you very much.

Mr. BURTON. Mr. McHugh. We will continue until we get to the 5-minute mark and then we will recess for the vote.

Mr. MCHUGH. Mr. Walker, thank you for being here. Again, I appreciate the work and the effort that GAO has provided on this very important issue, certainly in the past 6 years that I have been working on it and that effort continues today.

Let me ask you a general question with respect to all these dire predictions. I have read your testimony and I understand you are currently analyzing them in-depth. But have you seen anything in your studies thus far that would suggest to you that the $2 to $3 billion estimate the Postal Service is currently projecting is in any way unreasonable or likely far too high?

Mr. WALKER. We are still analyzing the projection. I can't draw a conclusion at this point in time. Nothing has come to our attention that I am aware of that would cause us to say that it is unreasonable. It is also based on no increase in postal rates as well.

The biggest uncertainty associated with that projection is frankly, the Postal Service doesn't know and frankly nobody in America knows how soft the economy is going to get and how long it is going to last. That is probably the biggest uncertainty that exists.

Mr. MCHUGH. I appreciate that. Obviously, you have said here many times that certainly one of the major challenges of many, and one of the more frustrating things about this problem, is that it is so multi-faceted. Some of my colleagues like to talk about productivity. Others like to talk about confining unnecessary, in their view, competition, etc.

But clearly one of the major problems is the fact that the structure, as you call it, the need for structural reform, is one that has been in place for 30 years. Would you agree with that?

Mr. WALKER. That is correct. I mean, the world is fundamentally different than it was 30 years ago. The type of competition that the Postal Service is facing is very different. There are several foreign countries that have postal services offices on our soil. They are starting out at first to be able to get some of the international bulk market.

There is nothing to preclude them from trying to be able to cherry pick some of the domestic market through contracting type activities, etc. I think we have to keep that in mind.

It is just a whole new ballgame. The other thing is that on the productivity front there has been, it is my understanding through speaking with my very capable staff, that there has been only about an 11 percent productivity increase since the early 1970's in the Postal Service.

Now, to its credit, last year I think the Service had about a 2.4 or 2.5 percent increase, which is maybe the best year ever and clearly one of the better years. But their service's ability to sustain productivity increases over time has not been good in the past and obviously it is something we hope can happen in the future to keep down prices.

Mr. MCHUGH. Yes, I believe it is the largest since 1993, and I think that is a tribute to the current Postmaster General. It is a little difficult to get too terribly productive in a $60 billion a year industry when 76 or 80 percent of your costs are driven by the employees.

You do have a very aggressive automation underway. Mr. Otter mentioned some shortfall figures. They did spend over $5 billion; I think most of us agree that is a lot of money, even on Capital Hill. But when the core of your service is to walk that individual to every household in America, unless you give them roller blades, productivity is a little hard to achieve, I would think.

Let me just finish up with a couple of comments. I think, my colleagues, we have to remember that when we get caught up—and I am a Republican and I am proud of that fact, we have to remember the phrase "competing against the private sector." We should always pause and ask ourselves, who is competing against whom.

I think our constituents, when they go to the Postal Service want to be able to buy certain services and certain products like envelopes and boxes and want to be able to mail a box at the Postal Service and most of us would expect them to do that.

There are a number of great delivery companies in the private sector. I think we have to be cognizant and sensitive to their positions as well. But the fact of the matter is that we have allowed the Postal Service one door to exit their current conundrum. Then we sit around and criticize them for walking out the door. Coffee cups and novelty tee shirts are probably not the best idea. I think it was a show of desperation by the Postal Service to try to generate revenues. Thankfully, they have ended that. We do have to level the playing field.

Our bill required taxes on their competitive products and gave increased oversight to the PRC. Subpoena power required them to

operate under Anti-Trust Provisions. There were those who were deeply concerned about the recent FedEx-USPS partnership and such.

But at the end of the day, the reality is that they are operating in a 30-year old paradigm that doesn't work any more. It doesn't work for either the Postal Service, those folks who depend upon them, or those folks who choose very effectively to compete against them.

When you have a Postal Service that can't, under law, put itself up for winning the Federal Government contract for overnight-urgent mail, I think that suggests that we have to do some things that will allow them to operate differently and require them to operate differently. I hope we can come to that agreement.

Mr. Chairman, again, thank you for your leadership.

Mr. BURTON. Thank you, Mr. McHugh. We are going to rely on your research and previous commitment as subcommittee chairman on this legislation that we are going to be working on.

Mr. MCHUGH. You are too good to me, Mr. Chairman.

Mr. BURTON. Mr. Cummings.

Mr. CUMMINGS. Mr. Chairman, we only have about 8 minutes to vote. Do you mind?

Mr. BURTON. No. If you like we will be glad to recess and you can speak when we come back.

Mr. CUMMINGS. I appreciate that.

Mr. BURTON. We will stand in recess. We have two votes on the floor. I apologize. This is one of the problems we have to deal with in the legislative process. We will be back in 20 or 25 minutes.

We stand in recess until the fall of the gavel.

[Recess.]

Mr. BURTON. General Walker, over the years the General Accounting Office has done considerable work on the Postal Service's finances and its delivery performance. To what extent will the Postal Service's current financial situation impact the delivery of the mail? Do you have an answer to that?

Mr. WALKER. There does not appear to be an immediate threat in any way to the Postal Service's ability to continue to deliver the mail. The simple fact of the matter is that while it is losing money, it has lost money before and it still has borrowing authority.

But the fact of the matter is that we project, at least based on the information we have been given so far from the Postal Service, that the financial situation will become particularly critical at the end of 2002.

What we think is important is to recognize that we need to deal with the structural problem here. Yes, we need to improve productivity. Yes, we need to cut costs. Yes, we need to try to minimize rate increases.

But in order to try to accomplish all of those objectives, it is not only certain management actions that are going to have be taken. Certain legislative reforms are going to have to be necessary as well.

Mr. BURTON. Let me ask you this question and then, Mr. Cummings, I think you were next. I apologize. I will yield to you.

Seventy-five to eighty percent of the total costs of the Postal Service are personnel. We have tried over the years to encourage

automation. I think they have taken steps to use new technologies and automation to speed up delivery service.

It seems that with the new technologies that we have, there could be more use of automation and technology. Without disrupting the personnel that works for the Postal Service, it seems to me, and maybe you have done some research on this, that through attrition, through people retiring, through people leaving the Postal Service, I don't know what the figures are per year, if you can't give me that, maybe the Postal Service can, let us say that out of 900,000 employees there are 60,000 that leave in a year, maybe even more than that.

It seems that there could be an incremental change from heavy use of personnel for certain delivery processes to a heavier reliance on automation and without firing people or laying people off, just through attrition and retirements and a transfer to automation we could make the kind of economies that we see in the auto industry.

In the auto industry, I think they did it with layoffs. I am not saying we should do that because I think we have great people in the Postal Service and through attrition you could do that. But they went to robotics, instead of having people putting screws and bolts in on the assembly line.

Why can't that be done in an orderly fashion and reduce costs? If it can be done, why isn't it being done?

Mr. WALKER. Well, clearly technology is part of the answer, additional use of technology. It is my understanding that the Postal Service has ended up doing more in the area of technology with regard to first-class mail, to try to automate more of that type of activity.

But you properly point out that it costs money in order to be able to design and implement the new technology. Ultimately, if you are going to achieve the productivity increase and reduce overall costs, it has to come from some place.

You properly point out, Mr. Chairman, 75 to 80 percent of the costs of the Postal Service deals are people costs. Therefore, ultimately you are going to need to get that cost down.

What needs to happen is an integrated plan that focuses on desired outcomes, that focuses technology investments along with strategic work force planning so as much as possible you can do what you just said? Based upon attrition, you can end up hopefully being able to save money through attrition, and use technology to increase productivity.

I don't know that plan exists, quite frankly, Mr. Chairman. That is something you ought to ask the Postal Service.

Mr. BURTON. We will address that to the Postal people and the Postmaster General when we get a chance.

Mr. Cummings.

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

Comptroller General, I just want to thank you for your testimony. It has been very enlightening, to say the least. You know, as I listen to you, you made a number of comments which led me to believe, you know, I kept saying, is this operation run like a corporation? Because it seems to me if it were truly run like a corporation, either it would be out of business or it would be doing pretty good.

In other words, you talked about a number of the issues and it seems as if, if there were certain key folks in certain positions that had certain responsibilities you wouldn't have things such as these nontraditional efforts to raise money and things of that nature.

In other words, it seems to me that you would have methods by which you could control what you are doing and, at the same time, change as society changes and as technology changes. It seems like something is out of kilter there.

Mr. WALKER. The Postal Service has a lot more restrictions placed on it, both on the rate-setting side or the revenue side, and on the labor side than would exist in the private sector.

For example, if you take on the rate side, there are a number of factors that the Postal Rate Commission can consider, and in fact that it does consider, in setting rates. But a lot of it is driven by cost and the desire to minimize overall rates, which we all can agree to.

In the private sector, I know you would see a lot more market oriented consideration in determining what you are going to end up charging for particular classes of mail. You would see a lot more consideration on what the likely rate increase would have on volume, the elasticity issue.

You would try to minimize overall rate increases, but what you would also see is you would see a circumstance where the rate increases would be geared more toward areas where there is less competition and where it is less likely to have an adverse effect on volume, which obviously could cut revenues.

On the labor side, clearly collective bargaining is very important. We want to support collective bargaining. You want to have cooperative labor-management relations. That hasn't always been the case at the Postal Service and other entities as well.

You generally don't find circumstances in the private sector where statutorily you are required to go to binding arbitration if the parties reach an impasse.

Take the FAA, the Air Traffic Controllers, that obviously is a vital function for the public, just as postal workers provide a vital function for this country for reasons that I articulated. But the FAA, Air Traffic Controllers don't have binding arbitration if they reach an impasse.

Now, part of the problem is, if you are not going to do that, if you go through mediation, where is it going to go? In the case of the FAA it comes to the Congress. That is problematic, too.

So, I think what we need to do, Mr. Cummings, is there needs to be a plan that recognizes we have to try to minimize costs, we have to try to increase productivity, we have to try to minimize rate increases and there are things that can and should be done administratively within the context of current law.

I also think we have to look at what type of legislative reforms might be necessary, given the passage of 31 years and a fundamentally different economy to try to look at some of the framework and see if that framework might have to be modified in light of changes in the economy and in light of increasing competition.

Mr. CUMMINGS. I have just one other question. Let us assume you had maximum cooperation from the Congress and you were able to do the things that you think you need to get done to accom-

plish what you want to accomplish here, what kind of timetable are you talking about in turning it around so that you are operating in the black? Not you, but I mean the Postal Service.

Mr. WALKER. The Postal Service, yes.

Mr. CUMMINGS. You are such an expert, you sound like you need to be in the Postal Service.

Mr. WALKER. I have already got a good job, Mr. Cummings.

Mr. CUMMINGS. I thought maybe you were looking for a night job.

Mr. WALKER. I have a night job already, too. Last week Mr. Horn tried to make me chief operating officer of the U.S. Government. I told him I had a good day job and a night job, I might add.

But in any event, I do believe, as we say in our testimony, that it is incumbent upon the Board and management to come forth with a proposal. But I think we need to have a clean sheet of paper here.

I don't think we can necessarily assume that the past problems or obstacles that have existed, including relevant political considerations, I think we have to at least put those options on the table. I think we have to talk about them because ultimately we have to make this situation more relevant for the 21st century.

We are not going to be able to get around that. It is just a matter of when we are going to come to that realization and when we are going to act on it.

Mr. BURTON. Thank you, Mr. Cummings.

Mr. Clay.

Mr. CLAY. Thank you, Mr. Chairman. Mr. Chairman, at this time I would also like to request unanimous consent to submit my opening statement for the record.

Mr. BURTON. Without objection.

Mr. CLAY. Mr. Walker, thank you today for your testimony, also. You have several questions I would like to go through with you. What steps can the Postal Service take to ensure that their e-commerce activities will result in a positive return on investment and how long can the Postal Service pursue these initiatives if they don't make money.

[The prepared statement of Hon. Wm. Lacy Clay follows:]

Wm Lacy Clay

Statement of the Honorable William Lacy Clay
before the

Government Reform Committee hearing

"The U.S. Postal Service's Uncertain Financial Outlook"

Mr. Chairman:

As a founding member of the Congressional Postal Caucus, I am most interested in today's hearing. The United States Postal Service and its Board of Governors have made headlines by predicting a possible end to universal service and cutbacks in service, if Congress does not pass legislative reform.

As a member of the House Financial Services Committee, I am interested in getting to the bottom of the Postal Service's financial status. I am concerned that the Postal Service may face anywhere between a $2 billion and $3 billion deficit for Fiscal Year 2001. These estimates follow earlier ones where the Service projected net income that ranged from $150 million surplus to the current "billions of dollars" deficit.

Today for the first time in its history, the Postal Service is being placed on the General Accounting Office High Risk list. Placing the Service on this list means that it can no longer accomplish its mission of providing universal service at uniform, affordable rates. It's finances are in jeopardy. This is an early warning. We need to examine the underlying causes if we are to help the Service improve.

The "high risk" designation parallels banking practices. When a bank experiences serious problems, bank examiners go into the financial institution and look at their books. More often than not, it is risky lending practices, or in this case, risky business practices which overtake the institution. In the banking world, risky business ventures typically involve a bank getting into areas in which they don't belong. Banks risk capital on high risk, low ROI (return on investment) activities.

Mr. Chairman, I believe we must look closely at postal activities. Do they engage in unprofitable activities? Are non-postal activities contributing to the institution's failures? Are postal e-commerce ventures booming and making a profit, or dot.tanking – going the way of so many dot.com companies? How does the Postal Service track expenses and costs? Are postal projections and predictions accurate? If not, what can and should be done to ensure a more realistic accounting? And finally, how well does the Postal Service track actual costs and savings from productivity initiatives?

I look forward to a critical review of these matters and welcome today's witnesses. Thank you.

On the e-commerce area, today the postal service told me the following:

For FY 2000, e-commerce revenue was $26,443,000

For FY 2000, e-commerce expenses were $30,162,000

For FY 2001, the postal service is predicting to generate $104 million in revenue for ecommerce activities, a 400% increase over 2000 projections. Ain't gonna happen, pal!

Mr. WALKER. Mr. Clay, I would be happy to provide something for the record on that but I can't answer it right here at this time.

Mr. CLAY. Do you know how much money they are losing on these activities?

Mr. WALKER. On the e-commerce activities, I don't. We recently received some information. I think one of the things that has to happen in general in government, including the Postal Service, is to move more toward activity-based costing where we have more information with regard to types of products and services and functions. Postal has more than most, but not enough.

Mr. CLAY. Along those same lines, how much money is the Postal Service counting on from its new products and services?

Mr. WALKER. Mr. Clay, I would respectfully suggest that they would be in a better position to answer that than I would.

Mr. CLAY. OK. Last September, GAO made several recommendations to address a number of inconsistencies and problems it found with information the Postal Service provided on its e-commerce activities. What action has the Postal Service taken to respond to GAO's recommendations?

Mr. WALKER. If it is all right, Mr. Chairman, I would like Bernie Ungar to come up who I think held his hand up earlier. He leads our work in the Postal area. He might be able to address it.

Mr. UNGAR. Mr. Cummings, as you indicated, we did make three recommendations to the Postal Service. I think one of the most important ones was for the Postal Service to get a better handle on its revenues and expenses from its e-commerce products.

The Postal Service did agree with all of our recommendations, that one in particular. It has taken action to implement a new system to collect and allocate costs and report revenue.

We just got information recently from the Postal Service, so we have not had a chance to assess it yet. But we are certainly pleased that the Service took our recommendations to heart.

Mr. CLAY. So, do you think they will make money off of their activities?

Mr. UNGAR. We are still analyzing that. The information to date would suggest that the Service is still having problems making money, but again, we are in the early stages at this point.

Mr. CLAY. Mr. Walker, the Postal Service was recently chastised for approving over $200 million in bonuses for managers. How typical is this sort of behavior when every dollar is needed to cover necessary and critical expenses?

Mr. WALKER. I am not intimately familiar with the bonus system that the Postal Service has. I do, however, know that it is based on somewhat of a balanced scorecard approach. It has specific measures that are set in advance and include results, financial performance, on-time performance, and certain employee-related issues as well.

In the private sector generally you would find that it is important to have a well-defined plan that has balanced measures, that considers profitability but also considers other factors like productivity improvement, which I know there is a factor at the Postal Service.

We would be happy to take a look at it, if you like, Mr. Clay, but it is my understanding that it is a plan that has existed for some time.

It is not unusual to see bonuses paid in the private sector when a company is losing money, because it depends on whether it is intended to be a profit-sharing arrangement or whether or not the bonus structure is based upon other measures that, even though they may not result in immediate profit, may end up resulting in positive outcomes over time.

But without reviewing the exact program, it would be tough for me to tell where I think that stacks up.

Mr. CLAY. So, irrespective of the $3 billion deficit that is being projected, it is OK to pay the bonuses. Is that what you are saying?

Mr. WALKER. What I am saying is merely because they are paying bonuses doesn't tell me that there is a problem. What I would want to do is to look at what is the nature of the bonus program. How is it set up? What are the key measures? How well are they defined? How reliable is the information and how do these bonuses compare to other comparable entities, if you will.

Mr. CLAY. Mr. Walker, one final question. The Postal Service has reported that its worker compensation expenses are increasing substantially and are difficult to control. Why are these costs increasing so dramatically and what efforts are underway to bring them under control?

Mr. WALKER. I think the Postal Service would be in the best position to answer that, but I will tell you this: We do have concerns about this issue. We do have concern about the so-called "lost days" rate. How many lost days does the Postal Service have on average per worker per year?

As you probably know, Mr. Clay, Treasury Secretary Paul O'Neill is a big proponent of focusing on these issues, as I am. This was one of his lead efforts when he was chairman and chief executive officer of Alcoa.

I think that is an area that clearly has to be focused on to a greater extent. It also could be a combination of what has occurred over years when there hasn't been as positive labor-management relations and possibly some of the related stress factors.

Bernie.

Mr. UNGAR. Last year one of the major reasons for the increase was in effect a speed-up by the Department of Labor in processing claims. We also have just begun work, at the request of Mr. Horn, to look at the Workers' Compensation Program. So, we are also trying to get a handle on what is actually causing those problems and the increases and what can be done to prevent the increases.

Mr. BURTON. Thank you, Mr. Clay.

General Walker, thank you very much for being here. We really appreciate it. We will probably be back in touch with you in the future.

Mr. WALKER. Thank you, Mr. Chairman.

Mr. BURTON. Postmaster General Henderson, would you come forward? I understand you have an association with you who might want to answer some questions as well. As always, we will swear you in before you sit down.

[Witnesses sworn.]

Mr. BURTON. Make no mistake about it; those Members who are not here will be aware of everything that is said. There will be some of these Members coming back. This is Wednesday and we are going on a 2-week break, so there will probably be a lot of the Members who are leaving.

This is very important and the gravity of the situation with the Post Office will be conveyed not only to the Members of the committee who are not here right now, but to the leadership and the White House. I intend to contact the White House because I am not sure they are aware of the shortfall.

I was just informed, and maybe you can address this in your opening remarks, General Henderson, that the shortfall of $2 to $3 billion may be under-estimated. It could be as high as $4 to $5 billion from what I have been told. So, if you could address that in your opening remarks, I would really appreciate it.

STATEMENT OF WILLIAM J. HENDERSON, POSTMASTER GENERAL OF THE U.S. POSTAL SERVICE

Mr. HENDERSON. Thank you, Mr. Chairman. I am very glad to be here today to talk about the Postal Service. I am pleased that after 30 years of working in the Postal Service next month I will be leaving.

I want to thank you for your help in trying to push reform and former Chairman McHugh's help in trying to push reform. I think that is critical to the future of the Postal Service.

I also want to thank the 800,000 employees across America who work for the Postal Service for their outstanding customer satisfaction scores of 92 percent customer approval. That is the highest in the Federal Government and also for their on-time service performance with externally measured first class mail, which is 93, and for 14 quarters has been 93 or better all across the Nation. That is excellent work that these employees do.

My disappointment of my tenure as a 10-year Postmaster General is the fact that we didn't get postal reform. We have talked about what is happening today for the last 4 or 5 years. We have talked about the fact that there is going to be a decline in demand for postal products 1 day and the Postal Service has to be given tools to avert that.

I have been in Congress talking about this theme. Today, you are seeing it as a reality. I will put up slide No. 1. I will just show you something that drives Postal costs. It is something, Mr. Chairman, that you mentioned earlier.

If you will look at that graph, you can see that the red line is the cost per work here and the yellow line is the net income. There is a direct correlation between cost per work year in the Postal Service and net income.

If you take revenue per piece, which is the price of postage and go back 30 years, you will see the price of revenue per piece tracks identically to the cost per work year. So, there is the driver.

If you will go to slide No. 2, you will see that the yellow cylinders are the actual growth and the red part is the planned growth. You will see AP–5, 6 and 7, that is after the rate increase. You will see that revenues are well below planned after the rate increase.

If you will go to slide No. 3, the point of this slide is that over the last 2 years we are processing 8 billion more pieces of mail, 3.1 more million deliveries with 20,000 fewer employees. So, you can see the impact of automation on the Postal Service.

Finally, the last slide, this is a slide that explains exactly where we are today. The yellow line is where we projected the $480 million loss. You see the top line there. When we received the opinion from the Postal Rate Commission, we adjusted that line to $1.3 billion, accounting for the $800 million that you mentioned in your opening statement.

When we had actual performance in quarter one, which is the green line, you will see that expectations for revenue were very low. Now, we are projecting out between $2 and $3 billion right there. But if the economy goes south even from where it is today, postal mail volume is a surrogate for the economy, it could be worse.

I just want to be candid with you. We can't do much about that revenue line as it stands today. We don't have any tools, really to effect the revenue. We just have to adjust our costs and our expenses. That is where you see some of what would be characterized as more radical things being talked about.

We have to respond to lessening revenues. We talked about this as being a major problem in the reform hearings that former Chairman McHugh conducted. We talked about the fact that today it happens to be the economy. Tomorrow it could be bills and payments, the $17 billion being taken away from the Postal Service. It has to have tools to adjust. Without those tools, unfortunately, rate increases come along.

The Postal Service, as a matter of policy, doesn't like raising rates. We have some options that we are going to look at for this upcoming talked about rate case.

But nonetheless, the problem exists; the problem of declining revenues is a fact in today's economy. I know you will understand this because you have been a part of that discussion.

That is where we are today, Mr. Chairman. Thank you.

[The prepared statement of Mr. Henderson follows:]

Statement of
William J. Henderson
Postmaster General and Chief Executive Officer
United States Postal Service
before the
Committee on Government Reform, U.S. House of Representatives
April 4, 2001

Good morning, Mr. Chairman. I want to thank you and the Members of the Committee for the support and encouragement you have provided during my tenure as Postmaster General. As you know, I will be leaving the Postal Service when my 3-year contract with the Board of Governors expires in May. I appreciate this opportunity to talk with you about where we are in the Postal Service today and about the future of this institution.

The Postal Service stands on the cusp of what should prove to be its most dynamic and rewarding century of service to the American people. Within the postal community as a whole, the challenge is to update a shared vision of what the Postal Service can and should be in today's fluid environment, and to install the incentives and tools to get what the Nation wants from it.

Since becoming Chief Operating Officer in 1994, what I have found is an organization eager to set high expectations for itself, and to make the commitment necessary to exceed them.

Seven years ago, when our on-time performance numbers for overnight local delivery of First-Class Mail averaged in the low 80s, who would have thought that 90 percent was physically achievable, especially in the big urban areas like Washington and New York? But we're now working on a fourth year in a row at 93 percent or better. In our independent Customer Satisfaction

Measurement, the percentage of people rating the Postal Service "excellent" has doubled over the same time period. The managers and employees of the Postal Service put a lot of hard work into these achievements, and I'm proud of what they have accomplished.

Over this period, the Postal Service has experienced some of the best growth in mail volume in its history. We invested heavily to expand automation and technology for improved productivity. In the year 2000, Total Factor Productivity grew by 2.5 percent, the best record since 1993.

During the last seven years we have also succeeded in holding down the prices our customers have had to pay. The last two rate increases were among the smallest and most affordable in the history of the Postal Service.

Since 1994 the Postal Service also posted some of its best financial results, including four years in a row with net income, prior to Fiscal Year 2000.

As you know, in recent months the Postal Service's finances, along with the economy in general, have taken an unfavorable turn. Our latest forecasts project losses in the range of $2-3 billion for this Fiscal Year.

Through our Accounting Period 6 ending February 23, our revenue fell below plan by $344 million, or 1.1 percent. Compared to the same period last year, revenue was up only 1.8 percent, despite the recent rate increase. In the first quarter, including the holiday season, First-Class Mail volume actually dropped, for the first time in years. More recently it is almost flat. After years of growth, usage of our high-margin product, Priority Mail, is in decline.

Costs are only slightly over plan at this point, despite growth in several components that are beyond our control, including fuel prices and arbitrated wage awards.

In the face of this adversity, the Postal Service, as currently structured, unfortunately has only rather blunt instruments available to it.

- Our finances are structured to be hand-to-mouth. Break even means that prices and costs are supposed to stay in balance, and the Postal Service cannot build earnings for the longer term like a private firm.
- The process for adjusting rates is largely outside the Postal Service's control.
- It takes a large, cumbersome, slow omnibus rate proceeding to align prices with changing costs.
- While the Governors have final responsibility for rates, including some modification authority, this option arrives late in the process when much of the damage may already have occurred.
- The nature of basic service obligations and networks remains fixed, and the numbers of customers to be served grows, whether the economy is booming or soft.
- The law allows multi-billion-dollar wage decisions to be passed to unaccountable outside arbitrators, so that the parties escape the responsibility to work out the organization's future themselves.

All of this makes the Postal Service uniquely vulnerable to rapid shifts in its markets. The current financial challenge arises against a backdrop of explosive growth in communications technology and revolutionary restructuring

of the commercial marketplace. Previous commercial relationships among service providers and between providers and customers are changing at an unprecedented pace and on a global scale.

The question to be asked is, can we reasonably expect at this point that the Postal Service will regain the steady progress it made in the 1990s, without a major modernizing reform? I doubt it.

Across the world the answer other advanced countries have reached for their own posts is no. They already have revolutionary commercial reforms of their postal systems well underway, and the officials I talk to cannot understand how the United States would choose to lag behind.

Mr. Chairman, with your permission, I would like to personally thank Congressman John McHugh for the leadership he has shown over the last five years, in taking up and carrying forward the mantle of postal reform. I continue to believe that this country will ultimately choose to move to a more commercially viable postal structure required to meet our current and future challenges. When that happens, John's efforts will deserve much of the credit for giving this problem the visibility and recognition it deserves.

I do not know that postal reform must follow any one model, or be achieved in a single stage. But I am certain that, to be successful, reform must provide the opportunity, the incentives, and the accountability for the Postal Service to evolve with its markets. Without an ability to probe for new ways of doing business and to rapidly adjust to forces of demand and competition, the

postal system will become increasingly outmoded, and will have trouble meeting its very important responsibilities to the public.

Universal service for all Americans in every corner throughout the length and breadth of this country has been the hallmark of a growing, healthy Postal Service over its entire history. A seriously weakening postal system would find it more and more difficult to carry the full load of universal service, where the volume of traffic does not cover the full cost.

In recent years the Postal Service has invested increasing attention in improving customer focus and seeking opportunities for new methods, products, and services. We want to take full advantage of the efficiency and better service that technological progress and new business relationships can provide for the benefit of our customers. Our recent business alliance with FedEx is just one example. An ongoing process of creative reinvention and reorientation will be required to enable the Postal Service to maintain and improve its relevance for the American public in the years ahead.

During my time as Postmaster General and before that as Chief Operating Officer, I believe the Postal Service has proved that it is willing and determined to make the changes necessary to stay up to date and maintain the value of its service. It is clear, however, that the current legal structures for regulation and governance of the postal system do not provide enough incentives and tools for change. The present structures are heavily biased toward maintaining the status quo. Risk-taking is discouraged and any mistake is punished. Every initiative

that would change the way things have been done before immediately incurs a heavy burden of persuasion.

The bottom line is that the postal community collectively is accustomed to holding the Postal Service on a short rope. Checks and balances are valued more than innovation and improvement. Over the longer term, in the fast-paced world of communications today, this is a formula for growing irrelevance, weakening service, declining usage, spiraling costs and prices – a formula for increasing obsolescence and failure.

The solution is not unfettered commercial freedom, but greater application of market-based controls and accountability. This is the direction that offers the best return for the American people. It is the direction that our trading partners overseas are taking. And in one form or another, it is the direction we need to take in this country, and will take, in my opinion. For the sake of a smooth transition and as little disruption as possible, both for the general public and for the huge section of American commerce that is so heavily reliant on the Postal Service, reform sooner is better than reform later.

Thank you very much, Mr. Chairman. I will be pleased to respond to questions.

Questions submitted to Postmaster General William J. Henderson In follow-up to the Government Reform Committee's Oversight Hearing on April 4, 2001

Questions submitted by Chairman Dan Burton:

1. Recently the Postal Service announced that it was suspending over 800 capital projects nationwide. How much savings will this generate and what factors were used to determine which projects to halt? What impact will suspending capital construction and renovation projects have on the Postal Services physical infrastructure, operations, automation plans and cost savings?

The freeze on capital commitments was a fiscally responsive action taken to ensure that cash is available to meet current obligations. Although planned commitments have been reduced in fiscal year 2001 and will probably be reduced in 2002; we will still have capital outlays of approximately $2.7 billion in 2001 and $2.2 billion in 2002. These expenditures will be for infrastructure investments and for labor replacement efficiency investments that have already been contracted. We expect that the freeze on new contracts will continue at least through this fiscal year. We will continue to plan for additional projects that produce productivity gains and contract for them when funding is available. We will also proceed with selected investments related to health and safety of our employees and customers, all legal requirements and other emergencies

The action to freeze new capital commitments was done recognizing that in the long run this could have a negative impact. Given our financial situation there was no choice. Continuing to proceed with additional investments when the funding was not going to be available was not an option. We will monitor the impact of delaying major investments and will take action to sustain operations until funding is available to make improvements.

2. Please describe all of the cost saving and productivity measures that you have considered in the past year.

Postal Service cost reduction initiatives for FY 2001 fall into two broad categories: Program and automation-related savings and our Breakthrough Productivity Initiative (BPI).

Major automation programs and others total $454 million in cost reductions for FY 2001 and include: Flat Sorting Machines, Delivery Bar Code Sorters, Remote Bar Code Sorting Programs, Identification Code Sort, Tray Management System, Auto Air Assignment and Semi Auto Scan Where You Band System, Robotics, MTE Service Centers and Small Parcel and Bundle Sorters.

Breakthrough Productivity Initiative programs totaled $756 million in cost reductions for FY 2001 and include: Operations Initiatives, Transportation, Supply Chain Management and Overhead Reduction.

2a. Hypothetically, if all of these savings and productivity measures were implemented, how much would have been saved? How much was actually saved?

The Postal Service expects to achieve this level of savings. We measure the level of savings by using Total Factor Productivity (TFP). Year to date, through accounting period 9, TFP indicates we have saved over $900 million through productivity improvements. With four accounting periods remaining, we expect to achieve the $1.2 billion in combined (automation and BPI) savings.

2b. Please provide an example of a cost-saving measure that was not implemented. Please explain why the measure was not implemented and give us an idea of how much would have been saved had the measure been implemented.

Cost saving measures go through a rigorous review before they are implemented. If they involve capital investments, they go through a capital investment analysis to quantify the benefits and determine the rate of return. If they do not require capital investments they are built into the operating budget and agreed upon by field personnel. We are not aware of any programs that were "left on the table" over the last year. Occasionally, some potential savings program might conflict with our public service requirements or be in conflict with a labor contract and will, therefore, not be initiated.

3. If your cost containment efforts could save three billion dollars, how would that impact your decision to file a rate case this year? How would it have impacted the Board's May 8, 2001, decision to overrule the Postal Rate Commission's recommendations in Docket No. R2000-1?

The Postal Service is committed to reducing expense growth, but there are limitations to what can be achieved by cost containment. The cost of labor is currently growing greater than the rate of inflation and this limits the Postal Service's ability to reduce expenditures. Three billion dollars represents significant resources and rapid expenditure cuts of that magnitude would result in service degradation. Three billion dollars is, for example, the average annual expense for approximately 60,000 letter carriers. Or it represents three-fourths of the Postal Service's total transportation expenses. Another way of looking at $3 billion is that it is almost double the Postal Service's annual expenses for postmasters. If the Postal Service could make expense changes and resource reductions of this magnitude instantly, the May 8th decision to modify rates could have been avoided.

Nevertheless, from 2001 through 2003 the Postal Service has planned for $ 2.5 billion in cost savings, which is close to the $3 billion mentioned in the question. Achievement of these savings will lead to an unprecedented string of cost savings, but will not eliminate losses or the need for another rate filing because of the level of cost inflation experienced by the Postal Service and less revenue growth resulting from the current soft economy. The Postal Service's finances have been negatively affected by surging fuel and utility expenses; by a labor arbitration award that advanced virtually all city carriers a grade in their pay scale; and by the loss of cash that was foregone due to the inadequate rate recommendations of the Postal Rate Commission.

In addition, the Postal Service needs to fund network growth that is equivalent annually to adding a city the size of Chicago to the network (new deliveries on city and rural routes) whether or not we receive increased revenue from mail volume growth. Due to weakening volume and revenue growth, inflationary cost pressures mentioned above and the impact of funding network growth, an additional rate increase is required to re-balance revenues and expenses.

4. Has the Postal Service generated a net profit from its e-commerce and other new revenue initiatives, such as e-bill pay? If not, when will these initiatives generate net income? Were your initial projections for these initiatives overly optimistic?

The Postal Store—formerly called Stamps Online—has taken in over $40M in postage revenue, though this is typically considered core rechanneled product revenue.

NetPost CardStore, launched in December 2000, has a net profit of $6,758 for the period of inception through April 2001.

Although other eCommerce initiatives have not yet shown a profit, it must be remembered that none of the Postal Service's eCommerce products are very old -- most have been in the market for less than a year.

Were the initial projections for these initiatives overly optimistic?

Although projections are lower than anticipated, our business plan calls for positive operating contributions beginning in FY 2003 and break-even in FY 2004.

4a. What new revenue initiatives does the Postal Service plan to implement in the next year, and what are your cost and revenue projections for all such initiatives?

No final decisions have been made regarding new programs for FY 2002. Therefore, cost and revenue projections cannot be made at this time. We expect to make final decisions on new revenue initiatives in the fall of 2001.

4b. Has the Postal Service developed an accurate system to determine the attributable costs of its new revenue initiatives? If not, please outline any plans to do so.

The Postal Service has developed a report titled, *Defining a Consistent Approach to Product Costing for New E-Commerce Initiatives.* The Postal Service is in the process of applying this conceptual approach to the eCommerce products. In this year, we plan to put into place mechanisms that will allow us to calculate attributable eCommerce costs in the following year (FY2002 costs).

(NOTE: This information was provided to GAO in February 2001, in response to a letter from Bernard Unger to Mr. Nolan).

5. It is my understanding that the Postal Service has a moratorium on closing post offices and, by statute, it cannot close small post offices solely for operating at a deficit. However, the Postal Service has roughly 500 mail processing plants many of which are under-used. Have you considered consolidating these plants and if so, how much would be saved annually?

We are in the process of conducting Area Mail Processing studies to identify opportunities for us to consolidate our operations and reduce expense as a result. This activity has been recently initiated and expense estimates have not been completed at this point.

6. The Board of Governors recently directed Postal management to review the possibility of reducing mail delivery to five days a week. How much would this save and what impact would it have on mail processing?

The study is ongoing. The BOG requested a report within 90 days. Findings will be presented to the BOG on July 9.

7. According to the General Accounting Office, the Postal Service has total outstanding debts of $9.3 billion dollars. If the Postal Service exercises its full borrowing authority of $3 billion each of the next two years the Service could reach its statutory borrowing limit of $15 billion by the end of next year. Will this scenario cause the Postal Service to run out of cash? What is the Postal Service's strategy to pay off its debts?

Under such a scenario, the Postal Service would no longer retain legal authority to increase its debt and could very likely run out of cash. To lower debt outstanding, the Postal Service must earn net incomes. To accomplish this, our current strategy calls for an additional rate increase as well as aggressive productivity improvement and cost reduction efforts to bring postal finances into balance. While our preference is for minimal necessary rate increases, the current financial situation, resulting from shortfalls in revenue from the last two rate proceedings and from the current softening economy as well as the cost of an ever expanding delivery network, mandates that we consider additional price increases.

8. The use of electronic alternatives to the mail such as E-mail, direct deposit and electronic bill paying are becoming more common. To what extent will the increased use of these electronic alternatives impact the Postal Service's financial position?

The impact of e-mail, direct deposit and electronic bill paying is reflected in the Postal Service's First-Class non-presort letter mailstream. In FY 2000, non-presort volume declined 2.6 percent. Through Quarter 2 of FY 2001, non-presort volume is down an additional 2.0 percent. Every percentage decline equates to a $225 million annual loss in revenue. Driven in part by the use of electronic alternatives, the Postal Service expects that annual declines of First-Class non-presort letter volume will continue in the two to three percent range.

8a. What discussions has the Postal Service had with the Federal Reserve regarding the efforts of the Federal Reserve to replace paper-based transactions with electronic bill payment technology?

None at this time.

9. We understand the Postal Service has recently instituted a new breakthrough productivity initiative to expedite mail processing and to increase productivity. Please explain this initiative?

The Breakthrough Productivity Initiative is a comprehensive multi-functional effort to drive costs out of the organization. To accomplish this, BPI is focused on:

Improving productivity in mail processing, delivery, and customer service operations;
Reducing overhead and administrative costs;
Reducing the amount of transportation used and the cost of that transportation;
Reducing the cost of all goods and services purchased as well as reducing consumption.

9a. How much of this initiative has been put on hold because of the decision to suspend capital projects?

None at this time. The Breakthrough Productivity Initiative would not be substantially impacted by the capital freeze until FY 2003.

10. Why isn't automation saving the Postal Service money? What steps are being taken to ensure the success of automation projects?

Automation is producing savings and cost avoidances greater than original projections. Since 1987 we have invested $5.4 billion in letter mail automation projects and through 2000 we have achieved approximately $19 billion in savings/cost avoidances against original projections of about $18 billion. Operating budgets in the areas impacted by operations have been reduced and will continue to be reduced. Productivity gains have been realized this fiscal year. Career complement has been reduced by over 21,000 since its peak in 1999.

11. The Inspector General has identified numerous instances where poor contracting practices have exposed the Postal Service to hundreds of millions of dollars of waste. The IG reported instances in which the Postal Service failed to competitively bid contracts as well as instances in which the Postal Service paid for work that was not completed or for work that was not performed at all. The IG also noted instances where contracts were poorly drafted or did not fully protect the interests of the Postal Service. What are you doing to address these contracting problems?

We disagree with the OIG's most recent testimony to the Congress reporting the loss of millions of dollars through fraud, waste and abuse due to poor contracting practices. We found that much of the dollar amount stated in that testimony resulted from over-estimates, questionable projections, or questioning business decisions that balanced operational and service issues with costs differently than the OIG recommends. Subsequent meetings with members of the OIG staff have been held to discuss our differences.

As for the matter of competitively bid contracts, our Purchasing Manual (PM) is very clear that competition, whenever feasible, is the best method of identifying best value sources. However, the PM allows the purchase team to decide when and if it is appropriate to award a noncompetitive contract. Such a decision must be made within prescribed parameters and a business case must be made and documented to support that decision. Our data indicate that over 94% of our contracts awarded in FY 2000 were competitive.

The instance cited by the OIG that the Postal Service paid for work for a major telecommunications contract that was not completed or not performed at all, is misleading. In this situation, the purchase team had identified the billing discrepancies, had been proactive in establishing contract administration procedures to address incorrect billings and asked the OIG for assistance. This effort led to a cumulative recovery of $12 million from erroneous billings by offsetting from the next month's billing. The OIG included in their report of losses an extrapolation of potential costs of $58 million on this contract if no effective cost controls had been established when those cost controls were actually in place at the beginning of contract performance. None of the projected $58 million was paid by the Postal Service.

The Postal Service averages more than 50,000 contract awards annually. All of these awards are subject to various levels of oversight, including management review, the Postal Service's internal bid protest procedure, the Postal Service Board of Contract Appeals, the courts, the General Accounting Office and the OIG. On comparatively few occasions, these reviews or other information reveal that individual actions are inconsistent with our policies or good business practices. When these are found, we assess them, and implement appropriate corrective actions. We are not tolerant of cost inefficiencies in our purchasing processes and are implementing the best practices of commercial supply chain management to help improve USPS productivity.

12. What is your justification for using revenue guarantees in contracts and strategic alliances?

The Postal Service has on occasion included revenue guarantees in contracts with suppliers and in strategic alliances with our business partners. A revenue guarantee may be established for a strategic alliance when the revenue potential of the alliance is reasonably quantifiable but its full potential over the term of the alliance is unknown. The objective is to minimize capital investment while maximizing cash flow.

In a purchasing scenario, the revenue guarantee is used in much the same way as we would use a guaranteed minimum in an indefinite delivery contract. In this case, the objective is to guarantee the Postal Service a ready source of supply for critical requirements while minimizing the supplier's risk.

12a. How many of your programs currently have revenue guarantees? Have these revenue guarantees been met and, if not, how much has the Postal Service had to pay to meet these during the last five years?

Three programs have included revenue guarantees: eBillPay, Mail Transportation Equipment Service Centers (MTESCs) and, Mailing Online. The programs are in varied stages of contract performance. In the last five years, the Postal Service has paid approximately $2.6 million in guaranteed revenues under the MTESCs contracts. Mailing Online and eBillPay provide revenue guarantees of $325,000 and $1 million, respectively, for the current year. Through May 2001, no revenue guarantee payments have been made under either of these programs.

13. The Postal Service's employee bonus program has been criticized because payments have been substantially greater than net Postal revenues. In the last fiscal year, employees received $280 million in bonuses even though the agency lost $200 million.

The Economic Value Added (EVA) Variable Pay Program is not a bonus program. It is a group pay-for-performance program which covers over 84,000 non-bargaining employees. This program takes a portion of an employee's pay and makes it contingent upon the attainment of certain performance measures. The program has pre-established, measurable performance indicators, and a sophisticated formula for providing incentive credits based on organizational success. The program is not an after-the-fact "bonus" program that provides subjective evaluations of the eligibility and size of bonus payments. The Postal Service's EVA Variable Pay Program is a proven driver of organizational success and is a key component of the total compensation plan for managerial and non-bargaining employees. Certain employees gave up overtime payments in order to participate in the EVA program. None of the participants receives cost of living (COLA) pay increases.

The potential incentive under the EVA Variable Pay Program is determined by actual EVA, calculated at the end of each year. In FY 2000, although net income was negative, indexed EVA was positive. The level of EVA was a direct reflection of performance during FY 2000. Specifically, over 6.2 billion additional pieces of mail were delivered to 1.7 million additional delivery points by the equivalent of 6,200 fewer employees. This performance equates to Total Factor Productivity improvement of 2.5 percent and represents cost savings of $1.6 billion.

In Fiscal Year 2000, approximately $280 million was charged to net income for the Variable Pay Program. This is the amount reflected in employees Variable Pay Reserve Account, of which 1/3 is paid out each year.

13a. Does the bonus program provide the right incentives and motivate the right behavior? Should the bonus system be revised so bonuses to Postal executives and officers are based more on the agency's financial performance?

The EVA Variable Pay Program has been successful in providing the right incentives and motivating the right behaviors to drive organizational success in the Postal Service. The group incentive program is funded by financial performance as measured by Economic Value Added (EVA). Full incentive credits are then provided if organizational units achieve a balanced scorecard of measures focusing on our customers, our employees, and the business. [

13b. Does the bonus program include sufficient incentives for managers and supervisors to cut costs? Should gains in Total Factor Productivity be given greater emphasis?

The EVA Variable Pay Program is not a bonus program and covers over 84,000 non-bargaining employees, not just Postal executives and officers. Additionally, it is based on the Postal Service financial performance as measured by Economic Value Added (EVA). Full incentive credits are then provided if organizational units achieve a balanced scorecard of measures focusing on our customers, our employees, and the business.

The EVA Variable Pay Program provides sufficient incentives for managers and supervisors to cut costs. The EVA funding mechanism and the productivity measures under our business goals provide sufficient balance to achieve financial and productivity success without abandoning our commitments to our customers and employees.

Total factor productivity has the proper emphasis in the incentive system. This goal must be achieved by the organization in order for managers and supervisors to achieve current year payments in the Voice of the Business area. In addition, a total factor productivity is complemented with field productivity measures.

13c. The Voice of the Customer component of the bonus program is based in large part on delivery performance of First Class and Priority Mail. Does the Postal Service measure the delivery performance of all major classes of mail? If so, why aren't such performance statistics included in the bonus program? If not, why not?

The Postal Service measures delivery performance against all major classes of mail. Some of these measurements are independently measured by outside contractors, while others are measured internally. Through FY 2001, the Postal Service chose First-Class Overnight and Priority Mail as the compensable indicators under the group incentive plan to ensure a focus of all employees on these externally measured indicators that are deemed most critical to our customer service mission. For FY 2001 we intend to expand the Voice of Customer indicators to include First Class (2/3 Day) and Express Mail.

13d. At what point is the financial performance of the agency so deficient that bonuses should not be awarded?

By design, the EVA Variable Pay Program provides positive incentive credits when expenses are kept at a level to sustain our postal rates below the general inflation rate. This can occur even when the simpler financial measure of net income is negative. And since the group incentive program contains positive credits from prior years' performance, some of the credits can be paid out even if there is negative EVA. While the numbers will change from year to year, the amount needed to produce negative EVA is about $2.3 billion net income; and to deplete the incentive reserve account would be about $3.0 billion net income if the organization completely fails to achieve other performance goals. The sophisticated design of the program will make these negative incentive outcomes automatic if organizational performance is a complete failure.

The EVA measure drives the right behaviors even when there is negative net income. Remember, the business mission of the Postal Service is not like those of the private sector. While the private sector seeks to maximize their profits, the Postal Service mission is to break even over time – with revenues being restrained to cover expenses and capital requirements.

13e. We understand that amounts contained in bonus accounts for some employees are quite large. Do you see a fundamental problem with officers receiving large bonuses when the Postal Service is in such financial turmoil?

The Postal Service Variable Pay Program is not a bonus program and all employees covered by the program must accomplish measured performance criteria. The amount of incentive compensation earned is proportionated to actual results achieved and to individual base salary, and base salary is proportionated to responsibility. The exceptional performance of Fiscal Year 2000 is clearly evidenced by the TFP performance of 2.5%, equating to savings of $1.6 billion. Without this performance, directed by officers of the organization, our net loss would have been $1.8 billion. Amounts in the EVA Variable Pay Program reserve accounts are built over time and the plan has been providing positive credits since 1996. Unlike a bank account, however, these accounts can grow only if the organization is successful, and are reduced if the organization is unsuccessful. Through this mechanism, the Postal Service can put pay at risk and build a stakeholder relationship with the 84,000 technical and support staff, postmasters, supervisors and managers who can effect postal performance and customer service.

14. In the April 13, 2001 edition of the *PostCom Bulletin,* former Postal Service Chief Financial Officer Michael Riley stated that "the personnel policies of the U.S. government and the Postal Service in particular are one massive system of incentives to do the wrong thing." He further stated that [t]he right incentive system can ... save at least $2 to $3 billion per year." Do you agree with Dr. Riley's analysis in that article? If not, why not?

There are many observations and recommendations in Dr. Riley's article in the *PostCom Bulletin*. Some of his analysis contains observations with which we agree, some with which we don't. We do agree that a properly designed incentive program can produce extraordinary results for the Postal Service, as evidenced by USPS results from 1995 to present.

14a. Does the practice of downgrading managers who reduce personnel costs, and promoting managers who increase personnel costs provide the proper incentives to cut costs and increase productivity?

Managers are not downgraded in the Postal Service for reducing personnel costs and increasing productivity. Like most large, complex organizations, the Postal Service has built a management structure that provides greater levels of pay for those employees who take on greater levels of responsibility. For example, postmasters are measured under an evaluation system that provides higher-grade levels for greater numbers of customers served.

14b. Should the personnel policies of the Postal Service be modified to encourage experienced outside managers to seek employment with the Postal Service? Should, as Dr. Riley suggests, less emphasis be placed on years-in-service, and more placed on job performance and productivity improvements?

Certain policies of the Postal Service could be modified to encourage experienced outside managers to seek employment with the Postal Service. Most notably, the statutory salary cap needs to be lifted so the USPS can recruit qualified executive talent. Aside from the statutory salary cap, however, there is sufficient freedom to bring in outside talent, even with the statutory mandate to emphasize "opportunities for career advancements of all officers and employees and the achievement of worthwhile and satisfying careers in the service of the United States (39 USC 101c).

15. The IG has reported instances of improper payments to senior employees for relocation expenses. In one instance it was revealed that two Postal Service executives received nearly $250,000 just for relocating to new homes closer to their office in Washington, DC. One of these executives was paid more than $140,000 to move 2.5 miles closer to work.

15a. What controls does the Postal Service have to ensure that relocation expenses for Postal executives are appropriate?

The relocation policy for employees is well documented in policy handbooks and the Board of Governors now approves officer relocations.

Relocation payments have not been used to circumvent the pay cap.

16. The IG reported that the Service pays its executives miscellaneous relocation expenses of $10,000 or $25,000 without requiring proof of expenses incurred. These packages are up to five times the size of comparable private sector benefits.

16a. How can the Postal Service justify miscellaneous relocation payments of $10,000 and $25,000 when Fortune 500 Companies and other Government agencies are paying substantially less for similar relocation costs?

We use benchmarked data from the Employee Relocation Council (ERC), a not-for-profit membership organization whose members include more than 60% of Fortune 1000 corporations as well an numerous federal government agencies. ERC indicates that one month's salary is the common allowance for miscellaneous expenses for executives. According to ERC, 82% of these companies do not require itemization or documentation to receive the miscellaneous expense allowance. The $10,000 available to Postal Career Executive Service managers is within this "one month" standard. Officers of Fortune 500 companies receive far larger salaries, on average, than Postal Service officers (In 2000, James Kelly, Chairman and CEO of UPS, received compensation of $1.6 million and Fred Smith, CEO of Federal Express earned $4.3 million, compared to former Postmaster General Henderson's compensation of $161,800). In that context, given the congressionally mandated pay cap, the $25,000 miscellaneous expense relocation payment is not inappropriate for an officer of that level.

17. Workplace safety is one area in which the Federal government has looked to improve the overall well being of its employees. There is also a major cost factor to the USPS when an excessive number of employees are injured. Please supply the Committee with the most current information regarding the number of employees who are injured. Also, what is the Postal Service Board of Governors or Postal Management doing to address workplace injuries?

In Fiscal Year 2001 the Postal Service converted to the private sector's record keeping Total OSHA Injury/Illness Case Rate. Using a total injury/illness case rate rather than the previously used lost-time case rate places emphasis on proactive prevention of occupational injuries/illnesses as a measure of success.

The OSHA total injury/illness (I/I) case rate is the number of all OSHA recordable injuries/illnesses multiplied by 200,000 and divided by the actual number of hours worked by all employees during the course of the year. This incidence rate enables both internal and external performance comparisons.

The year to date (AP9), national rate is 7.86 compared to 7.95 for the same period last year. For AP 9 the total number of OSHA I/I cases was 44, 606 compared to 45,521 for the same period last year. If first-aid cases are included in counting injuries, the total for this year to date is 50,171 compared to 49, 479 for this period last year. In the Postal Service, the OSHA I/I rate equates to approximately 8 of every 100 employees experiencing an injury or illness. Using the latest published data (1999) from the Department of Labor, the manufacturing industry's OSHA Total Injury/Illness rate was 9.20 and the trucking and warehousing industry's (our competition) was at 8.7. Our rate is considerably lower than these two comparable private industries.

17a. What is postal management doing to address workplace injuries:

In addition to converting to the private sector's accident record keeping requirements, we also made the OSHA total Injury/Illness rate one of our important compensable indicators of our pay for performance program for management. We established a target of a 3 percent reduction on last year's end-of- year performance for headquarters, area, and performance cluster management teams.

Every performance cluster and major facility that was not achieving their OSHA Injury/Illness target by AP 7 of this fiscal year has provided headquarters with action plans to attain this year's and next year's goals. All other performance clusters that were achieving their target are to provide headquarters with their action plans by the close of Postal Quarter III. These plans will focus on improvement this year and ensure that we will begin next fiscal year with a continuous focus on reducing accident/injuries.

We have an ongoing effort with OWCP to reduce medical costs through a program to unitize the preferred provider network; we should know results by January 2002.

Accident prevention efforts continue to encourage safe work behaviors. These efforts help slow flow of injury compensation claims to OWCP.

Since AP 7 our performance has improved from only 6 of our 11 areas and 42 of our performance clusters achieving their targets to 9 of the 11 areas and 50 of the performance clusters achieving their targets at the close of AP 9.

We are also developing a five-year plan for improvement on the OSHA Injury/Illness rate and reduction of the associated costs.

18. Please describe the impact of the Board of Governors' May 8, 2001, decision to overrule the Postal Rate Commission's final recommendation in Docket No. R2000-1 on the Postal Service's operating income in fiscal years 2001 and 2002. Given this development, when does the Postal Service now anticipate hitting the debt limit? Will this development alter the freeze on capital spending?

By itself, the Board of Governors' modification of the Rate Commission's decision reinstated cost estimates disallowed by the PRC and will add approximately $200 million to this fiscal year's operating income and $1 billion to next year's.

Clearly, all other influences constant, the modification will increase Postal Service cash flow, particularly in the next fiscal year and extend the risk of reaching the debt limit from fiscal year 2002 to fiscal year 2003. The increased revenue and cash provided by the modification, however, must be analyzed in conjunction with all other factors that drive financial performance, including resumption of the Capital Investment Program. Given future uncertainties and the recent and prospective increases in debt, the Postal Service must continue to monitor its capital commitments closely. At this point, it is too soon to determine the extent to which the freeze on capital spending may be altered without impairing future liquidity.

19. At the April 4, 2001, hearing, you suggested that the Postal Service's contract dispute resolution process would be improved if it were modeled on the Railway Labor Act. What specific legislative reforms do you propose?

The Railway Labor Act, which is designed to minimize the impact on the public of labor disputes in vital transportation industries, is only one of the alternative models Congress might consult in designing a more effective contract impasse resolution process for the Postal Service. The problem is that final and binding interest arbitration, as currently provided under the Postal Reorganization Act, does not encourage the parties to make realistic bargaining decisions. Rather, the present statutory system permits a party to avoid facing up to tough decisions and allows a third party, who is accountable to no one, to resolve the dispute.

Possibly, a system based on the Railway Labor Act would provide a solution, by providing postal employees a right to strike, with necessary protections for the American public against the impact of a strike or strike threat on essential postal services. Alternatively, a less sweeping solution might make crucial changes in the current arbitration system, such as requiring the arbitrator to consider the impact of any decision on the public's interest in affordable universal postal services.

20. The Postal Service has reported that its worker compensation expenses are increasing substantially and are difficult to control. Why are these costs increasing so dramatically and what efforts are underway to bring them under control?

The Postal Service has been taking steps, within our authority, to control our workers' compensation costs:

For a number of years we have had in place a safety program that has resulted in an OSHA Injury/Illness rate that is significantly lower than those of our private sector competitors.

The Postal Service has aggressive programs to provide "limited duty" assignments to employees recovering from job-related medical conditions and rehabilitation assignments for employees with permanent job-related medical restrictions.

The Postal Inspection Service and the Office of Inspector General continues to aggressively pursue workers' compensation fraud committed by employees and medical providers.

We recently entered into an agreement with one of the largest Preferred Provider Organizations (PPO) to use their provider network to reduce our medical costs below what OWCP's medical fee schedule would allow. The pilot program was initiated during March 2001 and will be expanded rapidly if cost savings are confirmed.

However, overall management of the workers' compensation program resides with the Department of Labor. Other than initial controversion, the Postal Service has no authority to contest workers' compensation claims filed by employees and has no input into the claims adjudication process. Under current OWCP rules, Postal Service Injury Compensation staff cannot even telephone a claimant's doctor to discuss a claimant's medical condition or describe the job requirements of available limited duty positions. This has hampered our ability to craft job offers tailored to the claimant's condition and has substantially impacted our rehabilitation efforts in recent years. We believe that this plays a partial role in the dramatic increase in our workers' compensation expense seen in FY2000 and 2001.

During Fiscal Year 2000, and through March 31 of the current fiscal year, the Postal Service has experienced unprecedented increases in the cash outlays as well as the number of new and existing claims paid on our behalf by the Department of Labor (DOL) Office of Workers' Compensation programs (OWCP). We are especially concerned that the magnitude of increase in new claims is many times greater than the change in the underlying reported injuries that form, by law, the basis for these claims. DOL data indicates that the severity of our reported injuries has declined substantially while the rate of approval for new claims has increased.

In FY2000 "new" compensation claims, i.e., paid claims for injuries initially reported during the charge-back year ending June 30, 2000, increased by 27.9 percent. During this same period reported injuries increased by only 5.9 percent. Moreover, the Department of Labor reported much of the increase in our reported injuries as either "first aid" or "no lost time" injuries. Historically, injuries of this type did not receive workers' compensation. Approved new compensation claims, both in terms of absolute numbers and relative to reported injuries, have continued at historic highs through FY2001. In FY2000, "new" medical claims increased by 8.0 percent. The level of approved new medical claims also has continued at record levels in FY2001. Both the FY2000 and FY2001 "new" medical claims levels are in excess of the changes in the underlying reported injuries.

The FY2000 charge-back from the DOL was $638 million, an increase of approximately $73 million or 12.9 percent. We anticipate a FY2001 charge-back of approximately $695 million, exclusive of the DOL "fair share" administration fee, the fee DOL charges USPS and other agencies to cover their administrative overhead. (The DOL has informed us that this fee will increase by over 50 percent to more than $30 million in FY2001. Only non-appropriated agencies are assessed this fee.)

In FY2000 total paid compensation claims (i.e., for employees injured in FY2000 plus all prior years since Postal Reorganization) increased by 8.5 percent. Year to date, in FY2001, the numbers of the claims paid has increased further, although at nothing near the FY2000 rate.

In FY2000 total paid medical claims increased by 7.0 percent. Year to date, in FY2001, this trend has also continued, albeit at a slower pace.

In FY2000 the average cost per medical claim increased by almost 14 percent. This has moderated somewhat in the current year.

We continue to discuss these trends with DOL in order to pursue improvements to the system and to our performance.

21. In January 2001, the Postal Service entered into a seven-year, $6 billion contract with Federal Express for air freight delivery services for Priority, Express and First Class mail. A number of concerns have been raised about this contract. Specifically, concerns have been raised that the contract was unfairly awarded by the Postal Service since other companies were not given a chance to bid.

21a. Please explain the rationale used by the Postal Service for not competing this contract.

The Postal Service recognized that the competitive bidding process did not lend itself to the very complex task of linking its transportation system, which is one of the largest in the world, with that of a contractor. Instead, the Postal Service approached this matter much as a private sector business would: It determined which carrier was the most likely to meet its needs, and subsequently engaged in extensive negotiations to ensure that the contract was commercially reasonable. The Postal Service drew upon its own knowledge and experience with the air transportation industry, and on a market study performed by PricewaterhouseCoopers (PWC). In preparing its market study PWC relied upon publicly available information. The study exhaustively analyzed the capabilities of many air transportation contractors prior to deciding that FedEx was the only one that met the Postal Service's requirements.

The Postal Service established several requirements for this contract. Two of those key requirements were that the air transport contractor be financially stable and have what is known as a "shared network." A shared network is essentially one which transports mail from a number of customers, thereby providing services at a cheaper cost since all the customers support a portion of the contractor's overhead costs. Currently, the Postal Service uses a series of "dedicated networks." These dedicated networks transport only Postal Service products. Thus, the contractors' overhead costs are not apportioned to any other customers, and consequently, will be higher than those associated with a shared network.

21b. What savings would have been realized had the contract been competed?

As stated in the answer to 21a, these requirements did not readily fall within the competitive contracting procedures outlined in our contracting regulations. As a result, in accordance with Postal contracting regulations, the agreement with FedEx was negotiated and awarded on a sole source basis. It would be inappropriate to speculate whether the Postal Service would have realized any additional savings had the contract been competed, since competition in this instance was not feasible or appropriate.

It should also be noted that it is the policy of the Postal Service to award contracts to the suppliers offering the best value. The Postal Service conducted an exhaustive analysis of many air transportation contractors prior to deciding that FedEx would provide the best value to the Postal Service.

21c. How did the Postal Service ensure that Federal Express would not obtain an unfair competitive advantage by virtue of this contract?

The Postal Service must purchase such goods and services as are necessary to fulfill its mission of timely mail delivery. In this instance we determined, among other things, that a shared network would be the best way to meet certain mail delivery needs. Further, in this regard the Postal Service chose FedEx as the supplier that offered the best value to the Postal Service for meeting those needs.

With respect to any perceived limitation on competition, it should be noted that the agreement between FedEx and the Postal Service was submitted to the Department of Justice's (DOJ) Anti-Trust Section for review shortly after it was executed on January 10, 2001. Representatives from the Postal Service and FedEx have been diligently working with DOJ representatives to assist them in their understanding and review of the agreement. To date, DOJ has not issued an opinion in the matter.

21d. Also, what contingencies have been developed by the Postal Service for the delivery of the mail in the event Federal Express is unable to perform under the contract?

The Postal Service has always had contingency plans in place in the event there were performance failures associated with its air transportation contractors. Those same plans would apply to performance failures on the part of FedEx.

In the event there were isolated performance failures of short duration, the Postal Service would repossess any tendered mail and combine that mail with the other untendered mail for that market(s). After determining the most efficient alternate transport method, that mail would either be trucked or placed on commercial carriers until the performance failure was abated.

In the event of a more widespread, long-term performance failure (to include a total performance failure), the Postal Service would be required to make two determinations. First, on an interim basis, a determination of the most efficient alternate transport method would be made. Pursuant to that determination, mail would either be trucked or placed on commercial air carriers.

In addition to establishing interim service, the Postal Service would investigate and determine the availability of alternate air carriers. A contract would be awarded to the carrier or carriers that best met the needs of the Postal Service.

22. What measures is the Postal Service taking to mitigate the impact of rising fuel costs?

To minimize fuel costs the Postal Service considered a number of fuel purchasing, fuel delivery vehicle mileage reduction strategies, that could significantly reduce the cost per gallon of fuel, leverage the Postal Service's purchasing power, reduce vehicle usage (and eliminate the need for fuel). The following were initiated:

An Internet reverse auction was used to receive bids for the eastern seaboard of the United States so the Postal contract transportation suppliers or fuel retail stations servicing Postal contractors could purchase fuel in bulk at a reduced price. Those reduced prices would be captured by reducing the rate per mile of our contractors. The effective date was November 2000. The reverse auction was not as successful as hoped so the remaining areas of the United States were competitively bid but had not been awarded as of May 30, 2001. Once fully implemented the program is expected to avoid $25 million in fuel costs each year.

The Voyager card, which is part of the GSA SmartPay program, is being used and is allowing the Postal Service to capture tax data on its purchases. The card is structured such that many state excise taxes are exempted at the time of purchase reducing the total cost of the fuel. Where possible, the taxes not exempted at purchase, but refundable are being pursued for refund.

An initiative was developed to review most contract transportation routes to look for redundancy and combine or eliminate service. To date 28 million miles per annum have been eliminated, which reduces our dependency on fuel by approximately 4 million gallons.

A comprehensive Fuel Management Business plan has been developed but not finalized or approved; we anticipate a late FY 2001 approval with implementation starting in FY 2002.

In addition to the Business Plan, an initiative is being developed to review most Postal Vehicle Service transportation (service owned and operated by the US Postal Service) that will look for redundancies, similar to the contract transportation routes reviewed this Fiscal year, further reducing our dependency on fuel.

23. Comptroller General Walker, in his written testimony before the Committee on April 4, 2001, stated that during the 1990's Total Factor Productivity increased only 1.6 percent. This was less than each of the two proceeding decades. Why did TFP increase by such a paltry amount in the 1990's, especially in light of the Postal Service's investments in automation and other technology for improved productivity?

Postal Service productivity during each of the preceding three decades is shown in the table:

Decade	% TFP Growth
1970-1979	6.9
1980-1989	0.3
1990-1999	1.9

Total Factor Productivity during the 1990's was less than TFP growth during the 1970's and higher than TFP growth during the 1980's. Three factors contributed to the lower than average productivity growth in the 1990's: 1) Efforts to improve customer service and satisfaction, 2) Technology and infrastructure investments to improve distribution, delivery, and service, and 3) Worksharing programs

Customer service and satisfaction improvements:

TFP growth was lower than average during the 1990's because the Postal Service invested substantial sums in improving customer service and satisfaction. While many of these efforts have had a short-term negative impact on productivity, the Postal Service has deemed the service and customer satisfaction benefits to outweigh the costs. Through the 1990's service performance for First-Class Mail improved from 84 percent to 94 percent on-time delivery. The percentage of customers who viewed overall Postal Service performance as excellent, very good, or good, grew from 85 percent to 92 percent. While the "value" of service quality improvement is not captured in the TFP measure, it is essential to the long-term future of the organization. Though some service improvements may adversely impact productivity, management believes that the benefits of improving service outweigh the negative impact to TFP

Technology and infrastructure investments:

During the 1990's the Postal Service invested heavily in technology and infrastructure to improve the distribution and delivery of mail, and reduce labor costs. This includes purchasing delivery bar code sorters, additional remote bar coding systems, and point-of-service retail terminals. It is not unusual to see slow or declining productivity growth during periods of rapid capital expansion or major capital investments. A surge in capital investments will impact productivity in the short term, as the investments are made to provide a return over time. The Postal Service began to see positive productivity returns on these investments beginning in the fourth quarter of 1999 when TFP increased 2.3 percent compared to the same quarter of the previous year. TFP has been positive in every subsequent quarter.

Worksharing programs:

Worksharing discounts that were introduced in the 1980's provide cost savings for the Postal Service and our customers, but also impacted TFP gains. Worksharing incentives shift a greater proportion of the workload associated with automation compatible mail to business mailers. While improving the productivity of the economy as a whole, prime productivity improvement opportunities have been transferred outside the Postal Service. Work sharing discounts continued into the 1990's. As higher and higher levels of efficiency are achieved, incremental productivity improvements become more and more challenging.

In FY 2000 TFP increased 2.5 percent, which is equivalent to reducing expenses by $1.6 billion. This achievement was significant in that it was achieved largely by a substantial reduction in resource usage. Previous TFP increases of this magnitude were largely fueled by workload increases. Further reductions in resource usage continue to drive positive TFP results in FY 2001. TFP has increased by 2.0 percent, to-date in FY 2001 against a projected year-to-date increase of 1.3 percent. This represents a cost savings of over $900 million.

24. Governor Fineman, in his written testimony, noted that since 1995, the Postal Service has increased the First Class rate less than the rate of inflation.

24a. Have any subclasses had rates increase by more than the rate of inflation since 1995?

(a). **Yes.**

24b + c. If so, which subclasses? What has been the percentage rate increases for those subclasses?

The inflation rate as measured by CPI for the period January 1995 through July 2001 (the date that rates are to change) is 18.7%. Those subclasses that will have increased more than the rate of inflation are:

Priority Mail (23.8%)
Classroom Periodicals (26.1%)
Bound Printed Matter (24.3%)
Library Rate Mail (81.3%)

Questions submitted by Congresswoman Ileana Ros-Lehtinen:

1. Considering that the Hispanic population has grown dramatically in various parts of the country, what steps has the United States Postal Service taken to attract the Hispanic market with its high percentage of buying power?

Reaching out to the multicultural marketplace has been established as a business goal. Focus of our efforts has been on both our customers and the communities we serve. These activities are designed to showcase postal products and services and establish partnerships between the community and the Postal Service.

In 1996 the Postal Service's Marketing Advisory Board, a volunteer group of accomplished private sector senior executives and entrepreneurs, recommended the USPS pursue marketing opportunities in the growing multicultural marketplace. In March 1997, acting upon this recommendation, postal management created, staffed and budgeted a specialty markets program to oversee USPS efforts to generate new revenue from African American, Hispanic, and Asian market segments. Since the formation of this group, the USPS has been very active marketing to multicultural markets. In the Hispanic market, the USPS has been a regular advertiser on Spanish-language television, radio, magazines, and newspapers.

In the year 2000, the Postal Service began communicating the importance of multicultural markets to the entire postal and mailing industry. At the National Postal Forum, the premier mailing industry trade show, the USPS convened a panel of multicultural marketing experts. This general session before thousands of Forum attendees highlighted the USPS recognition of the buying power of the multicultural marketplace with particular emphasis on the Hispanic market. This session led directly to a major accomplishment for the USPS, the launching in September 2000 of its Spanish-language Web site, www.usps.com/correo.

Other activities have included:

- **Expansion of our Sure Money service, "Dinero Seguro" to 2000 more sites, with additional sites to be added by this summer. This international funds transfer service from the United States to Mexico was first tested in 870 offices in California, Texas and Illinois with great success.**
- **Development of a diversity component to the training program for Retail Associates to ensure recognition of all customers.**
- **Updating of the *Hispanic People and Events on United States Postage Stamps* publication, which is in English and Spanish and is used to showcase postal stamp products at community events and activities.**
- **Developing *Let's Do Business Guide* for small, minority, and women-owned businesses in both English and Spanish.**
- **Updating the Associate Supervisor training module for customer service to include understanding of both the business needs of the multicultural community and the individual customer needs that signage efforts provide.**
- **Sponsoring the Hispanic Chamber of Commerce conference, to promote business development efforts in the Hispanic Community, with emphasis on conducting business with USPS. We also work throughout the year on local and regional events that further leverage our products and services directly to the Hispanic market.**
- **Partnering with other national Hispanic organizations that provide ongoing opportunities for us to promote the value of conducting business with the USPS and to address the needs of the Hispanic community (LULAC, LARAZA, IMAGE Inc., National Hispanic Society, Hispanic Chamber of Commerce, Cuban Foundation, etc.).**
- **Conducting community recruitment efforts for postal jobs including pre-test workshops to help applicants get ready for the postal examination.**

- **Surveying our diverse customers to identify any special needs they have in conducting business with the Postal Service, including signage, specialty products, and other services.**
- **Entering into a Special Agreement with KMART in Puerto Rico to use postal vehicles to promote their own credit card. This is the first time postal vehicles have been used for advertisement. The vehicles will feature Spanish-language signage advertising the credit card in selected neighborhoods in San Juan, Bayamon, Carolina, Guaynabo, and Rio Piedras. The campaign is designed to reach over 25 percent of the island's population that live in the San Juan area.**

2. Are there bilingual personnel at the United States Postal Service to address the needs of customers in areas where a majority of customers are not fluent in the English language?

We recognize that this is a service that would be beneficial in many communities. Some local post offices have assigned supervisors with bilingual skills to high-traffic retail locations to help with lobby lines and complex postal transaction activities. We will also be exploring the possibility of adding a bilingual requirement to our retail associate positions in high volume Hispanic communities.

Our Atlanta performance cluster provides an excellent example of ways to reach bilingual customers. They are currently in the process of conducting lobby director training for their bilingual employees. They have also allocated additional hours for those offices with a highly diverse presence and will be tracking the increase in revenue and customer satisfaction against last year's results.

Bilingual Signage Translations
To meet the needs of our limited and non-English speaking customers, we are developing and translating instruction sheets for the most commonly used postal forms into key languages for ease of use. The forms to be translated are Signature Confirmation, Delivery Confirmation, Insurance, Mover's Guide, Post Office Box Application, Customs Forms, Global Express Mail, International Express Mail, Express Mail (domestic), Registered Mail, Domestic Money Orders, and Certified/Return Receipt Requested. The form instruction sheets will be translated into Spanish, French, Chinese, Vietnamese, Japanese, German, Russian, Filipino, Korean, Hindi, and Somali. The translated information will be distributed in targeted locations such as New York, Los Angeles and San Francisco.

Multicultural Small Businesses Targeted
We have established ongoing coordination and partnerships between Retail, Marketing, Consumer Affairs, and Diversity Development to ensure that we are meeting the needs of our customers and expanding opportunities to grow our business. This spring, an integrated advertising effort targeting small businesses has been launched nationwide. As part of this campaign, multicultural businesses in ten major markets have been targeted with TV, print, and radio advertising. The advertising directs these businesses to our Web site, usps.com, which has been enhanced with multilingual pages to provide businesses the specific customer acquisition, fulfillment or retention tools and information they need.

Questions submitted by Congressman Felix Grucci:

1. General Henderson, as you may know countless main streets and their small businesses across the nation depend on the Post Offices for both their services as well as the customers they attract.

That being said, what if any consideration did the Postal Service Board of Governors take when they decided to freeze all capital commitments for this year. In particular did the Board consider the impact that a freeze on capital would have on both the Postal Services as well as on the economy of so many communities?

The Board and management were aware of the impact and the risk taken when it froze capital commitments. The freeze on capital commitments was a fiscally responsive action taken to ensure that cash is available to meet current obligations. Although planned commitments have been reduced in fiscal year 2001 and will probably be reduced in 2002, we will still have capital outlays of approximately $2.7 billion and $2.2 billion in 2001 and 2002, respectively. These expenditures will be for investments in infrastructure and for labor replacement efficiency investments that have already been contracted. We expect that the freeze on new contracts will continue at least through this fiscal year. We will continue to plan for additional projects that produce productivity gains and contract for them when funding is available. We will also proceed with selected investments related to health and safety of our employees and customers, all legal requirements and other emergencies.

The action to freeze new capital commitments was done recognizing that in the long run this could have a negative impact. Given our financial situation there was no choice. Continuing to proceed with additional investments when the funding was not going to be available was not an option. We will monitor the impact of delaying major investments and will take action to sustain operations until funding is available to make improvements.

Questions submitted by Congressman Tom Allen:

1. Are you aware that the workplace environment in Southern Maine postal facilities is often portrayed as hostile by its workers?

Yes, we are aware that some of our employees feel the work environment at some postal facilities is considered hostile. A number of initiatives have been implemented in the Maine performance cluster to create a positive, welcoming work environment. Those initiatives include personal outreach by the district manager in conjunction with the lead plant manager and key staff members, through communications with over 600 employees at town hall meetings, round-table discussions, and informal sessions about workplace environment issues. These ongoing communications with employees include:

- **Discussion of sexual harassment.**
- **Establishment of an Employee Speak Out line, a toll-free phone line for employees to share or seek information about workplace issues.**
- **Establishment of quarterly round-table discussions with employees to ensure ongoing dialogue about workplace issues, including sexual harassment.**

The Maine performance cluster has also sponsored key events during Women's History Month, including a health fair for women, and a joint celebration of women in the postal workplace with the Maine state coordinator for the National Organization for Women (NOW). The cluster also created a Women's Alliance Network to support, encourage and empower women in the Maine performance cluster, as well as to provide developmental assistance; and expanded a local mentoring program to include an additional 25 women. The USPS has also created an area-level Women's Advisory Council, composed of key female executives in the Northeast Area, to provide ongoing support and input to the Maine leadership for additional initiatives.

These initiatives reflect strategies implemented to date. The district manager and the area vice president are committed to continued focus and attention to these issues.

1a. Aside form the widely publicized sexual harassment cases, postal workers have complained to me about ethnic comments, religious insensitivity, and other work-related problems. What does the Postal Service plan on doing about this?

The USPS requires four hours of training for all employees to address workplace issues. One hour of the training each year has focused on workplace violence awareness. By definition, workplace violence includes not only physical violence but also insensitive and abusive communications. The remaining three hours are intended to address such topics as conflict management, ways to improve communications, and understanding.

Supervisors and managers will also be able to take advantage of a newly created communications lab program that will be piloted and ready for general use beginning in fiscal year 2002. The lab provides instruction and practice for supervisors and managers in how to communicate more effectively with peers and subordinates when addressing work performance, providing work instructions and settling conflicts.

For the last two years, the Variable Pay Program has included a measure based on scores from a survey of postal employees to six key questions that address the work environment. This measure will continue in FY2002. Human Resources serves as a clearinghouse and an advisor to the field in improving the work environment as measured by the survey and other key indicators.

Communications surrounding discipline and dismissal create the most potential for misunderstanding, elevated emotions, and conflict. A guide for how to appropriately manage discipline situations that could lead to dismissal was recently revised. The guide, *Professional Parting*, describes in detail the roles and responsibilities of supervisors and managers as well as union officials in working through the process.

Several of these initiatives were referenced in the report of the USPS Commission on a Safe and Secure Workplace, issued last August. The report made recommendations in a broad range of areas for improvement of the postal work environment. A cross-functional task group is working to implement the commission's recommendations as soon as possible and we anticipate that a significant number will be implemented by the close of FY2001.

The Postal Service is firmly committed to eliminating sexual and other harassment through awareness, education, and enforcement of our zero tolerance policy. The policy makes two points abundantly clear: first, that sexual harassment is illegal and will not be tolerated, and second, that employees who sexually harass other employees will be disciplined or removed from the Postal Service. It must be noted that many of the cases filed against the Postal Service do not rise to the level of the legal standard of sexual harassment. Rather, some cases are indicative of workplace climate issues that are currently being addressed in forums such as mediation.

A comparison between the Postal Service and other federal agencies illustrates a more accurate picture of our record on workplace climate issues. For example, the Merit Systems Protection Board reported that 15 percent of male and 33.9 percent of female employees surveyed in the federal sector had experienced sexually harassing behavior in the preceding two years. The Califano Report and the Voice of the Employee (VOE) survey results, however, suggest that the base rate for perception of being harassed by postal employees in fiscal year 2000 is about 3 percent to 6 percent, which is substantially less. Whether instances rise to the level of sexual harassment *per se* or are workplace climate issues—we are taking bold and clear definitive steps to prevent them.

It is our responsibility to ensure that swift action is taken in each and every case—one instance or one case is one too many. Additional future plans include the development of a lecture series on sexual harassment prevention and awareness best practices and enhancing our current online sexual harassment Web toolkit. We are also reviewing our recruitment, orientation, and leadership development tools to identify gaps regarding sexual harassment materials. We are certifying additional employees to serve as sexual harassment prevention facilitators when intervention activities are necessary. Our ultimate goal is to treat every employee with dignity and respect; therefore, we are working to identify and analyze trends identified in the Califano report, EEO complaint and VOE survey data and to develop new strategies to address sexual harassment and other workplace climate issues.

2. Since my election in 1996, postal employees have frequently contacted me as a last resort, with complaints about insensitivity in the workplace. Now, instead of greater accountability to Congress, the Postal Service has testified that they need less oversight from Congress. My chief of staff recently met with Elizabeth Johnson, the Postal Service's District Manager for Maine. Ms. Johnson outlined plans to improve the workplace environment. Can you assure me that you will work with Ms. Johnson to ensure that her plans to address workplace harassment will be successful? Without effective Congressional oversight what guarantees do Members have that their constituents concerns are being taken seriously?

Yes, in fact some of the activities implemented in Maine will be mirrored nationwide. For example, our current plans include holding a series of town hall meetings in locations where employee concerns are greatest. In addition to the activities discussed above, headquarters continues to support the Maine performance cluster as well as all other areas through weekly communications from management, prevention and awareness posters, mandatory training for all employees, training and awareness videotapes, service talks material, and employees' and managers' guides. To ensure success, we will also support the Maine District by closely monitoring any activity, conducting periodic on-site reviews, and offering hands-on guidance related to training and prevention activities.

In fiscal year 1999, the Postal Service made it a requirement to train all 800,000 craft and EAS employees on sexual harassment prevention and awareness. Next year, plans include additional mandatory sexual harassment prevention training for all 800,000 postal employees.

In addition, we disseminated publication 552, *An Employees Guide to Understanding Sexual Harassment*, to every employee's home, and publication 553, *A Supervisor's Guide to Understanding Sexual Harassment*, was given to all supervisors and managers. In calendar year 2000, postal attorneys conducted 181 briefings on sexual harassment prevention as well.

We have also developed a comprehensive action plan that ensures cross-functional implementation and messaging. Our goal is to disseminate information on a consistent basis. Last month, new sexual harassment prevention and awareness posters were shipped to facilities nationwide. Most recently, memoranda to the officers and statements from the chief operating officer; vice president, Diversity Development; and senior vice president, Human Resources, have appeared in numerous postal media reaffirming our commitment to providing a workplace free of sexual harassment and inappropriate behavior.

We are also updating our sexual harassment policy as well as our *Manager's Guide to Understanding Sexual Harassment*, *Employee's Guide to Understanding Sexual Harassment*, and Initial Management Inquiry Process materials. We are working cross-functionally to determine appropriate follow-up for pending complaints and to develop new strategies to address inappropriate workplace behavior, such as conducting periodic site inspections.

Additional training on sexual harassment has been and will continue to be provided to all employees, supervisors, managers and postmasters. Moreover, a series of service talks have been developed for delivery to all employees during the months of June and July. The Maine performance cluster also maintains contact with key union and management association representatives to quickly identify locations where sexual harassment issues or concerns may exist. Each of these proposals, activities, and initiatives is designed to ensure that not only the Maine Performance Cluster, but the entire Postal Service workplace environment, is successful in addressing workplace climate and sexual harassment issues.

Questions submitted by Congressman Danny Davis:

1. Is the postal service going to increase postal rates? If so, when and by how much?

The rates as modified by the Governors, which amount to an average increase of 1.6 percent increase, will be implemented on July 1, 2001. Bearing in mind that it requires about a year from the time rates are proposed to the time new rates are implemented, the Postal Service is planning to file for new rates before the end of this calendar year. It had previously appeared that this rate increase might be in the range of 10 to 15 percent.

1b. Will ratepayers bear the brunt of the postal service's financial difficulties?

As you know the Postal Service does not receive any subsidies from the Federal treasury. In any organization that is self-sustaining, those who use the services must pay for them. Despite our successful achievements in automation, productivity gains, reduction of career complement, and other areas, we are in the position of having to raise rates next year to generate income to cover current and projected losses. Mailers in 2001 and 2002 will have received the equivalent of a $3 billion loan because rates will not have covered the costs of the postal system in those years. Such "loans" draw cash from the Postal Service. Rates need to be increased to enable the Postal Service to generate the cash that it needs to operate.

2. Why can't the postal service cut its costs more rapidly to respond to changing conditions?

The answer to this question lies in the nature of Postal Service costs. Data for FY 2000 show that only 58% of Postal Service costs are considered "volume variable", or costs that vary as volumes increase or decrease. The remaining 42% can be considered "institutional or fixed costs." While these costs can change over time, in the short run, they will remain the same. The Postal Service needs to maintain a significant infrastructure of buildings, vehicles, transportation and delivery networks, etc. These costs cannot be cut quickly in response to declining volumes. Our delivery network is a good example. We go to (or by) every house and business 6 days per week (5 days for most businesses) regardless of the mail volumes. Our delivery network steadily expands, even though volumes may be flat or declining.

We have considerable costs relating to retirement for Postal Service employees. These costs relate to employees who have already retired and do not vary according to volumes. Our injury compensation costs approximate $1 billion annually, including the cost for Post Office Department employees who were injured prior to the Postal Reorganization Act of 1971. Most of these employees have been on compensation rolls for some time.

Labor contracts limit our ability to use more flexible employees such as part time and casual employees. Although casual employees may be eliminated at any time, there are "no-layoff" provisions in our contracts that limit our ability to quickly reduce the number of both full-time and part-time career employees.

3. Is the postal service really on track to lose $2 billion to $3 billion?

The $2 billion to $3 billion loss projection was updated May 2001 to a $1.6 billion to $2.4 billion loss. The change in the estimate was based on the BOG rate modification and additional expense reductions from program spending cuts and an administrative hiring freeze. The loss projection continues to be driven by revenue shortfalls, which for the first nine accounting periods of this year are approximately $1 billion less than plan.

3a. Given the number of times the numbers have changed, what assurance can you give us that these deficit projections can be trusted?

The current projection is based on known and expected costs, and forecasted revenue, with the greatest uncertainty related to revenue growth. However, as with Corporate America and state and local governments, our revenues are coming in below expectations. This primarily relates to the softening of the economy. As recently as last fall, none of the mainstream economic forecasters were predicting the weakness that has since become apparent. It has always been difficult for forecasters to predict turning points in economic growth patterns. We have just gone through one of these transitions and have reacted very rapidly to it in terms of updating the Postal Service forecasts. Even with the uncertainties experienced in predicting the economic events of this year, however, the projected $2 billion loss means that our expenses exceed revenues by only 3%.

4. How confident are you in your mail volume estimates?

The Postal Service maintains numerous data systems that provide accurate volume estimates. The volume data are scrutinized by the Postal Rate Commission, the General Accounting Office and outside auditors. While no data series can ever be free of error, our mail volume estimates have generally been quite good, within about one percent of actual volumes.

Given the size and magnitude of the Postal Service, however, even a small forecasting error can lead to a significant swing in Postal Service finances. A one-percent swing can result in a revenue shortfall of $700 million or more, which combined with an inadequate rate recommendation and increasing cost inflation, could place the Postal Service's finances seriously out of balance. This is essentially what has happened over the last year and one-half.

[NOTE: FOR GFY 2000 FIRST-CLASS MAIL VOLUME GREW 1.6% THROUGH Quarter 3 OF FY 2001 FIRST-CLASS MAIL VOLUME GREW 0.3%.]

5. Do you believe that the postal service needs to continue to automate its core business functions given the $2 billion loss?

Yes, based on the proven benefits of automation, the Postal Service needs to continue to improve operations through reengineering and technological advancements including further automation and other mechanized handling projects.

5a. If you do not automate, what will be the impact on postal operations in the future?

If we do not continue to automate and invest in other technologies, postal operations will be less efficient and more costly because so many of the Postal Service's operations are labor-intensive. With labor costs accounting for about 76% of Postal Service costs, we must identify and deploy the latest technology and automated equipment.

6. Have you received the labor savings you anticipated from automation? Have these positions been reduced?

Automation is producing savings and cost avoidances greater than original projections. Since 1987 we have invested $5.4 billion in letter mail automation projects and through 2000 we have achieved approximately $19 billion in savings/cost avoidances against original projections of about $18 billion. Operating budgets in the areas impacted by operations have been reduced and will continue to be reduced. Productivity gains have been realized this fiscal year. Career complement has been reduced by over 21,000 since its peak in 1999.

7. How reliable are postal revenue and expense projections in predicting the effect of economic downturns?

Economic downturns are difficult to project. Unforeseen economic downturns are almost impossible to predict -- and their impacts unprojectable. The Postal Service employs nationally prominent economic analysts, the same used by corporate America, and endeavors to plan for estimates of economic change. This is reflected in our revenue, volume and expense forecasts. The most recent economic slowdown occurred very rapidly, however, as demonstrated in the business pages of newspapers in recent months as business after business has reported disappointing earnings and reduced earning projections. The Postal Service has been impacted similarly to virtually every major U.S. Corporation.

As recently as December, most mainstream economic forecasters were not projecting the slowdown that has occurred in the first two quarters of this calendar year. This slowdown was not reflected at that time in the independently produced macro forecasts that the Postal Service purchases from DRI (now DRI*WEFA). Further, in its November rate decision, the Postal Rate Commission found "the short-term outlook does not appear to involve any risk of unforeseeable financial harm to the Service. " PRC, Docket No. R2000-1, November 13, 1991 (Emphasis added).

8. Do you support NSA's based upon guaranteed mail volume? If yes, what are your plans to implement NSA's on a broader, larger scale and when do you expect the postal service to move in that direction?

The Postal Service believes that any NSA that is beneficial to both the Postal Service and the mailer and which does not cause any harm to nonparticipating mailers should be considered. Depending on the merits of the specific proposal, this potentially could include NSAs which include a customer's guarantee to tender a specified volume of mail as one of the provisions. Plans to move forward with NSA's on a broader scale are being carefully reviewed.

9. Could you describe some of the type of benefits a NSA will produce?

NSA's hold the potential for many types of benefits. An NSA might result in more mailer worksharing and reduced costs to the Postal Service. An NSA might result in new volumes and increased contribution to the Postal Service. An NSA might provide the opportunity for the Postal Service to test a new premium service or new processing steps or delivery practices.

9a. What resources are you allocating to expedite the implementation of NSA's?

The Postal Service has been actively studying NSAs for more than a year and has worked with individual mailers who are developing NSA proposals for consideration. To date, however, none of these customer-specific proposals has been refined sufficiently to bring before the Postal Rate Commission. In addition, over the past several years, the Postal Service has brought cases to the Postal Rate Commission, which have been, in effect, "niche" classifications that address the needs of small groups of mailers. These types of classifications have sometimes been referred to as "de facto" NSA's. A good example of these is the classification for nonletter-size Business Reply Mail, which was established first as an experiment and then as a permanent classification. We plan on continuing to explore further such ideas.

At the same time, the Postal Service always must weigh the benefits versus the costs of any proposal. Any filing before the Postal Rate Commission is a fairly resource-intensive undertaking as evidence must be prepared and documents and testimonies must be produced. Following the filing of a request, technical witnesses and attorneys must be prepared to answer questions for a month or more before testifying. Given the nature of these proceedings, there are a limited number of people sufficiently versed in postal economics and law to successfully meet the challenges. Also, their skills may be needed elsewhere.

While there certainly may be potential NSA's that make sense, under our current regulatory environment they are time-consuming and costly relative to the expected increase in contribution. Therefore, while we fully intend to pursue NSAs, we need to do so wisely.

9b. Are you working with the PRC to realize NSA's?

Yes. As mentioned above, the Postal Service has worked successfully with its customers and the Postal Rate Commission to gain approval of various "niche" classification proposals that meet the needs of small groups of mailers. At the same time, we would invite the Postal Rate Commission to develop a means for handling these cases in a manner that better reflects their size and scope. While the Postal Rate Commission's rules allow for expedited consideration under certain circumstances, it is entirely possible that even a small filing can consume significant resources in litigation. We would like to work with the Postal Rate Commission to develop a process that will allow for more rapid consideration of NSAs and other limited classification and rate changes while ensuring that the public interest and due process rights of our customers and other intervenors are protected.

10. Since NSA's are a kind of cost-saving experiment focused on an individual mailer, can't the postal service use the experience and information it gains in the process to make system-wide changes to improve efficiencies and lower costs?

Yes. We believe that system-wide changes may result just as readily from the experience and information gained through a range of NSA's, "niche" classifications, or other types of experimental cases. The Postal Service continues to be interested in improving efficiencies and lowering costs for the broadest range of mailers possible. However, unless the approval process for small rate or classification changes is further streamlined, it will be difficult to implement many experiments that could provide data that would later result in system-wide cost savings.

11. The Office of Inspector General recently released a report on the postal service budget in which they recommended that a cost accounting system be developed. What action have you taken on this recommendation? Do you know how much it will cost? What is the downside if you do not fund such a program?

In reviewing the recommendation, the Postal Service determined that the concerns identified in regard to "cost accounting" actually revolved around the ability to track commitment activity on purchase orders. As we noted in our response to the Inspector General, we are continually considering new and enhanced accounting and financial systems. However, it is not financially feasible to do so at the present time. Cost estimates of purchasing and installing a new general ledger system that would support management and cost accounting functions could easily approach $100 million. We are in the early stages of researching acquisition of a new general ledger system, with a target to transition to the new system in FY 2004. When we formally evaluate system alternatives, we will consider the costs and potential benefits of various features. Also, we are beginning to roll out activity-based costing systems in our plants, with the expectation that the roll-out will expand as the value of the increased management information proves itself.

Questions submitted by Congressman Henry Waxman:

1. In the past five months, the Postal Service has changed its projected deficit from $480 million to $960 million, to $1.3 billion. The Service is now saying that the deficit will be in the $2 to $3 billion range.

1a. Why didn't the Postal Service see this coming earlier?

Revisions to Postal Service estimates have been driven by rising inflation and softening revenue directly related to the weak economy. As recently as last fall, none of the mainstream economic forecasters were predicting the weakness that has since become apparent. It has always been difficult for forecasters to predict turning points in economic growth patterns. We have just gone through one of these transitions and have reacted very rapidly to it in terms of updating the Postal Service forecasts. Each update was a reaction to a major event and is described below.

In January 2000, when the R2000-1 Omnibus Rate Case was filed, the estimated net income for FY 2001 was $500 million. When the strategic plan was developed in the summer of 2000, the FY 2001 net income estimate was updated to reflect recent events. Cost estimates were increased by $300 million to reflect recent fuel inflation. Bargaining unit employees wages that include cost-of-living adjustments linked to CPI were increased $430 million to account for more recent CPI projections and interest and other expenses were updated by $170 million. These cost increases were offset by new management developed Breakthrough Productivity Initiatives that reduced costs by $550 million. The net result was a projected $150 million net income for FY 2001.

By October 2000, when the Board of Governors approved the FY 2001 operating plan, it was apparent that revenue projections were optimistic based on actual performance in FY 2000. Specifically, the forecast used for the Strategic Plan projections assumed revenue shortfalls of $600 million in FY 2000. The actual shortfall was well over $800 million. Accordingly, $630 million for First-Class and Priority Mail revenue growth was removed from the FY 2001 operating plan resulting in a net loss projection of $480 million.

In January 2001, the FY 2001 net loss estimate was updated to reflect the impact of Postal Rate Commission Decision that reduced the size of the rate increase requested by the Postal Service in the R-2000-1 docket. This reduction had a $800 million impact and increased the FY 2001 net loss estimated to $1.3 billion.

In February 2001, the net loss estimate was further revised to incorporate Quarter I, FY 2001 results and a new volume and revenue forecast that reflects more recent economic conditions. This update produced an estimated additional shortfall in revenue for the remainder of the year between $500 million and $1.5 billion depending on the extent of the soft economy and was the basis for the net loss forecast between $2 billion to $3 billion.

Reflecting the Governors decision to modify rates by an average of 1.6 percent effective July 1, 2001 and management actions to reduce expenses, in May 2001 the FY 2001 net loss estimate was revised to $1.6 billion to $2.4 billion.

1b. How reliable are Postal Service revenue and expense projections in predicting the effect of economic downturns?

Economic downturns are difficult to project. Unforeseen economic downturns are almost impossible to predict -- and their impacts unprojectable. The Postal Service employs nationally prominent economic analysts, the same used by corporate America, and endeavors to plan for estimates of economic change. This is reflected in our revenue, volume and expense forecasts. The most recent economic slowdown, however, occurred very rapidly, as demonstrated in the business pages of newspapers in recent months as business after business has reported disappointing earnings and reduced earning projections. The Postal Service has been impacted similarly to virtually every major U.S. Corporation.

As recently as December, most mainstream economic forecasters were not projecting the slowdown that has occurred in the first two quarters of this calendar year. This slowdown was not reflected at that time in the independently produced macro forecasts that the Postal Service purchases from DRI (now DRI*WEFA). Further, in its November rate decision, the Postal Rate Commission found "the short-term outlook does not appear to involve any risk of unforeseeable financial harm to the Service. " PRC, Docket No. R2000-1, November 13, 1991 .

2. As I understand it, postal officials feel that the Postal Rate Commission short-changed or cut roughly $1 billion from the Service's request for additional revenue. How much of your projected deficit is due to the economy? How much is left from your projected deficit and who or what is responsible for the remaining deficit?

Please see response to question 1a for details on the components of the projected deficit. Our original projection was that the Postal Rate Commission's recommendations would increase our net loss $800 million. The Governors' modification of the Postal Rate Commission's recommendation limits the additional loss to $600 million. The balance of the projected deficit is due to the economy.

3. The Postal Service's track record in forecasting mail volumes and revenues have had real world consequences for ratepayers. For example, in the first quarter of this fiscal year, the Service had excess costs because it based its staffing and resource allocations on overly optimistic forecasts of First-Class mail and Priority mail volumes that failed to materialize. Doesn't the Postal Service need to do a better job of forecasting its mail volumes and revenues? What are you doing to improve the quality of these crucial forecasts?

Recognizing that forecasting is part art and part science, the Postal Service is committed to doing everything it reasonably can do to improve the quality of its revenue and volume forecasts. The Postal Service engages is an active research program on the demand for its services and continuously updates forecasts to reflect that research and the latest information on the marketplace and the state of the economy.

Given the size and magnitude of the Postal Service, however, even a small forecasting error can lead to a significant swing in Postal Service finances. A one-percent swing can result in a revenue shortfall of $700 million or more, which combined with an inadequate rate recommendation and increasing cost inflation, could place the Postal Service's finances seriously out of balance. This is essentially what has happened over the last year and one-half.

4. At least a part of the Postal Service's financial problems appear to be related to its inability to capture promised savings. I believe the phase you use is to "drive costs out of the system." Last year, you announced a "breakthrough productivity" plan. A billion dollars was going to be cut in each of the next three years.

At the Postal Forum in Nashville in March 2000, PMG Henderson announced a promise to reduce expenses by $4 billion by 2004. However, not all of the savings are attributable to "Breakthrough Productivity." After Mr. Henderson's speech, the Postal Service included approximately $1.2 billion in cost reductions and productivity improvement in the FY 2001 budget."

Actually, the Postal Service's record of achieving targeted productivity improvements has been very good over the last few years. In FY 2000 we achieved a total savings of $1.6 billion as measured by Total Factor Productivity. In FY 2001 we have achieved over $900 million through May, well on our way to a target of $1.2 billion. At the end of FY 2001, we will have made substantial progress towards Mr. Henderson's target and we have "pencilled in" approximately $1 billion in the FY 2002 budget. (The FY 2002 budget is not yet finalized.)

4a. What changes have you made to this plan and why? (USPS is now only banking on achieving half of the planned breakthrough.)

No changes have been made to this plan. Management is committed to achieving productivity increases as measured through Total Factor Productivity that produce savings of $1 billion per year.

4b. Why won't we see the promised one billion dollars in savings?

Our goal is to achieve these savings. Based on current trends and year to date performance, the total savings from productivity improvements for FY 2001 will very likely exceed $1 billion and as mentioned above, an additional $1 billion in savings is included in the FY 2002 budget.

5. In September 2000, GAO issued a report that discussed the Postal Service's e-commerce ventures. To date, have you generated net income from your e-commerce activities? If not, do you have any idea when these initiatives will generate positive net income?

The Postal Store—formerly called Stamps Online—has taken in over $40M in postage revenue, though this is typically considered core rechanneled product revenue.

NetPost CardStore, launched in December, 2000, has a net profit of $6,758 for the period inception through April, 2001.

Although other eCommerce initiatives have not yet shown a profit, it must be remembered that none of the Postal Service's eCommerce products are very old; most have been in the market for less than a year.

6. The Postal Service has reported declining growth in first-class mail volumes and an increased use of automation in processing mail. Given this, shouldn't there have been a corresponding decease in work-hours and overtime usage?

Automation is producing savings and cost avoidances this year. This fiscal year, 2001, through week 2 of accounting period 10, the Postal Service is using 13.5 million fewer work hours, in the field than we did for the same period last year. For the same period this fiscal year in the field overtime hours are 925,000less than the same period last year.

7. The Board of Governors announced yesterday that it is studying the impact of reducing delivery from six to five days a week. What impact would cutting Saturday delivery have on customer satisfaction?

As a result of the Board of Governors' request, postal management created a task force to study the impact of reducing delivery from six to five days a week. As part of a comprehensive review, the task force is attempting to assess customer reaction to a reduction in delivery days. This assessment, which is ongoing, includes reactions from business mailers, major mailers, and household recipients.

8. Would you support the creation of a presidential commission to identify inefficiency and waste in the Postal Service and recommend methods for improving mail service? If not, why not?

We believe that the difficulties facing the Postal Service cannot rightly be attributed to classic Washington villains such as "waste" and "inefficiency", but evidence a far more serious problem. Essentially, the Postal Service is laboring in an aggressive and changing business environment, under a statutory charter that has not been modernized in over 30 years. Any adequate resolution of this situation will require a substantial dose of legislative reform.

We believe that postal reform legislation is needed now, and will support whatever means appear to provide the quickest path to that goal. Creation of a presidential commission might provide a useful step along that path. On the downside, however, creation of a commission could also postpone progress toward meaningful reform, perhaps for a year or two, while the commission completes its study and prepares its report. It is also possible that a commission would merely duplicate the work on reform already done by responsible parties or, at worst, frustrate progress toward reform with what is sometimes referred to as "paralysis through analysis".

9. In the last Congress, I sponsored H.R. 2535, legislation which would authorize the Postal Service to phase-in rate increases. Has the Postal Service considered changing rates for mailers who prefer regular, small increases on a different schedule from the changes for individual piece users who may find frequent, small increases inconvenient? Does current law prohibit such a system?

The current law does not necessarily preclude phasing. However, the Postal Rate Commission's rules as they stand do not easily accommodate phasing. Instead, the Commission's rules contemplate that the Postal Service will present a single-stage rate proposal. While the Commission could arguably change or waive its rules, it would need to be done well ahead of time, in light of the time it takes to plan and develop an integrated filing for rate and fee increases.

The concept of implementing rates at different times is intriguing. Most often, as mentioned in the question, this approach is associated with less frequent changes for individuals and more frequent changes for other customers. The Postal Service is always interested in having more options and more flexibility in developing rates for customers.

However, neither phasing rate increases over time nor changing rates for different products at different times would be free from complications. For instance, while phasing rate changes may have appeal to customers by mitigating the impact of a rate change, the initial phases of any rate changes must provide sufficient funds to operate the Postal Service in the interim. At the same time, any phasing system should balance predictability and flexibility. By predictability, we mean that customers should be able to plan on future rates, and the Postal Service should be able to plan on future revenue expectations. At the same time, operating and economic conditions do change, and any system must be able to adapt accordingly.

While we find these alternative approaches interesting, several issues would need to be addressed if they were to be adopted. For instance, small businesses and other institutions that have access to meters and other forms of postage payment also use the single-piece rates used by individuals. Also, the discounts other customers receive for sorting and barcoding bulk mailings are based on the single-piece rates. While these issues are not necessarily insurmountable, they would need to be addressed.

10. The Postal Service has been critical of the current ratemaking process. In the Board's letter to Congress, it states that the entire ratemaking process may take up to 18 months. (I note that the Postal Rate Commission must issue its recommended decisions within ten months.)

10a. What portion of the 18-month period is necessary to insure adequate public notice and participation?

For notice and participation, the Postal Reorganization Act requires no more than the 10 months allowed for the Commission to issue a Recommended Decision. Depending on circumstances, and with cooperation by the Commission and participants, notice and participation by interested parties could be accomplished in significantly less time if the levels of documentation and scrutiny required by the Commission's rules were reduced.

10b. What portion of the 18-month period typically is consumed by your preparation for the proceeding?

The 18-month estimate generally, and simplistically, assumes that 6 months is required to prepare the Request, testimony, and documentation required to be filed by the Commission's rules. Experience shows that this is a reliable minimum, barring no special circumstances or complications. Viewed more broadly, preparation of an omnibus rate case takes much longer, since cost studies and other financial and operational analyses used for ratemaking are continually being pursued and refined in the time between rate cases. Furthermore, ongoing data systems used in ratemaking are maintained and revised continually on an annual or more frequent basis.

10c. Has the Postal Service explored ways to cut down on preparation time?

The Postal Service has explored ways to reduce preparation time. Realistically, however, the minimum amount of time tends to be controlled by the Commission's rules which require certain substantive analyses and a certain level and quality of documentation to support the Postal Service's request. Its worth noting that the amount of materials the Commission requires the Postal Service to file in support of a rate increase necessitate the use of a two-ton truck to transport them. In the past, we have suggested changes in the Commission's filing requirements that would expedite and ease the burdens of preparation.

10d. Would rate cases be simpler and faster if the Postal Service supplied cost data on an ongoing basis to the PRC, so that the Commission staff would be well acquainted with the data when the request was filed. If yes, does current law permit such a procedural change?

The Postal Service provides numerous cost and financial reports to the Commission each accounting period, quarter, and on an annual basis. To a large extent, however, such periodic reports cannot anticipate the integrated mix of proposals the Postal Service develops to support its Request for rate recommendations designed to satisfy a particular prospective revenue requirement. Furthermore, typically time consumed in an omnibus rate case is not the result of the Commission's inability to analyze and consider data and information presented by the Postal Service, but because of the due process requirements under the current ratemaking regime.

Simply stated, it takes a substantial amount of time for the various parties, along with the Commission to pour over the reams of paper along with all of the diskettes and tapes and then ask thousands of questions in writing before the oral-cross examination. Subsequently, these parties can make their own proposals and the process, albeit with less paper, work starts anew. Finally, all of these parties get a final turn to say why each other's proposal is wrong.

Furthermore, in recent omnibus rate cases, the Commission has itself called for new information during litigation that did not exist prior to filing. Commission demands for updating, combined with due process expectations, have created additional pressures weighing against timely completion of the hearings process.

11. In your speech last May at the National Postal Customer Day celebration, you stated that, " there was so much the Postal Service could do to increase the affordability of mail and create incentives for the growth of the mailing industry." You went on to advocate the ability to offer negotiated service agreements that guarantee one rate in exchange for a guaranteed volume threshold. Do you currently support NSA's based upon volume? If yes, please explain. Should there be PRC approval prior to such an agreement? If not, why not?

The Postal Service believes that any NSA that is beneficial to both the Postal Service and the mailer and which does not cause any harm to nonparticipating mailers should be considered. Depending on the merits of the specific proposal, this potentially could include NSAs which include a customer's guarantee to tender a specified volume of mail as one of the provisions. Under the Postal Service's current regulatory framework as established by the Postal Reorganization Act, we are required to submit requests for all domestic rate and classification changes to the Postal Rate Commission. However, as discussed elsewhere, I believe that a comprehensive revision of the postal ratemaking process is necessary. One postal reform goal is to streamline postal ratemaking, including the implementation of any NSA agreements. The approval of an NSA rate or classification should be consistent with the rules established for similar mail which is not subject to an NSA. For example, if the mail covered by the NSA would otherwise be within the "competitive" category, little if any oversight would be needed as long as the NSA provided sufficient revenue to cover the attributable costs of the mail and a reasonable contribution to institutional costs. On the other hand, if the mail covered by the NSA would otherwise be within the "noncompetitive" category, we would expect that a similar approval process would be followed as would be used for a general rate change for the noncompetitive products.

12. NSA's based upon volume are opposed by mailers who feel they will not qualify for any discounts based upon volume. How do you respond to these mailers' concerns?

The Postal Service does not intend to enter into any NSA unless it increases the total contribution from the mail tendered by the participating customer. Therefore, nonparticipating customers would benefit, as the institutional costs they are required to pay through their rates would decrease. In addition, the Postal Service intends to offer the same rates, terms and conditions to any mailer who is similarly situated and able to meet the requirements of an NSA.

13. Since the first two companies were approved by the Postal Service in 1999, the PC Postage program has grown to include well over 400,000 customers, including many small businesses. PC Postage is of enormous benefit to the Postal Service. It results in less misdelivered mail by properly formatting addresses. It makes mail more readily processed by automated systems, and saves the Postal Service money. What is the current status of this program?

PC Postage is an important component of our goal to provide convenient access to postage. As of May 2001, six PC Postage products have been approved for distribution to the public. Those products will be provided by four different companies and used by over 400,000 customers. The Postal Service lauds the advances made by PC vendors because multiple products in the marketplace provide customers greater choices to meet their mailing needs. Other products and applications of PC Postage technology are currently in various stages of development by private industry.

Mr. BURTON. I know how hard you have worked trying to get postal reform through. A number of us in the Congress have been supportive of what you wanted. We have not always been able to have the kind of bipartisan support for one reason or another. I am not blaming Democrats or Republicans. I am just saying it wasn't there.

Congressman Waxman and I think Congressman Davis, as well as the Republican Congressmen, I think are more committed today to reform. We are a little bit late, but hopefully we can get something done.

But I wanted to point out to you something that I just saw today. Have you seen one of these?

Mr. HENDERSON. What is it?

Mr. BURTON. It is a device that you can e-mail from anywhere in the world. You can just carry this with you and if you want to send a message to your wife or your girlfriend.

Mr. BARR. Mr. Chairman, I would like the record to reflect that I do not use that to send messages to my girlfriend, only official duty.

Mr. BURTON. I am sure you don't.

Mr. BARR. Only official duty.

Mr. BURTON. E-mails are easily traceable any more, as I know.

Mr. BARR. That is precisely the point.

Mr. BARR. In any event, with this kind of technology, and I will be expressing this to my colleagues on both sides of the aisle, with that kind of technology the Postal Service is definitely in a very competitive area.

The thing that troubles me, and maybe you can explain this a little bit; you are talking about losing some market share now. You are talking about declining revenues probably in part because of the technology.

But with these kind of technologies, not only e-mails, but with faxes, if they raise postal rates, let us say another 2 cents a letter for first class mail or 4 cents or whatever they decide to do, is it not logical to assume that more people will be sending e-mails, which is much less costly, than to just continue to buy stamps just because of the cost?

Won't more businesses start doing that?

Mr. HENDERSON. I think the general trend, regardless of the rates for postage, is going to be to use more electronic services as opposed to hard copy. There is though, the very effective ad mail, advertising mail. There is a lot of technology around that. That is going to grow remarkably, I think. Because they can still reach your mailbox. They have a lot of data about you. It has high privacy to it. It has terrific prospects for the future.

For packages, we still are the cheapest available residential pick-up and delivery organization in the United States. So, I think there are opportunities there. The elasticities based on pricing, they are sensitive.

If you look back at every rate case, all except for the one that we raised rates across the board 10.3 percent, volume has declined before it came back. So, there is a concern there about that.

Mr. BURTON. My assistant was just pointing out that standard e-mail is 17 cents and it is much less profitable than the first class mail.

Mr. HENDERSON. Yes, in terms of total profit, not margin, but in terms of total moneys we get from it. Yes, that is one of the phenomena we are having right now, that we are trading what was our growth product, first class mail, 34 cents, for 17 cents for standard at standard A. So, we are delivering mail to your mailbox that is generating a lot less revenue for us. That is a big concern.

Mr. BURTON. Well, if you raised the rates on that class of mail as well as first class mail, won't that cause a potential decline in that revenue source as well?

Mr. HENDERSON. That is right. There is a potential decline. But that is the only tool, absent rate reform; I mean that is the only tool that the Governors have to ensure the fiduciary responsibility that they have been entrusted with by the President. That is the one tool they have.

We can cost-cut our way. We can close, you know, if you look at Post Offices, there are opportunities there. 26,000 of the smallest Post Offices in the United States, it takes over $2 to take in $1. You have some places like Cape Cod where you have seven townships and 53 Post Offices.

So, there are some infrastructure inefficiencies.

Mr. BURTON. But those are stopgap measures, are they not?

Mr. HENDERSON. That is right.

Mr. BURTON. I mean that is a one-time thing. You might save $1 billion in 1 year or maybe $1.5 billion. But the problem is going to continue and once you have eliminated that problem, you are still going to have the revenue drain you are talking about.

Mr. HENDERSON. That is right. You have to have reform.

Mr. BURTON. We are trying to figure out how to put together a bipartisan package. You know, the Postal Reform bill, H.R. 22, didn't get the support that it needed for a number of reasons. It should have, but it didn't. So, we are going to try to come up with a different approach.

I want to ask one other question and that is, we were talking about automation and new technologies helping replace the huge amount of revenue that is paid for personnel. What I was suggesting earlier is that the 75 to 80 percent of the costs are personnel cost, personnel-related, retirement benefits, health benefits, as well as salaries.

If you had everything the way you wanted it, if everything tomorrow could be changed the way you wanted it, could we, through retirements and normal attrition, transfer to a more automated system so we would still have the Postal delivery system, but through a more automated system as far as handling the mail is concerned that would be able to generate enough savings so that we would not have to have these Postal rate increases?

Mr. HENDERSON. It depends on what the outcome of binding arbitration is on your remaining workers. We have a huge effort underway for automation. In fact, if you look at letter mail, mail processing costs, that are where the focus has been, with the billions of dollars. You will see that the actual costs are declining in that area.

But if you are going to get wage increases of 4, 5 or 6 percent annually and keep doing that, it is just like going from a push mower to a riding mower but paying three times as much money. You are not netting out on the bottom line. So, you have to get a handle on your work hour costs.

Mr. BURTON. So you are suggesting what in the area of binding arbitration?

Mr. HENDERSON. Well, I think that is right ought to be an alternative to binding arbitration.

Mr. BURTON. Such as?

Mr. HENDERSON. Well, there is the Railway Labor Act. You could think up a new way of settling disputes. I think that the voice of the customer needs to be heard in the outcome of a labor dispute and not just an arbitrator saying, hey, I am cutting the baby 50–50 or I am going to give them the average wage increase across America.

I think that process needs to be re-examined and relooked at. I think labor's voice needs to be heard. I am not knocking collective bargaining. I think collective bargaining is important. I am just trying to figure out a new way to resolve the dispute process that doesn't result in these extraordinary work hour increases that drive rates.

Mr. BURTON. Have you discussed with the labor leaders in the Postal Service the problem that they are facing with alternative sources of correspondence and how that will affect them if that is right isn't some kind of change in the binding arbitration?

Mr. HENDERSON. Well, I have talked with them about the future.

Mr. BURTON. I mean being priced out of the market place. We have seen in industries like the auto industry where many companies are going offshore. Well, you are not going to go off-shore, well, you might even go off-shore with some of the competition that is coming into this country and opening up facilities, which was mentioned earlier.

But you are not going to go offshore to build a Post Office like we do a car. But devices like the one that Congressman Barr has are becoming more and more in vogue and people are using them.

If the labor force continues to price itself up, thus driving the cost of the service up, it seems that more and more people will be turning toward these alternative sources of communication.

Has anybody, yourself included, discussed, sat down and had long discussions with the leaders of the unions about how this would affect them?

Mr. HENDERSON. Yes. Our labor union leaders are well informed. In fact, they write about it in their magazines, about the future of the Postal Service and the need for Postal reform. I wouldn't say there is any agreement on an alternative to arbitration.

They are very concerned. I don't mean to speak for them. But they are very concerned about the notion of eliminating collective bargaining. They are very much opposed to that. They wouldn't support anything like that and we're not proposing that. But they are concerned about the future and they do understand postal costs intuitively.

Mr. BURTON. It seems like to me that that is kind of like the Gordian Knot that Alexander the Great had to face. I am not sure

what the answer is, but it seems to me at some point that is going to have to be one of the things we are going to have to sit down and figure out.

We will try to talk to Mr. Gould and some of the other people who are in charge of the various unions and see what their suggestions are on how to deal with that.

Your successor, whoever it happens to be, we will try to have them in the loop, too, and get everybody together. As I said earlier in my opening statement, it is extremely important that all segments of the Postal community, not only the Postal unions and the people who run the Post Office and the Postal Rate Commission, but also those who are involved in competition that would be effected by Postal reform legislation, need to sit down and try to work out their differences.

Let me just ask a couple more questions here and then I will yield to my colleagues here.

Do you agree with the decision by the Comptroller General to add the Postal Service to its high-risk list right now?

Mr. HENDERSON. I agree with Mr. Walker in adding the transformation process. He didn't add the Postal Service. He added the Postal transformation process to his high-risk list. I think he should. I think the efforts that we have had in Postal reform and the fact that we have not been able to achieve reform and the conditions today and looking into the future, I think it warrants any help we can get. I am open for anybody to get on this bandwagon.

Mr. BURTON. Do you have any other recommendations to make to the Board of Governors or the new Postmaster General on what kind of actions can be taken to get the Postal Service off of that list and get things moving in the right direction?

Mr. HENDERSON. I think it is going to take a cooperative effort between the management of the Postal Service, the Board of Governors, and the Congress, which plays a moving role, to come up with a strong bipartisan piece of legislation that will help the Postal Service and that it moves through Congress with the support of the American people.

We can't do it by ourselves. We have shown that. We have also some legal restrictions and thus far, until you have a problem it doesn't seem that people want sit back and take notice. I think if they get rate increases in the summertime or a proposal, I think people will really take notice, and they should.

Mr. BURTON. Let me just say that unfortunately, one of the strengths and weaknesses of the legislative process is we usually don't respond until there is a shrill cry from some place. We should be a little bit more far-sighted, but it seems like we aren't.

Mr. McHugh down there has been working on this and talking about this for a long time, as we have said. It has fallen on deaf ears and now we are into almost a crisis situation.

Mr. Barr, do you have any questions right now?

Mr. BARR. I do. Thank you, Mr. Chairman.

Mr. Postmaster General, I appreciate your being here. Again, I would like to tell you directly as I said earlier, and I mean this very sincerely, I do think we have the best Postal Service anywhere in the world.

Having lived and worked in other countries, I am very familiar with the fact that ours is better by far than almost any other and certainly better than every other.

My experience, having been a temporary carrier during college, is very first-hand knowledge. That continues to this day. I meet frequently with postal employees and Postmasters in the Seventh District of Georgia.

From time to time when we have a problem in management or with employees, it is my experience that the Postal Service has always been very receptive to working with us and working with a particular Post Office to straighten it out.

My concerns, like yours, are certainly not with the employees themselves. They do an outstanding job under very difficult conditions sometimes.

I share the concerns of other Members of this committee and I think, the general public, with some of the things we are seeing and reading about nowadays. It is not something new.

I pulled up in our computer system a letter that I had recalled writing back in 1997 to Chairman McHugh. This was in response to a news report back in the middle of 1997 about the new Postmaster in Atlanta throwing a party for herself costing $45,000. It is that sort of abuse of the public's moneys that give us concern.

I just saw, as I am sure you have, this article from just a couple of months ago about Postal Service executives using chauffeur-driven limousines. I would appreciate your comments on that, whether that has been cut out completely.

Also, if you could, comment on the reports that I alluded to earlier with regard to the possibility of cutting back Saturday delivery. I think if there is one thing that the Postal Service can do that will guarantee its demise it is cut back or eliminate service on Saturday.

I can't understand why something so self-destructive would even be considered. I certainly understand that you all have to look at cost-cutting measures. Certainly that is important. From time to time you have to consider raising the postage rate. I think all of us understand that. We may not always agree with the amount or the timing. But I certainly, for one, understand that does have to happen from time to time.

I also understand that many of your costs, not all of them, but many of your costs are beyond your control, the cost of fuels, for example.

So, I commend the Postal Service for exploring ways to streamline its operation, and encourage you to look at other ways of doing so. But I would urge you to look at constructive ways of saving money, not self-destructive ways.

Again, I would think that looking at curtailing Saturday deliveries would guarantee that millions of Americans would seriously begin to look elsewhere for alternative ways to have their mail delivered.

I would like to know what is the thought process that is going on that would lead to even considering something like that, given what seems to me to be the obvious self-destructive nature of it.

Mr. HENDERSON. Let me go back to the first few issues. With 80,000 managers and 800,000 employees, you are going to have in-

stances of people abusing the rules of doing something that they should not do.

I can assure you when that occurs, we work very closely with the Inspector General. We take immediate action. If we have to change the rules, we do that. If we have to discipline somebody, we do that. If we have to fire somebody, we do that. So, we are going to have instances of that. We are not proud of those instances. We take action as a result of learning of those things.

With regard to Saturday delivery, what we are going to do is do an internal study to see how much Saturday delivery actually costs us and what savings are there. It is not a decision. A decision to curtail Saturday delivery has not been made.

We have done this in the past. We did it in the 1970's. In fact, in the 1970's I was a part of the task force that looked at what Saturday delivery cost us.

Then we are going to talk to our Board of Governors. They have asked us to put a value on it and we are. That is what they publicly asked us to do yesterday. Our operating people will do that.

But there is no decision made today to eliminate Saturday delivery. There are some constituents of Saturday delivery that have to be considered, some voices. One are the newspapers. Newspapers rely on the Postal Service's Saturday delivery in many places. That is the only effective way they have of reaching their customers. There has to be some consideration of that.

Another one would be remittance mail. Remittance mailers, people who receive their bills on Saturday are more likely to pay their bills right away than those who receive their bills on Monday. That is a study that the remittance mailers have made. So, there is obviously a financial impact on those folks.

Those are things we are aware of. We are not going to be irrational here. We are going to be prudent. But we do have a problem. We have a problem that our customers are saying, "Don't raise rates, don't raise rates."

The demand for Postal products is declining.

Mr. BARR. Mr. Chairman, could I just pose one quick followup question, please?

I understand that the economy does have both an indirect and a direct bearing on the manner and frequency with which people use the Postal Service. It is the same as virtually every other service available to the public. I don't think that looking at curtailing Saturday delivery is irrational. It is super-rational, and that is the problem.

It is looking at Postal delivery in terms of nothing but dollars and cents. Therein, I think, lies the problem. You could look at the dollars and cents of curtailing delivery every other day, I suppose, and one could come up with a super rational argument that, hey, it makes sense to do that. Let us do it.

I think you are making a serious mistake even suggesting that you are going to open that can of worms. It is already causing, maybe not a firestorm, but a lot of people asking very serious questions about the Postal Service. It is drawing a tremendous amount of attention to you, not all positive.

I think there is just so much room for improvement in other areas, why you would bite off that at the beginning of this exercise

is something I don't quite understand. I would urge you all to move that off of the table. Look at these other areas and consider such drastic steps as curtailing Saturday delivery way down the road, if at all.

You are doing more than just making some adjustments to save you money. You would be fundamentally altering what the Postal Service means to American citizens if you do that. I think that would be a fatal mistake for the Postal Service to do that. I don't think you ought to even go down that road at this point, even studying it.

Thank you, Mr. Chairman.

Mr. BURTON. Mr. Davis.

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

Mr. Henderson, let me commend you for what I think has been your ability to hold together a very complex system that was fraught with many needs and problems. While it is easy for people to throw darts from the outside, sometimes when you get on the inside, you see things a little differently.

I think that you have demonstrated real management skill and insight in terms of being the keeper of a complex system and a complex process and especially the fact that we have seen some improvements relative to on-time delivery.

I commend you and your staff for the work that you have done.

When we talk about change and we talk about changes and everybody is saying we need some legislative fix, one of the things I have also observed is that it is oftentimes much easier to say things than it is to do them. Oftentimes, after all is said and done, more gets said than done.

So, it is easy to talk about the fixes. In your mind, when we talk about legislative changes or restructuring, what comes to mind?

Mr. HENDERSON. Well, I think the two big targets are: One is pricing freedom and the other one is some solution other than arbitration to collective bargaining disputes. They are the two main drivers of the Postal Service. Those are two areas that I think need attention.

We have talked about some other areas like the ability to introduce new products in a rapid way. We have talked about the ability to use our income for broader investments.

If you look at the posts around the world, and I know, Mr. Chairman, you see a growing move to unleash these postal services, and I say "unleash" them because they go very aggressively into the commercial markets.

I just had a meeting last week with Klaus Zumlichel who is the head of the Deutsches Post. He is the head of the largest logistics company in the world. He just bought the largest bank in Germany. He has an express mail business similar to the Postal Service's and then he has a mail monopoly. He owns 51 percent of DHL.

I am not suggesting that we ought to become Deutsches Post. But I am pointing out that the world is really changing rapidly. We are like a Third World country post. We have these 31-year old laws.

People ask me from foreign countries all the time, "Why doesn't the Postal Service change its legislative construction? Why is it lag-

ging behind the likes of Royal Mail and the likes of the TPG, the Dutch Post?"

I really don't have an explanation for them. They come over here and they say, "You are destined for just higher prices. You know, we have studied that model."

When I came to the Postal Service in 1972, we were the model for the whole world. Everybody was coming to the United States to see this new postal organization that was independent from government but still a part of government. Now they come here and they are shocked.

Some of my colleagues in foreign posts have been there a long time and they just don't understand it. You know, I have been a voice for reform until my voice has almost run out. I don't know what is going to precipitate it, I really don't. But I think those areas of pricing and controlling our labor costs are imperative.

Mr. DAVIS. It seems to me that a part of our financial difficult has come as a result of our inability to deliver on promised savings, I mean where projections were made that we were going to be able to reduce costs. And we have not been able to deliver on those promises.

Could you share why we were not able to deliver on those promises?

Mr. HENDERSON. Well, I think we have done a better job than we get public credit for in terms of delivering. We talk about labor productivity. We have had positive labor productivity in 1997, 1998 and 1999. In a year of declining mail volume, we have positive productivity this year. Last year we had the highest productivity we have had in 9 years.

The difficulty is that you are wage rates go up beyond your productivity levels. Therefore, you net out at a cost. That is a fundamental issue with the Postal Service.

And, there are a lot of fixed costs in the Postal Service. We come to your house, for example, we send a letter carrier by every day, regardless of whether they have 50 pieces of mail or 5; when they have 5 pieces of mail, you lose a lot; when they have 500 pieces of mail, you make some money.

So, the infrastructure itself, it is a service to the American people, but it has built-in inefficiencies in it. You are not going to not get mail. I don't think anybody here is suggesting that we not deliver to everyone every day. In doing that, if you don't have a robust mail system, it loses money.

I will give you another example of the business cycle. We make all our money in the first two quarters of our fiscal year, September through quarter two. Our fiscal year begins in September.

We lose money the remaining two quarters of the fiscal year. Somebody says, "Why do you do that?"

It is because mail volume dries up. The last two quarters of our fiscal year doesn't have the robust mail volume. It is like the water pressure in your house is going down and somebody says to you, "Why don't you take out some pipes?"

It is a fixed infrastructure and without robust volume, it is inefficient.

Mr. BURTON. Thank you, Mr. Davis.

Mr. Otter.

Mr. OTTER. Thank you, Mr. Chairman.

Mr. Henderson, I apologize for being gone while you were giving your testimony, however, I did read your very informative written testimony. I guess coming from Idaho I am not different than anybody else. You always hear from me when there is a problem. You don't hear from me when I get all my mail, especially all my bills, then you don't hear from me.

But those are the questions generally that I think I am asked. I don't hear from anybody that says, "Gee, the Post Office did a great job for me today."

I hear from them when they say that you are not doing a good job.

One of the questions that I have relates to my opening statement. My opening statement referred to one of the highest cost or loss areas in the Postal Service, which seems to be the undeliverable mail or mail not deliverable at this address.

The figure that I had was $1.5 billion. Is that representative? Is that about correct?

Mr. HENDERSON. That is in the ballpark.

Mr. OTTER. But this is not a phenomena that just happened in the last few years. This is something that has been building and so it has been part of that almost $10 billion in total net losses that you are carrying on the books right now; isn't it?

Mr. HENDERSON. The net loss is $3.4 billion.

Mr. OTTER. Aren't you carrying a loss of what I thought was in excess, with this year, pretty close to $10 billion?

Mr. HENDERSON. You are talking about the negative net income?

Mr. OTTER. Yes.

Mr. HENDERSON. Yes.

Mr. OTTER. OK. That has to be paid for somewhere, sometime.

Mr. HENDERSON. That is right.

Mr. OTTER. You talked about the Deutsches Post. Are you familiar with the program they have, the Siemens Group has a national registry for the change in addresses, that technology?

Mr. HENDERSON. Is that Fast Forward?

Mr. OTTER. Yes.

Mr. HENDERSON. Yes, I am.

Mr. OTTER. Now that technology has been around for quite some time; hasn't it?

Mr. HENDERSON. Yes.

Mr. OTTER. That technology seems to avert on-going costs that would add up to the $1.5 billion. Have you looked at that program?

Mr. HENDERSON. Those are two separate issues. Undeliverable as addressed is mail that has the wrong address on it. Fast Forward says, I am going to move from Washington, DC, to New York City and when the mail is addressed to me in Washington, DC, it will automatically re-barcode the mail and send it to New York City.

Undeliverable as addressed is just a service that we provide. We try to deliver mail to the address on the envelope. If that address is bad or doesn't exist, we obviously can't deliver it. We have to dispose of it. But they are two separate things. They are not the same thing.

Mr. OTTER. OK. So, then, take me through how it adds up to $1.5 billion loss. You have already got the 34 cents for the piece of mail

that wasn't deliverable. Does it cost you that to store it or what do you do with it?

Mr. HENDERSON. It costs us that to handle it. It is a cost to the Postal Service of handling mail that has a bad address on it. I can't tell you when we accept it if it is a bad address or not. When we sort it and we can't find the address, we dispose of the mail.

In America there are 630 million pieces a day. There are going to be some bad addresses in that volume. That is just a part of the service that we provide.

Mr. OTTER. OK. Let us move to another area that is a cost. That is $300 to $500 million in advertising for a product on which the Post Office enjoys a total monopoly.

Mr. HENDERSON. That number is not accurate.

Mr. OTTER. What would the number be?

Mr. HENDERSON. It is $161 million and it is primarily devoted to the non-monopoly, the very competitive mail. When we don't advertise, our share of the market goes down. It measurably goes down. When we do advertise, our products grow.

So, it is an essential to stay competitive. We have been doing this for years.

Mr. OTTER. There is one other area I would like to get in to that I mentioned in my opening statement, the byproducts that you produce, including the Internet high tech. How much has the Post Office spent to get into the e-mail?

Mr. HENDERSON. Well, we have our own e-mail system, obviously, that we use for interoffice communications. I couldn't tell you off the top of my head how much it cost to install that e-mail system. I can tell you for the record. But it is a significant savings for us, being able to go to a computer and if I want to talk to my Chief Financial Officer, to be able to e-mail.

Mr. OTTER. No, I understand that. What I mean is, you don't offer an e-mail product available to the market place?

Mr. HENDERSON. Yes, we do offer a secure service to the marketplace.

Mr. OTTER. Yet, then isn't it your testimony also that one of the things cannibalizing the first class mail system is the e-mail?

Mr. HENDERSON. Well, e-mail is not having much of an impact on first class mail because correspondence had gone away before e-mail came along. I mean there is an assumption, and I think a logical assumption, by most people, that e-mail really banged us.

People didn't write letters. By the time e-mail came along, people had stopped writing each other all across America. What e-mail represents is a technology that really leads to electronic data exchange, the B-to-B stuff, that has really been slowing down. That has affected us, but not just the general e-mail.

Mr. OTTER. But you are not offering that product?

Mr. HENDERSON. We offer a secure e-mail, but not just the general e-mail. I think Social Security is the major customer of that right now. We offer several varieties. We have a stamp. We offer secure document services and those sorts of things, and we have revenue streams from them.

Because they have upfront costs, they are not profitable yet. But we have been instructed by our Governors to create P&Ls for all of them. We implement all the GAO's recommendations, so we are

watching them very closely. According to our market research they are promising, but they are not big deals.

I mean on a $67 billion base these are very small initiatives. We are really focused on our core business. That is where the Postal Service is going to hang its hat. We are actually learning them.

We have an e-bill pay service. One of the reasons we got into electronic bill paying was to understand it better because it is going to cannibalize the $17 billion of our core product, which is first class mail. We do understand it a lot better right now than we did before. It may not be the early threat that we thought it was going to be. But learning experiences for the organization are very important.

Mr. OTTER. Thank you, Mr. Henderson. I appreciate it.

Thank you, Mr. Chairman.

Mr. BURTON. Mr. McHugh.

Mr. MCHUGH. Bill, again, as I said earlier, thank you for your service. Thank you for the hard work you have put forward. I know all of us on the committee wish you well in your future endeavors, whatever they may be.

Some of us may envy your escaping this current milieu but you have certainly served your time and done more than your part. You will go with our thanks.

One thing I am a little unclear on is on part of your talk with Mr. Barr. If the large newspapers want Saturday mail, does that mean we keep it or get rid of it?

Mr. HENDERSON. It doesn't mean we keep it. I was just pointing out that I have been talking to them and I know that they are not very fond of it.

Mr. MCHUGH. I am not sure how we would vote on that.

Let us talk a little bit about what Mr. Otter probed you on. I heard you correctly, I believe, that the largest share of your mail advertising goes to your competitive products. But clearly there is some direction toward your first class monopoly. What is happening to your first class monopoly?

Mr. HENDERSON. It is eroding. I mean it is virtually irrelevant. If you were going to invest in a letter delivery company today, you could not raise the venture capital to do it. There are just too many other investments that have greater returns.

The margins on a 34-cent letter are fractional. So, while we have protections that were relevant years ago, I think those protections today are not as relevant. Also, you have electronic alternatives.

As Chairman Burton said, it is free, virtually free to send an e-mail or communicate with somebody electronically. That is going to occur, so the monopoly will be eroded over time.

Mr. MCHUGH. So, if you are required to do something, even though I understand it is not a major portion of your budget, I don't think prudent business practices would suggest that you shouldn't advertise for something you are required to do and you are already losing money on it, so you don't want to lose share further. Would that be a fair statement?

Mr. HENDERSON. That is an accurate statement.

Mr. MCHUGH. I would like to talk about potential savings. Again, Mr. Barr's question, can I assume you don't know what the actual

cost versus the supposed benefits of delivery of Saturday mail are at this moment?

Mr. HENDERSON. Not at this second, no. But I will know within 90 days.

Mr. MCHUGH. So, you are trying, which I think would be an important business practice, to assess a very important part of your delivery system and find out what the investment is versus the return?

Mr. HENDERSON. That is right.

Mr. MCHUGH. Let us talk about another part, another distasteful thing, but something I am wondering if you are looking at. You are currently on a self-imposed moratorium on the closure of Post Offices that are operating. You are limited by statute from closing smaller rural Post Offices, something that I am very interested in, solely on the basis of economic concerns.

Has anybody looked at perhaps streamlining those organizations and possibly assessing if that moratorium were to go away what the cost of savings could be there?

Mr. HENDERSON. Yes, we are looking at that. We are looking at the infrastructure, what we need and what 40,000 Post Offices cost us across the United States. How many do we need? You do most of your business in the largest 7,000. The remaining Post Offices are there as a convenience to America.

As I said to Chairman Burton, in the 26,000 smallest offices of the 40,000, it costs over $2 to take in $1. That is a very expensive infrastructure. Yet, it is a presence. I understand the non-economic side of it. People feel like they are losing their identity when they close their Post Office, their sense of history.

The two things that Americans dislike most in rural America, and you know this, too, is the fact when their newspaper closes or their Post Office closes. They feel like they are somehow lost. We understand that. But we have to examine every aspect of our infrastructure, what it costs and then we have to talk about it with our customers in the pricing mechanism.

Mr. MCHUGH. Last, before my time runs out, you have recently made a commitment, for lack of a better word, to find savings in the elimination of 75,000 man-years over the next 5 years. When roughly 80 percent of your costs are derived from a sole source, I think it is logical that in desperate times you look at that kind of saving.

But I don't think you lose 75,000 man-years of service and not have some diminutive effect upon the service itself. Were you able to assess the tradeoffs that were involved in that kind of action?

Mr. HENDERSON. Yes. We have not done anything yet that would affect the excellent service that Americans get all across this Nation. That would be a serious tradeoff. That is something, quite frankly, we were asked the day before yesterday by our Governors.

We were asked to say, "What does it cost to have 95 percent"—and I am using this as an example—"95 percent on-time delivery in Washington, DC, whereas 6 or 7 years ago it was in the 40's or 50's?"

Here is one of the individuals here, our Chief Financial Officer, who helped improve service in this capital metro area. So, we are

going to look at all aspects of it. There is nothing sacred. There are no sacred cows in the Postal Service going forward.

Mr. MCHUGH. If I may, Mr. Chairman, one final question. I appreciate the committee's patience.

There has been a lot of talk today about inefficiencies. I know you would be the first to admit that you can, you are trying and, hopefully, will do better. We need to be supportive of your effort there as well.

Just for those who may not know, what is the price of a first class stamp in America compared to other countries, even those that have totally modernized and reorganized their structure?

Mr. HENDERSON. Well, it is about half of what it is in Germany, for example. That is held up as the model for the world right now.

Mr. MCHUGH. Thank you, Mr. Chairman.

Mr. BURTON. Half of what it is in Germany?

Mr. HENDERSON. Yes, sir.

Mr. BURTON. Mr. Scarborough.

Mr. SCARBOROUGH. Thank you, Mr. Chairman.

I just want to followup with a few questions regarding efficiencies at the Post Office. The Postal Service has been investigating automated sortation and information technology now for quite a few years.

However, we hear reports from the GAO that the Postal Service has only increased its efficiency by about 10 percent over the last three decades. Would you give us an update on what is happening with that process and why efficiency improved at a faster rate?

Mr. HENDERSON. That indicia that GAO is talking about is an indicia that we created. It is called "Total Factor Productivity." It is not labor productivity. It is Total Factor Productivity. It really measures the health of an industry. Total Factor Productivity takes into account labor productivity, but it also takes into account capital you invest and the cost of supplies and services.

So, it has an indicia in it that is called labor productivity. That is a gauge of our automation. If you looked at the productivity level in 1988, prior to automation, and you looked at it today and we had the same productivity today that we had in 1988, you would have to add 100,000 workers to the roles of the Postal Service.

Automation has made a huge impact. But we also get 1.8 million deliveries a year additional in the Postal Service and have had for years. If you say, "What is that?" We are adding a city the size of Chicago annually. So, there is a counter balance there between growth in mail volume, which has been traditional up until this year, and growth in deliveries.

You balance that with what you are able to take out in automation. If you look at the mail processing, the productivity of letter mail, that is primarily where these billions of dollars have been focused, you will see that the actual costs of mail processing of letter mail are declining.

That is why you can have only a penny increase in the price of first class postage.

Mr. SCARBOROUGH. OK. Well, you said, "Well, we have also been picking up more volume of work." But in this U.S. News and World Report article that has been passed around, the people are talking about your work force has grown, which, of course, it needs to

grow. But it has grown to 900,000, which this U.S. News article says is the second largest work force in America, right behind Wal-Mart.

Have you parted with FedEx recently? I am wondering, in that partnership with FedEx are you looking at best practices regarding not only automation but also labor, sort of handling labor practices and how to make that whole process more efficient from top to bottom?

Mr. HENDERSON. We do that as a matter of practice. But we don't have any agreement with FedEx to do that. Our Federal Express agreement is essentially a transportation agreement. They will in the future fly first class, express and priority mail.

We in turn allow FedEx boxes to be on Postal property. I will add there is not exclusivity to this. We will talk to anybody.

Mr. SCARBOROUGH. You would allow UPS to place their boxes on your property?

Mr. HENDERSON. We would likely talk to UPS if they wanted to talk.

Mr. SCARBOROUGH. OK. I was just joking with you. You don't have to if you don't want to.

Mr. HENDERSON. Thank you.

Mr. SCARBOROUGH. I would suggest, looking at private industry. This is in reference from the U.S. News article that was sent around. It says labor costs, and everybody has talked about this, eat up 76 percent of your revenues, which I certainly understand the problems inherent there. They say that compares to 56 percent at UPS and 42 percent at FedEx.

One final question I have has to do with your postal rate increase for magazines. I don't have information in front of me right now. But if I am not mistaken, at the beginning of the year that rate increase shot up about 10 percent. There is now a proposal on the table to increase that another 15 percent.

That is a pretty dramatic increase, 25 percent in about 6-months time. That is a heck of a hit for the magazine industry and more importantly, for the consumers to get those magazines delivered. Is it not?

Mr. HENDERSON. It is a heck of a hit for the magazine industry. We work with them. Their costs are higher than the other classes of mail. That is unfortunate. If we had a different rate-setting process, for example, magazines generate a lot of mail. They are at one point in the value chain. They have business reply mail inside of them. They have subscriptions that you write oftentimes and send first class mail.

But we have to treat them like a commodity. That is one of the fundamental flaws. You ought to be able to look at the value chain of these things that generate a lot of mail. We are not able to under the current cost-setting regime.

Mr. SCARBOROUGH. I appreciate your responses and appreciate your time here. I really do think a 25 percent increase in 6 months is a little bit excessive.

Thank you.

Mr. BURTON. Thank you, Mr. Scarborough.

Mr. LaTourette.

Mr. LATOURETTE. Thank you, Mr. Chairman.

I apologize. I had to go listen to the new Secretary of Transportation, Mr. Mineta, next door. I did hear the opening statements of some of my colleagues, though.

Anybody who wonders why you find yourself in this situation should have watched Ms. Wilhite on CSPAN this morning who did a great job for the Service talking about the increase in fuel costs, the impact of technology on your mail volume and some of the sag in the economy.

I did want to go back to something Mr. Scarborough was asking you about. I think the last time you were before the subcommittee that doesn't exist anymore there had been some news accounts and reports of the pending agreement with FedEx. Now we know that has gone forward.

If I could, I would like to revisit some of those issues. At that hearing, and sadly, I am not one of those guys who goes back and gets a transcript, so we are going to have to rely on my faulty memory. But I think I expressed some concerns about the anti-competitive nature of it. I think you made the observation that you had a legal opinion at the time that it didn't have to be bid. There has now been litigation that confirms that position.

I am aware of and I assume you are aware of the fact that some of your regional carriers are making the observation that they could deliver the same service for less money. The question I have for you, despite the fact that you are right legally or not, and you clearly are, but if that is a valid claim, my question is, why would one of the largest contracts in the Postal Service's history, to my understanding, one, be of a 7-year duration, and two, not be opened up for competitive bids so that you get the best price for the service?

Mr. HENDERSON. Well, we did an extensive evaluation of Federal Express. We are in litigation, so I am limited in what I can talk about. But I can tell you that this is the best transportation arrangement that the U.S. Postal Service has ever had in its history.

It is going to be terrific for the American people. Priority Mail is going to be virtually 100 percent on time. Trust me, it is a terrific deal.

Mr. LATOURETTE. I think Federal Express is a wonderful company. I am not disparaging their ability to move things around the world in any way. The question is, if in fact, I think the specific figure that I saw was something like a 35 percent savings.

Are you saying that because of the value of having this on-time delivery it doesn't matter what it costs or that the increased costs justifies the benefits or are you disputing the fact that in fact these services could be obtained by the Service for less money?

Mr. HENDERSON. What we are saying is that in the past we have paid a fully loaded cost. In other words, we have had to lease a fleet. We pay for the whole fleet. Now, we have a variable cost. We don't have to lease a fleet. We are leasing space.

It is the same arrangements we have with the airlines. If you look at flying mail, 28 cents a pound on the commercial airlines as opposed to at one point on our leased airplanes it was $1. But with Federal Express we get the variable costs and not the fully loaded costs because they have other things that they are charging against it. That makes it very economic for us.

Mr. LATOURETTE. It is my understanding that some of the terms of the agreement put a ceiling, if you will, on the amount of mail that Federal Express is obligated to carry. Is that correct?

Mr. HENDERSON. I think that is a minimum. That is a level of detail that I am not familiar with.

Mr. LATOURETTE. I think it is a maximum, too. So, the question I have is do you know that not to be true? If it is not, I won't even ask the question.

Mr. HENDERSON. I don't know the answer. I can get the answer, but I don't know the answer.

Mr. LATOURETTE. If you could. My specific question is if there is in fact a maximum that they are obligated to carry. It seems to me in some of the literature, at least prior to this agreement, they listed the Postal Service and the Postal Service listed FedEx as a competitor, and you were in certain product lines.

But having a maximum obligation, it appears to me, if that is one of the contract terms, seems to place in the hands of a former competitor a great deal of power over the U.S. Postal Service. So, I would be interested in the answer to that.

The last observation, if you can sort of dig up the answer to the question as well, at the previous hearing we talked about having FedEx boxes at Postal Services. As a matter of fact, in my District office in Paynesville, I can look out on a beautiful square where I see three mailboxes and I see one FedEx box. Not only the placement of the FedEx boxes, but how the Postal Inspectors are going to be utilized relative to FedEx activities.

My specific question is whether or not anyone at the Postal Service has solicited or received an opinion from the Justice Department or anywhere else as to whether or not we have come up proper with some of the Anti-Trust laws of this country. Anything that the Service can provide in writing, I would very much appreciate.

Mr. HENDERSON. OK.

Mr. BURTON. Thank you, Mr. LaTourette.

Let me just ask a couple of more questions to followup on Mr. LaTourette's. You said you did an evaluation. I have high regard for FedEx, UPS, all the major deliverers, so I am not picking on anybody. But, why wasn't there a competitive bid on that contract that set out all the criteria that you required, all the things that you required, and then when you got the bids to make sure they could meet all the requirements or else the bid was null and void?

Mr. HENDERSON. There is a short answer and then I will provide for the record a very detailed answer.

Mr. BURTON. OK. That will be fine.

Mr. HENDERSON. The short answer is we didn't look at the competitive field. We had an evaluation by outsiders, experts. Really, there was no one——

Mr. BURTON. Who were those outside people?

Mr. HENDERSON. Price Waterhouse Coopers. Our transportation people felt very strongly that it was unnecessary. We litigated that. I mean that was the complaint against us and we won the litigation. It was a very thorough job that was done.

We think we have a wonderful partner in Federal Express, as I said to Mr. LaTourette. It is the best transportation deal we have

ever had in the Postal Service, both from a economic point of view, but more importantly from a service point of view.

This is going to take a product that has been 2 or 3 days in the marketplace and make it 2 days 100 percent, virtually 100 percent of the time.

Mr. BURTON. I was told, and I don't know how accurate this is, that the contract is around $6 to $7 billion. According to some of their competitors that have contacted a number of us in the Congress, $2 to $3 billion could have been saved if another carrier had the contract.

Is that a stretch?

Mr. HENDERSON. That is more than a stretch. That is a leap.

Mr. BURTON. Just out of curiosity, how do you know that?

Mr. HENDERSON. Because we did an evaluation. We have been in the transportation business for a long time. We have arrangements with a number of people all across America, many of which are complaining now. So, we know their internal costs. We understand the efficiencies of air transportation. I can tell you, and I will provide you in writing a detailed rebuttal to what those folks are saying.

Mr. BURTON. We would like to have that for the record just so we have all the facts straight. I guess Price Waterhouse evaluated that as well.

Mr. HENDERSON. I will be happy to provide you that evaluation.

Mr. BURTON. OK.

We have asked many questions today about the Postal Service and how they have saved money in the past and where they might save money in the future. Hypothetically, if your cost containment efforts could save you $3 billion, how would that impact your decision to file a rate case this year?

Mr. HENDERSON. It could postpone the decision if you made $3 billion in cost savings. This year, if you got them now, you could actually postpone the rate increase. But ultimately, it is a short-term fix. Ultimately, you need postal reform. We need postal reform.

Mr. BURTON. I understand because we talked earlier in the meeting today about if you close down Post Offices and you went with cluster boxes and closed Post Offices and did some other economies, you could probably save a one-time savings of a few billion. But that would only postpone the inevitable.

Mr. HENDERSON. That is right. It is not a fix. It is what David Walker said from GAO. There are some short-term fixes like raising rates or cutting costs. But long term, if you don't have transformation, he calls it "transformation," if you don't have postal reform it is not going to fix the problem.

Mr. BURTON. Let me ask you this: Let us say that we are working on a postal reform bill that meets the problem, and we are going to try like heck to do that, in the interim, so that we don't cause some small businesses and other mailers who are using the mail a great deal, using the Postal Service a great deal, to keep them from either going out of business or losing a great deal of profit and making them uncompetitive, magazines and other things like that, could these short-term economies you are talking post-

pone it while the Congress tries to reach an agreement on a postal reform bill? Could that postpone a rate increase?

Mr. HENDERSON. In my opinion, it will not. We are going to look at some ways. John Nolan, the Deputy Postmaster General, is heading up an effort to look at some creative ways of getting finances with the Postal Rate Commission without a huge rate increase. We have not completed those yet.

But we are going to work with the industry, people like magazine publishers and newspapers and all to see if there is a way. This conversation came about over the last several weeks, especially at the last National Postal Forum where we had all of our customers.

We are going to study alternatives here. But we are in a vice right now. We are in a box. We have declining volumes, revenues way under planned. The solution to price increases in the long haul is to support your efforts in postal reform.

Mr. BURTON. Could you keep Mr. Davis and myself and Mr. Davis and Mr. Waxman and Mr. McHugh in the loop on that as well as other Members of the Congress, so we can be as up-to-date as possible without having everybody come in for another hearing?

Mr. HENDERSON. OK.

Mr. BURTON. We will now call our third panel, Mr. David Fineman, the vice chairman of the Board of Governors and the following members of the Board, Tirso del Junco, Alan Kessler, Ernesta Ballard.

Am I missing somebody?

Mr. FINEMAN. No. It is just a little bit different. Mr. John Walsh is here and former Governor McWherter is not here.

Mr. BURTON. Mr. Walsh, we will have you in his stead.

[Witnesses sworn.]

Mr. BURTON. I guess, Mr. Fineman, you are going to make the opening statement.

Mr. FINEMAN. Yes, sir.

Mr. BURTON. OK, Mr. Fineman, you are recognized.

STATEMENTS OF S. DAVID FINEMAN, VICE CHAIRMAN, BOARD OF GOVERNORS, U.S. POSTAL SERVICE, ACCOMPANIED BY TIRSO DEL JUNCO, GOVERNOR, U.S. POSTAL SERVICE; ALAN C. KESSLER, GOVERNOR, U.S. POSTAL SERVICE; ERNESTA BALLARD, GOVERNOR, U.S. POSTAL SERVICE; AND JOHN WALSH, GOVERNOR, U.S. POSTAL SERVICE

Mr. FINEMAN. Thank you, Mr. Chairman.

Let me take this opportunity to first, before I say anything, to thank you for holding these hearings and to thank you for your interest in the Postal Service and thank you for your interest in reform.

Congressman McHugh, I want to thank as well, as well as Congressman Davis, for their interest in reform.

I want to take another opportunity to do one more thing. One of the things that the Board of Governors does, maybe our most important thing, is the hiring and firing of the Postmaster General.

We are in the process now of looking for a new Postmaster General. I want to take this public opportunity with the Congress to thank Mr. Henderson for his years of service with us. It clearly was a good choice for us to have made in the hiring of Mr. Henderson.

We have a prepared statement which I have given to you. I don't want to reiterate it at this late hour.

Let me just take a couple of minutes to tell you what the frustration is of being on the Board of Governors of the Postal Service and why we are coming here today to ask you for the necessary reform, much of which has been spoken about this morning.

The frustration is actually a rate case. We have talked about what a rate case could be. Let us talk about a rate case was. The actual process, begins 6 months ahead of time and we are now in that process, of saying to the management, OK, let us go look and study what a rate case should be.

Following that 6 months, management come back to us. Over some period of time we meet and discuss the various rates. Then actually a truck pulls up to the Post Office, our offices, unloads tons of paper and takes it over to the Postal Rate Commission.

The Postal Rate Commission then holds hearings for about 10 months. Following that, a decision comes back to the Board of Governors and then we have a opportunity to modify that decision.

Let us look at what we did here. We sent that decision back to the Postal Rate Commission. What does the Postal Rate Commission do? It reviews that decision again and it comes back to the Board of Governors.

What does the Board of Governors have an opportunity to do? We can implement the decision, even though we might not necessarily agree with the Postal Rate Commission, and in this case, we sent it back to the Postal Rate Commission again for a review.

During that period of time, the Postal Rate Commission can send the decision back to us. We are still waiting, actually, for the decision to come back. It has been over there about 30 days or so.

During that period of time we have no power. We can't change our rates. Our hands are tied. There is no ability to run the Postal Service as you would run a private business.

At the same time, as you have mentioned before, the largest part of our costs are fixed by a third party.

Under those circumstances, Mr. Chairman, we come to you, we come to Congress and ask you please enact some legislation that gives us the power to do in 1971 what Congress said, which is to act like a business.

Thank you, Mr. Chairman.

[The prepared statement of Mr. Fineman follows:]

STATEMENT OF S. DAVID FINEMAN
VICE CHAIRMAN, BOARD OF GOVERNORS
UNITED STATES POSTAL SERVICE
BEFORE THE HOUSE COMMITTEE ON GOVERNMENT REFORM

April 4, 2001

Good morning, Mr. Chairman and Committee members. I am David Fineman, Vice Chairman of the Board of Governors. Also here are Governors Ernesta Ballard, Dr. Tirso del Junco, Alan Kessler, and John Walsh. We appreciate this opportunity to speak with you, on behalf of the Board, about the financial challenge facing the Postal Service and the critical need for legislative reform.

The American people look to the Postal Service to deliver mail six days a week to every community and neighborhood throughout the country, at uniform, affordable rates. For many years the Postal Service has benefited from dependable growth in volume and revenue, which was used to expand and improve its network and raise the level of service.

Each year the Postal Service adds 1.8 million new addresses to its delivery network. This is the equivalent of a brand new city of Chicago every year. Our ability to control costs and to improve productivity over the last several years has allowed us to accommodate these new delivery points without raising average prices above the rate of inflation.

This Board is proud of the fact that since 1995, we have had only two rate increases, both of them just one penny on the First-Class rate, which was less than the rate of inflation. The Board's decision to delay the earlier of those two

rate increases from June 1998 until January 1999 saved our customers $800 million in postage during that seven-month period alone.

Unfortunately, it appears we may have turned a corner into a more perilous environment. First-Class Mail volume is nearly flat. The mix of mail in the system is changing unfavorably, so that margins are shrinking. Arbitrated wage rates are outpacing growth in revenues.

The Postal Service competes in a dynamic, technology-driven, global marketplace. It carries into this environment statutory tools provided more than 30 years ago, for an organization conceived to have a more static place in the world and a more dependable financial base. The Board is concerned that a serious mismatch between its legislative charter and the modern marketplace puts the preservation of universal service at risk.

The Board has taken strong and comprehensive measures to attack the recent deterioration in our financial picture to the full extent of current authority. While in recent years the Postal Service has had good success with programs for controlling workhours and other cost elements, it is apparent that extraordinary steps are now essential.

- We have directed management to review all current programs and projects and to curtail or eliminate all non-essential activities.
- We have eliminated $1 billion from the capital commitment budget for this fiscal year, in order to conserve the cash to meet our obligations, and will match future commitments to cash flow.

- We are aggressively reviewing all tools available under the present legal and regulatory framework to improve our financial situation.
- We have directed management to prepare a rate filing, to get the Postal Service back on a pay-as-you-go footing, maintain financial viability, and achieve break-even as the law envisions.
- We have challenged the Postal Rate Commission to reconsider its most recent recommended decision, which falls short of our revenue requirement.
- We have directed management to evaluate rate needs over the longer range, and to review the Commission's ratemaking rules to see if changes can be made in a more timely fashion.

Most of these steps are painful. Many of the delayed capital projects are badly needed. Their postponement will make it even tougher to meet responsibilities to our customers and our employees. The Board has a responsibility to assure that the Postal Service has the financial resources to pay the bills when they come due. This includes the salaries of our over 800,000 employees.

The statutes under which the Postal Service operates contribute to our financial problems, and limit what can be done to address them. The Postal Service has been given limited authority over its prices, services, wages, and other central elements for the management of the postal system.

Across the world, the most advanced nations are rapidly modernizing their postal systems along much more commercial lines. The United States, with 40

percent of the world's mail, lags far behind. Without enactment of vigorous reform in this country, universal service and affordable rates – one or the other, or both – must inevitably erode.

This is not a result that the American people should have to face. This country deserves postal services and structures as robust as any in the world. For a number of years, members of this Committee have led a search for a consensus reform package. I believe virtually the entire mailing community now recognizes a need for change. On behalf of the Board, we pledge that the Postal Service will do all that it can, both to manage the current financial challenge, and to contribute to the success of a comprehensive postal reform measure.

Thank you. We will be pleased to respond to questions.

Questions submitted to Governor S. David Fineman In follow-up to the Government Reform Committee's Oversight Hearing on April 4, 2001

Questions submitted by Chairman Dan Burton

1. In an attempt to contain costs, has the Board considered reducing the workforce through attrition?

Yes, whenever possible workforce reductions will be accomplished first through attrition. If attrition does not accomplish the necessary reductions the Postal Service will follow the legal (Reduction in Force) and contractual rules for downsizing.

2. How frequently does the Board of Governors meet with major mailers or trade associations representing these mailers?

Within the limitations imposed by the part-time nature of the appointment and our other responsibilities, the Governors attempt to make themselves available to mailers or their trade associations as necessary and appropriate. Postal Forums, held twice yearly, afford an opportunity to visit with a range of mailers. One or more Governors have attended the last several forums.

Since Robert Rider became Chairman and I became Vice Chairman in January we have sought opportunities to meet with a fair cross section of mailers. In February, we hosted a meeting of a dozen mailers and association representatives. In March, Chairman Rider met with the Steering Committee of the Saturation Mailers Coalition in Washington, D.C. In April, I attended a meeting of the Graphic Communications Association in San Antonio, Texas, attended by many major mailers.

Of course, there are other less structured occasions to visit with mailers. Many attend our monthly meetings and take the opportunity to share their thoughts with us. Our meetings held outside Washington afford the opportunity to meet mailers from other parts of the country.

It is important that the Governors understand the interests and concerns of our customers. We will continue to take advantage of opportunities to do so, and seek out opportunities to meet with our customers.

3. You recently directed Postal management to review the possibility of reducing mail delivery to five days a week. How much would this save? What impact would it have on mail processing?

The study is not complete yet. The BOG requested a report within 90 days. Findings will be presented to the BOG on July 9.

4. Do you agree with the decision by the Comptroller General to add the Postal Service to its "High Risk" list?

I appreciate, and am in agreement with, the action of the Comptroller General in placing the Postal Service's transformational process on GAO's High-Risk list. I agree, as well, with the reasons for his action.

The Postal Service transformational process is governed by a now outmoded regulatory structure that was put in place 30 years ago. That process was intended to enable the transformation of the Postal Service to a self-sufficient independent entity that would be able to run in a business-like manner, to "break even" financially and, most importantly, to assure affordable universal postal service. The Postal Service has maintained unswerving commitment to those goals over the last 30 years and has made great progress in achieving them. Accordingly, the Postal Service itself has not been placed on the High-

Risk list; the transformational process, which governs the latitude of the Postal Service to operate as a business, has been placed on the High-Risk list.

As Comptroller General Walker stated in his April 4, 2001 testimony before your Committee, that transformational process is in urgent need of reform.

> **"Overall, the Service, however, faces major challenges that collectively call for a structural transformation in order for it to remain viable in the 21st Century. The last major reform of the Postal Service occurred in 1970. The world has changed fundamentally since 1970. It will change even more in the coming 31 years....Accordingly, we are adding the Postal Service's transformation efforts to our High-Risk List, ..."**
>
> **"Let me emphasize, we are not putting the entire Postal Service on our High-Risk List."..."Rather, we are focusing on the challenges associated with the transformation effort and the related obstacles that must be addressed in order to enable the Postal Service to truly transform itself for the 21st Century."**

I concur with that testimony of the Comptroller General and fully support the efforts he and your Committee have initiated to address and resolve the needs of the Postal Service, its customers and the public. The Governors of the Postal Service will support these efforts with our full commitment and cooperation.

4a. What actions will the Board take to remove the Postal Service from the General Accounting Office's "high-risk" list?

Resolving the structural issues now impeding the Postal Service transformation process will require the absolute commitment and cooperation of the GAO, Congress, the Board of Governors, postal management, unions and management associations, and the entire mailing community.

In this, also, we concur with the forceful statement of the Comptroller General in his April 4, 2001 testimony before your Committee that the following actions need to be taken:

> **1. The Postal Service should develop a comprehensive plan in conjunction with Congress and its other key stakeholders, such as the postal unions and management associations, customers, and the Postal Rate Commission, that would identify the administrative and legislative actions needed to address the Service's financial, operational and human capital challenges and that would establish a timeframe and specify key milestones for achieving desired results.**
>
> **2. The Postal Service should provide summary financial reports to the Congress and the public on a quarterly basis. These reports should provide all interested parties with an understanding of the Postal Service's financial conditions and its future outlook; and,**
>
> **3. The Postal service will work with the GAO and Congress "to identify and analyze possible improvement options" including options developed by other countries' for the transformation of their postal services " options for addressing the Service's short-term and long-range challenges."**

The Board will lead the Postal Service effort in this process. In furtherance of these recognized objectives, the Board has exercised its role by acting on its primary responsibilities in recent weeks. First, we selected a Postmaster General who will provide leadership and managerial strength to the Postal Service. We believe that Jack Potter is particularly well suited to lead the Postal Service through this transitional phase. Second, the Governors met our fiduciary duties to the Postal Service by acting responsibly in the ratemaking process when we voted unanimously to modify the rates recommended by the Postal Rate Commission. The third of these responsibilities is to guide the development of policy and business strategy for the Postal Service. Pursuant to that, the Governors have advised Congress of the critical parameters for postal reform.

5. As Governors of the United States Postal Service, it is your job to "direct and control the expenditures and review the practices and policies of the Postal Service." In essence, you are similar to a private-sector corporate board of directors, with ultimate responsibility for the success or failure of the Postal Service. Looking back over the last few years, what would you have done differently to prevent the current financial situation?

In hindsight, we should have acted more aggressively on the timing of postal rate decisions. Specifically, we should not have deferred implementation of Docket No. R97-1 rates to January 1999. This decision cost the Postal Service $800 million in additional net incomes through fiscal year 1999. Additionally, we should have filed for the last rate increase in 1999 instead of 2000. Further, some of the aggressive actions that management is now taking toward decreasing our workforce, better evaluating our use of automation, should have been taken in a more aggressive fashion. That action would have reduced the estimated fiscal year 2001 deficit by $950 million. However, it should be noted that management actions have contributed significantly to lessening the negative impact of the current financial situation. Specifically, in fiscal year 2000, over 6.2 billion additional pieces of mail were delivered to 1.7 million additional delivery points by the equivalent of 6,200 fewer employees than the preceding year. This performance equates to Total Factor Productivity improvement of 2.5 percent and represents cost savings of $1.6 billion. Through the end of May of this year, similar employee reductions have been attained along with Total Factor Productivity of 2.0 percent, representing cost savings of over $950 million. Had this performance not been accomplished, the net loss in FY 2000 would have been $1.8 billion as opposed to $199 million and the cumulative net loss through FY 2001 would be approximately $1.4 billion instead of $422 million.

6. According to the General Accounting Office, the Postal Service has total outstanding debts of $9.3 billion dollars. If the Postal Service exercises its full borrowing authority of $3 billion each of the next two years the Service could reach its statutory borrowing limit of $15 billion by the end of next year.

6a. Will this scenario cause the Postal Service to run out of cash?

Under such a scenario, the Postal Service would no longer retain legal authority to increase its debt and could very likely run out of cash. The combination of operating losses and the magnitude of cash outlays for capital determine Postal Service cash and debt balances.

6b. What is the Postal Services strategy to pay off its debts?

To lower debt outstanding, the Postal Service must earn net incomes. To accomplish this, our current strategy calls for aggressive productivity and cost reduction efforts to bring Postal variances into balance. We believe that there must be some rate increases, although the Board hopes to keep those increases at a minimum.

7. The Board has reduced the Postal Service's planned capital commitments by $1 billion dollars. How long can the Board delay capital investments before the lack of funding begins to negatively impact on postal infrastructure and operations?

The freeze on capital commitments was a fiscally responsive action taken to ensure that cash is available to meet current obligations. Although planned commitments have been reduced in fiscal year 2001 and will probably be reduced in 2002; we will still have capital outlays of approximately $2.7 billion in 2001 and $2.2 billion in 2002. These expenditures will be for infrastructure investments and for labor replacement efficiency investments that have already been contracted. We expect that the freeze on new contracts will continue at least through this fiscal year. We will continue to plan for additional projects that produce productivity gains and contract for them when funding is available. We will also proceed with selected investments related to health and safety of our employees and customers, all legal requirements and other emergencies

The action to freeze new capital commitments was done recognizing that in the long run this could have a negative impact. Given our financial situation there was no choice. Continuing to proceed with additional investments when the funding was not going to be available was not an option. We will monitor the impact of delaying major investments and will take action to sustain operations until funding is available to make improvements.

8. GAO has reported that the Postal Service is experiencing an intensifying financial squeeze, growing operational challenges, and increased competition from the private sector. The Service has noted that its legal and regulatory framework limits the steps it can take to address some of these problems. What essential elements should be part of postal reform?

A meaningful postal reform proposal should include the following elements:

- **Pricing flexibility, including a faster rate setting process, the ability to customize services for major customers, and freedom to price non-monopoly products.**
- **Product flexibility, including the ability to introduce new products without resorting to overly cumbersome administrative proceedings.**
- **Labor and operations flexibility, including replacement or repair of the binding arbitration process.**

9. The Postmaster General has announced his retirement. What unique qualifications and leadership traits will the Board be looking for when selecting the next Postmaster General? When does the Board anticipate making an announcement?

The Board of Governors announced the selection of John Potter as the next Postmaster General on May 21, 2001. We believe that Mr. Potter will provide leadership and managerial strength to the Postal Service.

10. Has the Postal Service generated a net profit from its e-commerce initiatives, like its e-bill pay program? If not, when do you think these initiatives will generate net income?

The Postal Store—formerly called Stamps Online—has taken in over $40M in postage revenue, though this is typically considered core rechanneled product revenue. We do believe that there have been some additional purchases of postage through the Postal Store, however, it is difficult, if not impossible to determine the exact amount.

NetPost CardStore, launched in December 2000, has a net profit of $6,758 for the period inception through April 2001.

Although other eCommerce initiatives have not yet shown a profit, it must be remembered that none of the Postal Service's eCommerce products are very old, most have been in the market for less than a year.

Our eCommerce products are earning revenue, and exhibiting positive growth on a consistent basis.

Questions submitted by Congressman Danny Davis

1. The Board recently announced a freeze on capital commitments that will affect more than 800 facility projects. Why was this freeze imposed and how long will it last?

The freeze on capital commitments was a fiscally responsive action taken to ensure that cash is available to meet current obligations. Although planned commitments have been reduced in fiscal year 2001 and will probably be reduced in 2002; we will still have capital outlays of approximately $2.7 billion in 2001 and $2.2 billion in 2002. These expenditures will be for infrastructure investments and for labor replacement efficiency investments that have already been contracted. We expect that the freeze on new contracts will continue at least through this fiscal year. We will continue to plan for additional projects that produce productivity gains and contract for them when funding is available. We will also proceed with selected investments related to health and safety of our employees and customers, all legal requirements and other emergencies

The action to freeze new capital commitments was done recognizing that in the long run this could have a negative impact. Given our financial situation there was no choice. Continuing to proceed with additional investments when the funding was not going to be available was not an option. We will monitor the impact of delaying major investments and will take action to sustain operations until funding is available to make improvements.

2. Will postal service financial difficulties result in a huge backlog of needed capital investment in post offices and postal facilities?

There will be a backlog. The size and the impact of that backlog will depend on the length of the freeze. The action to freeze new capital commitments was taken with the recognition that, in the long run, this could have a negative impact. Given our financial situation there was no choice. Continuing to proceed with additional investments when the funding was not going to be available was not an option. We will monitor the impact of delaying major investments and will take action to sustain operations until funding is available to make improvements.

3. What impact would cutting Saturday delivery have on customer satisfaction?

Postal management created a task force to study the impact of reducing delivery from six to five days a week at the direction of the Board of Governors. As part of the initiative, the task force is attempting to assess the impact a reduction in delivery days would have on customer satisfaction. The study is not complete yet. The BOG requested a report within 90 days. Findings will be presented to the BOG on July 9.

4. The rate increase is affecting the growth of mail volume. How does the postal service weigh the long-term effects of raising rates on its revenues? Isn't an endless cycle of rate increases self-defeating?

We directly account for these impacts. The Postal Service includes in its revenue and volume forecasts econometrically estimated own-price elasticity impacts. These elasticities reduce volumes for the impact of rate increases.

Every time we have increased postal rates in a general rate increase, revenues have increased. Our elasticities reflect this history. We are sensitive to the fact that price increases could be self-defeating in particular markets but we are not able to price separately for the customers in these markets under the current regulatory structure.

5. In your letters to Congress, you talk about the collective bargaining system and compulsory arbitration. What do you hope to accomplish by raising this issue now and how would regulatory reform impact this?

The mandatory interest arbitration process needs to be modified. The problem is that final and binding interest arbitration, as currently provided under the Postal Reorganization Act, does not encourage the parties to make realistic bargaining decisions. Rather, the present statutory system permits a party to avoid facing up to tough decisions and allows a third party, who is accountable to no one, to resolve the dispute.

It has been suggested that a system based on the Railway Labor Act would provide a solution, by providing postal employees a right to strike, with necessary protections for the American public against the impact of a strike or strike threat on essential postal services. Alternatively, a less sweeping solution might make crucial changes in the current arbitration system, such as requiring the arbitrator to consider the impact of any decision on the public's interest in affordable universal postal services, or the use of last-best-offer or "baseball" arbitration.

6. Should the postal service be a profit-making entity? If so, what level of profit would you consider appropriate?

If the Postal Service remains an integral part of the government, it is by no means clear that it should operate merely to break even, or at a loss. If, as some argue, exposure to the profit motive is what makes private businesses and their employees more innovative, productive, and efficient, the same might prove true for a government establishment. It may be feasible to use profits to pay employees at a rate above the statutory ceiling as a means to attract and retain the best employees. Moreover, a profit-making Postal Service may be able, ultimately, to pay the federal government a dividend.

The essential function of the Postal Service, and its reason for existence, is to deliver fundamental universal services to the American public at reasonable prices. Whatever shape it takes, postal reform must further that ultimate goal.

7. What actions has the postal service taken to work with the Inspector General to provide whistleblower protections to all postal employees?

All postal employees currently have whistleblower protection. Echoing the provisions of 5 U.S.C. 2302(b)(8), postal regulations (Employee and Labor Relations Manual, section 668.118) state:

> **"No one may take or fail to take a personnel action as a reprisal for a disclosure of information by an employee or applicant which the employee or applicant reasonably believes evidences:**
>
> > **a. A violation of any law, rule, or regulations; or**
> > **b. Mismanagement, a gross waste of funds, an abuse of authority, or a substantial and specific danger to public health or safety, if such disclosure is not specifically prohibited by law or if such information is not specifically required by Executive Order to be kept secret in the interest of national defense of the conduct of foreign affairs."**

Employees or applicants who believe that a personnel action has been taken against them in violation of the above whistleblower provision, have several appeal procedures available to them, depending on the nature of the personnel action taken and on whether the employee is covered by a collective bargaining agreement or not. These appeal procedures include the Equal Employment Opportunity complaint process, the Merit Systems Protection Board appeal process, the negotiated grievance process (for bargaining unit employees), and the Postal Service's internal appeal procedures (for non-bargaining unit employees). In addition, allegations of reprisal, which cannot be brought under any of these procedures, can be appealed directly to the Office of the Postmaster General.

Over the last several months, postal officials have been working with the Inspector General to enhance this whistleblower protection by refining the language of the provision (for example, to provide specifically for disclosures made to the Inspector General) and to improve the appeal process. Postmaster General William Henderson recently announced the Postal Service's commitment to such enhancements. As required by the Postal Reorganization Act and collective bargaining agreements, proposed changes will be shared with postal management associations and unions before any changes become final.

8. Have you received the labor savings you anticipated from automation? If yes, how many positions have been reduced?

Automation is producing savings and cost avoidances greater than original projections. Since 1987 we have invested $5.4 billion in letter mail automation projects and through 2000 we have achieved approximately $19 billion in savings/cost avoidances against original projections of about $18 billion. Career complement has been reduced by over 21,000 since its peak in 1999, while we have increased our volumes by 7.9 billion pieces and we have added 3.3 million additional deliveries to the network.

Questions submitted by Congressman Henry Waxman

1. The Board announced yesterday that it is studying the impact of reducing delivery from six to five days a week. What impact would cutting Saturday delivery have on customer satisfaction?

Postal management created a task force to study the impact of reducing delivery from six to five days a week at the direction of the Board of Governors. As part of the initiative, the task force is attempting to assess the impact a reduction in delivery days would have on customer satisfaction. The study is not complete yet. The BOG requested a report within 90 days. Findings will be presented to the BOG on July 9.

2. The Board recently announced a freeze on capital commitments, affecting more than 800 facility projects. Could the freeze delay overdue improvements and the associated efficiency gains needed to help postal rates down? In other words, are freezing capital commitments a band-aid that will be penny-wise today and pound-foolish tomorrow?

The freeze on capital commitments was a fiscally responsive action taken to ensure that cash is available to meet current obligations. Although planned commitments have been reduced in fiscal year 2001 and will probably be reduced in 2002, we will still have capital outlays of approximately $2.7 billion and $2.2 in 2001 and 2002. These expenditures will be for investments in infrastructure and for labor replacement efficiency investments that have already been contracted. We expect that the freeze on new contracts will continue at least through this fiscal year. We will continue to plan for additional projects that produce productivity gains and contract for them when funding is available. We will also proceed with selected investments related to health and safety of our employees and customers, all legal requirements and other emergencies.

The action to freeze new capital commitments was done recognizing that in the long run this will have a negative impact. Given our financial situation there was no choice. Continuing to proceed with additional investments when the funding was not going to be available was not an option. We will monitor the impact of delaying major investments and will take action to sustain operations until funding is available to make improvements.

3. The Postal Service has reported declining growth in first-class mail volumes and an increased use of automation in processing mail. Given this, shouldn't there have been a corresponding decease in work-hours and overtime usage?

Automation is producing savings and cost avoidances this year. This fiscal year, 2001, through week 2 of accounting period 10, the Postal Service is using 13.5 million less work hours, in the field, than we did for the same period last year. For the same period this fiscal year in the field overtime hours are 925 thousand less than the same period last year.

4. Would you support the creation of a presidential commission to identify inefficiency and waste in the Postal Service and recommend methods for improving mail service? If not, why not?

We believe that postal reform legislation is needed now, and will support whatever means appear to provide the quickest path to that goal. Creation of a presidential commission might provide a useful step along that path. On the downside, however, creation of a commission could also postpone progress toward meaningful reform, perhaps for a year or two, while the commission completes its study and prepares its report. It is also possible that a commission would merely duplicate the work on reform already done by responsible parties or, at worst, frustrate progress toward reform with what is sometimes referred to as "paralysis through analysis".

5. In the last Congress, I sponsored H.R. 2535, legislation which would authorize the Postal Service to phase-in rate increases. Has the Postal Service considered changing rates for mailers who prefer regular, small increases on a different schedule from the changes for individual piece users who may find frequent, small increases inconvenient? Does current law prohibit such a system?

The current law does not necessarily preclude phasing. However, the Postal Rate Commission's rules as they stand do not easily accommodate phasing. Instead, the Commission's rules contemplate that the Postal Service will present a single-stage rate proposal. While the Commission could arguably change or waive its rules, it would need to be done well ahead of time, in light of the time it takes to plan and develop an integrated filing for rate and fee increases.

The concept of implementing rates at different times is intriguing. Most often, as mentioned in the question, this approach is associated with less frequent changes for individuals and more frequent changes for other customers. The Postal Service is always interested in having more options and more flexibility in developing rates for customers.

However, neither phasing rate increases over time nor changing rates for different products at different times would be free from complications. For instance, while phasing rate changes may have appeal to customers by mitigating the impact of a rate change, the initial phases of any rate changes must provide sufficient funds to operate the Postal Service in the interim. At the same time, any phasing system should balance predictability and flexibility. By predictability, we mean that customers should be able to plan on future rates, and the Postal Service should be able to plan on future revenue expectations. At the same time, operating and economic conditions do change, and any system must be able to adapt accordingly.

While we find these alternative approaches interesting, several issues would need to be addressed if they were to be adopted. For instance, small businesses and other institutions that have access to meters and other forms of postage payment also use the single-piece rates used by individuals. Also, the discounts other customers receive for sorting and barcoding bulk mailings are based on the single-piece rates. While these issues are not necessarily insurmountable, they would need to be addressed.

6. Would you support legislative reform allowing you to set rates for competitive products?

The Postal Service Board of Governors has called for a comprehensive review of the Postal Reorganization Act including the provisions that established the framework for pricing postal products and services. In general, the Board supports legislative reform that would simplify and streamline postal ratemaking. We recognize that many of the products and services we sell have few direct competitors and that the public interest might reasonably require some regulatory oversight of the pricing of these products. However, some product and services such as Priority Mail have been identified as "competitive" with other private sector alternatives. Our customers and the nation as a whole will benefit if we are allowed to price these products in response to marketplace signals. The Board of Governors believes that increased pricing flexibility for competitive products should include the ability for Postal Service management to directly set the prices for competitive products. We are, however, willing to adopt guidelines that will ensure that each product covers its attributable costs and makes a contribution to the institutional costs of the Postal Service.

6a. Should you determine whether or not a product is competitive or should the PRC?

The determination of whether a product or service is "competitive" should be made by evaluating the characteristics of the product and the marketplace in which it is sold. We believe that the determination of whether a product is "competitive" should be made by Postal Service based on its evaluation of the market conditions. Any determination that a product is competitive may reasonably be reviewed by the Postal Rate Commission.

7. How reliable are postal revenue and expense projections in predicting the effect of economic downturns?

Economic downturns are difficult to project. Unforeseen economic downturns are almost impossible to predict – and their impacts unprojectable. The Postal Service employs nationally prominent economic analysts, the same used by corporate America, and endeavors to plan for estimates of economic change. This is reflected in our revenue and volume forecasts. The most recent economic slowdown, however, occurred very rapidly, as demonstrated in the business pages of newspapers in recent months as business after business has reported disappointing earnings and reduced earning projections. The Postal Service has been impacted similarly to virtually every major U.S. Corporation.

As recently as December, most mainstream economic forecasters were not projecting the slowdown that has occurred in the first two quarters of this calendar year. This slowdown was not reflected at that time in the independently produced macro forecasts that the Postal Service purchases from DRI (now DRI*WEFA). Further, in its November rate decision, the Postal Rate Commission found "the short-term outlook does not appear to involve any risk of unforeseeable financial harm to the Service. " PRC, Docket No. R2000-1, November 13, 1991 (Emphasis added). Neither did the Fed react to the onset of the slowdown until after the New Year, when it first cut interest rates on January 3rd.

8. What actions have you taken to assure relocation payments are only paid when the person moves and is warranted? Has the use of relocation payments been used to circumvent the pay cap?

Relocation policy for employees is well documented in policy handbooks and officer relocations are now approved by the Board of Governors.

Relocation payments have not been used to circumvent the pay cap.

9. Do you feel that marketing is an appropriate role for the Postal Service? How do you quantify the revenue generated from advertising? What is your total advertising budget allocated for FY 2001?

Like all large organizations, including several government agencies, the U. S. Postal Service uses marketing and advertising to inform the American public of the services and products we offer. Marketing and advertising helps increase Postal Service revenues, which, in turn, helps keep stamp prices low and provides funding to re-invest in advanced equipment to ensure improved production which helps provide better service to the public and helps hold down costs. The Postal Service uses standard systems that most corporations utilize to measure the impact of advertising by recording the number of people—referred to as "impressions"— who see our advertisements. While it is difficult to quantify specific revenues that can be attributed to advertising, it is clear that revenues increase when a specific product is featured in an advertising campaign, and, consequently, when that produce is not featured, revenues are less. The advertising budget for 2001 $156.1 million.

10. Should the Postal Service change from its current contracting practices and follow the Federal Acquisition Regulations (FAR)?

No. The Postal Service's business and competitive objectives cannot be achieved by following the Federal Acquisition Regulation (FAR). Congress recognized our need to operate in a competitive business environment when it passed the Postal Reorganization Act of 1970 (the Act) and specifically, and appropriately, exempted the Postal Service from most laws concerning federal contracting. Among other things, the Act allowed us to establish purchasing policies and procedures that enable us to hold down operating costs while providing low cost, high quality, universal mail service. Thirty years have passed and we find ourselves in a business environment that is more competitive and technology-

driven than ever. Over that period of time our purchasing policies and procedures have evolved, and successfully so, to keep pace with those changes.

While we have adopted some federal purchasing practices, the Act requires the Postal Service to operate from its own revenues, not taxpayer subsidies, to fulfill its mission to the public. Because of this we have charted a more businesslike purchasing approach similar to that used in the private sector in order to operate more effectively in a highly competitive commercial marketplace.

Three basic models were used in drafting our purchasing policies: the 1982 OFPP "Proposal" recommending numerous reforms in federal procurement; commercial practices, as exemplified by the Uniform Commercial Code; and the FAR. However, our Purchasing Manual avoids prescribing the elaborate processes that are more typical of the FAR, and places greater emphasis on the use of commercial practices and allowing the contracting officer latitude to exercise informed business judgment and discretion. The Purchasing Manual emphasizes significant policies and processes, rather than detailed procedures.

We believe that our policies combine the efficiency of private sector purchasing with the commitment to fairness and accountability expected of a public agency. We also believe that providing qualified contracting officers the discretion to exercise their business judgment, reinforced by management control and oversight, is the best insurance that our purchases are conducted fairly, and that purchasing-related decisions are made based on the business and competitive objectives of the Postal Service.

11. How confident are you in your mail volume estimates?

Our mail volume estimates have generally been quite good, within about one percent of actual volumes. However, given the size and magnitude of the Postal Service even a small forecasting error can lead to a significant swing in Postal Service finances. A one-percent swing can result in a revenue shortfall of $700 million or more, which combined with an inadequate rate recommendation and increasing cost inflation, could place the Postal Service's finances seriously out of balance. This is essentially what has happened over the last year and one-half.

12. In September 2000, GAO issued a report on the Service's e-commerce initiatives. How is the Board reviewing the Service's e-commerce initiatives and how long do you plan to pursue these initiatives if they do not make money?

The Strategic Planning Committee of the Board of Governors and the entire Board are reviewing the performance of all eCommerce initiatives. The Board reviews them on a semi-annual basis and the Strategic Planning Committee reviews them on a quarterly basis.

Mr. BURTON. Thank you very much. Let me start off by saying I presume that you sent to, previously, Mr. McHugh and Mr. Davis your recommendations on how to streamline the process.

Mr. FINEMAN. I think that is a fair question. During the previous administration, I would say, that the Board of Governors could not reach consensus. We are appointed by various Presidents and we are a bipartisan group. The statute provides five of us be of one party and four of another. There was no consensus reached by the Board previously.

The letter which we sent to the leaders in Congress and to the President of the United States set forth the views of all of the members of the Board as it is constituted today.

Mr. BURTON. Was it individual views or the unanimous view of the Board?

Mr. FINEMAN. The letter that we sent to the leadership and to you, Mr. Davis and Mr. McHugh, and all Members of Congress, we assume, have it now, is the unanimous views of all of the members of the Board.

Mr. BURTON. I don't have that letter in front of me, but does that letter spell out the reforms that you think are necessary to make this operate in a more efficient, business-like manner?

Mr. FINEMAN. I think what it does is it sets forth in general principle the kind of reforms that we think are necessary.

Mr. BURTON. Let me suggest, and I suggested this in my opening comments today, that every segment of our society that is interested in the problems we face needs to get to the relevant committees, and particularly this committee, since we have the jurisdiction, the recommendations that they think should be incorporated into a postal reform bill.

Now, we have a lot of good things in the bill and Mr. McHugh and Mr. Davis fashioned in previous Congresses. But obviously there were some problems with that; otherwise we would have gotten it passed.

What we would like to have is the direct mailers, the newspapers, the magazine people, the Board of Governors, everybody tell us from their point of view, individually or collectively as groups, what you think ought to be in the bill so we can craft it as quickly as possible and try to meet the requirements that are necessary to solve the problem and make this more like a business instead of, it sounds like a hodgepodge of things.

I can't imagine you playing ping-pong with those rate increases. That is what you were doing. They sent it to you and you sent it back. They sent it to you and you sent it back. Obviously, that is not the way to run a business. There has to be a final decision-making process that is going to stand.

So, if you and your colleagues on the Board have some suggestions, as quickly as you can reach agreement, we would sure like to have those.

Mr. FINEMAN. We will submit them to you, Mr. Chairman.

Mr. BURTON. Would you do that?

Mr. FINEMAN. Yes, sir.

Mr. BURTON. In an attempt to contain costs, hearings the Board considered reducing the work force through attrition?

Mr. FINEMAN. We have told management to go forward with every kind of cost saving that they can attempt to reach. We obviously don't want to decrease service. But at the same time, we have put everything on the table, Mr. Chairman. One of them is obviously reduction in our work force. But we don't want to reduce service.

Mr. BURTON. I understand. But have you urged and taken a look at automation and other new technologies that might be able to not take the place of people, but those who are leaving through attrition or through retirements, to cut down the costs? Much like I said before when the auto industry went to robotics.

Mr. FINEMAN. Absolutely, Mr. Chairman. That is one of the things that we have done. I think we can be proud of the automation system that has come about. We have heard the Postmaster talk about the productivity gains that we have had.

Mr. BURTON. But I was wondering if there is more.

Mr. FINEMAN. I think there is a higher bar that can be reached. I think that I speak for everyone on this Board in saying that to you. That is the challenge that we have given to management.

Mr. BURTON. We would like to have the recommendations for that as well.

Let me ask one more question here while I have the time. How frequently does the Board of Governors meet with the major mailers or trade associations that represent them?

Mr. FINEMAN. I cannot say that there are regular, periodic meetings. I can say that Chairman Rider, who is not here today, and myself met with I believe it to be all the major mailers organizations to have a frank conversation with them. Obviously, they talked to us about rates. We talked to them about reform. We had a very, very frank conversation.

There is not a regular periodic meeting. I do personally believe that we have to reach out and meet with those mailers on a regular basis.

Mr. BURTON. Well, they are very concerned, a number of them, as you know, the smaller ones about going out of business because costs are getting out of control. The larger ones are concerned as well. So, I hope you will make those as frequent as you can. I know you have a lot on your plate.

The Postmaster General, who we all agree has done an outstanding job, has announced his retirement. What unique qualifications and leadership traits will the Board be looking for when they select the next Postmaster and when do you anticipate making an announcement?

Mr. FINEMAN. Well, we have no one right now. I want to make that perfectly clear. We are still in the process of interviewing. When we leave here we are going to leave to begin some more interviews this afternoon. We conducted some yesterday afternoon. We have been working on this for some period of time.

I think it is probably one of the most difficult jobs in government. Not a whole lot of people are raising their hand volunteering. We are trying to seek out the best person from both the private sector and government service who can lead an organization of almost 800,000 people, 38,000 locations, with all the problems that this

committee has gone through earlier this morning, into the 21st century.

I guarantee you that this is at the top of our priorities, Mr. Chairman.

Mr. BURTON. I am sure it is. Since we are all trying to see more sound business practices incorporated into the Postal Service, I hope you will look long and hard at people in the free enterprise system who have shown superior talents in using business practices to streamline businesses.

You will notice a lot of the major corporations will steal an executive from one to the other because they are so effective at dealing with these complex problems when we have so much competition. I hope you will do the same thing.

Mr. FINEMAN. We will. Thank you, Mr. Chairman.

Mr. BURTON. Mr. Davis.

Mr. DAVIS. Thank you, Mr. Chairman.

Mr. Fineman, let me appreciate the work that you and your colleagues do as members of the Board of Governors. Let me also express an appreciation for the frustration that you amplified as you started your testimony. It does seem to me that it would be somewhat difficult to be part of a management operation but not really have the authority to make management decisions that impact heavily upon what it is that you do.

So, I think we heard you when you talked about the Postal Rate Commission and the relationship between the two and where the Board sits in relationship to where they are.

But let me ask you, in your letters to us, you have mentioned collective bargaining and compulsory arbitration as some concerns. Let me ask what it is that you would hope to accomplish by raising that issue and what is it that you think legislatively might be done that could alleviate whatever problems you see with the issue?

Mr. FINEMAN. Congressman, you come from Chicago and I come from Philadelphia. We could argue as to which town is more of a labor town, whether it is Philadelphia or Chicago.

My friends in the labor unions in Philadelphia, I am sure, would argue hard for Philadelphia. There is no intention, and I want to make this perfectly clear, no intention on our part to take away from the collective bargaining process. I believe in the collective bargaining process, as do my colleagues.

What we are talking about is the third party arbitrator who makes these decisions in a vacuum. I think that there are various models that are out there that we should look at—I say "we" collectively with Congress, as to what else can be done.

I am a lawyer, Labor Law 101 told us that when there is friction between labor and management when they negotiate a contract. At the end of the day after both parties negotiate the contract, because they have risks on both sides, they probably walk out and they have better labor-management relationships.

That is what I think we have to find. One of the things that Postmaster General Henderson mentioned was the Railway Labor Act. I think that is a good place to start. That is the kind of thing that we are talking about, Congressman.

Mr. DAVIS. Has there ever been, to your knowledge, any cost or amount put on the difficulties that we have experienced or continue

to experience relative to labor-management relations and how much time and how much energy, and ultimately how much of the cost of operating the system this becomes for us?

Mr. FINEMAN. I can't tell you with any specificity what it is, but there is not infrequently a Board meeting where it isn't something that is discussed, the amount of time that people spend at mediations, arbitrations, spend on grievances.

Now, there is a great success story at the Postal Service, one that has been modeled all over the United States, which is the Redress System in which we try to mediate the differences between the parties before they get to the grievance stage.

It is a real success story as to how they have been able to lower costs. But obviously, it is a great cost, Congressman.

Mr. DAVIS. If we could get a better handle on that, in all likelihood, we could actually save ourselves a great deal of money as well as time and other kinds of things.

Mr. FINEMAN. I believe so.

Mr. DAVIS. Let me ask you, even though this was not a part of your testimony, but I couldn't help but be intrigued as we were listening to the discussion relative to partnership with FedEx. I was trying to figure out how can we determine marketplace impact on ultimate costs unless we are negotiating with the marketplace as opposed to an entity within the marketplace.

Would you have any idea?

Mr. FINEMAN. I can only say that this Board, when the FedEx contract was discussed with it, was concerned about many of the things that the Congress was concerned with as well. As a result, we decided that we would hire our own counsel to look at that contract. We listened to the experts from Price Waterhouse. We listened to experts about a fairness opinion from Morgan Stanley. We became convinced that it was the right thing to do.

Mr. DAVIS. I don't doubt any of the experts. It just seems to me that that is a concept in terms of free enterprise that I have a little bit of difficulty understanding. But certainly we will get additional information, I am sure.

Mr. FINEMAN. Yes, sir.

Mr. DAVIS. Thank you very much, Mr. Chairman. I have no further questions.

Mr. BURTON. I just have a couple more questions. I want to thank you very much for your patience. I know it has been a long day and your rear end starts falling asleep.

Mr. FINEMAN. We are still with you, Congressman.

Mr. BURTON. What is that saying? "The mind can't focus on things that the rear can't tolerate?" It is something like that.

There is a potential rate increase pending now. You have played ping-pong with it. The economies that we have talked about today that the Postmaster talked about could affect the profitability of the Post Office or non-profitability of the Post Office.

Is it absolutely essential that there be a rate increase in the not too distant future or can this be handled through economies in the Post Office while we try to fashion some kind of solution here in the legislative branch?

Mr. FINEMAN. We are going to attempt to do everything we can not to have a rate increase. But on the other hand, if it is abso-

lutely necessary, we will go forward with it. We are going to do what we have to do in our fiduciary obligation.

I would say this: One of the things that I heard some of the Congressmen talking about earlier is the fear that I have and it is the system that doesn't provide any solution for us. Because the fear that I have is that if we impose a rate increase and then we deplete the amount of mail that we have, this is only a spiral that we can't get ourselves out of.

Mr. BURTON. That is absolutely right.

Mr. FINEMAN. When we met with the mailers, you know, and they are begging us that their companies are going to suffer as a result of a rate increase, I feel for them. That is the question of reform. That is the question as to why we need reform.

The other part of it is that we cannot do this under present statute. We have no choice because we have this cost-based system so we can't do anything without a market-based system. It is a frustrating position to be in. I feel the pain, to some degree, that the mailers have. I want to feel their pain. I say to them, "I want you to sit in my seat for a minute as the steward here and not roll up this deficit."

I think you have to remember something. What we have been able to do before, when we talk about a rate increase, one of the things that the system does allow us is that we propose rates to the Rate Commission. It will take them almost 10 months to get back to us.

Then we have a choice as to when we impose the rate. The rate is not going to be imposed at the time we make the submission to the Postal Rate Commission. We will do everything in our power; particularly if some of the measures that we have asked management to reach out for can be implemented within that period of time.

Mr. BURTON. I think the point that you made we have made and it has been made over and over again. The analogy was the car business. If you are having a problem, lacking sales and lacking revenues, if you raise the price you certainly aren't going to solve the problem. You are going to compound it. I am afraid that that might be what you are talking about.

We are going to try to talk to the White House, and I hope you will as well and the new Postmaster will as well, telling them that this is a problem that needs to be addressed by not only the legislative but also the executive branch and some leadership to really try to force this issue.

Let me ask one more question and then I will let you go. Has the Postal Service generated a net profit from its e-commerce initiatives, do you know, like its E-bill Pay Program?

Mr. FINEMAN. At this point I can't tell you that we have. The numbers that have been given to us by management so far indicate that there are losses. The losses are small in relationship to the general revenue of the Postal Service, but they are not profitable at this point.

Mr. BURTON. Well, any information you can give us on that or anything else that you think might be a helpful solution, we would like to have.

Do any of the rest of you have any comments you would like to make? We appreciate you all being here.

Mr. DAVIS. Mr. Chairman, before you wrap up, I would just like to be sure that you have unanimous consent for Mr. Towns to submit his remarks for the record and that we have unanimous consent to leave the hearing open so that individuals who have questions and were not here can get those in.

Mr. BURTON. Without objection, it is so ordered. We will ask if the Members have questions if we can submit them to the people who testified today for answers in writing.

Mr. FINEMAN. We will look forward to answering them. Thank you again, Mr. Chairman.

Mr. BURTON. Thank you very much. We will continue to work with you to solve this problem.

We stand adjourned.

[Whereupon, at 2:05 p.m., the committee was adjourned.]

[The prepared statement of Hon. Edolphus Towns, Hon. Donald Manzullo, and additional information submitted for the hearing record follows:]

Statement of Congressman Edolphous "Ed" Towns
Government Reform Postal Hearing
April 4, 2001

THANK YOU, MR. CHAIRMAN. THANK YOU FOR HOLDING THIS IMPORTANT HEARING ON THE STATE OF THE UNITED STATES POSTAL SERVICE(USPS). WHILE I BELIEVE THAT IF WE STILL HAD A SUBCOMMITTEE ON POSTAL ISSUES WE WOULD HAVE BEEN ADDRESSING THESE ISSUES FOR THE PAST FEW MONTHS, IT IS NO LESS IMPORTANT THAT WE ARE HERE TODAY. LET ME STATE FROM THE OUTSET THAT I HAVE THE UTMOST ADMIRATION FOR THE MEN AND WOMEN WHO SERVE THE US POSTAL SERVICE. THESE ARE DEDICATED PEOPLE WHO SERVE WITH PRIDE, DIGNITY, AND HARD WORK OFTEN IN ADVERSE CONDITIONS. I KNOW THAT IN THE 10TH CONGRESSIONAL DISTRICT IN NEW YORK, I HAVE WORKED WITH THE POST OFFICE ON A VARIETY OF ISSUES. WHILE THERE HAVE BEEN SOME LONG AND HARD BATTLES, THE POSTAL SERVICE HAS ALWAYS BEEN WILLING TO WORK WITH MY OFFICE AND THE COMMUNITY TO ADDRESS THOSE ISSUES.

ALSO, IN 1999, THE CONSUMER FEDERATION OF AMERICA CONDUCTED A NATIONWIDE SURVEY WHICH SHOWED THAT THE VAST MAJORITY OF THE AMERICAN PEOPLE RATE THE POSTAL SERVICE VERY FAVORABLY AND AS CONSUMER FEDERATION EXECUTIVE DIRECTOR SAID AT THE TIME "LIKE THE POSTAL SERVICE AS IT IS".

I FIRMLY BELIEVE THAT THE POSTAL SERVICE MUST MAINTAIN UNIVERSAL SERVICE, AT REASONABLE RATES. UNIVERSAL SERVICE AT REASONABLE RATES PROVIDES A BRIDGE BETWEEN ALL AMERICANS. THERE IS NO DIVIDE. UNLIKE TECHNOLOGY WHERE INDIVIDUALS MUST MAKE SIGNIFICANT INVESTMENTS TO PARTICIPATE - EITHER BY BUYING HIGH PRICED EQUIPMENT OR SEEKING OUT ACCESS THROUGH SOME OTHER MEANS. THE POSTAL SERVICE REQUIRES ONLY THAT YOU HAVE ENOUGH MONEY TO PLACE A STAMP ON AN ENVELOPE OR POSTCARD. THE MISSION OF THE POSTAL SERVICE AS OUTLINED IN THE THE POSTAL REORGANIZATION ACT OF 1970 IS AS TRUE TODAY AS

IT WAS THEN: " TO BIND THE NATION TOGETHER THROUGH THE PERSONAL, EDUCATION, LITERARY, AND BUSINESS CORRESPONDENCE OF THE PEOPLE." WE, HOWEVER, LIVE IN A VERY DIFFERENT WORLD TODAY.

HERE IS THE PROBLEM – WHILE WE KNOW THE AMERICAN PEOPLE LIKE THE SERVICE THAT THEY RECEIVE, YOU FACE A SERIOUS DEFICIT AND A CHANGING MARKET. THE QUESTIONS ARE - HOW SERIOUS ARE THE PROBLEMS ? HOW DO WE ADDRESS THEM WITHOUT CHANGING THE QUALITY AND QUANTITY OF SERVICE? HOW DID WE GET TO THIS POINT AFTER POSTAL RATES WERE RAISED JUST A FEW SHORT MONTHS AGO?

TECHNOLOGY HAS PROVIDED US WITH A GREATER MEANS OF COMMUNICATION AND COMPETITION HAS PROVIDED US WITH MORE EXPRESS MAIL OPTIONS. IF THE POSTAL SERVICE IS TO CONTINUE TO MEET THESE NEW AND EVOLVING CHALLENGES THERE IS NO DOUBT THAT THERE MUST BE SOME CHANGES. I LOOK FORWARD TO

DONALD A. MANZULLO
SMALL BUSINESS
CHAIRMAN

FINANCIAL SERVICES
FINANCIAL INSTITUTIONS AND
CONSUMER CREDIT

INTERNATIONAL MONETARY
POLICY AND TRADE

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Statement of Congressman Donald Manzullo
Chairman, Committee on Small Business
Before the
House Committee on Government Reform
Postal Service Oversight Hearing
April 4, 2001

Thank you Mr. Chairman for the opportunity to make a statement as part of this important oversight hearing. As the Chairman of the Committee on Small Business I feel it is important that this Committee know of an important matter within the Postal Service that affects small business owners.

As you know, last year the Postal Rate Commission recommended a discount for PC Postage as part of the rate case. At the time, the Postal Service did not support this proposal. This year, however, as yet another rate case is being considered, I understand the Postal Service is now re-considering their position on this issue. I fully support for this initiative currently under consideration within the U.S. Postal Service (USPS) for including a discount for PC postage in the upcoming rate case.

Such a discount would clearly be in the best interests of the American small business community. Through a reduced rate, the USPS would justifiably be passing along millions of dollars in savings to small businesses and other mailers. By reducing the budget small businesses spend on postage, as well as saving time and resources, this initiative would be a major factor in enabling small businesses to grow and expand – which, in turn, is the engine for growth in the U.S. economy. Moreover, the advent of PC postage technology has enabled small businesses around the country to provide the same cost-savings to the USPS that have long justified the discount currently provided to larger mailers through workshare discounts. The time has come for the USPS to give this same discount to the small businesses that are producing the same cost-saving benefits.

There are other important reasons for USPS to establish this discount. A reduced rate for PC postage would also be an important step forward in the USPS' ongoing efforts to save money through increased automation and by transitioning postal service operations to the information platform. And it would give the PC postage program, in general, a major boost – which brings new customers to USPS.

At a time when the Postal Service is coming under criticism for their financial management, the PC postage program is an example of the USPS getting it right. It makes sense by bringing the Postal Service into the Internet age. At a time when the Postal Service is confronting critical challenges involving lost market share to private competitors, PC Postage generates new and increased revenue opportunities in key areas of growth.

This afternoon I will be sending a letter to you Mr. Henderson, and Mr. Nolan, expressing these concerns. I would request that a copy of this letter be inserted in the record along with a copy of my statement. Thank you again Mr. Chairman.

Sincerely,

Donald A. Manzullo
Member of Congress

PRINTED ON RECYCLED PAPER

Testimony before the Committee on Government Reform
of the U.S. House of Representatives in hearing on "Financial Woes Facing Postal Service," Washington, D.C. April 4, 2001

by

Delford M. Smith
Evergreen International Aviation, Inc.

Thank you for permitting me to submit written testimony on a matter of tremendous import, for my company, the U.S. air carrier industry as a whole, and the American economy. My name is Delford M. Smith. I am the founder and Chief Executive Officer of Evergreen International Aviation, Inc. ("Evergreen"). Evergreen has been a faithful provider of airfreight and related services to the Post Office for more than three decades. We currently provide dedicated airfreight services and ground handling services to the Post Office in Alaska and the continental United States, and carry international mail.

In summary, it is Evergreen's belief that the Transportation Agreement (the "Agreement") which Federal Express Corporation ("FedEx") and the United States Postal Service ("Post Office") signed on January 10, 2001 is very harmful to airfreight competition, exposes the Post Office and the American people to significant risks of hazards, increased prices, and failure of mail service, and was unfairly awarded, without any regard to the competitive bidding process, or to the numerous carriers who have served the Post Office and the nation for decades.

This is why the Agreement is disastrous for competition:

At present, the Post Office uses a network of carriers to cover its airfreight needs. Contracts for these local services are competitively bid, with as many as thirty bids received for a given contract. When FedEx takes over Post Office mail delivery under the Agreement, in August 2001, the existing contracts which the Post Office has with these regional airfreight carriers will be terminated. Some of these smaller carriers rely on the Post Office for significant percentages of their revenues. With these revenues gone, jobs will be lost, certain carriers may fail, and the far-reaching, diversified network which the Post Office has developed will deteriorate. The planes owned and operated by these carriers will be retired, sold, or dedicated to other purposes.

While the Post Office has its problems, the existing network of regional air carriers is not one of them. By entering into this Agreement, the Post Office is removing the checks and balances of a competitive market from the picture, and is creating a single behemoth, FedEx. The Agreement will not be up for renegotiation until 2008. By then, many of these regional air carriers will no longer be in business. What competition will exist to stop FedEx from naming the price of the next contract?

Competition will also be harmed by the unhealthy concentration of market share in one company. FedEx named the Post Office as one of its competitors in its last annual report. Now, under the Agreement, it has the right to receive detailed information about the Post Office's operations, and to limit the amount of mail the Post Office will be able to put on FedEx planes. While Congress may have originally intended that the Post Office, as a government organization, be exempt from the reach of the antitrust laws, I doubt this great body meant to extend that protection to FedEx. The Post Office has essentially delegated its monopoly power to a private company. This does not enhance competition, it stifles it. And with a lack of competition comes an increase in prices; which, if I'm not mistaken, is exactly what the Post Office was trying to avoid.

This is how the Agreement puts the American People at risk:

The Post Office's existing network of regional air carriers diversifies the risks inherent in air mail delivery. An adverse event affecting one of the carriers will not bring the entire system to a halt. Under the Agreement, however, the Post Office has ignored this simple principle - diversification to mitigate risk - and has put all its eggs in one basket.

FedEx has one primary sorting facility, its "SuperHub", located in Memphis, Tennessee. If that headquarters is disabled, whether by nature, power failure, general mechanical failure, computer systems failure, radar failure, terrorist activity or some large civil disturbance, the Post Office's capacity to deliver its Express and Priority Mail is disabled, completely, along with it.

FedEx has one existing five-year collective bargaining agreement with the FedEx Pilots Association. A strike by the pilots can cripple FedEx, and, by extension, the Post Office.

FedEx is a publicly held corporation. It is traded on several stock exchanges. It, like every privately held corporation, risks certain events arising with little notice at any time: bankruptcy, hostile takeover, corruption, fraud, change in board control, failure of financial products, over-leveraging and other similar events. The risk of any of these events implicates the Post Office, because the risk that the Post Office will not be able to transport mail by air and the risk of an event adverse to FedEx are one and the same under the Agreement.

The Agreement also implicates national security -- something that, remarkably, may not have ever been considered by the Post Office. The Civil Reserve Air Fleet ("CRAF") is a highly successful partnership between the airline industry and the Government that is considered essential to national security. Under CRAF, air carriers voluntarily contribute aircraft in the event the military is unable to fulfill airlift requirements during an emergency or wartime situation. The CRAF program creates a large reserve of strategic aircraft capability for the Government, without requiring the Government to purchase, man, or maintain these assets. The CRAF program has saved the Government an estimated $100 billion since its establishment in 1952. For example, participants in the CRAF program flew thousands of missions for the Government during Operation Desert Storm/Desert Shield. Significantly, the two participants who flew <u>more missions</u> than any other carrier were Evergreen and Emery, and they were two of a handful of carriers – which initially did <u>not</u> include FedEx – to fly into the hostile Gulf region.

The Agreement creates two adverse risks with respect to the CRAF program. First, the inevitable elimination of smaller regional carriers will limit the number of aircraft available for Government use during a national emergency. Second, it will be difficult, if not impossible, for the Government to use FedEx planes during a national emergency. Although they will be the single largest air fleet for package delivery in the United States, FedEx will be responsible for carrying U.S. mail. Therefore, the decision to use or not use the FedEx fleet in a national emergency will at best be difficult. Any decision

would have a profoundly negative consequence. Do we deliver the mail or maintain the Marines? Hardly an easy choice; and certainly not a choice that the Government should willingly (and needlessly) put itself in a position to have to make.

The Postal Inspection Service is responsible for protecting the U.S. Mail with the police power of the United States. The Postal Inspection Service's work ensures the legality, and therefore, the safety, of what is transported through the mails. It further serves as a deterrent to criminal use of the mails. But the Postal Inspector's involvement in the Agreement is between Scylla and Charybdis. If the Postal Inspection Service is not involved, it effectively will be ceding its obligation to provide police protection to a private company. If the Postal Inspection Service is involved, does that confer Federal police protection - and thus an unprecedented competitive advantage - on FedEx? FedEx will be using the same facilities, planes, tracking equipment and personnel for its own packages and for the Post Office's. It would seem difficult to isolate.

This is why the Agreement was unfairly awarded to FedEx:

The Post Office is obligated - except in rare circumstances - to solicit bids on contracts worth over $10,000. The principle of competitive bidding, of course, is central to the transparency, integrity and cost-effectiveness of government agencies.

For this Agreement, the largest in the Post Office's history, it did not solicit bids. Instead, it claimed that only one company could provide the services it needed, and therefore there was no requirement to seek competitive bids, or even to give notice to potential competitors.

One of the flaws in the Post Office's logic, however, is that even FedEx was not, at the time negotiations began, capable of providing the services which the Post Office claimed it needed. FedEx and the Post Office began discussions on the Agreement in August, 2000. The Agreement was signed in January 2001 and FedEx has $100 million and until August 2001 to prepare to perform under the contract. To undertake the massive workload contemplated, FedEx plans many new hires and expansion of certain routes. Thus, FedEx was

basically given a one year exclusive opportunity to conform to the requirements of the Contract in derogation of the principle of competitive bidding. Had the regional carriers been given a year, they may have been able to - as FedEx did - undertake new hires or expansion or even merge in order to competitively bid on the contract.

As a matter of principle, the single largest contract ever awarded by the Post Office should have been awarded in the course of the transparent, pro-competitive process of bidding.

Now, the Post Office claims that competitive bidding was unnecessary because of the extraordinary benefits it will receive, including substantial cost savings and the efficiency of a single network. Neither of these reasons justifies the Agreement.

First, those of us in the industry seriously doubt that there is a real cost savings associated with the Agreement. I, for one, believe that if Evergreen were given a chance to bid, we would be able to provide the Post Office with a significantly less expensive option, an option that would increase, rather than decrease competition, would improve rather than aggravate the Postal Service's financial woes, and would continue to diversify the risks both to the Post Office and to the American people.

Second, the efficiency of a single network comes at too high a price. The existing system of several different data systems is a stop-gap against the failure of the next data system. While the logistics of transfer of the mail is not seamless in the current system, that system is insurance and protection against the failure of the network as a whole. Also, the current system keeps competition healthy by spreading the Post Office's significant fiscal outlays among many competitors.

Finally, a broader vision should take issue with the Post Office's commitment to profit to the exclusion of every other value. The Post Office is not a corporation, it is an arm of the Government. As the courts have said: "It is the right and duty of the government to conduct [postal services] for the interest of all."

I fervently hope that this Government - this Committee - will protect the public by closely scrutinizing and questioning this Agreement and the process that led to it.

Thank you for your time and interest.

Statement of
Karla W. Corcoran, Inspector General
United States Postal Service
Before the
House Committee on Government Reform
April 4, 2001

Chairman Burton and Members of the Committee, on behalf of the Office of Inspector General (OIG), United States Postal Service, I am pleased to submit this written statement concerning actions the Postal Service can take to improve its performance, accountability, and financial position.

As a result of the efforts of the House Committee on Government Reform, and in particular the leadership of Representative John McHugh, Congress created an independent OIG for the Postal Service in 1996. I am the first independent Inspector General for the Postal Service under the Inspector General Act and have held this position since January 1997.

As you know, under the Inspector General Act, my office conducts independent audits, reviews, and investigations of postal programs and operations. Therefore, we are uniquely situated to bring to Congress and Postal Service stakeholders an independent assessment of postal operations because we are knowledgeable of postal operations but do not report to Postal Service management and are not under their control.

This statement brings to your attention some of the issues regarding opportunities to improve critical management practices of the Postal Service, including contracting, budget and return on investment, labor management,

systems development, computer security and privacy, and strategic planning. In one review we identified almost $1 billion in cost avoidances over a 7 year period for a project to establish a nationwide toll-free response line. In another project, which is still in draft, we have potentially identified that outsourcing a major repair function would cost the Postal Service $1.1 billion more over a 10 year period than performing the function in-house. In addition, our other projects have identified almost $515 million in fines, recoveries, restitution, potential savings, and cost avoidances on postal operations over a number of years. Finally, we have identified $64 million in costs that could have been spent in a more appropriate manner.

We would like to note that the Postal Service has generally been receptive and responsive to issues we have brought to their attention over the last four years. Because of their willingness to address these issues, we are developing an effective working relationship.

The Postal Service is projecting a $2 to $3 billion loss this year and has indicated that a rate increase is needed along with reform flexibility in the areas of labor and operations, pricing, products, investments, and oversight. The Postal Service has indicated that the main reasons for this projected loss include reduced revenues from the Postal Rate Commission's decision, cost of living adjustments, and a continued soft economy. While we are in the process of assessing the reasonableness of this projected loss it is apparent that the Postal Service is facing significant financial challenges as evidenced by the deterioration in its current financial condition.

While the Committee is assessing the Postal Service's call for reform, the Postal Service must still address their critical management and financial practices. While progress has been made by the Postal Service in recent years to improve these practices, we believe that continued effort must be given to improving

performance and accountability throughout the Postal Service. Specifically, we believe:

- Contracting activities need proper control and oversight to prevent fraud, waste, abuse, and mismanagement;
- Performance data and financial information must be reliable for senior managers to make sound business decisions;
- Labor management and personnel practices must be improved;
- Mail processing systems must deliver;
- Computer security and privacy must preserve the customers' trust.; and
- Organizational structure and strategic planning must address the core mission.

Critical Management Practices

Although the Postal Service is seeking reform, we believe there are many improvements it can make today to strengthen its performance and improve efficiency. The following sections discuss the major issues that the Postal Service needs to address.

Contracting activities need proper control and oversight to prevent fraud, waste, abuse, and mismanagement

The Postal Service operates an $8 billion per year contracting program. We have found that the Postal Service has not always followed its own procurement policies or sound contracting principles. Over the last four years, our reviews

have disclosed that such contracting practices have resulted in $467 million in fraud, waste, abuse, mismanagement, and other recoveries on postal contracting programs.

As a result of our efforts and with the subsequent cooperation of Postal Service management, the Postal Service recovered over $12 million from a major telecommunications contractor and can avoid an additional $58 million in erroneous billings. Because the Postal Service did not adequately monitor contractor performance, it was repeatedly billed for work that was not performed and for substandard work. Postal Service management is reviewing all future bills to ensure correct billings, which should result in future savings.

In another recent case, a married couple who were Postal Service employees defrauded the Postal Service of more than $3 million because internal controls were ineffective. One spouse approved nonexistent purchases submitted by the other. The couple then fled to Venezuela with the proceeds and converted the stolen money into foreign investments, jewelry, and real property. Both employees were caught, returned to the United States, and convicted. As part of their sentence, the couple was ordered to repay over $3 million. Forfeiture actions to recover the money are currently underway. In order to prevent such frauds in the future, the Postal Service needs to ensure that appropriate internal controls exist and are enforced and that systems and data are available to validate contractor charges for services rendered, or work performed.

The Postal Service awards millions of dollars annually in cost reimbursement contracts. Our work has shown the Postal Service has not always reviewed and approved its contractors' cost accounting systems prior to the award of cost reimbursement contracts. This impairs the Postal Service's ability to effectively review contractor billings, creates the potential for billing frauds and may result in excess charges to the Postal Service.

For example, we identified significant deficiencies in a major contractor's estimating system and concluded that the Postal Service could not rely upon any of the contractor's proposed costs. This contractor has received more than $1 billion in postal contracts to date. Reliance on this system could result in the Postal Service paying for costs that are not associated with postal work. To date, we have questioned $37 million in proposed costs from this contractor, and our work on reviewing other contracts is continuing.

On numerous occasions we have found situations where contractors were improperly involved in writing their own contracts. For example, in one case a contractor was allowed to establish the Postal Service's contract requirements. The contractor then received a series of sole source contracts, valued in excess of $300 million, to provide these requirements. Under federal government contracting regulations this conduct would be specifically prohibited; however, under postal policies this is not specifically prohibited. We determined that if these contracts had been competitively bid, the Postal Service could have saved $53 million.

We have also identified repeated examples of contractors providing multi-million dollar services without a formal contracting agreement. The Postal Service has used "letter contracts" and "strategic alliance agreements" which do not contain adequate provisions to protect the interests of the Postal Service. The use of strategic alliances in the Postal Service is a growing practice, particularly in its electronic business initiatives. For example, in one major electronic commerce initiative, the Postal Service entered into a long-term relationship with a contractor to provide new electronic commerce services. The contract did not fully address computer security, privacy of Postal Service customer information, and audit rights. One clause that was included could have restricted the right of the Postal Service to investigate criminal activity relating to the contract. Although these deficiencies were brought to Postal Service management's

attention almost one year ago, the contract still has not been amended to address these issues.

Our work further identified instances where contract management could be improved to support contracting decisions and the review of contractor billings. We have identified many instances where there was not adequate information available to support payments to contractors. We also determined that quality assurance procedures and training of Postal Service contracting officials needed to be strengthened to properly monitor work performed by contractors. For example, in one investigation we determined that the Postal Service paid over $800,000 for asbestos abatement work that was either over billed or not performed. As a result of our investigation, Postal Service management ensured that the work was completed, initiated actions to obtain refunds for all over billings, and ensured that the contractor reimbursed the additional costs that were incurred by the Postal Service.

Another example of poor controls deals with inadequate monitoring of contractor performance. In one case that we are still reviewing, a contractor was responsible for reporting performance information on a major 10 year, $3.6 billion equipment network. As part of its responsibilities, the contractor reported on its own performance as well as prepared and verified its own invoices. In our opinion, approving contractor bill payment is an inherently postal function that should not be delegated to a contractor. Furthermore, under no circumstances should a contractor be allowed to approve its own bills for payment. Management recently received our draft report and has yet to respond.

Finally, we note that the Postal Service is exempt from standard federal contracting rules to enable it to realize greater efficiency and operate in a more business-like manner. As demonstrated in the examples above, our reviews of postal contracting practices suggest that although the Postal Service has realized some efficiencies, they have also weakened important internal controls. We

believe that while a strict adherence to federal contracting regulations is not needed, there is a clear need to strengthen internal controls throughout all postal contracts. These controls are the Postal Service's first line of defense against fraud, waste, abuse, and mismanagement.

Performance data and financial information must be reliable for senior managers to make sound business decisions

During some of our reviews, we found that Postal Service officials did not always effectively plan, control, and allocate organizational resources to invest in and support the Postal Service's goals. Further, we found that the Postal Service could improve its estimates for return on investments so that they can be achieved and supported. The Postal Service is a $65 billion business and must require that timely and accurate information be provided to senior managers for making informed business decisions. While we recognize the challenge in managing a budget of this size, Postal Service management can more effectively control and address its projected budget shortfall with accurate information to support budget estimates

In our review of the process used to manage the Postal Service Headquarters' $4.1 billion budget, we noted that 50 of the 100 program budgets that comprise this figure were not based on current or complete studies and analyses to ensure that program funding requirements were appropriate. Therefore, Postal Service officials could not be assured that the programs were appropriately staffed and funded and that cuts may have a long term detrimental effect on other aspects of the program, including revenue.

The Postal Service tracks expenses when paid, but it does not track expenses that have been incurred but not paid. While we have been told that this does not affect the overall postal budget because the major expenses are salaries and benefits, it is very significant at the program level. At this level, other expenses,

such as contracts, travel, and goods and services, are of major concern. Vice presidents and program managers have expressed concerns to us regarding the inability to monitor expenses on a timely basis. In addition, without this information, it is difficult for them to effectively develop, justify, and defend program budgets.

The Postal Service uses a detailed process to justify and analyze the cost/benefits of projects over $5 million for major equipment programs and facilities. In work that we have performed over the last four years, we have noted that for many projects management presented programs for approval without adequate documentation and analysis. We have recently completed a comprehensive review of this process in which we evaluated the methods used by the Postal Service to validate and monitor this annual expenditure of several billion dollars. We are also reviewing performance measurements to determine whether they are complete and reported timely to senior Postal Service managers. These measures will allow managers to track subsequent program performance and adjust funding in order to assure that Postal Service funds are justified, cost effective, or beneficial to their operations.

The Postal Service uses return on investment to determine the economic viability and cost benefits of its programs. We continue to question some of the Postal Service's return on investment projections because they do not always possess the data to make these projections. Lack of accurate data could have a direct impact on postal income projections.

For example, we have looked at return on investment on numerous postal projects. In each of these reviews we believe that Postal Service management could have used more reliable and complete data. In one instance, a $500 million automation project for 23 sites was projected to have a return on investment of approximately 5 percent. However, our analysis showed that the return on investment at the time of approval should have been almost a negative

9 percent. Therefore, the approval of this investment was based on inaccurate information.

In a draft report we previously discussed, we reviewed a program to repair postal equipment. The Postal Service estimated savings from the program to be $300 million over a 10 year period. Instead we found that the program, as deployed, may not result in the projected savings, but will result in costing the Postal Service $1.1 billion more over the 10 year life of the program.

We are also concerned that the Postal Service has entered into a number of agreements whereby the Postal Service is guaranteeing revenue to their business partners. The Postal Service assumes the risk in the venture, even though it does not know what the revenue will be.

For example, in one recent agreement the Postal Service provided an annual revenue guarantee over the 10 year life of the contract, even though the Postal Service has little or no experience in this area. To date, in an ongoing review, we have not been able to verify how the revenue guarantees were derived, but the amount of revenue being guaranteed appeared to us to be unrealistic. Further, the Postal Service has not yet been able to provide sufficient information to justify the revenue guarantee. Furthermore, in the year since this program commenced, the Postal Service told us that revenues from the program have been below their original projections. The Postal Service is currently revising their projections based on the economic slowdown.

Labor management and personnel practices need to be improved

Controlling personnel costs is imperative to the Postal Service because these costs account for over three quarters of its operating budget. Labor management relations are significant to the viability of the Postal Service. Poor labor management relations can have a negative impact upon employee morale and

productivity. Our work has shown that the Postal Service has had difficulty in labor management relations and we believe there are opportunities for cost savings.

One of the concerns that has continued to get media, congressional, and employee attention is the Postal Service's pay for performance program, which covers 84,000 employees. We reviewed this program and questioned whether the Postal Service should be making payments under the program at the same time it was requesting a rate increase, considering a reduction in workforce, and projecting a net profit, which was less than the projected payout. Since then, we have learned that the actual payments were $197 million at the same time the Postal Service lost $199 million.

The Postal Service justifies the pay for performance program, stating that productivity improvements are driven by this program and are promised at the beginning of the year before knowledge of actual profit or loss is known. In addition, the Postal Service believes that without this program they would not have achieved their reported record productivity improvements. We are continuing to review this program to determine whether it actually enhances productivity.

As part of their efforts to improve working conditions, the Postal Service commissioned a study on violence in the workplace. The study concluded that although employees believed they were at greater risk to be a victim of workplace violence than the average worker in the United States, actual results did not support this belief. The Postal Service has acknowledged these concerns, and continues to take actions to address these issues, such as the improvement of their threat assessment capability and ensuring that managers are accountable in this area. In addition, they have established a workplace environment improvement program to enhance working conditions.

However, we continue to receive allegations from employees who believe they have been harassed, intimidated, and subjected to violence. We continue to find this troublesome and believe it has a potential impact upon the financial profitability of the Postal Service because of increased grievances, Equal Employment Opportunity (EEO) complaints, work slowdowns, and morale issues.

Recently, we issued four audit reports documenting employee allegations that certain Postal Service managers at facilities in New Jersey, California, South Carolina, and Alaska have utilized intimidation, harassment, and abusive management practices. In one of these cases, during our interview with the manager, he played with an empty .38 caliber shell casing. In response to these reports, the Postal Service has taken steps at these facilities to improve the work environment by conducting climate assessments and initiating joint labor-management meetings.

The full cost of these problems to the Postal Service is difficult to assess. For example, the Postal Service is unable to provide the cost of processing the 126,000 grievance and arbitration cases currently pending. While the Postal Service has developed a new grievance tracking system, it does not track cost. Knowing how much these employee related problems are costing the Postal Service – and it could be in the millions of dollars – might give management more of an incentive to correct this situation.

The Postal Service has announced that with the projected loss, there could potentially be office closings and reductions in force. These events can be traumatic to employees and may increase workplace tension. The Postal Service needs to be able to react to any workplace incident that may arise from this tension. We note that the Postal Service has recently closed 23 out of 55 remote encoding facilities, primarily staffed by contractors, without adverse incidents.

Recently, we completed audits of 26 Postal Service districts' violence prevention and response programs. These reviews disclosed that the Postal Service effectively responded to violent situations. However, they need to proactively follow threat assessment procedures to prevent workplace violence. If such situations would erupt, the potential financial liability could be substantial. Further, even though the Postal Service is taking cost cutting measures, reductions in this area would be inappropriate.

In the area of workplace safety, the Postal Service has potential liability in terms of:

- Substantial fines from the Occupational Safety and Health Administration, including treble damages if the violation is determined to be willful. Furthermore, significant violations have the potential for shutting down postal facilities.

- Workers' compensation claims, potential lost workdays of Postal Service workers, and claims for workplace injuries by Postal Service contractors and customers.

For example, in one review we found that Postal Service management did not ensure that appropriate action was taken to correct safety violations and safeguard employees. We were told that these unsafe conditions were not corrected due to concerns that repairs could cause mail delays.

Individual Postal Service managers have direct authority over large sums of money and resources, and when not judiciously administered, this authority may result in abuse, affect the public's trust in the Postal Service, and depress employee morale. The following are examples where incidents occurred. In each case, Postal Service management took corrective action.

- A review of an EEO settlement agreement revealed that Postal Service managers have the authority to settle EEO complaints against themselves. In one example, a former vice president approved a settlement of $52,000 where he was the alleged discriminating official.

- Our reviews of relocation payments questioned the payment for employee moves of less than 20 miles when there appeared to be no benefit to the Postal Service. We identified over $240,000 in relocation expenses paid to two senior Postal Service officials for local moves, without full disclosure to the Board of Governors.

- We found some executives misused official vehicles and used Postal Service employees as chauffeurs for prolonged periods of time throughout the Postal Service. This occurred because controls over the vehicles were either inadequate or nonexistent. Specifically, we found over 520 instances (460 instances by one individual), involving nine executives, where inappropriate use took place. However, we could not determine the full extent of the misuse because of the lack of documentation.

Mail processing systems must deliver

Since 1998, the Postal Service has deployed $3.2 billion in automated mail processing equipment. We recognize that the Postal Service has been a leader in implementing and integrating automated mail processing equipment. While we support their initiatives to improve automation we believe it is imperative that the Postal Service ensures that the technology works as intended and that their investments are sound. We reviewed $1.2 billion of this deployed equipment and identified instances of defects and immature technology. This condition existed because the Postal Service does not always follow their process for ensuring projects are developed on time, within budget, according to requirements, and with expected benefits.

Numerous systems we reviewed have contained defects and immature technology. Because of these problems, the Postal Service often lowers the performance requirements in order to justify deployment. In most cases, Postal Service management then relies upon manual labor to supplement the performance shortfalls of these systems, which contradicts the original premise for automated equipment investments. The following are examples of postal systems and the issues that existed at the time of deployment, and at the time of our reviews. Postal Service management recently informed us that these issues have been addressed. We will verify this information as time permits.

For example, the Postal Service expended $81 million on a mail processing automation project that was intended to process 15 mail trays per minute. When the equipment was deployed, the actual performance was only 10 mail trays per minute. Despite this reduced capability, Postal Service management chose to deploy the system without assessing the negative impact on the original savings used to justify the approval of this automation project. Therefore, it is unclear whether the Postal Service will achieve the anticipated savings on this project.

We reviewed another automation project originally intended to provide mail transport equipment at 42 postal sites, at a projected cost of $500 million. However, because of a lack of reliable cost and performance information, $500 million will only provide for deployment at 23 sites. Furthermore, the deployment has been delayed by a year. In addition, we identified at least $27.9 million more in program costs than originally projected.

After reviewing a $38 million robotics automation program, we determined the Postal Service was not capturing performance data to assess the effectiveness of the program. Without this data, Postal Service management could not accurately determine what, if any, return on investment was achieved. In addition, only 73 of the 102 units purchased were installed, and 9 were

subsequently removed by the receiving facilities. These 9 facilities determined, after deployment, that the units were of limited productivity and usefulness.

Finally, we reviewed a new $495 million system to replace existing retail systems at post offices. At the time of project approval, the system was designed to capture detailed retail transaction information. However, we determined the system was not performing as originally required. As a result, Postal Service managers were not able to fully assess performance problems, identify issues to improve systems operations, or determine future training needs.

Computer security and privacy must preserve the customers' trust

In order to maintain the public's trust in the Postal Service, the security of its computers and the privacy of the information they contain must be ensured. This is particularly important in the electronic commerce area, where major private providers have been victimized by attacks upon critical computer systems, and by the theft of customers' sensitive personal information. A breach in computer security could paralyze mail operations and result in a loss of revenue through the compromise of the Postal Service's electronic commerce operations. Risks in this area could increase exponentially as a result of the Postal Service's recently announced initiative to allow all Postal Service employees to connect to the postal network from home.

Recently, we led an international team of investigators in convicting a group of hackers that attacked computer systems, including a postal system, throughout the United States and Canada. The team is continuing to investigate other hacker attacks against postal systems originating from inside and outside of the Postal Service. The Postal Service has been very cooperative in our investigations by identifying potential attacks and working with our office to resolve security incidents. We have also commenced a program to conduct penetration testing of computers throughout the Postal Service and, working with

Postal Service management, have identified weaknesses in various systems that could, if not corrected, compromise Postal networks.

We are aware that computer security is a major congressional priority. Last year, based upon the work of this Committee, Congress passed the Government Information Security Reform Act to improve government computer security. The Postal Service has concluded, and we agree, that this Act does not apply to postal computer operations. However, our audit and investigative work has determined that the Postal Service does not meet the best practices recommended by the Act and that a comprehensive computer security program is needed to protect critical systems, postal operations, and electronic business initiatives. In response to our activities, the Postal Service has agreed to improve computer security.

One of the main concerns in electronic commerce today is the preservation of personal privacy and the continued availability of Internet services. The Postal Service has commenced an aggressive campaign to provide a variety of electronic commerce services, including selling postal products on-line and providing electronic services. We recognize that electronic commerce presents major challenges and we, as well as the Postal Service, agree that security and privacy concerns are paramount.

However, we have identified several security and privacy concerns in these areas that we have discussed with Postal Service management, including their protection of information and disaster recovery. We are not disclosing the details of these reports in this statement but would be happy to discuss them in private with the Committee. We commend the Postal Service for recently appointing a Chief Privacy Officer and Chief Information Security Officer which will focus Postal Service management's efforts in these important areas.

We remain concerned that recent electronic business agreements with contractors and other business partners may have an adverse impact on postal computer security. Such agreements must contain language that will ensure postal computer security and privacy are not compromised. We have recommended that the Postal Service develop standard procedures to ensure that postal computer security and privacy are protected whenever there is connectivity between postal computers and the computers of their business partners. A breach in computer security in this area could result in theft of valuable information, jeopardize relationships with Postal Service business partners and customers, and result in a loss of revenue.

Organizational structure and strategic planning must address the core mission

In numerous reviews of postal programs, we have identified organizational issues such as fragmentation, decentralization, and a need for better focus, which affect the Postal Service's ability to control its costs and improve performance. An organization of the Postal Service's size, i.e., over 900,000 employees and 38,000 facilities, requires an efficient organizational structure that utilizes efficient business practices.

The following are examples of how decentralization and fragmentation affects the efficiency of the Postal Service:

- In one audit we found that the Postal Service deployed a $38 million automated system to process mail trays to reduce operating expenses. The systems were poorly planned and did not include all needed components. Because the decision to use the equipment after installation was not centralized, some managers who originally requested the system, unilaterally decided to remove the equipment and place it in storage. While on the one hand we understand managers not wanting ineffective

systems, on the other hand, the Postal Service has invested in this technology, much of which is now in storage or has been dismantled.

- The Postal Service incurred $23 million in repair expenses for a northwestern facility, originally purchased for almost $27 million. Postal Service management requested that we determine why this occurred. We found that because the decision to waive procurement requirements was decentralized, a Postal Service manager was able to bypass safeguards requiring a detailed engineering study prior to the purchase, which should have detected the building defects.

- We reviewed a revenue protection program and found that because the responsibility for the program was fragmented between Finance, Marketing, and area and district finance managers, each with a different focus, deficiencies were not prevented through early detection. Because of this lack of focus and fragmentation, we found that mailers perceived that they had been treated unfairly by the Postal Service. This process was an important tool for protecting postal monies and ensuring postage due the Postal Service was paid and expenditures for collection activities reduced.

Conclusion

In conclusion, while we believe that the Postal Service needs to improve in the areas noted above, we also recognize the challenge the Postal Service faces and applaud their efforts to meet this challenge. Specifically, we have noted that the Postal Service:

- Is aggressively seeking new technologies and business innovations to continue its role as a world leader in the delivery of communications and logistics services;

- Has recognized technology and has employed it in areas such as travel, contracts, and other areas to improve timeliness and efficiency;

- Has improved their threat assessment program and ensured that managers are accountable for these programs;

- Has identified automation initiatives as a way to control labor and workers' compensation costs;

- Has made a concerted effort to improve computer security, including appointing a chief information security officer and chief privacy officer; developing a comprehensive strategy to tighten computer and Internet security; and creating a computer emergency response team; and

- Has recognized at the highest levels the impact of technology on its core business processes and undertaken a concerted effort to redefine its mission into the 21st century and beyond.

We believe that in addition to these efforts, the Postal Service must continually reexamine its mission, core business functions, and fundamental management practices. The Postal Service should also seek appropriate guidance from Congress on its mission and core business functions. The independent oversight provided by Congress and the OIG will continue to assist the Postal Service as they make decisions in these challenging times. In our view, in order to ensure the success of future Postal Service operations, Congress and Postal Service management need to address these issues.

THE U.S. POSTAL SERVICE'S UNCERTAIN FINANCIAL OUTLOOK, PART II

WEDNESDAY, MAY 16, 2001

HOUSE OF REPRESENTATIVES,
COMMITTEE ON GOVERNMENT REFORM,
Washington, DC.

The committee met, pursuant to recess, at 10 a.m., in room 2154, Rayburn House Office Building, Hon. Dan Burton (chairman of the committee) presiding.

Present: Representatives Burton, Gilman, Morella, Shays, McHugh, LaTourette, Barr, JoAnn Davis of Virginia, Otter, Schrock, Waxman, Owens, Mink, Norton, Kucinich, Davis of Illinois, Tierney, and Clay.

Staff present: Kevin Binger, staff director; Daniel R. Moll, deputy staff director; David A. Kass, deputy chief counsel; Mark Corallo, director of communications; John Callender, counsel; S. Elizabeth Clay, professional staff member; Sarah Anderson and Scott Fagan, staff assistants; Robert A. Briggs, chief clerk; Robin Butler, office manager; Josie Duckett, deputy communications director; Leneal Scott, computer systems manager; John Sare, deputy chief clerk; Corinne Zaccaagnini, systems administrator; Phil Barnett, minority chief counsel; Denise Wilson, minority professional staff member; Ellen Rayner, minority chief clerk; and Jean Gosa and Earley Green, minority assistant clerks.

Mr. BURTON. Good morning. A quorum being present, the committee will come to order.

I ask unanimous consent that all Members' and witnesses' opening statements be included in the record. And without objection, so ordered.

I would also like to ask, we have some people who would have liked to testify today, that are not testifying. They have some statements that they would like to include in the record. And without any objection, we would like to include their statements in the record. So, without objection, we will put those in the record as well.

I ask unanimous consent that all articles, exhibits, or extraneous or tabular material referred to be included in the record. Without objection, so ordered.

I have been advised that we are going to have a vote in a few minutes. So what we are going to do is we are going to have Mr. Waxman, Mr. Waxman has to meet with the leadership on the Democrat side, so we are going to have him give his opening statement and then we will let him go. We will then recess until we

have the vote and then we will come back. I apologize for the delay but it is not me calling this vote.

I will now yield to Mr. Waxman for an opening statement. I will reserve my time until we come back after the vote.

Mr. Waxman.

Mr. WAXMAN. Thank you very much, Mr. Chairman, for allowing me to make my opening statement first. Because I have a conflict, I will have to leave in a minute. I will try to get back to the hearing, but if not, I will certainly review the record.

Today, we begin part II of oversight hearings on the U.S. Postal Service's uncertain financial outlook. I want to begin by commending Chairman Burton for his continued commitment to postal issues. The financial status of the Postal Service is an important matter deserving of our time and focus. The impact of recent postal rate increases on mail volume and postal revenue is an important subject and one that we will vigorously discuss today.

Much has taken place since our first hearing on April 4th. Two days after our hearing, Senator Harkin introduced S. 71, a resolution expressing the sense of the Senate that 6 day mail delivery should not be reduced. Tomorrow, Representative Danny K. Davis, chairman of the Congressional Postal Caucus, will introduce a companion House Resolution. I urge my colleagues to lend their support to this measure.

Two weeks after our first hearing, the Coalition to Preserve Universal Mail Service presented an outline of a legislative approach to address the financial crisis facing the Postal Service. We will be able to explore the matter of reform further since many of the Coalition members are present today.

On May 7, the Postal Board of Governors voted to implement a new postal rate schedule. Under this schedule, rates for a 1 ounce, first-class letter stay at 34 cents, and an additional ounce will cost 23 cents. The cost for postcards will increase 1 cent, and rates will also increase for express mail, certified mail, and domestic money orders.

On Monday the Mailers Council unveiled its first quarterly report card on the Postal Service. The grades reflect the Postal Service productivity in six categories, ranging from retail services to revenue per work hour. This performance tool will be issued quarterly and is designed to help the Postal Service achieve greater productivity. And late yesterday the Postal Board of Governors released a series of principles to guide postal reform.

I look forward to working with the chairman and members of the postal community as we discuss the actions needed to improve postal management and finances. I want to welcome all of today's witnesses. In particular, I am glad to see that Congresswoman Pat Schroeder, who served in the U.S. House of Representatives from 1972 until 1996, will testify today. Among her many accomplishments, Representative Schroeder served on the Committee on Post Office and Civil Service, so she is clearly no stranger to postal issues or postal finances.

Mr. Chairman, I look forward to working with you. I will certainly get the record of all the witnesses. Those I am not able to hear personally, I will have a chance to get their testimony. Thank you.

[The prepared statement of Hon. Henry A. Waxman follows:]

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BERNARD SANDERS, VERMONT,
INDEPENDENT

Statement of
Representative Henry A. Waxman
May 16, 2001

Mr. Chairman, today we begin part two of oversight hearings on the "U.S. Postal Service's Uncertain Financial Outlook."

I want to begin by commending Chairman Burton for his continued commitment to postal issues. The financial status of the Postal Service is an important matter, deserving of our time and focus. The impact of recent postal rate increases on mail volume and postal revenue is an important subject and one that we will vigorously discuss today.

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Mr. BURTON. Thank you, Mr. Waxman.

I think we will go ahead and proceed with opening statements until we are called to the floor. That way we can expedite some of the things that need to be done.

We received, as Henry alluded to, a letter from the Postal Board of Governors, and, although we have not yet reviewed that, since we want to have everybody on the same page, I think we will make available to all the interested parties the recommendations of the Board of Governors as far as postal reform is concerned. This is a letter that was dated May 15. We just received it this morning. So we are making 100 copies and will have those for anybody who is interested. If we run out of copies, we will get some more. The reason we want to do that is we want to make sure that you understand what they are recommending and we want to get input from everybody so that we can come up with the best possible solution to the problem.

At our first hearing on this issue held last month, we heard from a number of distinguished witnesses, including the Postmaster General, the Comptroller General, and members of the Postal Board of Governors. Postmaster General Henderson discussed the agency's gloomy financial forecast and projected losses of more than $2 billion, and some believe as high as $3 billion, this year. The independent and nonpartisan General Accounting Office reported that the financial, operational, and work force challenges facing the Postal Service are so severe that the GAO added the agency's need to address these challenges to its "High Risk" list. I think just yesterday Senator Thompson in the Senate mentioned how important this issue is, because it is now one of the highest risk areas of the Government. The Board of Governors stressed the need for postal reform, and also discussed steps taken in recent weeks to address problems facing the agency.

I want to say, Representative Davis, I will be glad to cosponsor your resolution on the 6 day mail delivery not being changed. So put me on, if you would.

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

Mr. BURTON. The Board suspended capital construction projects, ordered a study of 5 day mail delivery, and directed the Postal Service to prepare for a new rate case.

Since the hearing, the Board announced that it was going to raise rates effective July 1. In announcing the new rates, the Board took the unusual step of overturning the Postal Rate Commission. In fact, this is I believe only the second time since the enactment of the Postal Reorganization Act in 1970 that the Board has overruled the Postal Rate Commission and raised rates. We are disappointed that happened. I talked to the Board of Governors yesterday and will be meeting with them next week to talk about what the future prospects are for additional rate increases. I think we need to solve this problem with a minimal impact on the American people and the people who are doing mailing, and a lot of you are here today.

Prior to the Board's announcement, several Members of Congress, including myself, Congressman McHugh, and both the House and Senate Majority Leaders, contacted the chairman of the Board of Governors urging them not to raise rates. But they did not pay

much attention to us. So we are going to have another meeting with them to see if we cannot have a little more input.

I am very concerned about the July rate increase. I am also concerned about reports of another more substantial rate filing being proposed for later this year. The impact of these increases on businesses and consumers can be devastating. The increases are a temporary solution to a long-term problem. They could also have the unintended consequences of driving postal business away. Rate increases could force some mailers to seek alternatives or cause them to close down entirely. Other mailers will pass the additional cost on to consumers resulting in higher prices for products being shipped through the mail. And if we have a rate increase on first class mail as well, then it is going to be inflationary because it is going to hit everybody.

Today we will learn how the Postal Service's dismal financial forecast is impacting postal stakeholders, including the mailing community and the postal work force. The Postal Service is a massive bureaucracy. With about 900,000 employees, the Postal Service has the second largest work force of any company in the United States. I think the only one bigger is Wal-Mart. Labor costs account for almost 80 percent of the agency's budget. The GAO has reported that over the next decade about half of the postal work force will be eligible to retire. The departure of these dedicated professionals will leave a void in terms of knowledge and experience. However, their departure also provides the agency with an opportunity to restructure and refocus its massive work force.

Challenges facing the postal community, including mailers and the postal work force, illustrate the need for comprehensive postal reform. We must work on a bipartisan basis to produce meaningful legislation that will ensure universal mail service at affordable prices for all Americans. We recently sent a letter to the President requesting the assistance of the White House on this issue. I have also discussed the need for postal reform with the Secretary of Commerce, Don Evans.

The postal issue is such a big issue it will affect every segment of our society. It is an issue that has not yet been raised with the administration, but we are going to make sure that everybody over there is made aware of it as quickly as possible so that we can have the assistance of the White House in putting pressure on all interested parties to get a solution passed by the Congress. We have a great opportunity to reform the Postal Service. We have the attention of all the stakeholders, including the mailers and the postal employees, management and the American people.

We have with us today a number of distinguished witnesses. On the first panel, we have representatives of the mailing industry. Our lead off witness on the panel is former Congresswoman Pat Schroeder. Pat was a member of the Post Office and Civil Service Committee and she is now president and CEO of the Association of American Publishers. On panel II we will hear from postal employee union representatives. I will look forward to hearing from all of you in just a few minutes.

[The prepared statement of Hon. Dan Burton follows:]

Statement of Dan Burton (R-IN), Chairman
Committee on Government Reform
Hearing on the "U.S. Postal Service's Uncertain Financial Outlook, Part II"
Wednesday, May 16, 2001

Good morning and welcome to today's hearing of the Government Reform Committee. This is the Committee's second hearing this Congress to examine the financial problems facing the U.S. Postal Service.

At our first hearing on this issue, held last month, we heard from a number of distinguished witnesses including the Postmaster General, the Comptroller General, and members of the Postal Board of Governors.

Postmaster General Henderson discussed the agency's gloomy financial forecast and projected losses of more than $2 billion this year. The independent and nonpartisan General Accounting Office reported that the financial, operational and workforce challenges facing the Postal Service are so severe that the GAO added the agency's need to address these challenges to its "High-Risk" list.

The Board of Governors stressed the need for postal reform and also discussed steps taken in recent weeks to address problems facing the agency.

The Board suspended capital construction projects, ordered a study of five-day mail delivery, and directed the Postal Service to prepare for a new rate case.

Since the hearing, the Board announced that it was going to raise rates effective July 1. In announcing the new rates, the Board took the unusual step of overturning the Postal Rate Commission. In fact, this is only the second time since the enactment of the Postal Reorganization Act in 1971 that the Board has overruled the Postal Rate Commission and raised rates.

Prior to the Board's announcement, several Members of Congress including myself, Congressman McHugh, and both the House and Senate Majority Leaders contacted the Chairman of the Board of Governors urging them not to raise rates.

I am very concerned about the July rate increase. I am also concerned about reports of another more substantial rate filing being proposed for later this year. The impact of these increases on businesses and consumers can be devastating. These increases are a temporary solution to a long-term problem.

They could also have the unintended consequence of driving postal business away. Rate increases could force some mailers to seek alternatives or cause them to close down entirely.

Other mailers will pass the additional costs on to consumers resulting in higher prices for products shipped through the mail.

Today we will learn how the Postal Service's dismal financial forecast is impacting Postal stakeholders, including the mailing community and the postal workforce.

The Postal Service is a massive bureaucracy. With about 900,000 employees, the Postal Service has the second largest workforce of any company in the United States. Labor costs account for almost eighty percent of the agency's budget.

The GAO has reported that over the next decade, about half of the postal workforce will be eligible to retire. The departure of these dedicated professionals will leave a void in terms of knowledge and experience. However their departure also provides the agency with an opportunity to restructure and refocus its massive workforce.

Challenges facing the postal community, including mailers and the postal workforce, illustrate the need for comprehensive postal reform.

We must work on a bipartisan basis to produce meaningful legislation that will ensure universal mail service at affordable prices for all Americans. I recently sent a letter to the President requesting the assistance of the White House on this issue. I have also discussed the need for Postal reform with the Secretary of Commerce, Don Evans.

We have a great opportunity to reform the Postal Service. We have the attention of all of the stakeholders including the mailers, the postal employees, management and the American people.

We have with us today a number of distinguished witnesses. On our first panel we have representatives of the mailing industry.

Our leadoff witness on the first panel, former Congresswoman Pat Schroeder, was a member of the Post Office and Civil Service Committee. She is now the President and CEO of the Association of American Publishers.

On panel two we will hear from Postal employee union representatives. I welcome all of our witnesses and look forward to their testimony.

Mr. BURTON. Mr. Davis, if you want to make your opening statement before we run out of time; we still have 11½ minutes on the clock. So we will recognize you.

Mr. DAVIS OF ILLINOIS. Thank you very much, Mr. Chairman. I want to, first of all, thank you for your ongoing commitment to postal reform. I also want to thank you for calling this hearing today.

Last month, we had an opportunity to hear from the Postal Service Board of Governors and the General Accounting Office. At that hearing the witnesses painted a grim picture for the future of the Postal Service unless postal reform is enacted. In fact, Postmaster General Henderson suggested that the Postal Service is projected to have a budget shortfall of between $2 and $3 billion this fiscal year.

In an effort to cut costs, the Postal Service has frozen fiscal year 2001 postal facility projects. In Illinois alone, some 26 postal projects have been affected. Additionally, the Postal Service is also doing exploratory study on the idea of reducing mail delivery from 6 to 5 days. Of course, my constituents expect 6 day mail delivery. I am pleased, along with Representative John McHugh and Members of the Congressional Postal Caucus, to introduce bipartisan legislation tomorrow that will address the issue of 6 day mail delivery.

I am also honored that today we will have an opportunity to hear from other stakeholders, like the mailers, publishers, and postal unions. The recent action by the Board of Governors to increase postal rates by an average of 1.64 percent is sure to spark a lot of conversation. The action by the Board of Governors speaks volumes for the need to reform the current system. The increase which goes into effect July 1 is expected to generate an additional $975 million in revenue. However, we all know that this is no panacea.

In my congressional district alone, the Postal Service plays a vital role. Aside from the constitutional mandate of binding our Nation together through universal service, the Postal Service employs over 5,000 people, generates more than $25 million in Federal taxes and $5 million in State taxes. In addition, one of the biggest postal customers in the service is located in my district, R.R. Donnelley and Sons.

It is in the Nation's best interest to have a viable and stable Postal Service. We cannot guarantee stability and viability operating on rules that were written in 1970. We have moved into a more sophisticated and technologically based economy. Therefore, the rules of the road should reflect these advances in technology.

We have many challenges before us, Mr. Chairman, the energy crisis, the rise in fuel prices, labor-management issues, and the need for postal reform. However, I am confident that through your leadership and with the full cooperation of all of the Members of the Congress, with an executive branch that understands the problems that we are facing, with the motivated constituency, that we are going to be able to find a solution to these problems.

So I thank you again, Mr. Chairman, for convening this hearing. I welcome all of the witnesses and look forward to a rather productive day.

Mr. BURTON. We really appreciate your interest and input, Congressman Davis. I am looking forward to working with you to find a solution.

We have about 7 minutes on the clock. I think we will recess for the vote and then we will come back as quickly as possible to have final opening statements and hear from our witnesses. So we will be back in about 10 minutes.

[Recess.]

Mr. BURTON. The committee will be in session.

We heard from Mr. Waxman, Mr. Davis, and myself. We will now hear from Mr. Otter. You are recognized for 5 minutes.

Mr. OTTER. Thank you, Mr. Chairman. Let me associate myself with both your and the ranking member's remarks in welcoming our first and second panel today.

I want to draw your attention, prior to beginning my opening statement, to the stack of mail that is here that I received. It was 2 days mailing out of Idaho, and if we had not had 6 day mailing, I would not have gotten it in 11 days. But it all came from one little old town in Idaho and it is relative to the Postal Service.

For years the U.S. Postal Service management has touted that they favor a business-like approach. I applaud that philosophy. But if they are going to talk the talk, then they must walk the walk. We all benefit from the services of the Postal Service. But it must be held accountable. The Postal Service management cannot continue its practices of increasing rates on the consumer when the Postal Service's financial problems lie within its own organization—or perhaps inorganization.

It is not right to force and over-tax the American public to continue bailing out the Postal Service's $3 billion deficits. For too long the Postal Service has had the opportunity to reduce its debt. For example, on several occasions the Postal Service has had recommendations made to them on how to reduce cost. Several of these suggestions could be adopted now. For example, Price Waterhouse Cooper outlined proposals that would reduce the costs for the Postal Service by $500 million to $1 billion a year. However, even after paying the bill to Price Waterhouse Cooper, rather than heed their recommendations, the Postal Service has ignored them and refused to change.

The Postal Service has also built and maintained and annual advertising budget of hundreds of millions of dollars despite its monopoly on first class mail. This is a direct conflict for the American people to subsidize a Government agency to compete with our friends and neighbors in the private sector.

The new Postal Service rate increases brought on by the Postal Board of Governors, who voted unanimously to overrule the Postal Rate Commissioners' protests, are drastic increases for the Postal Service to impose on the Americans to make up for inefficiencies that are solely of its own making. It is unfortunate that men and women of the U.S. Postal Service are under a management team that has run this organization into financial chaos. The employees of the Postal Service deserve and should have better management, and so should the American people.

Mr. Chairman, it is time for the Postal Service to operate in a more business-like fashion. It faces financial pressures but the U.S.

Postal Service can, and must, cut costs, improve productivity, and become solvent rather than continuing to pass their financial woes onto an American public. Thank you, Mr. Chairman.

Mr. BURTON. Thank you, Mr. Otter.

Mr. Clay, do you have an opening statement?

Mr. CLAY. Good morning. I want to welcome the witnesses from both panels testifying today. I want to especially welcome former Congresswoman Patricia Schroeder. She gave many years of distinguished service to the House of Representatives.

Mr. Chairman, thank you for this second hearing on the U.S. Postal Service's uncertain financial outlook. The first hearing, held of April 4, 2001, provided insight into the planning and projections of the Postmaster General and the management of the U.S. Postal Service. Questions were also raised regarding the exceptionally large deficit projections for the current fiscal year.

The hearing today receives testimony provided by magazine publishers who, of course, are bulk mailers, and the testimony of representatives of those who do such a tremendous job of getting the mail delivered. Their testimony and ideas will be solicited on a range of issues. Among them are: the direction and impact of current postal reform, projected postal rate increases, labor-management relations, and the impact of these and additional issues on their respective organizations and on the country as a whole.

Mr. Chairman, I ask unanimous consent to submit my statement to the record. Thank you.

Mr. BURTON. Without objection, so ordered.

[The prepared statement of Hon. Wm. Lacy Clay follows:]

Wm Lacy Clay

Statement of the Honorable William Lacy Clay before the Committee on Government Reform

"The U.S. Postal Service's Uncertain Financial Outlook – Part Two"

Good Morning! I want to welcome the witnesses from both panels testifying today. I want to especially welcome former Congresswoman Patricia Schroeder. She gave many years of distinguished service to the House of Representatives.

Mr. Chairman, thank you for this second hearing on the "U.S. Postal Service's Uncertain Financial Outlook".

The first hearing, held on April 4, 2001, provided insight into the planning and projections of the Postmaster General and the management of the U.S. Postal Service. Questions were also raised regarding the exceptionally large deficit projections for the current fiscal year. The hearing today receives testimony provided by magazine publishers who, of course, are bulk-mailers and the testimony of

representatives of those who do such a tremendous job of getting the mail delivered.

Their testimony and ideas will be solicited on a range of issues. Among them are the direction and impact of current postal reform; projected postal rate increases; labor management relations; and the impact of these and additional issues on their respective organizations and on the country as a whole.

Mr. Chairman, I ask unanimous consent to submit my statement to the record.

Mr. BURTON. Mr. Gilman.

Mr. GILMAN. Thank you, Mr. Chairman. I want to commend you for conducting this hearing this morning, another in the series of our hearings on the Postal Service. I am pleased that the full committee is continuing to devote its time to the current issues facing our Postal Service. It is imperative that we examine all the factors leading up to the Postal Service's current financial projections.

At our April 4th hearing, the committee heard testimony from the Postmaster General reporting the Postal Service losses of $2 to $3 billion this fiscal year. Furthermore, on May 8th the Postal Board of Governors announced a postal rate increase. All of this combined leads to increased costs by mailers and places a work force of 900,000 employees in flux, all of which can eventually affect all of our constituents.

When I hear the Postal Service suggest that jobs may have to be cut in order to help control costs, we are all left to wonder how the Postal Service will maintain the core mission of universal service. As I noted at the last hearing, there are many reasons we can point out to answer how the Postal Service has found itself in these troubled waters—continued decline in volume, insufficient revenues, and electronic communication which they did not properly prepare for, as we looked at that years ago.

However, these factors have all been foreshadowed by this committee, and our colleague, Mr. McHugh, the gentleman from New York, while working diligently to bring postal reform before this committee, was not getting the kind of support that was needed. Accordingly, it is now time for this committee to fish or cut bait and to finally approve a reasonable postal reform measure. And that does not include just closing post offices.

Additionally, the Postal Service must also be prepared to take responsibility for the difficult economic times they now are experiencing. The Postal Service has known for some time the problems of inefficiency in its system which exist. Both the GAO and the Postal Service's IG have repeatedly testified before the Postal Subcommittee on the many difficulties the Postal Service has had in realizing opportunities of savings.

So we look forward to examining these issues. We look forward to examining ways to help our Postal Service get on a sound financial footing. Thank you, Mr. Chairman.

Mr. BURTON. Thank you, Mr. Gilman.

Mr. Cummings.

Mr. CUMMINGS. Thank you very much, Mr. Chairman. I am glad that we are holding this hearing on the Postal Service's current financial position, the impact of postal loss projections, and the impact on postal business and the postal work force.

At the April 4th hearing, GAO placed the Postal Service's transformation efforts on their "High Risk" list, so that Congress, GAO, and others can focus on the postal financial, operational, and human capital challenges. The Postal Service has projected a deficit of $3 billion. They have attributed the loss of revenue to e-mails, rising fuel costs, Government regulation, and e-commerce.

Mr. Chairman, there is widespread agreement that reform is needed for the Postal Service. I have received numerous calls and packages from my constituents regarding postal reform. In fact, I

just received a postal reform proposal yesterday from a small businessman in my district outlining a possible solution to the financial crisis at the U.S. Postal Service.

I agree with the Coalition to Preserve Universal Mail Service when they recommended that postal reform should project universal service at fair and reasonable prices. The Coalition further stated that the Postal Service should not submit a request for higher postal rates any time before 2002, nor should it impose service reductions on the American people.

We all want a strong and stable Postal Service. As such, this committee and Congress will continue to work with the Postal Service and others to develop a long-range strategic plan that truly assesses postal reform.

I look forward to the hearing and the testimony of our witnesses. I hope they will be able to help us examine postal losses in revenues, postal rate increases, deficit in mail volume projections, competition, information technology, and budget forecasting. I thank you.

Mr. BURTON. Thank you, Mr. Cummings.

Mr. McHugh.

Mr. MCHUGH. Mr. Chairman, let me echo the words of others in expressing my appreciation for your efforts here to bring what I think increasingly people are realizing is a very, very troubling state of affairs with respect to the U.S. Postal Service. I am sure most people are tired of hearing me talk about this issue. I know over the past 6 years I have grown weary of my voice. So, with your consent and the committee's, I would ask unanimous consent to enter my full statement into the record.

I would just say, Mr. Chairman, I spent some time yesterday and this morning reading the testimony and there is a great deal of talk about the issue of flexibility and the way in which certain provisions in the bill that we first worked on over the past 5 years now and others have proposed that the Postal Service be afforded some sort of flexibility. I would just say to the benefit, I hope, of some in this room, if the events over the past 2 weeks have not proven to people that the Postal Service today has ultimate flexibility, that the Postal Service today, for better or worse, has total unobstructed rights to set whatever rates they may choose to, I am afraid those people are beyond instruction.

We have to begin today, for the many interests that are represented in this room, particularly to the interests that Mr. Otter spoke about and the reading of his letter, the American people, the more than 800,000 Postal Service employees, to deal with this issue in a forthright manner. We can talk about the failures of the system, we can talk about the failures of the people within that system. But, ultimately, the failure to act will be upon our heads. This is our responsibility.

So I would hope that our first hearing and continuing today will provide some sort of impetus to do what many, many good people, a good number of whom will be seated at that front table both in the first and second panel, have been laboring so hard in quiet desperation to achieve over the past 5 years, and that is meaningful reform that addresses the challenges that the Postal Service meets and does it in a way that is fair to those against whom it competes,

but, most importantly, is fair for those who rely upon it, the American people. Thank you, Mr. Chairman. I yield back.

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

OPENING STATEMENT OF CONGRESSMAN JOHN M. McHUGH
COMMITTEE ON GOVERNMENT REFORM
POSTAL OVERSIGHT HEARING
MAY 16, 2001

Good morning. I would like to thank the Chairman for calling this second hearing on the Postal Service's financial problems. It is indeed a timely hearing.

Last month, the Comptroller General of the United States, David Walker, testified before us that the Postal Service is in the midst of a serious financial and operational crisis that – absent legislative change – placed the Postal Service's ability to meet its universal service obligations at "high risk." The GAO is independent and nonpartisan. We may not always like what they have to say, but GAO calls it as they see it based on firm, factual information and analysis.

As I stated last month, I have always feared that rather than undertaking reasonable and gradual change as we tried to accomplish through last Congress's Subcommittee-approved Postal Modernization Act – a well-refined bill endorsed by a wide array of postal employee organizations, nonprofit and commercial mailers, community newspapers, and several legislators including Senate Democratic Leader

Tom Daschle – Congress would await a worsening crisis and be left with choices of desperation in its duty to provide universal mail delivery that binds the nation together.

Because of our careful work to advance postal reform the past six years, we fortunately don't have to start from scratch. Those efforts resulted in the Postal Modernization Act – twice passed by the Subcommittee in a bipartisan manner with the inclusion of all amendments offered by the Minority. As opposed to the severe constraints the Postal Service faces from outdated governing laws, the Postal Modernization Act provided the Service and its employees true pricing and managerial tools to confront the serious decline in revenue. The Postal Modernization Act substantively addressed the demands of the American mailing consumer for rate stability and service quality. And, the Postal Modernization Act met the concerns of small business and private sector competitors who need strong rules to protect the public interest from unfair competition.

Mr. Chairman, I want to reiterate to all Committee Members our willingness to work with anyone, on any side of the aisle, to enact substantive postal reform in 2001. The Postal Service, its 850,000

dedicated employees, and the 281 million American citizens who depend on universal service at affordable rates are counting on us.

In that regard, it is important to note that despite extensive support for our bill, there was opposition. Each group must make their own decisions as to the merits of legislation and whether to support or oppose. Indeed, most of the witnesses appearing today, took the time to work with us on ways to improve the legislation. Practically all of these groups took out their pens and papers and tried to come up with constructive ways to move reform forward.

However, I was deeply disappointed, albeit not surprised, to read today's testimony of the Main Street Coalition. I cannot stand by without correcting the record on a variety of points raised in their testimony that are completely inaccurate. Setting aside for the moment that their description of the bill has no basis in reality – for example, contrary to their testimony, the bill included specific statutory language creating, for the first time, a strong postal regulator, and prohibitions against unfair competition and discriminatory pricing – they state that the Board's recent decision to increase rates justifies their ability to say "I told you so."

This is just plain wrong. I believe it's important to underscore that because of the bill's price indexing system, consumers would have seen lower rates compared to the above inflation, twice in one year increases. Currently, the Postal Service has sole discretion to determine the overall level of revenues to be extracted from captive customers, and as such, has little reason to control costs. Clearly, an independently administered price index system would represent a vast improvement in protecting the public interest.

More importantly, I would like to quote from Main Street's last testimony before this Committee two years ago:

"We often hear the warning that it would be unwise to wait until the Postal Service is broken to fix it. But without evidence of present or imminent "breakage" – such as declining volume or revenue trend lines over a representative period of time – demands for change of the nature proposed in HR 22 rest on little more than conjecture."

I would suggest that the Comptroller General's testimony from last month, and the GAO's placement of the Postal Service on its high risk list, underscore to the contrary the problems we face.

Mr. BURTON. Thank you, Mr. McHugh. And once again, we want to thank you for all the work you have put forth in this area. Working with you and the rest of the committee, hopefully we will get a solution.

Mr. Tierney.

Mr. TIERNEY. I will put my remarks on the record, if I may, Mr. Chairman.

Mr. BURTON. Mr. Shays.

Mr. SHAYS. Mr. Chairman, I am delighted you are having this hearing. I think it is a very important hearing. I do not have a statement.

Mr. BURTON. Mrs. Mink.

Mrs. MINK. Thank you, Mr. Chairman. I want to express my appreciation to you, Mr. Chairman, for calling this hearing and for continuing the pursuit for facts and information concerning this whole problem of postal service that affects every single individual in our various constituencies.

I want to welcome all the panelists that have been invited here, and especially my former colleague, Pat Schroeder, and look forward to her comments.

Mr. Chairman, this whole issue of postal service is a very confounding one in terms of my district. I represent the rural areas in my State of Hawaii, and it has always been extremely frustrating for me to realize that the term "universal service" does not apply to almost half of my district. They do not have home delivery. By universal service, I have always felt that the promise made to the American family was home delivery. But we do not have home delivery.

We have post offices, of course. And the idea that some of them might be closed in these rural communities is very frightening to the people who live in these remote areas. Now they have to be able either to walk, and many of them are senior citizens and cannot, or they have to be able to drive a car to the post office which sometimes is 10 or 15 miles away to pick up their mail. And the hours that the post office is open in these remote areas is very confining. It is like 8 to noon, or maybe noon to 4, or some hours like that. And so we have a huge population that has a very, very difficult time even as it is to get their mail at a post office box. Post office boxes are not easy to come by. They are very limited. Sometimes you have to wait for years to get a box, so you have to share one with someone. And not only that, Mr. Chairman, you have to pay for the box. Even if the fee is nominal, like $10 a month, it is still a fee that they pay that nobody else does for this universal service.

So I am very confused about this promise of universal service. And as I look at this whole issue of postal service, I want to make sure that what the promise to America was is that this service to every single homeowner in this country was, indeed, universal. That was really the essence and philosophy of the Postal Service, that everybody, no matter where they lived, could at least feel the comfort that the mail would arrive at their place of residence, or in the case of half of my district, at their post office.

So I look with great interest, Mr. Chairman, at the various implications of the suggestions that are being made. I want you to know

that I sit here as a rural member of the United States of America very concerned that this idea of universal service not be prejudiced in any way and that the people of the remote places in America can continue to rely on the Postal Service. Thank you very much.

Mr. BURTON. Thank you, Representative Mink.

Mrs. Morella.

Mrs. MORELLA. Thank you, Mr. Chairman. I want to thank you for this second hearing concerning the uncertain financial future of the U.S. Postal Service. After 5 years of operating at a surplus and a comparably minor loss in fiscal year 2000, the Postal Service's announcement of a potential $2 billion to $3 billion deficit in fiscal year 2001 came as quite a surprise to this committee.

Since the committee's April 4th hearing, the Postal Service has taken many reactionary steps, like suspending capital improvement projects, and studying 5 day delivery service, to stabilize its financial outlook. Many of my colleagues and I were recently shocked to learn that on May 8th the Postal Board of Governors voted unanimously to increase postal rates an average of 1.64 percent, overturning the Postal Rate Commission's April 10th reaffirmation of its decision not to raise rates. The April 4th hearing clearly illustrated many factors causing the Postal Service to project losses in the same calendar year that they have already raised rates. However, additional rate increases and possible cuts in service were never suggested as the prescription to the Postal Service's malady.

As I stated in the April 4th hearing, our reliable and affordable postal service is the hallmark of our Nation's infrastructure. For many neighborhoods, the post office plays a more active role in the fabric of the community than simply providing a facility for the dissemination of the mail.

So today I am eager to hear from the postal stakeholders, those who are most affected by these sudden shifts in policy and who have first-hand experience of the challenges facing the Postal Service. I am interested in learning what reforms they feel might be necessary to preserving this great institution.

Mr. Chairman, you have a great line up of people who are going to be testifying on both panels. Some of us will be back and forth on the Foreign Operations bill on the floor of the House right now. But I particularly want to acknowledge and also thank my former colleague Pat Schroeder for being here on the first panel. Thank you, Mr. Chairman.

Mr. BURTON. Thank you, Mrs. Morella.

Vice Chairman Barr.

Mr. BARR. Thank you, Mr. Chairman. Let me echo the sentiments of other committee members in thanking you not just for this hearing today, but for your pattern of conducting regular and consecutive oversight hearings on issues.

I notice in today's Wall Street Journal that Senator Thompson of Tennessee, in referring to the problems with the Postal Service, says "It is obvious that the ox is in the ditch big time." Mr. Chairman, that may very well be true. And if it is, the last person we want trying to remove the ox is Rube Goldberg. Now I know I run the risk that a lot of young people do not know who Rube Goldberg was, but I know the chairman does and a lot of the folks here do.

In looking through the statements today, I find one of the more revealing and very accurate statements in the testimony of Mr. Sombrotto, president of the National Association of Letter Carriers of AFL–CIO. In his very first page of his prepared remarks, he notes something that I think ought to catch the attention of all of the folks, not just on this committee but who are here today and who are in charge of trying to resolve these problems. He draws attention to the fact that the legislation under which the Postal Service operates and the framework within which it is trying to come to grips with the problems that face it is more than 30 years old. That legislative mechanism, the Postal Reorganization Act of 1970, predates even the notion, much less the implementation, of the Internet and other advanced electronic communications.

I think it is more than time for us to take a look at the underlying legislation. I cannot imagine that those involved directly in this process, the Governors and the other individuals involved with the Postal Service, would not wholeheartedly join in that effort to take a look at the legislation which is woefully outdated and work with us to revitalize the mechanism within which the Postal Service operates.

It is not enough any longer to say that we have the best delivery service anywhere in the world. We do. And many of us, myself included, have lived and worked and travelled in other countries and we know first-hand that is true. But that is no longer enough to get us just by saying we have the best postal service in the world. The Postal Service has very serious problems. It is failing within the framework put together by our Government more than 30 years ago to meet the challenges of the Internet Age.

That is why I commend you, Mr. Chairman, other members of this committee, for beginning the very, very hard, but I believe absolutely essential, process of taking a new look at this legislation, making sure that we do not have Rube Goldbergs hiding out there in the mechanism somewhere, and in doing this to help the Postal Service and help not only American households who would not understand the logic, as we do not either, of saying, gee, the best way to meet these challenges is to cut back service, which is what we considered at the hearing last month. I hope that one has been put to bed and, as Steve Forbes said, "beheaded, buried, burned, and a stake driven through its heart so it is never to rise again."

The solution to meeting the challenges posed by higher energy costs, competition from other entities is not to cut back service, it is not to make yourself even less desirable. We need to look at other more innovative ways. And I salute those such as Mr. Sombrotto and others that we will be hearing from today for recognizing that and urging us to move in the direction of modernization rather than sticking our head in the sand. Thank you, Mr. Chairman.

Mr. BURTON. Thank you, Mr. Barr.

Before we recognize the first panel, let me just say that a number of the interested parties have, at our request, been holding get togethers and meetings to see where they can find common ground to make recommendations to this committee on a legislative proposal to deal with this problem. And I would urge all of the people who are interested, which is just about everybody, especially the

main groups to sit down together when you have the time, and we will be happy to meet with us if you so choose, and send us any recommendations you have so we can put all of that in the mix when we are drafting legislation to deal with this. Of course, Mr. McHugh's H.R. 22 will be one of the keystones in that formulation.

We will now welcome the first panel. Former Congresswoman Pat Schroeder, Jerry Cerasale, John Campanelli, John Estes, and Gene Del Polito. We have a practice of swearing everybody in. So if you would please stand and raise your right hands.

[Witnesses sworn.]

Mr. BURTON. Please be seated.

We will now recognize the Honorable Pat Schroeder for her opening statement. If you could, Congresswoman Schroeder, you remember this, if you could keep your remarks to 5 minutes, we would sure appreciate it.

Thank you.

STATEMENTS OF PAT SCHROEDER, PRESIDENT AND CHIEF EXECUTIVE OFFICER, ASSOCIATION OF AMERICAN PUBLISHERS; JERRY CERASALE, BOARD MEMBER, MAILERS COUNCIL, SENIOR VICE PRESIDENT, DIRECT MARKETING ASSOCIATION, INC.; JOHN C. CAMPANELLI, PRESIDENT, R.R. DONNELLEY LOGISTICS; JOHN T. ESTES, EXECUTIVE DIRECTOR, MAIN STREET COALITION FOR POSTAL FAIRNESS; AND GENE A. DEL POLITO, PRESIDENT, ASSOCIATION FOR POSTAL COMMERCE

Ms. SCHROEDER. Thank you very much. And I really want to compliment you and the committee. I think this attendance is amazing and it says everybody is very, very concerned about the status of the Post Office. So thank you, Mr. Chairman, for your leadership and the leadership of others on this committee for having this hearing and for inviting me to testify.

I, in my life after Congress, am now head of the Association of American Publishers, which basically represents the majority of book publishers in America. We have profits and nonprofits. We mail Bibles, we have textbooks, we have medical journals, you name it, whatever is out there it is in our membership. And we are terribly concerned about what has been going on. That is why I am here today. We love books. Books R Us. We think that we should have been part of this educational-cultural-scientific-information clause that the Congress had put in the Postal Reform.

Yet, we were terribly surprised during the last rate increase to find out we were not. To really explain why it is dramatic, I brought a chart. Visuals are always wonderful. Look at the black line, there would be two kinds of similar book mailings that people might have used during the last 10 years. We basically use the Bound Printed Matter, although a lot of our people use other classes, too, but Bound Printed Matter is the main thing that books use. So we picked out two random ones. And as you can see, through the last decade, it went along just keeping up with inflation. But then, boom, launch, launch. There it goes. And now we have the news the rate might go up even more. We got this average of 18 to 36 percent increase and then we got the message that there will

probably be another 15 percent increase, that means as much as a 50 percent hike on books.

Now this Congress has cared so much about education, about reading, about having printed matter in the home. The year of the brain went on and on about children who start school, who have books in the home, who are around printed matter, and who have people reading to them do much better. I know all of you have been involved in many, many, many of the literacy efforts of the administration. Everybody is concerned about America's literacy rate which has looked awful for a very long time. One of the solutions we know is to get books into the home. One of the ways to do it is to get them there through the mail. And yet, we are really pricing them out. Somebody is going to have to pay for this, either the consumer or someone, or people will not purchase them. It is just that simple.

We have worked hard on "Get Caught Reading." We appreciated many people here working with us. But I think all of us know we have to do everything that is possible. We just saw the latest studies come in about fourth graders. It was absolutely appalling that 60 percent of fourth graders read at a basic level or below. According to the "Twilight of American Culture," there are 120 million adults who only read at a fifth grade level. We know kids now spend 12 times as much time in front of a TV set as they do reading. I could go on and on. Books. We think books.

We were surprised because in this rate case, we thought being part of the educational, cultural, scientific, and information rate they would take that into account, which they did not. They also went on to say during the rate case, "Oh, but you have many more costs in this class, that is why we are having to raise it." And we would say,"What costs?" "Well, we cannot show them to you." There is no transparency. You are fighting a 2 ton marshmallow. You punch it and it punches you back and you have no idea what is in it because they will not tell you what the costs are. If you order books on the Internet through Amazon, or Barnes and Noble, or Borders, you will find most of them now are using private services because the Postal Service is pricing themselves out. Look, this affects so many book clubs. This affects children's book clubs. Even Dolly Parton mails 10,000 books a month to children in her area who are between the ages of zero and 5 because she thinks it is that important.

One of the things I think is essential, because I have spent so much time in this area having been on the Post Office and Civil Service Committee and having sat through many of these hearings, is we do not need another Postal Rate Commission hearing this summer. I think what you are doing is absolutely right on target. Thank you for writing the President and the Secretary of Commerce and getting everyone involved because we really need to delay the rate commission till we get some reforms done. Everybody says, "we have got to reform, but, oh, not that one, and not this one, and just do something but not that." This is an emergency. In every single nation, if you cannot protect your borders with a military, if you cannot deliver the mail to people, if you do not have a strong currency, what is a country about? This is absolutely essential. So having universal service, being able to do this

is critical. I think if you just continue to allow it to hemorrhage with more and more rate increases and not getting essential reform done, we will be right back here next year. It will just go on and on. So, thanks for calling attention to the problem.

I also think there is a way to phase in the rate increase so you do not chase more and more people out of the system. Now more and more books are being chased out of the system. I guess I could give you all sorts of things that we could do. My 5 minutes are up. But I do think it is very, very important that we look at many options. We are ready to do it. We are ready to work with you any way we can. And we thank you once again.

[The prepared statement of Ms. Schroeder follows:]

STATEMENT OF PATRICIA SCHROEDER
PRESIDENT AND CHIEF EXECUTIVE OFFICER
ASSOCIATION OF AMERICAN PUBLISHERS
BEFORE THE
COMMITTEE ON GOVERNMENT REFORM, U.S. HOUSE OF REPRESENTATIVES

MAY 16, 2001

Good morning, Mr. Chairman and members of the Committee. I want to thank you for inviting me to be appear today and to address issues that are of critical importance not only to the Association of American Publishers and its members but also to the American people. The future viability of the Postal Service is a matter of national interest that deserves prompt attention by this Congress.

I am President and Chief Executive Officer of the Association of American Publishers (which for purposes of the remainder of my statement shall be referred to as "AAP"). AAP is the principal representative of the book publishing industry in the United States. It has over 300 members which encompass large and small publishing houses, as well as university and other non-profit publishers. AAP members publish hardcover and paperback books in every field – fiction, general non-fiction, poetry, children's literature, textbooks, reference works, bibles and other religious books, and scientific, medical, technical, professional and scholarly books and journals.

The primary means used by many of AAP's members to deliver books is through the mail. These members make particular use of Bound Printed Matter ("BPM") –a subclass of mail that largely consists of books but that also contains some catalogs. An issue that has received little public attention thus far, but which will have a devastating effect on the distribution of books, is the recent round of rate increases implemented by the Postal Service affecting the Bound Printed Matter subclass. On May 8, 2001, the Board of Governors took the highly

unusual step of voting to implement a second round of rate increases in a single year. As of July 1, 2001, the rates for sending books through the mail will have increased – on average – by over 18% since January 1, 2001. For some book mailers, however, the increases are significantly greater and are as high as 36%. These increases are the largest incurred by any class of mail. Thus far, the Postal Service has failed to provide any credible explanation for the increase in rates for Bound Printed Matter other than to claim that costs associated with the subclass have increased dramatically over the past two years. Yet, the Postal Service has no explanation for the underlying cost increases.

Now, book mailers are faced with the prospect of yet another rate increase as a result of the Postal Service's projected $2 to $3 billion deficit. The additional increase could be as much as 15% across-the-board. If these additional rate increases are implemented, rates for some book mailers – when combined with those that are already scheduled to go into effect on July 1, 2001 – will have increased by as much as 50% over a two- year period. I do not have to go in great detail to explain the effect that these rate increases, cumulatively, will have. Quite simply, many book mailers will not be able to afford to send books through the mail at present volumes. Others will pass these costs directly on to consumers which, eventually, will result in lower volumes of books being sent through the mail. It is also likely that some small publishers will have to discontinue sending books through the mail altogether. As there are few economical alternatives for shipping books, it is likely that higher rates will result in fewer books reaching the public.

All of this brings me back to the purpose of my appearance before you today. Consistent with the goals associated with the encouragement of reading and the promotion of literacy, there is a national interest in the broad dissemination of books through the mail at economical rates.

Throughout the years, Congress has undertaken numerous initiatives aimed at improving literacy and encouraging reading. Two years ago, it enacted the Reading Excellence Act that appropriates over $260 million annually to improve children's reading. Last year, it enacted the Literacy Involves Family Together Act which reauthorized and increased funding for the Even Start literacy programs. And, of course, H.R. 1, which contains the President's education proposals, provides for additional funding mechanisms to promote literacy among children. Other literacy measures have been part of legislation such as the Workforce Investment Act, the Head Start Improvement Act and the National Literacy Act, among others. Congress has consistently promoted literacy efforts because of the wealth of research that confirms the importance of reading to development in every stage of life – from infancy, through childhood and adolescence, to adulthood. Reading is one of the most important means of binding the nation together.

Are there enough books and reading materials in homes today? Unfortunately, the answer is "no." According to the Educational Testing Service, students are reading less and less. They spend 12 times as much time watching television as they do reading. A recent study by the National Assessment of Educational Progress found that only 60% of fourth graders read at the basic level or higher. Many adults do not fare much better. According to The Twilight of American Culture by Dr. Morris Berman, there are 120 million adults who read at only a fifth-grade level. In response to these alarming statistics, AAP and other groups have initiated programs to promote and encourage reading. AAP, for example, has designated the month of May as "Get Caught Reading" Month to remind young adults of the joys of reading. Other organizations such as First Book, Reading is Fundamental and the Dollywood Foundation have

programs designed to distribute new books to disadvantaged children at no cost. Those books, by the way, are distributed to children through the mail and sent at Bound Printed Matter rates.

Excessive increases in rates for sending books through the mail certainly stand at odds with the national interest in promoting literacy and encouraging the broad dissemination of reading material. More significantly, the increases are directly contrary to Congress' longstanding position – as expressed in the Postal Reorganization Act – that mail with educational, cultural, scientific and informational value should be protected from inordinate postal increases.

AAP is well aware of the financial problems faced by the Postal Service and stands willing to work with the Postal Service, other mailers and this Committee to craft a legislative solution to the emerging Postal crisis. As the Committee considers the issue of reform, AAP believes that the following considerations must be taken into account:

Increases in rates cannot substitute for control of costs. The Postal Service must recognize that increases in rates are not a substitute for effective cost controlling measures. The situation faced by book mailers clearly illustrates this. Instead of attempting to understand the reasons for the 40% increase in unit costs for Bound Printed Matter and to find ways to control those costs, the Postal Service reflexively sought to pass these cost increases on to book mailers. Incredibly, at the same time, the Postal Service also imposed a new rate structure on book mailers that required them either to transport book mail deep into the system or pay even higher rates. The Postal Service claims that the new rate structure "mitigates" the full effect of the rate increase on book mailers. The simple fact is that many book mailers do not have volume that allows them to transport mail economically to Postal facilities closer to the point of delivery. The rate increases for these mailers will, in many cases, exceed 30%. Yet, even those larger

mailers who have the resources to transport and drop their mail deeper in the Postal system will see increases that, in some cases, exceed 20%. Despite AAP's insistence the new rate structure would only worsen the effect of the rate shock experienced by book mailers, the Postal Rate Commission and the Postal Service proceeded with implementation. In short, the solution offered to lessen rate shock was a set of so-called discounts that book mailers largely cannot use.

We have repeatedly heard the Postal Service state that it must have greater pricing flexibility. I fear the manner in which the book mailers saw their rates increase in the last rate case is a precursor of what such flexibility really means. AAP fails to see the wisdom of providing such flexibility if the Postal Service is unable to institute measures to ensure that its costs can be maintained at reasonable levels and if it fails to listen to the needs of mailers. Ultimately, there must be greater accountability upon the Postal Service to monitor, justify and control its costs. If the Postal Service fails to better understand and control its costs, the Postal Service will continue to lose customers and volume and, over time, become unable to sustain itself.

The Postal Service must achieve greater productivity. Ultimately, costs will not be controlled and dramatic price increases will not be avoided unless the Postal Service improves its productivity. AAP believes that the Postal Service's current predicament is due, in large part, to low productivity. According to data compiled by the General Accounting Office, the Postal Service has experienced only an 11% increase in productivity over the past three decades. This is the case despite billions of dollars invested by the Postal Service on automation – efforts that should have dramatically increased productivity over the long-term.

Apply rate criteria that take into account the educational, cultural, scientific and informational value of the mail matter. Any legislative reform effort should continue to require

that the Postal Service and the Postal Rate Commission effectively apply rate-making criteria that take into account the educational, cultural, scientific and informational value of the mail matter. These criteria already exist, but they are not being fully applied to the subclass—Bound Printed Matter—that is principally used to ship books. In fact, just as the cost increases for Bound Printed Matter are unexplained, the composition of the subclass has gone unexamined. Indeed, the postal ratemaking process appears to cling to the outdated view that Bound Printed Matter is mainly used for catalog shipments, and seems more interested in accommodating those types of mail shipments than encouraging the broad dissemination of books. Before enacting reforms of the ratemaking process, Congress should ensure that the Postal Service and Rate Commission are fully following the directives that Congress has already given them. In the case of books, they are not.

As for the subject of the reform, although we support legislative reform that truly provides rate stability, we continue to urge that any new ratemaking system must account for the value of the mail matter being sent. Abandoning ratemaking criteria that take into account the content of the mail could subject many mailers to far steeper increases than they currently face. Ultimately, any rate stability that results from the imposition of price-caps is meaningless if based on rates that are too high to begin with.

The Postal Service has indicated that it is considering delaying the filing of the next rate case until the end of the year or early next year. We call upon the Postal Service to examine every means possible to delay the filing of a rate case. This would provide time for Congress, the Postal Service and mailers to devise a solution to the Postal Service's current fiscal predicament. AAP also understands that the Postal Service is considering phasing in the next rate increase in order to mitigate its effect on mailers. While AAP hopes that a new rate case can be avoided and

believes that rates should not be raised until the Postal Service has taken efforts to cut its costs and improve productivity, if another rate case becomes inevitable, AAP would prefer to see rates phased-in over time rather than imposed on mailers all at once.

Ultimately, AAP believes that the Postal Service needs to adhere to its core mission of providing universal service at affordable rates. AAP questions whether this mission could continue if the Postal Service were privatized, as some commentators have recently suggested. Privatization works only if there is effective competition for the full range of services provided by the Postal Service. For many mailers, including many book mailers, there is no economical or practical alternative to the Postal Service. If the Postal Service were privatized, there is no guarantee that mail service which customers rely upon would continue, or even if it did continue, that it would be offered at affordable rates.

Mr. Chairman, I want to again thank you for inviting me here today and I look forward to working with you and other members of the Committee in moving forward to develop a consensus on Postal reform.

SUMMARY OF STATEMENT OF PATRICIA SCHROEDER
PRESIDENT AND CHIEF EXECUTIVE OFFICER
ASSOCIATION OF AMERICAN PUBLISHERS
BEFORE THE
COMMITTEE ON GOVERNMENT REFORM, U.S. HOUSE OF REPRESENTATIVES
MAY 16, 2001

AAP is the principal representative of the book publishing industry in the United States. It has over 300 members which encompass large and small publishing houses, as well as university and other non-profit publishers. AAP members publish hardcover and paperback books in every field – fiction, general non-fiction, poetry, children's literature, textbooks, reference works, bibles and other religious books, and scientific, medical, technical, professional and scholarly books and journals.

The primary means used by many of AAP's members to deliver books is through the mail. These members make particular use of Bound Printed Matter ("BPM") –a subclass of mail that largely consists of books but that also contains some catalogs. As of July 1, 2001, the rates for Bound Printed Matter will have increased – on average – by over 18% since January 1, 2001. For some book mailers, however, the increases are significantly greater and are as high as 36%. These increases are the largest incurred by any class of mail. If the Postal Service seeks to increase rates yet again, through the filing of another rate case this summer, rates for some book mailers will have increased by as much as 50% over a two year period.

There is a national interest in the broad dissemination of books through the mail at economical rates. The recent increases are directly contrary to Congress' longstanding position – as expressed in the Postal Reorganization Act – that mail with educational, cultural, scientific and informational value should be protected from inordinate postal increases. As the Committee considers postal reform, AAP urges that the following issues be taken into account:

Increases in rates cannot substitute for control of costs. The Postal Service must recognize that increases in rates are not a substitute for effective cost controlling measures. There must be greater accountability by the Postal Service to monitor, justify and control its costs.

The Postal Service must achieve greater productivity. Costs will not be controlled and dramatic price increases will not be avoided unless the Postal Service improves its productivity.

Apply rate criteria that take into account the educational, cultural, scientific and informational value of the mail matter. Any reform effort should continue to require that the Postal Service and the Postal Rate Commission effectively apply ratemaking criteria that take into account the educational, cultural, scientific and informational value of the mail matter. Currently, these criteria are not being fully applied to Bound Printed Matter. Any new ratemaking system must account for the content and value of the mail being sent.

Finally, the Postal Service needs to adhere to its core mission of providing universal service at affordable rates. AAP questions whether this mission could continue if the Postal Service were privatized. Privatization only works if there is effective competition. For many book mailers there is no economical alternative to the Postal Service.

Mr.BURTON. Thank you, Representative Schroeder. And as I said before, any recommendations that you have that we could put in the mix, we would sure appreciate.

Mr. Cerasale.

Mr. CERASALE. Thank you very much, Mr. Chairman, members of the committee. It is a pleasure to be here and be invited to speak. I am Jerry Cerasale and I am on the Board of Directors of the Mailers Council. It is a pleasure to be sitting here next to one of our distinguished trustees. In another life, I am the senior vice president for Government Affairs for the Direct Marketing Association. But I am here today on behalf of the Mailers Council.

We are a pretty diverse group. We represent 70 percent of all the mail in the United States carried by the U.S. Postal Service. We are so diverse that any recommendation that you might have on postal reform you will have members of the Mailers Council support it. You will also have members of the Mailers Council oppose it. Our membership agrees that there should be postal reform, they just do not necessarily agree on what is the answer to postal reform.

But we do agree on something that we think is very important for the Postal Service, and that is cost control. A major ingredient of cost control is productivity and productivity improvement. We think that the Postal Service has not done well. As we look at Total Factor Productivity from 1972 to 1998, we find the Postal Service has increased productivity by 9.1 percent, which is not very good. And most of that increase came before the 1991 recession. Historically, the Postal Service has focused on productivity and improved it. But the focus has not remained and things have slipped.

So the Mailers Council decided that we wanted to try and get a constant focus on postal productivity improvement. So we developed the Mailers Council Quarterly Report Card on Postal Service Productivity. The first of which was released on Monday and the results are on the chart over on the right. We hope to highlight with this report card both the positive and negative trends in productivity in the Postal Service very early to encourage continued efforts where things are going well and to begin immediate action to correct problems that we see.

We chose for this productivity report card quite a few measures. Because no measure is perfect, we think that a diverse number of measures will likely show, that basket will show correct and accurate trends. We also at the Council wanted to try and measure different functions independently so we can try and show management areas where they can focus efforts to improve productivity.

As we look at the grades on the chart, the first set are internal productivity grades. That is taking a look at improvements within the Postal Service. We chose some areas to try and get, as I said, a long-term and diverse view. Revenue per work hour, D+; volume per work hour, we give them a grade of D+; unit labor costs, C; mail processing is a B, very good. We were encouraged by that. That shows what has happened with all the efforts by the Postal Service in machinery and so forth to help improve the productivity of mail processing, and I think it is represented by this grade. Delivery and retail services, both in the C range. These grades rep-

resent both a mid-term and short-term view of Postal Service productivity recently.

We also wanted to use a benchmark and tried to pick some private sector areas in productivity and compare the Postal Service with them. The grades shown here in the next four are not grades of the private sector, but Postal Service compared with the private sector. And they are in the C and C-range, representing that the Postal Service has not done as well as we would hope that they would do.

We are also concerned with salary limits on Postal Service managers. We would like to see if we can lift those to try and help the Postal Service attract and retain talented leaders that are needed in this time. But we would urge that any additional compensation be also tied to productivity increases at the Postal Service.

The recent events—the two rates cases in 6 months, the threat of another rate filing soon—are proof of the need for the Postal Service to improve productivity. Using the William and Mary system, in which I have invested a great deal of my disposable income recently, the Postal Service measures a 1.8 GPA. We need some 4.0s in order to really improve the situation at the Postal Service. And the real factor in this is not the first column with the grades, it is those empty three columns. We need to see improvement consistent up through there, and we hope that you look forward to seeing these quarterly reports as much as we do.

Thank you very much. I am willing to answer any questions you have.

[The prepared statement of Mr. Cerasale follows:]

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MAILERS COUNCIL

TESTIMONY
OF THE
MAILERS COUNCIL
BEFORE THE

COMMITTEE ON GOVERNMENT REFORM
HOUSE OF REPRESENTATIVES

MAY 16, 2001

TESTIMONY OF
JERRY CERASALE
ON BEHALF OF THE
MAILERS COUNCIL
BEFORE THE
COMMITTEE ON GOVERNMENT REFORM
HOUSE OF REPRESENTATIVES

Mr. Chairman and members of the Committee, my name is Jerry Cerasale and I am senior vice president of Government Affairs for the Direct Marketing Association. Today I am testifying as a board member of the Mailers Council, the nation's largest mailing association. Our members represent for-profit and nonprofit mailers that use the United States Postal Service to deliver correspondence, publications, parcels, greeting cards, advertising and payments. Collectively the Council accounts for as much as 70 percent of the nation's mail volume.

The Mailers Council's believes that the Postal Service can be operated more efficiently, supports efforts aimed at containing postal costs, and has the ultimate objective of lower postal rates without compromising service.

We greatly appreciate this opportunity to testify on the future of the Postal Service. Let me state emphatically that we need a healthy Postal Service. This institution is a vital business partner to all of our members—an irreplaceable one to many. The Postal Service makes it possible for American businesses to market their products and services, and to get them delivered. In many areas of the country the Postal Service is our only delivery option. We need the Postal Service to get its fiscal house in order, because it if does not, many of the companies we represent will simply be unable to operate. The Postal Service contributes substantially to a vital United States economy, and its demise would make it exceptionally difficult, if not impossible, for the nation to avoid moving from an economic downturn to a full-scale recession. The seriousness of this situation is difficult to overstate.

During the next two years the Postal Service will face financial pressures unseen in over 30 years. The Postal Service is predicting large deficits that would likely be followed by substantial rate increases. The effect on American businesses and their cost of goods and services would be substantial. Today, postal management, labor organizations and the Mailers Council all agree on the severity of the problem, if not on a precise solution.

This is a situation that demands the attention of mailers, Congress and the White House. We are especially appreciative of your efforts, Mr. Chairman, to involve the Bush Administration in this dialogue. The Council and many of our members have written to and met with White House staff members to urge their attention to the Postal Service's plight.

Let me note that in the past four years the Council has repeatedly asked for the opportunity to meet with the entire Board of Governors to discuss the future of the Postal Service, and each time they have denied our request. That is because the Board has an unpublished policy of refusing to meet with any group—including mailers. We did not understand why the governors believe this is an acceptable business practice. In this time

of financial crisis, we believe the advice and assistance of every significant member of the postal community—especially the ratepayers—are important. A recent meeting between two governors and a dozen mailers was an encouraging sign. They've opened the door a bit; we'd like to see them open it all the way, and for everyone. At the beginning of every open session of the governors' two-day monthly meetings, the chairman routinely reads a statement noting that the public may observe, but cannot participate in those meetings—because there are other opportunities to do so. We hope meetings between the governors and mailers become one of those opportunities.

We welcome this opportunity to debate the future of an institution that touches every American. We are alarmed at the state of postal finances, but mailers, which pay over 90 percent of the revenue collected by the Postal Service, are equally concerned with the response to this crisis by postal management. They have encouraged the governors to approve the filing of a dramatic price increase. Raising prices is certainly the easiest response available, but we believe it would not be the wisest.

As we stated in letters to you and to the chairman of the Postal Service's Board of Governors earlier this year, the contemplated postage increase would be counterproductive to the Postal Service's goal of increasing revenue. We know from experience that a double-digit increase will devastate volume in the months immediately following the new rate implementation. This time, such plans will ensure permanent volume losses in several mail classes. Many small businesses that use the mail exclusively to market their businesses, and small publishers that operate on exceptionally thin margins, simply cannot absorb two large, back-to-back postage increases. Some mailers would experience a 25 percent rate increase in 18 months—something we might expect from OPEC, but not from the Postal Service.

To give you an appreciation of what a postage increase costs business mailers, let me remind the committee members that for us, a postage increase is never "just" a penny. Postage can be one of the largest, if not the largest, item on a member organization's expense ledger; so postal increases can be the single biggest cost increase in a given year. A one-penny increase in a First-Class stamp costs most Americans only a few dollars more a year. But for a business that mails invoices, magazines, newsletters, newspapers or advertisements, a typical postage increase translates into thousands or millions of dollars in additional expenses.

As one example, the postage increase implemented in January cost Hearst magazines an additional $7 million. If the Postal Service follows through on plans for an additional 15 percent increase, that will cost this company another $10.6 million—annually.

We believe the Postal Service must consider alternative steps in response to declining revenues. Implementing large increases guarantees that many mailers will mail less often, or stop mailing completely. If that occurs, mail volumes will decline even further, creating the need for yet another rate increase. We could see postal rates spiral upward with more increases that continue to be substantially higher than the rate of inflation.

The Postal Service adopted a short-term strategy to its recent problems by eliminating or postponing over 800 postal facility projects. That will reduce expenses now, but will not cure the Postal Service's long-term problems. We feel similarly about the possibility of eliminating six-day delivery.

Postmaster General Henderson and the Board of Governors have both called for postal legislative reform as the solution to the Postal Service's financial problems. Some of our members believe that reform legislation is the answer, although they do not agree on the type of reform; others suggest the need for a presidential commission to decide what type of legislation would be appropriate. Because of this disagreement among our members, we are unable to take a position on postal legislative reform. But what we unanimously agree on is the need for the Postal Service to immediately improve its management, because legislative reform is not going to be quick or easy, and good legislation cannot counter the effects of poor or inadequate management. And the primary focus of postal management must be on improving postal productivity.

Last year we published a comprehensive study of postal productivity. Acknowledging that the Postal Service is unlike any other government agency or private sector organization, we stated our belief that comparing postal operations to similar industries can help determine whether the Postal Service has been reasonably successful in improving its productivity. The study shows that for most of its history the Postal Service has failed in this endeavor.

Since the 1991 recession, the Postal Service's Total Factor Productivity (TFP) compares unfavorably with all business productivity measures generated by the Bureau of Labor Statistics. The Postal Service's productivity growth record since Congress implemented the Postal Reorganization Act on July 1, 1971, is inconsistent. Between 1972 and 1998, the Postal Service experienced only a 9.1 percent growth in TFP, most of which occurred prior to the 1991 recession. The Postal Service experienced high productivity growth only in the years 1973, 1978, 1990 and 1993, and an overall negative productivity growth for all other years combined.

On Monday, May 14, we released a new study of postal productivity: the Mailers Council Quarterly Report Card on Postal Service Productivity. This is the first in a series of new quarterly Report Cards that will grade the Postal Service on its ability to enhance its overall financial performance by improving its productivity. Each Report Card will grade the Postal Service's productivity relative to its own performance in previous quarters, and to productivity trends in the private sector. We believe that by highlighting such trends the Postal Service can achieve greater productivity growth, thereby reducing the frequency and size of postage rate increases.

The Postal Service historically has experienced periods where cutting costs is its single greatest management concern, and others where improving service is its primary objective. When revenue is up, some managers often lose their focus on cost containment; when revenue is down, managers give insufficient attention to maintaining or improving service. This problem occurred most recently in FY 1999. After two years of dramatic profits, managers failed to recognize and respond to excessive spending as mail volume failed to reach predicted levels. The response was a belated cost-cutting program that affected service, and that was detrimental to employee morale.

To help the USPS maintain a more steady approach to its management, and to recognize those occasions when it achieves this goal, the Council decided to publish these quarterly reports on postal performance—from the customers' perspective. Our objective is to use the Report Cards to focus on productivity as a way to highlight negative trends as early as possible, and to

trends as early as possible, and to praise significant improvements.

Each quarterly Report Card will help highlight—for postal management, for users of postal services, for postal legislators and regulators and for the public generally—the status of postal productivity performance, in relation both to recent Postal Service trends and to productivity trends in the private sector. The Mailers Council believes that by highlighting such trends the Postal Service can achieve greater productivity growth, thereby lessening the frequency and magnitude of rate increases.

Today, finding ways to improve postal productivity is the most significant challenge facing the Postal Service and all postal customers. If labor cost increases were zero, increases in productivity could be zero, and rate stability would be achieved. However, because postal labor costs are increasing, the Postal Service must improve its labor productivity to achieve postage rate stability. If labor costs increase while labor productivity declines, the Postal Service will never achieve rate stability.

The first Quarterly Report Card highlights both problem areas and signs of success. It includes grades for six different internal productivity measures that range from a D+ to a B+.

- Revenue per Work Hour, D+;
- Volume per Work Hour, D+;
- Unit Labor Costs, C;
- Mail Processing, B;
- Delivery, C-;
- Retail Services, C.

When comparing the USPS against the private sector, the grades were much lower, with the highest mark a C.

- Similar Activities, C-;
- Non-Durable Manufacturing, C-;
- Mature and Emerging Substitutes, C;
- Major Postal User Groups, C-.

Grades reflect the Postal Service's productivity for each sector. For example, the Delivery rating is not a grade based on whether the Postal Service letter carrier consistently delivers letters at the expected time each day; it is a grade that indicates whether the Postal Service is improving the productivity of all employees working in the delivery area.

Periodically during the last 30 years the Postal Service has reported sporadic period of productivity improvements, like those shown in the last two quarters. We are encouraged by these recent successes, but note that several of the category grades are unacceptably low. More importantly, what we need to see now is consistent productivity increases over an entire fiscal year. That's what we'll be looking for with each quarterly report card and the final, year-end grade.

Our report card does not offer specific suggestions for how the Postal Service can improve productivity. We do not wish to micro-manage postal operations, and believe the Postal Service not only has the ultimate responsibility for determining what should done, but is in a much better position than mailers for determining what can be done to improve productivity. Of course, we would gladly offer any assistance the Postal Service may request.

Additional details on our methodology and the credentials of the economists who developed the report card are included in Appendices A and B of this testimony.

As noted previously, Mr. Chairman, the Mailers Council is divided on recent proposals for comprehensive legislative reform.

However, there is one urgent legislative issue on which we wholeheartedly agree, and one I hope you and other members of this oversight committee will address: the salary limits on senior postal managers.

We are gravely concerned about the Postal Service's ability to attract and retain the type of talented leaders it will need to cope with the challenges this institution faces. Many individuals who have come from the private sector to accept the position of postmaster general do so out of a sense of duty to the nation, as an exercise in public service. But can we expect young, talented managers to move their families from lower cost of living cities to the very expensive Washington, DC area? Ask any vice president at Postal Service headquarters about this problem and you'll hear many stories about employees who turned down the opportunity for promotion because they could not afford what amounts to a substantial pay cut they would endure because of the higher cost of housing and other essentials in the nation's capital.

Salaries for USPS managers covered by the Postal Career Executive Schedule (PCES) are dramatically below comparable positions in the private sector and with foreign postal administrations. As a result, several USPS senior managers in recent years have left the Postal Service for private sector positions that pay significantly more in base salary, and include benefits unavailable to employees of any federal agency. Some managers have left as soon as they were retirement eligible, while others left before that date. As this pay gap increases, retention problems will increase; recruitment of talented managers from the private sector will be impossible.

Postal officer and employee compensation is restricted to the maximum rate on the Executive Schedule level I, under section 5312 of title 5, currently set at $161,200. The solution is to separate the Postal Service from the Executive Schedule, which would require a change in Title 39. We recommend Congress either lift the limit on postal pay and leave compensation issues to the Board of Governors, or set the PMG's salary ceiling at a level more appropriate for the manager of an organization with more than 787,000 employees and 27,000 post offices, and index that amount for inflation. As important as the increase in base compensation, we believe the Board of Governors must tie additional compensation to increases in postal productivity—as is often the case in the private sector.

To summarize, the Postal Service faces challenges that could threaten its very existence. We are concerned about the agency's ability to attract and retain the skilled managers it will take to ensure that the Postal Service survives another century of service to the nation. We firmly believe that those managers must continue to focus on productivity improvements if they are to restrain postal costs, and ultimately postage rates. If postal management cannot consistently improve its productivity, costs will rise to the point that the Postal Service will price itself out of business.

Mr. Chairman, I am prepared to answer any questions you and your colleagues may have.

MAILERS COUNCIL

REPORT CARD ON US POSTAL SERVICE PRODUCTIVITY
FIRST QUARTER, 2001

Introduction

This is the first in a series of new quarterly Report Cards that will grade the US Postal Service (USPS) on its ability to enhance its overall financial performance by improving its productivity. Each Report Card will grade the USPS' productivity relative to its own performance in previous quarters, and to productivity trends in the private sector.

The Report Cards are produced by the Mailers Council, a coalition of over 50 corporations, nonprofit organizations and major mailing associations. Council members represent for-profit and nonprofit mailers that use the United States Postal Service to deliver correspondence, publications, parcels, greeting cards and payments. Collectively the Council accounts for nearly 70 percent of the nation's mail volume.

To develop the economic comparisons and resulting grades the Mailers Council selected the Washington Economics Consulting Group, led by the company's president, Dr. James A. Clifton. An economic consultant and expert witness with more than 20 years experience, Clifton has worked with associations, corporations and government agencies. He has extensive experience examining the Postal Service and its finances. Clifton has testified as an expert witness at numerous hearings before the Postal Rate Commission, the regulatory body that reviews all requests for postage rate increases.

This document offers information as a supplement to News Release 01-5, which announces the publication of the first Report Card. On the pages that follow we include additional background information, our objectives in undertaking this project, the methodology and definitions. Finally, we offer a detailed description of each grade category and how we derived the first quarter grade.

REPORT CARD

Postal Service Productivity

Fiscal Year 2001

SECTION A— USPS Internal Productivity

CATEGORY	PRODUCTIVITY GRADE FIRST QUARTER	SECOND QUARTER	THIRD QUARTER	FORTH QUARTER	FINAL GRADE
Revenue per Work Hour	D+				
Volume per Work Hour	D+				
Unit Labor Costs	C				
Mail Processing	B				
Delivery	C-				
Retail Services	C				

SECTION B— Private Sector Benchmark Comparison

CATEGORY	PRODUCTIVITY GRADE FIRST QUARTER	SECOND QUARTER	THIRD QUARTER	FORTH QUARTER	FINAL GRADE
Similar Activities	C-				
Non-Durable Manufacturing	C-				
Mature and Emerging Substitutes	C				
Major Postal User Groups	C-				

EXPLANATION OF MARKING SYSTEM

A-Superior
B-Above Average
C-Average
D-Below Average
F-Failing

This first quarter report card reviews postal productivity for the USPS' fourth quarter of FY 2000

Background

The Postal Service historically has experienced periods where cutting costs is its single greatest management concern, and others where improving service is its primary objective. When revenue is up, some managers often lose their focus on cost containment; when revenue is down, managers give insufficient attention to maintaining or improving service. This problem occurred most recently in FY 1999. After two years of dramatic profits, managers failed to recognize and respond to excessive spending as mail volume failed to reach predicted levels. The response was a belated cost-cutting program that affected service, and that was detrimental to employee morale.

To help the USPS maintain a more steady approach to its management and to recognize those occasions when it achieves this goal, the Council decided to publish these quarterly reports on postal performance—from the customer's perspective. Our objective is to use the Report Cards to focus on productivity as a way to highlight negative trends as early as possible, and to praise significant improvements.

Objective

Mailers Council members are interested in restraining postal costs to ensure postage rate stability while maintaining service quality. The Council believes placing an emphasis on productivity is the key to postal rate stability. To examine our concern about the poor state of postal productivity since Congress created the USPS over 30 years ago, we published an extensive study in March of 2000: "Postal Productivity; Real Improvements Needed Now." (For a copy of the study visit the Mailers Council's website: www.mailers.org.)

We continue our examination of postal productivity with this new Report Card. Each quarterly Report Card will help highlight—for postal management, for users of postal services and for the public generally—the status of postal productivity performance, in relation both to recent Postal Service trends and to productivity trends in the private sector. The Mailers Council believes that by highlighting such trends we can help the Postal Service achieve greater productivity growth, thereby lessening the frequency and magnitude of rate increases.

Today the most significant challenge facing the USPS and all postal customers is finding ways to improve postal productivity relative to changes in postal labor cost. If labor cost increases were zero, increases in productivity could be zero, and rate stability would be achieved. However, because postal labor costs are increasing, the Postal Service must improve its labor productivity to achieve postage rate stability. If labor costs increase while labor productivity declines, the Postal Service will never achieve rate stability.

Methodology and Definitions

Grades reflect only the Postal Service *productivity* for each sector. For example, the Delivery rating is not a grade based on whether Postal Service carriers consistently deliver letters at the expected time each day; it is a grade that indicates whether the Postal Service is improving the productivity of all employees working in the delivery area. Although objective data is the foundation for grading, judgments by economists experienced in the postal area are also factored into the final grades assigned in each category.

The Mailers Council's Report Card grades were determined based on reviews of data from two sources:

- USPS accounting period data, and
- private sector productivity data produced by the Bureau of Labor Statistics (BLS) at the US Department of Labor.

The resulting grades are offered in two sections:

- Section A, USPS Internal Productivity, and
- Section B, Private Sector Benchmark Comparisons.

Section A, USPS Internal Productivity

These productivity measures are drawn from Postal Service accounting period (AP) data. A postal AP is a four-week period that forms one thirteenth of the postal fiscal year. Each AP begins on a Saturday and ends at the close of business on the Friday four weeks later. APs begin with the start of each postal fiscal year, which differs slightly from the federal fiscal year (October 1–September 30). Historical measures are based on the revisions to these data. Data for the most recent quarter are based on initial releases of three or four postal APs, depending upon the quarter considered.

An annual grade will eventually be assigned for each productivity measure that incorporates annual data, and data that is otherwise revised from initial accounting period reports. The annual grade will reflect revisions to the aggregate of the four quarterly reports, based on the revised data that the Postal Service only releases annually, and any revisions BLS or WECG may issue.

Section B, Private Sector Benchmark Comparisons

Although the Postal Service is in many ways a unique institution, the Mailers Council believes it is essential to compare certain postal operational areas with those in the private sector that are in some ways similar. For example, postal retail operations are quite similar to many private sector retail outlets. Also, many large mailers operate sizeable mail sorting and delivery operations.

Ideally, measures of trucking and air transport productivity would be useful comparables, but they are not available in the BLS data set. Similarly, a single comparable that mirrored USPS delivery service would be cleaner than the several measures we use. After carefully considering the BLS data availability and the limitations of its use, we selected four categories that allow a fair comparison between USPS and private sector activity.

Section A, Descriptions and Grades

1. Revenue Per Work Hour

Description
Quarter-to-quarter USPS labor productivity changes are measured relative to the immediate past quarter for six categories (see Report Card). The most standard measure of productivity is output per unit of labor input, included in Report Card Section A as measure two. For a large enterprise producing many different products and services with widely varying value-added, however, a better proxy for productivity changes in the short run may be revenue per work hour. Such a measure is useful in the case of postal productivity measurement because it enables us to weight heterogeneous output and produce an overall measurement of quarterly changes in productivity that is weighted in some sense by the relative value added of each type of output, whether a First-Class letter or a periodical or package. We define this measure as follows:

Mail Volume x Price ÷ Total Workhours

As a tool for evaluating USPS performance, one might think of this productivity measure as being akin to what USPS management uses internally for its own purposes: revenue per piece of mail. Our focus with each Report Card is on productivity, however, so the denominator of interest is work hours, not mail pieces.

Grade
We have assigned a letter grade of D+. Fifty percent of this grade was based on comparing fourth quarter of 2000 to fourth quarter of 1999. Revenue per work hour was positive the fourth quarter of 1999 at one-half of one percent, but was barely one tenth of one percent for the fourth quarter of 2000. For this half of the grade, we assign a failing grade. Fifty percent of this grade is based on comparison with the third quarter of 2000. Revenue per work hour was falling marginally in the third quarter and rising marginally in the fourth quarter of 2000. The fourth quarter of 2000 was also below our medium term trend productivity estimate for this measure, earning a C- for this half of the grade.

2. Volume Per Work Hour

Description
Key, service-wide measures of output-labor productivity are calculated as follows:

Mail Volume ÷ Total Workhours
Mail Volume ÷ Total Employees
Mail Volume ÷ Career Employees

Although the Report Card and other measures using this productivity measure focus on workhours, other measures of labor input are used here in a qualitative sense to arrive at the letter grade.

Grade

For the fourth quarter of 2000, we have assigned a letter grade of D+. Fifty percent of this grade was based on comparing fourth quarter of 2000 to fourth quarter of 1999. Volume per work hour was positive in 1999 for that quarter at nearly one percent but has declined to less than one-third of one percent for the fourth quarter of 2000. For this half of the grade, we assign a failing grade. Fifty percent of this grade is based on comparison with the third quarter of 2000. Volume per work hour was improved in the fourth quarter of 2000 relative to the third quarter but running well behind the first two quarters of the year. However, fourth quarter productivity was running just at medium term trend, earning a C for this half of the grade.

3. Unit Labor Costs

Description

This measure traditionally accompanies productivity studies because one of the causes of increasing unit labor costs can be lagging productivity gains. In assigning a letter grade, we look at five unit labor cost measures. We also look at the obverse of such measures in the detailed tables, namely, what volume of mail is being produced per dollar expenditure on labor. For understanding postal productivity, this may be a more direct statistic than the normal focus on labor costs per mail piece. Labor cost per unit of output (unit labor costs) is calculated as follows:

Total Personnel Compensation ÷ Mail Volume
Operating Labor Costs ÷ Mail Volume
Non-Operating Labor Costs ÷ Mail Volume
Total Non-Personnel Operating Expenses ÷ Mail Volume
Total Personnel Compensation Other Than Salaries and Benefits ÷ Mail Volume

Grade

Changes in unit labor costs for various segments of the USPS work force have shown very recent improvement, namely slower rates of increase in the fourth quarter of 2000, in comparison to the same quarter for 1999 and by comparison with the third quarter of 2000. For some of these measures the improvement was dramatic compared to the third quarter of 2000, which saw extraordinary increases in unit labor costs for non-operations labor and non-personnel operating expenses. In the case of the latter, unit labor costs increased more in the fourth quarter of 2000 than the fourth quarter of 1999, but for the remaining four measures used to assign this grade, there was a slowdown in the increase in unit costs. However, these recent improvements must be evaluated in light of the rising trend in unit labor costs, and the fact that the last several quarters have seen increases in unit labor costs above the trend. We assign an overall grade of C, balancing the dismal trend performance with some hope evident from the later quarter.

4. Mail Processing

Description

Quarterly productivity comparisons four through six seek to measure USPS labor productivity beyond a service-wide measure, namely for major service sectors that make up the Postal Service. Due to inherent limitations from using accounting period data from the Postal Service, and the lack of availability of other quarterly data which would permit greater precision and a timely release of these reports, measures four through six do not precisely measure mail processing, delivery or retail service productivity. They approximate it.

For example, First-Class mail (letters, bill payments) and Standard A mail (magazines, catalogs, newsletters) are not the only mail classes using the mail processing operations of the Postal Service. Furthermore, portions of First-Class and Standard A bypass one or more mail processing steps. Nonetheless, these two classes of mail incur most of the Postal Service's mail processing costs and mail processing labor resources. Therefore, the output from the use of these processes in these classes is indicative of what may be happening to the level of labor productivity in the mail processing operation. Quarterly Report Card grades in Section A, measures four through six, are reconciled with annual data during the fourth quarterly report for any year. The reconciliation removes most deviations from mail processing productivity as measured using the less perfect quarterly data.

The issues raised above are more important when considering Mail Processing (measure four) than when considering Delivery and Retail Services (measures five and six). For Delivery we consider total mail volume, because almost all mail is delivered through USPS operations (some international operations being the main exception). For Retail Services we consider only First-Class mail, because most, though not all, Retail Services are devoted to First-Class mail.

To measure how well management is containing Mail Processing costs, we use this calculation:

Mail Processing Costs + Plant and Equipment Maintenance Operations Costs ÷
First-Class + Standard A Mail Volume

The reciprocal of this measure reflects the volume of mail processed for every dollar spent on mail processing. The calculation, in a way, reflects how productive this operation is, given the costs. A general decline in measure four or increase in its reciprocal indicates how effective the management has been in containing this cost segment.

Grade

Unit mail processing costs were falling in the fourth quarter of 2000, but they were falling by more in the fourth quarter of 1999. In arriving at the overall grade of B, we have weighted equally the D+ we assign for comparison with the 1999 fourth quarter, and the A- we assign for comparison with the third quarter of 2000, and the fact that recent improvements are better than the modestly falling trend.

5. Delivery

Description
To measure how well management is containing Delivery costs, we use this calculation:

Rural + Other Delivery and Vehicle Services Operating Costs ÷ Total Mail Volume

The Rural, Other Delivery and Vehicle Services operating costs per unit of output provide a measure of how well management is containing this major cost segment. The reciprocal of this measure shows the number of mail pieces delivered for every dollar spent on delivery. The calculation, in a way, shows how productive this operation is given the costs involved. A general decline in Delivery or an increase in its reciprocal indicates how effective management has been in containing this cost segment.

Grade
Unit delivery costs for the fourth quarter of 2000 increased at a substantially slower pace than for the fourth quarter of 1999, and at a slower pace than for the third quarter of 2000. However, the overall trend of USPS unit delivery costs is very poor, the single most worrisome cost and productivity factor Postal Service-wide. Our assignment of a C- grade for the fourth quarter of 2000 only reflects improvement over a dismal medium term trend, for which we have assigned a benchmark grade of D- for internal tracking purposes. The fourth quarter, indeed all quarters for the year 2000, are running above that troublesome trend.

Retail Services

Description
To measure how well management is containing Retail costs, we use this calculation:

Customer Services and Sales ÷ First-Class Mail Volume

The Customer Services and Sales Expenses divided by the First-Class mail volume provide a measure of how well management is containing this cost segment. We are using First-Class mail volume for this measure because it is by far the major user of Customer Services. The reciprocal of this measure shows the number of mail pieces receiving Customer Services for every dollar spent on customer services and sales. The calculation, in a way, shows how productive this operation is given the costs. A general decline in this measure or increase in its reciprocal indicates how effective management has been in containing this cost segment.

Grade
Unit cost increases in this area have worsened somewhat compared to the fourth quarter of 1999, but have moderated compared to the third quarter of 2000. For all of the year 2000, each quarter is close to medium term trend. These factors warrant a letter grade of C.

Section B Grades

1. Similar Activities Businesses

Description
We allocate Postal Service labor by the four basic processes noted in the table below, and then weight similar private sector processes for which BLS reports productivity numbers by the same USPS weights.

The four processes and private sector comparables are as follows:

USPS Process	BLS Private Sector Comparable
Mail processing	Non-durable manufacturing
Delivery	Linen supply, fuel oil dealers, nonstore retailers, telephone communications, radio and TV broadcasting, cable and other pay TV services
Retail Services	Commercial banks
Transportation	Railroad transportation

This methodology enables us to measure overall USPS labor productivity relative to a composite of private sector comparables for the four basic processes that constitute postal services. BLS produces most of the above private sector productivity data annually, not quarterly. What we measure, therefore, is current USPS quarterly performance compared to medium-term private sector performance, consisting of a moving three-year average for each BLS data series.

Grade
Relative to private sector comparables for the major activities which make up postal services (mail processing, delivery, transportation and retail services), USPS productivity was positive for all of 2000, but it was rising over 3% for the comparables, using a three-year moving average. In the third and fourth quarters of 2000, aggregate USPS productivity growth was running well behind that of the first two quarters. For the fourth quarter of 2000 at annualized rates, USPS productivity growth was 1.25% compared to our private sector medium term composite of 3.43%. We assign a grade of C-, recognizing that we are comparing a medium term trend with the latest quarter for USPS, but also recognizing that this quarter is lagging relative to the first half of 2000.

2. Quarterly Data for Business

Description

Although the measure for Similar Activities Businesses comes as close as is possible using BLS data to measuring the productivity performance of similar processes in the private sector as the four basic postal processes, it has the limitation of comparing the most recent postal quarter to a private sector trend measure. The trend to current quarter data is useful, but a comparison of quarterly USPS data with quarterly private sector data is also useful. The measure of Quarterly Data for Business accomplishes this by comparing quarterly postal productivity performance with quarterly private sector productivity performance. We compare three BLS measures to Postal Service data:

- manufacturing non-durable goods,
- non-farm business, and
- non-financial corporations.

The limitation of this measure is just the opposite of the Similar Activities in Businesses. We are achieving comparisons of the same quarterly data, but for much broader measures of private sector activity than would be ideal for examining postal productivity by process. However, the combination of the first two measures in Section B achieves a practical balance of being able to look at recent comparable performance with the private sector and performance against a medium-term benchmark with BLS productivity numbers that are more tailored to individual postal processes.

Grade

The assigned letter grade of C- reflects the following facts about fourth quarter, 2000, aggregate productivity for USPS by comparison with non-durable manufacturing activity. USPS productivity is positive for this quarter at 0.31% indeed rising somewhat from the third quarter, but it is rising for non-durables manufacturing by nearly one percent for that quarter. USPS productivity was weak for the fourth quarter by comparison with broader measures of productivity growth in the private sector such as non-farm business

3. Mature and Emerging Substitutes

Description

Although it is often done, comparing USPS productivity measures with emerging, rapid growth industries such as the Internet and email applications is not always valid. These emerging industries may well present strong substitutes for existing USPS services; however, they do not make good productivity benchmark comparisons because the Postal Service and these emerging industries are at entirely different stages of their lifecycles. The "S" curve high sales growth and high productivity growth of the emerging industries is very much due to their "newness," and will not be the same once they become mature, with growth possibilities limited to average Gross Domestic Product growth rather than the higher growth that comes from displacing older technologies.

A better productivity benchmark comparison would be one that examines mature substitutes for postal services, and then factors in the performance of emerging substitutes in the high-growth sectors in a qualitative way in assigning a grade. The mature and emerging substitutes we consider in assigning a letter grade are as follows.

Labor Productivity Measures for Mature Substitutes

- radio and television broadcasting,
- radio broadcasting stations,
- television broadcasting stations,
- household audio and video equipment,
- telephone and telegraph apparatus, and
- radio and television equipment.

Labor Productivity Measures for Emerging Substitutes

- electronic computers,
- computer terminals,
- semiconductors,
- telephone communications,
- communications equipment, and
- cable TV and other pay TV services.

Using the school report card analogy, we are measuring the productivity of one student (the USPS) to that of a peer group (mature substitutes), and against the "best in the class" (emerging substitutes). If the Postal Service drops farther and farther behind these types of emerging substitutes, rather than closing the productivity gap due to the expected drop off in productivity growth as these emerging industries mature, then the Postal Service may not be able to offset cost increases with productivity gains. The situation would be even worse if, for example, relatively mature competitive substitutes (such as telephones) suddenly have new uses that enhance the productivity of that universal delivery service at the expense of postal services (such as facsimile transmissions). For all these reasons, we believe these types of comparisons are useful and warrant a grade for USPS performance relative to these other groups.

Grade

A simple average of four emerging substitutes shows productivity growth of 5.6% for a three-year moving average ending with the year 2000. We exclude electronic computers from this calculation as being redundant with semiconductors. For seven mature substitutes, the corresponding productivity growth averages 1.1%. USPS productivity growth for the fourth quarter of 2000, converted to an annual rate, was 1.25%. A little better than mature substitutes, well behind emerging substitutes. This warrants a grade of C for the Postal Service, but a cautionary note is in order. One can expect emerging substitutes to ultimately supplant some postal services, given the wide gap in productivity growth performance.

4. Major Postal User Groups

Description

The comparison of Postal Service productivity with major postal user group productivity is a useful Report Card exercise. Postal services are an important input to these industries, so postal productivity directly affects the productivity (and costs) of postal user groups. If the productivity performance of these user groups is well above or well below postal services, it affects the degree to which they can, for example, absorb below average USPS productivity without affecting their own efficiency and profitability.

The major user group industries against which USPS productivity is measured are:

- greeting cards,
- periodicals,
- newspapers,
- catalog and mail order houses,
- commercial banks,
- stationery stores,
- news dealers and newsstands, and
- envelopes.

We measure USPS productivity performance against high/low measures for these user groups and the median, but we concentrate on the unweighted mean in assigning a letter grade.

Grade

Major user groups of postal services are experiencing on average a medium-term productivity growth trend ending with the year 2000 of 2.8% for the seven groups examined. This is more than double the 1.25% that USPS experienced in the fourth quarter of 2000 on an annualized basis. A grade of C- for the Postal Service reflects the fact that the Postal Service is lagging far behind what its largest customers—on average—expect by way of enhanced productivity within their own industries and organizations. Other things being equal, this disparity in productivity growth is contributing unwelcome pressures on costs that user groups face because of lagging USPS productivity growth.

Mr. BURTON. Thank you, Mr. Cerasale.

Mr. Campanelli.

Mr. CAMPANELLI. Good morning, Mr. Chairman and members of the committee. I appreciate the opportunity to be here and certainly was encouraged by your opening statements. My name is John Campanelli and I am president of R.R. Donnelley Logistics, which is a business unit of R.R. Donnelley and Sons Co. The company is an integral part of the U.S. direct mail marketing industry, which contributes over $1.5 trillion annually to our economy and is responsible for employing over 10 million Americans.

Both my oral and written statement focus on three basic points. First, what we see as the future mission of the U.S. Postal Service and the essential elements of postal legislative reform that will enable this new, more tightly focused mission. Second, a review of what the Postal Service can and must do under current law authority to position itself for reform and continued viability. And third, what the Postal Service should avoid doing as it moves forward.

As the largest single consolidated user of the Postal Service outside of the Federal Government, my company has a significant stake in assuring the continued viability of America's postal system. Our views on postal reform can be summarized as strongly supporting the continuation of reasonably priced universal mail service. We share our customers' and your constituents' need for a distribution channel that will service every residential and commercial address every day with predictability and reliability.

While we are obviously concerned about the future, I also want to state our serious concern about the present situation facing the Postal Service. The combination of rate increases of the past 6 months, along with the additional rate case that has been announced for filing sometime in the near future, is just unacceptable for the Postal Service's customers and will likely do more harm than good to the Postal Service bottom line.

Let me turn briefly to discuss the future mission of the Postal Service that can guide reform. First and foremost is enhancing the Postal Service's historic core competency in last-mile delivery to the home and office. The "last mile" core competence begins with the local post office, the local delivery unit goes to the home and office, and back. This kind of well-defined focus requires that the Postal Service does have the ability to change to market conditions and presents policymakers also with a threshold test question that they can use in evaluating the impact of a given provision upon reform; namely, will this provision help the Postal Service to leverage the scale and scope it currently enjoys in the "last mile" delivery network.

In addition, legislative reform also requires that we recognize the human side of the change equation. This means the postal employee and management organizations must have a meaningful place in the reform process. If reform ultimately affects employment, it also must include measures to mitigate the impact that any potential change has on employees.

Similarly, there is a serious and legitimate debate between the Postal Service and the private sector competitors on how to assure fair rules of competition between a Government agency fulfilling an important public policy goal such as universal service and a private

competitor seeking to fulfill an equally valid commercial objective. Certainly, my company does not want the Postal Service to be able to unfairly compete with the private sector. Conversely, undue restrictions upon the Postal Service can only limit consumer choice and is unworthy of reform and harmful to the continued viability of the Postal Service in providing uniform-priced universal service.

While reform is needed to achieve these goals, the Postal Service should not wait for legislative reform to realize the increased efficiency from its delivery network, as pointed out by Jerry in the Report Card. Certainly, any effort to increase the efficiency by actions permitted under current law would not eliminate the need for current reform. On the contrary, such actions will have the effect of better positioning the Postal Service to leverage the gains that reform can offer. In particular, acting now could enable the Postal Service to permanently avoid large upstream capital investments in plant and equipment that may well become stranded due to new alliances, new work-sharing opportunities, and the mix change in the mail itself in the coming years. In my written statement, I have included several ideas that are possible and, in fact, overdue under current law.

What the Postal Service should avoid doing in the future, and I fully recognize the Postal Service finds itself in difficult financial straits, the imposition of additional rate increases that are several times the rate of inflation, at a time when most businesses in the country are going through severe belt-tightening exercises, has a potential to do far more harm than good and provides no long-term benefit. More importantly, such rate increases are clearly inconsistent with the objectives of the Congress, the administration, and the private sector in revitalizing our Nation's economy. Rather than continually raising rates, the Postal Service should follow the lead of the private sector in reducing costs as rapidly as possible.

In conclusion, Mr. Chairman, the U.S. Postal Service is an integral part of our Nation's communications and commercial infrastructure. While the future may be uncertain, the economic importance of the Postal Service is unmistakably clear. You and your colleagues are to be congratulated and commended for bringing the proper attention to this issue to Congress, the administration, and to our Nation. Thank you.

[The prepared statement of Mr. Campanelli follows:]

Testimony of

John C. Campanelli
President
RR Donnelley Logistics

Before The

Committee on Government Reform
U.S. House of Representatives

Concerning
The Challenges Facing The U.S. Postal Service
And Postal Legislative Reform

Wednesday, May 16, 2001

Good morning, Mr. Chairman and Members of the Committee. My name is John Campanelli and I am President of R.R. Donnelley Logistics, which is a business unit of R.R. Donnelley & Sons Company. As you know, Mr. Chairman, R.R. Donnelley is a Fortune Most Admired company that enriches lives by connecting people with the power of words and images. We provide comprehensive and integrated communications services, including premedia, digital photography, content management, printing, Internet consulting and logistics, to help customers deliver effective and targeted communications in the right format to the right audience at the right time. Our blue chip list of more than 4,000 customers includes many of the world's major retailers, catalog merchandisers, newspapers, magazine, book and directory publishers, e-commerce companies, and corporations in the legal, mutual fund, and health care industries.

While I have a brief oral statement offer this morning, I would ask that my entire written statement be included in the record. Both my oral and written statement focus on three basic points:

- What we see as the future mission of the U.S. Postal Service and essential elements of postal legislative reform that will enable this new, more tightly-focused mission.
- A review of what the Postal Service can, should, and must do now under its current law authority to position itself for reform and continued viability.
- What the Postal Service should avoid doing as it moves forward.

A. Introduction.

I'll begin by thanking you, Mr. Chairman, for the opportunity to offer my company's views on the challenges facing the U.S. Postal Service. As the large single consolidated user of the U.S. Postal Service outside the federal government, my company has a significant stake in assuring the continued

viability of America's postal system and we greatly appreciate your leadership on this important issue. Moreover, we are an integral part of the U.S. direct marketing industry, which contributes more than $1.5 trillion annually to our economy and is responsible for employing over ten million Americans.

Before outlining our specific views on postal reform, my company wishes to acknowledge the great work being done by many of our industry's leading trade associations, including both PostCom and the Association of American Publishers, who join me on the panel this morning, as well as our colleagues at the Magazine Publishers of America, the Direct Marketing Association, the Parcel Shippers Association, and the Alliance of Non-Profit Mailers. All these associations have all made substantial contributions to the dialogue over postal reform and deserve recognition for their efforts.

In discussing postal reform, it is also important to set forth a general business philosophy in order to provide a context for our views. It can be summarized as this: R.R. Donnelley & Sons Company has a deep belief that the effective competition which governs and maximizes the operations of the private sector can and should be employed by the U.S. Postal Service to meet the legitimate public-interest need of providing reasonably-priced universal service to all Americans.

And it is reasonably-priced universal service, Mr. Chairman, that underpins our strong support for postal reform. We share our customers' need for a distribution channel that will service every residential and commercial address every day with predictability and consistency. We foresee no change to this requirement and, therefore, are concerned that the changes needed to assure the Postal Service's long-term viability remain unrealized.

Indeed, the need for reform becomes striking when one steps back and fully assesses the position of the Postal Service in a rapidly changing global economic landscape. Competitive threats to the Postal Service's financial base from traditional delivery service providers and alternative distributors of information are compounded by the arrival of new off-shore competition and new technologies which portend the loss of substantial volumes and the revenues in the near future, especially in the vital business reply and business transaction category which includes such things as business to business statements, renewal forms, and invoices.

And while we are obviously concerned about the future, I want to take a moment to state our serious concern about the present situation facing the Postal Service. The rate increases of the past five months – along with the case that has been announced for filing in the near-term – are simply unacceptable for the Postal Service's customers.

We are grateful to those in the Administration and in Congress who have heard our concerns and who are taking responsible steps to minimize the shock that these kinds of percentage increases portend.

B. **The Future Mission Of The U.S. Postal Service & Essential Reform Elements.**

In the broadest sense, preparing the USPS for the future requires a tight focus upon a two-part mission. First and foremost is enhancing the Postal Service's historic core competency in last-mile delivery in becoming the gateway to the home and office. This "Last Mile" core competence begins at the local delivery unit, goes to the home and office, and ends back at the local delivery unit.

Second, is the Postal Service offering the market a high-value understanding of mail's role in customer response management and how users of the mail can more effectively employ hard copy mailed print in their overall communications strategy.

This kind of well-defined focus will require that legislative reform empower the Postal Service to respond to changing market conditions as it offers and prices its services to its customers and as it works to achieve increased system operating efficiencies. This tightly-focused mission also requires that legislative reform further catalyze the Postal Service's leveraging of the scope and scale it currently enjoys in its "Last Mile" delivery network as a way of assuring that universal service continues into the future.

A "Last Mile" strategy by the Postal Service would require the private sector to become a more active participant in the postal value proposition. Reform should simultaneously capture the benefits that the entire postal system could gain from employing private sector capabilities for enhanced sortation and delivery between the production line and the local inbound post office. In the view of many, this vision is the heart of the "Last Mile" strategy we're advocating for the Postal Service.

The private sector is prepared to handle the additional responsibility this strategy would require. For example, we have hub sites that could be used as comailing, enhanced sortation, and processing centers that could provide new levels of efficiency in reaching high volume DDUs. Similarly, as we have planned our distribution network over the past several years, we have contemplated the need to take product from other print sources and provide it with precisely the kind of leveraged scale this vision contemplates. These competitive networks could complement the larger USPS network and provide customers with an alternative regardless, I might add, of the originating product source.

There are other components of reform that are equally important. Transforming the Postal Service into a more focused and nimble organization will be a substantial task. This requires that reform recognize the human side of the change equation.

This means that both postal employee and management organizations must have a meaningful place in the reform process. My company is respectful of the challenges that massive organizational change will present to USPS employee and management organizations. However, the rewards are also substantial – not the least of which is the continued competitiveness and relevance of the Postal Service in an economy that is increasingly global and digital. If reform occasions a displacement of employment, it must include measures to mitigate the impact that such changes may have upon the organization and its employees.

Similarly, there is a serious and legitimate debate between the Postal Service and its private sector competitors on how to assure fair rules of competition between a government agency fulfilling an important public policy goal such as universal service and a private competitor seeking to fulfill an equally valid commercial objective.

Certainly, my company does not want the Postal Service to be able to unfairly compete with the private sector. Conversely, undue restrictions upon the Postal Service can only limit consumer choice and is unworthy of reform as well as harmful to the continued viability of uniform-priced, universal service. A balance requires that the Postal Service place primary emphasis on its core business while strictly

observing current (and future) prohibitions against using monopoly revenues to support non-core and/or non-postal services and activities.

C. **Use Of Current Law Authority To Advance Reform.**

To state an obvious, but important, truth, the Postal Service should not and does not need to wait for legislated reforms to begin to realize the increased efficiencies and improved competitive position that could be derived from its delivery network. A foundation exists in the successes of past worksharing partnerships with industry to offer great opportunities for greater USPS competitiveness. The future is NOW for building upon these past successes, and for redefining and enhancing the Postal Service's "Last Mile" capabilities!

Moving ahead expeditiously to remove barriers to increasing efficiency would certainly not obviate the need for nor be inconsistent with legislated structural reform. To the contrary, acting now will have the effect of better positioning the Postal Service to leverage the gains that reform can offer. Immediate action has the potential of substantially enhancing the value of the Postal Service and its local post office network. Acting now could enable the Postal Service to avoid large upstream capital investments in plant and equipment that may well become stranded as innovative alliances are developed, as worksharing grows, and as the mix of mail changes in coming years.

Without getting into too much detail today, let me provide a few examples of enhancements that are possible now and are already overdue:

- The Postal Service should explore with its customers the desirability of expanding worksharing by specifically aligning discounts with the value created by the worksharing. Currently, incentives do not match with cost savings generated. Postal rate incentives to use the most efficient forms of containers and deepest entry into the system should be reflected in combined rates that are keyed to the most efficient forms of sortation and entry in combination. In that way, mailers get the most accurate price signal and efficiencies of scale are properly rewarded.

- Current rules governing sortation, containerization and acceptance scheduling need to be re-examined. In the age of automated delivery sequencing and computerized invoicing, multiple classes of mail can be combined for the purpose of achieving densities that are a precondition to dropship and presort discounts.

- Mixed mail pallets could also provide additional opportunities to both commercial shippers and the Postal Service to control costs by maximizing cube and weight loads when transporting mail.

- New services that have the potential to add value to existing destination delivery unit (DDU) dropship discounts, such as creating a product return rate that relies on reverse routing by logistics companies, needs to be moved to the front burner.

- The Postal Service must and can readily take steps to reduce the red tape that entangle the use of the mails in general and particularly those mailers who seek to maximize the Postal Service's

last mile service. The transmission of information about the mail in electronic formats is not only faster and cheaper for both the Postal Service and shippers, but is more reliable at lower cost than the current paper systems.

- Lastly, the Postal Service must, in cooperation with shippers, establish a real-time, web-based communications system that permits consistency in delivery so that shippers and mailers can organize their schedules to assure that mail and products get to the consumer when the consumer expects them. The Postal Service must also establish external and objective performance measurements for all types of mail.

The Postal Service need not delay these kinds of improvements pending the passage of comprehensive legislative reform. The classification provisions of existing law are available and should be employed to the fullest extent practicable, as should the existing administrative rules encouraging experimental services. Indeed, Mr. Chairman, my company has worked closed over the past several years with both Congressman McHugh and Congressman Davis on clarifying the view from Congress that the Postal Service has the authority under current law to expand its use of private sector cost reduction and service quality capabilities through the use of negotiated service agreements (NSAs).

D. **What The Postal Service Should Avoid Doing In The Future.**

Having shared some thoughts on how the Postal Service can build on its strengths and better position itself for the future, let me mention some possible USPS initiatives that I believe would be counterproductive to its ongoing success.

As I mentioned earlier, we were very troubled with the Board of Governors decision last week to overrule the Postal Rate Commission's recommended rate increases that were implemented in January and impose another round of increases in July. What changes our concern to alarm are the statements that the Postal Service may well file a new rate case this July, which would mean yet another round of rate increases in the spring of 2002.

While I recognize that the Postal Service finds itself in difficult financial straits, the imposition of a sequence of serial rate increases that are several times the rate of inflation at a time when every business in the country is going through a severe belt tightening exercise has the potential to do far more short and long-term harm than good to the Service's bottom line. More importantly, these rate increases are entirely inconsistent with the policies and objectives of the Congress, the Administration, and the private sector to revitalize the economy. Rather than continually raise rates, the Postal Service should follow the lead of the private sector in reducing costs as rapidly as possible.

Of more particular concern to those of us in the logistics business is the modification decision to cut parcel post dropship discounts incentives for both sectional center and destination unit delivery. Although the law of unintended consequences may be the culprit here, this decrease in the economic value of dropshipping sends the wrong signal to parcel shippers and transporters and we urge the Governors to immediately to reverse this decision. If left unchanged, these inconsistent actions will cause the Postal Service's private industry partners to slow or stop their investment in the infrastructure and people necessary to take on an increasing role in processing and sortation.

Finally, recent press reports reveal that on the heels of the Board of Governor's announcement of more rate increases, postal officials stated that the door is still open to service cuts, including the curtailment of Saturday delivery. The Postal Service is the only delivery entity that has a regular schedule of Saturday delivery. Abandoning this service is, to say the least, not the best option for an entity whose strength lies in its everyday, everywhere "Last Mile" delivery network.

E. **Conclusion.**

The U.S. Postal Service is an integral part of our nation's communications and commercial infrastructure. Preservation of Universal Service insures that a single, unified communication network continues to bind every segment of our population, regardless of geographic location or socio-economic standing. A host of technological trends, domestic and foreign competition, and challenges arising out of the USPS' 30 year-old governing charter mean that meaningful reform must occur soon if the USPS is to remain viable in the competitive landscape.

Mr. Chairman, you and your colleagues are to be congratulated for giving this issue the attention it deserves and we look forward to working with you in advancing meaningful reform. That completes my prepared statement. I would be happy to answer any questions you or your colleagues may have.

NALC NEWS

National Association of Letter Carriers, AFL-CIO • 100 Indiana Ave., N.W., Washington, D.C. 20001

FOR IMMEDIATE RELEASE
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Sombrotto Urges Speedy Action On Postal Reform Legislation

WASHINGTON — The head of the 315,000-member National Association of Letter Carriers urged Congress today to quickly enact postal reform legislation in order to bring financial stability the U.S. Postal Service and allow it to continue as a key communications link for all Americans.

NALC President Vincent R. Sombrotto, in testimony to a House Government Reform Committee hearing, said the union has worked for more than six years with Rep. John McHugh (R-NY) and other members of the committee on H.R. 22, McHugh's postal reform legislation.

"I fear that if we do not act soon, even the far-reaching goals envisioned in H.R. 22 will not be enough to put the Postal Service on a stable foundation," Sombrotto said, noting the advent of Internet and other advanced electronic communication and intense global competition within the delivery service marketplace.

"If we are to continue to provide the high level of service the American public has come to expect from us, then we must take action and we must take it soon," he said.

Sombrotto said the Postal Service needs a statutory framework that will enable it to find new ways of generating revenue, including negotiated service agreements and creating joint ventures with private companies.

He dismissed recent public overtures by the Postal Service for consideration of an end to six-day delivery saying it would only make the Postal Service less attractive to customers.

Instead, he said, the Postal Service needs to have more timely delivery as well as innovative services and products that meet customers' changing needs, and for businesses, flexible and market-driven pricing, plus accurate and timely information about the progress of their mailings and perhaps new logistical and inventory control services.

Sombrotto cautioned the panel that any reform legislation must not undermine the collective bargaining rights of postal employees, saying the current right to third-party binding arbitration when contract negotiations reach an impasse is essential to future labor-management relations.

He added that suggestions that third-party arbitration be exchanged for the right to strike "are a non-starter for us."

Sombrotto said models cited by proponents of such a trade, such as the Railway Labor Act, "would drastically undermine the rights of all postal employees."

"Binding arbitration enables our members to do their job and, when management is not willing to achieve a negotiated settlement, provides letter carriers with a fair way to get a fair contract for their work," Sombrotto said.

He said the NALC "will not support any postal reform bill that includes erosion of collective bargaining rights and, specifically, third-party arbitration." Without binding arbitration, he said, there would be no pressure on management to negotiate fairly and constructively.

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Mr. BURTON. Thank you, Mr. Campanelli.

Mr. Estes.

Mr. ESTES. Good morning, Mr. Chairman. Thank you for the opportunity to address you and the members of the committee. Our written statement tells you who Main Street is and what it is about. Quite briefly, we represent consumers, business and trade publishers, religious publishers, technology and communications companies, large and small newspapers, and financial institutions. These groups yesterday placed in the "Washington Post" a statement of what they believe postal reform should do and what postal policy should be. With your permission, I would like to offer that ad as a part of the record for the committee.

Mr. BURTON. Without objection. I would like to see that as well.

Mr. ESTES. Mr. Chairman, I would like to make five points. First, it is really not our intention to rehash Main Street views on postal reform as those were embodied in H.R. 22. We briefly mentioned our views with respect to H.R. 22 in order to orient the full committee about where we were coming from and why we felt from a policy standpoint many of the provisions, but not all, of that bill were not in our best interest nor represented a viable approach for the Postal Service. We recognize that there was disagreement. There were those that embraced that bill and there were some, like us, that did not.

But rather than go over that again, we really welcome your opportunity, the opportunity extended to us to look at a new approach. That will involve H.R. 22, we realize that, and it will involve other things. So we are looking forward to that, and we thank you for that opportunity.

Second, Mr. Chairman, the Postal Service problems today we think are really in two facets. There is developing a long-term solution which is critical, I think we all agree to that, and there is also the necessity to develop a short-term temporary fix. I would cover the long-term approach in a second. But with respect to the short-term approach, we think, Mr. Chairman, that the committee, you, should rely heavily on the efforts of the General Accounting Office initiatives, also on frequent consultation with GAO by this committee coupled with aggressive oversight of the Postal Service by this committee.

The short-term goals we believe are first. Imperatively and critically look at the facts. Since 1995 through 2000, Postal Service revenues and Postal Service volume has increased. It has been a steady trend. That is a good, solid fact. We are faced with something now, how serious is that that we are faced with now, and how much out of synch is that with the overall trend for the last 5 years of the service, we have to get to the bottom of that and we have to look at it. It is not just enough to look at a few facts in isolation in our judgment.

A second point on the short-term solution, Mr. Chairman, we think it is essential to insist on a limited mission for the Postal Service now, this is on a short-term fix, so we can get our arms around this and really find out what is going on over there from the standpoint of financial management and cost control.

And last, we think immediate improvements are essential for financial forecast. The financial forecasting is not that good over

there and we think something has to be done. GAO has recognized that, too.

Our third point, Mr. Chairman, you asked for things that jump out at us. Three things do.

Labor costs. We have stressed at length in our statement about labor costs and how we think they should be addressed and some of the problems that the union and the Service faces. Historically, the unions gave up the right to strike. That is a big thing for a union to give up. In return for that, they got compulsory arbitration. Is that a good approach or not? But there is quid pro quo there and a tradeoff. And that was done knowledgeably with an effort to try and find a solution to the labor problems back in 1965.

Mr. Chairman, another thing we set out as a major challenge is rate-setting.

And third, something has to be done we think about management compensation; that is high level, top level compensation at the Service. As you said and as others on the committee have said, this is one of the biggest organizations in the world. And from a comparability standpoint, if we are going to attract qualified people that have the experience that is needed, we have to look at the compensation package that is being extended. We think it is inadequate.

Mr. Chairman, we have called for a Presidential commission to assist you with respect to developing a national reform program. We applauded your effort in your letter to the President. We think you probably did not have a commission in mind. We hope you would rethink that and look at it. We think it will be helpful.

Finally, Mr. Chairman, my fifth point is we are here to help. We want to be a part of the team and we want to find a solution. It is critical for all of us. Thank you.

[The prepared statement of Mr. Estes follows:]

STATEMENT OF JOHN T. ESTES
EXECUTIVE DIRECTOR, MAIN STREET COALITION FOR POSTAL FAIRNESS
BEFORE
THE COMMITTEE ON GOVERNMENT REFORM & OVERSIGHT
U.S. HOUSE OF REPRESENTATIVES
MAY 16, 2001

STATEMENT
ON BEHALF OF THE MAIN STREET COALITION
FOR POSTAL FAIRNESS

May 16, 2001

Chairman Burton, members of the Committee on Government Reform, thank you for the opportunity to provide testimony on the challenges facing the United States Postal Service (USPS). My name is John T. Estes and I am executive director of the Main Street Coalition for Postal Fairness (Main Street). Main Street was formed in response to a growing tendency by the Postal Service to favor large volume mailers over its regular postal customers. Main Street members represent a variety of interests, including those of the individual First Class mailers, banks, technology and communications companies, religious mailers, consumers and other nonprofit groups, as well as business and trade publications, and large and small newspapers. According to the Postal Service, Main Street members represent roughly 40 percent of the annual circulation of the Postal Service. In my testimony, I will outline the impact those challenges will have on the members of Main Street and explain what we think should be done.

The management, efficiency and an appropriately defined mission of the USPS are crucial to the operations of all Main Street members. So right up front let me make it clear that although there may be some who want to see the Service sink, but do not put us in that boat.

We have noted in an Attachment to this paper that if the reliability of the mail system is impaired, either suddenly or gradually, there will be not only a major political crisis, but also a major economic crisis. It is in the public interest and it is in our interest to prevent this from happening.

I have appeared before the former Subcommittee on the Postal Service in the 105th and in the 106th Congress in hearings on H.R. 3717 and H.R 22, respectively. We opposed some of the main principles of those bills not because we oppose postal reform. We do not. Main Street and its members are supporters of the Postal Service and we understand the need for postal reform. We just think the general approach that was urged in those bills would take the Service down the wrong path.

The record is clear on the specific reasons for our opposition, but let me summarize the main points we stressed in urging rejection of those proposals. In our view, those bills would have :

- disproportionately increased the cost of the First Class stamp,
- favored large mailers over small,
- disregarded the views of consumers and given USPS increased authority to set discriminatory prices for postal products,
- created a price cap system that would not have worked, according to most of the economists who appeared before the committee,
- continued to encourage unfair competition by a government agency with the private sector, and
- failed to provide effective oversight of USPS rates and operations.

I mentioned my earlier appearances before the former Postal Subcommittee because of the impact the legislation last year, had it been enacted, would have had in relation to the action last week by the USPS in raising postal prices. The action last week by the USPS Board of Governors in overturning the recommendations of the independent Postal Rate Commission and barging ahead with rejected rate increases raises serious questions about the wisdom of providing the USPS with rate setting flexibility and expanded operational autonomy as proposed in that legislation. In addition, the failure to advance the legislative proposals last year

followed by a series of missed financial forecasts and panicky USPS press releases threatening reduced service this year show that the crisis at the Postal Service is a crisis in management. These events may result in a chorus of "I told your so" by the proponents of the rejected legislation. Ironically, the action by the Board of Governors in pressing ahead with another $1 billion rate increase this year can justify the same "I told you so" chorus from the opponents of that legislation. The action of the Governors is a clear example of what would happen if "rate flexibility" were the norm and restraints on the Postal Service's ability to unilaterally raise rates were relaxed.

It appears to us that the lesson to be learned from this is that a fresh approach for postal reform is required.

We should point out that we do not appear here to push for legislation rolling back the recent rate increases, even though we disagree with them from both a process and substantive standpoint. The record shows that the PRC offered to consider additional evidence from the USPS to justify the rejected rates. The Postal Service, however, did not seek to reopen the record and provide the data and instead proceeded unilaterally to increase the rates.

That action was critical. Some in our coalition, such as the business to business periodicals industry, have already absorbed postal rate increases totaling 60% in this past decade. The religious press periodicals, which carry little or no advertising, typically spend 20% to 22% of their budgets on postage, which means that for them, as well, any increase is substantial. In addition, those First Class mailers that mail heavier weighted mail are particularly damaged by this action. For example, the banking industry, also one of our members, estimates that the new increased rate after the first ounce for First Class mail will cost it an additional $52 million dollars a year. Based on 1999 data, the last available, total postage costs for that industry were $2.6 billion dollars a year!

The problems at the Postal Service, or challenges, as you call them, Mr. Chairman, involve both process and procedure as well as management. The process and procedural challenges can be addressed by legislation. Unfortunately, the management problems cannot. They must be addressed by a change in the attitude with a renewed focus on cost management and less on pricing. Raising rates instead of controlling costs is exactly what just happened several weeks ago, and that is exactly the approach that HR 3717 and HR 22 would not have discouraged

There is little if any doubt that the reform issue should be addressed. The question is how to do that expeditiously and effectively.

A PRESIDENTIAL REFORM COMMISSION

Mr. Chairman, you, the USPS Board of Governors and others have urged the Administration to get involved now with this problem. As you said in your April 23, 2001 letter to the President:

> "Clearly change is needed and your [the President's] leadership in this area would be critical to the enactment of any meaningful reforms. I am confident that the Administration working with the Congress, the Postal Service and its various stakeholders can develop a long-term solution without having to resort to increasing rates or reducing the quality or affordability of universal mail service."

Although the USPS disagreed with you with respect to increasing rates, the thrust of your remarks seeking Administration involvement is right on target. The situation at the Postal Service is a national problem and national leadership is appropriate and needed in developing a solution. In our judgment, this could be most effectively accomplished by establishing a Presidential Postal Reform Commission to develop recommendations for the Administration to submit to the Congress. Set forth in the Attachment is the basis for this proposal and some of the issues which we would hope the commission would explore.

This is not a new proposal by Main Street. We first advanced the commission concept six years ago in testimony on postal issues before a Senate Committee. As a result, we are faced with a situation where the most fundamental issue of postal reform, one that a commission should consider before any other, has not yet even been addressed, much less resolved. That question is: *What do we want the Postal Service to be?* Over these many years, as you know, there has developed a wide spread belief among many that unless USPS problems are addressed, the Postal Service could indeed be headed for disaster. And yet we have never seriously attempted to resolve this basic public interest question: exactly what does the American public, the mailing community - Postal Service stakeholders, and the Congress want the Postal Service to be?

Assessing the needs, strengths, weaknesses and future of the USPS demands more than can be obtained or expected from busy and overworked congressional staff members, however competent or from the ad hoc testimony of witnesses who have a vested interest or are otherwise engaged in postal matters. A commission of independent and nonpartisan individuals would examine why the USPS is foundering. The commission could examine whether the problems of the Postal Service are due to rapidly changing communications technology, or are due to inadequate management, or whether there are other reasons for the inability of the postal system to meet expectations. In this regard, one area we find exceptionally bothersome is the inadequacy of postal management compensation when compared with that provided in the private sector for comparable positions of responsibility.

The Presidential commission approach worked in 1970 and it can work again. Some may say this is merely a delaying tactic. We do not believe so. Whatever legitimate concerns may exist about delay can be met by setting a reasonable deadline for reporting proposals to the Congress during the term of this

Congress. This approach would set in motion a means of developing and recommending, initially outside the political arena, a national postal reform policy and jump starting the legislative process by providing the Congress with specific nonpartisan and independent proposals.

The foregoing represents a proposal to address the longer range reform difficulties facing the Postal Service. Meanwhile immediate solutions should be addressed.

BASIC PRINCIPLES OF POSTAL POLICY

In assessing the challenges facing the Postal Service, whether for the longer term, as discussed above, or for the short term, we believe certain core principles must be observed:

- the Postal Service should remain a public service available to all Americans;
- it should not favor or discriminate among Americans,
- it should be required to operate as efficiently as possible *and held accountable* if those standards are not met;
- the goal of the Postal Service should be to fulfill its primary mission of serving as a delivery system for the nation's correspondence, periodicals, newspapers, etc. within a system that efficiently accesses every village, city and state in the country,
- it should have a primary purpose of binding the nation together as called for under current law— it should not divide the nation by unrestricted initiation of new competitive ventures with the private sector, and by extending favored treatment to some mailers and not to others.

These core principles should govern the evaluation of a number of key issues or challenges now facing the USPS. We have set out in the Attachment some Main

Street positions and views on critical Postal Service challenges, including cost management, cost control, competition and universal mail service. In addition we would like to highlight, the following:

LABOR COSTS

The current form of compulsory arbitration between management and labor in resolving disputes over terms and conditions of employment appears to be set in political concrete and apparently for that reason cannot realistically be scrapped or substantially revised as long as labor is bound by a no-strike obligation. Removing the ban on strikes does not appear to be a rational alternative. Because roughly 80% of USPS costs are labor related, it is clear that postal rates and postal service efficiency will to a great extent mirror the increase or decrease in those costs. One option, and there may be others, is to substantially reduce the size of the workforce through a variety of means, including, but not limited to hiring freezes, contracting out some work and early employee retirement programs. In addition, and perhaps most importantly, productivity must be substantially increased through automation. Despite the ability of other industries to accomplish this goal, the employment census at the Postal Service continues to rise, and costly automation programs are apparently not resulting in significant productivity increases. Of all the management problems confronting the USPS, this may be the most critical. Solving it will mean a giant step forward in returning sound, respected management to the Service.

RATE SETTING

Another issue which the Postal Service believes is a challenge to its effectiveness and which was addressed in the aforementioned legislation involves the process by which rates are set. The Postal Service and some others have

proposed replacing the current cost of service rate setting with price cap rare setting.. Under both systems, the cost of service is a key ingredient in setting postal rates. If costs are not recovered, the systems won't work. A major difference is that under price caps, which the Postal Service favors, it would from time to time be granted significant flexibility it does not now have in setting postal rates, an issue we discussed above. The Service also contends the current cost of service approach is cumbersome and time consuming. The facts are that rate cases are almost always decided in at least eight months, which is two months or 20% ahead of the ten month statutory limit. That time could probably be shortened significantly by improvements in the manner in which the Postal Service transmits data to the Postal Rate Commission as well as PRC authority, which it does not now have, to audit cost, productivity, volume and the annual financial reports of the Postal Service. In addressing this challenge the inquiry should be into what and should be done to expedite the existing process, and to give the Postal Service more flexibility, where needed, without sacrificing rate payer protection. Finding that solution would avoid abandoning a fair, open and predicable procedure in favor of an untested price cap approach for postal rate setting.

In summary, Main Street is deeply concerned about the challenges facing the Postal Service that could if not addressed not only threaten the Service, but also the industries and organizations we represent. We pledge our cooperation to work with you and stakeholders in the postal community to resolve these immensely important problems We also urge you to consider carefully a Presidential Commission recommendation to the Administration to supplement the current and temporary action now undertaken by the Comptroller General of the United States in placing the Service on the General Accounting Office high-risk list. That will help in the short term, but as you have pointed out it is the future of the Postal Service that is of greatest concern.

ATTACHMENT

THE NEED FOR A PRESIDENTIAL COMMISSION ON POSTAL REFORM
By The Main Street Coalition for Postal Fairness

The United States Postal Service (USPS) has strayed from its mission of providing universal mail service at reasonable and nondiscriminatory rates. As a result, the USPS has created fundamental problems for itself and the American public by not focusing on cost management and cost containment. Unless these concerns are addressed, the nation's mail service will be placed in jeopardy.

The country urgently needs a non-partisan, presidentially-appointed postal reform commission to advise the administration on developing a national postal policy. Such a commission must explore the public policy questions of what the Postal Service's mission is, what it should be and how it should be reformed. As it develops this new national postal policy, the commission must:

- Refocus the Postal Service on cost management and containment.
- Ensure that the Postal Service stays focused primarily on its mission of delivering the mail.
- Maintain universal postal service at reasonable and nondiscriminatory rates.

Why a presidential commission? Assessing the needs, strengths, and weaknesses of the USPS demands the objectivity and experience of executives from the private sector. These private sector representatives must find out why the USPS is floundering. A commission must determine whether the problem is due to rapidly changing communications technology, to inadequate management personnel or due to other reasons. Finally, it must recommend a solution.

If the reliability of the mail system is impaired, either suddenly or gradually, there will be not only a major political crisis, but also a major economic crisis. It is in the public interest to move promptly to prevent this from happening.

The Main Street Coalition is a nonprofit corporation representing approximately 40 percent of the Postal Service's volume. Member companies and associations include the American Bankers Association, American Business Media, Computer and Communications Industry Assn., Cahners Publishing Co., Associated Church Press, Greeting Card Association, Hallmark Cards, Inc., National Consumers League, National Rural Electric Cooperative Association, Newspaper Association of America and the Tribune Company.

May 2001

I. Cost Management and Cost Containment

A healthy Postal Service—one with its costs under control—is crucial to the future of the mailing community. Unfortunately, that description hardly fits the Postal Service today. The Postal Service has been unable to rein in its labor costs regardless of the amount of money and effort devoted to automation. Labor costs currently represent about 78 percent of total USPS costs. That is $54 to $55 billion of its roughly $70 billion operating budget.

Even the Postal Service Board of Governors has recognized that "business as usual" in the labor-intensive operations that characterize postal costs cannot continue. The Postal Reorganization Act mandates compulsory arbitration when labor and management cannot agree after collective bargaining reaches an impasse. The Board's March 2, 2001, letter to the President in part stated: "The Act . . . has often placed some 80 percent of our [USPS] costs in the hands of a third-party arbitrator with neither understanding nor responsibility for our role and mission."

In February of this year the Postal Service's CFO advised its Board of Governors that the USPS net loss for this fiscal year could reach $2 to $3 billion. This report raises the question "How could USPS project a FY01 surplus of $150 million in September 2000 and then a FY01 deficit of up to $3 billion only months later?" This abrupt turn-around raises serious questions about the Postal Service's ability to manage costs, particularly when the Postal Service's response is to seek yet another major rate increase this year.

The General Accounting Office has stated that unless the Postal Service's problems are addressed, we can expect serious consequences in the future. The fact that for the past six years, the House Government Reform Committee has been unable to reach a consensus and report out postal reform legislation shows that a bipartisan top-level commission is urgently needed. This is particularly true since, for the first time since the 1970 postal reorganization, there is no House oversight subcommittee with postal responsibility and jurisdiction.

In the last Congress, a well-intentioned but fatally defective postal "reform" bill (HR 22) failed to receive solid support on Capitol Hill. One of the most touted features of that legislation was the shift of ultimate rate-setting authority from the Postal Rate Commission to the Postal Service. That shift would have done nothing to control costs, or to resolve the difficulties with the labor arbitration mandate facing the Postal Service. However, it would have exposed the Postal Service's smaller customers to escalating rates, without any protection from an intervening regulatory body such as the Rate Commission. Such protection is important not only to First Class business users of the postal system, but also to the "Aunt Minnie" users of the postal system, as well as the vast majority of periodical titles, which have long been the target of adverse changes in periodical rate design.

The Example of Periodicals

Most of the country's magazines are totally dependent upon the Postal Service for delivery of their product to subscribers. This is particularly true for small circulation business-to-business, nonprofit, religious, rural, educational and scientific publications. These are the publications that give American consumers and companies the information that our nation's industry and commerce needs in order to function. These publications are rarely sold on newsstands and, except in very rare cases, cannot be delivered by alternate delivery companies.

Postage is one of the largest expenses facing publishers, and USPS' cost of processing periodicals is increasing *more* rapidly than *both* inflation and its own labor costs. Publishers cannot continue to pay for postal inefficiencies in an era in which competition for revenue is increasing. **If postal costs and rates are not brought under control, a significant number of these periodicals will cease publication, even if the economy remains healthy.**

The medical, automotive and agricultural industries would be particularly hard hit. So would religious publications. Religious organizations already have cut back the frequency and size of their periodicals because of extraordinary postal rate increases. While it is possible that some publications could be distributed electronically over the Internet, that is true for very few. Finally, start up publications in these important fields would be severely reduced because of the possible rate increase of 30 percent they would face next year (in addition to last January's increase of 10%+). Periodicals rates have increased 60 percent in the past decade. Something must be done.

Only a Presidential commission with the status and stature of the 1970 Kappel Commission will be able to divorce the true needs of the Postal Service from the politics that impede serious legislation. Only a commission as eminent as the Kappel Commission would have the authority and respect to be able to propose the changes that are needed to bring the Postal Service successfully into the 21st century.

II. Straying from the Postal Mission
(a) Competing with the Private Sector

The United State Postal Service has become quite bold in its efforts to use its $70 billion in revenue to leverage its monopoly into other markets and to "grow" its services beyond its mandate. **Monopoly abuses by government entities are no less repugnant to a free marketplace than like abuses by private sector companies. Indeed, they may be worse.**

Recently the USPS announced and implemented several contractual and partnership agreements with technology, e-commerce, and banking firms in order to launch a suite of USPS electronic financial services. The Postal Service also has announced plans to assign e-mail addresses to all Americans or all physical addresses, to take control of the ".us" domain, and to deploy computer kiosks in all post offices for sending and retrieving e-mail.

These are rapidly emerging areas of e-commerce with hundreds of small entrepreneurial companies seeking to develop new products to meet the demand of the e-commerce marketplace. The last thing the industry needs is a federal government agency, with $70 billion in revenue, injecting cross-subsidized government-financed products into this market in an effort to "grow" its revenues. The Postal Service is immune from the antitrust laws, and its electronic ventures are subject to *no regulatory oversight whatsoever,* so long as they do not deal with hard-copy "mail."

Today we find USPS trying to turn itself into an Internet portal for e-commerce services—no different than Yahoo!, American Online, or Excite. In fact, USPS is explicitly describing itself this way in internal communications with its employees despite the fact that it is a government agency. We hope that a presidentially-appointed postal commission would agree with Main Street that the Postal Service, as a government agency, should not engage in non-postal activities and should not operate in the private sector e-commerce market. Moreover, we would hope that such a commission would prevent the Postal Service from continuing to inject itself into competition with established, competitive commercial industries.

Notwithstanding the legal, policy and macroeconomics issues raised by these activities, it is fundamentally unfair for the American taxpayer and the average citizen buying a stamp to be forced to become an unwitting financial underwriter for the U.S. Government's efforts to launch competitive ventures in commercial business against the private sector. **The USPS is funding its new enterprises with revenue derived from its statutorily imposed postal monopoly**. Every U.S. citizen and company that buys a 34-cent stamp is actually a financial partner for the agency's commercial market ventures. Astonishingly, in some cases, the companies would be financing their own competition!

While the Postal Service is undertaking these new ventures by simply reinterpreting its current statutory authority, the Postal Service and some Members of Congress actually sought

(unsuccessfully) to codify USPS' *ultra vires* activities with new and explicit statutory authority. In the 106th Congress, H.R. 22 (the Postal Service Modernization Act), contained a provision for a "private law corporation." This corporation would be a subsidiary of the Postal Service that could engage in "non-postal products and service" businesses in the private marketplace. It could have done anything it wanted, including buying computer companies, telephone companies, and even professional sports franchises.

(b) Favored Treatment

The Postal Service has compromised its mission by participating in questionable speculative ventures in the private sector and in extending discriminatory and favored treatment to certain segments of the public, to the detriment of others, just to grow its government revenues.

A Presidential commission should recommend that a halt be called to these activities by the Postal Service unless it can be demonstrated they are consistent with its core mission. Alternately, the commission could recommend that the USPS' mission be radically altered. In any case, the Commission should include an audit of Postal Service practices and activities and decide whether they are consistent with the obligation of furnishing the public with efficient and universal nondiscriminatory postal service. We believe that the commission will conclude that the Postal Service has strayed far from its mission and has lost sight of the equitable and nondiscriminatory nature of that mission.

We hope that the Presidential commission will look at the Postal Service with a critical eye. We have—and what we see is alarming. Instead of focusing on delivering mail, the Postal Service has focused on diversions like selling phone cards and electronic debit cards, and creating credit card fulfillment operations, and electronic e-payment businesses. **Time after time the Postal Service has mounted new operations in direct competition with the private sector and in areas where there has been no market failure.** The Postal Service's advertising budget is one of the largest in the country, even though eighty percent of its income comes from monopoly mail.

The roots of this excess go back more than twenty years to an era when the Postal Service started consciously using First-Class mail revenues to cross-subsidize third-class (advertising) mail. This was done in an effort to pull advertising dollars out of the print and other advertising media in order to grow third class volumes at the Postal Service.

Indeed, in its 1997 Marketing Plans, the Postal Service specifically noted that one of its goals was to "create the platform for moving substantial revenues from pre-printed newspaper inserts to mail." The federal government has no business consciously attempting to move revenues from the private sector to the public sector—whether those private sector revenues come from newspapers, magazines, or e-commerce companies.

Just recently, third class volume overtook First-Class volumes, and now such unsolicited advertising mail is the biggest item the Postal Service delivers.

Nowhere has the Postal Service ever reported to Congress or the President that it had changed its core mission, or that it now viewed itself as being in the advertising business and in competition with newspapers and other media. We hope the commission would recommend that the Postal Service has no business in selecting favorites from the mailing community and penalizing other businesses. Clearly such conduct by a federal agency is not in the best interests of the country. The Postal Service, we remind the reader, is a federal government agency, not a private company. It is in the mail business, not the advertising business.

The Presidential commission should look carefully at this aggressive policy of the Postal Service. The commission might very well conclude that such activity may be perfectly appropriate for a private company competing in the private sector without monopoly privilege or status, but is totally inappropriate for a government agency with a monopoly over 80 percent of its roughly 70 billion dollar annual revenue.

III. Universal Mail Service at Reasonable and Non-Discriminatory Rates

Finally, and most importantly, the most deeply-rooted concepts in the history of our postal system are the reliable, secure delivery of individual citizens' and companies' personal and business letters and delivery to all parts of the Nation at uniform rates. Both have survived the advent of the telegraph, the telephone, and the fax machine - and can and should survive the coming of the Internet as well. Universal service allows all Americans to send and receive both information and objects readily, regardless of where they reside or do business.

A Presidential postal reform commission should strive to understand the need and purpose for universal service and then ask: how can we insure that this basic, universal service remains affordable and reliable? And what can we do to make it more useful and attractive to present and future generations of users?

The role First-Class letter mail plays in American society must be understood if rational recommendations are to be made about the future of the Postal Service. A Presidential commission examining the future of letter mail must consider the public values that mail serves.

While millions of other First-Class letters are sent daily throughout the nation by small businesses and consumers, not everything Americans send each other by First-Class mail is "pure information" that might just as well be e-mailed to the recipient. For instance, some mail, such as greeting cards, are much more. Greeting cards incorporate art, cultural symbolism, and a personal message into one envelope. This is typical of what the Postal Reorganization Act means by describing the Postal Service's assignment as "bind [ing] the

Nation together through the personal, educational literary, and business correspondence of the people."

This is mail volume that the Postal Service can and should keep—even if bulk-entered bills, statements, and other letter mail should migrate in large quantities to electronic channels. How it can be kept is a question to which the Presidential commission should pay serious attention.

The fact that First-Class mail serves social and cultural "nation-binding" functions as well as just conveying information is a perfect departure point for the commission to probe the question of universal service as an indispensable public service. Where the basic rationale for the class of mail is communication, whether from consumers or business, our policy choice historically has been in favor of First Class price uniformity for an individual letter and it should stay that way. **It should not cost a citizen more to mail a letter across the country than across town.**

The same reasoning has and should continue to govern delivery to remote or thinly-populated regions. While there are differences between, for example, city and rural letter carrier operations, neither the rate nor the frequency of delivery has been allowed to vary on the basis of delivery address. A Presidential commission should not lose sight of these principles.

The importance of the public interest and social values served by the tradition of reasonably priced universal service cannot be overlooked by a Presidential commission. For that reason, such a commission should take a broad approach to social costs, economies associated with mail volumes and a universal service network and "efficiency." Its investigations should be required to cover not just the economic but also the social and cultural benefits made possible by reliable, affordably priced letter mail service for individual citizens, provided on a basis of national uniformity and universal availability.

Please contact Main Street Executive Director Jack Estes at Tel:(202) 220-9798;Fax (202)-289-7675 with questions or for more information.

MAILERS COUNCIL

REPORT CARD

Postal Service Productivity

Fiscal Year 2001

SECTION A— USPS Internal Productivity

CATEGORY	PRODUCTIVITY GRADE FIRST QUARTER	SECOND QUARTER	THIRD QUARTER	FORTH QUARTER	FINAL GRADE
Revenue per Work Hour	D+				
Volume per Work Hour	D+				
Unit Labor Costs	C				
Mail Processing	B				
Delivery	C-				
Retail Services	C				

SECTION B— Private Sector Benchmark Comparison

CATEGORY	PRODUCTIVITY GRADE FIRST QUARTER	SECOND QUARTER	THIRD QUARTER	FORTH QUARTER	FINAL GRADE
Similar Activities	C-				
Non-Durable Manufacturing	C-				
Mature and Emerging Substitutes	C				
Major Postal User Groups	C-				

EXPLANATION OF MARKING SYSTEM

A-Superior
B-Above Average
C-Average
D-Below Average
F-Failing

Mr. BURTON. Thank you, Mr. Estes.

Mr. Del Polito.

Mr. DEL POLITO. Mr. Chairman, thank you very much for the privilege and the opportunity to appear before you today on the issue of postal reform. You have my written statement and I would just like to add a few thoughts to it.

First of all, I have got to tell you I am delighted they took down that report card. The last time I saw a report card that bad was the one I had to turn into my parents in my senior year in high school. It just evoked bad memories.

I speak in my testimony about the incentives that underlie the Postal Service, and I characterize them as misdirected. Now I deliberately chose not to characterize them as good or bad because such value judgments really do not work, do not matter. The only issue is whether or not the incentives that are laid before people get them where they need to go and get them to do the kinds of things that they should be doing. Clearly, when you take a look at the incentives that underlie today's postal system, which, incidentally, stem from the Postal Reorganization Act itself, they are not working for an institution that now must find its way within a competitive environment.

So, in other words, if you want to change the way the Service's stewards behave, you have got to do something to change the incentives that underlie postal law. Because if you do anything less than that, you will fail to achieve meaningful postal reform. Getting the incentives right is going to be the key to postal reform.

Now around the time of my son's first birthday, he began to show signs of his autism. That started our family down a long and arduous road for his rehabilitation. And much of the work that we ended up having to do with him was based on a behavioral training method that clearly laid out the rewards and the consequences of his responses to various learning tasks. Now he is 11 and he is doing fine. He has learned extremely well that there are rewards for working hard and there are consequences for slacking off. When he does well he earns a Nintendo time. When he goofs off he loses his Nintendo privileges.

Clearly, a child who began life with so debilitating a disability was able to learn very, very quickly how to respond to the incentives that were set before him. Why then some people have such a hard time appreciating that adults who do not have such disabilities will not learn to behave in accordance with the incentives before them to me is just an absolute mystery.

So again, to sum up, if you want to reform the Postal Service, you have to change the incentives that drive the behaviors of the people who operate the system. Thank you.

[The prepared statement of Mr. Del Polito follows:]

Association For Postal Commerce

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STATEMENT OF GENE A. DEL POLITO, PRESIDENT
ASSOCIATION FOR POSTAL COMMERCE
BEFORE THE
HOUSE COMMITTEE ON GOVERNMENT REFORM
MAY 16, 2001

INTRODUCTION

Mr. Chairman, Members of the Committee, my name is Gene Del Polito. I serve as the President of the Association for Postal Commerce (PostCom), an organization devoted to addressing the interests of those who use, and those who support the use, of mail as a medium for business communication and commerce. Most within the postal community are familiar with PostCom, even if only because of its widely read weekly postal newsletter, the PostCom Bulletin, or because of our internationally recognized postal news and information web site, postcom.org.

For the past three decades, the U.S. Postal Service has been operated in accordance with an act that was passed by Congress to address a crisis that threatened the integrity of America's postal system. As a response to the ills of its day, the Postal Reorganization Act of 1970 proved an effective remedy. It was created, however, at a time when the postal system in this country was still a major mechanism by which Americans shared their personal communications with one another. "Binding the nation together" through the mail wasn't just a nice sounding phrase, it was a necessity.

Over the past thirty years, things have changed considerably. Mail no longer is the primary vehicle by which Americans communicate with one another. Today, much more personal communication takes place by telephone and by email than it does through the U.S. mail.

THE TIMES ARE CHANGING--THE POSTAL SERVICE ISN'T

The way business is transacted in America, even by long-time mail users, has changed considerably as well. While mail remains an important medium for finding, communicating with, and transacting business with customers, it no longer holds the preeminence it did when Congress crafted postal reorganization. Today, the Internet, the World Wide Web, email, the telephone, cable, and other broadcast media play a much greater role in the transaction of American commerce. In addition, the Postal Service faces significant marketplace competition from providers such as Federal Express, United Parcel Service, Airborne, Emery Worldwide, DHL and other express, package delivery, and courier service operators, and foreign posts.[1]

The growth of these alternatives to mail has affected the U.S. Postal Service in a way that the crafters of reorganization never had envisioned. Furthermore, the reach, richness, and cost-efficiency of electronic communication technology improves each year. As a consequence, more and more communications will find their way out of the mail and into some electronic form.

Under present law, the U.S. Postal Service is directed to operate on a self-sustaining basis from revenue derived from the postage and fees paid by mail users. By law, the USPS must operate on a break-even basis. When costs outstrip revenues, it is directed under this law to seek an increase in postal rates and fees to a level that would assure break-even. For many years, this framework proved sufficient to ensure that our nation would continue to enjoy universal postal service.

Today, things are much different. It is increasingly difficult for the Postal Service to raise its rates without causing more of its customers to leave the mail and do business electronically. At the same time, the Postal Service has had difficulty containing its costs. For instance, at the time of its creation, the cost of human capital

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1 This is not to say that all of the Postal Service's present challenges stem solely from competitors and competitive alternatives. The nature of the softness in the present economy is merely a harbinger of the straits the USPS soon will face when electronic banking and bill payment become more commonplace.

accounted for approximately 80% of all postal costs. Thirty years later, labor costs still account for approximately 80% of all postal costs.

THE POSTAL SERVICE IS *NOT* A BUSINESS

While Congress in 1970 directed the U.S. Postal Service to operate in a business-like manner, Congress never intended the Postal Service to be operated as a real business. Congress never expected the Postal Service to function within a competitive environment. That's why it continued the Postal Service's monopoly over the carriage and delivery of most mail, and why the Postal Service's unique monopoly over access to the mailbox remains in effect today. In fact, the U.S. Postal Service is today as it always has been, i.e., an agency of the federal government operated largely as a public service by government employees.

With the advent of electronic communication, the real marketplace impact of the Postal Service's letter-mail monopoly suffered serious erosion. In addition to alternatives such as the World Wide Web, electronic data interchange, electronic funds transfers, and email,

Competitive businesses are characteristically driven by two complementary goals, i.e., the need to minimize their costs and maximize their gains. These forces don't operate within the USPS. The Postal Service by law is prohibited from making a profit, so there really is no natural incentive to maximize any gains. Furthermore, it is directed to raise prices when costs outstrip revenues, and, as a consequence, there's no driving incentive to minimize costs. Unfortunately, the incentives that underlie today's Postal Service are the opposite of what is required of an enterprise that must function in a competitive environment.

Former Postmaster General Anthony Frank illustrated how the Postal Service is governed by misdirected incentives in a talk he once gave to a group of mailers. He told them that under the contract the Postal Service has with its city letter carriers, if a carrier is given eight hours of work and completes it in less than eight hours, the carrier is given more work. If the carrier fails to complete the work in eight hours, the consequence is the

provision of overtime. Clearly, the "incentive" under such a scheme is to fuel the growth of costs, not to contain them. Similar "misdirected" incentives can be found elsewhere throughout the system.2

The reality we must face is that the Postal Reorganization Act has become a 21st century anachronism. The world has changed; the manner in which businesses and consumers communicate and transact their affairs has changed; but the nation's postal legislative and regulatory framework hasn't. The consequence is becoming increasingly obvious in the Postal Service's most recent financial reports and outlooks.

GOOD TIMES HAVE MASKED THE POSTAL SERVICE'S WEAKNESSES

During the late 1990s, the Postal Service benefited as much as other sectors of our economy from the unprecedented period of economic growth. It completed several successive fiscal years with operating surpluses, which it used to pay down prior year losses and maintain postal rate stability. These good times, however, masked the troubles that are in evidence now that the economy has softened and has exposed the weaknesses that underlay the USPS.

Today, the Postal Service is looking at an environment where mail volume growth is flattening and begun to show signs of a period of absolute volume decline. The lack of substantial mail volume growth means that in order to cover the costs of its huge operating infrastructure the Postal Service will have to raise rates by percentages that exceed the cost increases reflected in the general economy. Each new postal rate increase, however, will cause more customers to leave the mail for other more cost-efficient business communication and transactional alternatives.

There is a limit to the number, frequency, and size of postal rate increases many businesses will be able or willing to bear. Congress and the Administration soon will have to face the need to use taxpayers' funds to support this postal infrastructure, or to devise some other alternative that can ensure the provision of universal, reliable, and cost-efficient mail services.

The U.S. Postal Service (USPS) now finds itself awash in red ink. Critical mail volumes *are* declining

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2 The Postal Service's contract with rural letter carriers is a notable exception.

(particularly First-Class and Priority Mail), postal costs are growing at a greater than inflation pace, efforts by postal managers to stem the tide of red ink have flagged, and postal officials now seem committed to yet another round of postal rate increases, for which they apparently will ask by mid-summer. The straits are so dire that even the Board of Governors of the Postal Service has awakened to the seriousness of the Postal Service's problems, and has recognized that a solution beyond their sole reach is necessary and has called for postal legislative reform. For those who have been waiting for the Governors to awake from their apparent slumber, we can only say "it's about time."

POSTAL REFORM IS *ESSENTIAL*, THOUGH STILL VERY MUCH A CHALLENGE

PostCom began its call for postal legislative reform some seven years ago. Because of my own interest in electronic communication technology, our association was one of the first within our industry to setup a computer-based bulletin board system (BBS). Even then, with as primitive a technology as dial-up BBSs seemed to be, it was apparent that the manner in which Americans communicated and did business was on the cusp of profound change.

For the past six years, our organization and others within the business mailing community urged Congress to consider the enactment of meaningful postal legislative reform. This effort, regrettably, failed to garner the kind of broad-based support from all of the key postal constituencies that was needed to enact a meaningful postal reform measure.

That effort was a bruising learning experience. As a result, some believe that a different approach to postal reform may be needed. Our Board of Directors, for instance, has called on the President of the United States to create a Commission to study and make recommendations on the future organization and function of an American postal system to ensure the provision of universal, consistent and reliable, and cost-efficient postal services--services that would be provided in a manner that *facilitates*, rather than impedes the transaction of commerce.

There are others, however, who believe there is still a chance to craft a substantive postal reform without having to resort to a Commission. Indeed, Mr. Chairman, you have urged those of us who are a part of the

postal community to seek anew to address the need for postal change without encumbering ourselves with a strictly parochial perspective.

I am pleased to report, Mr. Chairman, that a coalition of mailers' representatives and the postal employee organizations has been meeting to see if it's possible to define a legislative outcome (using proposals considered by this Committee in the last Congress) that could better the structure and function of our nation's postal system while winning the support of our various constituencies. That work continues.

We recognize full well that our postal system is now and will remain for some time to come an integral part of this nation's economic infrastructure--as important to businesses as are air transportation, telecommunications, and power and water services. We can ill-afford a postal system that fails to operate cost-efficiently and reliably.

A FOUNDATION FOR REFORM HAS BEEN LAID

Mr. Chairman, while I can appreciate the wisdom behind using the work that has preceded us as the basis for our present work, I am all too painfully aware of some of the shortcomings inherent in previous legislative reform efforts. Former postal subcommittee chairman John McHugh (R-NY) worked assiduously to put together a reform proposal that promised to advance the integrity of our postal system. The work (by the very nature of the legislative process) reflected a number of compromises. He sought not only the support and participation of mailers, but also that of postal workers and postal competitors. The subsequent fruit of this labor resulted in a proposal that seemed to address adequately the situation that existed in 1996.

Unfortunately, in this Internet age, life seems to be lived in "dog years." Things have developed at a pace that few would have predicted, and I feel compelled to acknowledge that I don't believe that yesteryear's approach will produce the kind of legislative solution that is so sorely needed in 2001 and the years ahead.

Mr. Chairman, before going further, I want to make one thing perfectly clear. None of my concern regarding what I believe is the insufficiency of prior work should be interpreted as any criticism of the work undertaken by Mr. McHugh. To be frank, Mr. McHugh undertook his endeavor under the most trying of circumstances. When

the former postal subcommittee chairman held his first round of legislative inquiries on the nation's postal future, the U.S. Postal Service seemed blessed with abundance. Mail volume and revenue were at all-time highs. The USPS was turning in record year-end surpluses while paying down prior years' losses out of cash flow. While Mr. McHugh was all too painfully aware of the trends that would lead to the dilemma of today, there weren't many in this town that shared his vision. Many didn't buy into the need for structural postal reform; Mr. McHugh did.

Bills, however, do not find their way into law by dint of one person's effort. In order to garner the kind of support that would be needed to give a reform proposal a chance for enactment, a prodigious effort had to be put forth to attract support from the broadest possible constituency. That meant that compromise had to be the order of the day. As the former postal subcommittee chairman liked to say, no one would be well-served if we made the *perfect* the enemy of the *good*.

To win the support of mailers, Mr. McHugh built into his proposal the concept of fixing postal ratemaking flexibility in line with overall postal performance. To win the support of competitors, he sought to build a firewall between competitive and noncompetitive services in an effort to "level the playing field" between the Postal Service and its private sector competitors. To win the support of postal employees, the Chairman assiduously sought to avoid any matter that could possibly be portrayed as congressional interloping into the collective bargaining process, such as a cap of wages, or as an abandonment of the ubiquity of local post offices. As a result of all this compromise, an opportunity was forgone to define for Congress some of the essential public policy questions and issues that needed to be addressed in order to effect a more enduring resolution of the problems that plague our nation's postal system.

While he was postmaster general, Anthony Frank said that one of the assumptions that long had served as a definitive part of the compact between the government and postal employees was the belief that

employment at the Postal Service served as a gateway to the middle class for those who have no other way to get there. That, he said, is why the Postal Service paid skilled worker wages to semi-skilled employees.

If we assume for a moment that Postmaster General Frank's supposition was correct, surely we can recognize the laudability of at least one outcome. Postal employment provided employment to many people who otherwise might never have shared in the American dream. As far as postal legislative reform is concerned, it's now important for Congress to determine whether such a policy is essential to the structure and function of a future postal system. If Congress decided that the social benefits of postal employment should be retained, the only relevant concern would be how this is to be supported financially.

In a world where the power and reach of alternative methods for communicating and doing business will continue are to make inroads into core postal volumes and market shares, it is highly unlikely that a postal system can be sustained on the proposition that those who pay postal rates should bear its entire supporting cost. If the 1970s vision of the Postal Service as a governmental instrument of social policy is to be retained, then the Congress must find means to provide the institution with financial support in the form of taxpayer subsidies. If Congress is unwilling to fund such a system with taxpayer subsidies, then it must explore alternatives that do *not* include any such socially valuable, but *non-postal*, goals.

OTHER ISSUES THAT SHOULD BE ADDRESSED

In fact, there are many issues that *should* be explored as part of any restructuring of the nation's postal system including, but not limited to:

- Should our postal system be structured to provide the nation with some form of "universal" mail delivery service?

- How should universal service be defined?

- What are the alternative ways by which universal service can be provided?

- What are the costs and public policy consequences associated with each of these alternatives?

- Is the retention of a letter-mail or mailbox monopoly *essential* to the provision of universal mail service?

- Through what other means can Congress assure the continuance of universal mail service?

- What are the costs and consequences of these alternatives, and which makes the greatest sense within today's rapidly changing communication and logistical marketplace?

- What are the alternative means by which retail postal services can be most cost-efficiently and conveniently provided to American consumers?

- Are there alternatives to a system in which mail services are provided almost exclusively by an agency of the federal government?

- What are the costs and consequences of those alternatives?

- Is it essential that mail delivery service be effected solely by government employees?

- What alternative models should Congress consider in the development of a postal system?

- What are the costs and consequences of these alternatives?

- How viable are the alternatives already developed (or are under development) in other countries around the world that can be fruitfully applied to postal services here in the United States?

- What are the advantages and disadvantages to the government, mail users, and postal employees associated with the restructuring of the Postal Service into a stock corporation somewhat akin to what has been done in the creation of other stock-based government-sponsored enterprises?

- If a stock corporation were to be created, should the federal government all 100% of the stock, the majority of the stock, or the single largest block of stock, or no stock at all?

- Should stock be made available through an employee stock ownership program?

- What is the real market value of all postal assets?

- In what manner would the assets of a postal system formerly under the stewardship of a government agency be transferred to a stock corporation?

- What would need to be done to address the issue of the Postal Service's postal employee unfunded pension liabilities

- Should the employees of this new postal corporation by government employees, or should the transformation to a stock corporation include a "de-federalization" of the postal work force?

- And more....

While these issues were raised in the hearings that lead up to H.R. 22, they were not framed in a manner that would have caused Congress to address these matters more directly. Quite frankly, some were not explored in full simply because their mere discussion would have spelled the end to any effort to win the broadest possible constituency support. Furthermore, the absence of a nakedly apparent postal crisis made a full explication of these issues and alternatives little more than an interesting academic exercise.

Congress must determine whether it has the desire to endure the complexities of addressing comprehensive postal legislative reform without limiting its work because of political expediency. If it does, then the exploration of postal change must range beyond the limits H.R. 22 or any similar effort. If it doesn't, then our approach to reform must be tempered by a realization that any other effort *may* be insufficient and may require a re-exploration in not too-distant future.

There's an old saying: "If *wishes* and *buts* were candy and nuts, oh what a party we'd have." Perhaps the desire for a more encompassing probe of postal reform is a politically unachievable wish. If that's the case, then an exploration of alternatives that promise to be more "do-able" is far more preferable than a fatalistic resignation to an inevitable postal fiscal collapse.

IT'S THE INCENTIVES!!

To put it simply, the problems plaguing the Postal Service are rooted in the incentives that underlie the Postal Reorganization Act and function as the driving force behind postal behavior. If postal reform fails to restructure and redirect the incentives that motivate postal employees' (management as well as labor) behavior, we'll soon find ourselves at the legislative drawing boards once again.

My son knows all too well that if he behaves one way, he gets to play Nintendo. If he behaves another, his Nintendo privileges are lost. The incentives are clear, and, as a rational person, he responds in a manner tha maximizes his pleasure and minimizes his pain. In fact, these kinds of clear choices are what motivate most rational persons to behave in the most socially productive and personally rewarding manner. Why would anyone think the same principles shouldn't hold for the people who operate our postal system?

The most dynamic companies in America are those that are open to new ideas, that reward risk when prudently taken, and suffer real consequences when imprudence leads to disenchantment on Wall Street? Within the Postal Service, however, prudent risk is rarely rewarded. How can it be when the CEO of the Postal Service has a salary cap of $164,000 a year? And no one who works for the CEO can be paid a penny more. (In contrast, the chief executive officer of Canada Post and the CEO of Poste Italiane earn $400,000 a year, and the CEO of Deutsche Post earns approximately $1,000,000 a year.)

As for the consequences that await those who take imprudent risks, I recall all too clearly the comments National Association of Letter Carriers President Vincent Sombrotto once made in a pique of anger at postal management's failure to remove from postal employment a Chicago postmistress who spent more than $160,000 renovating a personal office in a building that was slated for demolition. "What this shows," he said,

"is that if you screw up enough, you just might get to become postmaster general." Clearly, an appropriate set of disincentives was lacking.

REFORM--NO MATTER THE DIMENSIONS--IS SORELY NEEDED

Mr. Chairman, at your request, the coalition of mailers and postal employee representatives mentioned above have been meeting to see what could be achieved with the work your Committee already has undertaken. While we still have a way to go before we can offer definitive recommendations, there appears to be consensus on the belief that any postal reform measure must provide real financial incentives (at least to those who serve as the Postal Service's "chiefs") when the USPS performs well when compared to suitable performance criteria.

The goal must be to provide incentives that will cause the chiefs to direct their subordinates to direct their efforts in a manner that facilitates the attainment of specific performance-based objectives. In addition, these performance-based criteria also must be tied to the provision of sufficient regulatory flexibility and postal pricing discretion to cause all postal employees to strive for excellence.

Mr. Chairman, it would be premature to say that these and other suggestions upon which we are working are ready to be vetted by you, the other members of your Committee, and your staff. I can assure you, however, that we are striving mightily to prepare and present soon the fruits of our work for your review and consideration.

All of us who rely on mail as a medium for business communication and commerce appreciate greatly the vigor with which this Committee has addressed this immediate need for postal reform. We, and most especially the Association for Postal Commerce, stand ready to assist you in this endeavor in any way possible.

Mr. BURTON. Thank you, Mr. Del Polito. That was very concise.

Let me start off by saying to Mr. Estes, we do not oppose a Presidential commission, but time is of the essence and I am not sure that commissions work in a real timely fashion. Usually, by the time you formulate the commission you are into 6 months, 3 months, 4 months, and then by the time they come back with a report you have got another 6 months, and then by the time it is published and everything it is well over a year before you have something. And I am not sure we have that luxury of time. That is why I have asked everybody that is concerned to give us suggestions on how we can improve on, if possible, H.R. 22 or add to it and come up with short-term solutions and a long-term plan that is going to maintain the viability of the Postal Service. So that is the first thing that we would like to have.

We are going to be meeting with the Board of Governors, at least some of the leaders on the Board of Governors, in the next week. And if any organization that is interested has suggestions on short-term solutions to the problem, I would like to have those so I could present those to the Board of Governors and ask them to take a hard look at those, especially anything that is a business-like solution to the problem. If there are ways that they can streamline or make the Postal Service effective in the short run, we would like to have those suggestions.

I would like to know from all of you, and I think you alluded to it a little bit in your opening statements, how the rate increase of January 7th affected your companies and your employees, and how you think the scheduled rate increase that is going to go into effect on July 1st will affect you. And also, if the Postal Service, if the Postal Rate Commission and the Board of Governors go along with it, if they have a huge rate increase, what that will do to you.

We will start with you, Ms. Schroeder.

Ms. SCHROEDER. Thank you. I think I addressed that very clearly. And that is, clearly, somebody has got to pay. What it really will do, I think, is cut down the number of books that are going into homes. And I just think, at a time when we are focusing on literacy, that would be disastrous.

Mr. BURTON. So it is just going to be incrementally worse.

Ms. SCHROEDER. Absolutely. I think it will.

Mr. BURTON. And it is going to cause an inflationary trend in the cost of books being sent through the mail.

Ms. SCHROEDER. Absolutely.

Mr. BURTON. Mr. Cerasale.

Mr. CERASALE. Well the Mailers Council has 70 percent of the mail but I think the thoughts are we probably put in 90 percent of the revenue. So that the $1 billion increase that is coming on July 1st will be $900 million coming from Mailers Council members. It will hurt them. You have rates that have gone up above the rate of inflation. And looking at the rumored rate increase being filed that will be above the rate of inflation again, this will significantly increase the cost of doing business, both in catalogs, in magazines, in financial institutions, sending out bills, etc. There is going to be I am sure some significant pressure to try to find alternative means to try and avoid these rate increases.

Mr. BURTON. Do you think that it will drive people to paying bills through the Internet and things like that, thus reducing the revenues to the Postal Service?

Mr. CERASALE. I am sure it will. Clearly, it has already begun. I think the softness in first-class mail volume is due in part to the competition and in part to the rates that are there. Business-to-business, many businesses are moving to a paperless billing system. I think if costs keep going up for postage that we are going to see major pressure and efforts to try to get individuals to move to a paperless payment system.

Mr. BURTON. Mr. Campanelli.

Mr. CAMPANELLI. Mr. Chairman, most of our customers establish a fixed budget for printing, distribution, mailing, etc. So when the cost per piece goes up they simply reduce the pieces, whether they be books, magazines, catalogs, that they send out. Generally, that impacts prospecting and trying to generate new business.

I also think that the other impact right now from an economic perspective is in technology and information technology and the Internet. That with the focus in industry turning from potentially creating new markets to webifying companies to drive cost out, that an area of increased postage going up will just have companies look at ways to use technology to off-set those costs, to bring those costs down. So in the near-term industry will be looking at webifying the business, using the Internet, using technology to drive out costs and that specifically will impact mail volume. I think, beyond that, the Postal Service could learn a lesson from that as well and focus their technology efforts on making it easier to do business and using technology to take out costs.

Mr. BURTON. So what I gather from what you are saying is that it is like a car company that was losing market share to raise the price of the car only guarantees more losses. And with the competition that is now apparent, which was not apparent 20 years ago or 30 years ago, the competition of the Internet and other services provided from other companies, if the Postal Service continues to raise rates, they are going to continue to lose market share.

Mr. CAMPANELLI. That is absolutely right. I have not seen any chip manufacturers raising their rates recently.

Mr. BURTON. Mr. Estes.

Mr. ESTES. Mr. Chairman, the business-to-business periodicals industry, which we represent through the American Business Media, in the past decade their postal rates have increased by 60 percent. That is in the past 10 years. The religious periodicals, who we also represent, now have as part of their budgets 20 to 22 percent going for postage. The amazing thing is that in this last action by the Governors the average postage increase for business-to-business periodicals went up 2.6 percent, but for the religious periodicals it went up 2.9 percent. And this is a business, so to speak, that does not carry advertising. It comes out of their contributions from their churches and whatnot. So they are being hit very hard right now. And last, the banking industry, who we also represent, for the last year that we had a survey, that was 1999, their total postage costs were $2.6 billion annually. The action taken by the Governors, as you pointed, kept the stamp the same but raised the second ounce to I think 23 cents. That action alone will cost the bank-

ing industry annually $52 million. So on three of the members we represent, that is the bottom line.

Could I say just one thing about the commission aspect. We would hope that any commission, if any commission ever develops, that there would be a deadline, like 10 months or something like that, and we put that in our paper.

Mr. BURTON. Yes. Thank you, Mr. Estes.

Mr. Del Polito.

Mr. DEL POLITO. Everybody else seems to have done a credible job in terms of documenting the disaster. I could add my own stories but it probably would not add anything to your knowing. But what I think you need to appreciate is that what they also have cost themselves with their customers is a tremendous amount of good will has been poured down the sewer.

I have never in my entire career in the postal community, which is now 18 years, seen people react to what they perceive to be the approach of the Board of Governors and the management of the Postal Service with such anger. If I have to hear one more time in any venue out of a postal service manager's mouth "We are going to go ahead and raise your rates because you have got no place else to go," the bottom line they need to appreciate is increasingly in the future people will have a place to go. If they are looking for a fiscal crisis to be able to act as the crutch for postal reform, they are about to get it big time.

They have got a key decision in front of them relative to what they do in July. If they file for a postal rate increase of any magnitude before the beginning of the next year, they are going to be making a tragic, tragic mistake. And, quite frankly, mailers are tired of being the monkey in the middle between games to be played between the Postal Service and the Postal Rate Commission over the fine points of the law that increasingly has become an anachronism.

It is nice to be able to hear that after 6 years people finally begin to agree that postal reform is a necessity. Now it is time to get it done.

Mr. BURTON. Thank you. Before I go to Mrs. Mink, let me just say that I would like to have excerpts of this, we are video taping this, I would like to have excerpts put on a tape so I can give it to the Board of Governors next week.

Mrs. Mink.

Mrs. MINK. Thank you, Mr. Chairman.

Mr. Cerasale, was it, of the Mailers Council, I looked through your testimony and I am struck by that paragraph in which you said that you have repeatedly asked to have an opportunity to sit with the Board of Governors and that this request has consistently been denied. What is the basis for that denial? Is it statutory, or is it simply some rule that they have adopted on their own that places them above the public?

Mr. CERASALE. It is not statutory, it is not really a rule that they have passed either. It is a policy that they follow. I can understand some of it. To a certain extent, they are a part-time board and to meet every single mailer they would use up all their time. However, we think that from the Mailers Council standpoint, we rep-

resent such a huge percentage of their customers, that it would be worthwhile for them to meet with us.

We had one meeting with a group of mailers with the chairman and vice chairman of the Board, and they at least expressed a desire to continue having these meetings periodically. So that we may have finally made a crack in the door of the Board that is running a service organization meeting with its customers.

Mrs. MINK. Thank you very much. Maybe they knew about this hearing today.

Mr. CERASALE. That is a possibility.

Mrs. MINK. Congresswoman Schroeder, as you know, tomorrow we will be debating on the floor the reauthorization of the Elementary and Secondary Education Act. A large component of that legislation has to do with the concern of the President and his administration, all the teachers, and people that are involved in analyzing public education today and why Johnny cannot read after the third grade. So we have weighed in tremendous resources for this campaign on literacy and reading and adequacy of the instruments given to teachers so that they are qualified to teach reading.

And in your testimony, you raise this specter of crippling what we are trying to do in our legislation to encourage the distribution of books and adequacy of our libraries and so forth by indicating that these rate increases that attack your particular membership is going to severely limit the publishing industry from getting these books out to the very people we want to assist. Where will the industry go to if the Postal Service insists upon these rate increases that will price you out of relying upon the Postal Service for this distribution?

Ms. SCHROEDER. Thank you so much for your question, Congresswoman Mink, because this is really what troubles me. There are many book clubs for children. Obviously, postage is a very key part of it. We do not know even how to price books if they are going to continue with 50 percent postage increases every year, and companies are not even going to offer them in the future if they end up having to absorb all these additional costs that they did not predict. How do you put out a business plan?

Now I would rather talk about reading than the business plan, but we are not going to get the reading material to the children if there is no business model that allows a company to stay in business that is doing that. And that is really where we are. A business person cannot predict what the costs are going to be when you saw that chart going straight up. They want to get stuff out to children but parents do not have a lot of money and so you want to keep it as low as you possibly can.

I think it is a tax on reading. I really do. And in the reform legislation this Congress passed when you were here, it very clearly said that should be taken into account, that the cultural issues, the educational issues, the scientific and information should be taken into account. It was not taken into account at all. They really whapped books. We are very concerned about what happens to those children's reading programs and adult reading programs that are out there.

Mrs. MINK. Thank you very much.

Mr. Estes, I think I have time for another question, in your testimony you made mention of the encroachment of the Postal Service into the electronic industry and establishing various partnership arrangements. You level some criticism on this movement and made a statement that the taxpayers, in fact, were being pushed into this particular partnership because we in essence pay for most of the revenues that the Postal Service receives. Can you elaborate on precisely what the Postal Service has done in your view that is an encroachment on their primary mission.

Mr. ESTES. Yes, Congresswoman. The problem that we see the Postal Service facing is one of getting into the private sector where we do not believe they should be. They ought not to be competing with private sector organizations, who are doing a good job. Now they have started up new ventures—e-mail ventures, e-bill pay ventures, with the American Express Co. a check fulfillment process, several others. Those have lost money. That money has to be made up somewhere from the revenue stream. And the revenue stream that is most often used to make up money is from the first-class revenue stream. And that is what we are really addressing here.

Basically, our concern is that the Postal Service as such, as a Government agency, a quasi Government agency, ought not to be in the business of starting up private sector ventures in competition with the private sector.

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

Mr. BURTON. Thank you, Mrs. Mink.

Mr. McHugh.

Mr. MCHUGH. Thank you, Mr. Chairman. Let me express my appreciation particularly to the individuals sitting at the front table who, in the case of John, and Gene, and Jerry, especially, were so actively involved in this process. Obviously, their presence here today reflects their continuing concern. And I am not sure why they have gone through what they have over the past several years and are still voluntarily here today. I am not sure we subpoenaed them, did we? No? [Laughter.]

They are here voluntarily, and my compliments to all of you.

Mr. Estes, you made a comment back in March 1999 before our subcommittee and I want to read it to you. "We often hear the warning that it would be unwise to wait until the Postal Service is broken to fix it. But without evidence of present or eminent breakage, such as declining volume or revenue trend lines over a representative period of time," you then reference H.R. 22, "demands for change rest on little more than conjecture." Would you like to update that statement?

Mr. ESTES. You are referring to the situation today with respect to——

Mr. MCHUGH. That is why we are here, sir.

Mr. ESTES. Right. Yes, sir, I can. As I mentioned a minute ago, the last 5 years have been pretty good with respect to volume and revenue. In looking at the data for this year of 13 accounting periods, we are now through 8 of them, and as a result of those 8 through 13 accounting periods, the revenue for the Postal Service is down from budget 1.8 percent, the volume is over budget by 0.9 percent, and the expenses are off by 0.1 percent. Those, to our way

of thinking, Mr. McHugh, represent a trend, or maybe there's a modification.

Mr. MCHUGH. I appreciate your qualified yes. Can we agree, and we've not agreed on a great deal in specific terms, objective wise, I think we have, can we agree that whatever trend lines, whatever quarters of fiscal revenues and expenditures may show, the current system doesn't work for your members? Wouldn't the data that you outlined and Ms. Schroeder and others have suggested, double digit price increases within the last several months suggest it doesn't work?

Mr. ESTES. Yes, we can agree that reform is essential.

Mr. MCHUGH. Then let me just say, you were very gracious in your comments and deferred remarks about H.R. 22. I have no love personally for H.R. 22. I told particularly some of the folks at the front table there and then our second panel, if I have to write a bill of my own hand, that wouldn't be it. But I don't have the only vote in this House. There are 434 others, as I know Ms. Schroeder recognizes. And we tried to do something that was passable, achievable.

You do, however, in your written statement, that will be part of the record, make some comments and observations about H.R. 22 that I have to tell you are simply incorrect. I commend you for your continuing interest, for the clarification of the comment you made earlier with respect to the condition and the crisis of the Postal Service.

I'm going to ask the chairman for unanimous consent that we can enter into the record a point-counterpoint of the concerns that you expressed. Because I think that's important. If H.R. 22 is a major part of reform, terrific. If it's not, that's fine too. But as you heard the chairman say, I think it is going to be the focus of a starting point. So I think it's important we proceed accurately.

Mr. BURTON. Without objection, that will be put in the record.

Mr. MCHUGH. Thank you, Mr. Chairman. And all I'm asking, Mr. Estes, is that you, when it is submitted, please read it and comment and return, so that we can at least understand each other based on facts. Is that fair?

Mr. ESTES. Mr. McHugh, yes, it's fair, and let me just add that even though we've disagreed on some of the substances of what has been proposed, you and your staff have always been gracious, as you are now, in listening to our concerns. So yes, it's eminently fair as you are.

Mr. MCHUGH. I appreciate that. Because really, what we all need to do is focus on the future. And Gene Del Polito made some comments about that in his testimony. He's been a muse of sorts to me and he continues to be.

What's important is not what happened yesterday. What's awfully important is what happens today and into tomorrow. So I've squandered most of my time on that. The good news here is we've dealt with these folks, all of them, and have appreciated their input. Mr. Chairman, again, my compliments to you.

If this were easy, we would have done it a long time ago. It's not. As Jerry said, even amongst his own membership, everyone agrees on the word reform, but it's like beauty, it's in the eye of the beholder. But it's all of our responsibilities now to find a common

bridge that we can cross that does more good than not. And your leadership, Mr. Chairman, has been exemplary and I deeply appreciate it. Thank you.

Mr. BURTON. Mr. Del Polito, did you have a comment about Mr. Estes?

Mr. DEL POLITO. I know that Jack remains unconvinced, unless he sees sufficient trends. But I would ask everyone to keep in mind, as I had said in my statement, that the fact that the crisis that the Postal Service is in right now may not be due to electronic diversion, it's coming and it's coming fast. I think everyone should take to heart the comment that former Postal Rate Commission Chairman Ed Gleiman shared with me over lunch 1 day in which he said, you know, we should count ourselves lucky. We've gotten a wakeup call. Because if we pass this one by, we're going to find that the crisis is going to be much worse than we ever imagined.

It's always amazing to see that people will build their houses on the San Andreas Fault and they'll be told, it's going to shake and the house is going to come down. But they don't believe it until it happens. And then you hear the weeping and the gnashing of teeth after they're sorry.

Mr. BURTON. I don't want to have a debate here, Mr. Estes, but go ahead.

Mr. ESTES. Just a quick comment. The Postmaster General, the current Postmaster General has indicated that e-commerce is not that much of a problem. He believes that people stopped writing letters some time ago. E-mail does not represent a threat to the Postal Service. I can give you the transcript of that if you'd like to see it.

The other is that the question of the Internet, Mr. Henderson believes, may be a blessing for the Postal Service, because of the added business that they will get in shipping and what-not. I can also make that available. It's a transcript of a hearing, of some testimony he gave.

Mr. BURTON. I'm not sure I agree with Mr. Henderson.

Mr. Davis was here for questions first. Is that all right? Mr. Davis has been here I think from the beginning. Mr. Davis.

Mr. DAVIS OF ILLINOIS. Thank you very much, Mr. Chairman. I really appreciated the testimony of the panel, all of you. Especially the passionate testimony or presentation from Representative Schroeder relative to reading and the importance of it, and the need to foster it as we try and guarantee further our sense of democracy.

I also detected, though, running through the panel a theme which essentially said that continued rate increases are going to have a seriously negative impact on your businesses, and on your industry. And I certainly can appreciate that. The question that I would raise in an effort not to be redundant, given this understanding, if you would, what would you propose as alternatives, or if you have any notions of alternative solutions? Would you be willing to share those with the committee?

Mr. CAMPANELLI. Congressman Davis, to kind of recap some of my testimony, fundamentally the Postal Service, and I do agree with Mr. Estes on this, should have a tighter scope and a tighter

mission. That is again focusing on getting the mails to the home and mail coming from the home.

There are many options upstream, through negotiated service arrangements, through additional work sharing agreements, and to have private industry handle a lot of the processing, sortation, transportation of the mails prior to that last mile that's effectively employed now. There are areas, a lot of areas, that can be expanded upon that to take that cost out and to use private industry to manage that piece of the business.

In addition to that, the areas of information technology also create significant opportunity for taking out time and cost. That is fundamentally how information gets to the Postal Service about the mail. And also, I would add to the comment that it's not so much the e-mail from the individual users, but it's the webification of business and industry and the business mail that's going to consumers that's going to cause the erosion of first class mail.

The final point is that in the process, there's a transformation going on in the types or shapes of mail. And the Postal Service has long been pretty good at processing letter sized mail. But as they get into larger pieces of mail, flats, magazines, catalogs and larger pieces of mail, that is where they have a lot of inefficiency. Using industry to move those pieces of mail, do more of the sortation, etc., and also within the Postal Service then combining classes of mail so that we don't have to treat those pieces of mail, books, magazines, catalogs, moving through the Postal Service independently, creating redundant infrastructure within the Postal Service to accept certain types of mail. To the extent that we can combine those and move those together through the Postal Service, we will create a more efficient Postal Service.

Ms. SCHROEDER. Congressman Davis, may I just add, I think that's very important. All of our businesses would probably be gone if they'd only had 11 percent productivity increase over three decades. The Postal Service invested in all sorts of machinery and technology to make themselves more productive. But somehow it didn't happen. There's been a real disconnect.

Continuing the focus what you really want, universal delivery, is very important. That's what its mission is. Keep it on that. Work on the productivity. But what you usually find is, whenever you push somebody, they blame someone else. If you're going to have a commission we often found all of the commissions were really a way to bury the issue of reform. When Congress did the base closing commission which had a date certain and Congress either had to accept the results or turn them all down, something did happen. They couldn't pick and choose.

If it gets to a crisis point where you think you have to have a commission I think you're going to have to do, something like the base closing commission, which I noticed the Wall Street Journal recommended today. But I think it is absolutely essential we stay focused on universal service and we get the productivity up far more than 11 percent over three decades. That's incredible.

Mr. DEL POLITO. In the terms of the longer term, one of the things I think you need to be aware of is that there really are a multiplicity of options from which we could choose in terms of how you could restructure a postal system in order to be able to have

it operate more efficiently, cost efficiently and productively. It's regrettable that each and every time we talk about more significant structural reforms people choose to characterize it in terms of privatization.

The issue I think that's important here in terms of redirecting incentives is not whether or not the private sector owns the enterprise or not, but whether or not the enterprise is structured in a manner in which it is able to function successfully within a competitive environment. A corporatized Postal Service, one that has a true stock corporation where 100 percent of the stock is owned by the Government and where the incentives are appropriately structured, could do a vastly superior job in satisfying the needs of the American people, its workers and the businesses that it serves without necessarily saying that Government has to abrogate its ownership or responsibility for it.

It's unfortunate that in many instances, in seeking out alternatives such as the way we've attempted to respond to H.R. 22, that everyone else, everyone wants to be held safe from whatever the options may be. Everyone wants a guarantee that nothing is put at risk. That kind of brings to mind the statement that a fellow by the name of Bayard Ruston gave to my graduating college class back in 1968, when he turned around and he said, those who actively pursue security lose it.

And if we're really going to be successful here, when we hear everything needs to be put on the table, we need to be serious about that. Because if we all seek to be sure that we are insulated from change, the very thing we seek to avoid we'll get.

Mr. CAMPANELLI. Representative Davis, I think that from the Mailers Council, the big key, echoing on Representative Schroeder's statement, is the productivity. It doesn't matter what reform you may come up with if you have reform. Whatever happens, whatever piece we have of the Postal Service, be it what it is today or what it might be in the future, the focus has to be on productivity to improve what's happening.

As you saw from that report card, even against the private sector, the Postal Service has not fared that well. But the one area where there was some light was the mail processing, where internally we've given it a B on our report card. That stems from, maybe too late, maybe it took too long, but it stems from a lot of capital placed into mechanization, placed into automation, trying to improve the productivity of the Postal Service.

One of the things the Service has done in this crunch time is to pull back on capital expenditure. That's a mistake. That is a major error. They should be moving forward to get more of those Bs and hopefully As on that report card.

Mr. DAVIS OF ILLINOIS. Thank you very much, Mr. Chairman. I know that my time has expired. And I'd just say that I think Bayard Ruston was right then, and he'd probably be right today.

Mr. MCHUGH [assuming Chair]. I thank the gentleman. And let me state for the record, while he's in the room, I never like to compliment someone unless they're here, Mr. Davis has been a leader over the past several years on the subcommittee when we were undertaking this endeavor. And he continues that leadership. We're working very diligently with he and our two staffs, along with the

chairman, of course, to try to find a bipartisan way to approach this issue. Because it doesn't check to see your party registration before it hits you, as I'm sure all of you know. So I compliment the gentleman.

Ms. Norton.

Ms. NORTON. Thank you very much, Mr. Chairman.

I apologize that I wasn't here to hear your testimony, because this is an area of great interest to me. Anybody who is interested in public policy has to be fascinated by this public-private policy dilemma and how to solve it. I listened to your responses and got a sense of your own suggestions. We had a prior hearing.

I'm struck, and of course it really goes not to what would you do to reform, but whether we know how to reform this entity. I would really like to have you address this. You've spoken of what amounts to short term and long term problems. We know about the long term problems, because even during the flush economy, there were bills here and they got stuck. They were mostly dealing with the notion that it was going to get worse and there were all kinds of problems that really didn't fit the 1970 bill we passed. Times have changed.

Now, we've got short term economic problems, financial problems exacerbating the problems that the Postal Service already has. I am very concerned that as we have these hearings and hear these suggestions, that we may yet fasten upon some of them. Because I do not feel yet that I know how to handle this hippopotamus. The Postal Service Act says that the Postal Service is to be a business. Of course, there is no business like it. And we are expecting of this business what we expect of any other business, free collective bargaining, management can change quickly when there are problems, we don't have any of that.

Of course, this is a business that is subsidized, so we can't compete in the ordinary sense of the word. Of course, there are things that you can't do in a market economy if you don't compete. These are the kinds of dilemmas that I don't know how to address. Nobody ever thought about technological communication at all when we passed the 1970 act.

I know that there is an unusual coalition of mailers and employees, and I know what you say. This is my dilemma. You say, no service reductions. I couldn't agree more with that. This is your universal coalition, your universal service coalition, you say, no increases in rates. Couldn't agree more with that. I consider that management 101.

Except management 101 goes for the businesses of the kind I'm most often used to. I don't know how to handle, you say the products ought to be improved. That's real vague, particularly since they can't, this is what your coalition said, since they can't compete. So you'd better watch out how you improve your products, because you can improve your products so you're competing right with somebody as the Postal Service acted like it was trying to do for parts of the 1990's with the private sector.

Then of course, the Congress is going to smack you down and you're supposed to promote, watch out about that, too, because when they promote it, as when they went over to the Olympics and promoted like any other business, Congress said, what do you

mean promoting that way? We don't promote that way. Well, that's how private businesses promote. God, I'd hate to be in the Postal Service and try to figure it out. What are you? What kind of hybrid are you?

You say eliminate inefficiencies. I'm looking now at what your coalition says, and increased productivity, again management 101. Every business knows how to do that. The difference is, all the businesses know how to do it according to management 101, and we have not created a Postal Service that operates according to management 101. I am asking whether or not, by asking for short term bargaining, that's the part that caught my attention. You said, don't let them do any of this. You say don't let them do any of this. You say, enable the board of Governors to address short term cash needs, more appropriately through bargaining rather than shortsighted strategies.

I'd like you to speak, are you asking for a time out to allow them to get some money so that they can continue until we find a mechanism to figure out how to do this? Or would you really like Congress to just absorb these suggestions and try to implement them without a more thorough look at this strange and unique animal? I am absolutely perplexed as to how to reform.

It is perfectly clear to me that there needs to be reform. You're talking about an organization, for example, part of what some in Congress want to do is get hold of collective bargaining. Better be careful here. You have got some of the worst labor management relations in the country in the Postal Service. You've got violence among employees in the Postal Service, there's so much stress there. You've got 125,000 unresolved grievances, a sure sign of a backlog.

I want to be careful there, too. So if all of you have any easy answers for how we can do one, two, three, four, I want to hear them. I'm more impressed with your notion that to give them some money and then let them go about it, then I want to know how do you go about it, how do we find out which is the right set of reforms to, in fact, plaster onto this absolutely unique business on the planet?

Ms. SCHROEDER. Congresswoman Norton, as always, you go right to the core of it. Having listened to this debate for 20 some years on the committee, I think there are two things that we really have to lay out there. No. 1, we created a critter like nothing else. It's not really private, it's not really public.

I think we've also created a Postal Service that's almost like the cowardly lion. They're really afraid to come and tell the Congress the real status. OK, OK, we can get along. Let's face it, about $1 billion is owed the Postal Service by the Government for revenue foregone, if you really read the statute the way I read it. But they're kind of afraid to come ask that, because then they get their hands whacked.

So part of the problem is, we have to clearly define what the Postal Service is. I think it has to become a Government agency that has more accountability to you where we can deal much straighter. I just don't think this half and half thing has worked. I really think we've got to be clear about it. I'm glad you said that.

I don't think we want to privatize it. Because you may say we don't know how to reform it, but we clearly could not privatize this, either. There is nothing; there's no model like that. How are you going to deliver mail not to a country, but to a continent, and still retain universal service, and the things that every person thinks that every government should be doing for its citizens, including me?

This half and half status has caused Congress to be able to micromanage. It's caused the Postal Service to be afraid to really level with us as to what's going on. And we find it's even very difficult to have the transparency that you would have if you had a Government agency. You would be able to have much more public records, much more information about the costs, much more availability to what's happened. We've been trying to meet with the Postal Service for 3 weeks and can't even get in. You know, that wouldn't happen, you'd call your Member of Congress.

So I honestly think you've got to decide what this beast is. We created something that doesn't fit anywhere, it's kind of imploded on us.

Ms. NORTON. Does anyone else have any response to that?

Mr. DEL POLITO. I tried to lay down in my statement the fact that I genuinely believe that what is at ill here and why you get the curious behaviors that you do out of the Postal Service is because of the way the incentives are structured that cause people to behave the way that they do.

I'll just give a very simple one, which was in my statement. They are now going through the process of trying to identify a new Postmaster General. They probably have already made a selection, and within the context in which the selection has to be made, I'm sure they've made a good one.

But the most we pay the PMG in this Nation is $164,000 and nobody gets paid more than he or she does. In Germany they pay their chief executive officer $1 million and he's got all kinds of stock options and other ways of increasing and maximizing his income when he makes that institution perform well. The same is also true of Canada. The Canada Post CEO gets $400,000 a year. Even the Italian post office pays their CEO $400,000 a year.

When you go looking to try and find out who's going to bring you the kind of creative energies and restructuring of incentives to get people to go forward, you've got to ask yourself, do I really want to take on that level of responsibility for $164,000 a year, but no matter how well I do, that's the most I could possibly earn. And if I screw up, I'm going to have everybody on my back chewing on my legs telling me what I've done wrong.

If you want to change the way they behave, change the incentives in the system.

Ms. NORTON. Thank you, Mr. Chairman. I do hope you're including more than incentives for pay for the CEO.

Mr. DEL POLITO. Yes, I am. [Laughter.]

Mr. MCHUGH. Well, whoever that candidate was, if they saw that, they've probably withdrawn. [Laughter.]

Mr. Shays.

Mr. SHAYS. Thank you. I'd like to ask each of you, first, if you agree that ultimately to solve this problem, you either have to raise

rates or a combination, cut costs or cut services. And I need to know, and I buy in totally with the fact that you have disincentives for logical action. So I'd like to ask each of you what you would do specifically, without a lot of rhetoric, and tell me which is your highest priority.

We'll start with you, Mr. Estes.

Mr. ESTES. Mr. Shays, I think the most important aspect to address is cost cutting and cost management. I refer you to an IG report that's part of the April——

Mr. SHAYS. No, just right now. I'm not going to dispute that, but bottom line is, cost cutting. Thank you.

Mr. CAMPANELLI. Well, I'd first start by saying the Postal Service has already raised rates. So doing it again isn't the answer. It does focus on costs. But it is, and a quicker way to get at that is better leverage private industry to handle more of the upstream processing and invest in the last mile delivery network for the Postal Service, a tighter scope of what they do, and focus on the universal service, going to the home every day, providing that service.

Mr. SHAYS. Wait a second, wait a second. Do what?

Mr. CAMPANELLI. Again, it would be to focus the Postal Service on the last mile delivery network, to leverage the scope and scale that they have that is unparalleled in the country.

Mr. SHAYS. But in giving you some choices, you're saying we need to focus on universal service, and that's going to cut costs?

Mr. CAMPANELLI. With that focus, then take the upstream processing where much of the Postal Service costs and inefficiency is, and use private industry to do that more effectively.

Mr. SHAYS. But we would cut costs, you're telling me we would cut costs by privatizing some of the services?

Mr. CAMPANELLI. Yes.

Mr. SHAYS. Fair enough.

Mr. CERASALE. Mr. Shays, we would say cut costs, of course, improving productivity is a way to try and hold and cut costs. I guess we should look at the total, not just the costs to the Postal Service but the total cost of mailers and the Postal Service in trying to deliver things, and we want to try and look at reducing the overall costs to customers of the Postal Service. It could be their costs as well as the Postal Service.

Mr. SHAYS. Thank you.

Ms. SCHROEDER. Thank you, Congressman Shays. I honestly believe in the whole theory of elasticity and inelasticity, you can't raise rates right now on top of what you just did, because you're going to lose volume. That only feeds on itself. It's the first time they've run a deficit after they just raised a rate. So you've got a real issue.

That drives you to costs, that drives you to infrastructure, that drives you to looking at these higher fees and figuring out how you streamline it or what you do about it. That's why I think we're here. I also think the Government needs to look at whether they have lived up to their commitment to the Post Office in revenue foregone, and whether we fully funded the pension fund, which I understand is a problem. It's those types of things that everybody's got to look at it.

Mr. SHAYS. Mr. Del Polito.

Mr. DEL POLITO. I think first, one of the things they should begin to look at is the wasteful programs that they still maintain that are not bringing in revenue. Someone was making references earlier to some of the e-commercial activities that they're involved in which at this point has been a drain on them. Those certainly can be cut.

They should take a look at other elements within their organizational structure that also are relatively non-productive and take steps to cut back.

No one wants to see the Postal Service not be able to pay its bills. I think as Ms. Norton tried to raise earlier, yes, we do want a breathing spell. And that breathing spell means that if you do need postal rate increases, smaller, more manageable postal rate increases are obviously a hell of a lot better than having to swallow them in one fell swoop. We've been telling the Postal Service that for years. I think they heard more frequent, I don't think they heard smaller.

Finally, there are things I think that the Governors can do themselves to alleviate some of the pressure that the Postal Service has. They've been asked several times, would you be interested in increasing your borrowing authority to get beyond the debt limit problems that you're facing today. They've said no. There's no reason why that debt can't be increased. There's absolutely no reason why some of the flexibility they need for operational purposes can't be provided.

Mr. SHAYS. Mr. Estes, I interrupted you. You wanted to explain about the GAO report.

Mr. ESTES. I just wanted to call your attention, Mr. Shays, to an IG report that was part of the record of the April 4th hearing that goes into some of the areas where cost cutting would be addressed specifically.

Mr. SHAYS. Thank you, Mr. Chairman.

Mr. MCHUGH. I thank the gentleman. Vice chair of the committee, Mr. Barr? No questions.

Next refer to my colleague from New York, who also was one of the most active members of the Subcommittee on the Postal Service over the past 6 years, Mr. Owens. No questions.

Well, as my father used to say when he punished me, we could do this all night, but—[laughter.]

I want to, on behalf of Chairman Burton and all the members of the committee, thank you for being here today, for your continued efforts, and most importantly, on that promise of continued cooperation. We certainly heard the message that you recognize the need to act in some way. We'll not reach a perfect solution nor one that makes everyone happy. But if we can reach one that, as I mentioned earlier, does more good than not and is at least palatable to the majority, perhaps that's the way we should go.

But either way, it's a great responsibility. Perfectly timed, thank you so much for your presence here today.

Rather than immediately call our second panel, and I know you gentlemen have been waiting patiently, as you just heard, we've been called for a vote, it would probably make the most sense from a time management perspective to allow the Members to go vote and hopefully come back as soon as we can. So with your indulgence, we will stand in recess until after this vote.

[Recess.]

Mr. BURTON [resuming Chair]. We should have another hour before there's another vote. We'll now welcome our second panel to the witness table. William Quinn, Clifford Dailing, Vincent Sombrotto and Moe Biller, who will be accompanied by William Burrus. So would you all please stand?

[Witnesses sworn.]

Mr. BURTON. Be seated.

As with our first panel, we'll ask you to try to confine your remarks to as close as possible to 5 minutes. We'll start with you, Mr. Quinn.

STATEMENTS OF WILLIAM H. QUINN, NATIONAL PRESIDENT, NATIONAL POSTAL MAIL HANDLERS UNION; CLIFFORD DAILING, SECRETARY-TREASURER, NATIONAL RURAL LETTER CARRIERS' ASSOCIATION; VINCENT R. SOMBROTTO, PRESIDENT, NATIONAL ASSOCIATION OF LETTER CARRIERS; AND MOE BILLER, PRESIDENT, AMERICAN POSTAL WORKERS UNION, ACCOMPANIED BY WILLIAM BURRUS, EXECUTIVE VICE PRESIDENT

Mr. QUINN. I'm Billy Quinn, national president of the National Postal Mail Handlers Union, representing more than 50,000 union mail handlers. Congress is obviously concerned about two related issues. The first is the difficult financial situation that currently confronts the Postal Service. The second is the need for reform of the Postal Reorganization Act.

On the question of postal finances, many of the Postal Service's current financial difficulties are beyond its control. The American economy began to slow late last year, and that slowdown occurred faster and deeper than predicted. As a result, the volume of mail has not grown as much as expected, and the mix of that mail has taken an unprofitable turn, thus causing deficits.

At the same time, fuel prices continue to rise, imposing additional costs on postal operations. Similar problems are facing thousands of other companies, and it is foolhardy to expect that the Postal Service would be immune from these general economic trends.

We therefore applaud last week's decision by the board of Governors to raise rates. Although some have suggested cataclysmic results and have complained about a second rate increase in the past 6 months, we believe in this instance that the board chose a responsible course of action. Indeed, no mailer who complaints about rates today ever acknowledges that rates did not increase at all for the 2 years prior to this latest round of increases.

Unfortunately, the Postal Service also has suggested that it might react to the economic slowdown in other less responsible ways, such as cutting back on services. We do not believe that the cutting of services on which the American public has come to depend is a solution to the current financial situation. Many in Congress like to blame the Postal Service or its dedicated employees for the Service's financial predicament.

But a review of history easily points the finger of blame in other directions. It is Congress, you should remember, that throughout the 1980's and early 1990's, used the Postal Service as a cash cow

by imposing unjustified costs on the Postal Service in order to reduce Federal budget deficits. And it was the House of Representatives, after several years of USPS surpluses, that passed the resolution June 1998 without any meaningful debate that essentially forced the board of Governors to delay a rate increase and forego more than $800 million that was needed to operate the Postal Service.

The Postal Service's competitors also share some of the blame. I can assure each and every member of this committee that United Parcel Service, FedEx and others have only one interest when they debate postal reform, and it is not the public interest, it is their own bottom line. Others may hesitate to say that publicly, but that's the fact of the matter.

That brings me to the second major challenge facing the Postal Service, the need for postal reform. On this issue, Congress needs to act to amend the current statute so we cannot argue against congressional intervention. But Congress needs to act in a responsible and informed manner. The Mail Handlers Union will support legislation that gives the Postal Service flexibility in pricing, the freedom to design or introduce new postal products, and the ability to borrow and invest with fewer constraints.

It is patently ridiculous, for example, that the Postal Service is unable to change its pricing structure to compete for the overnight business of the Federal Government. Frankly, I find that embarrassing, that the very government which demands universal service from the Postal Service does not utilize that service. As many of you know, we have been working with other employee organizations and with representatives of the mailing community to see if a consensus can be reached around these difficult issues.

While much work still needs to be done, I am encouraged that appropriate reform of the Postal Reorganization Act can be enacted. A key ingredient in any reform legislation, however, must be protecting the ability of the Postal Service to provide universal service to the mailing public by processing and delivering letters and packages at affordable rates. These rates must be sufficient to protect and support the infrastructure that universal service requires and to provide postal employees with a decent and fair standard of living.

To say that I am encouraged, however, is not to say that I am blindly optimistic. In the last few months, the board of Governors has used the Postal Service's recent financial difficulties to launch an attack on the collective bargaining process that has governed the Postal Service and its employees for the past 30 years.

That attack is wholly unwarranted. Postal reform legislation must not interfere with the PRA's current framework for collective bargaining. The collective bargaining process should be treated as sacred, and should not be changed either intentionally or inadvertently by enactment of postal reform.

This means that the collective bargaining process must be allowed to function without artificially imposed constraints, such as price caps that effectively become wage caps. The bargaining process must be allowed to set wages and benefits and the Postal Service must be allowed to pay for its labor costs through appropriate postal rates.

If fair and decent wages require an increase in postal rates, then the Postal Service must be allowed to raise its rates without jumping through the overly cumbersome hoops that currently exist. We look forward to continuing to work with the committee and its staff, to ensure that appropriate reform legislation is enacted.

I want to thank you for the chance to testify. I would be glad to answer any questions.

[The prepared statement of Mr. Quinn follows:]

National Postal Mail Handlers Union

William H. Quinn
National President

Mark A. Gardner
Secretary-Treasurer

Hardy Williams
Vice President
Central Region

Samuel C. D'Ambrosio
Vice President
Eastern Region

John F. Hegarty
Vice President
Northeastern Region

James C. Terrell
Vice President
Southern Region

Efraim Daniel
Vice President
Western Region

TESTIMONY OF

WILLIAM H. QUINN
NATIONAL PRESIDENT
NATIONAL POSTAL MAIL HANDLERS UNION

BEFORE THE

HOUSE COMMITTEE ON
GOVERNMENTAL REFORM

ON

CHALLENGES FACING THE U.S. POSTAL SERVICE

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Mr. Chairman and Distinguished Members of the Committee. I am Billy Quinn, National President of the National Postal Mail Handlers Union. On behalf of the more than 50,000 union mail handlers employed by the U.S. Postal Service, I appreciate the opportunity to testify about the challenges currently facing the U.S. Postal Service.

From recent hearings and press reports, it appears that Congress is most concerned about two related issues. The first is the difficult financial situation that currently confronts the Postal Service, with projected deficits for this year and next in the billions of dollars. The second is the need for reform of the Postal Reorganization Act, which is the legislation governing the Postal Service that originally was enacted in 1970.

On the question of postal finances, many of the financial difficulties that the Postal Service currently faces are beyond its control. The American economy began to slow late last year, and that slowdown occurred faster and deeper than predicted, at a pace that was unexpected by virtually all economic forecasters. As a result, the volume of mail has not grown as much as expected, and the mix of that mail has taken an unprofitable turn, thus causing deficits. At the same time, fuel prices continue to rise, imposing additional costs on postal operations. This slowing of the economy is not only affecting the Postal Service, of course. Similar problems are facing Federal Express, the United Parcel Service, and literally thousands of other private companies, and it is foolhardy to expect that the Postal Service would be immune from these general economic trends.

We therefore applaud last week's decision by the Board of Governors to raise rates slightly in an effort to reduce the expected deficit. The Board correctly rejected an arbitrary recommendation issued by the Postal Rate Commission late last year. Although some have suggested cataclysmic results, and have complained about a second rate increase in the past six months, we

believe in this instance that the Board chose a responsible course of action. Indeed, no mailer who complains about rates today ever acknowledges that rates did not increase at all for the two years prior to this latest round of increases.

Unfortunately, the Postal Service also has suggested that it might react to the economic slowdown in other, less responsible ways. For example, the Postal Service is considering whether to curtail residential delivery services one day per week or close non-profitable post offices. Both of these alternatives would reduce services upon which the American public has come to depend, and therefore should be rejected on that basis alone.

Whatever the solution, however, one thing is clear: the Postal Service needs to choose among these alternatives in an operationally prudent manner, without the intervention of Congress and without interference from the Postal Service's direct competitors. Many in Congress like to blame the Postal Service or its dedicated employees for the Service's financial predicament. But a little review of history easily points the finger of blame in other directions. It is Congress, you should remember, that throughout the 1980s and early 1990s used the Postal Service as a cash cow, by imposing unjustified costs on the Postal Service in order to solve general shortfalls in the federal budget. And it was the House of Representatives, after several years of USPS surpluses, that passed a resolution in June 1998 – without any meaningful debate – that essentially forced the Board of Governors to delay a rate increase and forego more than $800 million that was needed to operate the Postal Service.

As for direct competitors, they too share some of the blame. I can assure each and every member of this Committee that UPS, FedEx, and others have only one interest when they participate in the congressional debate over postal reform, and it is not the public interest, it is their own bottom line. Others may hesitate to say that publicly, but that's the fact of the matter.

That brings me to the second major challenge facing the Postal Service, the need for postal reform. On this issue, Congress needs to act to amend the current statute, so I cannot argue against congressional intervention. But Congress needs to act in a responsible and informed manner. The Mail Handlers Union will support legislation that gives the Postal Service flexibility in pricing, the freedom to design or introduce new postal products, and the ability to borrow and invest with fewer constraints. It is patently ridiculous, for example, that the Postal Service is unable to change its pricing structure to compete for the overnight business of the Federal Government. Frankly, I find it embarrassing that the very government which demands universal service from the Postal Service does not use utilize that service.

As many of you know, we have been working with other employee organizations and with representatives of the mailing community to see if a consensus can be reached around these difficult issues. While much work still needs to be done, I am more encouraged today than ever before that appropriate reform of the Postal Reorganization Act can be enacted. A key ingredient in any reform legislation, however, must be protecting the ability of the Postal Service to provide universal service to the mailing public. Postal employees must continue to process and deliver letters and packages at affordable rates, and these rates must be sufficient to protect and support the infrastructure that universal service requires and to provide postal employees with a decent and fair standard of living.

On the other hand, to say that I am encouraged is not to say that I am blindly optimistic. In the last few months, the Board of Governors has used the Postal Service's recent financial difficulties to launch an attack on the collective bargaining process that has governed the Postal Service and its employees for the past thirty years. That attack is wholly unwarranted. We strongly believe that any postal reform legislation must not impede upon the

often complex relationship between the Postal Service and its employees. This relationship, though at times difficult if not contentious, is best carried out within the PRA's current framework for collective bargaining. The collective bargaining process should be treated as sacred, and should not be adversely affected, either intentionally or inadvertently, by enactment of postal reform.

In simple terms, this means that any reform legislation should neither allow nor encourage interference in postal labor relations, either directly by Congress, or less directly through the Postal Rate Commission or some other legislatively imposed body. This also means that the collective bargaining process must be allowed to function without artificially imposed constraints, such as price caps that effectively become wage caps. The bargaining process must be allowed to set wages and benefits, and the Postal Service must be allowed to pay for its labor costs through appropriate postal rates. If fair and decent wages require an increase in postal rates, then the Postal Service must be allowed to raise its rates without jumping through the overly cumbersome hoops that exist under the current PRA.

We look forward to continuing to work with the Committee and its staff during the coming weeks and months to ensure that postal reform legislation is enacted in a form that the NPMHU can support.

Thank you for the chance to testify today. I would be happy to answer any questions you may have.

Mr. BURTON. Thank you, Mr. Quinn.

Mr. Dailing.

Mr. DAILING. Mr. Chairman and members of the committee, my name is Clifford Dailing, and I am the secretary-treasurer of the 100,000 member National Rural Letter Carriers' Association.

Rural letter carriers drive 3 million miles daily to deliver and pick up mail for 30 million customers on over 68,000 rural routes. Rural carrier routes average 46 miles, with 445 stops, delivering 2,875 pieces of mail daily. We offer all the services of a small post office by selling stamps, money orders, and accepting parcels and priority mail.

The Postal Service has added over 1 million new rural deliveries or addresses each of the last several years. I am here today to emphasize our commitment to the future of the U.S. Postal Service that guarantees universal service at uniform prices with 6 day delivery.

To accomplish that goal, however, we believe that Congress, Postal Service management and postal employees must accomplish three things. First, we need Congress to pass postal reform legislation that recognizes the changing face of America, both rural and urban and the changing nature of communication. Rural America, where our members work, depends on 6 day delivery for its commerce and information. E-commerce has not replaced hard copy on the farms and small towns spread across this country. And so far, has reached little even in the city.

Yet the Postal Service is experiencing tremendous financial problems that could result in a deficit this fiscal year between $2 billion and $3 billion. If we are losing money now, before millions of Americans begin using the internet for conducting business that involves the mail, what will happen when the internet actually starts reducing mail volume?

That eventually is one of the reasons why Congress must continue to pursue passage of postal reform legislation. We believe that it is imperative that all Members of Congress join with the leaders of this community in supporting postal reform immediately. The Postal Reorganization Act, or Title 39 of the U.S. Code, was written at a time when the Nation typed with electric typewriters on stationery paper, backed by carbon paper. We had phones but no cell phones, mail but no e-mail.

Today technology has changed our lives considerably. But some postal facts remain unchanged. We still have the lowest postage rates in the world while carrying 46 percent of the world's cards and letter volume. Every day we deliver almost 680 million pieces of mail, far more than any other Nation in the world. In this country, hard copy has not gone away. Nationally, we are in an economic slowdown. As a result, the Postal Service has collected far less revenue this year than was anticipated at the time the last postage rate case planned or filed.

Under current law, the Postal Service begins planning for a rate case almost 2 years before rates can go up. Look at where the stock market was back then. Remember what the price of gas was in 1999, and you'll see why the Postal Service, just like many organizations, is seeing a possible financial crunch. And it's easier to understand postal deficits when you understand that once the Postal

Service actually decides how and when it wants to raise rates, it takes another 10 months before that can occur.

What happens in the meantime? The economy can and often does change dramatically. Fuel prices, a major expense for the Postal Service service transport fleet of over 202,000 vehicles, can increase substantially. Our competitors can adjust the gasoline price escalations by adding a fuel surcharge to their delivery prices. But the Postal Service simply inhales our competitors' truck fumes for at least another 10 months.

That is one example of why the Postal Service needs greater flexibility in ratemaking, as well as in its financing, and in the agreement it can negotiate with its customers. We need legislation to take the current Postal Service into a new era. That brings us to the second major change. We need to ensure the survival of the Postal Service, one that is the responsibility of the Presidentially appointed members of board of Governors. The board directs and controls the Postal Service's expenditures, reviews its practices, conducts long range planning and sets policies on all postal matters. They also select the postmaster general.

With the retirement this month of Bill Henderson, the board is about to select a new postmaster general for this new era. We have a few suggestions for this individual, to provide the leadership the Postal Service desperately needs to thrive in this new era of electronic communication and competition. Begin by working with Congress to move postal reform onto the President's desk. Don't just testify at hearings. Go from member to member to inform and persuade.

Get out of the Postal Service headquarters. Travel with few staff and survive the postal universe. Do it regularly instead of relying on local managers for information. Find out for yourself how we can make this Postal Service a better organization. Visit the facilities where there are problems, so you can listen to managers' and employees' views. Be a good listener, and you'll hear about the tension that exists today in too many local offices, from small offices in isolated rural areas to the biggest post offices in America's largest cities.

What we're suggesting, Mr. Chairman, is that the new postmaster general must attempt to change the culture of the Postal Service. That is the third major objective we in the postal community must address if the Postal Service is to survive another century. We need to improve the postal workplace environment. We don't want managers who dictate but ones who want to cooperate.

The culture must change because today, too many workers feel they are not satisfied employees, and don't feel like winners. When employees feel like winners, managers do too. One particular important problem the new postmaster general can address to improve the postal workplace is our system of incentives. Managers and workers need to have incentives to reach their goals.

The Postal Service needs incentive based work force. The National Rural Letters Carriers has an incentive based work force for many years, one that uses what we call the evaluated pay system. Our system has consistently shown impressive results.

For example, rural letter carriers need less supervision, less help from part-time carriers, overtime is not an issue for us. As a result,

we have few disputes with our supervisors and managers, and thousands fewer grievances compared to the other postal unions. The only major difference in the way we perform our work compared to the other union workers in the Postal Service is our incentive based pay systems.

Rural carriers have the highest employee satisfaction index in the Postal Service. And not coincidentally, rural carrier customers have the highest customer satisfaction index. If we can accomplish these three goals, the passage of new postal law, the appointment of an enlightened PMG, and an improved workplace environment, we could see the U.S. Postal Service empowered to go on for the next 30 years.

Mr. Chairman, and committee, I thank you.

[The prepared statement of Mr. Dailing follows:]

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TESTIMONY

OF

CLIFFORD DAILING
SECRETARY-TREASURER

NATIONAL RURAL LETTER CARRIERS' ASSOCIATION

OVERSIGHT HEARING
STAKEHOLDERS' VIEWS

BEFORE THE

HOUSE GOVERNMENT REFORM COMMITTEE

ON THE

UNITED STATES POSTAL SERVICE

MAY 16, 2001

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First, we need Congress to pass postal reform legislation that recognizes the changing face of America—both rural and urban, and the changing nature of communication. Rural America, where our members work, depends upon six-day delivery for its commerce and information. E-commerce has not replaced hard copy on the farms and small towns spread across this country, and so far has replaced little even in the city. Yet the Postal Service is experiencing tremendous financial problems that could result in a deficit this fiscal year between $2 and $3 billion. If we are losing money now, before millions of Americans begin using the Internet for conducting business that involves the mail, what will happen when the Internet actually starts reducing mail volume? That eventuality is one of the reasons why Congress must continue to pursue passage of postal reform legislation. We believe that it is imperative that all Members of Congress join with the leaders on this committee in supporting postal reform immediately.

The Postal Reorganization Act, or Title 39 of the U.S. Code, was written at the time when the nation typed with electric typewriters on stationery paper backed by carbon paper. We had phones, but no cell phones, mail but no email. Today, technology has changed our lives considerably, but some postal facts remain unchanged. We still have the lowest postage rates in the world, while carrying 46 percent of the world's cards and letter

volume. Every day we deliver almost 680 million pieces of mail—far more than any other nation in the world. In this country hard copy has not gone away.

Nationally we are in an economic slowdown, and as a result the Postal Service has collected far less revenue this year than was anticipated at the time the last postage rate case planned or filed. Under current law the Postal Service begins planning for a rate case almost two years before rates can go up. Look at where the stock market was back then, remember what the price of gas was in 1999, and you'll see why the Postal Service, just like many organizations, is seeing a possible financial crunch. And it's easier to understand postal deficits when you understand that once the Postal Service actually decides how and when it wants to raise rates, it takes another 10 months before that can occur.

What happens in the meantime? The economy can and often does change dramatically. Fuel prices, a major expense for the Postal Service's transport fleet of over 202,000 vehicles, can increase substantially. Our competitors can adjust to gasoline price escalations by adding a fuel surcharge to their delivery prices, but the Postal Service simply inhales our competitor's truck's fumes for at least another 10 months. That's just one example of why the Postal Service needs greater flexibility in ratemaking—as well as in it's financing, and in the agreements it can negotiate with its customers. We need legislation to take the current Postal Service into a new era.

That brings us to the second major change we need to ensure the survival of the Postal Service, one that is the responsibility of the presidentially-appointed members of the Board of Governors. The Board directs and controls the Postal Service's expenditures, reviews its practices, conducts long-range planning, and sets policies on all postal matters. They also select the postmaster general. With the retirement this month of Bill Henderson, the Board is about to select a new postmaster general for this new era.

We have a few suggestions for this individual. Provide the leadership the Postal Service desperately needs to thrive in this new era of electronic communication and competition. Begin by working with Congress to move postal reform on to the President's desk. Don't just testify at hearings. Go from Member to Member to inform and persuade.

Get out of Postal Service Headquarters, travel with few staff, and survey the postal universe. Do it regularly. Instead of relying on local managers for information, find out for yourself how we can make this Postal Service a better organization. Visit the facilities where there are problems, so you can listen to managers' and employees' views. Be a good listener, and you will hear about the tension that exists today in too many local offices, from small offices in isolated rural areas to the biggest post offices in America's largest cities.

What we're suggesting, Mr. Chairman, is that the new postmaster general must attempt to change the culture of the Postal Service. That is the third major objective we in the postal community must address if the Postal Service is to survive another century. We need to improve the postal workplace environment. We don't want managers who dictate, but ones who want to cooperate. The culture must change because today, too many workers feel they are not satisfied employees and don't feel like winners. When employees feel like winners, managers win too.

One particularly important problem the new postmaster general can address to improve the postal workplace is our system of incentives. Managers and workers need to have incentives to reach their goals. The Postal Service needs an incentive-based workforce. NRLCA has an incentive-based workforce for many years; one that uses what we call the evaluated pay system. Our system has consistently shown impressive results. For example, rural letter carriers need less supervision, less help from part-time carriers. Overtime is not an issue for us. As a result, we have few disputes with our supervisors and managers, and thousands fewer grievances compared to the other postal unions. And the only major difference in the way we perform our work compared to other union workers in the Postal Service is our incentive-based pay system.

Rural Carriers have the highest employee satisfaction index in the Postal Service. And not coincidentally, Rural Carrier customers have the highest customer satisfaction index.

If we can accomplish these three goals—the passage of a new postal law, the appointment of an enlightened PMG and an improved workplace environment, we could see the U.S. Postal Service empowered to go on for the next 30 years.

Mr. BURTON. Thank you, Mr. Dailing.

Mr. Sombrotto.

Mr. SOMBROTTO. Thank you, Chairman Burton, for the opportunity to testify today on the subject of postal reform.

Before I get started, I would like to make a couple of brief comments. First of all, very late last night, an unprecedented and unconventional move, the Postal Service board of Governors submitted to this committee, as well as the Senate Governmental Affairs Committee their suggestions on postal reform. I would like for the NALC to have the opportunity to enter into the record some remarks as it pertains to their particular submission.

Mr. BURTON. Mr. Sombrotto, we encourage that, we'd like to have remarks and suggestions from all of you. We're going to put all of those things into the mix and try and come up with a bill that everyone can live with.

Mr. SOMBROTTO. Thank you. In order to supplement my testimony, I have a number of charts and graphs that I want to make available to the committee for their perusal. I am Vincent Sombrotto, president of the National Association of Letter Carriers, representing more than 315,000 active and retired letter carriers.

For more than 6 years, the NALC has worked closely with Representative John McHugh and other members of this committee to come up with meaningful postal reform legislation. Those efforts evolved into H.R. 22, a bold approach to reforming the postal service. I fear that if we do not act soon, even the far-reaching goals envisioned in H.R. 22 will not be enough to put the Postal Service on a stable foundation.

The Postal Reorganization Act of 1970 is more than 30 years old, and predates the advent of the Internet and other advanced electronic communications. Moreover, the legislation could not have anticipated the intense global competition that now exists within the delivery service marketplace. If the reports coming from the U.S. Postal Service are to be believed, we will be facing some major challenges in the near future.

Under the current system, the Postal Service is particularly vulnerable to economic fluctuations. For example, the Postal Service delivers more than 52 million pieces of financial mail each year. An economic slowdown, coupled with the reduced commercial lending and marketing cutbacks, results in lower mail volume and reduced postal revenue. Understandably, many feel that rates should not be increased until the Postal Service has cut their costs. However, the number of delivery points grow by some 5,600 addresses a day, and mail volume is relatively flat. The result is higher cost without increased revenue.

The Postal Service can and should be seeking the statutory freedom to expand the services they offer, including negotiated service agreements and creating joint ventures with private companies. Unfortunately, some of the suggestions put forth by the Postal Service have gone in the opposite direction. The Postal Service's recent overtures to cut back on service or erode collective bargaining rights are neither desirable nor are they feasible. Instead, the Postal Service should be looking at ways to enhance service.

If your product or service is running head to head into stiffer competition, whether it be from other businesses, emerging tech-

nologies or both, you don't reduce the quality of your product or your service so it's less attractive to its customers. You try to figure out how to improve your product or service. In the case of the Postal Service, this would mean more timely delivery and innovations that meet consumers' changing needs.

For businesses, the Postal Service could look to flexible pricing, information about the progress of mailings and perhaps new logistical and inventory control services. Ideas such as 5 day delivery are not an enhancement of service.

The other point that has been raised recently pertains to the collective bargaining system, which the Postal Service operates. Despite the commitment that John McHugh has made to the current collective bargaining system, and the agreement of many of our largest postal customers that changes to collective bargaining will not be part of the postal reform bill, some continue to bring up this issue.

I know that you, Mr. Chairman, have already understood that the NALC will not support any postal reform bill that includes erosion of the collective bargaining rights, and specifically third party arbitration. Without third party arbitration as a last resort, should the parties be unable to reach what the NALC has always sought, a negotiated settlement, there would be no pressure on management to negotiate fairly and constructively.

Calling for doing away with the rights of a neutral third party arbitration in exchange for the right to strike are a non-starter with us. As we march down the road toward postal reform, there are some key principles that we must adhere to. The preservation of universal service is paramount. This means providing full mail service to every address 6 days a week. Other essential elements, including enabling the Postal Service to enter into contractual agreements and providing it with the flexibility to adapt to unexpected changes in the economy, such as the recent increases in fuel prices.

The NALC is committed to working with all of the stakeholders in the postal reform debate. In addition to working with you, Mr. Chairman, and Congressman McHugh and Congressman Davis, we know that this has to be a bipartisan effort. We need active input of Ranking Member Henry Waxman as well as Danny Davis, who has also demonstrated great leadership behind this issue.

Thank you again for the opportunity to provide testimony here today. I look forward to working with you to meet the challenges of enacting postal reform. I'll be happy to answer any questions.

[The prepared statement of Mr. Sombrotto follows:]

VINCENT R. SOMBROTTO
PRESIDENT

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Testimony of

VINCENT R. SOMBROTTO, PRESIDENT

Before the
U.S. HOUSE OF REPRESENTATIVES
COMMITTEE ON
GOVERNMENT REFORM

May 16, 2001

CONGRESSIONAL TESTIMONY

Testimony of
Vincent R. Sombrotto
President of the National Association of Letter Carriers
Before the
U.S. House of Representatives
Committee Government Reform
May 16, 2001

Thank you Chairman Burton for the opportunity to testify today on the subject of postal reform. I am Vince Sombrotto, President of the National Association of Letter Carriers, representing more than 315,000 active and retired letter carriers. Our members are the men and women out on the streets of America delivering mail to more that 130 million places six days a week. They are a dedicated and professional group who work hard to serve the public.

For more than six years, the NALC has worked closely with Representative John McHugh and other members of this committee to come up with meaningful postal reform legislation. In the beginning we had some serious concerns about some of the provisions of the bill. Rather than walking away, we chose to work with Mr. McHugh and the end result was HR 22 — a bold approach to reforming the Postal Service. I fear that if we do not act soon, even the far-reaching goals envisioned in HR 22 will not be enough to put the Postal Service on a stable foundation. That is because every day without action is another day that the Postal Service continues to operate under an outdated statutory model and an expensive — albeit vital — universal service mandate. The "Postal Reorganization Act of 1970" is more than 30 years old and pre-dates the advent of the internet and other advanced electronic communication. Moreover, the legislation could not have anticipated the intense global competition that now exists within the delivery service marketplace. If we are to continue to provide the high level of service the American public has come to expect from us, then we must take action and we must take it soon.

If the reports coming from the United States Postal Service are to be believed, we will be facing some major challenges in the near future. Under the current system, the Postal Service is particularly vulnerable to economic fluctuations. For example, the Postal Service delivers more than 52 billion pieces of financial mail -- statements, invoices, payments -- each year. An economic slowdown, coupled with reduced lending by banks and marketing cutbacks all result in lower mail volume and reduced postal revenue.

There is an understandable sentiment that there should not be increased rates until the Postal Service has cut their costs. However, the number of delivery points grows by some 5600 addresses a day, and mail volume is relatively flat. The result is higher costs without increased revenue. Therefore, the Postal Service needs a statutory framework that will enable it to find new ways of generating revenue. The Postal Service can and should be seeking ways to expand the services they offer, including negotiated service agreements and creating joint ventures with private companies. Unfortunately, some of the suggestions put forth by the Postal Service have gone in the opposite direction.

The Postal Service's recent overtures to cut back on service or erode collective bargaining rights are neither desirable nor are they feasible. We hope that the Postal Service has finally recognized this reality and is prepared to work with us on finding ways to improve performance and to provide this great institution with the tools needed to succeed in this new economy. The Postal Service should be looking at ways to enhance service, not looking at five day delivery or cutting back on its core services. If your product or service is running head-on into stiffer competition — perhaps from other business, perhaps form emerging technologies, perhaps from both — you don't reduce the quality of your product or service so it's *less* attractive to customers. You try to figure out how to *improve* your product or service. In the case of the Postal Service, this would mean more timely delivery as well as innovative services and products that meet consumers' changing needs. For businesses, the Postal Service could look to flexible and market-driven pricing, accurate and timely information about the progress of their mailings and perhaps new logistical and inventory control services. Ideas such as five day delivery are *not* an enhancement of service.

The other point that has been raised recently pertains to the collective bargaining system under which the Postal Service operates. Despite the commitment that John McHugh has made to the current collective bargaining system and the agreement of many of the largest postal customers that changes to collective bargaining will not be a part of a postal reform bill, some continue to bring up the issue.

Let me make clear what you, Mr. Chairman, already understand — that the NALC will not support any postal reform bill that includes erosion of collective bargaining rights and, specifically, third-party arbitration. Without third-party arbitration as the last resort should the parties be unable to reach what the NALC has always sought — a negotiated settlement — there would be no pressure on management to negotiate fairly and constructively. Calls for doing away with the right of neutral third-party arbitration in exchange for the right to strike are a non-starter with us. The models cited, such as

the "Railway Labor Act" would drastically undermine the rights of all postal employees. Binding arbitration enables our members to do their job and, when management is not willing to achieve a negotiated settlement, provides letter carriers with a fair way to get a fair contract for their work.

As we march down the road toward Postal Reform there are some key principles that we must adhere to — in addition to protecting collective bargaining — including the preservation universal service and giving the Postal Service greater flexibility. The preservation of universal service is paramount. This means providing full mail service to every address, six days a week. As one of the members of this committee said at a recent breakfast for letter carriers, "we must stand up for universal service, because it is a key element in communication among Americans." Other essential elements include enabling the Postal Service to enter into contractual agreements and providing it with the flexibility to adapt to unexpected changes in the economy, such as the recent increases in fuel prices.

The Postal Service has a constituency that is as vast and diverse as the country itself. Legislation affecting this institution affects us all. That is why we have reached out and worked alongside other key players in the postal reform effort — not just elected officials, but some of the people and organizations that have a large stake in the future of the Postal Service. We have made significant progress in reaching agreement on a number of issues and continue to reach toward a comprehensive approach to reform that has broad support.

The NALC is committed to working with all of the stakeholders in the postal reform debate. In addition to working with you, Mr. Chairman, and Congressman McHugh, we know that this has to be a bipartisan effort. In order to address the challenges facing the Postal Service we need active input of ranking member Henry Waxman, as well as Representative Danny Davis, who has also demonstrated great leadership on the issue.

Thank you for the opportunity to provide the testimony here today, and I look forward to working with you to meet the challenges of enacting postal reform.

Mr. BURTON. Thank you, Mr. Sombrotto.

Mr. Biller.

Mr. BILLER. Chairman Burton, members of the committee, my name is Moe Biller, I'm president of the American Postal Workers Union, AFL–CIO, with a membership of 366,000. Thank you for your invitation to provide testimony today on the major challenges facing the U.S. Postal Service and the impact these challenges may have on the members of the American Postal Workers Union.

I have been a close observer of postal operations and postal labor relations and public policy as it affects the U.S. Postal Service for nearly 65 years. I've been President of the American Postal Workers Union almost 21 years. I have known and worked under 20 postmasters general of the United States.

We are appalled that the postal board of Governors has informed the Congress that they wish to destroy the collective bargaining process of postal employees as it exists today. As we understand it, the board of Governors has proposed that collective bargaining in the Postal Service be governed in part by the Railway Labor Act. The board of Governors apparently intends to pay lip service to the principle that postal workers should have the right to strike, but in the manner that this is proposed, the right to strike would be a total fiction.

Application of the Railway Labor Act to the U.S. Postal Service would not provide a meaningful right to strike, and the Postal Service knows this well. What they are really saying is that they would rather place wages, hours and working conditions into the hands of the President and the Congress rather than impartial arbitrators chosen by the parties.

Under the Railway Labor Act, when a labor dispute threatens to disrupt an essential service, the dispute is placed before a Presidential emergency board. This would inevitably happen whenever postal unions and management fail to reach agreement and the dispute would be dumped into the lap of the President and the Congress. No strike would be permitted and postal management would simply abdicate its responsibility to bargain.

This is obvious from looking at the railroad and air transit industry. For the past 15 years, every rail labor dispute has prompted Federal Government intervention. The recent Northwest Airlines dispute is another example of the right to strike, how the right to strike is fought under the Railway Labor Act. The Railway Labor Act also results in long delays. In the Amtrak dispute in the early 1990's, workers worked without a contract for more than 4 years.

It is perfectly clear that the board of Governors has no intention of permitting a strike. They simply want to deprive employees of any means to force the Postal Service into good faith negotiations. I can tell you that the detailed standards the board suggests by setting bargaining unit compensation, unlike the stance it proposes for setting management compensation, will not give postal workers fair and equitable treatment.

The Postal Service also wants to be free of the unfair labor practice jurisdiction of the National Labor Relations Board. Rail Labor Administration coverage would deprive the National Labor Relations Board of jurisdiction. The Postal Service would avoid finding that it committed unfair labor practices, including findings that if

the Service fails to bargain in good faith and discriminates against employees for protected activities.

Instead of an administrative remedy for unfair labor practices, postal unions would be forced into court to enforce the law. This would be time consuming and expensive for both the Postal Service, the unions and the courts.

In short, the board of Governors proposal is contrary to every sound tenet of labor relations. Postal workers would be deprived of free collective bargaining, which is still limited today, while the Postal Service is deprived of its stated goals. The board's proposal would build in more delay and more costs without resolving the problems for Postal Service labor relations.

The APW supports giving postal workers the right to strike under the National Labor Relations Act. If the Postal Service wants to be treated like a private sector employer, for example, UPS, postal employees should be covered by the National Labor Relations Act and have the right to strike.

Finally, I must comment on the proposal to strip veterans of their rights and to decimate employee fringe benefits. Veterans who have served their country with distinction deserve employment protections and postal workers deserve decent health and retirement benefits. The proposal to strip them of health benefits and retirement exposes the Postal Service desire to return postal employees to welfare eligibility. Postal workers are hard working and productive. The proposal by the board of Governors demeans these dedicated workers.

I would like those remarks to be added to the rest of my testimony.

Mr. BURTON. Mr. Biller, we will add the other remarks that you'd like to add.

Mr. BILLER. I apologize for the momentary delay. With me today is Mr. William Burrus, on my left, who serves as executive vice president of the American Postal Workers for 21 years. He served before that as the president of the Cleveland Area local of the American Postal Workers Union and other important offices. The testimony we're giving today is not just our personal testimony. However, it is given on behalf of our 366,000 dedicated employees of the Postal Service, which we are privileged to represent.

I took out the part where it says my remarks will be brief. [Laughter.]

I have little doubt that the process of considering these issues will be intensive and most likely extensive. During that process, the resources of the American Postal Workers Union, its staff and professional consultants are available to provide the committee with any assistance that might be helpful.

I'm going to address four more points in this brief testimony. Take out the word brief. First, I will state our views concerning the reasons for the present financial difficulties for the Postal Service. These views are based upon relatively indisputable public records of the Postal Service.

Second, I want to place the present challenges facing the Postal Service in perspective. The sky is not falling, and it's important that the Congress of the United States make sound policy decisions, notwithstanding the cries of the doomsayers.

Third, I want to emphasize that postal workers represented by the American Postal Workers Union have been and are an important part of successes achieved by the U.S. Postal Service since postal reorganization in 1970.

Finally, before concluding, I want to state a few basic principles that the American Postal Workers Union considers fundamental to any sound effort to improve the Postal Service through legislation. On the question of the Postal Service current financial situation, I want to emphasize first the comments of no less an authority than Postmaster General William Henderson and a member of the board of Governors, as they repeatedly pointed out in testimony before Congress and elsewhere the current financial problems of the Postal Service are a revenue issue and not a cost issue. The Postal Service is indeed an economic bellwether. The current sharp and unanticipated slowdown in our economy explains a substantial part of the current deficit projection of the Postal Service.

Very similar views were expressed by a representative of the General Accounting Office in their congressional testimony, to the effect that the biggest unknown about the postal revenue this year is how soft the economy will be. The critics of the Postal Service costs are largely business mailers. These same businesses profit handsomely because the Postal Service has reduced their postage rate by many billions of dollars in return for the performance of preparatory work.

In the recent rate case, the Postal Service acknowledged that it could not justify the current discounts on the basis of cost avoidance. As you evaluate the final strength of the Postal Service, it is important that you maintain some perspective on the present situation. There are two types of perspectives I would like to mention, short term and long term. I will deal with the short term perspectives first.

Congress and the mailing community are very concerned that the Postal Service has projected potential deficits of $2 billion or $3 billion for this fiscal year. We have the same concerns. Only 6 fiscal years ago, in 1995, the Postal Service enjoyed the largest increase in operating profits of any company in the world, and earned $1.8 billion. In two other years, the Postal Service generated profits of $6 billion and $1.3 billion.

By 1998, the criticism of the Postal Service was that it was generating too much surplus money. Thus, in the relatively short term perspective of 3 to 6 years, it's clear that the Postal Service as presently configured and operated has the capacity to generate substantial surpluses as well as substantial deficits.

The long term perspective I want to offer begins 31 years ago. In 1970, postal workers were at that time Federal Government employees engaged in the nationwide work stoppage. They withheld their labor because working conditions were intolerable and wage levels were unacceptably low. In 1970, postal workers in New York City qualified for welfare. It is important to recall that in the Postal Reorganization Act, Congress addressed the problems of inadequate pay by enacting an increase in postal wage, in fact, two of them.

Thereafter, Congress widely provided the free collective bargaining of wages, hours and working conditions. From 1970 through

2000, the real wages of bargaining unit postal employees has adjusted for inflation and have remained virtually unchanged. Those who call for a decrease in postal workers' compensation as a way of saving money must confront this fact. Postal workers will not accept a cut in real wages. We will not go back to inadequate pay and welfare in a number of areas in this country. Any attempt to take that approach to the financial problems of the Postal Service will be self-defeating.

So whether your perspective is short term, within the last 3 to 6 years, or long term, the 31 years since postal reorganization, the present financial crisis should not be permitted to obscure the fact that the Postal Service has succeeded in keeping postage rates in line with the underlying rate of inflation in our economy.

Next, I would like to discuss the third of my four topics, the contributions of rank and file workers to the success of the U.S. Postal Service. At this time, bargaining unit wages are only 57 percent of Postal Service operating revenues. I want to emphasize that this 57 percent includes all bargaining unit employees combined, not just APW bargaining unit employees. Rapid automation has reduced labor costs as a portion of postal revenues. Postal workers are now more productive than ever, and postal worker productivity has played an important part in keeping postal rates in line with inflation and our economy.

Finally, I want to outline the principles the APW considers as of fundamental importance should Congress consider legislation to change the postal service. One, the ratemaking process as it presently exists takes too long. Either the present ratemaking process must be compressed into 6 months or less, or it should be replaced with a different process.

Legislation must protect universal postal service, including 6 day delivery of mail. This is essential both for the public welfare and the financial health of the U.S. Postal Service.

Three, we support the provision of pricing flexibility for the Postal Service. As close observers of the antiquated postal ratemaking process and of the marketplace, we are convinced that the Postal Service has been forced to operate in a highly competitive market with one hand tied behind its back. Additional pricing flexibility is warranted.

And No. 4, the right to engage in collective bargaining for wages, hours and working conditions must be protected. Postal workers will not accept any effort to go back to 1970 or earlier. Any such effort, if it were accomplished, would be counterproductive. We have opposed in the past and we will continue to oppose legislation that places an artificial cap on postal wages. Such legislation would strike the heart of free collective bargaining.

Mr. Chairman, this concludes my prepared remarks. And Executive Vice President Burrus on my left and I are available to answer your questions. We'll be more than happy to make staff and professional consultants of our union available to the committee for consultation or any other assistance we can provide.

Thank you again for inviting us to be with you today.

[The prepared statement of Mr. Biller follows:]

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TESTIMONY OF
MOE BILLER, PRESIDENT

AMERICAN POSTAL WORKERS UNION, AFL-CIO

ON

"CHALLENGES FACING THE U.S. POSTAL SERVICE"

BEFORE THE

COMMITTEE ON GOVERNMENT REFORM
U.S. HOUSE OF REPRESENTATIVES

MAY 16, 2001

Congressional Testimony

TESTIMONY BY PRESIDENT MOE BILLER

Chairman Burton and members of the committee, my name is Moe Biller and I am President of the American Postal Workers Union, AFL-CIO. Thank you for your invitation to provide testimony today on the major challenges facing the United States Postal Service and the impact those challenges may have on the members of the American Postal Workers Union.

I have been a close observer of postal operations, postal labor relations, and public policy as it affects the Postal Service, for more than 60 years. I have been President of the American Postal Workers Union for nearly 21 years. I have known and worked with 20 Postmasters General of the United States.

With me here today is Executive Vice President William Burrus who has served as Executive Vice President of the American Postal Workers Union for nearly 21 years, and who served for many years as the President of the Cleveland, Ohio Area Local of the APWU and in other important offices.

The testimony we give today is not just our personal testimony, however, it is given on behalf of the 366,000 dedicated employees of the United States Postal Service represented by the American Postal Workers Union.

My remarks today will be brief relative to the importance and complexity of the issues before this committee. I have little doubt that the process of considering these issues will be

intensive, and most likely extensive. During that process, the resources of the American Postal Workers Union, its staff and its professional consultants are available to provide the committee any assistance or information that might be helpful.

I am going to address four points in this brief testimony. First, I will state our views concerning the reasons for the present financial difficulties of the Postal Service. These views are based upon relatively indisputable public records of the Postal Service. Second, I want to place the present challenges facing the Postal Service in perspective. The sky is not falling, and it is important that Congress make sound policy decisions -- notwithstanding the cries of the doomsayers.

Third, I want to emphasize that postal workers represented by the APWU have been and are an important part of the successes achieved by the United States Postal Service since postal reorganization in 1970.

Finally, before concluding, I will state a few basic principles that the American Postal Workers Union considers fundamental to any sound effort to improve the Postal Service through legislation.

Reasons for Deficits in Fiscal 2001

On the question of the Postal Service's current financial situation, I want to emphasize

first the comments of no less an authority than Postmaster General William Henderson and a member of the Board of Governors. As they have repeatedly pointed out, in testimony before Congress and elsewhere, the current financial problems of the Postal Service are a revenue issue not a cost issue. The Postal Service is indeed an economic bellwether. The current sharp and unanticipated slowdown in our economy explains a substantial part of the current deficit projection of the Postal Service. Very similar views were expressed by representatives of the General Accounting Office in their Congressional testimony, to the effect that the biggest unknown about postal revenues this year is how soft the economy will be.

Those who want to understand the present financial situation of the Postal Service should recognize that the gross domestic product in this country grew at a rate of 5 percent last year. This year it will grow at approximately 2 percent. That slowdown in growth, and its impact on first class mail volume growth, translates into approximately a 650-million-dollar swing in postal revenues from first class mail alone.

In saying this, I want to emphasize that first class mail volume is still increasing. So far this year the Postal Service is projecting a slower rate of increase in first class mail volume, not a decrease in mail volume.

Another very substantial factor has been the increase in energy costs. This inflated cost alone will drain approximately 500 million dollars in additional costs from the Postal Service in this fiscal year.

As an aside to those who might be focusing on postal wages as a way of finding money for the Postal Service, the extra cost of energy for this fiscal year of 500 million dollars would be enough to provide 3 percent additional compensation this year for postal workers represented by the American Postal Workers Union. This reflects the magnitude of costs other than wages that affect postal financial performance.

I have focused on rising energy costs first in my discussion of the reasons for the current financial problems of the Postal Service, because those are the most immediate reasons. However, there is another reason that in our view is equally important, and in the long term may be the most important.

It is now virtually indisputable that the Postal Service is providing overly generous postal-rate discounts to qualifying mailers. In addressing this issue, it is important that Congress recognize the magnitude of these discounts. The revenue lost by the Postal Service as a result of these discounts, if volume is held constant, is 50 percent of the total salaries and benefits paid to Postal Service bargaining-unit employees.

The critics of Postal Service costs are largely business mailers. Those same businesses are profiting handsomely by the fact that the Postal Service has reduced postage rates by many billions of dollars every year in return for the performance of preparatory work. In the recent rate case, the Postal Service acknowledged that it could not justify current discounts on the basis of costs avoided. This is such a critical point, that I am going to quote briefly from testimony given

to the Postal Rate Commission on behalf of the Postal Service:

> "[If] the proposed work share discounts were tied strictly to avoided costs, many discounts would need to be reduced. Instead, the Postal Service's proposal in this docket will generally maintain work share discounts at their present levels... . However, if the cost data presented in this docket are the beginning of a new cost trend indicating that the value of work sharing to the Postal Service has peaked , then the mailing community might anticipate smaller discount proposals in the future.

In laymen's terms, this means that the Postal Service is subsidizing presort houses and large mailers through unjustifiably large rate discounts. In defense [of these overly large discounts], the Postal Service has alluded to "fairness and equity," and "the effect of the rate increase on mailers." In short, the Postal Service has said that it does not want to discontinue subsidies of large mailers too rapidly. In assessing the "equity" of that position, it should be emphasized that the people bearing the costs of that subsidy are all the other mailers in the system.

As you evaluate the financial strength of the Postal Service, it is important that you maintain some perspective on the present situation.

Present Challenges Placed in Perspective

There are two types of perspective I want to mention, short term and long term. I will

deal with short-term perspective first. Congress and the mailing community are very concerned that the Postal Service has projected potential deficits of two or three billion dollars for this fiscal year. Only six fiscal years ago, in 1995, the Postal Service enjoyed the largest increase in operating profits of any company in the world and earned 1.8 billion dollars. In two other years, the Postal Service generated profits of 1.6 billion dollars and 1.3 billion dollars. By 1998, the criticism of the Postal Service was that it was generating too much surplus money. Thus, from a relatively short-term perspective of three to six years, it is clear that the Postal Service as it is presently configured and operated has the capacity to generate substantial surpluses, as well as substantial deficits.

The long-term perspective I want to offer begins 31 years ago. In 1970, postal workers - who were at that time Federal Government employees - engaged in a nationwide work stoppage. They withheld their labor because working conditions were intolerable and wage levels were unacceptably low. In 1970, postal workers in New York City qualified for welfare.

Leading experts in labor relations, economists, and experts on public administration and public policy intensively studied the Post Office Department to determine what to do about the crisis of 1970. President Nixon and his administration were intimately involved in finding solutions to the problems of the Post Office Department.

It is important to recall that, in the Postal Reorganization Act, Congress addressed the problem of inadequate pay by enacting an increase in postal wages. Thereafter, Congress wisely

provided for free collective bargaining over wages, hours and working conditions.

From 1970 through 2000, the real wages of bargaining unit postal employees (wages adjusted for inflation) have remained virtually unchanged. Those who call out for a decrease in postal workers' compensation as a way of saving money must confront this fact. Postal workers will not accept a cut in real wages. We will not go back to inadequate pay. Any attempt to take that approach to the financial problems of the Postal Service would be self-defeating.

I have heard and read criticism of the collective bargaining process under the Postal Reorganization Act, particularly its provision for final-and-binding arbitration when the parties fail to reach agreement.. Those who voice that criticism should recognize that over the past 30 years, the APWU has reached voluntary collective bargaining agreements on wages with management on six occasions. Each of those agreements required, on average, wage increases well within the range of inflation. On the four occasions the parties were required to resort to binding arbitration, neither party achieved all it desired. In each case, the agreement was the result of a decision by an experienced and responsible neutral arbitrator. There is simply no objective case to be made that postal wages or collective bargaining are a part of the problem for the Postal Service.

So whether your perspective is short term (within the last three to six years) or long term (the 31 years since postal reorganization), the present financial crisis should not be permitted to obscure the fact that the Postal Service has succeeded in keeping postage rates in line with the

underlying rate of inflation in our economy. Despite its present financial difficulty, the Postal Service has substantial strength and is capable of performing well, presently and in the future, as it is now configured.

So, I think it is plain that the present Postal Service circumstances, when viewed in long-term and short-term perspectives, and in the light of current financial developments affecting the Postal Service, can be understood. The sky is not falling, and the Postal Service is a strong and vital institution.

Next, I want to discuss the third of my four topics, the contribution of rank and file workers to the success of the United States Postal Service.

Bargaining-Unit Labor Costs Have Steadily Declined As A Proportion of Postal Service Costs

I am proud to say that under my administration, which has now continued for nearly 21 years, the American Postal Workers Union has never opposed automation. We do believe that postal workers who have their jobs drastically changed and in some cases downgraded as a result of automation deserve compensation, and every consideration, for the impact of automation on their lives. Collective-bargaining-unit labor costs have steadily declined as a proportion of total Postal Service costs. At this time, bargaining unit wages are only 57 percent of Postal Service operating revenue. I want to emphasize that this 57 percent that I am referring to is all bargaining-unit employees combined, not just APWU bargaining unit employees.

APWU bargaining-unit wages are now only 27 percent of Postal Service operating revenue and our wages as a share of postal revenues have fallen in nine out of the last ten fiscal years. (From 1996 to 1997 they remained virtually unchanged as a percentage of postal revenues.)

In some remarks I have read and heard recently about the financial position of the Postal Service, these numbers have been misstated and exaggerated. In response to those misstatements and exaggerations, I want to emphasize that the compensation of non-bargaining-unit managerial employees is approximately 23 percent of postal revenues. Bargaining-unit wages have dropped as a percentage of Postal Service revenues while compensation for managers has risen faster than compensation for bargaining-unit employees. Critics of collective bargaining and interest arbitration should focus their attention on the compensation of managers and supervisors to determine whether the Postal Service has acted appropriately in an area where it does not have to deal with the right to collective bargaining and interest arbitration.

My fundamental point is not to criticize management compensation, that is really not our concern. My point is that rapid automation has reduced labor costs as a proportion of postal revenues. Postal workers are now more productive than ever, and that productivity has played an important part in keeping postal rates in line with inflation and the economy.

So, one can see that the present financial condition of the Postal Service when viewed in perspective, reflects substantial strength and a generally sound performance. Furthermore,

analysis of the reasons for the deficit do not reveal any fundamental problem with the Postal Service, but instead reflect a confluence of economic factors that is relatively short term. A bigger long-term problem may be the fact that the Postal Service needs to adjust its presort and other discounts to avoid subsidizing large mailers at the expense of all other mailers. As the people who have borne the brunt of postal automation, both in the form of disrupted lives and a downgrading of compensation levels, we want to emphasize that the Postal Service deserves credit for effective automation, and workers deserve increases in their compensation to reflect their increased productivity.

Finally, I want to turn to my fourth topic, an outline of the principles the APWU considers of fundamental importance if Congress intends to consider legislation that would change the Postal Service.

Fundamental Principles for Postal Legislation

1. The rate-making process as it presently exists takes too long. Either the present rate-making process must be compressed into six months or less, or it should be replaced with a different process.

2. Legislation must protect universal postal service, including six-day delivery of mail. This is essential both for the public welfare and for the financial health of the United States Postal Service.

3. We support the provision of pricing flexibility for the Postal Service. As close observers of the antiquated postal rate-making process, and of the marketplace, we are convinced that the Postal Service has been forced to operate in a highly competitive market with one hand tied behind its back. Additional pricing flexibility is warranted; and

4. The right to engage in collective bargaining for wages, hours and working conditions must be protected. Postal workers will not accept an effort to go back to 1970. Any such effort, if it were accomplished, would be counterproductive. We have opposed in the past, and we will continue to oppose legislation that places an artificial cap on postal wages. Such legislation would strike at the heart of free collective bargaining.

That concludes my prepared remarks. Executive Vice President Burrus and I are available to answer your questions, and we will be more than happy to make the staff and professional consultants of the American Postal Workers Union available to the Committee for consultation or any other assistance we can provide.

Thank you for inviting us to be with you today.

APWU COMMENTS ON BOARD OF GOVERNORS PROPOSAL

As you know, the prepared testimony on behalf of the APWU expresses our support for postal reform that would give the Postal Service relief from the present unworkable rate process and give it needed pricing flexibility in areas where they are in direct competition with the private sector.

We are appalled that the Postal Board of Governors has informed Congress that they wish to destroy the collective bargaining rights of postal employees. As we understand it, the Board of Governors has proposed that collective bargaining in the Postal Service be governed in part by the Railway Labor Act.

The Board of Governors apparently intends to pay lip service to the principle that postal workers should have the right to strike. But in the manner that this is proposed, the right to strike would be a total fiction.

Application of the Railway Labor Act to the United States Postal Service would not provide a meaningful right to strike – and the Postal Service knows it. What they are really saying is that they would rather place wages, hours, and working conditions into the hands of the President and the Congress rather than arbitrators chosen by the parties.

Under the Railway Labor Act, when a labor dispute threatens to disrupt an essential service, the dispute is placed before a presidential emergency board. This would inevitably happen whenever postal unions and management fail to reach agreement and the dispute would be dumped into the lap of the President and Congress. No strike would be permitted and Postal management would simply abdicate its responsibility to bargain.

This is obvious from looking at the railroad and air transit industries. For the past fifteen years, every rail labor dispute has prompted federal government intervention. The recent Northwest Airlines dispute is another example of how the right to strike is thwarted under the Railway Labor Act.

The RLA also results in long delays. In the Amtrak dispute in the early 1990s, workers went without a contract for more than four years.

It is perfectly clear that the Board of Governors has no intention of permitting a strike – they simply want to deprive employees of any means to force the Postal Service into good faith negotiations. I can tell you that the "detailed standards" the Board suggests for setting bargaining unit compensation (unlike the standards it proposes for setting management compensation) do not give postal workers fair and equitable treatment.

The Postal Service also wants to be free of the unfair labor practice jurisdiction of the National Labor Relations Board. RLA coverage would deprive the NLRB of jurisdiction. The Postal Service would avoid findings that it committed unfair labor practices - including findings that the Service fails to bargain in good faith and discriminates against employees for protected activity. Instead of an administrative remedy for unfair labor practices, postal unions would be forced into court to enforce the law. This would be time consuming and expensive for the Postal Service, the unions, and the courts.

In short, the Board of Governors' proposal is contrary to every sound tenet of labor relations. Postal workers would be deprived of free collective bargaining, while the Postal Service is deprived of its stated goals. The Board's proposal would build in more delay and more cost without resolving the problems of Postal Service labor relations.

The APWU supports giving postal workers the right to strike under the National Labor Relations Act. If the Postal Service wants to be treated like a private sector employer, for example United Parcel Service, postal employees should be covered by the NLRA and have the right to strike.

Finally, I must comment on the proposal to strip veterans of their rights and to decimate employee fringe benefits. Veterans who have served their country with distinction deserve employment protections and postal workers deserve decent health and retirement benefits. This proposal to strip them of health benefits and retirement benefits exposes the Postal Service's desire to return postal employees to welfare eligibility. Postal workers are hard working and productive. This proposal by the Board of Governors demeans these dedicated workers.

I request that these remarks be added to our prepared testimony.

Mr. MCHUGH [assuming Chair]. Thank you, Mr. Biller. It's good to see you again.

Let me first of all explain the real Chairman's absence. As you probably heard, we had a vote. Rather than take more of your time, we dispatched me to vote and run back, so the chairman has gone to vote and he'll be back. I'll try not to infringe upon his questions.

Let me also say two things. No. 1, I appreciate the effort that all of you gentlemen and the organizations and the hard working men and women that you represent have made with respect to the Postal Service reorganization reform acts that we have put forward. I'm not one of those that happens to believe that by and large, the postal workers are the problem. I think they are, if not the answer, certainly the reason the vast majority of Americans think so highly of the mail service in this country, for all the complaining and all the pot shooting that goes on. They understand the vital role and the very unappreciated role that your members bring on their behalf each and every day.

It's a source of great criticism, which I understand on one hand, that postal employees represent 80 percent plus of the cost of the organization, and Mr. Biller has refuted that somewhat in his testimony. Nevertheless, it's a little difficult when you by law have to visit every household in America, or certainly provide mail to every household in America, every day, to do that without people, and good people. Your people are a tremendous asset to us. It's certainly something that we need to keep in mind as we continue to endeavor to deal with this situation.

Mr. Biller, you said in your comments the sky is not falling, if I heard you correctly. I take it you meant that you didn't feel that the current situation in the Postal Service merits radical reform? I don't want to put words in your mouth. But the question I would ask you, the Postal Service last week raised rates again, which Mr. Quinn felt was appropriate. I understand that. But it was a rather unusual step in that for, I believe, only the second time in the history of the Postal Rate Commission, they rejected the findings and voted to institute that second phase of the increase.

They had placed a moratorium on some 800 postal facilities across the Nation, either under construction or soon planned for reconstruction. Six or seven of those were in my district. Virtually every Member of Congress was touched by that.

They called for over a 5-year period a diminution of 75,000 manhours, man years, excuse me, the equivalent of 75,000 jobs, to be taken out of the Postal Service by attrition. And they've commenced a study on the possible termination of Saturday mail. Whether you agree with those or not, those are pretty affirmative steps, to put it in a kind light.

Would you gentlemen agree, based on what Mr. Biller said, that those steps were an overreaction? I'd be interested in exactly where you feel we are with respect to the Postal Service's current fiscal position. And it makes no difference to me who starts. Mr. Burrus.

Mr. BURRUS. Yes, Mr. Chairman. Much of the efforts by the U.S. Postal Service are suspected to be intended to place pressure on Congress to enact reform. It's not unusual in a year of collective bargaining by one of the labor unions or at a time when there's legislation pending before the Congress that we find ourselves going

from a $200 million deficit in 1 year to a $2 billion to $3 billion deficit projected in the following year.

Now, the numbers that you use, the 76 to 80 percent of the employee costs, as reputed by President Biller, it's only 57 percent of the unions represented at this table. But whatever figure is used, rate costs have not increased beyond the cost of the postage rate increase that was approved by the Postal Rate Commission. The Postal Service realized $2.8 billion in new revenue before the most recent action.

Wages have not increased anywhere near that. My bargaining unit, APW, is currently in negotiations, contract expires on November 20th, has not achieved a wage increase this year. So if they're experiencing or expect to experience a $2 billion to $3 billion deficit, it's creative bookkeeping. As President Biller said, the sky is not falling.

Certainly there is a need for postal reform, there's a need to look to the future. But all of the actions that have been announced that the Postal Service has serious difficulties, there are serious problems about those announcements, particularly the timing of them.

Mr. MCHUGH. Well, let me followup then. Last month, Chairman Burton convened a hearing and one of the people who testified was the Comptroller General of the United States, David Walker. In his both written and oral presentations, he said the GAO has found that the Postal Service is in the midst of what he described as a serious financial and operational crisis, that absent legislative change places the Postal Service's ability to meet its universal service obligations at "high-risk." Do you disagree with the Comptroller?

Mr. BURRUS. I don't disagree, but it relates to the future, it doesn't relate to a specific year. The GAO findings did not relate to the year 2001 and a projected deficit of $2 billion to $3 billion in that specific year. They were taking a long term view. And the impact of technology on the volume of first class mail into the future.

Mr. MCHUGH. With all due respect, he said, the Postal Service is in the midst, not on the verge, in the midst of a serious financial and operational crisis. I'm not assigning blame to that to anyone. I'm trying to—and I've heard and by and large I agree with your comments about the source of that is certainly not your workers. Please don't assume anything I asked was trying to impugn that your workers are the problem. I hope I stated clearly in the beginning I don't feel they are.

But I'm trying to ascertain, you as the leaders of those 800,000 people, how you viewed this challenge? Is it serious enough for us to take steps to do something about it? Clearly we shouldn't act in haste. Moe Biller cautioned us about that. I agree with that. And we shouldn't act imprudently.

But should we act, I guess is the other question?

Mr. SOMBROTTO. Well, the question is, what is the real picture? Once we define what the real picture is, then of course we have to deal with how we correct it. But there are flaws in that picture.

I've heard a lot and read a lot of testimony and read some statements by the board of Governors and so on. A lot of stakeholders have put their oar in the water, and they're all giving their own

views of why the Postal Service is in crisis. But I just want to respond to a couple of things, and that's why I provided some graphs for the committee's attention.

Since 1972, the consumer price index has gone up some 314 percent, since 1972, the consumer price index has gone up some 314 percent. Postal workers, letter carriers, those wages have gone up by some 297 percent. So that's well below the inflation rate.

Mr. MCHUGH. Are you saying that price caps aren't necessarily a wage cap, then?

Mr. SOMBROTTO. No, I'm not talking about wage caps, I'm just talking about what the reality is, what has happened. And postage rates have gone up some 286 percent.

So to summarize that, the CPI has gone up greater than letter carrier wages and postage rates have gone up less than the CPI. So if there's a problem here, then let's find out what the problem is, because it's got nothing to do with wages of postal employees and it's got nothing to do with collective bargaining. And it's got nothing to do with binding arbitration. I just wanted to make those points.

Mr. DAILING. Mr. McHugh, the issue that I'd like to address in attempting to answer your question is what we are meeting about, and that's the ability for the Postal Service to be competitive into the future. We recognize with your bill of H.R. 22 that something needs to shake out, some change needs to be done for the future of all of us to survive in providing universal service to all those customers out there.

One of the things that is always asked of me, of my rural mail carrier customers, when I pull up to that box and provide them with a stamp, is why don't they just go ahead and raise it up to 35 cents? Why just a penny? That's what our customers, or my customers, are asking me.

Now, I realize that's just a small portion of the big picture. Pricing flexibility, that type of reform, has to be done, and needs to be done through this Congress and the work of these committee members.

Mr. MCHUGH. Thank you. Mr. Quinn.

Mr. QUINN. Well, as I said in my statement, Congressman McHugh, there are a host of reasons that contributed to this projected deficit. And clearly, some of them are out of the Postal Service's control, a slowdown in the economy, the jump in gas prices, have a devastating effect on the Postal Service. Obviously, you've been the voice in the wilderness for a number of years, talking about reform. But I concur with your statements that the Congress shouldn't act in haste in this particular matter, that we certainly hope that some of these circumstances that contributed to the deficit are aberrations.

But as I also said in my statement, Congress is not without sin in this regard either, because Congress was tapping into the Postal Service's funds to address some of the issues facing it with the national deficit when that was a cause celebre 10 years ago. So I think everybody agrees that there's a need for reform. The question is, what kind of reform is going to be enacted. I hasten to caution you that Congress has to be extremely careful not to throw out the baby with the bathwater.

Mr. MCHUGH. Thank you. Speaking of aberrations, my sitting here is one and I will yield the Chair back to the Chairman. [Laughter.]

Mr. BURTON [resuming Chair]. Thank you, Mr. McHugh. Mr. Davis, have you had questions yet?

Mr. DAVIS OF ILLINOIS. Thank you very much, Mr. Chairman. Let me just indicate to the panel that I appreciate not only your testimony but also the work that your membership performs. It's not quite as glamorous as the old Pony Express, but I can tell you that the citizens of this country appreciate the fact that come rain, shine, sleet or snow, no matter how hot, no matter how cold, that they can expect to be able to communicate with other people across the Nation. So we appreciate that fact.

We've been talking about studies and reports and criticisms and analysis. The GAO issued a report earlier this year that talked about the fact that productivity had only increased 11 percent in the last 30 years, and that it actually declined 3.3 percent from 1993 to 1999. How do you gentlemen respond to that report, and what impact do you think that labor has had on productivity?

Mr. SOMBROTTO. I provided you with some material on that question. The total factor productivity that the GAO talked about, 11 percent over the 30 some odd years, is about consistent with what happens in the private sector in similar circumstances, that is in similar industries or businesses. But what they didn't take into account is the postal labor factor. When you take that into account during that same 30 odd years, the increase in productivity in postal labor is more than 32 percent.

So it has nothing to do with productivity. The productivity has been there. Total fact of productivity includes many facets. It includes the investment capital, investment changes that the workers have no, the employees have no part in. When you get to the labor itself, their labor has increased the productivity a significant amount in those 30 some odd years.

Mr. DAVIS OF ILLINOIS. So you're saying that, in reality, it has no real impact or it's not an issue?

Mr. SOMBROTTO. That is exactly what I'm saying.

Mr. DAVIS OF ILLINOIS. Let me then just ask another question. There have been concerns expressed that as we talk about postal reform, and that as we come up with a bill, that if it should include a postal rate indexing, that we really could be talking about putting a cap on the wages of postal employees. How do you respond, any of you actually?

Mr. SOMBROTTO. Caps are for baseball players, not for collective bargaining. The collective bargaining process happens to be, it's a national policy. And in collective bargaining, both parties sit down in an effort to fashion an agreement that reflects the involvement of each party in whatever the enterprise is.

We find it very comfortable for us to sit down across the table and make our case for what we contribute to the health and welfare of the Postal Service. Management has a right to make their case. We try to do that collectively without a third party, if we can. When we can't, then we have to go to a third party and we go through the same process. Both sides have an opportunity to put

their best foot forward, put their best evidence forward as to their position.

And in the end, a neutral makes that decision. We're comfortable with that. That's a democratic process in action. We don't see any need to be tinkering with that collective bargaining process.

Mr. DAVIS OF ILLINOIS. Anyone else?

Mr. BURRUS. A price cap does become a wage cap, and we would have no interest at all in having legislation passed that would impose on the collective bargaining process artificial limits. While it's true collective bargaining within the Postal Service since reorganization, we have never, particularly in recent years, achieved ECI, which was the benchmark in H.R. 22. But that does not stop the human spirit from attempting to exceed the ECI if that had been the cap.

The argument that was raised that, why would the unions be opposed to a cap that they've never achieved in 30 years, the highest increase received by postal employees in a single year has been a 3 percent increase. There have been occasions over the last 15 or 20 years the ECI has gone up over 4 percent.

So while we have never achieved that, to impose an artificial ceiling in the rights of workers to bargain collectively, free collective bargaining, would be an imposition and a distortion of the intent in 1970 where the unions were partially responsible for the passage of postal reorganization with the promise that we would have free collective bargaining. To renege on that promise some 30 years later we think would be a disservice to the working people that serve the American public.

Mr. DAVIS OF ILLINOIS. Thank you. I'm going to ask a question that does not necessarily relate to your testimony, but you were here this morning, and you all heard the testimony of the panel that came before. We heard notions of a more constricted, or a more limited, Postal Service as being a possible approach or a possible remedy for working through some of the difficulties that we're facing.

How do you respond to that? And the question becomes really, do we think that a more limited Postal Service could generate the revenue necessary to operate whatever part of the system that was left?

Mr. QUINN. Well, presumably, if the Postal Service hierarchy embarks upon some project that they believe is going to generate more revenue for the company, I don't see what the downside is. I believe what the thrust of the statements this morning are is that some of those endeavors the Postal Service made to generate additional revenue proved to be unsuccessful.

But I don't see in the long run why you should, as a matter of course, rule out any possible endeavors that could generate more revenue. It would obviously be better for the Postal Service, it would be better for the public, it would be better for Congress.

Mr. DAVIS OF ILLINOIS. I think my question really dealt more with, if privatization is to be increased or a part of the overall system, how much privatization might we be talking about? Or at what point do we take away more revenue than we're able to generate to make sure that universal coverage remains, or that we

have the money in the system to provide universal coverage or universal service for first class delivery?

Mr. QUINN. Well, when you talk about universal coverage, and privatization, it's oxymoronic. The fact of the matter is, the privateers are interested in skimming the cream off the top. The Congresswoman from Hawaii talked about the problems in the rural areas of that State that would be exacerbated a thousandfold if privatization were to take hold.

The fact of the matter is that private companies are not going to provide universal coverage, they're not going to go into areas of this great land of ours where they're not going to turn a profit. And I think the concept of that on its face is ludicrous.

Mr. DAILING. I have to agree with my counterpart that any type of privatization away from going to every mail box every day would be a devastating effect on the universal service. I have to reiterate again that we believe some very simple tasks could be accomplished in a type of postal reform and that would allow a pricing flexibility in the promotion of the products that the Postal Service can provide to the American public.

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

Mr. BURTON. Thank you, Mr. Davis.

Mr. Otter.

Mr. OTTER. Thank you, Mr. Chairman.

Mr. Quinn, in your testimony, you indicated that part of the problem was because of the economic downturn that began last year, and that was part of the problem, the reason you were now looking at maybe a $2 billion to $3 billion deficit in the Post Office operations this year. How do you account for, or what happened, then, before that? Because it seems to me that we're about $9.6 billion in debt, and that had to happen prior to last year, because the economy turned down last year. What happened to that money?

Mr. QUINN. Well, it's not in my bank account. The $9.6 billion that you're alluding to was accumulated over 30 years. The fact of the matter is that Congress itself knew that there were going to be problems in the adjustment when the Postal Reorganization Act was passed in 1970, and the fact is, through 1982, the Postal Service received subsidies from the Federal Government. They haven't received anything in subsidies for the past 19 years.

The fact of the matter is that the former Congresswoman from Colorado alluded to the revenue foregone, where the Postal Service used to receive far more moneys on mail for the blind or things along those lines. In addition, the fact of the matter is that through the year 1998, Congress put a hit on the Postal Service to the tune of $14 billion in the passage of numerous omnibus budget reconciliation acts.

If you factor in all of those things, plus the vote of the House of Representatives in June 1998 by a 393 to 12 vote, the House of Representatives in a non-binding resolution had the temerity to criticize the Postal Service for having surpluses in a number of years, four surpluses in a row. And said that the Postal Service had lost sight of the fact that it was a public trust and that the Postal Service in effect had imposed a stamp tax on the American people.

So the Postal Service has been put in the position when they do well, they're criticized and if they do poorly, they're criticized. But I think the fact is, going back to the statement that I made, the projections that were made by the board of Governors obviously had to have been based on the economy. Nobody foresaw the economy going in the tank as it did. And once the economy goes in the tank, you're going to have a commensurate reduction in business and in mail volume.

Mr. OTTER. Is it time, then, for us to have a vigorous and unabashed debate on whether or not affordable universal service is still appropriate for today?

Mr. QUINN. Well, I guess that's for wiser minds than I. But the fact——

Mr. OTTER. I think it's an important question that you need to look at.

Mr. QUINN. The fact is that Congress mandated universal coverage. And if Congress is going to mandate it, perhaps Congress should look at perhaps subsidizing it once again. I'm not taking a stance on that particular thing, but Congress is making an incredible demand on the Postal Service that certainly couldn't be made on any other company, UPS or FedEx, etc. And somebody has to absorb the costs for the universal coverage.

The fact is again, the privateers would love to take any kind of business from Boston to New York, Chicago to Los Angeles, because there's a lot more profit there. But when you go into the more rural areas of the country, obviously, that's not the case. But of course, the beginning lines of the Reorganization Act talk about binding the country through a universal mail system.

Mr. OTTER. If we did take a look at that, and we did privatize it, or part of it, and subsidized the rural area, would it cost us more or less than $2 billion a year?

Mr. QUINN. Well, I don't think you can take one particular year and say, we're looking at a deficit now of $2 million or $3 million. Although the Postal Service is mandated to turn a profit overall, it's not everything in 1 year or the next year. The fact of the matter is, from the mid-1990's on, there were 5 years in a row that the Postal Service turned handsome surpluses. Obviously a lot of that, those surpluses went to make up for the deficit that had been accumulated over the years. You alluded to that earlier.

But it's again, as I said to Congressman McHugh, you have to be very cautious in this regard that you don't throw the baby out with the bathwater.

Mr. OTTER. I agree, Mr. Quinn, and you were right and they were wrong, and I wasn't here. That's a joke. [Laughter.]

Mr. QUINN. Well, I have to agree with you, I don't know whether it was meant humorously or not, I was right. [Laughter.]

Mr. SOMBROTTO. If I may, they were partly right, they were partly wrong, and I was here. The fact is that we have universal coverage, that is the law now. And we're committed to universal coverage. And there's no reason why we can't have universal coverage and do it efficiently, if we run the Postal Service efficiently. That's all it needs. It needs management that runs the Postal Service efficiently.

It's got one of the most dedicated work forces in the world that work in the Postal Service. Men and women commit their lives to this job, to working in the Postal Service. Have to work at least 30 years before you can even think about retiring. So there's a commitment. Most postal employees, if you look at the average tenure of a postal employee, a postal employee is upwards of 20 years now, on the same job.

While people are changing jobs all over this country seven, eight times during their life time, letter carriers, clerks, mail handlers, rural carriers, all take the job with a commitment that they're going to stay on the job to see it through and meet the commitments of the laws that govern the Postal Service.

So all we need is, there's no reason why we can't have universal service. It's something that's desirable, something that's needed. But it also can be done and it need not run a deficit if it's done correctly.

Mr. BURTON. Thank you. Major Owens.

Mr. OWENS. The last speaker gave us all the answers. Why don't we act?

My question is, and I apologize for having to go back and forth, trying to cover three meetings, but is this meeting here any more than a high school forum, a general discussion that has no significance? What do you think of the fact that the ability, the capability of Congress to solve any of these problems has been drastically reduced? I think 6 or 7 years ago, we eliminated the Committee on Postal Operations and Civil Service. We had a whole committee, and then we reduced, we had the postal operations assigned to a subcommittee. Now we've wiped out the subcommittee.

So what do you think Members of Congress are going to be able to do? We don't have a decent staff to come up with decent legislation or study the problem and be able to deal with the critics. Where do we fit in the situation?

There are a number of very critical problems that need to be resolved. There are models out there for combined private-public operations, or a public operation which contracts some parts to private. There are all kinds of models we have, National Space Administration certainly is not hemmed in in certain ways that the Postal Service is hemmed in.

There are a number of ways we might solve the problem, but where's the power? Who really has the power to proceed to put together some of the recommendations that you've been making here and come up with some legislation that is going to be meaningful?

I don't see it here in Congress now. We don't have any clout any more. I'd like to hear your comments on that.

Mr. BURRUS. There continues to be a role for Congress to play in serving as the protector of the public in terms of providing universal service at an affordable cost. There continues to be a role. It's important that Congress plays that role.

Certainly the structure within the Congress has been modified over time that the Postal Service has not received the same type of oversight that it did back at the time of postal reorganization. I would imagine the Postal Service on occasion is happy that there is not that regular oversight.

But while Congress is being requested to provide some relief through postal reform, we believe that their consideration of that request should not be done with the backdrop that the Postal Service has lost $2 billion to $3 billion. All of the discussions that have transpired by the prior panel, as well as the questions posed to us, has taken as a fact that the Postal Service is going to lose $2 billion to $3 billion. All the reports by Postal Service management has been that if nothing changes, they could lose up between $2 billion to $3 billion. No one has said to this date that they have lost it or will lose it.

Mr. OWENS. Let me rephrase my question. Are you being set up for failure?

Mr. BURRUS. No.

Mr. OWENS. To quote from a postmaster general from a Cabinet a long time ago, the reduction of the congressional responsibilities from a full committee to a subcommittee and then wipe out the subcommittee, is somebody setting you up for failure so that privatization would be an inevitable answer, and privatization would be carried out by people, certainly, who don't represent the people, because the Congress has no capacity really to get deeply involved in that. We don't have a single staff person devoted fully to this pursuit, when you need a whole crew of people to stay on top of this very serious matter.

You expressed some ambivalence when you said, maybe you don't want somebody to monitor you all the time. We need a strong statement from somebody out there that Congress should get back in the game. If you don't feel we should get back in the game, then I don't think anybody else will.

Mr. BURRUS. The Postal Service has succeed in the past and can succeed in the future. The objectives are limited. They're being, now that we've got a Christmas tree, everybody wants to put ornaments on it. Flexibility in pricing, a shorter ratemaking cycle, when you add on collective bargaining and privatization and those other issues, they are non-starters. If the agenda is limited, Congress can play an important role, granting the Postal Service pricing flexibility and a shorter rate cycle.

We believe that with those changes, the Postal Service can compete in the future.

Mr. OWENS. Mr. Biller, do you have an opinion?

Mr. BILLER. He stole my thunder.

Mr. SOMBROTTO. I would hope that the Congress is going to play a role. Certainly many of us, and I venture to say most of us, are playing the role now. The chairman's suggestion that the stakeholders get together and see, work together toward trying to find a common solution to what is the problem, if that problem present itself. And to that extent, we have been meeting, we have been trying, and we will continue to do that. We will try to find a, if there is a serious problem and if there is a serious problem, how can we address that problem.

All that I've been saying on behalf of the members that I represent, that if there is a serious problem, you're not going to eliminate that problem by reducing service, by finding artificial means of trying to get over this what we hope is a blip in our operation.

Mr. OWENS. I apologize for being less diplomatic than you are. But that sounds like a Boy Scout approach. If we don't have a subcommittee or you don't have a committee addressing this matter, do you really think you're going to work things out in this informal way?

Mr. SOMBROTTO. No. Well, I don't know that we can work it out. But in conjunction with those that make these decisions, then you all are the ones that ultimately are going to have to present a postal reform. We hope that working with all of you that we will come up with a solution.

But we want to play a role, because we have people whose lives depend on our ability to play a role in that forum.

Mr. BURTON. Thank you, Major Owens.

Mr. BILLER. We don't organize or reorganize the Congress of the United States or its committees. So your complaint should be——

Mr. OWENS. Well, some powerful body, I was hoping there'd be a call to the majority party to re-establish a subcommittee or committee to deal with the problem. That's what my great hope was.

Mr. BURTON. Let me just say to Major Owens that we fully intend to get input from all the interested parties, and we fully intend to bring legislation to the floor that is bipartisan in nature. And, although there is not a subcommittee on postal reform or postal services right now, we've brought that to the full committee for the express purpose of raising the profile of the issue, so that we could get the problem solved.

And it is fully our intention to make this one of the No. 1 priorities of this session of Congress, because it has to be. Although we don't have a subcommittee or a full committee on post office, civil service, like we had before, I can assure you, this is going to be a top priority. I hope you'll be a participant in helping us solve it.

Mr. OWENS. I'm pleased to hear that, Mr. Chairman.

Mr. BURTON. Thank you, Mr. Owens. Mr. Barr.

Mr. BARR. Thank you, Mr. Chairman. I appreciate the hearing, appreciate the witnesses, both their written and oral testimony and their answers to questions. It's been very enlightening. And I commend your efforts and your commitment to work with all the parties concerned over the coming months of this session of the Congress to craft legislation that will help to do something that as far back as our founding fathers recognized was essential to the well being and the security of this Nation and that is to have universal, consistent postal service.

As I mentioned earlier, and I believe this very strongly, we do have the best postal service in the world. We want to keep it that way. But in order to do so, they're going to have to be changes made, there are going to have to be compromises probably made on all sides involved. And I commend what we've heard here today and appreciate the flexibility and willingness of these witnesses and the ones that hopefully previously will be committed also to working together to solve these problems and bring the Postal Service into the 21st century so it can compete properly, consistent with the national mandate that it I hope will continue to have for universal service.

I again want to thank the witnesses for their time and expertise here today, and their service, and look forward, Mr. Chairman, to

working with you and other members of the committee and interested parties to craft legislation.

Mr. BURTON. Let me just end by saying we will have some questions we'd like to submit to all the panelists for the record. But more important than that, we really do want your suggestions and your input. And I really do appreciate all of you, if you will, to meet collectively and with smaller groups to iron out differences that you have here. I see in the audience some people who have had some severe differences with the former bill, H.R. 22.

We really want to have everybody's input, and we're going to take all these issues and sit down with the major interested parties and try to work out differences that are really knotty, like cutting through the Gordian knot that Alexander the Great cut, and come up with a solution that we can all live with.

Everybody's not going to be completely happy, I'm going to tell you, there's going to be differences, you know that, when you have this many interested parties, there's going to be differences. But as the GAO said, the Postal Service is now in a high risk category. We can differ on that. We can have some differences of opinion. I heard what you said, I listened very clearly.

But according to a lot of the leadership in the various agencies, there's a very severe problem facing us. We don't want to wait until we get to the edge of the cliff before we stop the car. We want to try to stop the car and solve the problem before we get that far.

So we want your input, we request your input. I really, I think Major Owens has a point, if we waited around, it sounds like a debating society around here many times, and we don't get a lot done. But this is something that we have to get done. We are committed in this committee to getting it done. Senator Thompson is aware of the problem over there. I will be meeting with him.

I'll be meeting with the Board of Governors this week to talk to them about some of the problems, but we want your help, we want your input. If you give it to us, we'll do our damndest to solve the problem—pardon my language, we'll do our darndest to solve the problem.

With that——

Mr. BILLER. We thank you very much.

Mr. BURTON. Thank you, Mr. Biller. Thank all of you. We stand adjourned.

[Whereupon, at 2:15 p.m., the committee was adjourned, to reconvene at the call of the Chair.]

[The prepared statement of Hon. Dennis J. Kucinich and additional information submitted for the hearing record follows:]

Dennis J. Kucinich

OPENING STATEMENT

GOVERNMENT REFORM HEARING ON POSTAL ISSUES

MAY 16TH, 2001

Thank you, Mr. Chairman.

Last week, the United States Postal Service board of governors voted unanimously to implement a modified rate increase schedule, to take effect July 1st. Though the 34 cent rate that most of us pay when we send mail will remain the same, rates for various other types of mail – including postcards, express mail, certified mail, and money orders – will increase.

Essentially, what the Board of Governors decided to do was overrule the decision of the independent, Presidentially-appointed postal rate commission, which since January has twice rejected the Postal Service's proposals for new rate increases. This move comes on top of USPS' decision earlier this spring to freeze construction on postal facilities.

Why such drastic action? We heard the answer from the postmaster general last week : the postal service estimates losses of $2 to $3 billion based upon a slowing economy, high gas prices, and increased personnel costs.

This analysis begs a few questions:

- If gas prices are such a sudden burden, how come USPS had already included adjustments for fuel costs in its July filing with the Postal Rate Commission, back when the Postal Service expected a $480 million loss rather than a $2 - $3 billion loss?

- If increased labor costs are to blame for this overnight plunge into red ink, how come the real wages of bargaining unit postal employees have remained unchanged in the last thirty years?

- If arbitration with union-represented employees has been such a problem, as the Board of Governors has insisted, how is it that the percent of operating revenue consumed by collective bargaining agreements has declined six percentage points in the past 12 years?

More fundamentally:

- Why, as reported by the USPS Inspector General, does the Postal Service continue to fritter away more than $1 billion annually in waste, fraud, and abuse?

- Why did the Postal Service recently issue more than $280 million in executive bonuses?

- Why, when it has a first-class postage monopoly, does USPS need a $300-$500 million annual advertising budget?

- Why did it lose more than $84 billion on failed commercial ventures during the 1990s?

I hope this hearing proves more enlightening on these matters than the previous one.

Thank you, Mr. Chairman

Open Letter to the New Postmaster General

To Learn More, Go To **www.PostalFacts.com**

Dear Mr. Postmaster General:

Welcome to one of the world's most challenging jobs. We implore you to see it as a unique opportunity to set the USPS on a new course. As consumers and others concerned with postal operations, we have the most to gain from a viable, efficient postal delivery system. But frankly, we're concerned about past decisions and future directions. Allow us to offer our perspective on your most pressing priorities.

Restore Sound Postal Management. The mantle now falls on your shoulders to lead this massive bureaucracy out of a colossal crisis. Some say it is a crisis of postal policy. We see it as truly a crisis in postal management. How else can one explain a $3 billion slide from black to red ink in just five months? It is often observed that your government agency uniquely touches every American. But recently it has been too quick to touch our pocketbooks instead of controlling costs.

Return To The Mission. Postal carriers may know the path to every house, but postal management has lost its way through the changing communication landscape. It has been diverted by new ventures that turn into costly misadventures. Like a business lost in Internet Alley, it's time for the USPS to return to fundamentals. Its job is to deliver the mail promptly and affordably to every house. We expect our money to be used only for that purpose.

Increase Postal Services Not Rates. Just months after increasing stamp prices your agency seeks a new rate case that many believe will cause it to lose customers. It proposes eliminating post offices and Saturday mail delivery. Managers have no incentive to lower costs to customers who end up paying for executive bonuses even in bad years. Raising prices in the face of declining demand is indefensible, and a far cry from the smart management strategies we desperately need from you.

Stop Exploiting The Monopoly. To protect universal service, the USPS is entrusted with the power of a monopoly, which we urge you to use properly. Stop the practice of leveraging First Class monopoly revenues to pay for competitive services that are already provided by private-sector firms. Abandon unfair rates for some mailers, which are at the expense of others, especially First Class mailers, who are now paying more than their fair share.

Call For Conflict-free Leadership. The crisis facing the postal service demands national leadership by thoughtful and independent Americans. Postal reform legislation is no solution when postal fairness is sacrificed for postal pricing flexibility. A six-year effort to achieve political consensus in Congress has failed because of the varied and often conflicting interests coming from all corners of the postal community. Where can conflict-free leadership be found? A presidentially-appointed postal review commission.

Support A Presidential Commission. A Presidential Postal Commission is in the best interest of all Americans, and we urge you to support its appointment. An independent panel of distinguished Americans should look at all the facts, determine the appropriate mission of the USPS in the new century, and make policy recommendations that are fair to every mailer.

We urge you to act now to bring responsible, accountable management to this venerable and vital public service whose 226-year mission of providing postal services to "bind the Nation together" still remains valid today. You can count on our support if you honor these principles. For the sake of all Americans, we wish you success.

American Bankers Association
American Business Media
Associated Church Press
Computer & Communications Industry Association
Consumer Federation of America
Greeting Card Association
Newspaper Association of America
National Consumers League
National Rural Electric Cooperative Association

they didn't yet understand the complex factors affecting salmon. Environmentalists then saw this was a perfect way to pursue their broader anti-growth agenda—to force farmers off the land, blow up dams, get rid of barges.

But we look forward to the Administration's own reforms. The Klamath Valley mess would be a good place to start. Not only would Mr. Bush save 1,500 farms, but he'd let it be known junk science will no longer be allowed to ruin ordinary people's lives.

WSJ 5/14/01

Going Postal

Sure, mail carriers are an easy target. But it sure tells us about where the post office stands today that in scarcely a generation our public iconography of the U.S. Postal Service has moved from Norman Rockwell to two of the most annoying characters in sitcom history: know-it-all Cliff Clavin of "Cheers" and his "Seinfeld" counterpart, Newman. And after yesterday's Senate hearings in which we learned that the post office is going to lose more money despite two rate hikes this year, that's not going to change any time soon.

"It's obvious that the ox is in the ditch big time," said Tennessee Senator Fred Thompson, chairman of the Senate Governmental Affairs Committee. Senator Thompson was reacting to news of financial losses in the neighborhood of $2.4 billion, losses so high that the General Accounting Office has put the Postal Service on its "High Risk List." For its part the postal service has reacted as any protected monopoly: threatening to cut off Saturday mail delivery unless it gets further rate increases.

But the problem with the U.S. postal system is not its rates. It's the attitude. In most parts of its operations the Postal Service rewards everything but productivity, and its work force of almost 900,000 reacts in kind. Now, we don't believe that the nation's post offices are full of mail carriers spending their afternoons downing brewskies at their local Cheers. But one real problem is that there is almost zero incentive for carriers who could and would do more work to ask for it.

Almost everyone who uses mail is affected by this dynamic, including this newspaper. And if rate increases were simply a reflection of the market, that would be one thing. But a report card on productivity released Monday by the Mailers Council—a coalition of mass mailers whose members account for some 70% of America's mail—gets to the heart of the issue. Using six internal productivity measures, such as volume handled per hour, revenue per hour, etc., it rated the post office's performance for the first quarter this year and gave it low grades. The study also found a noticeable gap when the Postal Service was compared with the private sector.

As first-class mail declines due to alternatives such as overnight delivery services, faxes and email, the financial dilemma is being thrown into high relief: The post office has too many workers. This itself is largely a function of its failure to automate, most notably with parcels and other non-first-class mail. The problem is that as a service that is neither private nor entirely public, all sorts of political sacred cows are involved, such as the closing of post offices and processing centers in this or that Congressional district.

Senator Thompson says that in addressing the Postal Service's problems everything should be on the table. We hope he's right, because it's hard to conceive of a way to solve the structural problems without revisiting some of the service's monopolies and privileges. And the political reality of the Postal Service is that it may take the equivalent of a base-closing agreement to get Congress to sign onto a desperately needed rationalization of the service's operations.

Right now reformers appear to be divided between those who favor some legislative remedy and those who believe the time is ripe for a Presidential commission along the lines George W. Bush has already set up on Social Security. Ultimately this is not simply about what a letter or mailing should cost but what kind of post office America requires in this new millennium. As Controller General David M. Walker underscored at yesterday's hearings, the problems are all too real and "the answer is not merely to increase rates."

In short, what the next Postmaster General has to do is replace the Newmans with better technology and give the remaining Cliff Clavins—at all levels—incentives based on their productivity. It's never going to come from within.

individuals; it is also caused by greater longevity and even the increased prosperity that enables young people to live on their own. It is not going to be reversed by another round of denunciations of Murphy Browns more interested in career satisfaction than the joys of breast-feeding.

At the same time, the census news is also bad news. There are those who believe that, in a democracy, the fairest public policies are those that benefit the greatest number of people. If there are fewer families with children, such pro-family policies as child tax credits, elimination of the marriage penalty, support for public schools, or flex time for working parents would seem to ignore the majority who live alone or in households without children.

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Where Electric

By Phillip G. Harris

VALLEY FORGE, Pa.—President Bush is set to announce a free-market approach to energy policy tomorrow. Many critics are skeptical, claiming that deregulation has failed in California.

But take your eyes off California for a moment, and look elsewhere. You'll find that the deregulated electricity market of the mid-Atlantic region—including parts of Pennsylvania, New Jersey, Delaware, Maryland, the District of Columbia and Virginia—is working. It has been working since 1997. There are no brownouts. Power prices have declined and consumers are better off. It is the way deregulation is meant to work.

How did deregulation succeed in the mid-Atlantic states, and why hasn't it worked in some other parts of the nation?

In certain respects, the answer is simple. When we deregulated, we created a real regional market that matches supply and demand by ignoring political boundaries. Instead of a one-state market, we created a
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On AWSJ OpinionJournal.com

From Tom Bray's column:

As the environmental movement grows, the public grows increasingly skeptical.

Exhibit A is an impressively researched series of articles published in the Sacramento Bee by Pulitzer Prize-winning reporter Tom Knudson, who has often written sympathetically of the environmental movement. Titled "Fat of the Land," the five-part series focuses on how a supposedly grassroots movement transformed itself into "one that has come to resemble the corporate world it often seeks to reform."

Mr. Knudson cites the lavish offices, handsome salaries and "fat Wall Street portfolios" of many environmental organizations. The conservation movement raised a staggering $3.5 billion in 1999, Mr. Knudson calculates.

BOARD OF GOVERNORS

UNITED STATES
POSTAL SERVICE

May 15, 2001

Honorable Dan Burton
Chairman
Committee on Government Reform
House of Representatives
Washington, DC 20515-6143

Dear Mr. Chairman:

This responds to your invitation at the April 4 oversight hearing for suggestions from the Board of Governors regarding the shape of postal reform. Simultaneously, I am also providing these same comments to the Chairman of the Senate Committee on Governmental Affairs.

Reform must ensure that the Postal Service is able to carry out the universal service mission given to it by Congress. To achieve this end, reform should be as simple and understandable as possible, drawing from familiar marketplace models to the maximum extent consistent with the retention of universal service. Market solutions should be possible to bring needed reform to the critical areas of labor and employment and to protect the financial viability of universal service. We have enclosed summaries describing the principles that we would like to see guiding reform in each of these areas.

We believe that regulatory reform is needed for the preservation of universal service in a changing marketplace. Adjustments in pricing and products should be handled as much as possible as in any other business. The Postal Service should have an explicit universal service requirement to continue to provide regularly scheduled, daily delivery of letters in all urban and suburban neighborhoods and rural communities throughout the country, at affordable prices. The monopoly protection properly associated with supporting that obligation should be retained. We recognize that a level of regulation is required for the protection of universal service and the public interest in a monopoly environment. Regulatory intervention should be structured so that the Postal Service has the ability to attune its efforts to market forces as nearly as possible. This could be accomplished through application of an easy to understand indexing mechanism for services covered by the explicit universal service requirement, and through market pricing for all other services.

Without genuine market-driven reforms, it is not reasonable to expect that the Postal Service will be able to meet its universal service responsibilities indefinitely, as the protection of the postal monopoly is diminished in the market. With sufficient flexibility, we believe that a more businesslike Postal Service should be able to improve efficiency and financial viability. Only in this way can Congress expect to preserve the Postal Service's unique contribution as the last delivery mile, assuring access for all America.

For an organization as labor-intensive as the Postal Service, reform will be deficient and ineffective unless it also addresses the shortcomings of the current labor and employment process. In our view, the system fails the public interest when it delegates the most vital decisions about wages and working conditions to an outside arbitrator having no accountability for the future of postal services for the people of the United States. The private sector model for labor relations in organizations that provide essential services is designed to induce management and employees to decide their own future together, while also protecting the public interest with mechanisms for public input where needed. Drawing on that model, postal reform should be able to improve the accountability of this key ingredient of the Postal Service's performance. For other employment matters, the Postal Service should also be expected to operate more like a business.

The Board very much appreciates the Committee's exhaustive, trail-blazing efforts in the cause of postal reform, and your personal leadership as reflected most recently in your efforts to engage the new Administration. I think we all agree that the environment in which the Postal Service operates now demands a postal system held accountable to act much more like a business than is possible under the current 30-year-old legislation. We appreciate your courtesy in inviting our views and look forward to continuing to work with you to see that all Americans have the best possible postal services.

Sincerely,

Robert F. Rider
Chairman

Enclosure

FINANCIAL VIABILITY OF UNIVERSAL SERVICE

Current Law. By statute Congress requires the Postal Service to provide a maximum degree of effective and regular postal service in all communities throughout the country, including places where services are not self-sustaining. To cover costs, the law contemplates that the Postal Service will be able to maintain enough contribution from its overall business to offset the shortfall on economically unsustainable routes and services. In support of universal service obligations, the Private Express Statutes reserve the core of the letter delivery business to the Postal Service.

The law also relies on a regulatory model of control, in preference to market-based principles. To change prices or mail classification for domestic postal services, the Postal Service must first develop a voluminous evidentiary case for presentation before the Postal Rate Commission (PRC). In a pricing case, the PRC then has 10 months to receive the views and evidence of interested parties and issue a recommended decision to the Governors of the Postal Service for final action. The PRC develops its pricing decisions based on cost of service principles. Each subclass must cover the costs found attributable to it, plus a reasonable share of the institutional or overhead burden of the system. Institutional costs are assigned among the various subclasses based on statutory policy criteria such as fairness and equity, impact on customers and on competition, and educational, cultural, scientific, and informational value. Product and service classifications are also based on consideration of statutory criteria, including fairness and equity and the relative value of kinds of mail matter.

Deficiencies. The process for adjusting prices and services is long and cumbersome, typically requiring the major portion of two years from preparation to implementation. Economic and market factors are largely subordinated in the pricing policies prescribed in the current law, not only for monopoly services, but also for those services highly vulnerable to competing services or substitutes. While competitors often adjust their prices gradually, the long regulatory process tends to force postal price changes in large increments. All of these factors tend to make the Postal Service lag well behind developments in the economy and in the marketplace. As technology and market forces open up more and more of the mail stream to the threat of competitive diversion, the financial viability of the Postal Service is undermined. Universal service at affordable prices for all areas, including those hardest to serve, is placed at risk.

Some of these limitations are illustrated by the arduous course of the most recent rate proceeding. In retrospect, the case attempted to use previous experience from a long period of economic expansion to forecast needs for a time when the economy has slowed unexpectedly. As a result, the Postal Service is now providing universal service without fully covering the cost. The current regulatory system also discourages reasonable businesslike innovations to maximize total contribution, such as seasonal pricing and contract pricing.

Proposal. Reforms are needed to provide a better opportunity for the Postal Service to manage its business on behalf of the public as nearly as possible in line with market forces, consistent with the preservation of universal service. The Postal Service should have an explicit universal service requirement. This should cover regularly scheduled, daily delivery of letters in all urban and suburban neighborhoods and rural communities

throughout the country, at affordable prices. The monopoly provisions necessary to support this universal service requirement should be continued. High-volume routes serving business concentrations and affluent residential areas would be attractive targets for competitors who lack the same universal service responsibilities. For services outside the scope of the universal service requirement, the Postal Service should be expected to manage itself like a business, within a market environment.

Pricing regulation should be updated to introduce incentives for the Postal Service to operate more in accordance with market requirements while sustaining universal service. Results-oriented regulation should define broad expected outcomes, and the Postal Service should have responsibility to manage its business as needed to supply the defined level of performance for the American people.

For service covered by the explicit universal service requirement, the regulator should administer an indexing system, under which the Postal Service is encouraged to perform efficiently, and the public interest in fair and affordable rates is protected. The system should be simple and readily understandable, not cumbersome and complex. For all other services, the Postal Service should have the room to price according to market conditions in a businesslike way.

In place of the current mail classification process, the regulator should also limit its focus to service within the scope of the universal service requirement. In all other areas, the Postal Service should be able to adjust its products and services or introduce new ones as needed to advance its overall performance for the American people. Letter service, by itself, will not pay the cost of a universal service network reaching all communities and neighborhoods. Other services that fill mailbags or serve postal customers in associated ways in the market are needed to help fund universal coverage.

These changes would help to preserve universal service by positioning the Postal Service to function as an integral part of today's increasingly dynamic, technology-driven, global markets. As the traditional and newer economies continue to merge, letter monopoly protections will not be sufficient alone to preserve universal service. To maintain financial integrity, the Postal Service will have to be able to function as a thriving business in the marketplace. Under increasingly challenging conditions, revenue from stagnant or declining mail volume would not meet the cost of a growing universal service network at affordable rates, as the nation itself continues to grow. Only by joining with its customers to match their own immersion in the 21st Century economy can the Postal Service maintain the relevance and financial integrity of a universal postal system binding all of the nation together.

LABOR AND EMPLOYMENT REFORM

Collective Bargaining

Current Law. The impasse resolution procedure currently follows a public sector model featuring compulsory binding arbitration. When the parties in negotiation fail to reach agreement, the statute provides initially for a voluntary fact-finding process, led by a panel of three persons chosen by the Federal Mediation and Conciliation Service. If that process fails to produce agreement, or, as is typically the case, the parties choose not to engage in fact-finding, both sides then select a partisan arbitrator, and the two thus selected choose a third, neutral arbitrator to settle unresolved issues. In practice, the neutral arbitrator then issues an award imposing a new labor contract.

Deficiencies. The current process fails to require the parties to resolve critical workplace issues controlling the ability of the Postal Service to meet its responsibilities. The process does not encourage and enable change. In a period in which competitive and technological forces press the Postal Service to evolve rapidly to meet new challenges, the process has proved unable to accommodate significant progress. Critical issues of national policy have been left to a series of individual arbitrators having no public accountability for the results. Since 1981, 13 out of 20 labor contracts with the Mail Handlers, National Association of Letter Carriers, and American Postal Workers Union were resolved in interest arbitration. While such decisions substantially determine the largest component of Postal Service costs, the underlying interests of Postal Service customers and the American public are not required to be taken into account by the arbitrator.

Proposal. Postal collective bargaining should be reoriented based generally on the private sector model for essential services, most prominently reflected in the Railway Labor Act. This process brings to bear more intensive mediation procedures designed to lead the parties to reach their own resolution of the issues, and includes an opportunity for public policy input at the highest level, before a party can resort to self-help through strike or lockout. In addition, a specific detailed standard, reflecting the public interest, should be used in establishing the terms of the collective bargaining agreements.

If the initial negotiation period is not successful, a mediator of stature would be appointed by the National Mediation Board. The mediator would explore the differences between the parties in light of detailed standards reflecting the public interest, including—

- the interests and welfare of all postal customers
- a comparison of wages with the wages of other employees performing the same or similar services in the entire private sector
- the overall compensation presently received by employees, including wages, vacations, holidays, insurance, pensions, medical and hospitalization benefits, the continuity and stability of employment, and all other benefits received.

- relevant economic factors, including the previous financial record of the Postal Service, its present financial health, and anticipated future economic circumstances.

If the parties still failed to reach agreement, and did not provide for voluntary interest arbitration, the National Mediation Board could impose one or more cooling off periods. By executive order, the President could direct the appointment of a Presidential Emergency Board, with three neutral members, to explore the issues and provide a non-binding report. In making determinations, the Board would give due weight to the same statutory factors considered earlier by the mediator. Only if all of these measures failed, and Congress did not intervene to impose a settlement as it has done in several instances under the Railway Labor Act to protect the national interest, would the union be able to strike or the employer, to lockout employees.

Other Employment Reforms

Current Law. Presently, a number of employment benefits are subject to change from time to time by legislation, including pension and certain cost-of-living benefits for employees in remote locations. In addition, Postal Service salaries are capped by reference to the level paid to federal Cabinet officers. The law also overlays certain governmental personnel regulation outside the control of the Postal Service and its employees, including adverse action appeals to the Merit Systems Protection Board.

Deficiencies. Allowing benefits to change or adverse actions to be regulated both at the bargaining table and through legislation undermines the integrity of the bargaining process. This is a loophole excluding vital components of the postal job environment and major factors in the cost of its services from determination by management and labor together, with regard for the impact on their future and their customers. For example, in the past year employees received new Long Term Care insurance coverage and expanded Thrift Savings Plan options by legislation, without having to bargain for them. While, by law, wages and benefits are broadly intended to be comparable to those paid in the private sector, the upper limit on salaries prevents the Postal Service from approaching comparability at the executive level. This constraint adds to the difficulty in maintaining competitive services that will enable the Postal Service to retain the overall financial base required to pay for universal service at affordable rates.

Proposal. First, all future changes to all pension, insurance, medical and hospitalization benefits (including retiree health care), and any other changes to the hours or conditions of employment should be the subject of collective bargaining for bargaining-unit employees, rather than changed by legislation. Second, the limitation on maximum compensation should be eliminated. The Postal Service should provide compensation for officers, executives, and other non-bargaining-unit employees comparable to what is paid for comparable positions in the private sector of the economy. Third, the Postal Service and its employees should have full responsibility for adverse action procedures and other aspects of the employment relationship.

Submitted Questions, Government Reform Full Committee Hearing
United States Postal Service
April 4, 2001

1a. The USPS paid for Price Waterhouse Cooper for two studies in the past six years that identified an annual cost for processing Undeliverable As Addressed mail (UAA).

1b Did Price Waterhouse identify any potential ways of reducing the cost of the USPS' UAA mail?

1c. After paying for two studies what did the USPS do to reduce the UAA mail problem?

1d. Does it cost the USPS $1.5 billion annually to deal with Undeliverable As Addressed mail (UAA)? And is UAA mail the largest complaint against the USPS?

2a. Would automation and mechanization reduce costs?

2b. From 1995-1999, you were budgeted to spend $8,537 billion on capital investment in automation and mechanization equipment, however you only spent $5,298 billion, or 62% of your capital investment budget.

2c. Can you tell me why you didn't spend that?

3. You have consistently spent $300 to 500 million in advertising, even though the USPS maintains a monopoly on first-class mail. Do you think this money could have been used more effectively, such as making the USPS more efficient in dealing with Undeliverable As Addressed mail?

4a. One of the new changes for the USPS has been a shift to electronic mail.

4b. The USPS probably loses out on billions of dollars in potential revenue because companies are switching to this electronic billing?

4c. How much revenue has the USPS lost from its own e-commerce offerings?

5a. You are projected to be in debt anywhere from $2 billion to $3 billion, and to help with costs you looked for other areas of revenue, correct?

5b. And other areas of revenue include selling products such as phone cards, videos, T-shirts, baseball caps, stationary, greeting cards, ties, and selling advertising space on vehicles?

5c. And while attempting to develop these products the USPS has recently lost $85 million in this attempt. Could this money have been used for other initiatives to help productivity?

6. Your new electronic bill payment offering competes against the services a variety of financial services companies. Many of these companies are heavy customers of regular mail. Do you think it is fair for these companies to be, in essence, providing the investment capital for their competitor?

7. Do you believe there are any limits on the lines of business the USPS should get into?

8. What plans do you have to streamline the process by which innovative cost saving technology is introduced to the USPS?

9. What steps is the USPS taking to ensure that an aggressive program to quantify and capture all savings that result from the introduction of new automation systems being installed?

10. As businessmen, is this an appropriate time to ask for a rate hike from your customers? The economy is deteriorating and you are seeking to restore your prior year losses, as well as create a massive contingency fund at the expense of your mailers. Would USPS be better off protecting its volume base by not raising rates, and waiting until the economy improves or a reform bill is passed?

11. A potential alternative to a new rate case would be for the USPS to seek short-term solutions to its cash flow problems. What is your opinion regarding the concept of filing a rate increase based on a cash flow model, versus an accrued debt model?

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