Postal Regulatory Commission
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# ATTACHMENT D

## Message from the Chairman of the Board, James C. Miller III and Postmaster General & CEO, John E. Potter

Transformation became the watchword of the Postal Service in 2002. Our goal was to position the Postal Service to navigate a dynamic market environment and communications landscape successfully. The results speak for themselves.

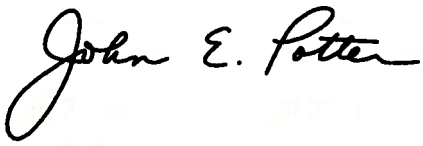
Our product and service offerings are marked by innovation, ease of use, and accessibility. We have reduced costs and increased productivity. Our people, the men and women of the Postal Service, have brought service performance and customer satisfaction to record levels.

This is just the beginning. The *Strategic Transformation Plan 2006-2010* has been created to take the next step. It builds on the momentum of our original *Transformation Plan* and stays focused on our core business and the strategies we know produce results. We will promote growth by creating more value for every customer. We will continue to reduce costs by improving efficiency in all our operational and business processes. We will bring service performance to even higher levels. We will use the best technology to make the mail a rich source of information both for our customers and our operations managers. We will achieve all this with an energized, customer-focused workforce.

The *Strategic Transformation Plan* will be updated annually. The business environment in which we operate continues to change almost daily. We cannot predict when or how today's technology will be overtaken by more advanced technologies. We cannot predict how events halfway around the world—or in our own backyard—will affect our costs. We cannot predict the final form of postal reform legislation—or even if it will occur. But we can do our best to prepare for the impact of these external factors. We understand that our *Plan* must be dynamic and adaptable. It must help us manage and succeed through periods of uncertainty.

We offer our commitment to continue the transformation of the United States Postal Service. Our goal is to ensure that the Postal Service can provide affordable, high-quality mail service to everyone in America—today and well into the future.

James C. Miller III



John E. Potter

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## Year References

All references to a specific year or "the year" refer to the government fiscal year ending September 30. However, specific month and year references pertain to the calendar date.

# EXECUTIVE SUMMARY

Transformation continues at the United States Postal Service. In the almost 4 years since publication of the first *Transformation Plan*, the Postal Service has delivered on its promise of focus and results. The *Strategic Transformation Plan 2006-2010* builds on the foundation of the earlier plan and continues its momentum.

In 2002 the Postal Service was emerging from the multiple shocks of an economic slowdown, September 11, and the anthrax attacks. Mail volume fell, and America's confidence in the mail was undermined. The 2002 *Transformation Plan* became the roadmap to recovery. It reinstilled confidence among postal employees and set challenging but achievable targets in service and cost management.

Today, service is the best it has ever been for all classes of mail. Productivity growth has been steady and strong. More than 80,000 jobs have been reduced through attrition and cumulative savings of at least $13 billion will have been realized by the end of 2005. Better service and stable rates have attracted new business. Direct mail volume is up 10 percent in 2 years. So far, at least, increases in direct mail revenue have offset losses caused by competitive, technological changes that are moving bills and payments online.

In the *Strategic Transformation Plan 2006-2010*, the Postal Service commits to making further advances in service, productivity, and employee engagement. The Postal Service will maintain a tight focus on core products to ensure that universal, affordable postal services continue to have the power to communicate, reach key audiences, and help bind America together. The Postal Service commits to continue taking $1 billion out of its cost base each year through 2010 while employing equally aggressive measures to grow the business.

## BEST VALUE IN THE MARKETPLACE

For postal customers, value is defined by quality of service, price, and ease of use. Over the next 5 years the Postal Service will continue to improve the value of its products to promote growth. It will focus primarily on advertising mail and package delivery services.

In the advertising market the focus will be to offer services that help businesses grow. New features will be added to First-Class Mail to make it a more powerful communication tool for advertisers and financial service providers. Small businesses remain an enormous engine of the nation's commerce, and the Postal Service is developing ways to make advertising mail more accessible and easier for them to use.

Customers of all sizes will see continued improvements in package delivery services as the Postal Service continues to automate operations, increase ease of use, and expand track and trace capabilities. These changes will better serve households and small businesses that use end-to-end package service. Improvements will also benefit consolidators who rely on the Postal Service for delivery only.

The Postal Service earns 85 percent of its revenue from businesses and institutions, all of which have choices in how they communicate, bill, and ship. To keep prices predictable, the Postal Service will transition to adjusting commercial rates annually, generally in line with the Consumer Price Index. To meet the unique needs of business customers, customized prices will be developed where possible.

Customers are now finding that the Postal Service is more convenient. Services are available via *usps.com*, 1-800-ASK-USPS, by mail, at Post Offices, self-service kiosks, grocery stores, and ATMs. The Web is making it easier and faster to deposit commercial mailings as transactions such as manifesting, postage payment, and entry scheduling move from paper to electronic media.

## BEST RUN COMMUNICATIONS AND DELIVERY SERVICE

Each day the Postal Service receives and delivers over 680 million pieces of mail. Distribution and transportation of these letters, parcels, catalogs, and magazines occur across a network of 38,000 Post Offices and retail outlets and 400 mail processing facilities. The mail is securely and reliably delivered to 143 million addresses. No single operation in the world comes close to this level of connectivity with households and businesses across America.

Over the past 4 years, operations have improved to produce better, more consistent service with fewer resources. Today, the Postal Service delivers more than twice as much mail as it did 2 decades ago, with the same number of employees. In the next 5 years, there will be more change. Delivery remains the largest cost center and will be the focus of intensive efforts to find new savings. The entire mail flow will be streamlined, made more flexible, and managed as a single, integrated network, not as multiple separate operations.

In the longer term, a standardized postal network will contain fewer types of processing facilities. Larger regional distribution centers will serve as primary nodes for multiple products, and smaller local processing facilities will process all mail destinating in their geographic areas. These changes will reduce costs and improve reliability.

Implementation of industry best practices throughout the mail value chain will eliminate costly rework and standardize operations that will benefit both the Postal Service and its customers. The Postal Service and the mailing industry must work together to raise quality levels by assuring correct and complete addresses and routing information.

Customer mail preparation requirements to qualify for discounts will evolve as postal networks are streamlined and new automated processing equipment is deployed. New tools will help handle fluctuations in demand at the lowest possible cost. Advance notification systems will tell how much mail is arriving. Tracking systems will show how mail flows across operations. Planning models will calculate required resources. Internal processes will also be further streamlined to reduce costs and allow the Postal Service to be more nimble.

## BEST PLACE TO WORK

The entire Postal Service will hold itself accountable to its customers to deliver more consistent quality and higher levels of customer service. The higher the quality of service targeted, the greater the importance of identifying and maintaining a skilled and committed workforce. The goal is an environment that encourages employees to strive to be the best. Therefore, the Postal Service will continue to build a performance-based culture and improve the skill sets of its workforce at all levels. Training and leadership development will emphasize teamwork and customer focus.

Postal employees are known for a deep commitment to service, which is witnessed daily in the thousands of communities they serve. Building on this commitment, the Postal Service will increase employee involvement at all levels and will continue to recognize high performers. Every employee will have the opportunity to move up in the ranks of the organization through outstanding performance and career development opportunities.

## THE POSTAL SERVICE IN 2010

The Postal Service exceeded most of the aggressive targets that it set in its first phase of Transformation. In the course of executing that *Plan*, postal employees gained invaluable experience and new levels of confidence in the organization's ability to meet challenges.

Despite the challenges ahead and the unresolved status of pending postal reform legislation, the Postal Service is confident that it will also achieve the goals in this next phase of Transformation. Certainly, the challenges are great, especially the declines in First-Class Mail and continuing increases in the number of delivery points. But the opportunities are greater. They include the promise of Intelligent Mail technology, the prospect of new savings through standardization, the power of the Postal Service's unique connection with every American household and business, and the potential of a fully-engaged 700,000-strong workforce committed to meeting customer needs.

# INTRODUCTION

The *Strategic Transformation Plan 2006–2010* is the Postal Service's blueprint for the future. Like the *Transformation Plan*, published in 2002, it describes how the Postal Service will improve the value of mail and, by doing so, help sustain a financially stable enterprise that best serves the nation's mailing needs as it provides affordable and reliable universal service.

The 2002 *Transformation Plan* helped the Postal Service become a far leaner, more effective and modern organization. It attained record levels of service and customer satisfaction, and will achieve its goal of $5 billion in cost reductions ahead of its 5-year target. Postage rates have been stable since 2002 as a result of improvements in postal productivity and a legislative change that temporarily eliminated postal overpayments to the Civil Service Retirement Fund.

Under the 2002 *Transformation Plan*, the Postal Service has been using the flexibility available within current law to think beyond what was perceived as possible only a few years ago. This is consistent with recommendations of the Government Accountability Office (GAO) and The President's Commission on the United States Postal Service.

## Government Accountability Office Review

The 2002 *Transformation Plan* was developed to address the challenges outlined by the GAO in 2001.[1] In its most recent follow-up to that study, the GAO concluded that the Postal Service:[2]

- Has had a notable result in controlling costs and improving productivity.
- Addressed a number of critical financial issues.
- Improved human capital.
- Greatly improved the transparency and quality of its financial information.

## The President's Commission on the United States Postal Service

In July 2003 the President's Commission on the United States Postal Service offered recommendations for improving the Postal Service. Progress has been made on many of its recommendations, including expanded customer access to postal services, negotiated service agreements, testing personalized stamps, and pay for performance.

## Purpose of the *Strategic Transformation Plan 2006–2010*

This plan enables the Postal Service to maintain and build upon the momentum of the 2002 *Transformation Plan*, while helping ensure that the organization can respond to changing customer needs, market requirements,

[1] *Major Management Challenges and Program Risks: U.S. Postal Service*, GAO-01-262, January 2001.

[2] *Major Management Challenges at the U.S. Postal Service*, GAO-05-207, January 2005.

technological developments, and legal requirements. The Postal Service will continue its commitment to take $1 billion out of the cost base each year, which, in combination with revenue growth strategies will sustain the mission of providing universal service at reasonable rates.

*This* Plan *is the Postal Service's blueprint for the future. It describes the strategies that will improve the value of the mail, helping to sustain a financially stable enterprise that provides affordable, reliable universal mail service.*

The Postal Service's challenges are considerable. Up to 2 million new delivery points are added to the postal network each year, equivalent to adding cities the size of Chicago and Baltimore. Meanwhile, First-Class Mail, which produces the greatest contribution to cover network costs, has been declining. Therefore, the Postal Service will require other means of financing growth of the universal service network. The ability to find financial relief through growth in other postal products is challenged by intense competition. Postal costs, especially for employee compensation, retiree health benefits, and fuel, are rising at rates much greater than inflation.

## How the *Strategic Transformation Plan 2006–2010* is Organized

The *Plan* is organized around the Postal Service's four strategic goals:

- Generate Revenue.
- Reduce Costs.
- Achieve Results with a Customer-Focused, Performance-Based Culture.
- Improve Service.

Each chapter includes strategic challenges and trends relevant to the goals. These are followed by the Postal Service's transformation strategies for 2006—2010. Recent accomplishments are discussed where they contribute to an understanding of future plans.

The *Plan* integrates and satisfies the requirements of four previously separate publications: the *Transformation Plan*, the *Five-Year Strategic Plan*, the annual *Performance Plan*, and the annual *Transformation Progress Report.* Appendix A provides details required by the Government Performance and Results Act.[3] Appendix B summarizes the stakeholder outreach program that supports the transformation process. Appendix C provides an overview of the Postal Service's fixed versus volume variable costs.

In addition to the *Strategic Transformation Plan 2006–2010*, the Postal Service will continue to publish its *Annual Report* and the annual *Comprehensive Statement on Postal Operations* (including the annual *Performance Report*). Each publication is available at *usps.com*, along with other substantive information on postal operations and finances. Together, these reports provide stakeholders with detailed information on postal policies, programs, resources, and performance.

[3] The Government Performance and Results Act (Public Law 103–62) requires federal agencies to publish a 5-year strategic plan and an annual performance plan.

# I. GENERATE REVENUE

The Postal Service is a self-sufficient agency deriving its revenues almost entirely from postage and fees paid by mailers. Postal operations are not supported by tax dollars. Revenue must completely cover the cost of operations, including growth of the universal delivery network, investments in future improvements, and numerous public service functions. The Postal Service must set prices to cover costs.

## STRATEGY: FOSTER GROWTH THROUGH CUSTOMER VALUE

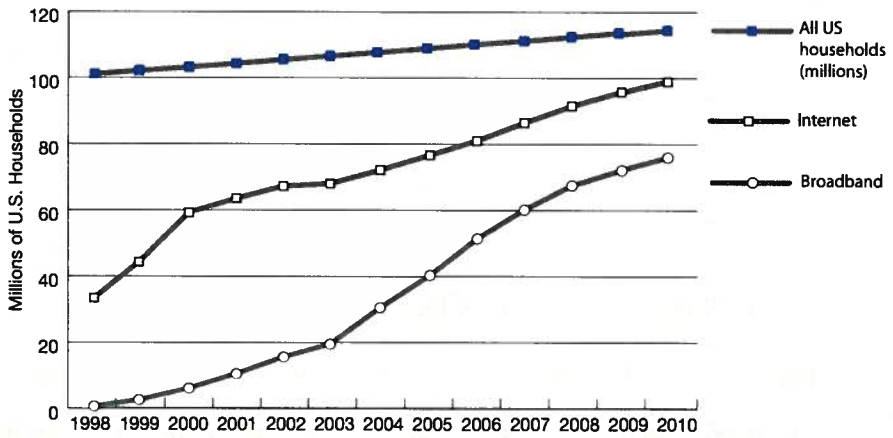
Create more customer value in core products and services to increase mail volume and revenue to continue financing universal service and the growing delivery network. Value includes increased product utility, improved ease of use and access, and more reliable, predictable performance at affordable prices.

## A. STRATEGIC CHALLENGES AND TRENDS

A number of key trends will influence customer use of the mail over the 5-year planning period:

- The Internet now reaches more than 71 percent of households and penetration is expected to increase. High-speed broadband makes Internet-based services easier to use and will likely increase the use of online alternatives to mail. The projected decline of First-Class Mail impacts the Postal Service's ability to continue to finance the growing universal service network. This is the single greatest challenge facing the Postal Service.
- Businesses attempting to contact and influence customers are finding it more difficult to reach mass audiences and are turning to more sophisticated techniques and technologies to reach selected audiences with more relevant messages.
- Consumers want readily accessible, relevant information to make better decisions, and the Internet is fast becoming their primary

**Projected Growth of Internet and Broadband**




*Source: Forrester Associates*

# IV. IMPROVE SERVICE

The Postal Service has been very successful in improving service under Transformation, even as it has reduced operational costs. Compared with 2002, postal customers now have more consistent and reliable mail service, easier access to products and information, and many more options for using the mail to maintain business and personal relationships.

## STRATEGY: PROVIDE TIMELY, RELIABLE DELIVERY, AND IMPROVED CUSTOMER SERVICE ACROSS ALL ACCESS POINTS

Improve the quality of postal services by continuing to focus on the end-to-end service performance of all mail. Ensure that postal products and services are designed and delivered to meet customer expectations and that all customer services and forms of access are responsive, consistent, and easy to use.

## A. STRATEGIC CHALLENGES AND TRENDS

The following challenges and trends are factors in planning for service improvements:

- Customers have increased expectations for service. They expect more personalized service across all channels without necessarily giving up the benefits of low cost and privacy.
- Express and package delivery providers are the most highly rated services in the country, according to the *American Customer Satisfaction Index at Ten Years* report published in 2005. Customers form their expectations based on experience with these companies and expect the Postal Service to provide equal value and features such as track and trace.
- More households are comprised of single heads of households or working couples, often with longer work hours, uncertain schedules, longer commutes, and frequent travel. Convenience is a critical service factor in accessing and receiving products and services.
- Customers are more likely to seek and compare information from a number of sources, increasingly using the Internet. They expect to be able to access information and manage their relationships with businesses, at least in part, on the Internet.

## B. TRANSFORMATION STRATEGIES

The preceding three sections of the *Plan* describe actions designed to create more value for customers, a strong, stable financial bottom line, and a more engaging and rewarding workplace. However, none of these outcomes are possible without the Postal Service keeping its eye fixed

squarely on its paramount goal to provide great service while protecting customer privacy and preserving the sanctity of mail. For postal customers, service has two key dimensions:

- The speed and reliability of end-to-end mail delivery.
- The quality of customer service provided at all customer contact points — at home, at their business, at the Post Office, on the phone, and online.

Under the 2002 *Transformation Plan*, the Postal Service successfully improved service performance across all product lines. At the same time it enhanced the quality of customer service and expanded access to postal services and information. Much of the success in end-to-end service performance resulted from the Postal Services' ability to make the most of advances in information technology. In addition to independent measurement systems, data from the passive scanning of mail containing Delivery Confirmation, CONFIRM, and Indicia Based Information (IBI), helped to pinpoint quality problems and improve service across all product lines.

Efforts will be focused on all components of the mail value chain, from mail creation through delivery. The Postal Service will continue to work closely with mailers to improve address quality, to maximize barcoding on all mail, and to improve the accuracy of information about their bulk mailings. New service measurement approaches will be developed to allow for an even more open and transparent mail system. More data will become available to help target processing bottlenecks and untimely or inconsistent distribution or transportation handoffs.

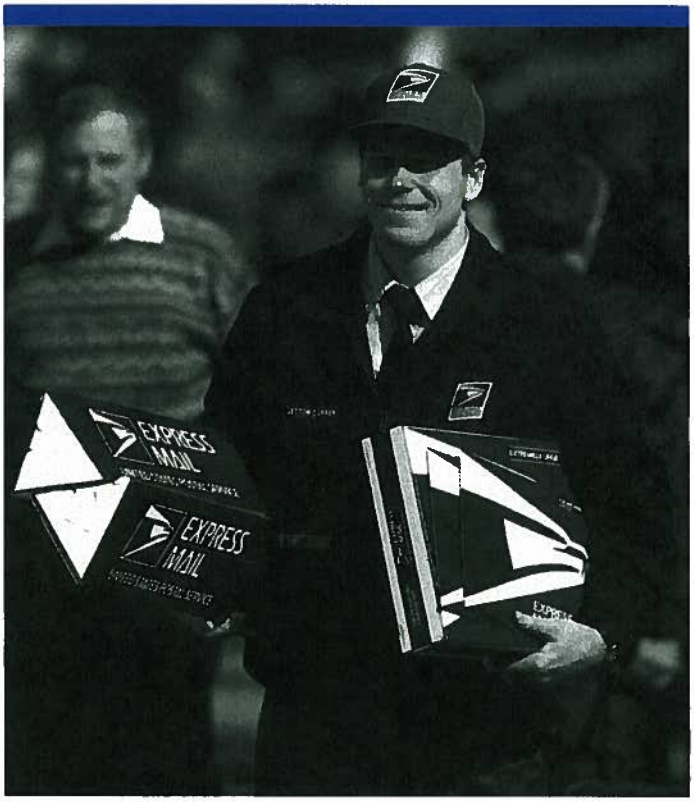
New customer access channels have been developed to give customers many more options for conducting postal transactions. Customers have the flexibility to do business with the Postal Service in person, over the phone, over the Internet, and by mail. Even so, there are still opportunities for improvement across all contact points. The Postal Service will continue ongoing efforts to make it easier than ever to use the mail, while providing a level of service that exceeds customer expectations — as is expected of one of the nation's premier service providers.

*The Postal Service will continue its aggressive efforts to provide timely, reliable, and high quality mail service, and improve the exchange of information with customers.*

## 1. Provide Timely, Reliable End-to-End Service

Customers expect timely, reliable mail service, and the Postal Service has delivered. For 2 years running, 95 percent or more of First-Class Mail with a next-day standard has been delivered on time. First-Class Mail service performance improved in all measured categories — overnight, 2-day, and 3-day service areas. Express Mail and Priority Mail continue to meet or

exceed objectives. Customers have taken note and customer satisfaction scores have never been higher. For 15 consecutive quarters, more than 93 percent of residential customers rated their overall satisfaction as excellent, very good, or good. Similar ratings came from the three categories of business customers surveyed. Ratings are from the Customer Satisfaction Measurement system, an ongoing independent assessment of customers' experience with the Postal Service.




An additional indicator of First-Class Mail service quality is the *Phoenix-Hecht Postal Survey*™, an independent measure of remittance mail (bill payments) processing performance. This survey is designed to measure and report total float, in the same manner that a remittance processing customer would experience it. The survey reports that since 2001 the average amount of time for delivery of remittance-type mail pieces has been reduced more than 8 hours.

Improved service was the result of refinements to sort plans to minimize handlings, improved OCR recognition technology, surface transportation reviews, and use of diagnostic tools, including feedback from mailers' own tracking systems. Approaches have been focused on improving service for all products.

The Transformation strategies described in the following sections will help the Postal Service attain even higher levels of service. The Postal Service's goal is to provide visibility through the entire mail value chain for all of its products — from mail creation, through deposit, processing, transportation, and delivery. Aggressive efforts will continue to improve quality by further expanding standardization, developing new data on in-process quality problems, and improving the exchange of information with customers. The Postal Service will place special emphasis on improving address quality, reducing undeliverable-as-addressed mail, and improving distribution performance using technology. Standardized operating processes, discussed in more detail in Chapter II *(Reduce Costs)*, will generate better control of each handoff during the 24-hour operating window and will result in more consistent service for all mail.

### *Increase Visibility Across All Product Lines*

For many customers, information about the mail is becoming almost as important as the mail itself. The quality and timeliness of information is often a determining factor in the customer's choice of a service provider. In 2006 the 4-state barcode will begin to provide new information about the mail, and enhancements to IBI information will also help. Service improvements for all products will continue to be made and be responsive to customer expectations. Potential adjustments to service levels will be reviewed to assure close alignment with customer expectations, market demand, and cost. As mentioned in Chapter I *(Grow Revenue)*, the Postal Service will provide product visibility throughout the system to enable customers to obtain information about their own mailings, regardless of shape and class.

### *Expand Service Measurement Capabilities*

*In 2006 the 4-state barcode will begin to provide new information about the mail. The Postal Service will explore expanding its service measurement capabilities for all mail.*

The Postal Service will continue to measure end-to-end transit time for First-Class Mail to maintain current high levels of service and identify further improvement opportunities. The current system was designed to measure service for single-piece First-Class Mail from the time the mail piece starts its journey at deposit to actual delivery. The Postal Service's goal is to assure that bulk-entered First-Class Mail attains the same high level of service given to single pieces. Standard Mail next-day certain service has been achieved for letter-size mailings entered at the destinating Sectional Center Facility. In addition, the Postal Service makes every effort to meet requested in-home delivery date windows for Standard Mail. Customers currently using CONFIRM or Delivery Confirmation can now track service on their own mailings, and additional reports will become available. The Postal Service also uses these systems with seeded mail to generate diagnostic data.

By combining the passive scanning of the various barcodes with improved start-the-clock acceptance information via improved bulk acceptance systems, it will be possible to measure service performance for all classes. To support service improvements for various commercial products, data from PostalOne!, Delivery Confirmation, CONFIRM, transportation tracking, and product tracking will be integrated and reviewed. In-transit scanning will be enhanced to create better diagnostic data so that bottlenecks can be eliminated throughout the system. This will assist in reducing cycle times over the entire mail supply chain. Priority Mail service strategies to extend current overnight reach will also be explored. In all cases, the objective is to provide highly reliable estimates of service performance while minimizing measurement cost.

### *Reduce Undeliverable-As-Addressed Mail*

The Postal Service will continue to increase the value of mail by working with the mailing industry to reduce undeliverable-as-addressed (UAA) mail by 50 percent by 2010. UAA mail is mail that must be forwarded, returned to sender, or treated as waste because the recipient information or address is incomplete, incorrect, or out of date. The handling and processing of UAA mail costs the Postal Service over $1 billion annually. In addition, because the return on mailers' investments in mail is reduced by the amount of mail that cannot be delivered, address quality has been identified by the Mailers' Technical Advisory Committee as one of its major areas of focus.

The Postal Service in developing new or enhanced services to ensure that mail is delivered to the right recipient, at the right address, the first time. New address hygiene services such as Address Element Correction will be offered to improve the completeness and accuracy of mailing addresses. Mailing lists that are sold commercially will be certified as to their use of these hygiene services.

Mailers will be encouraged to update customer information more frequently and closer to the date of mailing to reduce the need for forwarding services. Policies such as MoveUpdate requirements will be reviewed and strengthened for these mailers. Other types of UAA will be reduced by providing mailers with address hygiene tools and products based on secure technologies that identify incomplete or incorrect delivery address information before mail entry. Once UAA mail is entered into the mail stream, new processes will become available with the implementation of the 4-state barcode, such as OneCode/Address Change Service, to provide efficient feedback to mailers regarding their UAA mail. This will ensure that addresses are corrected before the next mailing.

Customers will benefit from the Postal Automated Redirection System (PARS), which reduces the number of days required to redirect mail that requires forwarding to a new address by recognizing and redirecting mail earlier in the distribution process. PARS is expected to substantially reduce UAA costs and greatly reduce the need for computer forwarding units that handled this mail before.

## 2. Improve Customer Service Across All Contact Points

Postal customers define quality as reliable, courteous, and responsive service. Further, they expect accurate, consistent information regardless of whether they come to a Post Office, contact the Postal Service by phone or the Internet, or ask their carrier about a product or service. The

Postal Service recognizes that customers form expectations on critical attributes such as waiting time in line based on their experience with other similar services, and compare Postal Service performance to best-in-class providers.

The Postal Service is committed to continuously improving the quality and functionality of its customer services and continues to focus on customer convenience across various access points. Strategies to provide online access from the home or office are being enhanced for more services and products. In order to reduce waiting time in line at many post offices, automated postal centers (APCs) have been introduced and later evening and Saturday hours have been implemented. Call center performance has been enhanced to improve both online and telephone access for problem resolution.

To stay abreast of rising customer expectations, the Postal Service is committed to incorporating new features and technologies to further enhance customer access. It will pursue strategic alliances where partners can help speed development and/or reduce shared costs. It will continue to place special emphasis on enhancing online and self-service capabilities to further reach out to customers where they live, work, and shop.

### *Continue to Improve Delivery Service Quality*

In multiple sections throughout this *Plan*, the Postal Service identifies areas where it is working to build upon the longstanding relationship between carriers and the customers they serve each day. Carriers will be more prepared to discuss customer needs and postal services. The strength of the carrier-customer relationship and the uniqueness of the Postal Service's daily connection to home and office is the basis for many business development strategies described in this *Plan*. In order for those strategies to succeed, however, current high levels of delivery performance must be maintained.

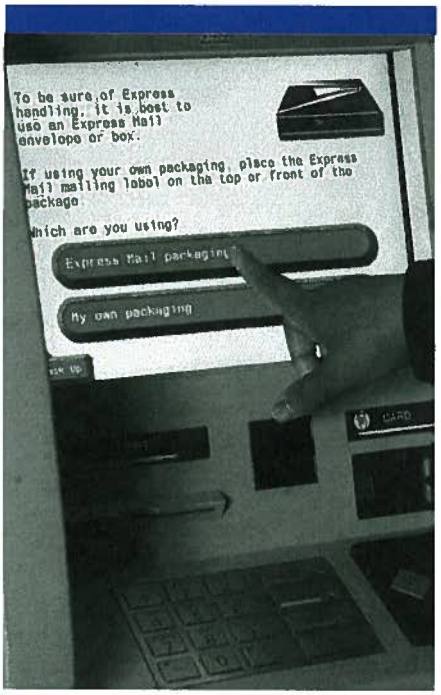
Under 2002 *Transformation*, the Postal Service implemented very rigorous efforts to isolate and eliminate problems in delivery service quality. Emphasis has been placed to minimize the largest customer dissatisfiers, notably time of delivery and misdelivery. Where these quality problems still exist, they will be reduced further. For areas where service levels are less than expected, additional focus will be received. The Postal Service will also step up efforts to minimize deliveries occurring late in the day.

### *Build Customer Awareness of New Forms of Access*

Major efforts have been made to make mail services quick, easy, and convenient, including the development of new ways for customers to obtain information and access postal services. Progress includes *usps.com*, the award-winning Web site, where customers can easily compare mailing options, print package labels with postage, schedule pickups, hold mail, and track shipments. Combined with a carrier coming to the home or office 6 days a week, this has been a major advance for time-starved customers. Customers can also purchase stamps in over 60,000 retail locations such as grocery stores, convenience stores, and ATMs. APCs have been installed in many Post Offices across the country, and now allow customers to mail on their own time, including evenings and weekends, when the retail counters are closed. The Postal Service's goal is to double the percent of retail transactions via alternate access channels to 40 percent by 2010.

Increasing awareness and use of these options is a high priority for the Postal Service. Many customers are unaware of all the ways and locations they can purchase postage stamps, not to mention all the other services that can now be completed quickly and easily right from their home or office. The Postal Service will expand on recent successful efforts to increase awareness. Advice and information about *usps.com*, Click-N-Ship, Carrier Pickup, and other services will continue to be featured in advertising and communications. The 700,000 employees of the Postal Service, who know their customers best, will continue to spread the word as well.

To stay abreast of rising customer expectations, the Postal Service is committed to incorporating new features and technologies to further enhance customer access. It will pursue strategic alliances where partners can help speed development and/or reduce shared costs. It will continue to place special emphasis on enhancing online and self-service capabilities to further reach out to customers where they live, work, and shop.




*The APC features an integrated scale and easy-to-use touch-screen menu, making self-service mailing easier than ever. It was recognized with the "Best Retail Kiosk" award from the Kiosks.org Association, which represents the electronic self-service kiosk industry.* KIOSK *magazine said the APC has the potential to "do for the Post Office what ATMs did for banking."*

### *Tailor Retail Improvements to Serve Customer Needs*

Innovations such as Click-N-Ship and the APC build upon what is already America's most robust and ubiquitous retail network. Customers can now access many services online, with pick up and delivery to their door. But that does not mean that the services available at Post Offices will be reduced in any way. Customers with more complex needs will continue to find full service at Post Offices, with retail associates prepared to explain the full ranges of services available or offer advice on how best to use mail to grow a small business. Services will be streamlined

and made more uniform from one location to the next, so customers can quickly and easily find the products that are right for them. The Postal Service made great strides simplifying forms and product information, and this work will continue in tandem with steps to simplify the product offerings themselves. The Postal Service will also continue to explore ways to better meet the needs of non-English speaking customers in Post Offices and on *usps.com*.

The Postal Service will continue efforts to serve customers at Post Offices in 5 minutes or less. This will be accomplished through more efficient staffing and scheduling, enabled by detailed data on transactions volumes and customer traffic. Incremental improvement targets will be established to improve performance to assure that by 2010 customers are served within the 5 minute standard.

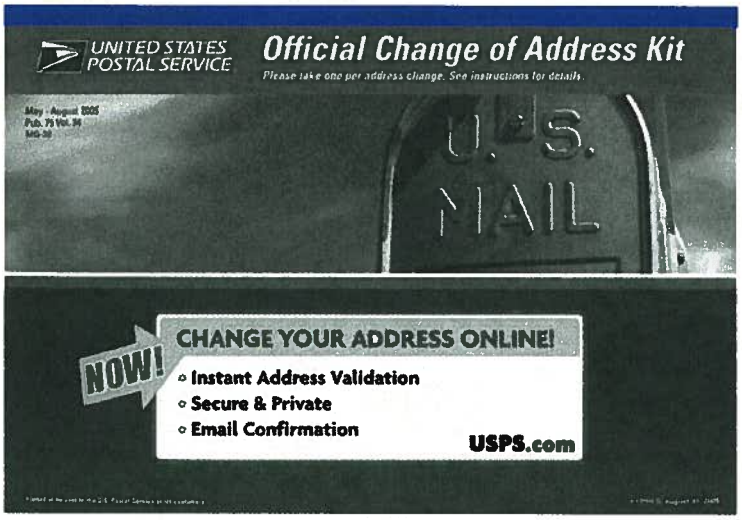
Extended evening and/or Saturday hours are being offered at select Post Offices where customers support extended service with adequate revenue. The goal is to align service with customer needs without increasing total cost. This will be done by adjusting staffing to more closely match customer traffic.

### *Promote New Technologies that Improve Change-of-Address*

Each year, 45 million change-of-address (COA) requests are submitted, roughly equivalent to the combined populations of New York, New Jersey, and all of New England. The Postal Service has recently introduced several improvements to make the process more convenient and efficient. It simplified the COA form, allowing customers to provide more complete and accurate information about their old and new addresses. With a strategic partner, the Postal Service reduced the cost to produce and distribute COA forms and notification letters, and continued to add new value for customers, including the introduction of Internet and telephone COA. These processes provide more accurate changes because customer-supplied address information is validated against address databases at the same time the request is submitted. The Postal Service's goal is to increase the annual number of COAs submitted online from almost 5 million today to over 20 million in 2010.

There are a number of other efforts underway to improve the convenience of changing addresses. This year the Postal Service will test email notification to customers that mail forwarding has begun, as well as follow-up reminders when forwarding is about to expire. It will also improve the availability of information about changing addresses and develop a secure automated process for customers to correct, modify, or cancel a COA submission if necessary.

The Postal Service has implemented a new, more secure process for mailers to update their mailing lists with change-of-address information. To improve the performance of mail forwarding, the Postal Service has worked closely with the mailing industry to enhance address quality, improve the filing and processing of COAs, and ensure more frequent use of move update products by qualified mailers. New NCOALink technology has allowed the Postal Service to license more companies as change-of-address providers, and made it possible to directly license COA data to end users. This improved process has increased the volume of verified addresses as well as the overall match rate. All of the improvements continue the high degree of privacy protection that postal customers have come to expect.




*The Postal Service will improve the convenience of changing addresses. With 45 million change-of-address requests each year, the goal is to have over 20 million submitted online by 2010.*

### *Enhance Support for Customers and Employees*

The Postal Service maintains a national network of integrated call centers handling more than 65 million contacts a year. It operates 24 hours a day, 365 days a year. Recent successes include automation of change-of-address and hold-mail transactions, handling of leave requests for most bargaining unit employees, fielding requests for advertising and mailing supplies, while continuing to provide product information to customers. In addition, over 29,000 Post Offices use the postal intranet to access *My Post Office* to retrieve customer service requests taken at 1-800-ASK-USPS or *usps.com*. *My Post Office* links these requests with local units, giving customers the benefit of a simple national contact point combined with local postal knowledge and expertise. While these successes have increased the total volume of contacts, annual cost savings continue to be realized. The Postal Service will continue to improve operation of the customer contact centers and related customer response groups by providing high-quality and complete first contact resolution that is faster, better, and less expensive. When necessary, it will ensure timely and efficient follow-up contact and resolution.

### *Nationally Recognized Privacy Policies*

The Postal Service's ability to safeguard the mail is a fundamental component to providing high-quality, reliable service. Mail remains one of the most private and secure means of communication. The Postal Service has long protected its customers from crimes involving the mail, including

identify theft. A recent Federal Trade Commission survey entitled, *Identity Theft Survey Report*, indicates that only 4 percent of identity thefts in the United States are attributed to stolen mail. As it adds new channels to access its services, the Postal Service will continue to assure the highest levels of protection for personal information collected from postal customers, employees, and business partners. The Postal Service will maintain the highest levels of trust in its privacy policies by measuring satisfaction and driving adjustments to policies or communication. In addition, it will simplify privacy policy compliance by increasing process efficiencies while reducing costs. Records management will improve by standardizing data retention practices, developing new policies based on industry standards, and more effective Freedom of Information Act processing.

### *Maintain Security and Trust*

The Postal Service's commitment to improved service continues with protecting the mail, employees, and customers. As a trusted and treasured national asset, the Postal Service faces a variety of security challenges which require aggressive investigative, preventive, and security responses. The Postal Service will continue to align its resources to provide vital services that secure end-to-end delivery of mail, protect employees in their work environment, protect the Postal Service infrastructure, and protect and educate consumers through fraud awareness initiatives.

The Postal Service will work collaboratively with internal and external groups to ensure new postal products and services are secure, thus maintaining customers' confidence in the mail and satisfying their personal and business needs. Providing the highest possible quality of service is the foundation of the Postal Service. Without service quality, growth would not be possible regardless of price.

## Summary

If there is one thing postal employees believe more than any other it is that the Postal Service exists for one reason – to provide universal service to all Americans, with the highest levels of quality, and at reasonable, affordable prices. The *Strategic Transformation Plan 2006-2010* is about continuing to deliver on the Postal Service's commitment to the nation. It is about working methodically to improve what is already the world's best mail service. Under this new phase of Transformation, the Postal Service will continue to exceed customer expectations – by focusing on core business, isolating and eliminating quality problems, managing to tough standards built around the customer, and quickly replicating successes across the organization. The Postal Service is also committed to changing with its customers, designing new products to meet new needs, and creating new solutions that customers value.

# CONCLUSION

The *Strategic Transformation Plan 2006–2010* is the blueprint for the future of the Postal Service. It responds to changes in the current business environment and attempts to anticipate further changes. Management will communicate the results of this planning effort to postal stakeholders and work with interested parties to adapt and refine strategies. The success of the *Plan* depends on close cooperation with the mailing industry and postal employees.

*The Postal Service will continue to transform. It will continue to deliver on its commitment to customers, employees and the American public. The Postal Service will continue to provide timely, reliable delivery to every address at reasonable rates.*

The four primary strategic goals — generate revenue, reduce costs, engage employees, and improve service — are not likely to change under any future legislative or regulatory environment. The performance objectives and strategies in the plan are designed to support achievement of the goals under most expected future conditions.

No plan can anticipate the future perfectly. Therefore, the *Strategic Transformation Plan 2006–2010* will be updated annually to reflect continued developments in the business and regulatory environment, including any legislative changes. Management will continue to report on performance annually, and objectives and strategies will be updated. Performance measures will also continue to evolve in order to drive results that matter to customers, employees, and the American public.

## The Future of the Postal Service

The *Plan* provides the necessary priorities and strategies for the Postal Service to be:

- More convenient and easy to use, with products and services that respond to customer needs and meet market requirements;
- A more effective communication and delivery channel by adding value to the mail through technology, with sufficient revenue generated by these improvements to continue to support the universal service network;
- A well-managed organization with high productivity levels and prudent financial management;
- One of the best places to work with a fully engaged workforce in a safe workplace;
- A leader in customer service and satisfaction, providing timely, reliable, and accurate delivery to every address at reasonable rates.

# ATTACHMENT E

January 26, 2009

KATHLEEN AINSWORTH
VICE PRESIDENT, RETAIL OPERATIONS

WALTER F. O'TORMEY
VICE PRESIDENT, ENGINEERING

SUBJECT: Audit Report – Retail Technology Strategy: Automated Postal Centers (Report Number DA-AR-09-004)

This report presents the results of our audit of the Postal Service's Automated Postal Centers (APCs) (Project Number 08YG029DA000). Our objectives were to identify the benefits of deploying APCs to non-Postal Service locations and assess the Postal Service's plans for APC deployment to such locations. See Appendix A for additional information about this audit.

## Conclusion

The APC Decision Analysis Report (DAR) states that the Postal Service could deploy APCs to retail space and other more convenient, less costly, non-Postal Service sites, and that reduced window clerk workhours at post offices resulting from customers' use of APCs should produce savings. Despite these initial expectations, the Postal Service has not reduced workhours as envisioned. APC program officials stated that the Postal Service recently relocated underperforming APCs to more advantageous Postal Service locations and they believe APC usage will increase. However, there is currently no clear plan that includes deployment of APCs to non-Postal Service locations and capital funding has not been approved for additional APCs.

While the U.S. Postal Service Office of Inspector General (OIG) recognizes the Postal Service's capital funding constraints, OIG blog results[1] indicate a desire to have APCs at non-Postal Service sites. The benefits of deploying or leasing APCs to more convenient non-Postal Service locations include the potential to reduce window clerk workhours, generate additional revenue, and enhance customer convenience. In addition, benchmark results show other entities have successfully used self-service kiosks to decrease costs and increase customer convenience. The Postal Service may be foregoing opportunities to realize the full benefits of self-service technologies by not fully incorporating self-service kiosks into the current retail technology strategy. See Appendix B for our detailed analysis of this topic.

[1] The blog was initiated in September 2008 as part of a new OIG program to facilitate an ongoing dialog on relevant issues affecting the Postal Service.

We recommend the Vice President, Retail Operations, in coordination with the Vice President, Engineering:

1. Develop a retail technology plan which includes a pilot deployment of Automated Postal Centers to non-Postal Service locations.

**Management's Comments**

Management disagreed with our conclusion that APCs have not reduced workhours. Management also disagreed with our recommendation to develop a plan to deploy APCs to non-Postal Service locations, stating they have already deployed them to such locations and/or unattended Postal Service sites. In addition, management stated they would consider placing APCs in additional non-Postal Service locations if funds become available for a purchase of additional machines. See Appendix C for management's comments in their entirety.

**Evaluation of Management's Comments**

While management correctly describes a recent 3-year trend (2005–2007) to support their statement that window clerk workhours declined at APC sites, they did not use the appropriate baseline for comparison. Our analysis appropriately compares window clerk workhours "before and after" APC deployment (see Chart 1). Fiscal year (FY) 2003 served as a baseline for our analysis because it was the period prior to APC deployment. Using this baseline, our comparison showed an immediate and substantial increase in window clerk workhours at APC sites after the Postal Service deployed the machines (FYs 2004 and 2005), and then a gradual decline; however, FY 2008 workhours were still nearly 12 percent greater than those used in FY 2003. Management's comments do not explain why window clerk workhours increased at APC sites after deployment while the number of window transactions decreased.

We believe our recommendation to deploy APCs to non-Postal Service locations is consistent with the Postal Service transformation plan's goal to place special emphasis on enhancing online and self-service capabilities to further reach out to customers where they live, work, and shop. We do not dispute that there are APCs placed in a few non-Postal Service locations that are capable of meeting targeted revenue goals. For example, we note that the APC revenue associated with a Las Vegas, Nevada grocery store was above the average of other APCs within the same locality. The intent of our recommendation was to emphasize the importance of a tactical plan and timeframes for capturing the transformation vision relating to self-service technologies on a larger scale. The current Postal Service strategy[2] is silent on positioning APC's in retail outlets. As such, we believe the Postal Service should reconsider our recommendation as it has the potential to help further modernize the customer experience while lowering Postal Service costs.

[2] *The Alternate Access Channels National Strategic Cookbook*, January 2009.

The OIG considers management's comments to the finding and recommendation non-responsive. However, we recognize Postal Service capital funding limitations, overall financial constraints, and current technology priorities. While we continue to believe our recommendation is worthwhile, we will not pursue audit resolution at this time and will continue to review technology plans, development, and funding priorities.

We appreciate the cooperation and courtesies provided by your staff during the audit. If you have any questions or need additional information, please contact Miguel Castillo, Director, Engineering, or me at (703) 248-2100.

E-Signed by Darrell E. Benjamin, Jr
VERIFY authenticity with Approvelt

Darrell E. Benjamin, Jr.
Deputy Assistant Inspector General
for Support Operations

Attachments

cc: Janet L. Webster
Dennis P. Yenke
Katherine S. Banks

# APPENDIX A: ADDITIONAL INFORMATION

## BACKGROUND

The Postal Service introduced APCs in 2004 and there are 2,491 in use today. APCs give customers a convenient alternative to counter services as most are located in post office lobbies and many provide basic services at any time of day or night, including weekends and holidays.

APCs can process many of the transactions that retail window personnel normally handle, freeing retail associates to focus on assisting customers with face-to-face transactions. For example, APCs can:

- Weigh and rate letters, flats, and parcels up to 70 pounds.
- Dispense variable rate postage in any denomination for Express, Priority, and First-Class Mail®; International Mail (under 1 lb.); and Parcel Post Mail or any selected special services.
- Provide Postal Service and mailing information, such as mailing options, different classes of mail, or special services.
- Print Express Mail forms and look up ZIP Codes.
- Provide the option to purchase Delivery Confirmation, Signature Confirmation, or Certified Services™; Insurance; or Return Receipt services.
- Accept debit and credit cards for payment.

The Vice President, Retail Operations, is responsible for providing tools and guidance that support the strategic direction in improving efficiency, increasing revenue, and decreasing costs. Specific responsibility for APCs falls under the Retail Service Network and Access Innovations. The Vice President, Engineering, defines and develops policies and plans for the lifecycle support of major Postal Service equipment and systems, including retail automation.

## OBJECTIVES, SCOPE, AND METHODOLOGY

Our objectives were to identify the benefits of deploying APCs to non-Postal Service retail locations and assess the Postal Service's plans for deployment to such locations. To accomplish our objectives we used the recently developed OIG blog[3] to gauge consumer interest in having APCs at retail and non-Postal Service locations. We also conducted meetings with Engineering and Retail officials to determine the reasons for not migrating APCs to non-Postal Service locations. In addition, we researched entities that use self-service technologies to establish benchmarks.

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[3] A website that displays in chronological order the postings by one or more individuals and usually has links to comments on specific postings.

We conducted this performance audit from August 2008 through January 2009 in accordance with generally accepted government auditing standards and included such tests of internal controls as we considered necessary under the circumstances. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. We discussed our observations and conclusions with management on December 15, 2008, and included their comments where appropriate.

## PRIOR AUDIT COVERAGE

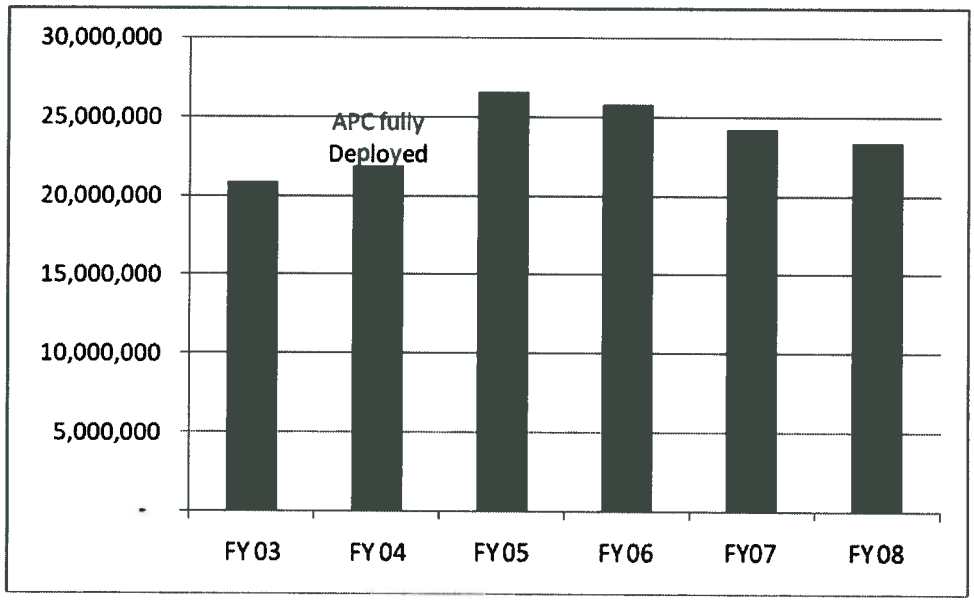
| Report Title | Report Number | Final Report Date | Monetary Impact | Report Results |
|---|---|---|---|---|
| *Deployment Strategy of Automated Postal Centers* | DR-AR-07-010 | June 7, 2007 | None | Analysis of FY 2006 actual transaction data for the best 3,000 Phase II APC candidate facilities indicated only about 50 to 100 of these facilities had sufficient APC-eligible transactions to potentially produce a cost savings. Purchasing 3,000 more APCs could result in a loss. |
| *Revenue Generation by Automated Postal Centers* | MS-AR-09-003 | November 7, 2008 | $1.67 mil | Management developed best practices for APCs, but had not implemented them consistently in all Postal Service districts. Effective implementation of best practices in the lowest performing 10 districts would result in approximately $1.67 million in funds put to better use over the next 2 years. |

## APPENDIX B: DETAILED ANALYSIS

### Window Clerk Workhours Increased

The benefits of migrating transactions to APCs include reduced window clerk workhours at post offices. Currently, 45 percent of all customer visits at the retail counter can be completed at an APC. However, as of October 2008, APCs were diverting only about 20 percent of eligible transactions from retail counters nationally – less than half of those possible. [redacted],[4] but, while window transactions decreased from FY 2004 to FY 2008, targeted workhours actually increased (see Chart 1).

**Chart 1 – Window Clerk Workhours at APC Sites**




[4] [redacted]

## Postal Service APC Migration Plans

The APC DAR states that the Postal Service could deploy APCs to retail space and other more convenient, less costly non-Postal Service sites. Furthermore, the *Strategic Transformation Plan 2006-2010* states that the Postal Service:

- Has a goal to double the percentage of retail transactions via alternate access channels to 40 percent by 2010.
- Places increasing awareness and use of APCs as a high priority.
- Will continue to place special emphasis on enhancing self-service capabilities to further reach out to customers where they live, work, and shop.
- Will pursue strategic alliances where partners can help speed development and/or reduce shared costs.

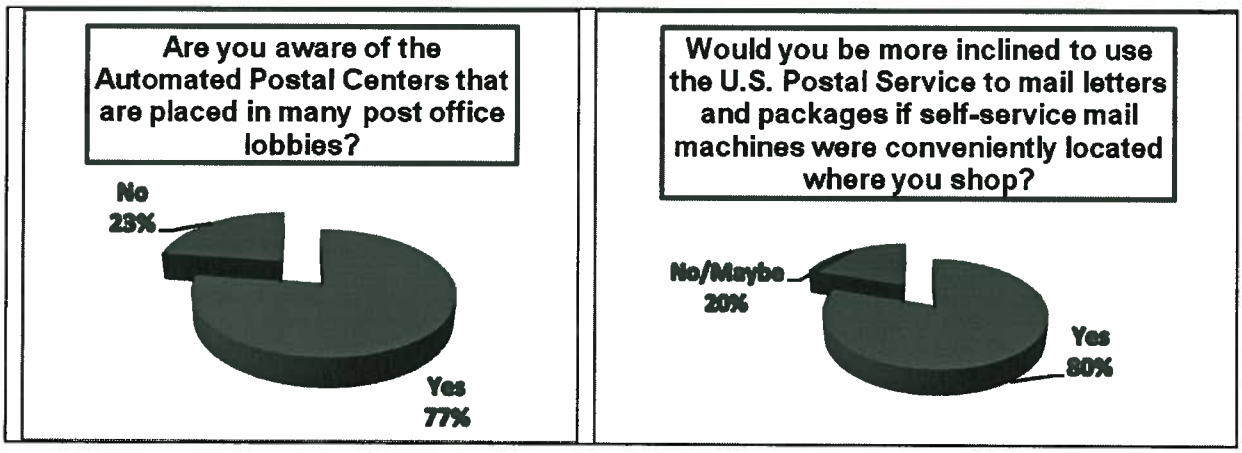
However, the Postal Service does not have a clear plan that includes deploying APCs to non-Postal Service locations. The benefits of deploying or leasing APCs to more convenient non-Postal Service locations include the potential to reduce window clerk workhours, generate additional revenue, and enhance customer convenience. APCs also complement internet technologies such as Click–N–Ship and, as discussed previously, OIG blog results indicate that customers desire to have APCs at non-Postal Service locations. Despite these potential benefits, the Postal Service plans to keep APCs primarily in post office lobbies. According to APC program officials, management recently relocated under-performing APCs to more desirable locations; therefore they believe APC usage will increase. In addition, funding is currently unavailable for additional APCs.

While we recognize the Postal Service is piloting its retail storefront in Schaumberg, Illinois, the Postal Service has not fully incorporated self-service technologies such as APCs into its retail technology plans. The Postal Service may be foregoing opportunities to realize the full benefits of self-service technologies by not fully incorporating self-service kiosks into those plans.

## Blog Results

Our blog results indicate that some customers would prefer that APCs be located at convenient non-Postal Service locations. Specifically, 117 of 152 (77 percent) of the blog respondents were aware of APCs and 120 respondents (80 percent) would be more inclined to use an APC if it were conveniently located where they shop.

**Illustration 1 – Blog Results**




Excerpts of blog comments highlighting favorable conditions for APCs include:

- *APCs should be in all offices and any place people gather to buy items.*
- *I think in major malls/shopping centers these APCs should be the norm.*
- *I think these machines are a great service. In fact they should be placed in every large apartment complex throughout the country for those who are at work and cannot necessarily get to the post office.*
- *Installing APCs in grocery stores would eliminate the need for special trips.*
- *They should be in any fairly safe 24-hour store, Wal-Mart, grocery stores, drug stores, shopping malls, and convenience stores.*
- *I think we would be crazy not to put APCs all over the place like ATMs. The potential for revenue is there. Someone walking by would say, 'oh yeah, I need some stamps.' There are probably more people like me who don't want to stand in long lines.*
- *I would use an APC if it was in a convenient place. This would help me avoid using leave from work to get to the post office before closing.*

## Benchmarking

We analyzed five companies that have successfully used or plan to use self-service kiosks. Generally, our benchmarks indicate that self-service machines decreased costs and increased convenience for customers as noted below.

- United Airlines' use of self-service kiosks diverted approximately 63 percent of its customers from the counter to the machine and significantly reduced the need for counter clerks. Specifically, over a 2-year period, management eliminated 25

percent of their vacant positions. Self-service kiosks complement internet technologies by enhancing customer service while lowering counter costs.

- Air Canada announced in February 2007 that it was realizing significant savings through the use of self-service kiosks. The company stated that it costs 16 cents to check in a traveler through a kiosk, versus $3 through a staffed counter. Self-service kiosks complement internet technologies to enhance customer service while lowering counter costs.

- Pitney Bowes, Inc. has developed a self-service kiosk which allows Postal Service customers to perform a wide range of tasks, permitting retail counter employees to focus their attention on those customers who have special or hard-to-meet needs more efficiently. Kiosk locations include 50 - 60 corporate and college campuses and Postal Service retail outlets in several countries.

- France's national postal operator, La Poste, signed a contract in October 2008 to lease 50 stand-alone kiosks and they hope to expand the number of kiosks over time. Pitney Bowes, Inc. has established leasing agreements with firms wanting kiosks to provide convenient mailing options for customers.

- Best Buy is providing express consumer convenience by installing a dozen freestanding, self-service vending machines through eight specific airports across the country.

# APPENDIX C: MANAGEMENT'S COMMENTS

UNITED STATES POSTAL SERVICE

January 15, 2009

LUCINE M. WILLIS

SUBJECT: Transmittal of Draft Audit Report – Retail Technology Strategy: Automated Postal Centers (Report Number DA-AR-09-DRAFT)

This letter is in response to Transmittal of Draft Audit Report – Retail Technology Strategy: Automated Postal Centers (Report Number DA-AR-09-DRAFT) dated December 31, 2008. We disagree with the conclusions and the recommended actions contained in this report.

**Conclusion Paragraph**

Conclusion paragraph, fourth line states:
"Despite these initial expectations, the Postal Service has not reduced workhours as envisioned."

**Management Response:**

This is not an accurate statement. As a result of the deployment of the Automated Postal Centers (APC) and in accordance with the APC DAR, District workhour budgets were reduced by 2.7M hours over the three year period of 2005 – 2007.

**Recommendation 1:**

Significant.
We recommend the Vice President, Retail Operations in conjunction with the Vice President, Engineering, develop a retail technology plan, which includes a pilot deployment of APCs to non-Postal Service locations.

**Management Response:**

Management does not agree with this recommendation as our retail technology plan already includes APCs in non-postal locations.

There are APCs currently deployed in non-postal and/or unattended postal sites in the Great Lakes Area, the New York Metro Area, and the Western Area. The existing APCs have been deployed to locations that are capable of meeting or exceeding their targeted revenue goals.

At this time, funds have not been authorized for a purchase of additional APCs. In the event funds become available, we will consider placement of APCs in non-postal locations based on quantitative and qualitative data.

There are no Freedom of Information Act (FOIA) issues relative to these concerns.

Kathy Ainsworth
Vice President, Retail Operations

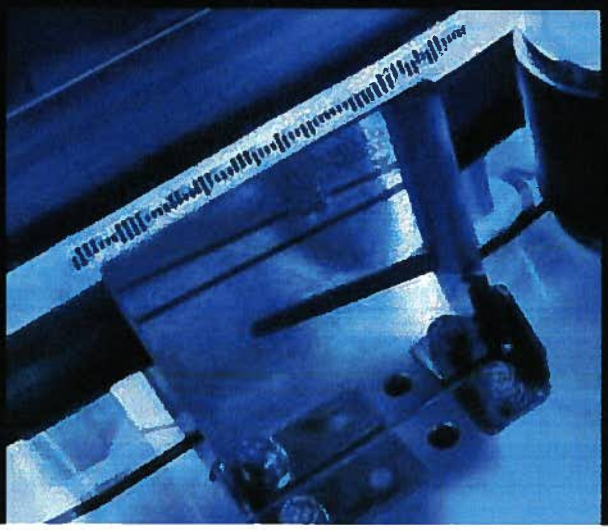
Walter F. O'Tormey
Vice President, Engineering

cc: Kathy Banks
Manager, Corporate Audit & Response Management

# ATTACHMENT F

# Ensuring a Viable Postal Service for America

## An Action Plan for the Future



UNITED STATES POSTAL SERVICE

# EXECUTIVE SUMMARY

For over 200 years, the Postal Service has fulfilled its mission to deliver trusted, affordable service to the nation. Its business model worked well because mail volume increased steadily as the nation grew. In recent years, however, as customer preferences have rapidly evolved and new technology has changed how Americans communicate and transact business, the model has faltered. Mail volume, instead of increasing, is declining dramatically, even as the cost of delivering mail to an expanding number of addresses continues to grow. As a result, the Postal Service's ongoing ability to finance universal service is at great risk.

In the face of these challenges, the Postal Service has responded aggressively, saving over $1 billion every year since 2001, including $6.1 billion savings in 2009 alone. Yet these savings are not sufficient to counter underlying shifts in the business of mail. A loss of more than $7 billion is projected for 2010, and with current trends expected to worsen over the decade, the Postal Service will be pushed more deeply into crisis. Without fundamental change, cumulative losses could reach more than $238 billion by 2020.

To avoid potential insolvency, the Postal Service has developed an ambitious but achievable plan, taking steps allowed under current law to reduce the projected gap by $123 billion. These savings would be unprecedented, even by the standards set over the last several years. And even if its plan was to succeed in every action that present legislation allows, the Postal Service would still face unsustainable losses of at least $115 billion by 2020. This remaining gap can be closed, and the Postal Service can continue to fulfill its mission at no cost to American taxpayers, but only with additional flexibility that would have to come through legislative changes. They include:

1. **Retiree Health Benefits Prefunding.** Restructure retiree health benefits payments to "pay-as-you-go," comparable to what is used by the rest of government and the private sector. This equates to an average of $5.6 billion in cash flow per year through 2016. Address overpayments to the Postal Service's Civil Service Retirement System pension fund.

2. **Delivery Frequency.** Adjust delivery days to better reflect current mail volumes and customer usage. Survey data show that the public favors 5-day delivery over using taxpayer funds and other alternatives.

3. **Expand Access.** Modernize customer access by providing services where the customers are. Increase and enhance customer access through partnerships, kiosks, and improved online offerings, while reducing costs.

4. **Workforce.** Establish a more flexible workforce that is better-positioned to respond to changing demand patterns as over 300,000 employees become eligible to retire in the coming decade.

5. **Pricing.** Ensure that prices of Market Dominant products can be based on the demand for each individual product and its costs, rather than capping prices for every class at the rate of inflation. In addition, pursue a moderate exigent price increase effective in 2011.

6. **Expand Products and Services.** Permit the Postal Service to evaluate and introduce more new products consistent with its mission, allowing it to better respond to changing customer needs.

7. **Oversight.** Reinforce these changes with more clearly defined, appropriate, agile oversight roles and more streamlined processes.

Without question, the current situation is a crisis for the Postal Service, the mailing industry, and indeed for all postal stakeholders. It is also an historic opportunity — providing a chance to make positive and very practical changes that not only meet the present crisis, but also lay the foundation for a leaner, more market-responsive Postal Service that can thrive well into the future.

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## INTRODUCTION

Since Benjamin Franklin was appointed the first Postmaster General, the agency known today as the United States Postal Service has fulfilled its mission to deliver trusted, affordable service to the American people. From the Pony Express to today's fast-changing digital world, the Postal Service has dramatically improved service and efficiency, ensuring that consumers and businesses get world-class mail services at reasonable prices.

The Postal Service is the world's most efficient post. A First-Class stamp costs just 44 cents, while other major posts charge an average of 78 cents. Customer satisfaction and service levels have reached the highest levels ever reported. For five years in a row, the Postal Service has also been voted the "Most Trusted Government Agency" for protecting customer privacy, and rates in the Top 10 of all public and private entities.

The Postal Service's business model dates to 1970, when it became an independent agency of the Executive Branch. In contrast to the heavily subsidized department it replaced, the Postal Service was designed to operate like a business, financing its operations from the sale of its products and services.

This self-financing model worked well for many years as mail volume grew with the nation. In recent years, however, volume has declined, and it continues to fall as technology rapidly reshapes the market and changes how Americans communicate and conduct business. The recent economic downturn accelerated this trend as businesses cut expenses and reduced their investment in mail.

For most businesses, there is nothing exceptional in this; they must continually adapt to technology and market changes. Unlike most businesses, however, the Postal Service is attempting to meet its 21st century challenges with a business model suited to the last century — one that does not acknowledge that a fundamental change has taken place.

*Mail is big business. The Postal Service is at the core of the trillion dollar mailing industry that employs more than 8 million people.*

Prudent management required that the Postal Service make substantial adjustments to compensate for the decline in volume and revenue. To the extent that current law allows, it has done just that, saving over $1 billion every year since 2001, including $6.1 billion in 2009 alone. Unfortunately, its ability to make adjustments is limited in the areas where costs are highest — wages and benefits, its network, and the interpretation of the Universal Service Obligation.

In 2006, Congress passed new legislation that significantly modified the postal business model. It provided limited pricing freedom in Competitive Products but offered little flexibility for the remainder of the business. The law also limited the Postal Service's ability to create new products and seek new sources of revenue. It capped prices at the Consumer Price Index by class for Market Dominant products, which is 88 percent of revenue. And without providing additional flexibility to control its costs, the law added a massive new obligation: to pre-pay future retiree heath benefits on a schedule that consumes 10 percent of revenue every year. These changes in the law were made just as volume had begun to fall and the recession began to take hold.

The Postal Service responded with comprehensive actions to transform operations. It increased the use of automation and substantially reduced its workforce, all while improving service. Despite these improvements, the Postal

### Understanding the Universal Service Obligation

The Universal Service Obligation ensures that every citizen can send and receive mail at affordable prices. This entails maintaining a delivery network that reaches all addressees, and providing customers with ready access to postal services, a range of products, uniform prices and mail security.

Service began to suffer significant net losses in 2007 primarily due to a legislatively imposed requirement to prefund future retiree health benefits.

This paper explains the current crisis and presents an action plan to meet it. The plan has two parts: the first includes aggressive actions that the Postal Service commits to making within existing law; the second describes additional actions, most requiring changes in law, that are vital to restore financial stability.

This plan is the product of more than a year of dialogue between the Postal Service and members of Congress, the Administration, the business community, postal employees, and the general public. To gain a fresh, objective perspective, the Postal Service solicited papers from a number of independent sources, and enlisted three of the world's most experienced and highly regarded management consulting organizations — Accenture, The Boston Consulting Group, and McKinsey & Company. All three were given free rein to talk with employees, customers, and anyone else whose opinions they considered relevant.[1]

## I. AN UNSUSTAINABLE BUSINESS MODEL

Since 2006, the Postal Service has faced the financial strain of steep declines in volume and revenue, combined with increases in network costs, wages and benefits, and new legal requirements. It began to incur large net losses in 2007 (Exhibit 1).

### Volume and revenue have fallen sharply

From 2006 to 2009, volume declined 17 percent, from 213 billion to 177 billion pieces, while prices remained capped at the rate of inflation — triggering a loss of

In 2003, the President's Commission on the U.S. Postal Service said, "Now is the time to...modernize the Postal Service to not only preserve its future, but also to ensure its service to all Americans." This action plan is fairly consistent with the President's Commission's findings.

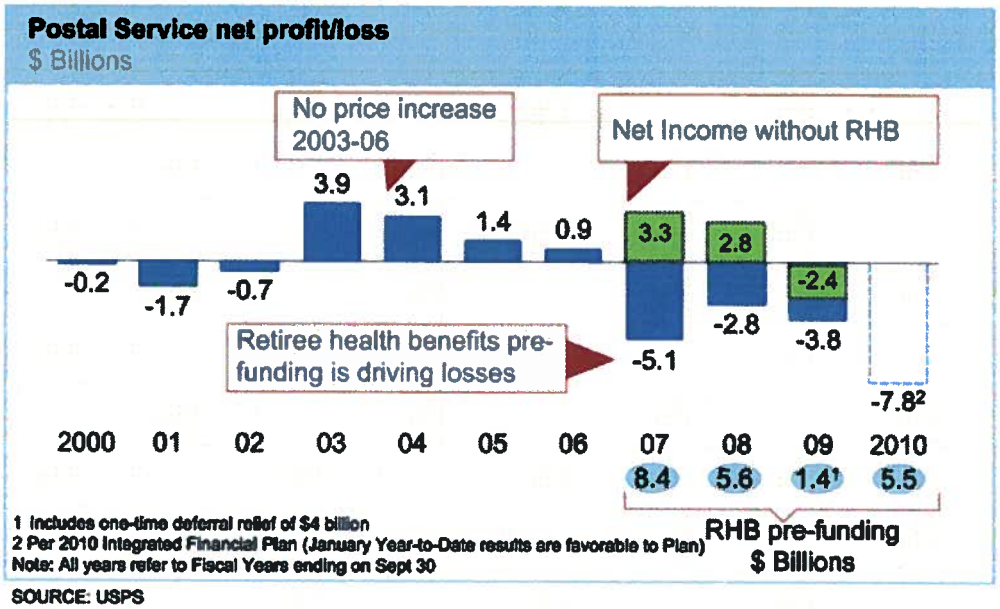
### Postal Service operations are not funded by taxpayers

Throughout most of the nation's history, its postal system was administered by the Post Office Department, a cabinet level agency. By the late 1960s, however, years of financial neglect and fragmented control had impaired the ability of the department to respond to changing conditions and increasing mail volumes.

Convinced that fundamental change was necessary, in 1970 Congress enacted the Postal Reorganization Act. This sweeping legislation created the Postal Service as an independent establishment of the Executive Branch and directed the new organization to bring modern business methods and practices to the national mail system. For 36 years, the Postal Service's business model worked very well for customers, employees, and the nation. The Postal Service was able to charge affordable prices and use revenues from its products to provide mail service to all areas of the country, charging customers the same prices regardless of delivery costs. It received no taxpayer subsidies to fund its operations.

The Postal Accountability and Enhancement Act of 2006 (the Postal Act of 2006) split postal products into Competitive and Market Dominant. At the same time, the Act put the bulk of revenue-generating products under a stringent price cap and gave the Postal Service limited ability to control its costs or increase revenue. The viability of the Postal Service under the Postal Act of 2006 relied on the underlying presumption that mail volume would continue to grow. It hasn't.

**Exhibit 1: USPS is experiencing unprecedented losses**



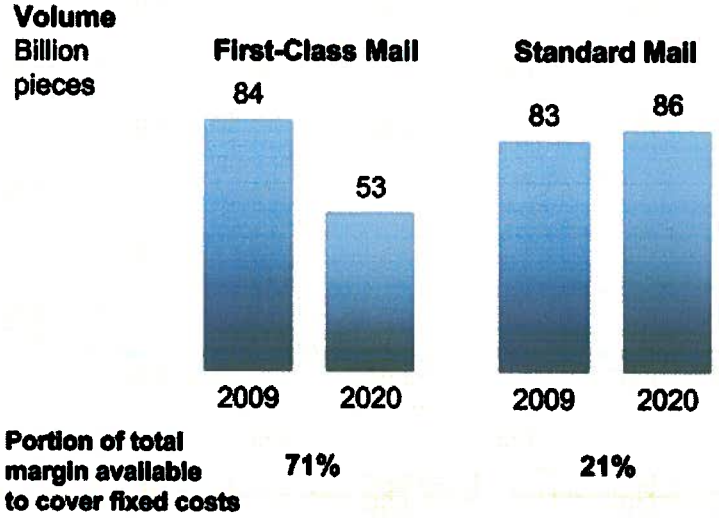

SOURCE: USPS

$15.8 billion in 2009 revenues.[2] First-Class Mail saw the largest volume decline, about 15 percent. This had a disproportionate effect on the bottom line since First-Class Mail provides the majority of contribution (Exhibit 2). In total, the volume decline outpaced even the most pessimistic forecasts.

While the recession accelerated the volume decline, its primary cause is a fundamental and permanent change in mail use by households and businesses. Hardcopy communication of all types continues to shift to digital alternatives. More people are paying bills and transacting business online. Advertisers are switching from print

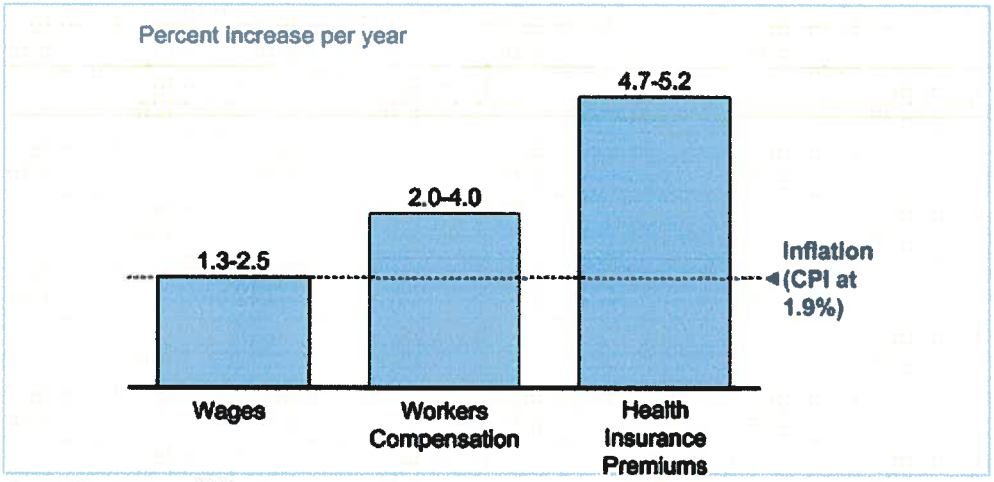
The volume of high-contribution First-Class Mail has declined sharply, and is expected to continue to fall.

**Exhibit 2: Changes in volume and contribution of the two largest mail classes**



Workforce costs will rise at a rate greater than prices, which are capped at inflation.

**Exhibit 3: Workforce costs are projected to rise between 2010 and 2020**




SOURCE: McKinsey analysis, Global Insight

to Internet and mobile channels. And while online purchases have increased the volume of packages, this part of the Postal Service's revenue stream is not large enough to offset overall mail volume trends.

## New costs and capped prices

A key driver of the cost of delivering mail is the obligation to deliver to virtually every mailing address, regardless of volume, 6 days per week. Fulfilling this duty requires an extensive network of Post Offices, processing plants, vehicles, and delivery employees. These costs are largely fixed, so they increase with the size of the network, which has grown by an average of 1.4 million new addresses every year. As a result of the growth in fixed costs and increases in other expenses, the total cost per piece of mail rose from 34 to 41 cents since 2006.

The Postal Act of 2006 was passed before volume had begun to fall sharply. It had the unintended consequence of constraining the Postal Service's ability to respond to the challenges in a financially responsible manner. The Act introduced two crucial restrictions.

First, it added a major new cost. It compelled the Postal Service to set aside money over 10 years to cover future retiree health benefits. This prefunding mandate requires that the Postal Service set aside, on average, $5.6 billion per year through 2016.[3] This has the effect of increasing total costs in this period by 9 percent a year. Prefunding is unique to the Postal Service within the public sector, and is not required in the private sector.

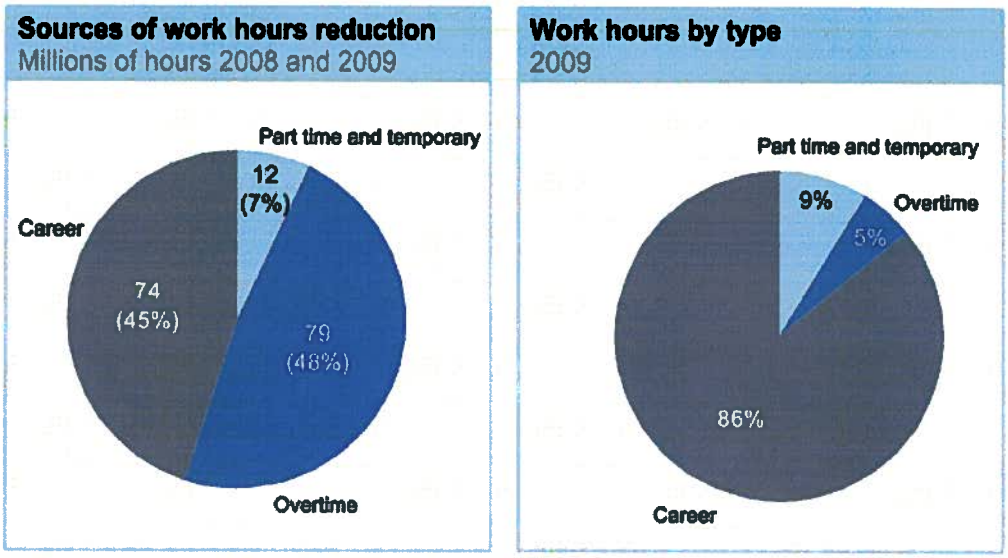
Second, the Act capped price increases at the Consumer Price Index (CPI) for each class of mail where the Postal Service is perceived to dominate a market (e.g., First-Class Mail).[4] Looking forward, the losses due to volume declines and retiree health benefits prepayments cannot be made up with increased prices (Exhibit 3).

## The Postal Service aggressively cut costs while improving service

The Postal Service responded to the volume declines by dynamically reducing work hours and improving internal operations. This reduced 2009 costs by $6.1 billion. In 2009, natural attrition and early retirement offers allowed the Postal Service to reduce the workforce by the equivalent of 65,000 full-time employees, or approximately 10 percent (Exhibit 4). This was the largest one-year reduction in postal history. The Postal Service also froze hiring and executive pay.

There is limited remaining opportunity to reduce part-time, temporary, and overtime work hours.

**Exhibit 4: Work hour reductions**




SOURCE: FY 09 10-K; 2008 and 2009 National Payroll Hour Summary Report

Operations were streamlined consistent with this smaller workforce. The Postal Service consolidated delivery routes, reorganized portions of its processing network, and renegotiated over 500 supplier contracts to obtain more favorable terms.

To boost revenue, the Postal Service enhanced programs such as Parcel Select, which provides last-mile delivery for FedEx and UPS, among others. It launched an advertising campaign ("If it fits, it ships") for Flat Rate Priority Mail, which is priced on the size of the box, not the weight or zone, making the shipping process more convenient. The Postal Service also introduced innovative new programs such as the "Summer Sale," which boosted volumes and retained customers by offering a 30 percent discount for incremental Standard Mail (advertising mail) volume. Additionally, it invested in expanding customer access through improvements to its website and partnerships with retailers.

## II. A RAPIDLY WORSENING CRISIS

Even with all these actions, the Postal Service has, in recent years, been unable to stem broader financial losses. In 2007, it began to suffer net losses, which are expected to exceed $7 billion in 2010. The Postal Service is now in the position of having to borrow from the Treasury to meet its obligations to the Treasury. Its future borrowing capacity is limited by law at $15 billion, a level it could reach in early FY 2011.

Industry experts confirm that the marketplace trends challenging the Postal Service in recent years are expected to accelerate. The organization will continue to face declining volume, stagnant revenue, large fixed costs, and rising workforce costs. Without additional action to address these trends, the Postal Service would face annual losses as great as $33 billion by 2020 (Exhibit 5).

## Volumes projected to steadily contract, and revenues to stagnate

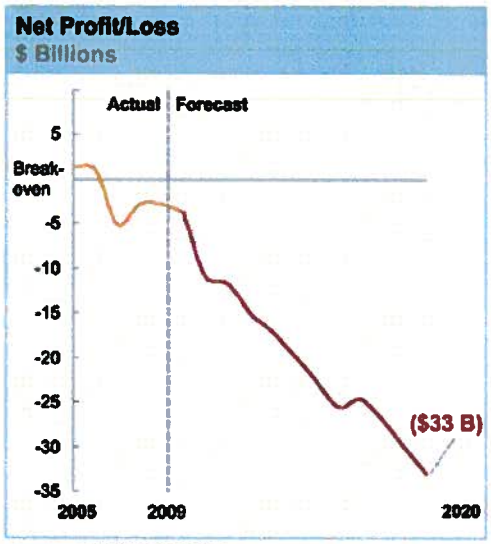
The recession is not only reducing volume due to declining business activity. It is also pushing businesses to find less expensive methods of communicating with their customers. In coming years, this will speed up the more fundamental underlying trends that are motivating customers to switch to electronic alternatives.

Total volume — which fell 17 percent from a high of 213 billion pieces in 2006, to 177 billion pieces in 2009 — is expected to drop an additional 15 percent by 2020, to a level of 150 billion pieces (Exhibit 6).[5]

In real terms, revenue will decline significantly over the next decade. In nominal terms, overall Postal Service revenues will be largely stagnant, rising from $68.1 billion in 2009, to just $69.3 billion by 2020. As a result, assuming prices by class remain capped at inflation, revenues per address will have fallen from a daily average of $1.50 in 2009 to $1.41 in 2020.[6]

**First-Class Mail.** Even as the economy rebounds, First-Class Mail volume will not return to past levels; it is expected to fall an additional 37 percent by 2020. Invoicing and payments will continue to move online, and businesses will continue to expand their use of electronic channels as a low-cost means to process payments and manage customer relationships.

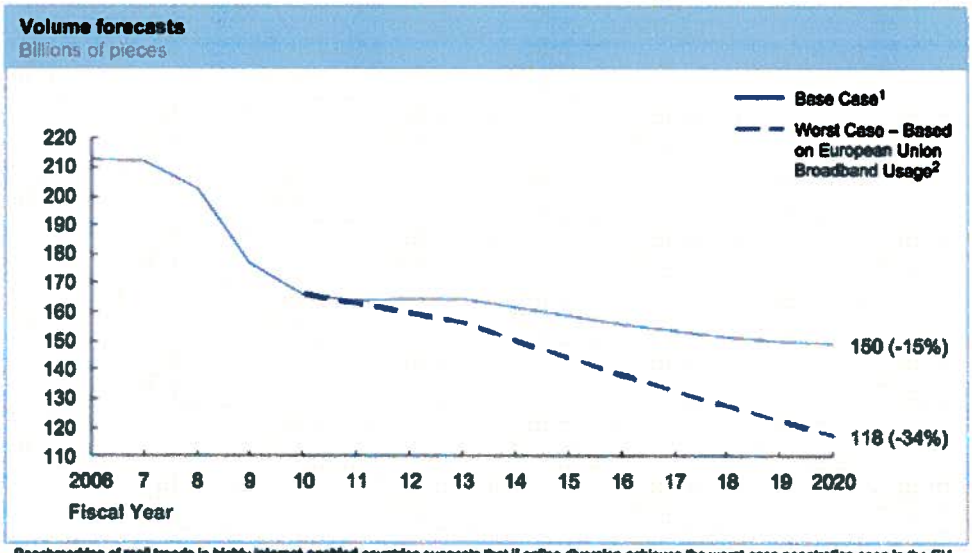
**Exhibit 5: Projected net loss in 2020**




SOURCE: McKinsey analysis

Without any additional action, negative forces result in increasingly large annual deficits, culminating in a $33B annual loss in 2020. Cumulative losses between now and 2020 would exceed $238B.

**Exhibit 6: Volume forecasts to 2020**




Benchmarking of mail trends in highly internet-enabled countries suggests that if online diversion achieves the worst-case penetration seen in the EU, the 2020 projection will fall below 120B pieces.
1 Baseline: Excludes all management actions not currently in the Postal Service budget beyond 2009. This assumes no major economic or other disruptions and no change in the postal oversight framework.
2 Worst case: Based in part on online diversion trends in highly internet-enabled European Union countries.
SOURCE: BCG analysis

The volume forecasts include high levels of uncertainty, although trends point downward.

This creates the perfect storm, eroding mail's primary role as an invoice and bill payment medium. The consumer shift online will result in a projected 1.1 billion fewer letters per year over the next decade, while businesses are expected to mail 10 billion fewer bills by 2020. Total bill and invoice mail volume is expected to fall by 44 percent, and the mix of mail is expected to shift away from First-Class Mail to less expensive Standard Mail.

**Advertising mail.** The volume of advertising mail has fallen rapidly in the recession along with most other advertising media. A large share of advertising investment has moved to Internet and mobile channels. One top marketing agency observed companies moving one-third of direct mail acquisition spending online. Consequently, the segment of the Postal Service's business that historically grew steadily with Gross Domestic Product (GDP) is expected to remain flat for the foreseeable future.

**Packages.** This segment is likely to experience some growth, but at a rate of only 3 percent per year. Letter volume declines will far outweigh package growth in both pieces and revenue.

## Costs will continue rising

Today, fulfilling the Universal Service Obligation involves more than 36,000 Post Offices, stations, and branches. Delivering mail 6 days a week involves 220,000 vehicles, $2.6 billion in air transportation, and 600 processing facilities.

As volume continues to decline and the number of addresses continues to increase, the cost to deliver each piece of mail will keep rising while revenue per delivery point falls. Each year through 2020, volume is expected to decline by 1.5 percent on average while approximately 1.2 million delivery points are added.

Maintaining the Postal Service retail network will be increasingly costly. The average Post Office is far more expensive to operate than other means of serving customers. The average Post Office transaction costs 23 cents per dollar of revenue, while the average transaction at a contract postal unit costs just 13 cents (Exhibit 7). In the past, Post Offices generated almost all postal retail revenue. Today, however, 29 percent is generated through *usps.com* and other alternative channels. Post Offices recorded

Given First-Class Mail trends, retail revenues are expected to fall another 40 percent by 2020.

**Exhibit 7: Channels for accessing postage & mailing packages**

| Outlet Type | Average Cost per Dollar of Retail Revenue | Convenience (Hours of operation) |
|---|---|---|
| Average Post Office[1] (Postage & Packages Only) | $0.23 | 9am – 5pm, Monday – Friday, limited weekend |
| Contract postal unit | $0.13 | Avg. 7am—9pm, Monday – Sunday |
| Online Postage (e.g. Click-N-Ship, PC Postage, eBay) | $0.08 - $0.12 | 24 / 7 |
| Kiosk (automated, self-service) | $0.12 | 24 / 7 |
| Stamps by mail, phone, Internet | $0.08 | 24 / 7 |
| Retail partners | $0.02 - $0.07 | Avg. 7am—9pm, Monday – Sunday |

1 Average cost for all retail transactions at a Post Office is $0.31-$0.39 per dollar of retail revenue.
SOURCE: USPS EDW system

117 million fewer transactions in 2009 than in 2008, adding to the network's overcapacity.

Despite this excess capacity, under current law Post Offices cannot be closed solely for economic reasons.[7] Yet by 2020, with retail revenues predicted to fall by another 40 percent, even more Post Offices will be pushed into the red.

Wages and benefits account for 80 percent of Postal Service costs, and work hours will also become more costly due to rising benefits costs. Total workforce costs are expected to increase from $56.5 billion in 2009 to $77.2 billion in 2020.[8] Workers' compensation is projected to rise by 2 to 4 percent, health insurance premiums by 4.7 to 5.2 percent, and retiree health benefits costs by 11.8 percent. Health care in particular will grow at a pace well above inflation-capped price increases. While the Postal Service has collaborated with its unions to structure reasonable compensation options, federal statutes hamper its ability to craft a market-based benefits package.[9]

Finally, the accelerated schedule requiring prefunding of retiree health benefits over the first 10 years of the 50-year liability will consume $5.5 billion to $5.8 billion per year through 2016. While these obligations will fall to $2.6 billion to $2.7 billion per year from 2017 to 2020, total funding for retiree health benefits will continue to exceed 10 percent of gross revenues through 2020.

## III. ACTIONS WITHIN MANAGEMENT CONTROL

### The Postal Service will work within current law to close part of the budget gap

The Postal Service evaluated various possible actions for their feasibility and impact on projected losses. The analysis identified four areas with the greatest potential to generate additional revenue and reduce costs under current law. By 2020, these actions are expected to reduce annual losses by $18 billion. Cumulatively, they will narrow the projected $238 billion financial gap by $123 billion. The four areas include product and service actions, productivity improvements, workforce flexibility improvements, and purchasing savings (Exhibit 8).

**Exhibit 8: USPS will take a series of actions to save $18 Billion by 2020**

**Actions within management control:**

| | Net profit benefit in 2020 |
|---|---|
| 1 Product and service actions | ~$2B |
| 2 Productivity improvements | ~$10B |
| 3 Workforce flexibility improvements | ~$0.5B |
| 4 Purchasing savings | ~$0.5B |
| Avoided interest due to reduced debt | ~$5B |
| Total | ~$18B |

As a result of collaboration between management and union leadership, the Postal Service has 200,000 fewer career employees compared to 2000, with the reductions achieved through attrition.

**Product and service actions.** The Postal Service plans to expand products and services across targeted mail and package segments to increase profits by $2 billion by 2020. For example, it will work to increase direct mail use among small and medium-sized businesses, and to increase volumes in both First-Class Mail and advertising mail through targeted promotions. It will continue to leverage its last-mile network to deliver packages to all households, forming partnerships with others serving the growing e-commerce industry. It will also continue to grow other retail services, such as passports and Post Office Box rentals.

**Improving productivity.** The Postal Service will continue to cut costs and capture additional productivity savings. Planned actions include further streamlining of plant operations, optimizing delivery routes, providing customer service through the most cost-effective channels, and consolidating administrative functions. Targeted efficiency enhancements will reduce costs by approximately $10 billion in 2020.

**Workforce flexibility improvements.** Continued attrition due to retirements will provide opportunities to establish a more flexible workforce better aligned with changing customer demand. Over the next 10 years, over 300,000 employees — more than half the current workforce — will be eligible to retire. This will provide an opportunity to make the workforce even more efficient by increasing use of flexible and part-time employees.

**Purchasing savings.** The Postal Service has additional opportunities to trim resource costs in several areas. For example, it will lower transportation costs by using fewer trips at fuller truck-load levels. It will also continue to negotiate favorable contracts and improve vendor and process management.

Eliminating the Retiree Health Benefits prefunding requirement would cover only part of the growing financial gap; other changes would still be necessary.

In each of these four areas, accomplishing improvements will be exceedingly challenging. For example, the Postal Service has achieved 91 percent automated letter processing, the highest in the world. More than 78 percent of volume is already handled through workshare programs, including presort, destination entry, and automation-compatible mail preparation. In addition, roughly 55 percent of the past savings in work hours were due to reductions in overtime and the non-career workforce. Further opportunity to significantly reduce hours in these areas is very limited.

## IV. A VIABLE POSTAL SERVICE: THE PLAN TO GET THERE

The Postal Service is committed to providing universal service to the American people, covering all costs and paying all debts with postal revenue. However, even if it achieves the savings in its management plan, the Postal Service would still face an annual loss of $15 billion in 2020 and cumulative losses of $115 between now and then (Exhibit 9). Further, there is considerable risk that the projected losses could be far greater. And while projections indicate that volumes are likely to fall to 150 billion pieces, alternate scenarios suggest that volumes could sink even lower.

Clearly, aggressive steps are required. That is why the Postal Service is seeking the flexibility to pursue additional opportunities in seven critical areas: 1) retiree health benefits prefunding; 2) delivery frequency; 3) access to services; 4) workforce; 5) pricing; 6) products, and 7) oversight (Exhibit 10).

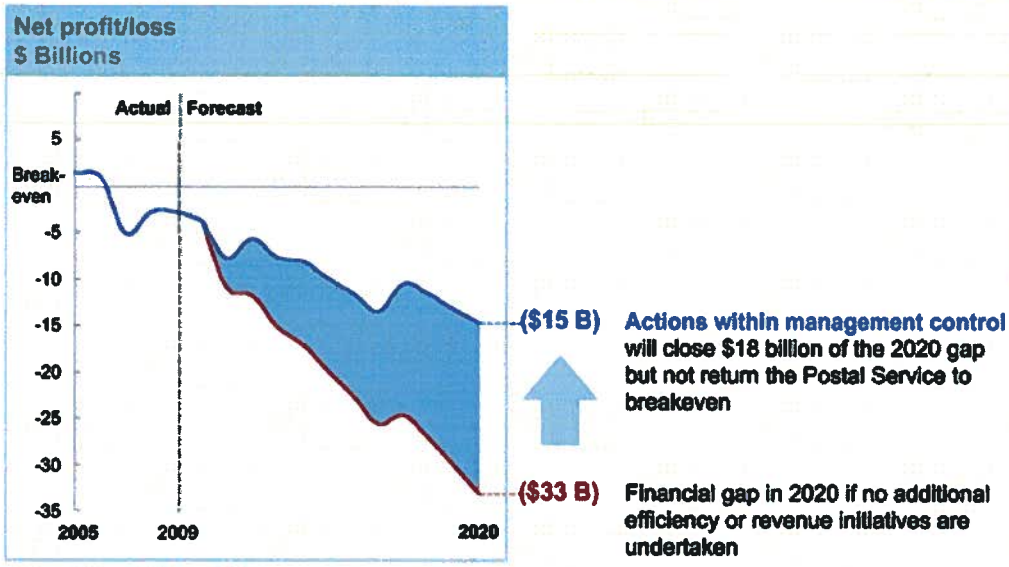
### 1. Retiree health benefits prefunding

The current retiree health benefits prefunding requirement has a significant impact on postal losses. The Postal Act of 2006 mandated a prefunding schedule of $5.5 billion to $5.8 billion per year through 2016. Congress must approve any future changes to that schedule, as it did in 2009.

The Postal Service seeks to restructure funding in a way that upholds its obligation to current and former employees and does not constrain cash flow during periods of volume decline. To do this, the Postal Service seeks

This crisis provides an historic opportunity to make changes that will allow the Postal Service to succeed as an independent agency of the Executive Branch. Its business model can work if it is recalibrated to 21st century realities.

## Exhibit 9: The financial impact of planned management actions




SOURCE: McKinsey analysis

to shift to a "pay-as-you-go" system, paying premiums as they are billed. Other federal agencies and most private sector companies use such a system.

In addition, the Postal Service Inspector General recently determined that the Postal Service overpaid, by nearly $75 billion, its contributions to the Civil Service Retirement System Fund (CSRS). The Postal Service will ask Congress to transfer this $75 billion to the Retiree Health Benefits Trust Fund. When it is added to the Fund's existing $35 billion balance, the Postal Service's retiree health benefits will be fully or nearly fully funded. As much as $50 billion can be saved over the next 10 years if the Postal Service does not have to prefund retiree health benefits.

## Exhibit 10: Postal Service of the future

Today
Limited ability to respond to market changes

Tomorrow
Flexibility to respond quickly to evolving market

| | From | To |
|---|---|---|
| Retiree health benefits | Pre-funded retiree health benefits requirement | "Pay-as-you-go" retiree health benefits in line with other government institutions |
| Delivery frequency | Mandated 6 day delivery regardless of changing volume | Flexibility to adjust delivery frequency to match volume and changing customer needs |
| Access | Primarily 9am-5pm brick-and-mortar Post Offices | Expanded access through an enhanced online presence, partnerships, and kiosks |
| Workforce | Limited flexibility to adapt to market and technology changes | Flexibility to capture natural attrition to match changing demand |
| Pricing | Strict inflation-based price caps by class | Flexible pricing reflecting market dynamics |
| Products | Restricted to postal products | Flexibility to introduce additional products consistent with broader mission |
| Oversight | Multiple bodies with overlapping roles and responsibilities and lengthy processes | Streamlined approach to oversight |

## 2. Delivery frequency

To adapt to changing mail volumes and consumer needs, the Postal Service must have the authority to reassess and adjust the frequency of delivery. A recent Gallup survey showed that two-thirds of Americans would rather have delivery days reduced than have increases in postage or have the government subsidize the Postal Service's losses with taxpayer funds (Exhibit 11).[10]

The Postal Service would move to a 5-day per week schedule if given the legislative changes required to adjust delivery frequency, thus eliminating delivery on Saturday, the lowest volume day. This would boost 2010 daily delivery volumes per address to 2008 levels. This would also help close a substantial portion of the net income gap, yielding annual savings (after initial implementation) of approximately $3 billion in 2009 dollars.

## 3. Access

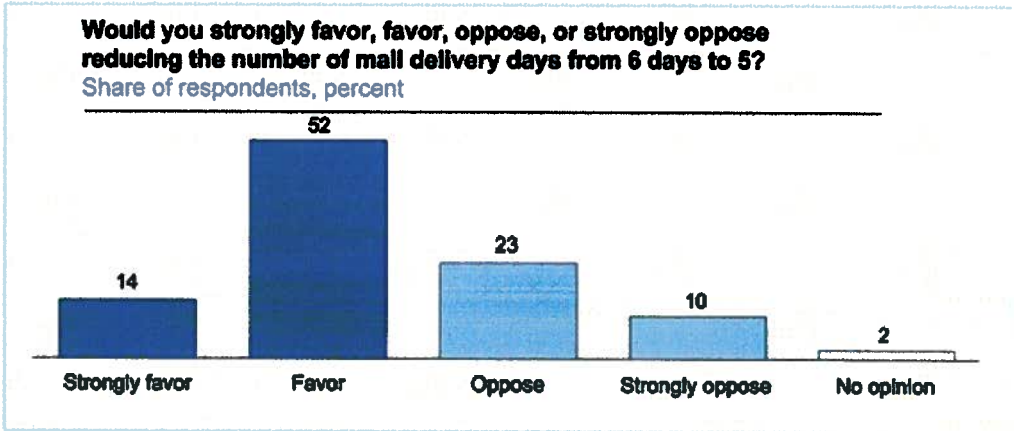
As consumer behaviors and needs change, so must the Postal Service. It must better align its retail network and the access it provides, investing in new options that improve service while lowering costs. Access will be expanded by serving customers where they already shop, creating more automated and on-demand services such as stand-alone kiosks and additional partnerships with retailers. The Postal Service will expand options available on its website and through its carriers, which provide access to most postal services without customers leaving their home or office.

As customers continue to shift to these new services, the Postal Service will minimize costs by reducing redundant retail facilities. Current customer research shows increased demand for new ways to access the postal services. For instance, 79 percent of Americans surveyed were not concerned about closing Post Offices if postal services were moved to other retail locations (Exhibit 12). Many actually preferred to have postal services provided in nearby retail locations rather than Post Offices.

Proposals to close facilities often lead to protests, and on a few occasions Congress has blocked changes through legislation. This response is not unique to situations involving the Postal Service. For example, recommendations to close or consolidate military installations have also met with resistance. However, because the Postal Service does not receive appropriated funds to maintain its network, postal customers are ultimately required to absorb the costs of political decisions that keep redundant facilities open.

Given the need for dramatic cost reductions, the American public is most in favor of eliminating Saturday delivery, rather than taxpayer subsidies or significant price increases.

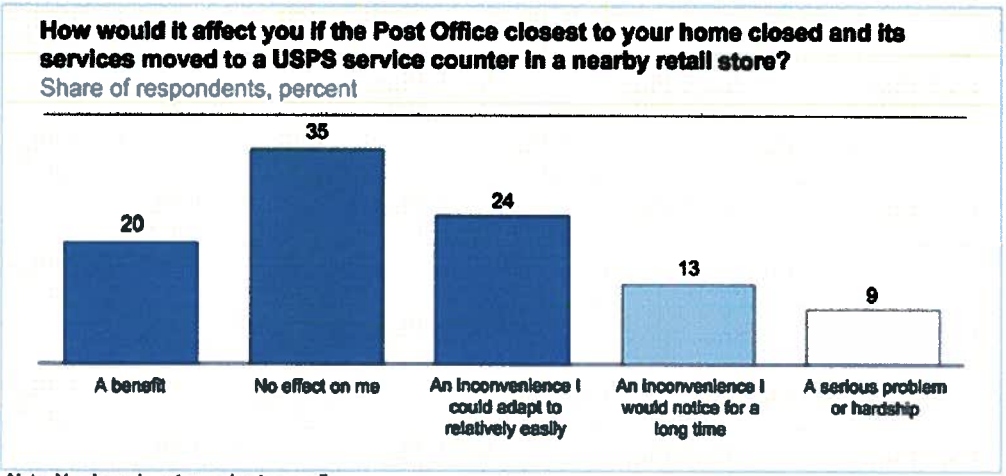
**Exhibit 11: Public opinion regarding delivery frequency**




SOURCE: Gallup Poll June 17-18, 2009

Almost 80 percent of consumers report they would benefit or would easily adapt if Post Office services were moved to a nearby retail store.

**Exhibit 12: Survey Data: Consumer acceptance of retail service options**




Note: Numbers do not sum due to rounding
SOURCE: Consumer survey, December 2009, conducted by McKinsey

## 4. Workforce

The Postal Service must become a leaner organization. The large number of expected retirements creates an important opportunity to achieve this through what can be an orderly process of attrition, and by establishing more flexible work rules through the collective bargaining process. Annually, approximately 5 percent of employees are eligible and expected to retire. It would not make sense to replace them with full-time employees if demand is moving in a direction better suited to a part-time workforce. Although the Postal Service would prefer to manage this change through collective bargaining, under existing law, arbitration is always a possibility. The financial health of the Postal Service and the affordability of postal products should be key considerations in any arbitration ruling. Therefore, the Postal Service will ask Congress to require arbitrators take into account its financial condition before making any decision.

When benchmarked against other large posts, the Postal Service employs the most full-time workers as a percentage of the total workforce. For example, the United Kingdom employs 22 percent part-time employees and Deutsche Post employs 40 percent part-time employees, while part-time employees represent up to 13 percent of this country's postal workforce. Providing increased workforce flexibility will help maintain service levels while reducing costs.

## 5. Pricing

The Postal Service needs the authority to adjust its pricing to better reflect market dynamics and offset future volume and revenue declines. Current law does not provide this. Instead, prices by class remain tied to CPI, and not to the key drivers of postal inflation. Also, the Postal Service may make only limited price increases under exigent circumstances. Therefore, it will seek legal modifications related to pricing, and pursue a moderate exigent price increase effective in 2011.

**Single price cap.** The first reform would apply the inflation price cap to Market Dominant products as a whole, rather than to each class of mail. This would allow adjustment of individual prices based on market demand and unit costs. Prices for some classes would rise above the rate of inflation while others would rise at a lower rate. This would provide flexibility over time

to address products that do not currently cover their costs.

**Preferred-class pricing.** Addressing the pricing of preferred mail — such as non-profit mail, Media Mail, Library Mail, and Periodicals — would ensure that these products get to a point where they cover costs while contributing reasonably to overhead costs. An alternative would be appropriations funding to cover the gap.

**Exigent price increase.** The Postal Act of 2006 allows price increases beyond the Consumer Price Index in extraordinary circumstances. Such increases are permitted if the Postal Regulatory Commission finds "that such adjustment is reasonable and equitable and necessary," and that there are "exceptional or extraordinary circumstances."[11] Using existing authority, the Postal Service will pursue a moderate exigent price increase in 2011. Larger increases will need to be pursued if changes are not authorized in connection with other issues, such as Retiree Health Benefits pre-payments and 5-day delivery. Given the largest volume declines since the Great Depression, the requirement to pre-pay billions of dollars in retirement health benefits, and the forecast for increasing net losses, among other unfavorable realities, the current situation should qualify (Exhibit 13).

## 6. Products

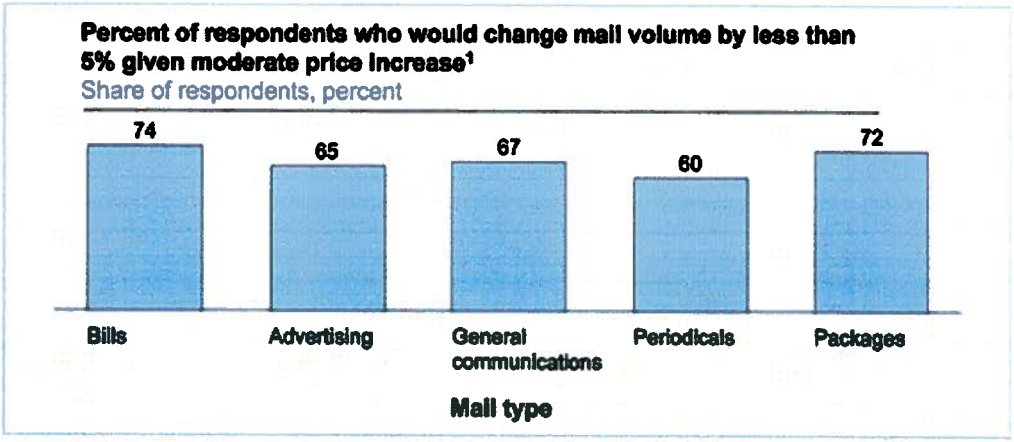
As technology and customer needs change, so will the definition of mail. The Postal Service seeks additional flexibility to innovate its products and better meet changing customer demands, while tapping into new sources of revenue.

Currently, every potential new product, including individual customer contracts, require before-the-fact review by both the Governors and the Postal Regulatory Commission. The existing review process can delay the implemention of customer contracts, leading to mailer frustration and providing an adventage for competitors.

Amending the current regulatory framework to broaden the definition of postal products and allow for streamlined, after-the-fact product reviews would allow the Postal Service to introduce new products and services in a more timely and customer-friendly way.

Although prices are capped by law, survey data show that small businesses would tolerate moderate increases.

**Exhibit 13: Survey Data: Small business response to price increase**




1. 5% price increase

SOURCE: Consumer survey, December 2009, conducted by McKinsey

### 7. Oversight

Congress modified the Postal Service's oversight model in 2006 at a time when volumes were increasing. The model includes Presidentially-appointed Governors (USPS) and Commissioners (PRC). Both are required to represent the public interest and have overlapping responsibilities to ensure affordable, quality, universal service to America. Additional oversight includes Congress, portions of the Executive Branch, the Government Accountability Office, the Postal Service Inspector General, and other federal agencies. In many situations, roles and responsibilities overlap and are not sufficiently clear. Oversight primarily involves changes to postal networks, products, prices, costing methods, service, Sarbanes-Oxley Act Compliance, and complaints.

The world is rapidly changing, yet the current oversight model constrains the flexibility and speed required to adapt and respond. It is crucial to clarify oversight roles and responsibilities and to streamline processes. Oversight changes are critical mechanisms to make this plan a reality. Since the Postal Act of 2006, the Postal Service has increased transparency and accountability. However, internal changes alone are insufficient. Changes in law are necessary to make oversight processes more responsive to market needs. They should include looking at issues such as time limits on reviews, and moving before-the-fact to after-the-fact reviews. Collectively, these changes would ensure continued protection of customer interests while providing flexibility to manage in the changing postal environment.

Only by balancing actions across all these areas will the Postal Service be able to close the remaining $15 billion deficit projected for 2020, while continuing to provide high-quality, affordable service. Taking action along just a few of them would exacerbate the financial situation and place an undue burden on any one group of stakeholders.

## THE PATH FORWARD

Even with the most informed projections, there is no way to know exactly what the future holds. Therefore, it is imperative that improvements to the Postal Service business model contain sufficient flexibility to allow the Postal Service to respond quickly in a financially responsible way no matter where the market turns. America can continue to enjoy quality, universal postal service at no cost to the taxpayer only if aggressive internal improvements are made in tandem with regulatory and legal changes.

The only way to close the Postal Service's income gap while providing the American people with the service they deserve is though a balanced approach that does not overtax any single part of the business or place a disproportionate burden of change on any one group. The Postal Service asks for the flexibility necessary for action along all seven proposals:

- Restructuring retiree health benefits payment to a pay-as-you-go system
- Adjusting delivery frequency to reflect volumes and customer needs
- Modernizing access to make it more effective and efficient
- Establishing a more flexible workforce
- Aligning pricing with economic realities
- Allowing faster introduction of a broader range of products
- Ensuring agile and appropriate oversight

If this plan becomes a reality, the Postal Service can build on its achievements and secure a strong future to meet the nation's changing needs. Delay increases the challenge and deepens the crisis. Success will require starting to work on solutions now.

# Appendix

Summary of some of the additional concepts that were evaluated but are not currently being pursued

### Changing First-Class Mail service standards

Moving First-Class Mail service standards from 1-3 days to 2-5 days would reduce cost and system complexity. Savings would accrue by consolidating facilities and divesting unused plants, virtually eliminating costly air transportation, and redesigning the network to simplify and standardize mail flows and processes.

The option to lengthen the delivery window for First-Class Mail will not be pursued at this time. When presented with this prospective change, mailers expressed concern about the cash flow consequences of a longer delivery window for bills and payments. Only 17—18 percent of consumers responded that a shift from 1- to 2-day local mail would be "an inconvenience I would notice for a long time" or a "serious problem or hardship." Nevertheless, mailers said they would likely reduce volumes if the standards changed. There is already a shift from First-Class Mail to Standard Mail due to its improved service. Reducing the First-Class Mail service standard would no longer provide the same level of product differentiation, thereby reducing the value of First-Class Mail.

### Shifting delivery to the curb or centralized boxes

Moving delivery from the door to a curb receptacle, or from the curb receptacle to a centralized "cluster box," would reduce costs by allowing for more deliveries per route. This option will not be pursued at this time. Mailers were concerned that shifting delivery to curb or community mailboxes would undermine the convenience and intimacy of mail and lead to customers checking mail less frequently. They said they would reduce volumes as a result. Roughly 15 to 20 percent of small and mid-sized businesses expected to reduce volume by more than 10 percent if delivery points were changed. Higher-volume mailers responded similarly. Shifting delivery points would also be expensive and slow to implement.

### Additional non-mail revenue generating options

Additional revenue opportunities will continue to be considered in the future. Some product ideas were drawn from international posts, which take a broad-based approach to product diversification. Ultimately, five areas stood out — parcel services, logistics, banking, integrated marketing, and document management. Building a sizeable business in any of these areas requires time, resources, new capabilities (often with the support of acquisitions or partnerships), and profound alterations to the postal business model. Accenture research shows that while international posts are still building these businesses and implementing the necessary steps to make them succeed, these lines of business tend to generate below-average profitability compared to industry benchmarks. (Details on *usps.com*.)

However, the other product areas examined are currently not viable for the Postal Service because of its net losses, high wage and benefits costs, and limited access to cash to support necessary investments. Opportunities to leverage the Post Office network to enter new markets, such as banking or consumer goods, are similarly limited by high operating costs and the relatively light customer traffic of Post Offices compared to commercial retailers.

### Becoming a federal government agency supported by appropriations

The Postal Service examined other business models, including a switch from today's self-funded Postal Service to a regular federal government agency supported by appropriations. This would be similar to the structure prior to the Postal Reorganization

Act of 1970. Under this model, Congress would determine the level of service provided, including the definition of universal service, pricing, and facility closures.

This model eliminates the tension that exists between the Postal Service's status as a governmental agency and its mandate to be self-supporting. This business model also ties political decisions to the funding responsibility for those decisions. For example, if Congress does not want facility closures, it would have to continue to fund those facilities.

The main disadvantage is taxpayer burden, especially given the deficits in the current economic environment.

### Moving towards privatization

Another business model option evaluated was privatization. This would be a dramatic measure requiring sweeping changes. The Postal Service would cease to be a government agency, and would operate as a private business owned by investors. This new private post would have shareholders and would compete with other private businesses. The postal monopoly would be reduced or eliminated. The Postal Service would be free to enter into any other businesses it saw fit, and it would be allowed to fail.

This model allows for greater flexibility in both revenues and costs. The Postal Service would have the ability, without political interference, to right-size its networks, design pricing approaches, adjust delivery frequency, and determine which products to eliminate or add. Those who support privatization point to the economic efficiencies of allowing market supply and demand to determine pricing and services offered, and to the assumption that competition would likely give rise to innovation and a more agile customer-responsive entity.

A look at privatization in other countries shows prices far greater than in the United States. A new private post could lose economies of scale inherent with processing and delivering the entire nation's mail. Presumably, other postal providers will quickly move in to serve the higher volume, profitable areas of the country, leaving higher cost rural and inner city urban locations without affordable service. To ensure universal service, subsidies would be required either through tax dollars or universal service fees charged to licensees. Nationwide affordable and uniform pricing would likely be eliminated, since private businesses would charge more to deliver to higher-cost areas. Elimination of the mailbox monopoly may raise concerns about the safety and security of the mailbox. Perhaps most importantly, there is the question of whether the Postal Service could find investors and equity if privatized, given that it has negative equity, operates in a declining industry, and is burdened with significant outstanding liabilities. Therefore, all the changes laid out here would be needed before privatization.

## Endnotes

1. The Boston Consulting Group projected mail volumes through 2020. Accenture analyzed the range of businesses that foreign posts have entered to see if these could raise profitable revenue to support the USO. McKinsey & Company developed an independent assessment of the Postal Service's current strategies and provided recommendations for future growth and cost savings options, over a ten year period.

2. $15.8 billion loss in revenues reflects aggregate volume decline (from 2006—2009) against 2009 prices.

3. Includes only the prefunding amount, not the costs of premiums for current retirees.

4. Price caps apply to Market Dominant products, including First-Class Mail, Standard Mail, Periodicals, Bound Printed Matter, Media Mail, Library Mail, and Special Services. In aggregate, they account for 88 percent of revenue and more than 99 percent of volume.

5. Volume projections based, in part, on extensive mailer interviews, consumer surveys and interviews, experience with other posts, and insight into other industries. Analysis developed by The Boston Consulting Group.

6. BCG analysis. Real (inflation-adjusted) revenue per delivery point per day (current dollars).

7. "The Postal Service shall provide a maximum degree of effective and regular postal services to rural areas, communities, and small towns where Post Offices are not self-sustaining. No small Post Office shall be closed solely for operating at a deficit, it being the specific intent of the Congress that effective postal services be insured to residents of both urban and rural communities." [39 U.S.C. 101(b)]

8. Assumes no action is taken to reduce workforce costs by 2020.

9. Regulations prevent the Postal Service from settling workers compensation claims (20 C.F.R. 10.5) and, unlike in most other industries, the Postal Service gets no subsidy to cover the costs for Medicare Part D prescription drugs. By law, the Postal Service may not have "a program of fringe benefits" that "on the whole" is less favorable than on July 1, 1971. [39 U.S.C. 1005(f)]

10. Sixty-six percent of consumers were reported to "strongly favor" or "favor" 5-day delivery over other options, including taxpayer subsidies, higher prices, lay-off of postal employees, and closing Post Offices.

11. P.L. 109-435 (Postal Act of 2006).

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All references to a specific year or "the year" refer to the Postal Service fiscal year ending September 30. However, specific month and year references pertain to the calendar date.

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FACT SHEET

# Expanded Access and Products

"Ensuring a Viable Postal Service for America," the Postal Service action plan for the next decade, describes a flexible, agile Postal Service that can adapt to America's changing mailing habits and preferences. The Postal Service understands that to best serve the American people in 2020 and beyond, it must be leaner and more able to quickly respond to customer mailing and shipping needs.

Don't look at the Postal Service and see only brick and mortar Post Offices. Look online at *usps.com*. Look at mobile devices. Look for Postal Service products at other retail outlets, grocery stores and pharmacies. Look for letter carriers to pick up packages at homes and offices. The Postal Service of the future will be different, but it will continue to drive commerce, serve communities and deliver value.

- Complete development of a world-class website that provides state-of-the-art technology, interactive communications tools, easier navigation and additional products and services to create the best consumer experience on the market.
- Expand existing applications on mobile devices for customer convenience and 24/7 access.
- Continue to modernize customer access by providing services at locations more convenient to customers — grocery stores, pharmacy, retail centers, office supply stores.
- Double the number of self-service kiosks, using the Postal Service's own Automated Postal Centers and new, innovative technologies through partnerships with private companies. Place kiosks in retail stores and popular consumer sites to increase convenience and expand access.
- Expand the number of places customers can access products and services beyond the 50,000 that exist today through partnerships.
- Complete current market tests with private companies to increase the availability of shipping and package services at retail centers and office supply stores popular with small business owners.
- Minimize costs by reducing redundant retail facilities to reflect customer behavior that is shifting away from visiting local Post Offices.
- Add a suite of hybrid mail products to better meet the changing needs of its customers that combines trusted and secure Postal Service addressing and delivery — whether in physical or electronic form.
- Continue to market and expand Priority Mail Flat Rate Box offerings, Parcel Select and Parcel Return services that provide a strong consumer and business suite of services.
- Establish a strong presence and large market share in the rapidly growing area of shipping recycled electronics and small appliances through the mail. Create new opportunities and pricing incentives to grow volume while retaining a fair return for First-Class Mail offerings.
- Secure flexibility in setting prices for all mailing products (Market Dominant) to ensure prices can be based on associated costs and demand for individual products, rather than capping each class of mail at the rate of inflation.
- Make the necessary legislative and regulatory changes to create the flexibilty to introduce new products that reflect changing customer needs, generate needed revenue and allow the Postal Service to compete more aggressively and fairly in the marketplace.