

**STATEMENT OF
POSTMASTER GENERAL/CEO
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BEFORE THE
SUBCOMMITTEE ON FEDERAL WORKFORCE, POSTAL SERVICE,
AND THE DISTRICT OF COLUMBIA
OF THE
COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM
UNITED STATES HOUSE OF REPRESENTATIVES
WASHINGTON, DC**

APRIL 17, 2007

Good morning, Chairman Davis, Congressman Marchant, and members of the Subcommittee. It is an honor and a pleasure to be here with you today as we prepare to enter a new era in the development of America's postal system.

Only four short months ago, a new and comprehensive governing statute for the United States Postal Service became law. It was the culmination of more than 10 years of effort by many of you here today, by your predecessors, by your colleagues in this body and in the United States Senate, by the Administration, by the members of the President's Commission on the United States Postal Service, and by forward-looking members of the entire postal community.

It was not an easy task, but it was a necessary one. The work of a previous generation of legislators, completed 37 years ago, established the modern Postal Service and its business model – one that created the foundation for more than three decades of success in serving the people of our nation.

To make that possible, the Postal Reorganization Act of 1970 converted a heavily subsidized Post Office Department into a self-supporting Postal Service. It created a system of management and staffing based on performance, merit, and accountability, independent of partisan influence. It resulted in fair wages and career opportunity for employees at every level.

This engendered the stability that permitted the new Postal Service to anticipate, plan, and invest in the future, moving it from an organization that relied primarily on inefficient and costly manual operations, to one that is today at the cutting edge in automated mail processing technology. This has contributed to steady improvements in service performance, customer satisfaction, and productivity.

In its last full year of operation, the Post Office Department's 741,000 employees handled 85 billion pieces of mail delivered to 95 million families and businesses. Last year, roughly the same number of employees handled 213 billion pieces of mail for a delivery base of 146 million addresses. Without advances in productivity and automation, and innovations such as customer worksharing, growth in mail volume over the intervening years would have required a staff of 1,800,000 employees – with the associated growth in costs.

Consistent with its mandate to break even over time, the modern Postal Service, over the course of 36 years of progress, has matched its expenditures with its income. It has not received an operational subsidy from Congress since 1982 – a full quarter century ago. Stamp prices, on average, have tracked the Consumer Price Index since the transition from the Post Office Department to the United States Postal Service became effective, on July 1, 1971.

And, perhaps most significantly for our nation, a productive partnership and cooperation with postal customers – a relationship marked by creative responses to their needs – contributed to the creation of a vibrant mailing industry that today plays a leading role in our economy. This is a situation not found anywhere else in the world.

Unfortunately, continued success under the original law became problematic over the last several years. Revolution in the communications and delivery markets – including technologies that could not have been imagined when the 1970 legislation was enacted – have challenged us like never before.

While the pace of change will continue, our nation is fortunate that so many have recognized, understood, and acted to preserve affordable, universal postal services for the people and businesses of America.

Representative John McHugh was among the first, more than 10 years ago. He worked tirelessly with his colleagues on both sides of the Hill to have them understand what was at stake and to involve them in developing a solution that would work for our country.

Comptroller General David Walker also understood that, without change, America's postal system would be in serious jeopardy. Testifying before the United States Senate six years ago, he issued a clear call for change, and described our finances and transformation efforts as high risk.

Mr. Walker's candid but fact-based assessment was instrumental to the genesis of our Transformation Plan, which was adopted in 2002, during my first year as Postmaster General. Our goal in developing the Plan was simple – to create strategies that would involve the entire organization and keep it focused on achieving steady progress in three key areas:

- Fostering growth by increasing the value of postal products and services to our customers;
- Improving operational efficiency; and,
- Enhancing our performance-based culture.

I am pleased to say we have been successful. That success is a reflection of the hard work, dedication, and professionalism of Postal Service employees in communities in every corner of the nation. They have stepped up to the challenge. They have given it their best. And they have made a difference.

Service performance, independently measured, has reached record levels – levels that some thought were impossible not so long ago. As we begin the third quarter of this fiscal year, nationwide service performance remains strong. In locations where service may not reflect national averages, we rely on our Area staff and, where necessary, headquarters resources, to work with our field managers to improve local service.

This commitment includes my personal involvement, as well. I have visited Chicago twice in the last month to assist in the achievement of the service levels that our customers expect and deserve. I can assure you that changes underway will deliver results.

Our customer satisfaction index – also independently measured – shows that 92 percent of our customers rate their experience with the Postal Service as excellent, very good, or good – commendable results for any business.

The customer experience is important to us. In fact, the respected Ponemon Institute has recognized the Postal Service as the most trusted agency of the federal government – for the third consecutive year – and among the 10 most trusted organizations – public or private – in the United States.

We are positioned to achieve an unprecedented eighth consecutive year of productivity growth. At the end of the last fiscal year, our debt was less than one-fifth of the \$11 billion outstanding when we created the Transformation Plan. Reducing and restructuring our debt has taken interest costs from more than \$300 million annually to only a few million dollars today. And we have reduced staffing by over 100,000 positions – without layoffs.

We have continued to improve the working environment for our employees. This is reflected, for example, in our safety programs, which include effective partnerships with the Occupational Safety and Health Administration. These have contributed to a 43 percent reduction in OSHA illnesses and injuries over the last five years. Working relationships marked by dignity and respect must begin with a workplace that protects the health and safety of our employees.

We have built on the original Transformation Plan with the implementation of our Strategic Transformation Plan 2006-2010. This is updated periodically to reflect changing market conditions, the achievement of existing Plan goals, and the addition of new ones. We fully recognize that, even with a comprehensive new postal law, it is incumbent on us to continue our pursuit of system efficiency, service improvement, cost management, and customer value, all based on the efforts of a customer-focused, performance-based culture.

When Comptroller General Walker called for postal transformation, he was also clear about the fact that the Postal Service, by its efforts alone, would be unable to fully surmount many of the challenges he identified. He also recognized that they could be overcome only in tandem with a fundamental revision of the Postal Service's basic governing statute, Title 39 of the United States Code.

By the end of last year, the seeds planted by Mr. Walker had thrived and were ready for harvest. The Postal Service had moved into phase two of its transformation efforts – with a strong record of success under its belt. And Congress had enacted the Postal Accountability and Enhancement Act, paving the way for longer-term success. The pieces were now in place for a future that would protect affordable, universal mail service for everyone in America.

With the progress and promise represented by both of these actions, the Government Accountability Office removed the Postal Service from its "high risk" list this past January. We are grateful for this recognition of the efforts of our people over the last five years. We fully appreciate our obligation to continue to bring focused, productive, and efficient management to every element of our business. And that is our continued commitment.

At the same time, we will do everything possible – both internally and in cooperation with the full range of industry stakeholders and government partners, particularly the new Postal Regulatory Commission – to implement the provisions of the new postal law efficiently and effectively.

Soon after the new law was enacted, we began to identify, plan, and manage the timelines and processes necessary for the successful and timely implementation of the provisions of the new law. We have restructured several functions to assure maximum levels of integration, cooperation, and success. Cross-functional workgroups, including representatives from finance, marketing, operations, human resources, and the law department are meeting regularly and making progress in developing the new processes, policies, and regulations necessary to implement the new law.

We have also initiated a dialogue with other federal agencies whose activities are affected by the new law. These include the new Postal Regulatory Commission, the Department of the Treasury, the Department of State, the Department of Homeland Security's Customs and Border Protection unit, the Federal Trade Commission, and the Government Accountability Office. Of course, ongoing liaison activities with both houses of Congress, particularly our authorizing and appropriations committees, are important elements of our efforts.

We have also made mailing community outreach a key part of our activities. Last month, along with the Postal Regulatory Commission, we participated in a number of events intended to provide the mailing industry with a better understanding of the new law and how it will affect them and, more importantly, listening to what the mailers need from the new law.

These activities included a symposium, sponsored by American University's School of Public Affairs, which examined key elements of the law, and a well-attended summit, which explored a wide-range of pricing, service, and process issues arising from the Act. This was a particularly valuable discussion as the Commission begins the process of drafting the regulations that will govern the new pricing regimen.

At the 2007 National Postal Forum, the leading mailing industry trade conference, senior officers of the Postal Service presented a number of sessions devoted exclusively to the new law. In addition, the Forum's opening general session, attended by more than 4,000 delegates, featured my conversation with Dan Blair, the chairman of the Postal Regulatory Commission. And, the Postal Service Board of Governors discussed the new law at a general session on the second day of the Forum and responded to questions submitted by attendees.

We are also working closely with the Mailers Technical Advisory Committee, whose membership consists of a representative cross-section of the mailing industry, on requirements arising from the new law. Most significantly, this includes the review of our service standards and the measurement systems that will support them. We believe that ultimate success in this area must take into account the needs and preferences of our customers, the costs of implementation – for mailers and for the Postal Service – and the use of compatible technologies that passively gather and report performance metrics.

The Mailers Technical Advisory Committee and the Postal Service are also hosting a Flats Symposium in May. As we prepare for the deployment of the new Flats Sequencing System, which will sort larger envelopes, magazines, and catalogs into delivery sequence, we look forward to this important conversation with mailers. While the flats sequencer will help us manage costs and bring the full advantage of automation efficiencies to this product category, it will require changes for the Postal Service and the industry. With our transition to a shape-based rate structure, rather than one that has been primarily based on weight, we believe this symposium will benefit all parties.

The new law has created a close, complex, and complementary relationship between the Postal Service and the Commission. As Chairman Blair has noted, he and I are now "connected at the hip." I look forward to working with the Commission, not only through the development of processes supporting the implementation of the new law, but on the day-to-day regulatory and oversight issues that will help to define the Commission's new role, as well.

The Postal Service has entered a period of accelerated transition. This will require flexibility, innovation, and focus to continue achieving our transformation goals within the context of the significant changes required by the new postal law. We have an enormous responsibility to do our part in achieving the law's goals of putting the Postal Service on a firm financial footing for the future and preserving universal service at affordable rates, with price increases tied to the rate of inflation.

It is my hope that some 30 years from today, a future Postmaster General will be invited to sit at this table and report on the progress that was made possible by the Postal Accountability and Enhancement Act of 2006. But, having said that, I would be remiss if I did not point out that the Act, while providing much needed flexibility in key areas such as price-setting and product differentiation, does not resolve the underlying issue of a business model that, simply put, is irrelevant to the reality of today's market, a fact recognized by the President's Commission on the United States Postal Service in its 2003 report, "Embracing the Future." Frankly, I do not believe any law, however well intended, can repair that broken model because mail volume is no longer growing at a rate sufficient to sustain the ever-expanding delivery network.

My position is not meant as criticism; rather it is an acknowledgement that the dynamics of the 21st century communications market have altered – forever – the basic assumptions of postal economics in a monopoly environment. The traditional postal monopoly, while it still exists as a matter of theory and law, particularly for what the new statute terms our "market-dominant products," does not exist in actual practice.

The explosive growth of electronic communications and an intensely competitive package delivery sector have led to the diversion of messages, transactions, and packages from the mail channel. Competition exists for every piece of mail that moves through our system. This has significantly slowed overall volume growth, with actual declines in some products, and resulted in shifts from higher-margin products to those making a lesser contribution.

In a practical sense, this means that mail volume growth can no longer match the historic trends of the last three decades and appears to be beginning to flatten. We can no longer depend on volume growing at a rate necessary to produce the revenue required to cover the costs of an ever-expanding delivery infrastructure.

This is not to say that the new law does not offer opportunities and needed relief from an overly restrictive, inflexible, lengthy, and adversarial pricing process. To the contrary, with the potential for annual rate adjustments tied to the Consumer Price Index for market-dominant products, we are in a much better position than ever to respond quickly as the market and our financial situation demand.

And with the separation of our competitive products portfolio from the market-dominant one, we will be able to operate far more nimbly in the expedited and package products sector. The new law is sensitive to the needs of the broader market and preserves the proper balance among the Postal Service and its private-sector competitors in this area in best serving customers.

Moreover, the new law does position us favorably for growth by supporting market-based pricing and making it possible to offer volume discounts. One of our greatest disappointments historically had been the reliance of other federal agencies on our competitors for package and expedited delivery services because the old law did not permit us to match their offers. Through the improvements made by the new law, we look forward to the ability to compete with others for the privilege of serving our partner federal agencies in new and better ways than had been possible in the past.

In addition, with a retail presence at 37,000 locations in communities from coast to coast, the Postal Service offers the potential for those agencies to provide convenient and cost-effective access to their programs through our facilities. For example, today we assist the Department of State by accepting over two-thirds of passport applications at almost 5,500 of our local offices.

Growth, of course, represents our greatest challenge going forward. Electronic billing and payment alternatives continue to adversely affect First-Class Mail volume, driving the transition from a transaction-based mailstream to one increasingly centered on marketing and advertising, both of which heavily rely on Standard Mail. Because of First-Class Mail's higher margins, it takes more than two pieces of Standard Mail to provide the profit contribution of each piece of First-Class Mail diverted from our system.

The good news is that marketers have learned that direct mail – whether First-Class Mail or Standard Mail – can add to the value of campaigns that also utilize other media. In this regard – and contrary to conventional wisdom – research shows that hard-copy mail and the Internet are complementary sales channels, with one increasing the effectiveness of the other.

Direct mail, particularly catalogs, increases the time consumers spend on a retail web site. It increases the likelihood they will buy. It increases the amount of merchandise they will purchase. And it increases the amount of money they will spend.

People are also finding new uses for the mail. The State of Oregon switched to mail ballots as a better way to conduct elections, resulting in far greater voter participation than in-person voting. This is an encouraging trend, and presents a unique opportunity for our democracy. It is something I will be discussing with a gathering of the secretaries of the nation's 50 states later this year.

Since a network of post roads and post riders tied 13 struggling colonies together more than 230 years ago, the Postal Service has taken great pride in helping to connect America's citizens with their government. Vote-by-mail is simply a current example of how this traditional role continues to evolve in a new century.

Mail is also at the core of the business model of some of today's most forward-looking businesses – businesses whose primary customer interfaces are the Internet and the mail. Netflix relies on the mail to distribute videos to millions of customers every year, taking advantage of the Postal Service's daily link to every home and business in the nation. This makes it quicker, easier, and more convenient than ever for busy families to enjoy current and classic movies without having to leave their homes.

Similarly, eBay, one of the fastest-growing businesses in the world, connects millions of buyers to millions of sellers, through the mail. Our productive relationship with eBay involves continued work with members of the eBay community to develop and offer service features that provide continually improved solutions to their shipping needs.

We will continue our work with all mailers, and using state-of-the-art technology, to add even more value to our products and services. One example is the new Intelligent Mail Barcode. It improves quality, cuts costs, and increases value – for mailers and for the Postal Service.

The Intelligent Mail Barcode simplifies, streamlines, and modernizes mail entry and payment procedures. It provides a window into operations as the mail moves through our system. This helps us to identify and eliminate operational bottlenecks, while it provides mailers with data that assists in planning and decision making in areas such as staffing, cash flow, inventory, marketing, and advertising. It contributes to more accurate addressing, helping to reduce the huge and unnecessary Postal Service and industry costs of undeliverable-as-addressed mail. It will also serve as the basis for providing actual service measurement data for specific mailings rather than simply sample-based aggregate system averages. Today, more than 60 mailers enjoy the benefits of the Intelligent Mail Barcode and we are continuing its expansion, anticipating full rollout in 2009.

The value of the mail goes beyond its advantage as a business driver. It is also an important part of the social fabric of our nation. We are particularly proud of our association with ADVO, Inc. and the National Center for Missing & Exploited Children through the "America's Looking for Its Missing Children" campaign. Through leads generated by the program's "Have You Seen Me?" cards, one of the most recognizable direct mail pieces in America, 144 missing children have been safely recovered.

Overall, direct mail is among the fastest-growing and most-effective advertising channels in America today. Mail gets attention. Its results are measurable. It can be targeted like no other media. That makes it more personal than any other. No other medium can tap into individual interests, or needs, like the mail. That makes it relevant. And that makes it welcome. There's nothing like it. That's why I'm bullish on the mail.

I am also a realist. I recognize that success under the new law will not be an easy lift, by any stretch of the imagination. We have never worked under a rate cap. We have never had to manage our costs by class of mail. Both are extremely challenging.

Significant portions of our costs – such as fuel, and employee retirement and health benefits – routinely exceed the Consumer Price Index. These are costs over which we have little control. While we all experienced a sense of relief as last year's stratospheric gasoline costs receded, they have begun, once again, to climb back up. With one of the largest vehicle fleets in the nation, and an infrastructure of almost 28,000 owned and leased facilities that must be powered, lighted, heated, and cooled, this is a cause of great concern for the Postal Service and for our ratepayers. For every one-cent increase in the price of gasoline, our costs rise \$8 million dollars annually.

We will maintain an intense focus on managing those costs we can control. We have had great success in this area over the last several years. We have picked the low-hanging fruit. We have stretched our arms to reach even higher. Yet we must do more.

Keeping our rates under the cap and, at the same time, being able to pay our employees a fair wage, requires that we find ways to remove at least an additional \$1 billion in costs each year. We believe this can be done. It will require discipline, difficult choices, and cooperation throughout the organization, as well as support from our customers, the Postal Regulatory Commission, and the Congress. But this is not about the Postal Service for its own sake; it is about our ability to preserve affordable, quality, universal mail service for all of America.

For example, we have been exploring the expanded use of contracted delivery services – one of the most cost-effective delivery modes available. This is nothing new. Since the earliest days of America's postal system, we have used contractors to move the mail safely and securely from point to point and provide box delivery along their routes.

In fact, much of the mail you receive each day – whether delivered by a city letter carrier or a rural letter carrier – has been handled by contractors providing over-the-road or air transportation. It has been paid for by a postage stamp that may have been purchased at a supermarket, convenience, stationery or greeting card store, or perhaps at a Post Office cleaned and maintained by a contracted service provider. Just as likely, postage was provided by a meter owned and leased by a private-sector provider. And you may have deposited or picked up your mail at one of almost 4,000 contract postal retail units operated by local business people in their communities. By augmenting the services we provide directly with the services provided by others, we have been able to better manage costs, improve efficiency, and provide even more convenient access for our customers.

Viewed within the totality of our business, contract delivery service represents the smallest portion of our outsourced activities – and an extremely small percentage of our overall deliveries. The Postal Service takes a number of steps in assessing contractors and subcontractors who are selected to provide mail delivery service. They undergo background checks, screening and fingerprinting. Their suitability is ultimately determined by the Postal Inspection Service, the federal law enforcement group charged with protecting the security of the mail. Any carrier – whether a Postal Service employee or a contractor – who is involved in the criminal mishandling of the mail is subject to the same criminal penalties contained in Title 18 of the United States Code.

Procedures governing contracting out, adjusting delivery routes, and protecting employees from involuntary layoffs are contained in the collective bargaining agreements with our unions. They are the product of joint negotiations, as required by Title 39 of the United States Code. This was one of the great advances of the Postal Reorganization Act of 1970 and it is a process that Congress has endorsed through its preservation in the Postal Accountability and Enhancement Act of 2006.

The collective-bargaining process is a complex exchange of positions, ideas, and proposals. Because it is a collective process, it requires both parties to consider and adjust their own priorities in the light of those of the other. Ultimately, it is intended to produce a working agreement with provisions acceptable both to management and to the labor unions – and that work for our customers. Possible violations of the resulting contract can be challenged and resolved through a multi-step grievance procedure, which includes third-party arbitration. The parties may also revisit existing contract provisions through the joint negotiation process.

We understand the concerns any labor organization would have with outsourcing. But it is not our intention to take existing work away from our letter carriers, nor is it our intention to lay off any carriers. That is something I pledge not to do.

With postage rates linked to inflation under the new postal law, contracting out remains an effective and necessary tool to help us manage costs to achieve this mandate. Yet I believe achieving productivity gains in the delivery function can limit the growth of contracted delivery work.

This is true, as well, of our mail processing and retail operations. We must have the ability to adjust our network to accommodate the changing needs of our customers, to achieve the highest return on our technology investments, and to adapt to shifts in the type of mail moving through our system. This is critical to our success.

Our ability to operate within the constraints of a rate cap requires that we achieve our productivity targets. We can choose either of two paths. Management and the unions can work together to maximize the opportunities to increase productivity in processing operations, retail, and delivery. If we do not do that, we will have created a situation that requires additional contracting out. I stand ready to work with our unions to secure the future of our organization and its people.

I am also hopeful that we will be able to reach a negotiated contract settlement with the NALC, as we have with the American Postal Workers Union and the National Postal Mail Handlers Union. While we are formally entering the interest arbitration process, I believe the parties – and the interests of our customers – are best served by an agreement reached jointly, without the need for third-party intervention. Therefore, I will continue my efforts to achieve this outcome.

Despite our progress in cost management, there has been some concern regarding the Postal Service's financial position this fiscal year, following four consecutive years of positive net income. As you know, we are projecting a loss of approximately \$5.2 billion this year.

This is primarily a function of a number of related issues connected to the creation and funding of a new Postal Service Retiree Health Benefits Fund by the new postal law.

- The \$3 billion in cash that the Postal Service placed in a federally mandated escrow account in Fiscal Year 2006 was designated to be placed into the Fund in the first quarter of the current fiscal year.
- Generally Accepted Accounting Principles require that the \$3 billion escrow funds, which had been considered restricted assets, be reported as a Fiscal Year 2007 expense.
- While we would have preferred a 30- or 40-year amortization schedule, the new law has a flattened 10-year payment requirement into the Fund that ranges from \$5.4 to \$5.8 billion annually, beginning this Fiscal Year.

It's important to put this into perspective. Although it will have a multi-billion dollar impact on our reported 2007 financial results, the additional cash required is approximately \$600 million.

These payment and accounting changes create a difficult financial situation in the short term; however, this will improve significantly in 2017 and beyond, when retiree health benefits should be fully funded and this payment is no longer required.

In closing, let me reiterate my sincere belief that the new postal law offers opportunities to the Postal Service and the entire mailing community. We acknowledge these opportunities do not come without added responsibilities. To take advantage of the opportunities and to fulfill the responsibilities, we will continue to improve every aspect of our business. We can do no less.

While some have asked me what might be changed in the law, I believe it is premature to consider, without sufficient experience, what – if any – revisions might be warranted. While this may be the subject of a fruitful discussion in the future, our immediate focus must be a smooth transition and implementation of the new law. I assure you that the Postal Service will do everything possible to do that successfully.

I would be pleased to answer any questions you might have.

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