



# Public-Private Partnerships: Best Practices and Opportunities for the Postal Service

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Public-private partnerships (PPPs) are an increasingly popular way for governments to achieve policy goals and develop infrastructure, while shifting short-term financial burdens away from taxpayers and strained government coffers. In the postal sector, PPPs have helped international postal operators reduce the costs of universal service and leverage the skills and know-how of private businesses.

Given the depth of the financial problems of the U.S. Postal Service, the time is right to consider greater use of PPPs. When designed and executed well, PPPs can be a useful instrument for the Postal Service to manage costs, secure capital needed to modernize its infrastructure, and acquire new know-how to spur product innovation. Some PPPs can also provide short-term injections of cash to the Postal Service as part of a long-term symbiotic arrangement, bolstering an organization which suffered a \$15.9 billion loss in 2012.

Foreign posts have used PPPs to lower the costs of providing retail services to the public through franchising initiatives and to upgrade their vehicle fleets while reducing fleet management costs. These strategies have also helped foreign posts adapt to the decline in the hard copy mail market by changing the nature of their costs from fixed to variable, so that costs fall along with declining mail volumes. In the United States, federal and state agencies have used PPPs to finance expensive public works projects.

### Highlights

There are real opportunities for the Postal Service to earn income from its real estate portfolio, upgrade its infrastructure, benefit from private sector innovation, and make its cost structure more variable so costs decline with volume.

PPPs have helped postal operators reduce the costs of universal service and leverage the skills of private businesses. The posts use a wide variety of PPP models successfully, including franchising, co-location in private retail facilities, and sale and leaseback agreements.

Foreign posts have used PPPs to lower or eliminate fixed costs in retailing, real estate, and fleet management. Turning these fixed costs into variable costs allows them to decline along with mail volume.

A key lesson from U.S. states and foreign governments is that there are benefits in centralizing and professionalizing PPP expertise and best practices.

The Postal Service has experience with PPPs in several functional areas, but does not use a cohesive PPP strategy or operational approach.

While the Postal Service does not use a single cohesive PPP strategy, it has experience with PPPs in a number of functional areas such as the Contract Postal Unit (CPU) program, which allows privately owned retail facilities to sell postal services. Worksharing — a program in which Postal Service customers obtain discounts for doing postal work that they can perform more efficiently — is essentially an innovative PPP available to the entire mailing industry rather than a single partner.<sup>1</sup> The Postal Service also has a number of marketing affiliate relationships with private businesses and operational partnerships designed to leverage private sector efficiencies.

Nonetheless, the Postal Service can learn from the experiences of foreign postal operators and other U.S. federal and state agencies. A key lesson from observing other public organizations is that there are significant benefits in consolidating PPP expertise within a single office. A PPP office can serve as a repository for best practices; standardize and disseminate such practices to functions throughout the organization; act as a champion for PPPs; and develop the financial, legal, technical, and communications skills that are necessary for the successful development of PPPs. Such an office could also serve as a well-defined and easily identifiable point of contact for potential partners.

This paper reviews lessons learned from the Postal Service's use of PPPs, and identifies critical success factors for effective PPPs based on the experiences of foreign postal operators and U.S. government agencies. The paper also identifies potential partnership opportunities for the Postal Service, and suggests adoption of some best practices to help guide a future strategy toward PPPs. While PPPs are not a panacea, the review indicates there is potential for the Postal Service to receive further benefits from greater use of PPPs, particularly through the establishment of a central, high-level PPP office.

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<sup>1</sup> See U.S. Postal Service Office of the Inspector General (USPSOIG), *Assessment of Worksharing*, Report No. RARC-WP-10-005, July 12, 2010, [http://www.uspsaig.gov/foia\\_files/rarc-wp-10-005.pdf](http://www.uspsaig.gov/foia_files/rarc-wp-10-005.pdf).

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# Public-Private Partnerships: Best Practices and Opportunities for the Postal Service

## Introduction

The U.S. Postal Service is facing several severe problems. Short-term issues include a loss of nearly \$16 billion in 2012 and serious cash flow concerns in 2013. In the long term, increased reliance on electronic communications by consumers and businesses has caused a decline in the core mail business. First-Class Mail volume peaked in the 1990s, while overall volume is down sharply from a peak of 213 billion pieces of mail in 2006 to 160 billion pieces in 2012, jeopardizing the Postal Service's ability to provide universal service through extensive and costly national networks.

Stabilizing Postal Service finances and remaining relevant in modern communications will require significant restructuring of operations and the workforce, and updating its product portfolio. However, the Postal Service is not well positioned, by itself, to make all of these transitions. Postal Service know-how is concentrated in the declining

**PPPs can help the Postal Service with cost avoidance, revenue generation, and infrastructure investments.**

traditional mail business, with the exception of e-commerce parcel delivery. Parcels, however, make up less than 20 percent of Postal Service revenues. U.S. public policy does not permit the acquisition and merger strategies that foreign posts have used to enter new markets, while the Postal Service lacks capital to acquire significant new technological capabilities. Furthermore, the Postal Service lacks the cash to make needed investments even in its

traditional business. The Postal Service was scheduled to replace large portions of the vehicle fleet in the mid-2000s, but has deferred the replacements, as well as many other maintenance and capital investment needs, due to a shortage of capital.

Strategic use of public-private partnerships (PPPs) could help the Postal Service to address these problems.<sup>2</sup> Foreign postal operators, other government agencies in the United States, and the Postal Service have used PPPs to achieve several business objectives, including

- Cost avoidance, such as reducing the need for public capital investment by transferring project financing in full or in part to the private sector. PPPs can also make organizational costs variable by replacing fixed assets with third-party-operated facilities. Organizations can make costs variable by taking a cost that is fixed in nature, such as owning and maintaining a vehicle or building, and turning it into a cost that is more flexible and can be more easily adjusted to meet

<sup>2</sup> The recent paper *Restructuring the U.S. Postal Service: The Case for a Hybrid Public-Private Partnership* by Ed Gleiman, George Gould, Ed Hudgins, and John Nolan discusses PPPs in the context of a large-scale restructuring of the postal system. *Restructuring the U.S. Postal Service*, January 2013, <http://www.napawash.org/wp-content/uploads/2013/01/Hybrid-Public-Private-Postal-Service-1-2-13-3.pdf>. This OIG whitepaper examines PPPs of a much narrower scope, and does not address the broader policy issue of large-scale industry restructuring.

demand. Making costs more variable is particularly important in the postal sector, where demand for mail continues to fall.

- Accelerating the development and introduction of product and process innovations.
- Developing new growth engines through diversification to serve new customer segments.

This paper will review lessons learned from the Postal Service's use of PPPs, and identify critical success factors for effective partnerships based on the experiences of foreign postal operators and U.S. government agencies. The paper also identifies potential partnership opportunities for the Postal Service, and suggests adoption of some best practices to help guide a future strategy toward PPPs. The review indicates there is potential for the Postal Service to receive further benefits from greater use of PPPs, particularly through the establishment of a central, high-level PPP office.

**Organizations can make costs more variable by taking a cost that is fixed in nature and turning it into a cost that is more flexible and can be changed to match demand.**

## Defining PPPs

The National Council for Public-Private Partnerships (NCPMP) offers the following definition of a PPP:

[A] contractual agreement between a public agency (federal, state or local) and a private sector entity. Through this agreement, a certain range of skills and assets of each entity (public and private) are shared in delivering a service or facility for the use of the general public. In addition to the sharing resources, each party shares in the risks and rewards potential in the delivery of the service and/or facility.<sup>3</sup>

This paper loosely follows the NCPMP definition. The NCPMP's definition goes beyond the mere procurement of products or services, which does not involve sharing assets or risks. At the other end of the spectrum, outright privatization of the public asset is also excluded from this definition. The term PPP is also used by governments and intergovernmental organizations in a broader sense. It encompasses any type of joint activity governments initiate to help achieve public policy goals and involves private companies, civil society organizations or other government agencies. Government-led

<sup>3</sup> Richard Norment, *The Framework of Public Private Partnerships*, May 11, 2011, <http://www.ncppp.org/events/conference-materials/implementing-partnerships-for-infrastructure/>, p. 5.

standardization activities or plans to revitalize specific industries or to speed up innovation belong to this category as well.<sup>4</sup>

There are numerous PPP models; all are variations on basic business and contractual arrangements that define the risks and responsibilities shared with or transferred to, the private partner. (See Appendix A for a detailed explanation of the main PPP models.) PPPs can be categorized in several ways. A simple but clarifying classification scheme aligns the types of partnerships along two axes: one based on the proposed time horizon, either short term (tactical) or long term (strategic); and the other on the primary business objective, either cost optimization or business development/new revenues. We will refer to this classification scheme throughout the paper.

**Table 1: A General Classification Scheme for Public-Private Partnerships**

	Cost Reduction	Revenue Generation
Tactical	<p><u>Cost Variabilization, Asset Monetization</u></p> <p>Reducing fixed costs and leveraging underutilized assets</p> <ul style="list-style-type: none"> <li>▪ Real property leases</li> <li>▪ Contract Postal Units</li> <li>▪ Franchised Post Offices</li> </ul>	<p><u>Go-to-Market</u></p> <p>Growing market for current products in new segments and geographies</p> <ul style="list-style-type: none"> <li>▪ Most USPS revenue-sharing alliances with strategic partners (such as hybrid mail partners)</li> </ul>
Strategic	<p><u>Long-term Efficiencies</u></p> <p>Creating economies of scale or scope, leveraging private-sector ability to manage efficiently</p> <ul style="list-style-type: none"> <li>▪ Worksharing</li> <li>▪ Parcel Select</li> </ul>	<p><u>New Spaces</u></p> <p>Diversification, capability to innovate</p> <ul style="list-style-type: none"> <li>▪ Postal joint venture with banks</li> <li>▪ Solution partnerships, i.e., digital mail</li> </ul>

### ***Cost-reduction Approaches***

The upper-left quadrant of Table 1 includes cost-reduction efforts of a tactical or short-term nature. These efforts generate immediate or nearly immediate cash savings and include real property leases and contracting out the management of postal retail facilities. There is some crossover of activities between this quadrant and the revenue generation quadrants, as this category includes efforts to reduce the burden of costly

<sup>4</sup> For instance the White House-created US Ignite Partnership, aimed at “connecting, convening and supporting startups, local and state government, universities, industry leaders, federal agencies, foundations, and community and carrier initiatives in conceptualizing and building next-generation ultra-fast network applications in education, manufacturing, health, transportation, public safety and clean energy.” US Ignite, “US Ignite Launches to Catalyze the Next Generation of Internet Applications,” June 14, 2012, <http://us-ignite.org/2012/06/us-ignite-launches-to-catalyze-the-next-generation-of-internet-applications/>.



infrastructure by using such properties to generate income, thereby reducing the net expenditure on a property. For example, where the Postal Service is unable to dispose of a Post Office due to service requirements or stakeholder opposition, executing a sale and leaseback agreement with a partner could reduce the net short-term costs of remaining in the facility.<sup>5</sup> Other tactics in this quadrant include selling and leasing back fleets of vehicles or providing Post Office franchises to third parties as a replacement for traditional retail facilities.

The second cost reduction quadrant focuses on strategic PPPs aimed at reducing costs or gaining efficiencies in the long term. Such strategies can change the basic cost structure of the Postal Service. Most infrastructure PPPs belong in this category: the private partner brings its technical and management skills to the construction, operation, management, and/or maintenance of a facility or public service. The public entity should carry out a Value for Money (VfM) analysis, a tool for comparing the overall value of a PPP to a traditional procurement approach. To justify entering into a PPP, the VfM or a similar analysis should show that over the long term a lease or concession arrangement will provide a better value than traditional public management and procurement approaches.

In the postal sector, this quadrant would also include strategic partnerships aimed at minimizing end-to-end processing and delivery costs. The Postal Service's partnerships with other delivery services such as FedEx and UPS fit in this category, as could its extensive worksharing program, in which private mailers receive discounts for performing some upstream activities such as mail processing and transportation.

### ***Revenue-generation Approaches***

Like cost-reduction approaches, revenue-generation PPPs can have either a long-term or a short-term focus. Short-term opportunities, in the upper right quadrant, are organized under the "go-to-market" heading. These involve products that are ready to be marketed to potential buyers. Choosing a PPP as the market entry tactic can help to overcome barriers to entry. Introducing a product in a new geographic area or entering a new market segment can be complicated and costly. It may expose the enterprise to several obstacles, such as a lack of local market or segment knowledge, entrenched competition, regulations, and additional operating complexity. There are also risks based on opportunity costs and financial losses due to improper assessment of market conditions. In the postal sector, partnerships with private retailers to provide alternative drop-off points for parcels are one example of PPPs that address these barriers.

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<sup>5</sup> This paper mentions leasing out real or personal property in several places. Potential changes to accounting rules could make leasing less attractive to many organizations from an accounting and taxation standpoint, but these changes are not expected to eliminate other incentives to enter lease arrangements. The other incentives for leasing include obtaining cash and leveraging external expertise. See Jeffrey Shell, Grubb & Ellis, *Changes to Lease Accounting: Will sale/leasebacks still make sense?* <http://www.grub-bellis.com/Data/Articles/ChangesLeasingAccounting.pdf>. Both the potential accounting changes and increased use of leasing could require the Postal Service to make changes to its systems for tracking real estate. The Postal Service has already begun to evaluate its systems to prepare for the potential changes. Timothy O'Reilly, Controller, U.S. Postal Service, memorandum to Joseph Corbett, Chief Financial Officer, "Fiscal Year 2012 – Management's Communication of Control Deficiencies," February 12, 2013.

Another example is the Postal Service's affiliate partnership arrangements with hybrid mail companies, which can market their services on the usps.com website.

Long-term revenue generation partnerships or "new spaces," on the other hand, include potentially high-value PPPs that have a longer payoff time through the generation of new revenue streams. These include foreign postal experiments with banking, and initiatives by the Postal Service and other postal operators to partner with providers of digitally enhanced postal services. Gaining new capabilities is often a reason for postal operators to seek PPPs, along with strategic diversification, speeding up innovative product development, and applying new technologies. From the perspective of a private sector partner such as a bank or mobile phone operator, a partnership with the public postal operator can allow it to leverage the brand and image of the post as well as the post's distribution channels, and broaden its geographic coverage.

## Lessons Learned from U.S. Postal Service PPPs

There are several examples of Postal Service PPPs aimed at both revenue generation and cost containment, and many partnerships have both types of benefits. PC Postage partnerships, for example, have allowed end users to benefit from new products, as vendors innovate and compete for consumers on the postal platform, while also avoiding certain retail costs for the Postal Service. Despite the successful deployment of some PPPs, there appears to be room for improvement.

A few promising PPPs, such as the Electronic Postmark (EPM) and hybrid mail programs, were discontinued or lost momentum before reaching their potential due to a lack of focused and sustained attention. These PPPs have a high potential value for the Postal Service and its customers. In addition, the U.S. Postal Service Office of Inspector General (OIG) found that the Postal Service had lapses in validating revenues received from some partners.<sup>6</sup> A review of relevant research and interviews with former postal employees and stakeholders involved in PPPs reveal the concerns listed below:

- The Postal Service has put its short-term financial interest at the forefront of initial discussions, reducing the interest of both private and governmental partners.<sup>7</sup>
- There are significant regulatory barriers to some PPPs. For example, the Postal Service is prohibited from offering new nonpostal products. If a potential private sector partner offers a nonpostal product, this prohibition might prevent the Postal Service from forming a partnership that would result in a marketable

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<sup>6</sup> USPSOIG, *Revenue Sharing Agreements Audit Report*, Report No. FI-AR-12-004, September 14, 2012, [http://www.uspsoidg.gov/foia\\_files/FI-AR-12-004.pdf](http://www.uspsoidg.gov/foia_files/FI-AR-12-004.pdf), p. 2.

<sup>7</sup> Interview with former executive who held roles in business development, strategic planning, and ID protection, February 25, 2013.

product.<sup>8</sup> The uncertainty impedes negotiations with businesses, despite possible synergies available through a PPP.<sup>9</sup>

- The stage gate approval process and requirements for short-term financial returns can dissuade innovation.<sup>10</sup>
- Success in forming and executing PPPs is largely dependent on the internal sponsor's luck in having the right personnel assigned to the partnership. The quality and mindset of legal personnel, in particular, can "make or break" PPPs.<sup>11</sup>
- Some of the best proposals are new, paradigm-shifting ideas that are not readily understood because they do not fit into past practices. A former manager involved with several successful innovations and partnerships acknowledged that "the really good ideas are the ones I didn't understand." The former manager said the Postal Service, like other organizations, needs to devote sufficient resources to properly analyzing new partnership opportunities, if only to understand the implications of saying "no" to a potential blockbuster technology.<sup>12</sup>
- The Postal Service can be slow and bureaucratic in reaching deals, launching new initiatives, and resolving partner complaints.<sup>13</sup>
- Potential partners report significant difficulties in locating and obtaining information from points of contact. One organization searched for one year to identify the relevant Postal Service contact person.<sup>14</sup> The organization eventually entered into a successful partnership with the Postal Service, but many businesses will not or cannot afford to be so persistent or patient.<sup>15</sup>

**A single centralized PPP office can provide a point of contact for potential partners, and implement and disseminate best practices.**

Another major takeaway from a review of Postal Service PPPs is that there is not a single entity within the Postal Service that collects, organizes, and studies the lessons learned from the various successful or unsuccessful partnerships, and shares results throughout the organization. Such an entity

<sup>8</sup> See Postal Regulatory Commission, *Phase II Review of Nonpostal Services Under the Postal Accountability and Enhancement Act*, January 14, 2010, Order No. 392, Docket No. MC2008-1 (limiting the Postal Service's ability to license its brand to private sector partners).

<sup>9</sup> Interview with senior Postal Service official in strategic planning, March 6, 2013.

<sup>10</sup> A product approval process under which new products must meet benchmarks before receiving approval to move to the next phase of development or implementation.

<sup>11</sup> Interview with a former Postal Service executive who held roles in business development, strategic planning, and ID protection, February 25, 2013.

<sup>12</sup> Ibid.

<sup>13</sup> Remarks by an experienced postal legal expert to *The Future of USPS?* Center for Research in Regulated Industries, Advanced Workshop in Regulation and Competition, Washington, DC, April 12, 2013 and USPSOIG, *Revenue Sharing Agreements Audit Report*, pp. 2-3.

<sup>14</sup> Interview with a Member of the Board of Directors, Urbana-Champaign Independent Media Center, January 30, 2013.

<sup>15</sup> See "Our Community Media & Arts Center," *Urbana Champaign Independent Media Center*, December 8, 2010, <http://ucimc.org/content/our-community-media-arts-center>.

could help overcome the personnel problems identified above, ensuring that qualified and motivated staff is devoted to vetting and executing partnership agreements expeditiously and is available to interested external parties. Such dedicated personnel might have provided assistance in sustaining and revitalizing the EPM program, while providing rigorous oversight of revenue collection, for example. A single office for PPPs could implement best practices such as creating a central repository to monitor the performance of revenue-sharing agreements. Furthermore, establishing a centralized office could resolve a lack of unified and up-to-date guidance on strategic alliances or partnerships, and would provide a first-stop address for potential partners.

## PPPs beyond the U.S. Postal Service

Both foreign postal operators and U.S. government agencies have addressed problems similar to the ones the Postal Service faces by using PPPs. This section presents non-exhaustive examples of some of their strategies and tactics. (See Appendices C and D for a more extensive review.) The categories and types of PPPs in Table 2 are useful but are not “carved in stone” — the field is evolving and solutions are often context-specific. For the Postal Service, there are opportunities to explore creative options inspired by (not necessarily patterned after) some of the examples reviewed in this section. As a unique federal entity with a large commercial presence, the Postal Service should also consider engaging other governmental entities in partnerships by borrowing from existing PPP models.

**Table 2: Classification of Foreign Post and U.S. PPPs<sup>16</sup>**

	Cost Reduction	Revenue Generation
<b>Tactical</b>	<ul style="list-style-type: none"> <li>▪ Real estate management</li> <li>▪ Fleet sale and leaseback agreement</li> </ul>	<ul style="list-style-type: none"> <li>▪ Parcel locker development and placement</li> <li>▪ Financial services at postal retail facilities</li> <li>▪ CRADA intellectual property partnerships</li> </ul>
<b>Strategic</b>	<ul style="list-style-type: none"> <li>▪ Franchising the retail postal network</li> <li>▪ Seaport concession</li> </ul>	<ul style="list-style-type: none"> <li>▪ Enhanced Use Lease</li> </ul>

## Experiences of Foreign Posts with Partnerships

As mail volumes decline around the world, PPPs enable posts to shift costs from fixed to variable costs that adapt to changes in demand. For example, postal operators have used PPPs to address the challenges of maintaining retail access and a dense delivery

<sup>16</sup> This classification table is based on a model developed by Jean-Philippe Ducasse and decision/analysis partners.

network as required under universal service obligations, and to manage the high costs associated with the network when these fixed costs have grown out of proportion to revenues.<sup>17</sup>

### ***Real Estate Management***

Like the Postal Service, many foreign postal operators have dealt with legacy real estate holdings designed for a business model that is being made obsolete due to declining mail volume. Over the past 30 years, they have gone through a process of setting up separate business units to leverage their real estate holdings. According to experts on European postal systems, the real estate unit often charges other business units, cost centers, and shared service centers for usage of space through internal transfer prices. This has helped improve transparency and performance accountability. The transfer price system has also facilitated a regular review of internal lease agreements, and has given management incentives to adapt space requirements to changing needs based on projected volumes and budgets.

### ***Fleet Management***

Foreign postal operators have turned fleet management from a mainly technical operation into a business function focused on maximizing usage of existing vehicles and reducing fixed costs. One PPP approach is similar to a real estate sale and leaseback agreement; the postal operator sells its aging vehicle fleet to a private firm which specializes in leasing, finance and vehicle fleet management. The private firm then leases a new fleet of vehicles to the postal operator and provides maintenance services. Postal operators in Italy, Estonia, and the Netherlands have implemented such PPPs. (See Appendix C for a description of their approaches.)

In this type of partnership, the postal operator may receive the following benefits:

- An immediate cash injection from the sale of their old fleet;
- Increasing the flexibility or variabilization of operational costs for the new vehicle fleet; and
- A modern fleet that keeps up with new automotive technologies, improves fuel efficiency, and meets environmental standards and requirements.

### ***Retail Partnerships***

Another strategy used by European postal operators is to establish the retail post office business as a separate business unit, incorporating it and ensuring private sector partners' commitment to developing the network through joint investments or an equity

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<sup>17</sup> In the United States as in Europe, retail post office sales generate a small proportion of total revenues. See U.S. Postal Service, "Postal Facts, A Decade of Facts and Figures," "Postal-Managed Retail Office Revenue," <http://about.usps.com/who-we-are/postal-facts/welcome.htm> (revenue from Postal Service owned facilities was \$10.6 billion in 2012, out of \$65 billion total revenues). An evaluation by the firm decision/analysis partners confirmed that the figure is as low or lower in Europe.

participation in the new entity.<sup>18</sup> Often, the investors have been banks engaged in the delivery of financial services through postal retail facilities. This strategy reduces the fixed cost burden for the postal operator, while maintaining the network's ubiquitous presence.

Similar to the Postal Service's Contract Postal Units (CPUs), foreign posts also contract with small and individual entrepreneurs to operate a postal retail facility under a franchise agreement. The franchise generally includes usage of the postal brand, training, postal technology, and access to the post's management and business systems. The agreement provides the small entrepreneur with a regular flow of clients and visitors to whom other products and services can be offered. On the other hand, franchising agreements with individual entrepreneurs can be more difficult to manage and may prove riskier than other partnerships.

**Table 3: Franchising**

<b>Case Study: Post Netherlands Transition to a Fully Franchised Retail Network<sup>19</sup></b>	
<b>Project Description</b>	<ul style="list-style-type: none"> <li>▪ Development of postal counters in retail shops. Between 1995 and 2006, most of the 2,000 post offices were closed and franchised; they were replaced with retail outlets in supermarkets, bookstores, stationers, and other retailers.</li> <li>▪ In 2008, the Dutch Post still had 250 post offices in addition to 1,850 service points. It decided to extend to 2,600 the number of outlets and to close all remaining self-standing post offices within the next three years. The last one was closed in 2011.</li> </ul>
<b>Main Business Objectives/Results</b>	<ul style="list-style-type: none"> <li>▪ Long process from fully owned to fully franchised network allowed for a smooth transition, reducing any harm to, and complaints from, from the general public and stakeholders.</li> <li>▪ Added customer convenience (more access points, longer opening hours).</li> <li>▪ Reduction of fixed costs consistent with mail volume declines.</li> <li>▪ Closure of the remaining 250 post offices in 2008-2011 was expected to contribute from 2013, a structural annual operational cost saving of 45 million euros compared to 2007.</li> </ul>

<sup>18</sup> In order to establish its retail facilities as a separate unit, the Postal Service would have to decouple retail from delivery, and recommended by the OIG in *Retail and Delivery: Decoupling Could Improve Service and Lower Costs*, Report No. RARC-WP-11-009, September 22, 2011, [https://www.usps.oig.gov/foia\\_files/rarc-wp-11-009.pdf](https://www.usps.oig.gov/foia_files/rarc-wp-11-009.pdf).

<sup>19</sup> PostNL, "TNT Post to strengthen retail network," March 5, 2008, <http://www.postnl.com/about/historical-information/newsitem.aspx?key=573478>; PostNL, *Business Developments*, Annual Report 2012, <http://annualreport2012.postnl.com/report-of-the-board-of-management/mail-in-the-netherlands/business-developments>; and de Volkskrant, *Small post offices are Bruna stores*, December 12, 1995, <http://www.volkskrant.nl/vk/nl/2844/Archief/archief/article/detail/408833/1995/12/12/Kleine-postkantoren-worden-Bruna-winkels.dhtml>.

Franchising strategies such as the ones used in Australia and the Netherlands are more comprehensive than the Postal Service's CPU program. The Dutch Post (now PostNL) is a good example of a post that over time used these strategies to drastically reduce fixed network costs. Over 15 years, PostNL has evolved from being fully owned-and-operated by its mother company to a fully franchised retail network.

As e-commerce volumes grow, postal operators have set up dedicated parcel delivery networks. Many posts are testing and deploying 24/7 self-service parcel lockers in order to reduce the cost of failed deliveries and to increase customer convenience. To finance these new postal infrastructure components and to limit fixed costs, several PPPs have been used in Europe.

**Table 4: Retail Location Partnerships**

Case Study: Itella (Finland) Parcel Locker Partnership <sup>20</sup>	
<b>Project Description</b>	<ul style="list-style-type: none"> <li>▪ Cooperation agreement between Itella (Finnish post) and retail chain Kesko on the installation of Smartpost automatic parcel points in all (75) of Kesko's current "K-Citymarkets" by the end of 2013.</li> <li>▪ In 2012, Itella signed a cooperation agreement with another major retail chain, S Group, which will see up to 350 parcel terminals established in the retailer's supermarkets around Finland by 2015.</li> <li>▪ The post provides the equipment, while the supermarket provides space, maintenance, and servicing of the parcel terminal.</li> <li>▪ This agreement is part of Itella's strategy to deploy parcel terminals, which started with the installation of 50 parcel points in 2011.</li> </ul>
<b>Main Business Objectives/Results</b>	<ul style="list-style-type: none"> <li>▪ Making terminals quickly available to a large number of customers.</li> <li>▪ Customer convenience (for pick up and return of e-commerce packages).</li> </ul>

<sup>20</sup> See Itella, "Smart automatic parcel will be K-city markets," March 30, 2012, [http://www.posti.fi/tiedotteet/2012/20120330\\_Smartpostit\\_Citymarketeihin.html](http://www.posti.fi/tiedotteet/2012/20120330_Smartpostit_Citymarketeihin.html) and Post and Parcel, "Itella deal to run parcel terminals in Finnish supermarkets," August 14, 2012, <http://postandparcel.info/49924/news/companies/itella-deal-to-run-parcel-terminals-in-finnish-supermarkets/>.

## U.S. Federal and State Government Agencies' Experiences with PPPs

Government agencies in the United States have significantly increased their usage of PPPs as they deal with aging infrastructure and resource constraints.<sup>21</sup> The most frequent users of PPPs are state departments of transportation; toll roads are among the most high-profile PPPs. This section will focus on limited examples that could be adapted to the Postal Service's needs under the right circumstances (More information and case studies can be found in Appendix D).

### ***Monetizing Underused Assets***

Changing demand patterns and policy directions lead many agencies to consider alternative ways to monetize assets they no longer use or just partially use, but which they cannot or do not wish to sell. PPPs can generate financial value from underutilized assets by providing new sources of revenue, or new sources of financing backed by the market value of these assets.

### ***Monetizing Real Estate***

Several models can be considered for funding construction or renovations on underutilized federal property. The Enhanced Use Lease (EUL) allows a private developer to lease underutilized property, with rent paid by the developer in the form of cash or in-kind services, most often tied to the agency's programs. The National Aeronautics and Space Administration (NASA) uses EULs to attract private interest and investment in order to further its mission, such as by using private sector assistance to meet renewable energy goals; to extend NASA's research capabilities; to improve infrastructure; and to generate revenue.<sup>22</sup> The Postal Service has previously entered into EULs as well.<sup>23</sup>

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<sup>21</sup> See Fawn Johnson, "Why you won't own your road," *National Journal*, March 16, 2013, <http://www.nationaljournal.com/magazine/why-you-won-t-own-your-road-20130516>.

<sup>22</sup> NASA, *NASA Desk Guide for Enhanced Use Leasing of Real Property*, February 2010, [http://www.hq.nasa.gov/office/codej/codejx/Assets/Docs/EUL\\_Desk\\_Guide\\_Feb\\_2010.pdf](http://www.hq.nasa.gov/office/codej/codejx/Assets/Docs/EUL_Desk_Guide_Feb_2010.pdf), pp. 2-3, and NASA Office of Inspector General, *NASA's Infrastructure and Facilities: An Assessment of the Agency's Real Property Leasing Practices*, August 9, 2012, <http://oig.nasa.gov/audits/reports/FY12/IG-12-020.pdf>, pp. 24-35.

<sup>23</sup> GAO Report No. GGD-99-23 contains a description of the EULs relating to the Grand Central Station Post Office, New York, NY, 1987 (99 years lease) and the Rincon Center Post Office, San Francisco, CA, 1985 (65 years lease). GAO, *Public-Private Partnerships: Key Elements of Federal Facility and Building Partnerships*, February 3, 1999 <http://www.gao.gov/products/GGD-99-23>, pp. 7, 10, and 16. However the GAO in Report No. GAO-09-283-R noted that the Postal Service had "little incentive to enter into EULs and rarely [did] so in large part because it had more authority than other agencies to sell unneeded property outright and use the proceeds for any mission related purpose. GAO, *Federal Real Property: Authorities and Actions Regarding Enhanced Use Leases and Sale of Unneeded Real Property*, GAO-09-283, February 17, 2009, <http://www.gao.gov/products/GAO-09-283R>, p. 16. Even after taking these comments into account, there are other reasons to use EULs. Leveraging private sector innovation is one such reason. In addition, even though the Postal Service has the legal authority to dispose of excess properties, it faces a number of practical barriers to doing so. Because of these barriers, the Postal Service must consider other options for making efficient use of real property.



**Table 5: Enhanced Use Lease**

Case Study: Yuma, AZ, Desert Proving Ground <sup>24</sup>	
<b>Project Description</b>	<ul style="list-style-type: none"> <li>▪ General Motors (GM) turned unused Army-owned land into a hot weather vehicle test facility for joint GM/Army use.</li> <li>▪ 50-year Enhanced Use Lease of 2,400 acres adjacent to Army's vehicle test facility</li> <li>▪ GM financed, built, and operates new testing facility (\$100 million) on secure Army-owned land.</li> <li>▪ GM provides in-kind maintenance and engineering services in lieu of lease rents.</li> <li>▪ Facility is used by GM and the Army for individual and joint projects.</li> </ul>
<b>Main Business Objectives/Results</b>	<ul style="list-style-type: none"> <li>▪ Army monetizes unused land.</li> <li>▪ Generates operational synergies between GM as a supplier and the Army.</li> <li>▪ Army receives services without tapping into federal funds.</li> <li>▪ GM also benefits from pre-existing, secure environment.</li> <li>▪ Local community benefits — 300 jobs created.</li> </ul>

### ***Infrastructure Financing and Operational Effectiveness***

In many of the most high-profile uses of PPPs, new costly infrastructure is funded by the private sector. To finance a seaport in Baltimore (see Table 6), a private operator retained revenue from the core terminal operations, and therefore had an incentive to develop the business further. In other scenarios, the private party derives its revenues from annual performance-related fees made by the public agency. The fee-for-performance approach requires a detailed definition of the quality indicators and performance targets needed to help the public agency monitor compliance with service level agreements. Such contracts can provide some assurance of effective management of the facility by the private sector.

It should be noted, however, that experts indicate the “financing” component should not be the sole justification of a PPP, since in the long run, private funds usually have higher financing costs. Many other elements are considered in the screening process. These include the public agencies’ recognition that private management would achieve operational gains thanks to the application of specialized know-how. For example, the private sector partner may provide specific marketing, sales, and operational skills that the state agency did not possess. The state agency could provide oversight and governance to enforce a pay-for-performance scheme.

<sup>24</sup> U.S. Army Enhanced Use Lease Program, *Yuma Proving Ground, AZ – Army Enhanced Use Leasing Use and Case Study*, [http://eul.army.mil/YumaGSA\\_Award.pdf](http://eul.army.mil/YumaGSA_Award.pdf), U.S. Army, *Yuma Proving Ground: Yuma, Arizona*, <http://eul.army.mil/ProjectSheets/yuma.htm>, and NCPPP, *Yuma Desert Proving Grounds: Yuma, Arizona*, <http://www.ncppp.org/resources/case-studies/public-safety/yuma-desert-proving-grounds-yuma-arizona/>.

**Table 6: Long-term Lease and Concession**

Case Study: Baltimore Seagirt Marine Terminal <sup>25</sup>	
<b>Project Description</b>	<ul style="list-style-type: none"> <li>▪ 50-year lease and concession to private operator Ports America (Highstar) to operate and maintain a marine terminal.</li> <li>▪ Ports America built a new container berth and funded new construction. It also made a \$100 million upfront cash payment and makes an annual payment to the state; it derives its income from the revenue generated by the Seagirt business.</li> <li>▪ State agency retains ownership and responsibility for security, while private partner keeps revenue from the terminal business.</li> </ul>
<b>Main Business Objectives/Results</b>	<ul style="list-style-type: none"> <li>▪ State should save \$200 million in capital expenditure and \$600 million in operating and maintenance costs over the lifetime of the project.</li> <li>▪ Project is estimated to generate nearly \$16 million per year in new tax revenue.</li> <li>▪ Project created 2,700 one-time construction jobs, plus an estimated 3,000 jobs directly and indirectly through new business.</li> </ul>

### ***Promoting Innovation through Intellectual Property***

PPPs can accelerate the launch of new services and grow a public agency's ability to innovate. The Cooperative Research and Development Agreement (CRADA) is a frequently used tool created in 1986 to allow the private sector to leverage government-owned intellectual property and publicly funded research. CRADAs are used, for example, to allow private firms to commercialize research developed by government-owned national laboratories. The government benefits by collecting direct payments or royalties. In 2009 more than 4,000 such agreements were active across the federal government. NASA plans to increase its use of CRADAs in order to stimulate innovation and commercialization of new technologies.<sup>26</sup>

### ***Lowering the Cost of Capital to Support PPPs***

Since the late 1980s Congress and the federal executive branch have proactively supported the development and implementation of public-private partnerships to finance and build public sector projects. Several federal credit assistance and financing tools encourage states to pursue private participation in transportation infrastructure. At least 32 state governments have established infrastructure banks to support surface transportation projects. The private activity bonds (PABs) program provides private developers access to tax-exempt interest rates, which lower the cost of capital

<sup>25</sup> See Maryland Port Administration, *Seagirt Marine Terminal*, <http://www.mpa.maryland.gov/media/client/terminals/smt.pdf>, and WBAL TV News, *Agreement Brings 5,700 New Jobs to Baltimore Port*, <http://mpa.maryland.gov/media/client/News-Publications/2009/11202009press.pdf>.

<sup>26</sup> NASA, *Plan for Accelerating Technology Transfer at NASA*, October 31, 2012, [http://www.nasa.gov/pdf/709314main\\_NASA\\_PLAN\\_FINAL.pdf](http://www.nasa.gov/pdf/709314main_NASA_PLAN_FINAL.pdf), p. 16.

significantly. The Transportation Infrastructure Finance and Innovation Act (TIFIA) of 1998 established a credit program which secures loans or provides loan guarantees for major transportation PPPs. Numerous state and local governments have used similar tactics.

## Lessons Learned from Foreign Posts and U.S. Agencies

The viability of a PPP is partly driven by industry-specific factors such as trends for long-term demand and the variability of revenue streams. Lessons learned from PPPs in the United States and abroad, however, point to common concerns and success factors which affect the ability to engage potential partners, align public agency stakeholders, and build and oversee sustainable partnerships. Experts warn PPPs should not be pursued solely for short-term financial gain. They often involve higher financing costs and service payments to private sector partners. Consideration of these long term costs should not be obscured by the possibility of an initial financial boost.

Other specific concerns expressed by participants and observers in PPPs include

- Loss of public control and flexibility, by constraining the government's ability to make further policy decisions related to property covered by a PPP.
- Loss of future public revenues, particularly for PPPs relating to toll roads, which have been criticized for trading valuable future toll revenue for upfront payments, potentially short-changing the public sector over time.
- Limited accountability and transparency.
- Concerns about foreign investments in sensitive areas.<sup>27</sup>

Governments can mitigate these concerns through careful preparation and consideration of the tools and factors outlined below.

### ***Dedicating Expert Resources to PPPs***

The preparation and approval of PPPs requires complex coordination between different agencies and levels of government, and a mix of financial, legal, technical, project management, and communications skills. To facilitate these tasks, several U.S. states have established PPP offices as public agencies, government-owned corporations, or advisory boards, primarily in the last few

**Several U.S. states and foreign governments have set up dedicated PPP offices.**

<sup>27</sup> See Fawn Johnson, National Journal, *Why you won't own your road*, Fawn Johnson, National Journal, Oops! Judge slams local public-private deal, May 13, 2013, <http://transportation.nationaljournal.com/2013/05/oops-judge-slams-local-publicp.php>, Charles Chieppo, GOVERNING, *When public-private partnerships are a bad idea*, March 13, 2013, <http://www.governing.com/blogs/bfc/col-public-private-partnership-cincinnati-parking-lease.html> and The Canadian Council for Public-Private Partnerships, *Why Choose PPPs*, <http://www.pppcouncil.ca/resources/about-ppp/why-choose-ppp.html>.

years.<sup>28</sup> Most of these offices are located in the state's department of transportation, as transportation projects are often states' priority area for PPPs. Experience from public agencies indicates that building expertise in PPPs involves a long educational process, in which the role of specialized external PPP consultants decreases over time as in-house skills develop.<sup>29</sup>

The national authorities of at least 40 countries have set up PPP offices.<sup>30</sup> In addition, the European Investment Bank and European Commission launched a European Public Private Partnership Expertise Center to share experiences, expertise, analyses, and best practices among national PPP authorities. The functions of PPP units include policy formulation and coordination, quality control, technical assistance, standardization and dissemination, and promotion of PPPs.<sup>31</sup> Experts who have studied PPPs and strategic alliances, including the Postal Service FedEx alliance, note there are significant benefits from the simple act of maintaining a single list or map of PPPs (and other types of partnerships) for an organization, such as facilitating the coordination of standards and priorities among different functions and sharing best practices.<sup>32</sup>

### ***Value for Money (VfM) Analysis Prior to Executing a PPP Agreement***

Some high-profile PPPs around the world, particularly those involving large infrastructure investments, have allegedly turned out to be poor deals for the public. In some cases the public sector entity avoided initial outlays, but did not adequately assess long-term value or risk, such as paying high interest rates to a private investor. VfM analysis is intended to ensure that the public sector is receiving the best possible value for its investment from a given procurement approach. The tool has been used most often in Europe, but it is used increasingly by American state departments of transportation in evaluating infrastructure PPPs. In a VfM analysis, the public agency compares the life cycle cost of an investment through a traditional procurement, often called a public sector comparator (PSC), with the life cycle costs of pursuing the project through a PPP.<sup>33</sup>

The government scrutinizes the PSC using a discounted cash flow analysis to project the net present value (NPV) of expected cash flows. The discount rate used in this analysis should reflect the government's time value of money in addition to a risk

<sup>28</sup> Brookings-Rockefeller Project on State and Metropolitan Innovation, *Moving Forward on Public Private Partnerships: U.S. and International Experience with PPP Units*, December 2011, [http://www.brookings.edu/~media/files/rc/papers/2011/1208\\_transportation\\_istrerate\\_puentes.pdf](http://www.brookings.edu/~media/files/rc/papers/2011/1208_transportation_istrerate_puentes.pdf), pp. 12-15.

<sup>29</sup> Interview with Richard Norment, Executive Director, NCPPP, October, 31, 2012.

<sup>30</sup> See World Bank Public-Private Partnership in Infrastructure Resource Center, *PPP Units Around the World*, <http://ppp.worldbank.org/public-private-partnership/overview/international-ppp-units>.

<sup>31</sup> Brookings-Rockefeller Project, *Moving Forward on Public Private Partnerships* pp. 6-11.

<sup>32</sup> Dr. Oded Shenkar and decision/analysis partners, personal communication, October 12, 2012.

<sup>33</sup> Federal Highway Administration, *Value for Money for Public Private Partnerships: A Primer*, September 11, 2012, [http://www.fhwa.dot.gov/ipd/forum/vfm\\_for\\_ppps](http://www.fhwa.dot.gov/ipd/forum/vfm_for_ppps); Claire Goldbach, Valerie Goldman, Richard Philips, and Ashlyn Seymour for The National Council for Public Private Partnerships, *Public Cost Comparator for Public-Private Partnerships*, April 2012, <http://www.ncppp.org/wp-content/uploads/2013/03/PS-042711-PublicCostComp-Paper.pdf>, pp.1-2, 6-7; and NCPPP, *Testing Tradition: Assessing the Added Value of Public-Private Partnerships* <http://www.ncppp.org/wp-content/uploads/2013/03/WhitePaper2012-FinalWeb.pdf>, pp. 8-11.

premium for the scope and likelihood of occurrence of risks involved in the project, such as the inflation costs, possible delays, and expected demand.<sup>34</sup> The PSC analysis should take into account the fact that the public sector is taking on more risk than with the PPP approach. The public agency then attempts to calculate the NPV of the PPP option to create an “apples-to-apples” comparison. The expected value of the PPP option is derived in a similar manner to the PSC, while accounting for any risk transferred to the private sector and payments made to the partner.

In addition to carefully quantifying costs, VfM analysis looks beyond the lowest cost bid and helps decision-makers determine value to the public over the lifetime of the agreement. The Postal Service does not formally use VfM analysis, but as a public entity with significant ongoing commercial activities, has access to relatively sophisticated evaluation approaches. Postal Service officials involved in PPPs might consider studying VfM practices as an additional tool for financial analysis. (See Appendix E for additional information on VfM,)

### ***Managing Risk***

Public agencies must build consensus on the levels and types of risk they are ready to transfer to a private partner over the long run. Transferring that risk will not fully shield them from negative external events such as private partners declaring bankruptcy. Agencies also need to convey the message that some government funding may still be needed to complement private financing.

Agencies should develop a good understanding of private partners’ selection criteria for a PPP, and strike a balance between protecting the public interest and ensuring the transaction is executable and financeable. The higher the risk transferred to the private partner, the more difficult the financing of the project. Criteria used by private partners include the level, predictability, and stability of cash flow streams; the impact of new laws or regulations; barriers to entry by potential competitors; ability to introduce process and service innovation throughout the project lifecycle; and the desired minimum rate of return.<sup>35</sup>

### ***Managing Stakeholders***

For PPPs to gain public acceptance, public agencies must address stakeholders’ concerns, which most often revolve around a few key points: loss of public control, generation of excessive private profits at the public’s expense, and questionable value for taxpayers’ money. Such concerns can be addressed partly through careful asset valuation and revenue-sharing agreements in which the public agency receives a portion of ongoing revenues from operations. The public agency also needs to consider

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<sup>34</sup> The idea that money available at the present time is worth more than the same amount in the future due to its potential earning capacity, <http://www.investopedia.com/terms/t/timevalueofmoney.asp>.

<sup>35</sup> See e.g. Laurene B. Mahon, Tom Osborne, “Public-Private Partnership Policy,” UBS, pp. 7,11 (presentation to the State of Maryland, Blue Ribbon Commission on Transportation Funding, January 4, 2011), [http://www.mdot.maryland.gov/Office\\_of\\_Planning\\_and\\_Capital\\_Programming/Blue\\_Ribbon/Documents/Meeting\\_Agenda\\_010411/BRC\\_Summary\\_Document\\_010410.pdf](http://www.mdot.maryland.gov/Office_of_Planning_and_Capital_Programming/Blue_Ribbon/Documents/Meeting_Agenda_010411/BRC_Summary_Document_010410.pdf).

keeping oversight responsibilities over private partners' products (including prices) and performance (through pay-for-performance mechanisms) under the agreement.

In a context in which PPPs are often seen as an easy source of capital, it is also important for public agencies to manage stakeholders' expectations. For example, stakeholders might be overly optimistic that savings in upfront capital costs are sufficient by themselves to justify a PPP.

### ***Managing the Overall PPP Process Effectively***

A well-organized, well-managed process will give potential partners confidence in the public agency's ability to meet deadlines and collaborate effectively over the lifetime of the project. Clear, thorough requests for proposal, design specifications, partnership agreements, and performance targets will ward off delays, frustrations, cost escalation, and disputes over contract execution. In addition, the public agency should have an exit strategy for a PPP, including defined triggers for when to exit, and agreed-upon dispute resolution mechanisms.

## **Future Opportunities for the Postal Service**

Through PPPs, there are real opportunities for the Postal Service to earn income from its real estate portfolio, upgrade its infrastructure, benefit from private sector innovation, and make its cost structure more variable so costs decline with volume. While it is not feasible to identify all the possible PPPs that the Postal Service could develop, a few broad categories stand out as potential high value opportunities.

**Table 7: Classification of Future PPP Opportunities for the Postal Service**

	<b>Cost Reduction</b>	<b>Revenue Generation</b>
<b>Tactical</b>	<ul style="list-style-type: none"> <li>▪ Fleet management</li> </ul>	<ul style="list-style-type: none"> <li>▪ IP licensing &amp; digital partnerships               <ul style="list-style-type: none"> <li>○ Revitalize the Electronic Postmark program</li> <li>○ Leverage website through affiliate agreements</li> </ul> </li> <li>▪ Sale and leaseback of real estate</li> </ul>
<b>Strategic</b>	<ul style="list-style-type: none"> <li>▪ Sale and lease back of real estate</li> <li>▪ Retail partnerships</li> </ul>	<ul style="list-style-type: none"> <li>▪ Real estate business unit</li> <li>▪ Logistics partnerships</li> </ul>

### **Upgrading and Modernizing the Postal Service's Infrastructure**

Postal operators and other public organizations have leveraged PPPs to pursue internal operational improvements in facilities and fleet management. The Postal Service has the opportunity to adapt these partnership models to address needs that have been identified by Postal Service management and several oversight bodies including

Congress, the OIG, and the Government Accountability Office (GAO). These priorities include reconfiguring the Postal Service's processing and retail networks, consolidating administrative offices, and replacing an aging vehicle fleet.

### ***Retail Partnerships***

The Postal Service has attempted several times to rationalize its retail infrastructure with mixed results. Stakeholder opposition and regulatory hurdles have prevented aggressive consolidation. Large-scale use of PPPs is one way to reduce fixed costs while meeting consumer needs for physical retail access. Franchising is an alternative to maintaining or building a chain of postal retail outlets that reduces investment, labor costs, and fixed assets costs. (See Table 3.) Franchising addresses the problem of aligning retail infrastructure and labor costs with declining volumes, shifting the risk of unpredictable changes in volume to private partners. In addition, the Postal Service could accelerate the pace of existing initiatives to provide services through partnerships with private retailers such as grocery stores. These approaches will allow the Postal Service to continue serving all Americans, while realigning its physical retail portfolio to reduce the financial risks and fixed costs of owning retail facilities.

### ***Fleet Management***

The Postal Service has an aging fleet of delivery vehicles and lacks the capital to replace the vehicles. Maintenance costs are increasing. Exploring the market for a sale and leaseback agreement is one avenue for improving the fleet. European postal operators have used this approach to receive immediate cash from the sale of their old fleets, increase the flexibility or variabilization of operational costs for the new vehicle fleet, and obtain the operational benefits of a modern fleet. (See Tables 12 and 13 in Appendix C.) In addition to the sales and leaseback, other forms of leases can reduce fixed costs. In an operational lease arrangement, the Postal Service would obtain as-needed access to modern vehicles and avoid taking on fixed costs (while paying a premium to do so).

### ***Optimizing the Processing Network***

The Postal Service has a nationwide network of more than 400 processing facilities of varying ages and configurations. An OIG study found that the number of processing and distribution centers (P&DCs), the key nodes in the network, could be reduced from over 260 to 135.<sup>36</sup> While most Postal Service initiatives are likely to require shutting down or moving operations among certain existing facilities, optimizing the P&DCs might require building or refurbishing more standardized processing centers in more strategic locations. In the medium to long term, optimization would yield substantial savings, but the Postal Service currently lacks capital, which could hinder its ability to make upfront investments in facility design and construction. PPPs could allow the Postal Service to obtain financing as well as design and building assistance from private partners. In addition, the Postal Service could consider obtaining private sector assistance with certain operations in the optimized network. The current worksharing program is a step

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<sup>36</sup> USPSOIG, *A Strategy for a Future Mail Processing and Transportation Network*, Report No. RARC-WP-11-006, July 6, 2011, [https://www.uspsdig.gov/foia\\_files/rarc-wp-11-006.pdf](https://www.uspsdig.gov/foia_files/rarc-wp-11-006.pdf), pp. i-ii.

in this direction, as it allows private sector entities to perform certain mail processing and transportation activities which they can do more efficiently than the Postal Service.

## **New Products and Revenue Generation**

Through partnerships with private vendors and by utilizing a robust platform business strategy, the Postal Service could develop and market new products and services that reflect an evolving mission to “bind the nation together” in a world where people are increasingly communicating digitally.

### ***The Postal Digital Platform: Innovation and Intellectual Property Partnerships***

As the OIG has written previously, the Postal Service could build two foundational layers that would constitute the building blocks of a postal digital platform: a digital identity and authentication layer and the secure messaging layer (eMailbox), which would link a person or business’s physical address to a digital address.<sup>37</sup>

**The Postal Service can take advantage of its potential as a digital platform through PPPs.**

The Postal Service could invite private sector innovators to build and contribute postal, governmental, and commercial applications on the platform. A number of innovative companies offer solutions that integrate, or could integrate, legacy postal applications and have physical and digital components. Specific opportunities include digital Collect on Delivery (COD) and digital escrow; e-government; identity services such as ID validation and in-person proofing, and digital, hybrid and reverse hybrid mail services.

Intellectual property (IP) could be a central issue as the Postal Service attempts to partner with vendors in the technology arena by licensing its intellectual property to third parties or vice versa. The OIG found in a series of audits that the Postal Service does not manage its portfolio of more than 750 patents to maximize commercial opportunities. A September 2012 paper calls on the Postal Service to “look towards partnerships for co-developing systems and services where IP can be generated and leveraged,” and to monetize its patent portfolio.<sup>38</sup> As a platform sponsor, the Postal Service could license its IP or let private developers build on it to develop services that would generate new revenue streams for the Postal Service.

The nature of the EPM and a brief scan of online market conditions indicate that EPM could be a lucrative example of such a service. The EPM extends the trust and assurance provided by the traditional physical postmark, producing an auditable time-and-date stamp on electronic information. The EPM provides evidence that the content of a document or file existed at a specific date and time, and protects the integrity of the document or file by ensuring that it cannot be altered without detection. Early EPM licensees paid the Postal Service quarterly fees for the right to market the EPM to several large companies, such as utility providers, who were interested in securing bill

<sup>37</sup> USPSOIG, *The Postal Service’s Role in the Digital Age Part 2: Expanding the Postal Platform*, Report No. RARC-WP-11-003, April 19, 2011, [https://www.uspsoig.gov/foia\\_files/rarc-wp-11-003.pdf](https://www.uspsoig.gov/foia_files/rarc-wp-11-003.pdf), pp. 11-13.

<sup>38</sup> John Callan, John Cronin, and Nathan Doudera, “Can Intellectual Property Save the USPS?” *Post & Parcel*, September 2012, <http://postandparcel.info/files/2012/09/Can-Intellectual-Property-Save-the-USPS.pdf>.



presentment and similar communications with customers.<sup>39</sup> There is a large and growing market for ensuring the security of data and transactions on the Internet. E-commerce sales totaled more than \$225 billion in 2012, while worldwide e-commerce sales are over one trillion dollars.<sup>40</sup> Financial service companies, utilities, and consumers continue to move toward online bill presentment and payment. The EPM is a service that the Postal Service could offer to these markets. If the EPM were used for even a small portion of online transactions, the Postal Service and private sector partners could earn significant revenues while providing consumers and citizens with a valued service.

### **Logistics**

The explosion in e-commerce parcels which is flooding postal networks is just one symptom of a global logistics revolution characterized by increasing globalization, dispersed manufacturing, and the need for speed in getting products into the hands of consumers. The global logistics revolution provides great opportunities for the Postal Service — facilitating commerce in this new age requires qualities that are core capabilities for the Postal Service, including ubiquity and efficiency in the first and last mile. Yet, in order to capture all of the opportunities present in this revolution, the Postal Service will need to consider partnering with private sector partners with expertise in logistics issues such as network design, routing protocols, and global trade flows. In such partnerships, the Postal Service could provide pickup in the first mile, delivery in the last mile, storage in postal facilities, and extensive retail access, while private partners could handle online sales, long-haul transportation, information technology services, and technical expertise in logistics planning and warehousing.

### **Real Estate Monetization**

The success of strategies pursued by other postal operators, and the sheer value and size of the Postal Service's real estate holdings, call for consideration of real estate management as a business line in itself with a mission to optimize usage and value creation. Many postal operators have separated the operation of fixed real estate assets

**The Postal Service has real estate holdings with a book value of \$29 billion, with a market value that could be much higher.**

for postal needs from financial asset management, recognizing the latter requires different competencies and justifies a separate business unit. A further step consists of including in the financial performance of the real estate business unit the fair market price of the usage of the fixed assets (transfer prices). The Postal Service has a large portfolio of fixed assets such as real estate, vehicles and technology, which may not be used optimally. Several

recent reports have identified real estate, in particular, as being underutilized. According to a recent GAO report the Postal Service owns more square footage than any civilian

<sup>39</sup> USPSOIG, *Management Advisory – Electronic Postmark Program License Fees*, Report No. MS-MA-10-001, September, 2, 2010, [https://www.uspsig.gov/foia\\_files/ms-ma-10-001.pdf](https://www.uspsig.gov/foia_files/ms-ma-10-001.pdf), pp. 1-3 and 6.

<sup>40</sup> Katie Deatsch, "E-commerce grows 16% in 2012," *Internet Retailer*, February 15, 2013, <http://www.internetretailer.com/2013/02/15/e-commerce-grows-16-2012> and eMarketer, "Ecommerce sales topped \$1 trillion for first time in 2012," <http://www.emarketer.com/Article/Ecommerce-Sales-Topped-1-Trillion-First-Time-2012/1009649>.

federal agency, including the General Services Administration. The Postal Service owns about 8,600 properties, totaling about 200 million square feet of interior space. The OIG estimates that Post Offices have 24 percent excess space, or 67 million interior square feet.<sup>41</sup> Total real estate holdings are worth \$29 billion, based on historical book value.<sup>42</sup> The OIG estimates the market value to be \$85 billion.<sup>43</sup>

Excess space is found in a variety of Postal Service operations. Both the OIG and GAO have identified significant underutilized space in Post Offices and processing facilities.<sup>44</sup> Furthermore, at approximately 80 percent of Postal Service retail facilities, revenues are insufficient to cover costs.<sup>45</sup> Both oversight agencies have suggested that the excess property in retail facilities could support e-government initiatives, retail kiosks and computer terminals, bill payment, and similar revenue-generating operations.<sup>46</sup>

Current market trends and corporate strategies are likely to exacerbate the excess space issue. Mail volume continues to decline, reducing the need for processing, sorting, and retail space. To adjust to declining volume, the Postal Service is undertaking the Delivery Unit Optimization (DUO) initiative. DUO involves relocating letter carriers out of local Post Offices and consolidating them into centralized delivery offices.<sup>47</sup> The existing retail operation will require less space and the office could then be downsized to a smaller space nearby.<sup>48</sup> The Postal Service has consolidated over 1500 facilities since 2011 under DUO.<sup>49</sup>

The Postal Service has the legal authority to pursue a number of strategies to address overcapacity. It is authorized to hold, sell, lease or otherwise dispose of its property.<sup>50</sup> So far, the Postal Service has identified some of its underutilized space and partnered with federal agencies such as the Internal Revenue Service (IRS) to utilize some excess properties; retained a national real estate firm to help with property management; and partnered with a few private and public sector parties to dispose of and/or monetize these assets. While the Postal Service can and should sell excess property, experience has demonstrated that the Postal Service faces practical difficulties in disposing of property, making this strategy infeasible as the sole manner of dealing with excess real

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<sup>41</sup> USPSOIG, *Nationwide Facility Optimization Audit Report*, Report No. DA-AR, 11-009, August 26, 2011, [http://www.uspsoidg.gov/foia\\_files/DA-AR-11-009.pdf](http://www.uspsoidg.gov/foia_files/DA-AR-11-009.pdf).

<sup>42</sup> USPSOIG, *Leveraging Assets to Address Financial Obligations*, Report No. FF-MA-11-118, July 12, 2011, [https://www.uspsoidg.gov/foia\\_files/ff-ma-11-118.pdf](https://www.uspsoidg.gov/foia_files/ff-ma-11-118.pdf).

<sup>43</sup> USPSOIG, *Pension and Retiree Health Obligations Management Advisory Report*, Report No. FT-MA-12-002, June 18, 2012, [https://www.uspsoidg.gov/foia\\_files/ft-ma-12-002.pdf](https://www.uspsoidg.gov/foia_files/ft-ma-12-002.pdf), p. 1.

<sup>44</sup> See, USPSOIG, *Nationwide Facility Optimization*, and GAO, *Federal Real Property: Strategic Partnerships and Local Coordination Could Help Agencies Better Utilize Space*, Report No. GAO-12-779, July 2012, <http://www.gao.gov/assets/600/592992.pdf>, p. 9.

<sup>45</sup> GAO, *Federal Real Property*, p. 8.

<sup>46</sup> *Ibid.*

<sup>47</sup> USPSOIG, *Delivery Unit Optimization Initiative Audit Report*, Report No. MS-AR-13-001, December 6, 2012, [https://www.uspsoidg.gov/foia\\_files/ms-ar-13-001.pdf](https://www.uspsoidg.gov/foia_files/ms-ar-13-001.pdf), p. 5.

<sup>48</sup> *Ibid.*

<sup>49</sup> *Ibid.*

<sup>50</sup> 39 USC § 401(5).

estate under current operating conditions.<sup>51</sup> In order to be proactive in dealing with excess property, rather than waiting for all external barriers to be eliminated, the Postal Service must consider other options such as PPPs.

Some additional real estate related PPPs the Postal Service could consider, where consistent with its overall business strategy and plans for the network, include

- The sale and leaseback of a select portfolio of properties, such as high-value city Post Offices;
- The sale and leaseback of large processing centers where vacant space can be leased for postal-related activities, such as the warehousing of e-commerce packages and print shop operations;
- Leasing space at facilities to telecommunications firms that wish to reach rural consumers without incurring substantial new infrastructure costs;<sup>52</sup> and
- A formal and comprehensive Post Office franchising program as part of a general policy to dispose of owned-and-operated post offices, similar to the programs used by some foreign posts.

According to European postal experts, further development and buildup of the asset management function within the Postal Service and subsequent internal transfer pricing for usage of assets could contribute to improving the financial performance, transparency, and accountability of management.<sup>53</sup> It would also help in assessing the rationale and value of any PPPs involving the sharing of assets. The OIG has recommended that the Postal Service set up policies and systems to identify areas in facilities that are actually usable and suitable for leasing arrangements.<sup>54</sup> This step will help the Postal Service in marketing and monetizing its excess assets.

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<sup>51</sup> See USPSOIG, *Barriers to Retail Network Optimization*, Report No. RARC-WP-11-005, June 9, 2011, [https://www.uspsoidg.gov/foia\\_files/rarc-wp-11-005.pdf](https://www.uspsoidg.gov/foia_files/rarc-wp-11-005.pdf); GAO, *Challenges to Restructuring the Postal Service's Retail Network*, Report No. 12-433, April 17-2012, <http://www.gao.gov/assets/600/590170.pdf>; and GAO, *Federal Real Property*. Some observers have advocated an approach which focuses only on selling unneeded facilities, but the OIG and GAO reports and several historical experiences suggest this is unlikely to result in aggressively rationalizing postal networks under the current policy and political framework. For a concrete example, the Postal Service recently deployed the POST plan, which involves reducing the hours of retail facilities which generate little revenue, after stakeholder resistance to closing such facilities. While the POST plan is expected to save money, it actually reduces real property utilization by definition. If stakeholder views are going to influence such strategic decisions, then a realistic approach to real estate management should take this into account, rather than being designed in a vacuum, with the potential for rapid abandonment when faced with significant opposition.

<sup>52</sup> See USPSOIG, *21st Century Post Office: Aligning with the National Broadband Infrastructure Initiative*, Report No. DA-MA-12-2012, January 23, 2012, [http://www.uspsoidg.gov/foia\\_files/DA-MA-12-002.pdf](http://www.uspsoidg.gov/foia_files/DA-MA-12-002.pdf), which recommends that the Postal Service partner with federal agencies and private sector Internet Service Providers to host broadband infrastructure, particularly for the provision of broadband in unserved and underserved rural communities through Wi-Fi hotspots.

<sup>53</sup> Analysis of Hans Boon and decision/analysis partners.

<sup>54</sup> USPSOIG, *Nationwide Facility Optimization*, pp. 2-4.

## Conclusion

The Postal Service can take advantage of PPPs to address many of its short and long-term problems. PPPs can reduce costs and make them more variable so they decline with volume, and allow the Postal Service to leverage the skills of partners to help the Postal Service meet its mission of binding the nation together, even as that mission requires more technological capabilities. While the Postal Service has engaged successfully in several PPPs, there is room for improvement. Foreign postal operators and other government agencies in the U.S. have used PPPs for long-term infrastructure financing, cost containment, and public policy needs. The experiences of the Postal Service and these other public sector organizations have shown that by following a set of best practices, public agencies can improve the likelihood of success with PPPs. Chief among these lessons is the value of establishing a high-level, centralized PPP office to champion and standardize best practices, and to build up the skill sets necessary to negotiate and implement PPPs.

## Appendix A PPP Definitions and Typologies

NCPPP definition: “[A] contractual *agreement* between a public agency (federal, state or local) and a private sector entity. Through this agreement, a certain range of *skills and assets of each entity (public and private) are shared* in delivering a *service or facility* for the general public. In addition to sharing resources, each party *shares in the risks and rewards* potential in the delivery of the service and/or facility.”<sup>55</sup>

The NCPDP definition puts the emphasis on the “sharing” dimension. As a result

- The traditional procurement for goods and services, which does not involve the sharing of assets or risks, is excluded, as is outright privatization of a public asset, which does not involve any sharing.<sup>56</sup>
- Outsourcing, while close to traditional procurement of services, involves the “sharing” of a company’s function; the private partner therefore assumes part of a significant business and operating risk. For this reason, outsourcing is generally considered a form of a PPP. In this respect, postal worksharing, which entails the sharing with business mailers (or presort companies) of upstream mail preparation/transportation/sorting tasks and risks that would otherwise have been borne by the post, is a variation of the outsourcing model. To some extent, workshare prices and eligibility requirements, as set out for each mail product in the Domestic Mail Manual (DMM), are equivalent to the “contractual agreement” referred to in the definition.

A portion of this definition is problematic: the requirement that the service or facility be destined “for the use of the general public,” (unless this requirement is intended to refer to the public interest). Seaports, one of the main areas of PPPs, are mostly used by freight shipping companies. The GAO’s definition of a PPP refers to a “public service” and this reference might be more appropriate.<sup>57</sup>

### PPP Typologies

Any PPP can be described in terms of four basic components:

- 1) **Scope:** What are the assets shared between partners (equipment, skills, buildings, IP, technology)? Is it a new facility/public service or an existing one, which needs to be restructured or modernized?
- 2) **Project delivery mix:** Who designs or develops/builds/upgrades/renovates? Who operates, manages, and maintains? Who sets or oversees rates, prices, and quality?

<sup>55</sup> Norment, *The Framework of Public Private Partnerships*, p. 5.

<sup>56</sup> Although it could be argued that a fully-privatized designated postal operator is still entrusted with universal service obligations (and in many cases obligations to perform services of general interest) on behalf of the State. This could be seen as a form of PPP.

<sup>57</sup> GAO, *Key Elements*, pp. 1, 5.

- 3) **Project funding mechanism:** Who finances the upfront cost or capital expenditure? The public agency, private partner, or both?
- 4) **Revenue model:** Who collects and retains the revenue generated by the asset? How are financial flows shared? What payments does the public agency make to the private partner (such as “availability payments” to cover operating costs)? Are payments performance-related?

There are several terms and acronyms used to describe PPPs. The majority of them simply reflect different combinations of the categories above, and variations thereof.

Most of these models can be related to two basic typologies.

- According to the scope of the tasks assumed by the private partner: D(esign), B(uild), (O)perations, (M)aintenance, F(inancing). This typology was designed for infrastructure projects. Two additional dimensions are often considered -- (O)wnership of the facility (when the private sector owns the facility being built), and (T)ransfer of ownership — when the contract provides for return of operational oversight to the public partner at a given point in time.
- According to the type of business or legal arrangement between partners: outsourcing (including facilities management), franchising, agency agreements, (long-term) lease, strategic partnership, joint venture, and concession.

Other terms found in the literature to describe PPPs are mostly variations of the above typologies (or a mix of the two, such as “Lease-Own-Operate”). Definitions of the most frequent PPPs are given below.

**Table 8: Typology of PPPs According to the Tasks Assumed by the Partner<sup>58</sup>**

DB (or turnkey)	Design – Build	A two-phase procurement method in which a single contract is executed for design and construction services. The private developer commits to build the facility for a fixed price and absorbs the construction risk of meeting that price commitment. With a DB delivery approach, construction can begin prior to completing all design details.
DBO(M)	Design – Build – Operate – (Maintain)	A single contract for the entire project with financing secured by the public agency, under which the contractor provides long-term operations (and maintenance services) for a specified period of time meeting specified performance requirements. The private entity thus bears the commercial risk of operating the facility. The public agency retains financial risk.
O&M	Operations and Maintenance	Public entity transfers to a private partner operations and maintenance of an existing facility
DBFO(M) or BOT	Design – Build – Operate – Finance – (Maintain)	DBFOM (as well as DBF and DBFO) are variations of the DB and DBOM methods for which the private partner provides some or all of project financing. The public sector agency retains ownership of the facility. Transfer at the end of contract may take place at a pre-set price or at then- prevailing market price.
DBFM	Design – Build – Finance – Maintain	In this model, the private sector takes the construction and financing risks, but not the operating risk: revenue generated by the facility or service is returned to the public agency.
BOOT	Build – Own – Operate-Transfer	Design, construction, operation, and maintenance are the responsibility of the contractor, who also owns the facility and retains all operating revenue risk and surplus revenue for the life of the facility. BOO therefore is a form of privatization. The BOOT method is similar, but the infrastructure is transferred to the public agency after a specified time period.

<sup>58</sup> Deloitte Research, *Partnering for Value: Structuring effective public-private partnerships for infrastructure*, 2010, downloaded from <http://www.deloitte.com/partneringforvalue#> on March 22, 2013, p. 19, AECOM, KPMG; Nossaman, *Discussion Materials* (Day 1 presentation to the Washington JTC P3 Educational Workshop), downloaded from <http://www.leg.wa.gov/JTC/Pages/PublicPrivatePartnershipsStudy.aspx> on May 22, 2013, August 2, 2011, pp. 31-45; and FHWA, *User Guidebook on Implementing Transportation Infrastructure Public-Private Partnerships in the United States*, July 7, 2007, [www.fhwa.dot.gov/ipd/pdfs/ppp\\_user\\_guidebook\\_final\\_7-7-07.pdf](http://www.fhwa.dot.gov/ipd/pdfs/ppp_user_guidebook_final_7-7-07.pdf), pp. 12-15.

**Table 9: Typology of PPPs According to Legal and Business Arrangements**

<p><b>Outsourcing (and facility management)</b></p>	<p>Outsourcing is a partnership whereby the public entity contracts a partner to delegate a part of its operation or a business function. This is frequently applied in the postal sector for non-core functions or for specific parts in the postal process. Outsourcing can be arranged on short notice and does not require investments on the part of the postal operator.</p> <p>Facility management relates specifically to the outsourcing of a non-core function relating to</p> <ul style="list-style-type: none"> <li>▪ <i>Space and infrastructure:</i> planning, design, workplace, construction, lease, occupancy, maintenance, furniture, cleaning, etc.</li> <li>▪ <i>People and organization:</i> catering, IT, health care, accounting, marketing, hospitality, etc.</li> </ul> <p>In the postal sector it is frequently applied by operators in both developing and developed countries for support functions such as security, technical maintenance and catering. This reduces the level of fixed labor costs, allows the engagement of specialized professionals, and allows the postal operator to focus on its core business functions. Other areas are IT (call centers and data processing), accounting and payments processing, and back office functions for specific products.</p>
<p><b>Franchising<sup>59</sup></b></p>	<p>A franchise agreement is a legal arrangement or license between two independent parties which gives</p> <ul style="list-style-type: none"> <li>▪ A person or group of people (franchisee) the right to market a product or service using the trademark or trade name of another business (franchisor);</li> <li>▪ The franchisee the right to market a product or service using the operating methods of the franchisor;</li> <li>▪ The franchisee the obligation to pay the franchisor fees for these rights;</li> <li>▪ The franchisor the obligation to provide rights and support to franchisees.</li> </ul> <p>“Business format franchises” are the most common type of franchising; they not only use a franchisor’s product, service, and trademark, but also the complete method to conduct the business itself, such as the marketing plan and operations manuals.</p> <p>The types of franchise arrangements available to a business owner comprise single-unit (direct-unit) franchises (an agreement where the franchisor grants a franchisee the rights to open and operate one franchise unit), and multiple-unit franchises (area development franchises, master franchises).</p> <p>Franchising of post offices is a form of partnership with the private sector that is increasingly common among postal operators. It can help the postal operator reduce fixed personnel costs, and promote a more entrepreneurial, client-focused approach.</p>

<sup>59</sup> See detailed definitions at International Franchise Association, “What is a franchise?” <http://franchise.org/franchiseesecondary.aspx?id=52625>.



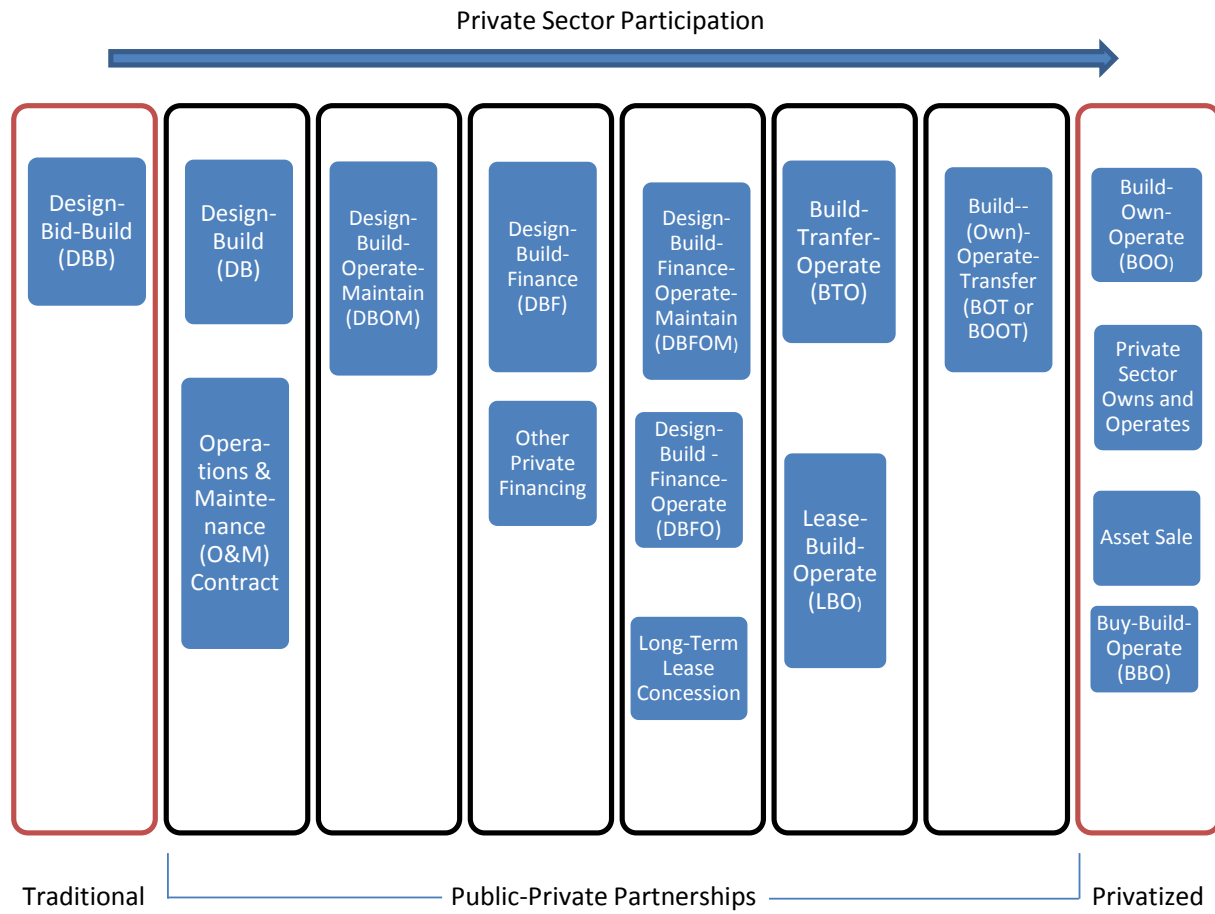
Table 9 (Cont.)

<p><b>Agency agreements</b></p>	<p>Manufacturers and suppliers of goods frequently appoint agents to act on their behalf to grow sales. A formal agreement is usually signed setting out the commission the agent will receive, the territory, duration, and other terms on which the principal and agent will do business together.</p> <p>An agent should be distinguished from a distributor, who will buy stock from the supplier and then sell it on to his customers at a mark-up, whereas an agent will find customers for the supplier, who then sells direct to the customers and pays commission to the agent.</p> <p>Agency agreements are widely used by postal operators as a first step of partnership, with the private sector distributing and selling products through the postal retail network. The agency agreement is a relatively simple arrangement and provides the postal operator variable fee income. One can see agency agreements in at least 100 countries addressing, for example, remittances, mobile telecom, consumer finance, insurance, and securities. Agency agreements are a type of partnership that support commercialization of postal operators and help to fill in spaces in the market and to reduce time to market.</p>
<p><b>Leasing agreements</b></p>	<p>The most frequent leasing PPPs are:</p> <p><u>Tax-exempt lease</u></p> <p>A public partner finances capital assets or facilities by borrowing funds from a private investor or financial institution. The private partner generally acquires title to the asset, but then transfers it to the public partner either at the beginning or the end of the lease term. The portion of the lease payment used to pay interest on the capital investment is tax-exempt under state and federal laws. Tax-exempt leases have been used to finance a wide variety of capital assets, ranging from computers to telecommunications systems and municipal vehicle fleets.</p> <p><u>Lease/Purchase</u></p> <p>A lease/purchase is an installment-purchase contract. Under this model, the private sector finances new equipment (such as computer systems) or facilities, which it then leases to a public agency. The public agency makes scheduled lease payments to the private party. The public agency accrues equity in the facility/equipment with each payment. At the end of the lease term, the public agency owns the facility or purchases it at the cost of any remaining unpaid balance in the lease.</p> <p><u>Sell and lease back (SLB)</u></p> <p>The public sector first sells assets, then leases them (or new, upgraded assets) from the private sector. This method provides a one-off cash injection (the proceeds from the sale) and thereby frees up capital to fund capital expenditure or for reallocation to core activities. It allows for a conversion of fixed costs and assets to variable costs, which can be scaled according to the size of the business operation. Tax benefits are realized by offsetting lease costs as an operating expense. The seller remains in day-to-day operational control of the property.</p> <p>Leasing of assets is an option for postal operators to reduce their needs for financing capital expenditure and costs related to fixed assets (depreciation). For postal operators this can be an attractive solution for vehicle fleets, and equipment such as sorting machines. Leasing can be seen as a partnership supporting sustainability of the main value chain components and adding to performance improvement.</p> <p><u>Enhanced Use Leasing (EUL)</u></p> <p>An asset management program enabling the public agency to long term lease state-</p>

Table 9 (Cont.)

	<p>owned property to the private sector for other uses than for its original mission, “in return for receiving fair consideration that enhances the agency’s original mission or programs.” In this case, contrary to the previous example, the owner is the public agency.</p>
<b>Strategic partnerships</b>	<p>A strategic partnership is a formal alliance between two commercial enterprises. It usually consists of one or more business contracts, and combines resources to create significant and sustainable value for both parties, to improve the value chain, or create economies of scale and scope. Strategic partnerships fall short of forming a legal partnership or corporate affiliate relationship.</p> <p>Strategic partnerships are increasingly seen in the postal sector’s more competitive business areas, for instance in courier and express markets, where national operators have developed strategic partnerships with global or regional operators. In the financial services area, strategic partnerships have been developed with a focus on distribution of third-party products via the postal retail network.</p>
<b>Joint ventures</b>	<p>Joint ventures appear as a step beyond strategic partnerships, where partners confirm their commitment to cooperate by creating a partnership or conglomerate designed to share risk or expertise, e.g., assets, investments, management and revenues. Parties agree to develop, for a finite time, a new entity and new assets by contributing equity. They exercise control over the enterprise and consequently share revenues, expenses and assets.</p> <p>Joint ventures are a more comprehensive type of partnership that move postal operators forward in commercialization, reducing time to market for new services and improving performance.</p>
<b>Long-term lease agreements/ concession</b>	<p>Under this model, publicly-owned facilities are leased to private sector concessionaires for specified time periods. The private operator usually collects and retains revenue. Concession agreements establish and regulate rates (e.g., toll rates in the case of a highway), and may cap the return on investment for the concessionaire.</p> <p>A frequent variation of concessions is a management contract: the operator will collect the revenue on behalf of the government but will not keep it, and will be paid an agreed fee (availability payment).</p> <p>Few postal operators around the world are operated on a concession or management contract basis, whereby the government remains the ultimate owner and appoints a contractor to manage the operation. LibanPost, Lebanon’s postal operator, operated by a private sector concessionaire, is one of them. Concessions can be seen as a form of integrated partnership to ensure sustainability, business continuity, and improved performance.</p>

**Figure 1: PPPs along a Continuum of Private Sector Involvement**



Source: National Council of State Legislatures<sup>60</sup>

<sup>60</sup> Jaime Rall, James B. Reed, and Nicholas J Farber, *Public-Private Partnerships for Transportation: A Toolkit for Legislators*, October 2010, <http://www.ncsl.org/documents/transportation/PPPTOOLKIT.pdf>, p. 4.

## Appendix B U.S. Postal Service Use of PPPs

The Postal Service has a long history of engaging in partnerships with the private sector. The Postal Service uses fixed price contracts and revenue-sharing (performance-based) contracts to determine compensation, with an increasing reliance on the latter method. Revenue-sharing agreements alone generate over \$2 billion a year in postage and other revenues.<sup>61</sup> In such agreements, the Postal Service normally oversees branding and contract governance, while the private sector partner takes the lead on operational and marketing issues.

Many Postal Service partnerships discussed here are close to the boundary of our formal definition of PPPs, as they involve Postal Service efforts to use partners as force multipliers or to reduce its own expenditures, similar to an outsourcing arrangement or even a traditional procurement. Because most initiatives in this paper involve production of Postal Service-branded services (such as the sale of postage at grocery stores or online postage through the PC Postage program) and the parties work closely together to establish frameworks and standards, such programs involve some shared resources and shared risk that distinguish PPPs. Thus, we include in the paper discussion of some programs that may blur the line between PPPs and other types of procurement.

The Postal Service attempted to create a standardized approach to PPPs in 2006 by publishing internal guidelines on the use of “strategic alliances” to achieve business objectives. The 2006 guidelines define a strategic alliance as a cooperative arrangement between the Postal Service and a private entity to share property and personnel in developing a joint product or service,” similar to the NCPPPs definition of PPPs.<sup>62</sup> This definition includes cost savings strategies or devices. These alliances can allow Postal Service partners to use tangible or intangible Postal Service property, or Postal Service personnel. The guidelines include requirements to perform formal financial analyses to determine the expected return on investment, including cost estimates, market valuation, revenue projections, and risk identification and analysis.

In 2011, the Postmaster General issued updated guidance to the marketing department with the intent of streamlining the complex, multistep stage gate process outlined in the 2006 guidelines, which required several approvals by high-level executives. The updated guidance requires partnership sponsors to notify the Postal Service’s executive leadership team of impending alliances; to seek clearance from legal personnel; obtain certification from financial experts that cost coverage requirements will be met; and seek advice from other relevant stakeholders. The OIG found, however, that the new guidelines were not disseminated widely throughout the

**The Postal Service has attempted to standardize PPP practices, but does not adhere to a single organization-wide set of standards.**

<sup>61</sup> USPSOIG *Revenue Sharing Agreements*, p. 1.

<sup>62</sup> U.S. Postal Service Handbook F-66, *Investment Policies and Procedures – Business Initiatives, Alliances, Real Estate Development, and Major Expense Investments*, February 2006.

organization, and some offices were following even older procedures than the 2006 guidelines.<sup>63</sup>

**Table 10: Classification of Present and Past Postal Service PPPs**

	Cost Reduction	Revenue Generation
<b>Tactical</b>	<ul style="list-style-type: none"> <li>▪ Contract Postal Units</li> <li>▪ Village Post Offices</li> <li>▪ Electronic Postmark</li> <li>▪ PC Postage</li> </ul>	<ul style="list-style-type: none"> <li>▪ Hybrid Mail</li> <li>▪ Electronic Postmark (general licensing agreements)</li> <li>▪ PC Postage</li> <li>▪ Non-technology licensing and affiliate agreements</li> <li>▪ gopost™ parcel lockers</li> </ul>
<b>Strategic</b>	<ul style="list-style-type: none"> <li>▪ Energy Savings Performance Contracts</li> <li>▪ Worksharing</li> </ul>	<ul style="list-style-type: none"> <li>▪ Cooperation with FedEx and UPS (Parcel Select and other programs)</li> </ul>

The following is a non-exhaustive overview of Postal Service PPP initiatives.

## Retail Facilities

The Postal Service operates more than 31,000 retail facilities. One of the strongest business imperatives for the Postal Service is to align the retail facilities with changes in demand, as mail usage declines and customers move to alternative access channels such as usps.com. Yet the Postal Service must continue to meet its obligation to provide universal service to all Americans. The Postal Service's retail PPPs are aimed at balancing these critical requirements.

### **Contract Postal Units**

In addition to retail facilities operated by the Postal Service, services are offered through other approved postal providers. Contract Postal Units (CPUs) are retail facilities operated by a private entity and staffed by nonpostal personnel. They are typically located in commercial retail facilities such as grocery stores and gas stations. CPU operators are compensated using two main models: either fixed-price contracts, or revenue-sharing arrangements in which the supplier keeps a share of the funds generated from the sale of postage products. CPUs must follow design requirements related to available space in the stores, in-store signage and displays, and related matters. There are approximately 3,600 CPUs.

The Postal Service also engages in more narrowly focused partnerships with thousands of suppliers. The Approved Shipper program offers services through businesses that

<sup>63</sup> USPSOIG, *Revenue Sharing Agreements*, p. 8.

focus on packaging and shipping services.<sup>64</sup> In addition, 64,000 supermarkets, pharmacies, and other stores sell postage stamps.<sup>65</sup>

### ***Sale and Leaseback***

Many Postal Service retail facilities are in historic buildings or otherwise valuable locations. In some situations, the Postal Service must unload excess capacity but retain a Postal Service-operated retail presence. On other occasions, local stakeholders wish to maintain the building itself while continuing to access postal services at the location. The Postal Service has developed creative partnerships to address these situations, including sale and leaseback agreements. In a sale and leaseback deal, an organization sells an asset to another party but retains access to it by leasing the asset from the buyer. The tactic provides immediate capital to the seller while permitting continued use for the asset's original purpose or for expanded uses.

In Urbana, Illinois, a nonprofit group executed a sale and leaseback agreement with the Postal Service to provide community access to a historic Post Office building. The nonprofit group purchased the retail facility from the Postal Service and used it for a community center aimed at hosting children after school and for programs aimed at closing the digital divide. The nonprofit group leases a portion of the facility back to the Postal Service at no cost for use as a postal retail location.

### **Technology Innovation Partnerships**

Several Postal Service PPPs leverage the ability of private sector vendors to innovate and provide new services for consumers. These partnerships help the Postal Service provide services that are congruent with, yet also modernize, the Postal Service's mission, while allowing the Postal Service to focus on its core competencies in mail delivery and infrastructure.

### ***PC Postage***

PC Postage is the trade name for the Postal Service's program that allows customers to print postage from a personal computer, rather than purchasing a stamp and affixing it to a mail piece. The postage includes several features to ensure its authenticity, providing assurance that revenue is being collected properly. While mailers can purchase digital and print postage directly from the Postal Service using the Click-N-SHIP feature on the usps.com website (which is operated by a private company in an outsourcing arrangement), several licensees sell the services directly to businesses or households. Licensed vendors include Stamps.com, Endicia, eBay, and Pitney Bowes. The program uses a revenue sharing approach in which postage revenue is sent to the Postal Service.

The PC Postage program is among the most successful and high profile partnership programs employed by the Postal Service. The program provides convenience to

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<sup>64</sup> GAO, *Action Needed to Realize Cost-Saving Potential of Alternatives to Post Offices*, Report No. GAO-12-100, November 2011, <http://www.gao.gov/assets/590/586334.pdf>, p. 12.

<sup>65</sup> U.S. Postal Service, *2012 Form 10-K*, November 15, 2012, <http://about.usps.com/who-we-are/financials/10k-reports/fy2012.pdf>, p. 16.

customers, and avoids the costs associated with selling physical stamps at retail facilities. A related customized postage program offers customers the opportunity to personalize their postage by supplying images of their choosing such as photos of themselves, family members, or pets. Stamps.com (through its PhotoStamps.com website) and Pitney Bowes (through a partnership with Zazzle.com) offer versions of customized postage. Some PC Postage vendors have partnered with providers of productivity software applications, integrating their postage services into applications such as word processing and address management software, providing convenience for end users. PC Postage vendors also have agreements with third party e-commerce sites that allow the PC Postage vendors to offer back-end postage solutions, while consumers interact with the e-commerce site on the front end.<sup>66</sup> This approach extends the reach of the Postal Service by leveraging the efforts of its partners to find postage buyers, without additional Postal Service expenditures.

## Coopetition

Coopetition is a business buzzword that refers to normally competing firms that look for ways to cooperate with each other, rather than compete head-to-head for business. There are a number of Postal Service current partnership programs with its major competitors. The Postal Service acts as a “last mile” partner for both UPS and FedEx, handling thousands of deliveries through the Parcel Select program, which is increasingly significant in the logistics and e-commerce space. Because the Postal Service is the most efficient provider to the last mile, the program lowers the total costs of package delivery for shippers, and ultimately consumers. Similarly, the Postal Service leverages the abilities of FedEx and UPS to provide service in the first and middle mile or through their large airline fleets. FedEx also provides international logistics for the co-branded Global Express Guaranteed service.

UPS recently introduced a program that allows customers of participating retailers to return merchandise by dropping it in any Postal Service mailbox, or at any Post Office. After a return package is dropped off at a Postal Service location, a UPS driver picks it up and the UPS ground network transports it back to the retailer. The Postal Service and UPS also have a partnership to reduce solid waste and greenhouse gases called “Blue and Brown Makes Green.” GHG reductions will come from increased last mile deliveries of UPS packages by Postal Service drivers and air freight consolidation on UPS planes.

## Real Estate Leases

The Postal Service owns 198 million square feet of active building space, excluding land and unused office space, including about 420 processing centers and plants, and 8,600 retail outlets.<sup>67</sup> As recently noted by the GAO, declining mail volume and operational changes have freed space in many facilities. The Postal Service is authorized to sell,

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<sup>66</sup> Stamps.com, *2010 Annual Report*, March 15, 2011, <http://files.shareholder.com/downloads/stmp/2479805871x0xS1144204-11-14915/1082923/filing.pdf>, p. 3-4.

<sup>67</sup> GAO, *Strategic Partnerships*, p. 5, and U.S. Postal Service, *2012 Form 10-K*, pp. 16-17.

lease, or dispose of property and is exempt from most federal laws dealing with real property and contracting.

In the mid-1980s, the Postal Service implemented PPPs with private developers in New York City and San Francisco to monetize prime real estate. In both cities, the Postal Service leased out space in historic properties in desirable downtown locations to private developers.<sup>68</sup> The developers then built additional commercial facilities on top of and next to the old postal facilities, and leased space in the new and historic buildings to other companies. The Postal Service continued to offer retail services out of a portion of the facilities. The developers were responsible for operating and subleasing the commercial portion of the facilities, and dealing with relevant regulations.<sup>69</sup> The GAO described the PPPs in favorable terms, referring to the San Francisco partnership as “lucrative for the Postal Service”.<sup>70</sup> The Postal Service earned millions of dollars in lease payments and used contractual provisions to transfer some of the project risks to the private developers.<sup>71</sup>

## Other Partnerships and Contractual Arrangements

The Postal Service has deployed a variety of partnership models with some success, but they have not become core programmatic approaches for the organization. Other successful initiatives, such as worksharing, have impacts similar to PPPs, although they also have elements similar to traditional procurement and are rarely discussed as PPPs.

### ***Sustainability Partnerships***

The Postal Service and other federal agencies use energy savings performance contracts (ESPCs) to privately finance improvements in energy efficiency that would otherwise not be financed (if at all) through appropriations, or in the case of the Postal Service, from revenues.<sup>72</sup> Under an ESPC, the Postal Service or other agency enters into a long-term contract (up to 25 years) with a private energy service company under which the company initiates energy efficiency measures using private funds.<sup>73</sup> The Postal Service then repays the contract out of the estimated annual savings. The Postal Service benefits through obtaining private sector expertise with no upfront costs. The Postal Service has reduced its reliance on such contracts in recent years because it has more legal flexibility than other agencies to shift funds to capital expenditures, and thus avoid the additional long-term financing costs of an ESPC.<sup>74</sup> The shared savings model, however, could be replicated in other areas where the Postal Service wants to avoid an upfront capital investment, and might be considered by the Postal Service as a vehicle

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<sup>68</sup> The Postal Service still owns the New York Grand Central Station Post Office building, and uses it for retail activities. In San Francisco, the air rights for the Rincon center were divided into three parcels, one of which is still owned and is in use for postal retail activities.

<sup>69</sup> GAO, *Key Elements*, p. 47-55.

<sup>70</sup> *Ibid.*, p. 53.

<sup>71</sup> *Ibid.*, pp. 50, 53.

<sup>72</sup> GAO, *Energy Savings: Performance Contracts Offer Savings, but Diligence is Needed to Protect Government Interests*, Report No. GAO-05-340, June 2005, <http://www.gao.gov/assets/250/246803.pdf>, p. 8.

<sup>73</sup> *Ibid.*, p. 2.

<sup>74</sup> GAO, *United States Postal Service: Urgency Needed to Address Aging Delivery Fleet*, Report No. GAO-11-386, May 2011, <http://www.gao.gov/assets/320/318032.pdf>, footnote 62.



for providing services to other government agencies. In addition, the current capital shortage could prompt reconsideration of ESPCs themselves.

## Appendix C Foreign Posts and PPPs

This Appendix reviews several types of partnerships among foreign posts according to their strategic intent.

**Table 11: Classification of Foreign Post PPPs**

	Cost Reduction	Revenue Generation
<b>Tactical</b>	<ul style="list-style-type: none"> <li>▪ Retail financial services</li> </ul>	<ul style="list-style-type: none"> <li>▪ Innovation (digital)</li> <li>▪ Retail financial services</li> </ul>
<b>Strategic</b>	<ul style="list-style-type: none"> <li>▪ Vehicle fleet leasing</li> <li>▪ Retail estate management</li> </ul>	<ul style="list-style-type: none"> <li>▪ Retail network partnerships</li> <li>▪ Innovation (digital)</li> </ul>

### Monetizing and Variabilizing Fixed Assets

Most postal operators are endowed with a large portfolio of fixed assets, such as land, buildings, vehicles, and equipment. As a result of changes in postal technology and business processes, a portion of these assets is no longer relevant, functional or adding value to operations. Other parts of the assets have exceeded their economic or technical life; while others are not fully usable due to market and organizational changes.

Fixed assets continue to create fixed costs such as depreciation, maintenance, and overhead, and add to operations expenditure. Fixed assets that cannot be adapted to fluctuations in business volume then become a burden.

For several reasons disposal of redundant or irrelevant assets is not always feasible in the postal sector when parts of existing premises are underutilized. Often the legal and institutional framework applicable to the public postal operator does not allow using fixed assets as collateral for corporate finance to attract capital to modernize or improve the business, or to modernize and upgrade the assets. The nature of business for today's postal operators does not always require full ownership of all fixed assets: business objectives can be achieved through enforceable contracts.

In the postal sector, the fixed asset turnover ratio provides insight into the actual usage of non-current assets. The ratio is 3.54 for the Postal Service based on 2012 figures. This ratio is higher than, for example, the ratio for La Poste (France) at 3.05 and much higher than Correos (Spain) at 1.30. The ratio of the Postal Service is slightly lower than bpost's (Belgium) with 3.85 and the UK's Royal Mail with 4.34, but much lower than Poste Italiane with 6.17, Deutsche Post with 8.13, or PostNL with 9.47.<sup>75</sup>

<sup>75</sup> Fixed asset turnover is a financial ratio that measures the efficiency of a company's use of its fixed assets in generating sales revenue or sales income to the company. It appears as a relevant ratio in this study for

Nearly all European postal operators have or have had one or more partnerships with the private sector to increase usage of the fixed assets, improve liquidity and capital resources, and facilitate the conversion of fixed assets (and fixed costs) into variable costs related to, and adaptable to, business volume. As they transform into leaner organizations, international practice shows there is still ample room for partnerships that add new services or operations to increase labor productivity; increase the use of non-current assets to optimize asset turnover; convert existing non-current assets through disposal and lease or leaseback of equipment, buildings or technology; and leverage the value of non-tangible assets of the postal operator (brand, intellectual property, marketing databases, and ongoing business relations) through partnerships inside and outside the country of operation.

### **Vehicle Fleet**

The Postal Service manages the world's largest civilian vehicle fleet, composed of about 213,000 owned vehicles that primarily support mail delivery. This fleet includes about 142,000 right-hand drive long-life vehicles (LLVs). The expected service life of the LLVs is 24 years, and they are now between 19 and 26 years old. The OIG has found it costs more to maintain some of the older LLVs than it would to purchase new vehicles.<sup>76</sup> The OIG has also recommended that the Postal Service deploy electric vehicles in urban areas.<sup>77</sup> Postal Service management has developed plans to purchase new vehicles, but the Postal Service's shortage of capital has prevented implementation.

**Table 12: Vehicle Fleet Management Strategies**

Management consultancy or interim management or internal task force	Strengthen the vehicle fleet management capacity, skills and insights with private sector practices of commercial fleet management. Fleet management transforms from a technical function focused on operations management to a complete business management function operating as a service to the business units needing the vehicles, fuel, staff and maintenance.
Sale and leaseback	Portions of the vehicle fleet are sold through a new or already established lease company; a special legal entity or other structure can be used. In addition to the sales and leaseback, other forms of leases can be used, varying from financial lease to full operational lease. In the latter case, many of the functions of vehicle fleet management can be transferred to the private sector (garages, parking lots, vehicle maintenance facilities, etc.).
Outsourcing	Portions of the collection and delivery transport could be outsourced. This step goes well beyond a "traditional" equipment lease. To further enhance the flexibility of available vehicles, several postal operators subcontract part of the operations to individuals and small local firms, whom they entrust with the collection or delivery of mail or parcels on certain days.

benchmarking in the postal industry, more than profit related ratios, although caution is required because the principles of valuation of the fixed assets may differ significantly. Fixed asset turnover ratio analysis by Hans Boon and decision/analysis partners based on postal data.

<sup>76</sup> USPSOIG, *Audit Report – Delivery Vehicle Replacement Strategy*, Report No. DA-AR-10-005, January 16, 2010, [https://www.uspsoidg.gov/foia\\_files/da-ar-10-005.pdf](https://www.uspsoidg.gov/foia_files/da-ar-10-005.pdf), pp. 1 and 5-8.

<sup>77</sup> USPSOIG, *Audit Report – Delivery Fleet Strategies*, Report No. CI-AR-12-006, [https://www.uspsoidg.gov/foia\\_files/ci-ar-12-006.pdf](https://www.uspsoidg.gov/foia_files/ci-ar-12-006.pdf), p. 13.

In light of the OIG's recommendations to replace part of the fleet with modern vehicles, it may be helpful to outline the strategy foreign posts use to involve the private sector in the management of their fleet; options are indicated in Tables 12 and 13.

The evolution of private sector participation in vehicle fleet management and operations has led to situations where many or all of the posts' light duty delivery vehicles (mainly minivans) are leased from private lease companies as a service and/or contracted out to private sector companies. Large trucks, tractors, or trailers are sometimes operated under lease contracts. As with other partnerships, such a move requires an assessment of value for money versus the cost and risk of operating an own vehicle fleet.

**Table 13: Vehicle Fleet Leases**

Case Studies: UK Royal Mail with LeasePlan UK Poste Italiane with LeasePlan Italia S.p.A TNT Post B.V. with ING Car Lease B.V. <sup>78</sup>	
<b>Project Description</b>	<ul style="list-style-type: none"> <li>▪ To increase profitability, focus on core business and reduce fixed assets, fixed cost, overhead and resources involved in other areas.</li> <li>▪ 3-Year Full Operational Leases: to provide a range of specialist services including procurement, administration, maintenance, repairs and disposal.</li> </ul>
<b>Main Business Objectives / Results</b>	<ul style="list-style-type: none"> <li>▪ Supply and maintain its 5,000 non-operational company cars (UK), 2003</li> <li>▪ Supply and maintain 16,000 operational delivery cars in 2011 (Italy)</li> <li>▪ Supply and maintain 600 Cleaner Cars in 2012 (Netherlands)</li> </ul>
<b>Success Factors / Lessons Learned</b>	<ul style="list-style-type: none"> <li>▪ Reduction of operations cost</li> <li>▪ Improved and flexible liquidity</li> <li>▪ Actual cost accountability</li> <li>▪ Shared cost savings</li> <li>▪ Exception reporting</li> <li>▪ Sustainable fleet management</li> </ul>

## Real Estate Models

Like the Postal Service, postal operators abroad have often faced issues related to unused or underused real estate assets. In many cases, mail sorting facilities and large post offices, which are often located near railway stations or in the center of cities and towns have become underutilized or unutilized. Post offices in centers of medium-sized

<sup>78</sup> Post and Parcel, "UK Royal Mail chooses LeasePlan to run its company cars," March 3, 2003, <http://postandparcel.info/7898/news/uk-royal-mail-chooses-leaseplan-to-run-its-company-cars/>; LeasePlan press release, "The fleet of the Italian Post Office will be managed by LeasePlan," March 2011, <http://www.leaseplan.it/it/noleggio-a-lungo-termini/chi-siamo/giornalisti/comunicati-stampa/1103.php>; and PostNL Annual Report 2011, 2012, <http://annualreport2011.postnl.com/corporate-responsibility/corporate-responsibility-performance/environment/21-company-cars>.

towns, and villages might have been constructed for manual mail processing, leading to excess space in the age of mail automation. Meanwhile, public retail space in post offices has often played a part in the social fabric of communities, creating strong resistance to the elimination of excess capacity.

With the transformation of the postal sector, the role of the private sector management and ownership of real estate for postal services has evolved. The main stages in the evolution of private sector involvement are the following.

### ***Creating a Real Estate Business Function in the Post, through Consultancy or Interim Management***

This is not a PPP, but a first important step towards more PPPs. The objective is to introduce or strengthen the commercial real estate management capacity and knowledge within the postal agency. Real estate management is transformed from a technical function focused on providing support for operations to a complete business management function, acting as an internal “landlord” providing office space or production space as a service to the business units needing space, renovation and maintenance.

Applying agreements for the usage of square footage and market-based internal transfer pricing promotes efficiency, transparent cost allocation, and performance accountability. This approach also incentivizes and helps management to seek ways to increase revenues through service diversification, colocation, and letting of space to third parties, among other means. In some countries this business unit has been established as a subsidiary of the post. Examples of such real estate companies are

- Deutsche Post Immobilien GmbH (DPI), a central entity renting real estate to postal business units within Germany. Other entities include Deutsche Post Real Estate Germany GmbH, Deutsche Post Immobilienentwicklung (real estate development), Deutsche Post DHL Corporate Real Estate management GmbH, and others dealing with construction or engineering. Deutsche Post operates through approximately 12,000 sites and 27 million square meters worldwide.
- Poste Immo (S.A.), a subsidiary of France’s La Poste with 1.7 billion euros equity with 1,100 specialized staff, manages real estate of 7 million square meters in 12,244 buildings, of which 8,354 buildings (70 percent) are owned by La Poste. A small part of the real estate is rented to third parties. With a market value of 4 billion euros, real estate is the single largest asset on La Poste’s balance sheet and the second biggest item in expenses.
- Others include Swiss Post’s Post Immobilien GmbH, Austria Post’s Post Immobilien GmbH, Vienna, the Netherland’s PostNL Real Estate B.V., and the UK’s Royal Mail Estates Ltd.

### ***Sale and Leaseback of Portions of the Real Estate Portfolio***

This is a PPP in which the postal operator transfers to the private sector risks of real estate management, such as generating inadequate rental revenues. Sale and leaseback allows postal operators to convert fixed assets into liquidity and transform high levels of fixed costs into variable costs. It can be structured through a contract with one or a few selected real estate investors, or through a real estate investment trust (REIT) — a special purpose vehicle that can be publicly listed on the stock exchange with a structure similar to the one mutual funds provide for investment in stocks.

The exact scope, function, and duration of lease contracts differ, and offer flexibility to the postal operator to adjust the usage of square footage to business needs, and to gradually vacate part of the building, which can be leased to third parties. For national retail chains and individual retailers (such as travel agents, mobile phone shops, newspaper kiosks, drugstores, or coffee shops) renting a portion of the ground floor in a postal building can be attractive given its prime location and the significant foot traffic to and from the post office and surrounding retail businesses. The second and higher floors are typically rented to service companies such as small law firms. From the investor's perspective, sales and leaseback tactics tend to be considered attractive to the extent that a portion of the building continues to be rented by a high-profile trusted entity that is expected to remain in business in the long-term.

In addition to sale and leaseback, “classic” leases are increasingly seen by posts as the preferred arrangement for new postal real estate such as new international mail centers, warehousing, and logistics centers. Lease contracts generally have a term ranging from 5 to 12 years, with options to renew the contract. For instance Prologis, a global owner and operator of industrial real estate leases 12 million square feet of warehouse space to Deutsche Post DHL in Europe, Asia, and North America.<sup>79</sup>

When the closing of a post office or the relocation to another building of an underused facility is not feasible, several other forms of partnerships with third parties can be used. Subletting of space in areas shared with (or adjacent to) postal services is common. Examples include postal banks that operate their branches in separate parts of postal buildings (for example, in Romania, Uganda, and the Philippines), travel agents in main post offices (for example, in Lithuania and the Kyrgyz Republic), or mobile phone SIM card dealers in Armenia's largest post offices.

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<sup>79</sup> Prologis Strengthens its Relationship with DHL with New Lease in Poland, *Prologis*, <http://www.prologis.com/docs/country/central-and-eastern-europe/Prologis%20signs%2033,800%20sqm%20with%20DHL%20in%20PPDabrowa.pdf>.

**Table 14: Real Estate Management – Germany**

Case Study: Sale and Lease Back and Onward Sale to REIT – Deutsche Post Immobilien GmbH-Lone Star Real Estate Fund <sup>80</sup>	
<b>Project Description</b>	<ul style="list-style-type: none"> <li>▪ Sales of 1,267 buildings and land owned and used by Deutsche Post within Germany in FY 2008.</li> <li>▪ Cash value of the transaction is 1 billion euros, for which the buyer raised 0.7 billion euros in bank financing and structured the deal through a special purpose vehicle. The real estate portfolio was a split 70 percent mixed-use properties and 30 percent logistics properties and development sites. The mixed-use properties typically comprise ground floor retail with offices and residential space on top and are 16,000 sq. ft. in size on average.</li> <li>▪ Deutsche Post continues to lease in most buildings part of the space available for its own operation, mainly retail, and about 20 percent of space has been rented to 3<sup>rd</sup> parties.</li> </ul>
<b>Main Business Objectives / Results</b>	<ul style="list-style-type: none"> <li>▪ Raise cash / liquidity.</li> <li>▪ Improve financial performance ratios and reduce fixed costs and fixed assets.</li> <li>▪ Focus on core postal business and transfer real estate management and rental and sales of unutilized or underutilized space to third party.</li> <li>▪ Strongly improved liquidity for Deutsche Post, Germany providing nearly 2 billion euros in funding and a basis for finance for business development.</li> <li>▪ Significant reduction in fixed assets and related fixed assets in buildings that were partly obsolete for current business model and operations.</li> <li>▪ Deal execution not generating public or political resistance; no straightforward closure of offices.</li> </ul>
<b>Success Factors / Lessons Learned</b>	<ul style="list-style-type: none"> <li>▪ Lone Star provided 300 million euros from own funds and arranged finance of 700 million euros from German and French banks.</li> <li>▪ The real estate outlook was positive in 2008 prior to the Lehman Brothers collapse. The continued role of Post in most entities kept investor appetite high, while major and high quality investment opportunities on the German real estate market are expected to remain scarce.</li> </ul>

## Retail Networks Partnerships

Many of the international models of retail partnerships combine different types of PPP models, responding to a need to reduce fixed network costs, adjust to changing customer access needs and demographics, and grow revenue.

<sup>80</sup> *The Wall Street Journal*, "Deutsche Post to sell properties to Lone Star," April 1, 2008, <http://online.wsj.com/article/SB120704078381279963.html> and Deutsche Post, "Deutsche Post World Net sells real estate portfolio to investor," April 1, 2008, [http://www.dp-dhl.com/en/investors/investor\\_news/financial\\_news\\_archive/2008/dpwn\\_verkauft\\_immobilienpaket.html](http://www.dp-dhl.com/en/investors/investor_news/financial_news_archive/2008/dpwn_verkauft_immobilienpaket.html).

The most common partnerships involve

- Conversion of fixed assets through franchising, and partnerships with municipalities or small companies in rural areas.
- Diversification to increase revenues, enter new spaces, and share costs through agency services agreements or joint ventures with banks, utilities, and governments. Developing a bundle of postal services combined with technology-based financial services and mobile telecom services and other e-based services is an increasingly common strategy.
- Go-to-market partnerships include alliances with IT partners to launch value added services such as authentication services, or with independent retailers to extend networks of parcels drop off or collection points.

A striking difference between the Postal Service and many of its peers is the degree to which the retail network has either been outsourced (for example PostNL, Deutsche Post and Royal Mail, to name a few, no longer own and operate a single post office), or has become an enabling infrastructure in support of private sector businesses and government services, as opposed to “just” a first and last mile provider of postal services.

### ***Franchising versus Postal Agencies***

Several operators which own and operate extensive networks experience financial losses at as many as 90 percent of their post offices. Since rural presence is considered a part of the postal universal service obligation (USO), operators often take the loss as a given-- a natural result of compliance with the USO that requires continued financial support from the state, market protection or internal cross-subsidies.

At the end of 2011, within the EU-15, about 60 percent of the 74,000 retail post offices were reported as not owned and not operated by the postal operator.<sup>81</sup> Australia has 80 percent of its post offices operating on a franchise basis, many in rural areas. Italy and Spain have yet to begin the process, and still own and operate 100 percent of their post offices.

The United Kingdom and the Netherlands have had an evolutionary process of over 20 years of repositioning the retail post office as a separately incorporated operation. The revenues of the retail network are predominantly from sales and distribution of nonpostal, fast-moving consumer services and goods; the costs are mainly variable and related to the performance of franchising partners.

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<sup>81</sup> Analysis performed by decision/analysis partners based on postal data. The EU-15 are the 15 highly developed countries that made up the European Union prior to the inclusion of several former Soviet bloc and other eastern and central European states in 2004.



**Table 15: Franchising/Licensing Model**

<b>Case Study: The Australia Post Franchising/Licensing Model<sup>82</sup></b>	
<b>Project Description</b>	<ul style="list-style-type: none"> <li>▪ Transformed Australia's Post Office network into a network of licensed and franchised branches including licensed post offices, community postal agents and post shops.</li> <li>▪ 3,000 licensed post offices (LPO), run solely as a post office or in conjunction with another business such as a news agency, dry cleaners or convenience stores.</li> <li>▪ 630 community postal agents (CPAs) operate in rural areas, 90 percent of which are collocated with another business such as a general store.</li> <li>▪ Flagship "PostShops" only in large cities, of which 30 (as of September 2012) have been converted into Superstores (mail + mail related businesses + parcels stations) owned and operated by Australia Post.</li> </ul>
<b>Main Business Objectives / Results</b>	<ul style="list-style-type: none"> <li>▪ Some of the PostShops are franchised (also known as Franchised Post Offices or Franchises).</li> <li>▪ LPOs offer postal products and services, bill pay, banking, money orders, postal packaging and mail services. Most also provide products and services such as stationery, greeting cards, phone cards, photocopies, facsimile, small gifts.</li> <li>▪ CPA: Focus on basic postal services; they don't offer agency services such as Postbillpay or Bank@Post.</li> <li>▪ PostShops converted into Superstores offer in addition to postal offerings, parcels lockers, a so-called "digital zone" allowing customers to shop online + eBay corner, counters dedicated to government services, kiosks for bill payments and other services.</li> <li>▪ Franchised PostShops offer only Australia Post products and services.</li> </ul>
<b>Success Factors / Lessons Learned</b>	<ul style="list-style-type: none"> <li>▪ Franchisee/licensee/postal agent model offers entrepreneurs opportunity to start their own business with an established brand, with training, technology and management support, and in most cases the option to expand their business to additional services adapted to the needs of the local market.</li> </ul>

An increasingly popular model is franchising of postal retail outlets. For the postal operator, the franchise is an alternative to that reduces investment, labor costs, and fixed assets costs, and solves the problem of finding ways to reduce the idle time of staff. Postal franchisees are believed by some to have a greater incentive than an employee of a state-owned entity because the franchisee has a direct stake in the business. Franchising relationships may present an opportunity for the postal operator

<sup>82</sup> Post Office Agents Association Limited, "Looking to buy a post office?" <http://poaal.com.au/post-offices/resources/looking-to-buy-a-post-office/>; Australia Post, "Operating as a post office," <http://auspost.com.au/about-us/operating-as-a-post-office.html>; Postalnews, "South Australia's flagship postal superstore opens in Adelaide," July 18, 2012, <http://postalnews.com/postalnewsblog/2012/07/18/south-australias-flagship-postal-superstore-opens-in-adelaide/>; and Australia Post, "Australia Post delivers new superstores and a Digital MailBox for all Australians," March 26, 2012, <http://auspost.com.au/about-us/australia-post-delivers-superstores-and-digital-mailbox.html>.

to improve customer service. At the same time, they may also present an increased risk in image, reputation, quality and continuity.

Franchise partners often include large, nationwide chains, such as supermarkets, bookstores, or drugstores, because of their foot traffic, the profile and retail expertise of the partner chain, and the availability of unused or underutilized space. They can also include small individual operators, who will most often propose nonpostal services responding to local demand, in addition to postal services.

The Australia Post retail outsourcing model is another example of extended retail outsourcing. It is based on a mix of business models, each corresponding to a different level of risk sharing between the post and its private partners. Contrary to the Netherlands, Australia still has a few owned and operated offices. Franchising appears a proven success formula in many other countries. The scope of franchise differs. In some cases such as in Brazil, the franchisees are also active in mail production, including printing.

### ***Creating a Sustainable Retail Network through Multiple Partnerships: UK Post Office Ltd.***

There are around 11,000 Post Office branches across the UK, of which 373 are directly managed by Post Office Ltd. The majority of other branches are either run by franchise partners or local subpostmaster agents (most of them members of the National Federation of SubPostmasters), as "subpost offices." As part of the Postal Services Act 2011, Post Office Ltd became independent of the Royal Mail Group on April 1, 2012 and is now owned by the government. Following separation from the Royal Mail Group, a 10-year agreement was signed between the two companies to allow Post Offices to continue to sell stamps and handle letters and parcels for Royal Mail.

In the UK, a Post Office's image, sales development, and customer satisfaction heavily relies on the business partners that operate retail outlets and run Post Office as a franchise; they range from individual entrepreneurs to small and nationwide retail chains. Its financial viability also depends on the number and range of business partners from both the public sector (government agencies, municipalities) and private sector, which leverage Post Office's network of 12,000 points to distribute to the public services and products — from fishing rods to foreign currencies — at affordable prices and cost, 6 days a week. What helps to make the business viable is the economies of scope incurred as more services from new and existing partners are added to the mix (spreading the network's fixed costs over more products, and increasing opportunities for cross-marketing).

The main business partnerships relate to local government services (partnership with municipalities for sharing local office operations costs, and the provision of local government services); (national) government and e-government services such as drivers licenses and residence permits; financial services on behalf of "partner banks" such as Bank of Ireland; and the provision of multiple agency services often through Post Office-branded products (e.g., prepaid phone cards, broadband Internet, Post Office HomePhone landline services).

Lessons learned from UK and Dutch partnership model can be summarized as follows:

- A national postal operator does not necessarily have to “own and operate” its network.
- There is a need to find the right balance between social public policy objectives (the “front office” of national and local governments, the social value of local offices), and the “enabling sales infrastructure” dimension (in support of banks, retailers, telecom operators, etc.). Both have spawned multiple partnerships, which increase the value of the Post Office platform.
- Successful franchising models take time to implement: The Dutch or British postal franchising models cannot be easily replicated — the Dutch model was implemented over a period of 15 years. More than a single model, a combination of partnerships (involving agreements with local governments, retailers, banks where possible, etc.) is often needed to ensure the long-term sustainability of the retail network — combining public policy, sales, and cost-reduction objectives.

## **Innovation Partnerships**

The scope of such alliances is very wide — in this respect, models used by posts do not differ much from those used by other companies. Both are looking to improve their value chains by leveraging strategic partnerships to gain access to new technologies that enable them to launch new products or adopt innovative processes. The main difference between posts and other large service companies possibly resides in the specific legal and regulatory constraints that in many countries limit the post’s margin to maneuver.

For this paper, the focus is on which models would be most conducive to a fast, cost-effective implementation of new innovation. For instance, the development by a post of an open digital or hybrid mail platform can lend itself to different forms of partnerships with private sector developers, who can extend the functionality of the post’s digital mail product and improve users’ experience. Different revenue models can also be considered such as revenue sharing or participation fees.

**Table 16: Examples of Strategic Alliances for Innovation**

Case Study: Digital Mail Box – Partnership with Telstra, AMP, and Westpac <sup>83</sup>	
<b>Project Description</b>	<p>Partnership with Telstra includes</p> <ul style="list-style-type: none"> <li>▪ Telstra as a participant in the Australia Post Digital MailBox (giving customers access to their Telstra communication documents like account statements and bills via the new Australia Post Digital MailBox).</li> <li>▪ Australia Post using Telstra's Australian based hosting and network services (e.g., Digital MailBox service to be hosted on Telstra's cloud platform).</li> <li>▪ Partnerships with Westpac (a bank) and AMP (a financial services company) as a user of the Digital Mail Box "to share information with its customers about their finances, investments and products, safe in the knowledge that their information is secure; backed by Australia Post and protected in our Australian based cloud provided by Telstra."</li> </ul>
<b>Main Business Objectives / Results</b>	<p>Telstra: Started with a MOU followed by strategic partnership agreement.</p> <p>AMP: MOU with Australia Post.</p>
<b>Success Factors / Lessons Learned</b>	Ongoing.

The choice of a "model," however, captures only one part of the whole picture. It explains just part of the success or failure of collaborations in the postal sector. In fact recent history of global postal strategies abounds with examples of

- MOUs signed at the CEO level that don't trickle down because of postal hierarchies, and thus don't lead to concrete collaborative activities. Ambitious work plans, therefore, never materialize.
- Joint pilot tests/proofs of concept of a partner's technology that are not implemented in a "real world" market environment, and the results of which therefore cannot be used as a basis for the preparation of a sound business plan.
- Joint, in-depth collaborative efforts involving both senior leaders and technical experts from post and partner, aimed at launching a new postal service, which never go beyond the business plan phase. Absent a concrete, final go/no go decision on the part of the post, the partner ends up losing interest in collaboration and confidence in the post's decision-making ability.

<sup>83</sup> Australia Post, "Australia Post and Telstra sign strategic partnership on Digital MailBox and IT network," June 01, 2012, <http://auspost.com.au/about-us/telstra-strategic-partnership-digital-mailbox.html> and Australia Post, "Westpac to partner with Australia Post on Digital MailBox," September 10, 2012, <http://auspost.com.au/about-us/westpac-to-partner-australia-post-on-digital-mailbox.html>. This program involves additional PPPs, including agreements with U.S. companies.

- Postal/private sector collaborative efforts negatively affected by widely-differing business cultures, or postal staff's reluctance to share information with private sector peers they see as "suppliers," if not potential competitors, rather than partners.
- Partnerships called off at the last minute because of government pressure or nomination of a new CEO or senior leaders.

The effectiveness of a post's innovation partnerships will depend on its ability to create a culture that encourages and rewards products and process innovation.

## Appendix D PPPs and Government Agencies in the United States

Federal and state governments have a long history of partnerships with the private sector to develop infrastructure projects. In the 19<sup>th</sup> century, the federal government worked with private railroads to facilitate westward expansion. The government provided the right-of-way and related development property while the railroads used private capital to build the rail facilities and rolling stock.<sup>84</sup>

Modern interest in PPPs accelerated in the 1980s, as the federal government looked to ways of funding projects through users rather than taxpayers. One response was to experiment in the early 1990s with alternative contracting methods such as design-build (DB) and design-build-operate-maintain (DBOM). At the time governments assumed that private investors could take over the entire public development process and deliver a self-supporting toll road that the government would own after a 30-35 year concession period.

In recent years public officials at all levels of government have increasingly suggested that private investment should take on a much larger role in replacing public funding for needed infrastructure, housing, and other capital-intensive projects. Advocates of PPPs claim that as much as hundreds of billions of dollars in private investment is available for PPP infrastructure projects.

### Summary by Key Sectors

Although most PPP literature focuses on infrastructure projects such as transportation, housing, water/wastewater treatment, the scope of PPPs is in fact much broader. In principle they can encompass many other services provided by U.S. states (e.g., lotteries, web portals) or municipalities including

- Transportation –These new projects are mostly express lanes that can be “tolled,” built next to existing freeways in heavily congested urban areas (High Occupancy Toll Lanes). According to sector experts, to be “financeable” by the private sector, such projects require a long concession period (e.g., 85 years) to allow for private investors to recoup their investment, or an upfront capital infusion from the state.
- Water and wastewater treatment – There are around 2,000 PPPs between municipalities and private companies to provide water and/or wastewater service. PPPs between municipalities and private entities can save customers anywhere from 15 to 25 percent through effective cost controls, innovations, economies of scale, and sound asset management practices.

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<sup>84</sup> See David Seader, *The United States Experience with Outsourcing, Privatization, and Public Private Partnerships*, NCPP, 2002, p. 1.

- Seaports – PPPs involve the private sector in a variety of capacities to provide construction, operations, maintenance, and/or financing of seaports. The trend for seaports is toward longer and more comprehensive tenant leases that incorporate construction and shift risk to the private sector. The substantial equity investment in these projects shows the private sector is willing to accept market risk, including economic fluctuations, if given a long-term agreement to operate the terminal and invest in capacity expansions.
- High tech – These PPPs involve sharing technologies in response to several strategic objectives by the public agency including transferring technologies from a public agency to private partners, promoting IT services through an open platform, reducing capital expenditure in IT systems through lease/buyback PPPs, outsourcing to acquire needed external IT skills, attracting IT contributions in cash or kind to policy goals, and mobilizing private sector expertise.

### Selected Examples of PPPs

Below are some specific examples of PPPs. The classification scheme in Table 17 focuses on the primary justification or characteristic of the partnership. Some types of partnerships would fit into more than one quadrant.

**Table 17: Classification of Government Agency PPPs in the United States**

	Cost Reduction	Revenue Generation
Tactical	<ul style="list-style-type: none"> <li>▪ State partnership for development of online services</li> </ul>	<ul style="list-style-type: none"> <li>▪ CRADA IP Licensing</li> </ul>
Strategic	<ul style="list-style-type: none"> <li>▪ Toll road concession</li> </ul>	<ul style="list-style-type: none"> <li>▪ Enhanced Use Lease</li> </ul>

**Table 18: Access to Cutting-Edge Technology**

<b>Case Study: Collaborative Partnership Between Texas Department of Information Resources (DIR) and NIC USA to Develop Texas.gov<sup>85</sup></b>	
<b>Project Description</b>	<ul style="list-style-type: none"> <li>▪ No tax dollars, 100 percent transaction-based self-funding model of partnership.</li> <li>▪ Texas.gov operates the state's "one stop shop" online portal, serving 70 state agencies and 180 local governments and 1 university with a total of more than 1,000 online services.</li> <li>▪ 7 year contract, renewable every year after 2016.</li> <li>▪ Project entirely funded from small transaction fees paid by users.</li> <li>▪ Partner responsible for development and implementation of new applications, operations, customer service, marketing.</li> <li>▪ Master agreement lays out partners' commitments.</li> <li>▪ State DIR keeps oversight of website's strategic direction, approves transaction fees and other rates, and monitors budget and performance. Governance structure includes a joint DIR/NIC USA Executive Steering Committee and a Customer Advisory Committee where 17 client agencies are represented.</li> </ul>
<b>Main Business Objectives / Results</b>	<ul style="list-style-type: none"> <li>▪ Project not only saves operational costs but also generates revenue for the state, which received \$31 million (share of revenue) in FY 2012.</li> <li>▪ Successful portal (many national e-gov awards), 2 million transactions per month.</li> <li>▪ Fast implementation of new IT/Web Tools.</li> </ul>
<b>Success Factors / Lessons Learned</b>	<ul style="list-style-type: none"> <li>▪ Private partner NIC USA is a specialist in self-supported web portals (projects in 23 U.S. states) and can draw from its portfolio of specific e-gov applications (e.g., payments modules) which leads to economies of scope.</li> <li>▪ First version of the site (Texasonline) although commercially successful went bankrupt in 2009 due to first partner BearingPoint's restructuring.</li> </ul>

<sup>85</sup> Texas Department of Information Resources, *Report on Texas.gov*, November 15, 2012, <http://www2.dir.state.tx.us/SiteCollectionDocuments/Texas.gov/2012ReportOnTexas.gov.pdf>, NIC Inc., "texas.gov," <http://www.egov.com/Partners/Pages/Texas.aspx>.



**Table 19: Monetizing Public Agencies' Patents or Research**

<b>Cooperation Research and Development Agreements (CRADAs)<sup>86</sup></b>	
<b>Project Description</b>	<ul style="list-style-type: none"> <li>▪ Created by the Federal Technology Transfer Act of 1986.</li> <li>▪ Used by federal laboratories to engage in collaborative efforts with non-federal partners to achieve the goals of technology transfer. It is not an acquisition or procurement vehicle.</li> <li>▪ Takes into account the needs and desires of private industry when commercializing a product (e.g., the need for confidentiality and perhaps for exclusive rights to a product), as well as a reward structure for government (e.g., sharing in royalties).</li> <li>▪ The government may contribute a wide variety of resources (personnel, services, facilities, equipment, and intellectual property) but not funds.</li> <li>▪ CRADAs allow the federal lab and its private partner to share patents and patent licenses for the research conducted (or inventions created) during the agreement, while also permitting one of them to hold exclusive rights to a single patent or patent license.</li> <li>▪ Many business models used including revenue-sharing, direct payment for the needed resources (e.g., fee for the use of facilities by partner), and royalties. Several alternative arrangements regarding licensing, but in all cases the government retains a nonexclusive, nontransferable license to inventions developed under the CRADA. This allows the government to use the invention, or to have it used on its behalf, anywhere in the world without royalty payments and without infringing on any patent rights.</li> <li>▪ Trade secrets or privileged information that develops during the course of a CRADA can be protected from disclosure for up to five years.</li> </ul>
<b>Main Business Objectives / Results</b>	<ul style="list-style-type: none"> <li>▪ Government benefits by getting direct payments or royalties.</li> <li>▪ Provides a framework to monetize public research and patents in support of economic growth.</li> <li>▪ As of 2009, there were 4,200 active CRADAs involving many agencies.</li> </ul>
<b>Success Factors/ Lessons Learned</b>	<ul style="list-style-type: none"> <li>▪ Most effective for the successful commercialization of products or processes originating in federal laboratories.</li> </ul>

<sup>86</sup> Lara Getz, "Fact Sheet: CRADAs, Cooperative Research and Development Agreements," American Security Project, November 29, 2011, <http://americansecurityproject.org/wp-content/uploads/2011/12/CRADAs-FINAL.pdf>.

**Table 20: Long-term Concessions**

Case Study: Indiana Toll Road Concession Lease <sup>87</sup>	
<b>Project Description</b>	<ul style="list-style-type: none"> <li>▪ Highway built in 1956, owned by the state of Indiana.</li> <li>▪ Concession bid won in 2006 by Macquarie (an Australian investment bank) and Cintra (European infrastructure developer).</li> <li>▪ 75-year concession lease, 156-mile toll road where concessionaire collects and keeps toll revenue.</li> <li>▪ Concession agreement establishes toll rates/possible increases, limits return on investment (ROI) for concessionaire, provides for mandatory rehabilitation investments (electronic tools, etc.).</li> <li>▪ Concessionaire operates, maintains, rehabilitates, and collects tolls.</li> <li>▪ Private sector financing: 20 percent equity, 80 percent debt.</li> </ul>
<b>Main Business Objectives / Results</b>	<ul style="list-style-type: none"> <li>▪ State of Indiana wants to monetize aging asset and use proceeds to fund other (200) transportation projects.</li> <li>▪ Save on operating costs vs. direct management.</li> </ul>
<b>Success Factors/ Lessons Learned</b>	<ul style="list-style-type: none"> <li>▪ Special legislation by state was narrowly passed. Failure to pass would have stopped project.</li> <li>▪ Several bidders, winning bid valuation well over expectations.</li> <li>▪ Very high bid valuation (\$3.8 billion) considered too high by some observers, given long-term uncertainty on traffic volumes. Bidder may have overpaid. As of 2011 operations were still unprofitable, with cash flows insufficient not capable of sustainable high level debt over the long term. Long-term financial sustainability questionable.</li> <li>▪ Very long term (75 years) seen by some as de facto privatization.</li> <li>▪ Quasi-monopoly status does not guarantee profitability.</li> <li>▪ A 75-year lease would make less sense in industries facing rapid technological changes.</li> </ul>

<sup>87</sup> FHWA, *Project Profiles*, [http://www.fhwa.dot.gov/ipd/project\\_profiles/in\\_indianatoll.htm](http://www.fhwa.dot.gov/ipd/project_profiles/in_indianatoll.htm), FHWA, PPP Case Studies, April 23, 2008, (downloaded from <http://www.dot.state.oh.us/groups/tft/Appendix%20B/Public%20Investment%20Articles/Indiana%20Toll%20Road.pdf> on June 5, 2013) p. 1, and Ryan Holeywell, "The Indiana Toll Road: A Model for Privatization?" *GOVERNING*, October 2011, <http://www.governing.com/topics/mgmt/indiana-toll-road-model-privatization.html>.

## Public Policy Drivers of U.S. PPPs

In this section, we highlight some policy tools that have encouraged the development of new PPPs in the United States.

### ***General Enabling Legislation***

Enabling legislation guides a state's PPP program development and the selection and execution of specific projects. In some states, legislative approval is also required for specific projects. Enabling statutes set conditions that promote or prevent PPPs, guide development of state PPP programs, provide foundations for PPP contracts, and affect the risks involved for each party. The first state PPP legislation was enacted more than 20 years ago in California. More than 30 states now have PPP legislation.

Such legislation generally addresses

- Scope of PPP – Some types of legislation allow a specific project to “test the waters”, or permit sector-specific PPPs, such as road infrastructure. At least 22 states with PPP legislation allow public authorities to engage with the private sector on infrastructure projects beyond highways and roads, such as ferries, pipelines, and rail or other public facilities.
- Level of state legislature oversight – The legislation states whether prior approval is requested for new PPPs, and what process public agencies should follow.

### ***Policy Tools to Lower the Cost of Capital***

Since the late 1980s federal and state governments have proactively supported the development and implementation of PPPs through new financing mechanisms, including

- State infrastructure banks (SIBs) – At least 32 state governments have established infrastructure banks to support projects in surface transportation. SIBs are revolving funds administered by states that support surface transportation projects. An SIB functions much like a bank by offering loans and other credit products to public and private sponsors of highway or mass transit construction projects. SIB assistance may include loans (at or below market rates), loan guarantees, standby lines of credit, letters of credit, certificates of participation, debt service reserve funds, bond insurance, and other forms of non-grant assistance.
- Private activity bonds (PABs) – PABs are tax exempt and can be issued by a government agency on behalf of private developers. Providing private developers and operators with access to tax-exempt interest lowers the cost of capital significantly, enhancing investment prospects.
- The Transportation Infrastructure Finance and Innovation Act (TIFIA) of 1998 – TIFIA established a federal credit program for eligible transportation projects of “national or regional significance” under which the U.S. Department of

Transportation (DOT) may provide secured loans to non-federal project sponsors, loan guarantees, and standby lines of credit that may be drawn upon during the first 10 years of a project's life. The program's fundamental goal is "to leverage Federal funds by attracting substantial private and other non-Federal co-investment in critical improvements to the nation's surface transportation system."<sup>88</sup>

So far these financing tools have played a key role in helping with the financing of PPPs, particularly in the transportation sector.

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<sup>88</sup> California Department of Transportation, *Transportation Infrastructure Finance and Innovation Act (TIFIA) of 1998*, <http://www.dot.ca.gov/hq/innovfinance/tifia.htm>.

## Appendix E A Brief Overview of Value for Money (VfM) Analysis

VfM is an increasingly popular tool for assessing the costs and benefits of PPPs. VfM is relatively new in the U.S. compared to Europe, Canada, and Australia.<sup>89</sup> In recent years, however, U.S. jurisdictions such as Virginia have adopted VfM and published guidance documents on the topic.<sup>90</sup> In addition, the Federal Highway Administration (FHWA) has recently published extensive materials on VfM and other aspects of PPPs. The FHWA's VfM guidance and related documents are available at

[http://www.fhwa.dot.gov/ipd/p3/toolkit/guidance\\_documents/index.htm](http://www.fhwa.dot.gov/ipd/p3/toolkit/guidance_documents/index.htm).

VfM analysis compares the net present value (NPV) of a PPP bid (or a hypothetical PPP bid, known as a shadow bid, if the analysis is done at the pre-procurement stage) to the NPV of pursuing the same project or program through a more traditional procurement. The cost of a traditional procurement forms the baseline for the VfM analysis; this baseline is called the public sector comparator (PSC). The VfM analysis should be performed before the public agency receives bids, and can be updated after parties have submitted their bids.

While there are various models, VfM for PPPs should consider

- Full Life-Cycle (FLC) cost and revenue analysis for each option – This should include all costs including human resources, construction, operation, maintenance, future capital improvement costs, and ancillary expenses such as legal fees.
- Estimate of Risk – The benefit of the majority of PPPs is transferring risk away from the public sector to the private sector. This risk transfer can outweigh the disadvantage of higher costs.
- Finding Net Present Value – Since PPPs are often over numerous years, and possibly decades, it is important to include a NPV analysis of future costs and income streams, and develop an “apples to apples” financial comparison.<sup>91</sup> Both methods might involve different future cash flows — the PSC could involve loan repayments to a financial institution, for example, while the PPP could include periodic service payments to a private partner over a longer period of time. To determine the relative values of these separate cash flows, the agency must

<sup>89</sup> Federal Highway Administration, *Value for Money: State of the Practice*, December 2011, [www.fhwa.dot.gov/ipd/pdfs/p3/vfm\\_state\\_of\\_the\\_practice.pdf](http://www.fhwa.dot.gov/ipd/pdfs/p3/vfm_state_of_the_practice.pdf), p. 48, and Dorothy Morallos, Adjo Amekudzi, Catherine Ross, and Michael Mayer, *Value for Money Analysis in US Transportation and Public-Private Partnerships*, *Transportation Research Record: Journal of the Transportation Research Board*, No. 2115, Transportation Research Board of the National Academies, Washington, D.C., DOI: 10.3141/2115-04, 2009, <http://people.ce.gatech.edu/~aa103/ValueforMoney.pdf>, p. 32.

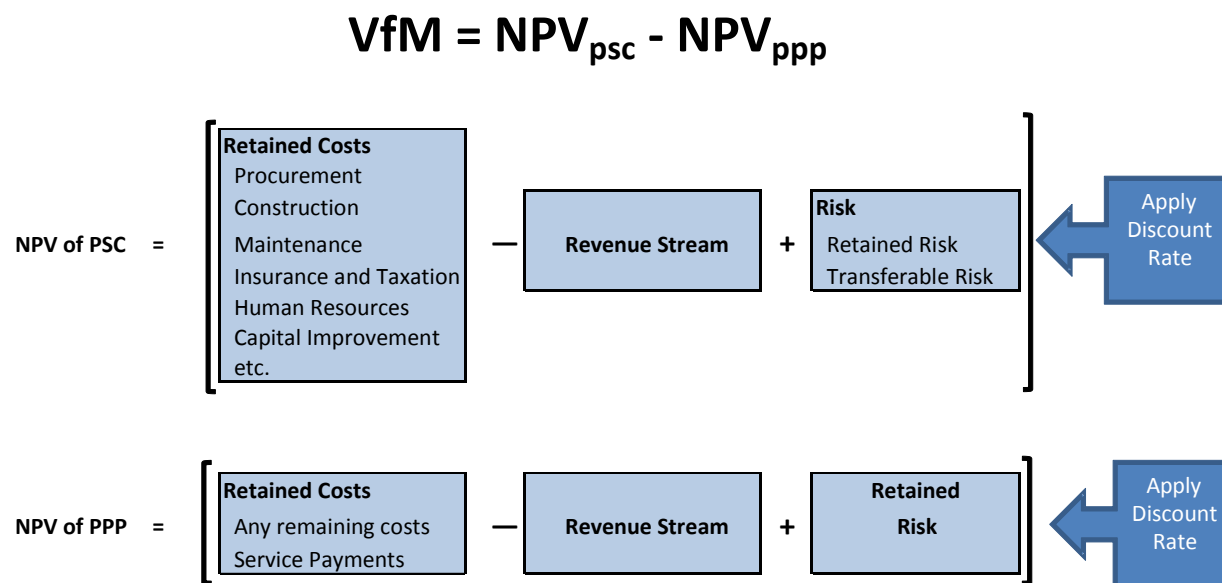
<sup>90</sup> Commonwealth of Virginia Office of Transportation Public Private Partnerships, *PPTA Value for Money Guidance*, April 2011, [http://www.vappta.org/resources/VDOT\\_VfM\\_guidance\\_document\\_August2012.pdf](http://www.vappta.org/resources/VDOT_VfM_guidance_document_August2012.pdf).

<sup>91</sup> NCPPP, *Testing Tradition*, pp. 8-11.

apply a discount rate — conducting a discounted cash flow analysis — to account for the time value of money. The discounted cash flow analysis will allow the agency to compare the NPV of both costs and revenues for the PSC and PPP. Small changes in the discount rate can change the outcome of the analysis and are often a point of contention. The FHWA advises public agencies to apply multiple sensitivity tests using “different discount rates to ensure that the outcome is not skewed or biased by the selected discount rate.”<sup>92</sup>

Figure 2 illustrates the VfM process.

**Figure 2: VfM Compares Net Present Value of Alternative Procurements**

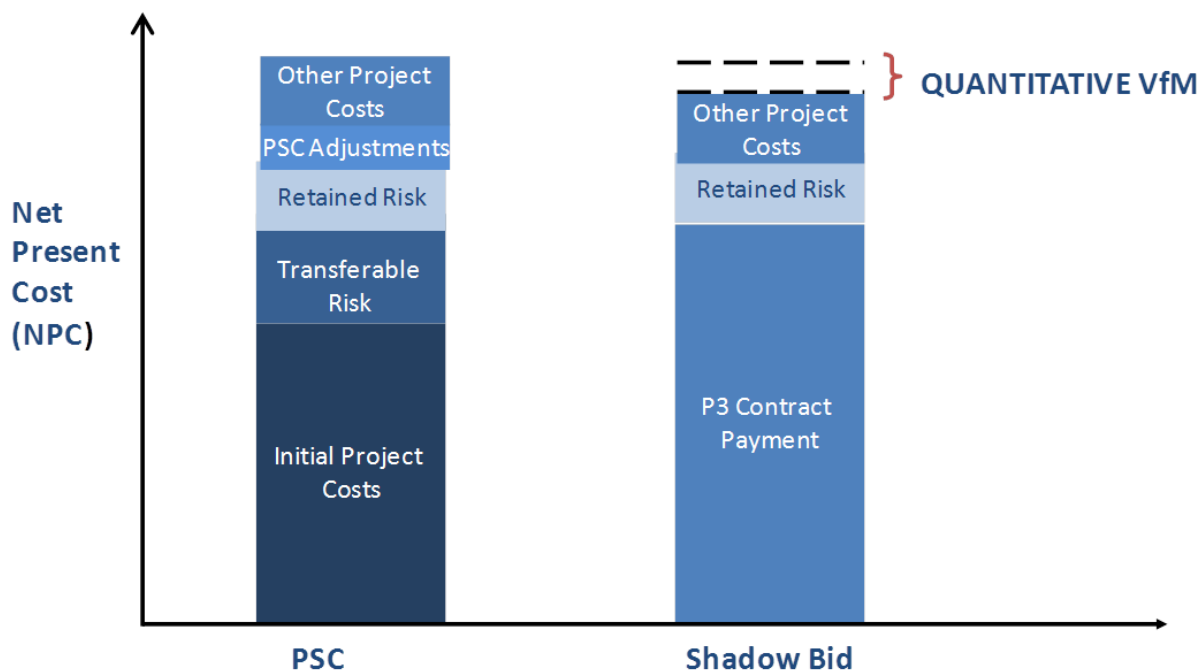


For clarity and simplification, Figure 2 focuses on *quantitative* issues in evaluating a PPP. In many or most cases, a public agency should also add formal consideration of *qualitative* issues, including potential effects on stakeholders, legal and regulatory issues, and the ability of private sector partners to achieve the project’s goals.

Figure 3 shows a potential result of conducting a quantitative VfM analysis. Figure 3 indicates the PPP achieves quantitative VfM because the net present cost of the PPP is less than net present cost of the public sector comparator. The results in this figure indicate a “go” decision for public sector entity considering a PPP, based on quantitative factors (although qualitative factors should also be considered for the conclusion to be determinative). On the other hand, if the net present cost of the PPP were above that of the public sector comparator, then this would indicate a “no go” decision for the public agency.

<sup>92</sup> FHWA, *Value for Money Primer*, December 2012, [http://www.fhwa.dot.gov/ipd/pdfs/p3/p3\\_value\\_for\\_money\\_primer\\_122612.pdf](http://www.fhwa.dot.gov/ipd/pdfs/p3/p3_value_for_money_primer_122612.pdf), p. 3-3.

**Figure 3: An Illustrative Outcome of a Quantitative VfM Analysis**



Source: Federal Highway Administration, P3 Toolkit, <http://www.fhwa.dot.gov/ipd/p3/toolkit/index.htm>

PPPs are often complex transactions and comparisons to other forms of procurement can be difficult. The PPP often involves a tradeoff between reduced risk to the public agency and higher long-term financing or service costs demanded by the private sector partner. Public sector officials and stakeholders can make tactical errors by focusing exclusively on either the benefits of the reduced risk in the PPP or the cost of higher financing in the PPP, to the exclusion of other factors. Therefore, a comprehensive comparison is needed to provide a more complete picture of the total costs of the project. VfM analysis can expose the potential benefits and drawbacks associated with the various options. This can make the difference between successful and unsuccessful projects.

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