

Executive Summary

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I. Introduction

We live in challenging times. Long-term technological and commercial trends, often termed the Second Industrial Revolution, are fundamentally reshaping national and international services for collection, transport, and delivery of all types of postal products. These trends will compel a fundamental transformation in our national approach toward the Postal Service as an institution and the delivery services sector as a whole.

At stake is the future of what has been, since this nation's founding, the right of every American to send and receive mail. The Postal Service exists as a governmental entity whose mission is universal service to all. That mission is a direct reflection of the values on which this country was founded, and it is those values of equality of opportunity that drive Postal Service management today just as they drove the managers of the Post Office Department.

In this *Transformation Plan*, the Postal Service respectfully submits to Congress and to the American people our views on the steps that must be taken now and the long-term options that appear feasible. With the valuable assistance of our stakeholders,¹ we have prepared this report as a decisive response to the challenges posed, a response that postal leadership embraces and commits to execute fully and effectively.

Today, a commercially and financially viable Postal Service remains vital to the American economy. The Postal Service delivers more than 200 billion pieces of mail each year (over 40 percent of the world's mail). It collects nearly \$66 billion in revenue annually and is the eleventh largest enterprise in the nation based on revenue. The Postal Service anchors a \$900 billion domestic mailing industry that employs roughly one in fifteen American workers. The Postal Service employs nearly 770,000 career employees, which makes it the second largest civilian employer in the nation. More than seven million Americans visit post offices each day. Additionally, more than 1.7 million new delivery points are added to the postal network each year.

The future role of the Postal Service, however, is uncertain. For any organization to remain viable and flourish, it must change. As technology, commerce, and society evolve, so too must government and corporate business models. This is no less true for the U.S. Postal Service than for any other enterprise.

The Postal Reorganization Act of 1970 (PRA) succeeded. It created an independent governmental entity well designed to deliver postal services in a more businesslike manner. The Act created a structure that enabled the Postal Service to function effectively over the last 30 years. With effectiveness came dramatic growth for the mailing industry, which contributed to economic growth and increased satisfaction for postal customers.

"The Postal Service has been a reliable, trusted provider of communications for more than two centuries. It is a basic and fundamental service provided to the people of America by their government. It helps keep Americans in touch, and it is the hub of a \$900 billion mailing industry. We are working to keep this critical national asset strong and vibrant, today and far into the future."

—Joint statement by the
Postmaster General and the
Chairman, Board of Governors

¹ This plan incorporates the comprehensive feedback received on the *Outline for Discussion: Concepts for Postal Transformation*, September 30, 2001.

The institutional model adopted in 1970 was not, however, designed to cope with the fundamental changes that are today reshaping the delivery services marketplace. These trends include the following:

Changing customer needs. With access to more information and more options than ever before, customers have a broad range of choices for delivery of messages, money, and merchandise—our three businesses. A single, basic, universal service, the premise of the PRA, is no longer sufficient to meet increasingly varied customer requirements.

Eroding mail volumes. Electronic alternatives to mail, particularly electronic bill presentment and payment, pose a definite and substantial risk to First-Class Mail® service within the next five to ten years.

Rising costs. Despite major gains in efficiency and productivity through automation of letter mail, the costs of maintaining an ever-expanding postal network are rising faster than revenue, especially costs outside the direct control of the Postal Service, such as retirement and health benefit liabilities.

Fixed costs. Universal service requires a significant infrastructure to deliver postal services.² Almost one-half of current postal costs are spent on these resources and that level does not increase or decrease when volume changes or when productivity increases. This creates a challenge for cost containment.

Merging of public and private operators into global networks. Former national foreign postal services, some privatized, have entered the U.S. domestic market; giant private firms that now dominate global parcel and express markets are entering an increasing portion of the postal value chain.

Increasing security concerns. Rising security concerns will require expensive and sophisticated countermeasures.

Consideration of these trends leaves no doubt that the time has come to address fundamental long-term questions. We at the Postal Service do not presume to have all of the answers. We do, however, in this report, offer our approach to transforming the Postal Service into an enterprise suited to the 21st century.

In the near term, we have concluded that substantial improvements in the efficiency of the Postal Service can be accomplished without major revisions to current law, provided our customers, our employees, and policymakers fully recognize and embrace the fundamental long-term transformation we are beginning. In this report, we describe our specific plans and seek support from Congress where incremental statutory changes are needed.

In the long term, we believe that fundamental restructuring of the legislative and regulatory framework for postal services is required. The public debate about postal modernization led by Congress over the last five years has illuminated important issues, many of which raise implications that stretch beyond legislative remedies presently contemplated. We need to address these larger issues and reach a national decision on the future of the Postal Service.

² Examples include more than 38 thousand post offices, stations, and branches, 240 thousand delivery routes to service over 137 million delivery addresses, 215 thousand vehicles, and significant annuitant retirement costs.

Over the next two to three years, it is vital that significant progress be made toward defining the long-term structure and role of the Postal Service. In support of that process, this report outlines three alternative models for the future role of the Postal Service. These range from a Government Agency, offering subsidized residual services not provided by the private sector, to a Privatized Corporation, a competitive company owned by private citizens. From among the conceptual models identified, we offer our own preliminary conclusion that a middle ground is the most appropriate: a Commercial Government Enterprise, owned by the government but structured and operated in a much more businesslike manner, with attributes appropriate to the unique role this institution plays in the nation.

In developing this report, we gratefully acknowledge the assistance of the full range of stakeholders in the postal industry. At the outset, therefore, we would like to articulate a firm commitment to all of these stakeholders, and especially to our customers. During this crucial transformation period, in order to maintain our financial viability and fulfill our universal service mission, we commit that we will:

- Foster growth by increasing the value of postal products and services to our customers;
- Improve operational efficiency; and,
- Enhance the performance-based culture.

This report describes how we will honor these commitments while remaining faithful to the vision that has inspired the post office for more than two centuries: that the Postal Service should bind the nation together by providing all Americans with vital communication and delivery service.

II. Meeting the Challenge

In order to address the challenges we face today and to prepare for transformation, we must push business effectiveness and operational efficiency to the limits permitted by current postal laws. With the support of customers, employees, and policymakers, there is much we can do, and are doing now. Building upon current efforts, we will implement the following specific strategies to support our commitments:

Growth through Added Value to Customers

Flexibility and growth will be essential for the Postal Service to transform successfully. To fulfill its universal service mission, the Postal Service must offer affordable products and services that serve the entire spectrum of its customer base, from large corporations to individual consumers. The Postal Service must also find ways to use existing resources to generate new revenues to offset anticipated losses from electronic diversion. Our products and services must also be flexible enough to adapt to 21st century technological advances.

With these requirements in mind, we will implement a number of specific growth strategies to increase value to our customers. We will:

- Work with the Postal Rate Commission (PRC) to create more streamlined processes for introducing targeted pricing initiatives, such as negotiated service agreements, and more regular and predictable price changes, such as phased rates.
- Expand access to postal services by doing business when and where our customers prefer.
- Move simple transactions to less expensive channels, improving customer service and increasing retail contribution.
- Develop “intelligent mail” products that not only track and trace from origin to delivery but also integrate information throughout the entire cycle of multiple business transactions.
- Work with customers to make sure databases are updated frequently and accurately, and explore the use of publicly available databases to improve the overall accuracy of address information.
- Make it easier to use postal services by aligning mail preparation and prices to customer needs and capabilities.
- Explore more innovative payment options for our customers through third party credit.
- Enhance revenue opportunities by leveraging existing assets and infrastructure, including postal-owned vehicles and facilities.
- Work with all package mailers to create a package offering that is simple, easy-to-access, information-rich, and takes advantage of our vast retail and delivery presence.
- Work with customers to add features that enhance the value of traditional products.
- Continue to seek opportunities to leverage our brand and assets to create new products and services with minimal investment.
- Strive to protect postal employees and customers from exposure to biohazardous material and to safeguard the mail system from future attacks.

Operational Efficiency

Cost containment is the most important customer-focused strategy, especially for large business mailers who rely most heavily on the postal infrastructure. In any network business, however, it is difficult to control costs when volume declines while the network itself continues to grow. This is the challenge faced by the Postal Service: increasing costs may have to be spread across a declining volume base.

In this difficult environment, we will achieve cost savings by implementing a number of specific measures designed to improve operational efficiency over the next five years. We will:

- Reduce operating cost by automating the flat mailstream and mail forwarding operations.
- Continue improving annual productivity through techniques such as benchmarking, standardization of best practices, and complement planning and scheduling.

- Explore new workshare and mail preparation opportunities to eliminate handlings in the presort-to-delivery supply chain.
- Experiment with new methods of reducing the time letter carriers spend in the office, for example, sorting flats into delivery sequence.
- Reduce transportation costs and improve transportation management by implementing network planning, routing, and tracking programs.
- Redesign the postal logistics network so that the number and location of processing centers, processing strategies for mail, and transportation modes and routes are optimized to meet customer service requirements at minimal total system costs.
- Revise purchasing regulations to allow for acquisition of goods and services in a manner similar to that followed by businesses.
- Explore alternative purchasing strategies for automation equipment and information technology to include leases and fees for services contracts.
- Optimize the retail network by lifting the self-imposed moratorium on post office closures and working with the PRC to significantly streamline the process for closing post offices.
- Pursue regulatory and legislative reform to provide the Postal Service the latitude to adjust service levels and delivery frequency to standards commensurate with the affordable universal service obligation.

Performance-Based Culture

Breakthrough productivity initiatives will be achievable only if we are able to make significant progress in our third commitment: enhancing our performance-based culture. For this, we must maintain an effective, diverse, and motivated workforce whose members know what is expected of them and who are recognized for individual and team accomplishments. The challenge to assure continuity of leadership has never been more important than it is today. Approximately 55 percent of Postal Service officers and senior executives and 36 percent of managers will become eligible to retire over the next five years. To address these challenges, we will:

- Enhance retention and recruitment strategies. Flexible and responsive retention tools and recruiting practices are necessary to address the attrition challenge.
- Strengthen succession planning to identify, to develop, and to select current and future leaders.
- Maximize the potential of available training and development programs in order to have a pool of potential successors at all levels of the organization.
- Change the culture of the Postal Service by improving our management of employee performance with data. This will be achieved by better defining expectations and measuring performance against those expectations. Accountability will be enhanced through greater use of performance-based pay to recognize individual and team efforts.
- Build a highly effective and motivated workforce by reinforcing management responsibility for a safe, secure, satisfying, and diverse workplace.

- Continue working with the labor unions to improve relationships, to reduce grievance costs, and to jointly examine modifications to the impasse resolution process we are recommending to Congress. The spirit of cooperation that resulted from the anthrax crisis set a solid foundation for future relationships.
- Optimize the ability to reposition the workforce by implementing data-driven assessment tools that will assist in determining skill needs and availability by location.
- Move repetitive transactional work to a shared services environment and explore outsourcing to reduce costs and increase efficiency.
- Improve the collective bargaining interest arbitration process to include a period of mediation. This would enhance the opportunity for the parties to reach mutual agreement on contractual issues.
- Reduce workers' compensation costs by implementing programs and developing employment opportunities for injured workers within and outside the Postal Service and by working with the Department of Labor on new initiatives and regulatory changes.

Enabling Functions

Enabling functions support attainment of the commitments described above. Focused financial management will enable the Postal Service to reduce outstanding debt, using it in the future for capital improvements where the value added by the investment exceeds the cost of debt. Enhanced financial management will also increase reporting transparency. Adopting business-driven purchasing and materials management procedures will enhance supply chain management. Applying information technology with universal connectivity will enable us to enhance security, add valuable product features, and manage operations in real-time. A continuing commitment to mail security will deny use of the mail to criminals while protecting the public and the Postal Service against external attacks and workplace disruptions.

Regulatory and Legislative Reform

Successful transformation of the Postal Service also depends in part on adoption of moderate regulatory and legislative reforms. These reforms will allow us to test new opportunities, to prepare for long-term structural transformation, and to prove our ability to deliver mail in a less constricted environment. Only in this manner will stakeholders have an opportunity to evaluate the extent to which such reforms add value. We will therefore seek expeditious implementation of the following regulatory, legislative and administrative changes:

Prices and Financing. Within the framework of the current rate-making process, the Postal Service will request several reforms to respond to customer pricing needs and restore postal finances to a more sound footing. We will seek approval for negotiated service agreements and other targeted pricing initiatives, reforms in procedures for introducing experimental mail classifications, phased rates, and inclusion of costs in the revenue requirement to finance the expansion of the delivery network on a current basis. The Postal Service believes that some of these reforms can be implemented administratively with the assistance of the PRC. In the event that efforts to achieve

these changes identify hurdles that cannot be cleared within the scope of our existing statute, we will ask Congress to enact legislation to remove those hurdles.

Facilities. The Postal Service will lift the self-imposed moratorium on post office closings and consolidations. The ultimate goal is to better serve our customers. A combination of rural delivery and alternative retail strategies may provide the most convenient access for the customer. To optimize facility networks, the Postal Service will also seek relief from legislative restrictions on post office closings and consolidations. Currently applicable administrative procedures should be streamlined or repealed, and appropriations riders referring to post office closings and 1983 service levels should be discontinued.

Flexible, Business-Driven Purchasing Procedures. Consistent with the way businesses purchase goods and services, the Postal Service will revise its purchasing regulations to the extent allowed by present law.

Labor and Employment Reforms. The Postal Service will seek more effective mediation procedures, including appointment of a neutral mediator by the Secretary of Labor, to help resolve bargaining impasses. In addition, repeal of the statutory salary cap is needed.

Our Commitment

In total, these near-term, customer-focused, operational, and performance-based strategies will generate \$5 billion in savings and cost avoidance through 2006, of which \$1 billion will be in post office operations. These savings will enable us to achieve some debt repayment and to hold rates steady from mid-2002 until calendar year 2004. If a rate increase is needed at that time, a moderate, negotiated increase will be pursued.

III. Preparing for the Future

The ultimate goal of Postal Service transformation should be to promote an efficient, reliable, and innovative delivery services sector that meets the diverse economic and social needs of the nation and all its citizens. It is becoming increasingly clear that the current structure of the Postal Service may soon be unable to support the achievement of that goal. Therefore, it is imperative to explore alternative business models to determine how best to structure the organization for future success.

Alternative Models

Fundamental structural transformation of an institution as large as the Postal Service will take many years to implement completely. Peering a decade or more into the future, therefore, this *Transformation Plan* reviews the full range of roles the Postal Service might be called upon to assume. While there are a number of potential paradigms for addressing the nation's postal policy objectives, this *Plan* describes three conceptual alternatives to the current model. Each would require structural legislative reform. The three alternatives are:

- **Government Agency.** An entity focused on providing essential services not adequately provided in the market and supported by government subsidies.

- **Privatized Corporation.** A business entity with private shareholders.
- **Commercial Government Enterprise.** A government-owned enterprise that would operate more commercially in the market to provide postal and related services.

In the Government Agency model, the nation would abandon the businesslike experiment begun by the PRA and retreat to a more standard government model. The Postal Service would concentrate more on its role in providing essential universal services and less on markets where customer requirements can be met by the private sector. The Postal Service might offer a stripped-down menu of products and services, eliminating a number of services currently offered and adjusting the workforce to the modified offerings and attendant lost volume. Significant declines in mail volume, especially First-Class Mail, would likely accelerate this process, shifting the center of gravity of the Postal Service toward delivery and retail services. It appears certain that, as before the PRA, the Government Agency created by this approach would be unable to fund public services entirely through postal revenues. The government would need to directly underwrite this shortfall. Over time, as revenues lag while the network continues to grow, the subsidy burden on the taxpayer could be expected to intensify under this model, a trend which would increase the pressure on traditional levels of service and access.

The second model, Privatized Corporation, would represent a complete conversion of the Postal Service into a privately-owned company dedicated to maximizing shareholder value. Postal Service managers would be subject to the supervision of a Board of Directors representing private shareholders with their own money at stake. There would be no expectation that the government would protect shareholders from commercial failure. Employees would no longer be under any form of civil service, and private sector labor and employment laws would apply. To address universal service coverage by the delivery sector as a whole, new regulatory safeguards may be needed. Other postal providers might be allowed to compete for delivery of universal services under contract with the government.

The third option, commercialization, carries the businesslike transition initiated by the PRA to the next level, but stops short of private ownership. Under this model the Postal Service would be a Commercial Government Enterprise wholly owned by the federal government. Postal Service managers would operate under more businesslike conditions. The Postal Service would offer both traditional and nontraditional products and implement market-based pricing, discounts and incentives, and business-based financing. The universal service obligation might be met under contract between the government and the Postal Service. A new labor model would be probable.

Recommendations

The near-term regulatory and legislative reforms described earlier will help to stabilize the postal system's financial base until more permanent legislative solutions are developed.

Long-term solutions have been the subject of ongoing debate and continuing disagreement within the postal community. The ultimate decision regarding the appropriate legislative framework is not the Postal Service's to make. Our experience

with the current system, however, leads us to certain conclusions about the changes that seem necessary. Therefore, we have included in this plan recommendations for transformational reform, recognizing that these matters will need to be debated further and resolved within the public policy arena.

In our view, of the three alternative models identified, the Commercial Government Enterprise is the option that will best allow integration of the postal system into the modern economy while preserving the ability of the Postal Service to fulfill its mission of universal service. While a conceptual model leaves many important details to be filled in, it appears that in principle, reorganization of the Postal Service as a Commercial Government Enterprise should permit major improvements in operational efficiency. Greater efficiency, in turn, should enable a financially viable Postal Service to maintain necessary universal services without direct government subsidies.

Transformation of the Postal Service into a Commercial Government Enterprise will likely require an extraordinary level of commitment from postal stakeholders. In the current political environment, postal reform legislation has faltered due in large part to an absence of consensus among affected parties. Basic economics will inexorably introduce tradeoffs between financial self-sufficiency and affordability, on the one hand, and the costs of underwriting an ever-expanding universal service network and other governmental obligations, on the other hand. We believe that a modern, self-sufficient postal system can be structured to continue providing universal service for all, at affordable prices. To do so, however, requires new flexibility to adjust networks and services to modern conditions and to minimize entrenched governmental rules and expectations that carry with them costs and inefficiencies. If the postal community is not able to achieve this break with the past, then it appears to us that the remaining options will be still more unpalatable to most stakeholders. We have not found much support for a Privatized Corporation that would reduce universal service, or a Government Agency that would require renewed federal subsidies. More likely, a continued stalemate would force the Postal Service to operate under its present, increasingly outmoded business model until enough customers abandon the system to make financial failure unavoidable.

A commercialized structure has been favored by liberalized national posts, either as a final operating model or as a transition to a fully privatized entity. Foreign policymakers have also generally concluded that restructuring the post office as a government-owned, commercial enterprise offers the best chance of achieving national policy goals in increasingly competitive markets.

The following are some of the changes that would be necessary to achieve a workable Commercial Government Enterprise:

Net Income and Retained Earnings. Production of net income and accumulated retained earnings are necessary to finance the expanding delivery network, decrease outstanding debt, and fund investments in technology.

Markets. The Postal Service should be free to make use of its assets and explore service offerings in related markets in order to help fund continuing universal service responsibilities.

Purchasing. Under a more effective, modern business model, legislative restrictions on the way the Postal Service acquires goods and services, including transportation, should be removed so that it can operate in a more businesslike manner.

Regulation. The Postal Service should have broad flexibility to set prices within overall parameters managed by the PRC and the Board of Governors, so that it could offer more moderate and predictable rate changes and so that users of monopoly services are not overcharged. Review of pricing and classification should be conducted through a complaint process. Outside the scope of the monopoly, pricing should be regulated under the antitrust and fair competition laws applicable to other businesses.

The Postal Service's universal service mission should continue, with the goal of preserving access to mail services for Americans nationwide on an economically sound basis. The standard for the number of delivery days and service levels should be flexible to accommodate changing conditions. The Postal Service should be able to make changes, subject to review for compliance, with broad criteria under a complaint system.

Labor and Employment. In order to increase the accountability of the organization with respect to overall performance, the Postal Service should negotiate with its employees' bargaining representatives about all employee benefits, along with wages and other working conditions. In labor impasses, the parties should be encouraged to resolve their differences themselves, through a compulsory mediation process similar to essential-service bargaining under the Railway Labor Act, which assures consideration of the public interest.

Consistent with other organizations in the mailing community, the Postal Service should follow private sector employment laws including those governing workers' compensation, equal employment opportunity, and alternatives to traditional employee dispute resolution processes. The Postal Service and its employees should not have costly, multiple avenues for complaints about workplace disputes.

IV. Conclusion

By any reasonable measure, transformation of the Post Office Department by the Postal Reorganization Act into a more businesslike Postal Service has been a success. After three decades of progress, however, pressing issues have been uncovered by a changing economy. The organization's structure and business focus are not aligned with the challenges of today's commercial environment. The Postal Service does not have the flexibility essential for successful management of a modern business. Postal laws create a tension between a public policy mission and structure and the businesslike necessity to deliver what customers want and will pay for in the marketplace. Until transformation is accomplished, the ability of the Postal Service to finance a continually growing universal service obligation without a government subsidy will be in serious doubt.

Today, all stakeholders face the need to reexamine the mission and structure of the nation's Postal Service. Alternative organizational models described in our plan represent possible future pathways for reform. No model comes with an assurance of success, and none accomplishes all possible goals. Each model offers benefits and

risks. The postal community spans a wide range of interests, with a diversity of perspectives on these issues. Resolution of differences has already proven difficult, but a consensus for change is necessary to equip the national postal system to perform its mission for the country in the decades ahead.

After careful consideration and consultation with stakeholders, the Postal Service believes that transformation requires action both in the near term and in the longer term. Both courses must be pursued concurrently. Near-term strategies include those steps we are taking now to improve value to our customers, enhance operational efficiency, and foster a more performance-driven culture. These strategies require only modest legislative and regulatory changes. Legislative reform for the longer term is needed to define a legal framework for the postal system over the next 30 years that remains consistent with the shared vision of the United States as a place where all citizens, in every part of the country, can participate equally and easily in the life of the nation.

Leadership Commitment

Successful transformation will require strong and committed leadership. Working together, the leadership of the Postal Service will forge a fundamentally new business model for the institution grounded in a business culture of performance and accountability. We recognize our responsibility to take definitive action and to offer our stakeholders a clear and compelling view of what we are doing and where we are going. We accept and welcome the role of Congress, our customers, our labor and management associations, and other stakeholders in this endeavor.

