

A. Purpose and Background

The purpose of this review was to conduct an independent assessment of the full costs of running the National Change of Address (NCOA) program, whether the USPS was recovering costs, and what were the related benefits of the NCOA program.

The Postal Service estimates that approximately 17 percent of the nation's population moves each year. These moves result in approximately 2.7 billion pieces of forwarded mail and 43.5 million change of address cards in 1997.¹ Such volume creates formidable obstacles in maintaining a high quality mailing list for customers that will be used for the preparation of mailings.

The NCOA program makes change-of-address information available to USPS customers who have name and address list that will be used for the preparation of mailing, to help reduce undeliverable or duplicate mail pieces. In 1986, the Postal Service implemented the NCOA program, which extends the Postal Service's use of mail forwarding information to update business mailers' address lists.

Before introducing this program, business mailers were notified of change of address information after their mail had been sent out and forwarded, returned, or discarded. The USPS now confronts this problem before the mail piece enters the mail stream by using licensees licensed by the Postal Service to provide commercial customers a mailing correction service for lists used for the preparation of mail.

B. Approach

The approach taken was to first determine the full costs of the NCOA program, then determine the revenues generated from the program, and finally to determine the related benefits. Additionally, this is the first of two reports to be issued on the NCOA program. The second report will assess the industry implications of including advertisements in the Welcome Kits.

B.1. Costs of Running the NCOA program

In determining the costs of running the NCOA program, we conducted interviews of key personnel, and reviewed the relevant cost data at the National Customer Support Center in Memphis, TN. Based on our review, we concluded there were three main categories of costs: direct costs, directly associated indirect costs, and indirect costs.

In calculating direct costs, we accumulated all costs that could be traced to the NCOA program directly in an economically feasible way. An example of such costs would be

¹ Comprehensive Statement of Postal Operations 1997, Pg. 52

the costs of all direct salaries and wages, (including benefits) of the employees who directly participate or support activities that can be traced directly to the NCOA program. Directly associated indirect costs are the costs of the support departments that are essential to the NCOA operations. An example of such costs would be the salaries and wages (including benefits) of the employees maintaining the microcomputers that support the NCOA program, but not in a directly traceable manner.

Moreover, indirect costs are those costs that could not be traced to the NCOA program in an economically feasible manner. Such costs would be overhead costs that have to be allocated to the NCOA program based on an estimated level (percent) of usage. Examples of such costs would be rent and utilities.

B.2. Assigning and Allocating Costs to the Three Stated Categories

1. Direct costs were assigned to the NCOA program on a 100 percent basis.
2. Directly associated indirect costs were allocated to the NCOA program based on the level of resources consumed by the NCOA program. For instance, the costs of operating and maintaining the mainframes in the Technical Support Department was allocated to the NCOA program based on central processing unit seconds utilized.
3. Indirect costs were allocated to the NCOA program based on surveys we conducted. We calculated that the NCOA program consumed seven percent (weighted) of the Administrative Support Department resources. Therefore, we used this rate to allocate rent and other general overhead expenses, such as depreciations to the NCOA program.

B.3. Full Costing of the National Change of Address Program

Based on the concept of full costing, we were able to determine the full costs of operating the NCOA program for fiscal year (FY) 1998. The costs by the three categories mentioned earlier are as follows:

➤ Total estimated direct costs:	\$1,044,597
➤ Total estimated directly associated indirect costs:	\$1,652, 817
➤ Total estimated indirect costs:	\$318,502
➤ Full Costing	<u>\$3,015,916</u>

Our analysis disclosed that the NCOA program generated \$1,918,521 in revenues from its licensees in FY 1998. Therefore, the full costs of running the NCOA program exceeded revenues generated in fiscal year 1998 by \$1,097,395.

Based on the concept of marginal costing (i.e., direct costs + directly associated indirect cost), the USPS revenues from its licensees would have exceeded the marginal costs of running the NCOA program in FY 1998. It appears that the NCOA program managers could have applied the concept of marginal costing when initially determining the prices set for the service provided to the mailing community. We discussed revising this paragraph for clarity during the outbrief any suggestions?????

B.4. Determining the Benefits of the NCOA program:

The simple concept of providing the mailing community with the opportunity to update their mailing list prior to mail entering the mail stream allows the Postal Service to avoid the rehandling costs associated with forwarding mail.

In order to quantify the benefits of the NCOA program we used an existing study conducted by Price Waterhouse in 1995 (Volume, Characteristics, and Costs of Processing Undeliverable-AS-Addressed Mail).

We applied a conservative approach in determining the benefits of the NCOA program. We started with the costs to forward a single piece of mail. Since the costs to forward a piece of mail in 1995 was \$0.2316², we started with this base cost and applied the consumer price index for 1996, 1997, and 1998 to arrive at an estimated costs to forward a piece of mail in 1998, \$0.2472.

After calculating the estimated costs of forwarding a piece of mail in 1998, we multiplied that by the number of addresses updated on mailers' address lists as a result of the NCOA program. The result would show the costs avoided by the USPS.

During fiscal year 1998, the NCOA licensees processed 109,634,114,940 addresses. Of that total, 4,830,521,256 addresses were updated on mailers' address list.

The calculation of benefits was based on the following assumptions:

- For every postal customer who moved and processed a change of address order the postal customer received one piece of mail during FY 1998 at their new address.
- Every address updated on a mailer's address list resulted in a correctly addressed piece of mail.

² Price Waterhouse Report, Volume, Characteristics, and Costs of Processing Undeliverable-AS-Addressed Mail, Contract # 104230-91-H-H053, and Pg. 5-5.

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- For the 4,830,521,256 addresses updated on mailers' address lists in FY 1998, the USPS avoided the costs of forwarding mail to the new addresses.

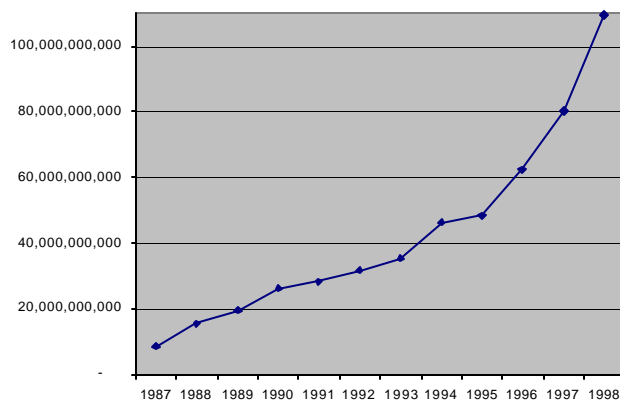
During FY 1998 the Postal Service was able to avoid \$1,194 billion in rehandling costs associated with forwarding mail.

C. Graphical Analysis, Change of Address Records Processed, and the Match Rate for Records Processed, 1987 – 1998

During the period 1987 to 1998, over five hundred billion mailers' addresses were processed by NCOA. Of that total more than twenty-one billion addresses were updated on multiple mailers' address lists, therefore reducing the amount of mail needing to be forwarded by the USPS.

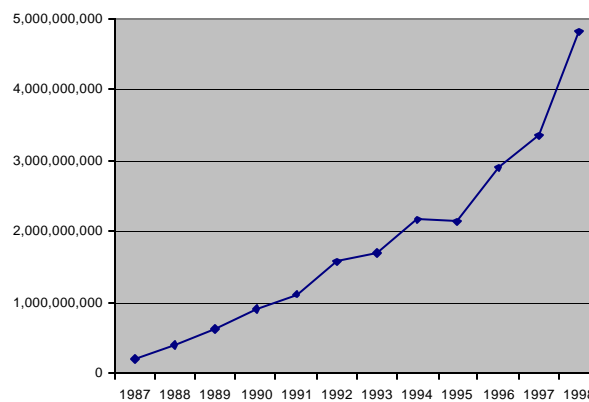
Our analysis disclosed that the number of records processed by the NCOA licensees as a result of the NCOA program, and the number matched has been steadily increasing over the last ten years, as depicted in graph #1 and # 2.

Records Processed, 1987 - 1998



Graph # 1

Records Matched, 1987 -1998



Graph # 2

D. Conclusions

Based on our analysis, it appears that under marginal costing the USPS NCOA program revenues exceeded expenses for FY 1998. However, under full costing, the estimated costs of the NCOA program for FY 1998 exceeded the revenues generated by \$1,097,395.

However, the rehandling costs avoided by the USPS in FY 1998 as a result of not having to forward mail when individuals, families, and businesses move was estimated at \$1,194,119,153. Therefore, the benefits of the NCOA program far outweigh the net costs (excess of expenses over revenues) of the NCOA program in FY 1998.

E. Recommendation

We recommend the Manager, Address Management, use full costing to establish rates NCOA licensees pay to receive NCOA service if the goal of the NCOA program management is to recover the full costs of the service they provide to the licensees.

F. Management Comments

The Vice President of Operations Planning concurred with the finding and the recommendation and provided a plan to implement the recommendation. See Appendix I. The plan indicates that adjustments to the annual licensing fee will increase during years 2000 and 2001. In addition, they will continue to monitor the annual license fees and adjust based on full-costing.

G. Evaluation of Management Comments

Management's comments were responsive to the issue raised in this report.

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NICHOLAS F. BARRANCA
VICE PRESIDENT, OPERATIONS PLANNING



March 30, 1999

COLLEEN A. MCANTEE

SUBJECT: Performance Audit of the NCOA Program

We have reviewed your draft report titled *Performance Audit of the National Change of Address Program*. As you know, we welcome your office's review and analysis of the National Change of Address (NCOA) operations and the calculation of the cost of providing NCOA to mailers through licensed commercial providers.

Your report indicates that, based on the full-costing method, the cost of operating NCOA during fiscal year 1998 was \$3,015,916. The report also notes the significant operational benefit of NCOA to the Postal Service. We are aware of the cost avoidance associated with providing address corrections prior to mailing, which eliminates the additional costs associated with forwarding a mailpiece. Your audit confirms the benefit of NCOA by identifying a cost avoidance of more than \$1 billion per year.

We agree with your conclusion that the estimated cost of the program for fiscal year 1998 exceeded the total amount of licensing fees collected; therefore, we have developed the following plan to support your recommendation that we recover that additional cost.

- To recover the full cost of providing administrative, operational, and technical support to NCOA licensees and their customers, we will increase the annual licensing fee to \$100,000 on July 1, 2000 and \$125,000 on July 1, 2001.
- We will continue to monitor annual license fees and adjust them based on the full-costing method identified during your audit.

If you would like to discuss our new licensing fee plan further, my staff is available at your convenience.

A handwritten signature in black ink, appearing to read "Nicholas F. Barranca".

Nicholas F. Barranca

cc: Michael L. Murphy