

## **CHAPTER 6**

**THE GOVERNMENT OF THE  
HONG KONG SPECIAL ADMINISTRATIVE REGION**

**POST OFFICE TRADING FUND**

**GOVERNMENT DEPARTMENT**

**Post Office**

**Financial performance of the Post Office**

**Audit Commission  
Hong Kong  
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# FINANCIAL PERFORMANCE OF THE POST OFFICE

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# FINANCIAL PERFORMANCE OF THE POST OFFICE

## Summary and key findings

A. **Introduction.** The role of the Post Office (PO) is to provide reliable and efficient mail services to the public at reasonable prices. Since 1 August 1995, the PO has been operating as a trading fund. The Post Office Trading Fund is required to generate sufficient revenue from its operation to: (a) finance its liabilities and expenses incurred in the provision of services; and (b) provide a reasonable return to the Government as its sole shareholder. In July 2001, the Postmaster General announced that the PO would incur an operating loss of \$103 million for the year 2001-02 and there was a need to revise the postage rates with effect from 1 April 2002 (paras. 1.1, 1.2, 1.5 and 1.7).

B. **Audit review.** Audit has conducted a review on the financial performance of the PO. Audit has found that: (a) it is possible for the PO to improve the financial performance of three of its new services and to reduce its operating costs; (b) there is a need for the PO to address the threats posed to it by one overseas postal administration and some overseas mailers bypassing the international mail system, competition in local mail, and an increasing use of electronic communication; and (c) the PO needs to take further action to reduce cross-subsidisation among its different mail services (paras. 1.8 and 1.9). The major audit findings are summarised in paragraphs C to F below.

C. **Scope for improving financial performance of new services.** In order to improve its financial performance, in recent years, the PO has introduced new services in addition to its traditional mail services. However, Audit has found that there is room for improvement in the financial performance of the following three new services of the PO (para. 2.1):

- (a) **Postshop service.** In December 1996, the PO launched the postshop service by opening a Postshop at the General Post Office (GPO). The postshop service involves selling souvenirs and postal accessories to customers. In 1997, the PO found that it was financially not viable to operate Postshops. Since 1998-99, the financial performance of the postshop service has deteriorated significantly. Its operating loss in 2000-01 was \$4.1 million. Since early 2000, the PO has reduced the number of staff engaged in operating the Postshop at the GPO in order to reduce operating costs. Audit considers that there is a need for the PO to continue finding ways of reducing the operating costs of its postshop service. The PO should also explore avenues of increasing the operating profit of the service (paras. 2.2, 2.3(a), 2.6, 2.7 and 2.10);
- (b) **E-post service.** In June 1997, the PO launched the e-post service. With this service, electronic messages are sent to the PO's e-post centres by electronic mail systems or through magnetic media. The e-post centres convert the customers' electronic messages to

traditional paper mail items which are then delivered to the recipients. Since its introduction in 1997-98, the e-post service had been incurring operating losses. Its operating losses from 1997-98 to 2000-01 totalled \$16 million. The PO has not been very successful in securing new customers for its e-post service although there is spare capacity at the e-post centres. Audit considers that there is a need for the PO to explore avenues of securing new customers for its e-post service (paras. 2.13, 2.15, 2.16, 2.18 and 2.20); and

- (c) **Remittance service.** The PO introduced the remittance service for the Philippines in 1999 and the remittance service for Mainland China in 2000. However, the service is not as successful as the PO anticipated. In 2000-01, the revenue of \$243,000 generated from the service was 11% of the estimated annual revenue of \$2.3 million. Audit considers that there is a need for the PO to further promote the remittance service so as to increase the operating profit of the service. If the demand for the service continues to be low, the PO should consider ceasing the service (paras. 2.26 and 2.28).

D. **Scope for reducing operating costs.** The financial performance of the PO can be improved by reducing its operating costs. Audit has found that there is scope for the PO to reduce its operating costs in the following areas (para. 3.1):

- (a) **Delivery frequency.** As at 31 August 2001, the PO operated 1,238 delivery beats which made one delivery a day (called once-delivery beats) and 452 delivery beats which made two deliveries a day (called twice-delivery beats). During the period January 2000 to December 2001, the performance (in terms of percentage of letters delivered) of twice-delivery beats was only slightly better than that of once-delivery beats by 1.2%. During the period April to September 2001, 24% of the twice-delivery beats delivered not more than 50 mail items daily in the second delivery and 30% of the twice-delivery beats delivered not more than 5% of the daily mail items in the second delivery. According to the PO's customer survey conducted in 1999-2000, reducing the delivery frequency to only once a day met only very little public resistance. If the PO adopted once-delivery beats throughout Hong Kong, 133 delivery postmen could be redeployed to perform other duties. The resultant potential annual saving in staff costs would be \$38.2 million. Audit considers that it is feasible for the PO to reduce its delivery frequency from twice to once a day. There is a need for the PO to consider converting its existing twice-delivery beats to once-delivery beats (paras. 3.2, 3.8 to 3.11 and 3.16); and
- (b) **Overtime work of delivery postmen.** In order to ascertain whether the overtime (OT) claims of delivery postmen were justified, Audit assessed the workload of the 120 delivery beats covered in the PO's Quality of Service Surveys during the period April to September 2001. Audit's analysis indicated that the OT claimed by some delivery postmen could not be justified by their workload, based on the PO's mail counts. Audit estimated that the annual OT allowance claimed by delivery postmen of all the 1,690 delivery beats which could not be justified by their workload would amount to \$21.3 million at 2001-02 prices. Audit considers that there is a need for the PO to strengthen its control over the OT work of delivery postmen and their claims for OT allowance (paras. 3.31, 3.32 and 3.36).

E. **Need to address threats.** With the growing trends of globalisation, deregulation and liberalisation in the communication market, the PO faces growing challenges in three areas, namely international mail, local mail, and an increasing use of electronic communication. According to the PO's estimation in 2001, it would lose \$24 million in annual revenue because one overseas postal administration and some overseas mailers exploited the local postage system by sending international mail to their agents in Hong Kong. The local agents will deliver the mail items directly to the addressees in cases where it is more economical for them to do so (e.g. in business districts). For mail items addressed to remote areas, they will pass them to the PO as local mail. In doing so, the overseas postal administration has deprived the PO of the receipt of terminal dues. Furthermore, in recent years, the growth rate of the PO's local mail traffic in business districts and densely populated residential areas has been adversely affected by the competition from local couriers and utilities companies which deliver their own bills. The financial performance of the PO is also affected by the increasing use of electronic communication instead of traditional mail. Audit considers that there is a need for the PO to find ways of addressing the threats it is facing (paras. 4.1, 4.4, 4.6, 4.8, 4.11(b), 4.12 and 4.14).

F. **Need to continue eliminating cross-subsidisation among mail services.** In March 1993, Audit recommended that the Postmaster General should review the pricing strategy of local mail service and surface mail service with a view to eliminating cross-subsidisation among different types of mail services. In April 1995, after reviewing the postal policy, the Economic Services Bureau (ESB) recommended that the PO should set, as a long-term postal pricing policy, the objective of gradually reducing the extent of cross-subsidisation among mail services, notwithstanding that the ESB considered that some element of cross-subsidisation was inevitable. In June 1995 and September 1996, the PO implemented higher percentages of postage rate increase for those services incurring losses than those services generating profits. However, the PO still has not been able to eliminate cross-subsidisation. An example of a heavily cross-subsidised mail service is the bulk bag service. The bulk bag service provides for posting of printed matter in bulk quantity by surface mail to places abroad. In 1996, the PO aimed to achieve breakeven for the service within three to four years. However, the service continues to be heavily subsidised by other profitable services. In 2000-01, the operating loss of the service was \$20.5 million, representing 65% of the PO's overall operating loss. Furthermore, the service to a few large customers has been heavily subsidised. During the period August to October 2001, the top ten users accounted for 97.6% of the total postage. Audit considers that there is a need for the PO to continue its efforts to reduce cross-subsidisation among its different mail services (paras. 5.1, 5.5 to 5.10, 5.13 and 5.15).

G. **Audit recommendations.** Audit has made the following major recommendations that the Postmaster General should:

*Scope for improving financial performance of new services*

- (a) with a view to reducing the operating costs of the Postshop at the GPO, consider:
  - (i) closing the Postshop and instead, setting up a Postshop Corner at the GPO to continue providing the postshop service (para. 2.11(a)(i)); or

- (ii) merging the Postshop with the Philatelic Counter (para. 2.11(a)(ii));
- (b) closely monitor the financial performance of the postshop service and explore avenues of increasing the operating income generated from the service (para. 2.11(b));
- (c) conduct a review on the market position and competitiveness of the PO's e-post service and, based on the results of the review, take necessary actions to increase the PO's market share or consider ceasing the service (para. 2.21);
- (d) conduct a review on the competitiveness of the PO's remittance service and, based on the results of the review, take necessary actions to increase the PO's market share or consider ceasing the service (para. 2.29);

*Scope for reducing operating costs*

- (e) conduct a comprehensive review of the existing twice-delivery beats so as to identify those delivery beats which can be converted to once-delivery beats (para. 3.17(a));
- (f) review the PO's system of controlling and monitoring the OT work of delivery postmen to ensure that the guidelines in Civil Service Bureau Circular No. 18/2000 are fully complied with (para. 3.37(a));

*Need to address threats*

- (g) in the comprehensive review on postal policy and services currently being conducted, in conjunction with the ESB, critically examine the threats posed to the PO and find practical ways of addressing them (para. 4.15);

*Need to continue eliminating cross-subsidisation among mail services*

- (h) continue taking action to reduce cross-subsidisation among the PO's different mail services (para. 5.16(a)); and
- (i) draw up a definite timetable to increase the postage rates for the bulk bag service so as to enable the service to achieve breakeven as soon as possible (para. 5.16(b)).

H. **Response from the Administration.** The Administration generally agrees with Audit's recommendations (paras. 1.10, 1.11, 2.12, 2.22, 2.30, 3.18, 3.38, 3.39, 4.16, 4.17 and 5.17).



## **PART 1: INTRODUCTION**

### **Background**

1.1 The role of the Post Office (PO) is to provide reliable and efficient mail services to the public at reasonable prices. It provides postal services over the counter at branch post offices and a mail delivery service covering every address in the territory. As at 1 March 2002, the PO's postal infrastructure consisted of 128 branch post offices and 3 mobile post offices.

### **The PO operates as a trading fund**

1.2 The Post Office Trading Fund (POTF) was established by a Resolution of the Legislative Council passed on 19 July 1995 under the Trading Funds Ordinance (Cap. 430). Since 1 August 1995, the PO has been operating as a trading fund.

1.3 A trading fund is an accounting entity set up to provide specified government services, as stipulated in the empowering Legislative Council Resolution, and services incidental thereto, on a financially autonomous basis. The Government's intention of introducing this accounting arrangement is to:

- (a) provide the management of the trading fund with the financial flexibility for delivering government services and incidental services in a commercial manner; and
- (b) make the management clearly accountable for the performance of the trading fund's operations.

1.4 Under the trading fund, the management retains all the trading fund revenue from service provision and has the discretion to allocate the resources of the trading fund to improve cost efficiency, to fund new activities in response to changing circumstances and to improve business viability.

1.5 At the commencement of its operation, the POTF was financed by an initial capital injection of \$2,101 million and a shareholder loan of \$900.4 million from the Capital Investment Fund. The POTF is required to generate sufficient revenue from its operation to:

- (a) finance its liabilities and expenses incurred in the provision of services; and
- (b) provide a reasonable return to its sole shareholder (i.e. the Government).

## Financial performance of the PO

1.6 The financial performance of the PO for the period 1 August 1995 (when it began to operate as a trading fund) to 31 March 2001 is summarised in Table 1 below. The exceptionally high profit of \$729.5 million in 1996-97 and \$1,218.1 million in 1997-98 from philately increased the PO's operating profit to over \$1,000 million for each of these two years. Consequently, in these two years, the PO was able to meet the target return of 10.5% per annum on fixed assets as determined by the Financial Secretary. However, income from philately has decreased significantly since 1998-99.

**Table 1**

**Financial performance of the PO  
for the period 1 August 1995 to 31 March 2001**

<b>Year</b>	<b>Revenue</b>	<b>Operating costs</b>	<b>Operating profit/(loss)</b>	<b>Rate of return on fixed assets (Note 1)</b>
	<b>(a)</b>	<b>(b)</b>	<b>(c) = (a) - (b)</b>	<b>(d)</b>
	<b>(\$ million)</b>	<b>(\$ million)</b>	<b>(\$ million)</b>	<b>(Percentage)</b>
1995-96 (Note 2)	2,376.2	2,075.2	<b>301.0</b>	<b>9.0%</b>
1996-97	4,469.4	3,340.8	<b>1,128.6</b>	<b>47.8%</b>
1997-98	4,929.7	3,696.8	<b>1,232.9</b>	<b>41.0%</b>
1998-99	3,519.1	3,668.9	<b>(149.8)</b>	<b>3.1%</b>
1999-2000	3,515.7	3,592.5	<b>(76.8)</b>	<b>2.1%</b>
2000-01	3,599.1	3,630.6	<b>(31.5)</b>	<b>1.8%</b>

Source: PO's records

Note 1: The rate of return on fixed assets is calculated as:

$$100\% \times \frac{(\text{Operating profit after taxation} + \text{Interest income after taxation})}{\text{Average net fixed assets}}$$

The average net fixed assets is calculated as:

$$(\text{Fixed assets at the beginning of the period} + \text{Fixed assets at the end of the period}) \times \frac{1}{2}$$

Note 2: This covers the period 1 August 1995 (when the PO began to operate as a trading fund) to 31 March 1996.

1.7 In July 2001, the Postmaster General announced that the PO would incur an operating loss of \$103 million for the year 2001-02 and there was a need to revise the postage rates with effect from 1 April 2002.

### **Audit review**

1.8 Audit has conducted a review on the financial performance of the PO. The audit objectives were to examine:

- (a) whether new services introduced by the PO in recent years are effective in improving its financial performance (see PART 2 below);
- (b) whether there is scope for reducing the operating costs of the PO (see PART 3 below);
- (c) the challenges the PO is facing (see PART 4 below); and
- (d) whether the PO is gradually eliminating cross-subsidisation among its mail services (see PART 5 below).

1.9 The audit has revealed that:

- (a) there is room for improvement in the financial performance of three new services of the PO, namely the postshop service, the e-post service and the remittance service (see PART 2 below);
- (b) it is possible for the PO to reduce its operating costs (see PART 3 below);
- (c) the PO needs to address the threats arising from one overseas postal administration and some overseas mailers bypassing the international mail system, competition in local mail, and an increasing use of electronic communication (see PART 4 below); and
- (d) the PO still has not been able to eliminate cross-subsidisation among its mail services although it implemented higher percentages of postage rate increase for those services incurring losses than those services generating profits in June 1995 and September 1996. Its bulk bag service continued to be heavily subsidised by other profitable services. In

2000-01, this service's operating loss of \$20.5 million constituted 65% of the PO's overall operating loss of \$31.5 million (see PART 5 below).

Audit has made a number of recommendations to address the above issues.

### **General response from the Administration**

1.10      **The Postmaster General** has said that:

- (a)      the PO agrees that its financial performance can be improved by reducing operating costs. Enhanced productivity and cost-savings have all along been actively pursued by the PO. At the top management level, the Postmaster General personally chairs a high-level Strategy Group on Sustained Profitability to steer departmental efforts in achieving increased productivity and cost-savings. At the operational level, the PO conducts regular workflow reviews, implements process re-engineering and increases the use of mechanisation in mail processing; and
  
- (b)      many branch post offices are not financially viable if the source of revenue is restricted to the PO's core services. To maintain the PO's infrastructure on a self-financing basis and to meet changing customer needs and fluctuating market demand, the PO needs to better utilise its infrastructure assets by providing new services that benefit customers and contribute towards diluting its fixed operating costs.

1.11      **The Secretary for the Treasury** generally agrees with Audit's recommendations.

## **PART 2: THE PO's ATTEMPTS TO IMPROVE FINANCIAL PERFORMANCE**

### **Introduction of new services**

2.1 In order to improve its financial performance, in recent years, the PO has introduced new services in addition to its traditional mail services. However, Audit has found that there is room for improvement in the financial performance of some new services of the PO. In Report No. 36 of the Director of Audit of March 2001, Audit has made a number of recommendations on the certification authority service and the logistics service provided by the PO. In this PART, the effectiveness of the PO's following three new services in improving its financial performance will be discussed: the postshop service (see paras. 2.2 to 2.10 below), the e-post service (see paras. 2.13 to 2.20 below) and the remittance service (see paras. 2.23 to 2.28 below).

### **Postshop service**

2.2 In December 1996, the PO launched the postshop service by opening a Postshop in an area which was set aside and refurbished as a standalone retail outlet at the General Post Office (GPO). The postshop service involves selling different types of souvenirs and postal accessories to customers.

### **Postshops financially not viable**

2.3 In June 1997, the PO completed a review of the postshop service. The review found that:

- (a) it was financially not viable to operate Postshops; and
- (b) to save operating costs, at the GPO, the Postshop should be merged with the Philatelic Counter.

2.4 In July 1997, the PO decided that no more new Postshops would be opened and instead, new Postshop Corners would be set up at selected branch post offices to provide the service. The PO envisaged that:

- (a) a Postshop Corner displaying various types of souvenirs and postal accessories would not be manned by dedicated staff; and
- (b) customers who wished to buy souvenirs and postal accessories would be served by the staff at postal counters of the branch post office.

2.5 In October 1999, the PO, upon realising that the poor financial performance of the postshop service was mainly attributable to the high staff costs of the dedicated staff manning the Postshop, decided to merge the Postshop with the Philatelic Counter at the GPO. The PO also planned to increase the number of Postshop Corners at various branch post offices because it was found that, being operated with existing resources, Postshop Corners were making positive contributions to the financial performance of the PO. However, in February 2000, owing to the high cost already incurred in establishing the Postshop, the PO decided to shelve the plan of merging the Postshop with the Philatelic Counter and keep the Postshop. As at 30 September 2001, there were 45 Postshop Corners at branch post offices.

### **Financial performance of postshop service**

2.6 The financial performance of the postshop service for the period 1997-98 to 2000-01 (Note 1) is summarised in Table 2 below. It can be seen from this table that:

- (a) the operating profit generated from the service decreased from \$25.7 million in 1997-98 to \$0.7 million in 1998-99; and
- (b) the service incurred an operating loss of \$2.1 million in 1999-2000 and its operating loss increased to \$4.1 million in 2000-01.

**Table 2**

**Financial performance of postshop service  
for the period 1997-98 to 2000-01**

Year	Operating profit/(loss) (\$ million)
1997-98	25.7
1998-99	0.7
1999-2000	(2.1)
2000-01	(4.1)

*Source: PO's records*

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**Note 1:** *Such information for the Postshop at the GPO was not available from the PO.*

2.7 In order to reduce operating costs, the PO has reduced the number of staff engaged in operating the Postshop at the GPO. In early 2000, a team of five staff, comprising one Senior Postal Officer and three Postal Officers working on a full-time basis and one Postman spending 50% of his duty time, operated the Postshop. For the quarter July to September 2001, the number of staff was reduced to four, comprising two Postal Officers working on a full-time basis and one Senior Postal Officer and one Postman, each spending 50% of their duty time at the Postshop.

### **Audit observations on postshop service**

2.8 **Audit has noted that:**

- (a) **in 1997, the PO found that it was financially not viable to operate Postshops (see para. 2.3(a) above);**
- (b) **since 1998-99, the financial performance of the postshop service has deteriorated significantly (see para. 2.6 above); and**
- (c) **since early 2000, the PO has reduced the staff engaged in operating the Postshop at the GPO in order to reduce operating costs (see para. 2.7 above).**

2.9 In response to Audit's enquiry, in February 2002, the PO informed Audit that:

- (a) in assessing the profitability of the PO's ancillary services such as the postshop service, it would be more appropriate to include only the cost of additional resources incurred wholly and exclusively in providing the service rather than the full cost;
- (b) in the PO's 2000-01 Service Cost Statement, out of the 15.75 staff who were allocated to provide the postshop service, only two (13%) worked full time in providing the service. This was the only additional staff cost required to operate the service. The other 13.75 staff represented the total number of staff deployed to provide the service over the counter in all the branch post offices concerned. However, these 13.75 staff posts could not be saved even if the service was ceased; and
- (c) on the basis of the costing method mentioned in inset (a) above, the postshop service made a net positive contribution of \$2.4 million in 1999-2000 and \$622,000 in 2000-01.

2.10 **Audit agrees that in assessing the profitability of a PO's service, the PO needs to consider the cost of additional resources incurred in providing the service. However, it is also necessary to take into account the full cost of providing the service because this enables the**

**PO to have all relevant costing information for optimising the use of its resources, and to improve its profitability. Audit noted that the contribution of the postshop service as calculated by the PO decreased significantly by 74% from \$2.4 million in 1999-2000 to \$622,000 in 2000-01 (see para. 2.9 above). Audit considers that there is a need for the PO to continue finding ways of reducing the operating costs of its postshop service. The PO should also explore avenues of increasing the operating profit of the service.**

### **Audit recommendations on postshop service**

**2.11 Audit has recommended that the Postmaster General should:**

- (a) with a view to reducing the operating costs of the Postshop at the GPO, consider:**
  - (i) closing the Postshop and instead, setting up a Postshop Corner at the GPO to continue providing the postshop service; or**
  - (ii) merging the Postshop with the Philatelic Counter; and**
- (b) closely monitor the financial performance of the postshop service and explore avenues of increasing the operating income generated from the service.**

### **Response from the Administration**

**2.12 The Postmaster General has said that:**

- (a) the postshop service is part and parcel of the PO's various initiatives introduced to achieve the objective of widening the scope of business in branch post offices so that they would become financially more viable and productive over time;**
- (b) the operating results of the postshop service (see Table 2 in para. 2.6 above) have been extracted from the PO's Service Cost Statement. This Statement shows the full cost of providing the service as a "stand alone" project. The full cost includes an allocation of fixed costs such as accommodation and counter staff costs incurred in maintaining the postal infrastructure with or without the operation of the service;**
- (c) with a view to improving the financial performance of the postshop service, the PO will, as recommended by Audit, critically review the manpower deployment and the prospect**



of merging the Postshop with the Philatelic Counter at the GPO. The PO will also keep in view the development of postal collectibles and introduce popular and innovative items; and

- (d) as the postshop service provides a positive contribution to the PO's overall financial performance, the PO will not consider ceasing the service at this stage.

### **E-post service**

2.13 In June 1997, the PO launched the e-post service. With this service, electronic messages (including monthly statements, invoices and circular letters) are sent to e-post centres by electronic mail systems or through magnetic media. The e-post centres convert the customers' electronic messages to traditional paper mail items (by printing the messages and enveloping them) which are then delivered to the recipients.

### **Service established by giving price concessions**

2.14 In order to secure a few large customers to use the e-post service and to establish its position in the market, in September 1996, the PO decided to provide the service to the Rating and Valuation Department (RVD) and the Water Supplies Department (WSD) at very low prices for three years. The service agreement with the RVD expired in May 2000 and that with the WSD expired in November 2000. The new service agreement with the RVD came into effect in June 2000 and that with the WSD came into effect in December 2000. Under the new service agreements, the charges to the RVD and the WSD have been increased. As a result, in 2000-01, although there was no growth in the e-post mail traffic, the financial performance of the e-post service improved significantly.

### **Financial performance of e-post service**

2.15 The financial performance of the e-post service for the period 1997-98 to 2000-01 is summarised in Table 3 below. It can be seen from this table that:

- (a) since its introduction in 1997-98, the e-post service had been incurring operating losses; and
- (b) in 2000-01, there was a significant improvement in its financial performance.

The heavy operating losses in the first three years from 1997-98 to 1999-2000 were mainly due to the PO's pricing strategy in offering special price concessions to the RVD and the WSD.

**Table 3**

**Financial performance of e-post service  
for the period 1997-98 to 2000-01**

Year	Operating profit/(loss) (\$ million)
1997-98	(5.3)
1998-99	(7.3)
1999-2000	(3.1)
2000-01	(0.3)
<b>Total</b>	<b><u>(16.0)</u></b>

*Source: PO's records*

**Utilisation of printers and envelopers**

2.16 The PO has two e-post centres. In 2000, the centre in Tseung Kwan O operated 44 hours per week and the other centre in Kwun Tong operated 99 hours per week (Note 2). Based on their operating hours at that time, the utilisation rate of their printers was 56% and the utilisation rate of their envelopers was 82%. However, like other operational centres of the PO, the e-post centres can operate round-the-clock. Calculated on this basis, in 2000, the utilisation rate of the printers was 11% while that of the envelopers was 33%. Therefore, there was spare capacity at the e-post centres.

2.17 The PO has been anxious to secure new customers for its e-post service. Since May 1998, a dedicated account manager has been assigned to market the service. Marketing tools such as presentations and seminars were used to promote the service. Promotional leaflets were distributed to potential customers.

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**Note 2:** *As at 1 February 2002, the operating hours of these two e-post centres were similar to those in 2000.*

2.18 Despite the marketing efforts, the PO has not been very successful in securing new customers for its e-post service. According to the market information collected by the PO in mid-2001, the market for the service was very competitive. Besides the PO, there were other operators providing similar services in the market. These competitors offered very competitive prices. As a result, the PO could not increase the utilisation of the printers and envelopers to earn more revenue.

### **Audit observations on e-post service**

2.19 **Audit has found that:**

- (a) **since its introduction in 1997-98, the e-post service has been incurring operating losses (see para. 2.15 above);**
- (b) **in 2000, there was spare capacity at the e-post centres (see para. 2.16 above); and**
- (c) **the PO has not been very successful in securing new customers for its e-post service (see para. 2.18 above).**

2.20 **Audit considers that there is a need for the PO to explore avenues of securing new customers for its e-post service.**

### **Audit recommendations on e-post service**

2.21 **Audit has *recommended* that the Postmaster General should:**

- (a) **conduct a review on the market position and competitiveness of the PO's e-post service, taking into account the terms offered by other service providers in the market. The review should identify practical ways for the PO to secure new customers; and**
- (b) **if the results of the review indicate that the PO's e-post service is competitive, take necessary actions to increase the PO's market share (e.g. by revising its marketing strategy and carrying out more intensive marketing campaigns). Otherwise, the Postmaster General should consider ceasing the service so that the resources can be redeployed to provide other more profitable services.**

## **Response from the Administration**

2.22 The **Postmaster General** has said that:

- (a) the e-post service is expected to break even in 2001-02. To further enhance its profitability for the year 2002-03, the PO is actively negotiating with a number of potential customers to bring in additional revenue and to enhance the utilisation of the printers and envelopers;
- (b) the following contributions should also be taken into account in assessing the financial viability of the e-post service from the overall perspective:
  - (i) postal revenue generated through locking in e-post customers to use the one-stop shop postal service; and
  - (ii) savings in total postal operating costs through bulk processing, and improved addressing format leading to an increase in the read-rate of automatic sorting machine in processing the e-post items; and
- (c) accordingly, the PO will not cease this service at this stage. However, the PO will continue to assess the market situation and review its market position and competitiveness.

## **Remittance service**

2.23 In 1994, due to keen competition from banks, the PO ceased its remittance service with 13 overseas postal administrations, including the Philippine Post.

2.24 In 1996, the PO considered that there was a need for it to provide remittance service to Mainland China in view of the increasing demand by philatelists there to remit money to the PO for ordering philatelic products. Therefore, it started negotiations with the China Post with a view to launching a remittance service for Mainland China. In the same year, the PO considered that there was also a market for remittance service for the Philippines because there were a large number of Philippine domestic helpers in Hong Kong who needed to remit money home. Therefore, the PO studied the potential for developing a remittance service with the Philippine Post.

### **Remittance service was expected to be competitive**

2.25 In June 1999, the Executive Council (ExCo) approved a Post Office (Amendment) Regulation under the Post Office Ordinance (Cap. 98) to facilitate the PO to provide remittance service with the China Post and the Philippine Post. ExCo was informed that:

- (a) the PO believed that the remittance service provided by the PO with these two postal administrations would be competitive; and
- (b) the proposed remittance service was expected to generate an annual revenue of \$2.3 million by way of commission received.

### **Audit observations on remittance service**

2.26 The PO introduced the remittance service for the Philippines in December 1999 and the remittance service for Mainland China in March 2000. **However, Audit has found that the service is not as successful as the PO anticipated. In 2000-01, the revenue generated from the service was only \$243,000, which was 11% of the estimated annual revenue of \$2.3 million. An operating loss of \$4 million was incurred for the service in 2000-01.**

2.27 In response to Audit's observations, in February 2002, the PO informed Audit that:

- (a) in assessing the profitability of the PO's ancillary services such as the remittance service, it would be more appropriate to include only the cost of additional resources incurred wholly and exclusively in providing the services rather than the full cost;
- (b) in the PO's 2000-01 Service Cost Statement, out of the 9.47 staff who were assigned to provide the remittance service, only one staff in the PO's Financial Services Division was assigned to provide back-office support exclusively on the service on a part-time basis. This was the only additional staff cost incurred in providing the service. The remaining 9 staff were the total front-line staff resources for providing the service throughout the PO's counter network. However, these 9 staff posts could not be saved even if the service was ceased; and
- (c) on the basis of the costing method mentioned in inset (a) above, the contribution from the remittance service in 2000-01 amounted to over \$86,000.

2.28 **Audit agrees that in assessing the profitability of a PO's service, the PO needs to consider the cost of additional resources incurred in providing the service. However, it is also necessary to take into account the full cost of providing the service because this enables the PO to have all relevant costing information for optimising the use of its resources, and to improve its profitability. Audit noted that, even if the costing method in paragraph 2.27(a) above was adopted, the contribution of the remittance service in 2000-01 as calculated by the PO was very small (see para. 2.27(c) above). Audit therefore considers that there is a need**

**for the PO to further promote the remittance service so as to increase the operating profit of the service. If the demand for the service continues to be low, the PO should consider ceasing the service.**

### **Audit recommendations on remittance service**

**2.29 Audit has recommended that the Postmaster General should:**

- (a) conduct a review on the competitiveness of the PO's remittance service taking into account the services offered by competitors in the market; and**
- (b) if the results of the review indicate that the PO's remittance service is competitive, take necessary actions to increase the PO's market share (e.g. by revising its marketing strategy and carrying out more intensive marketing campaigns). Otherwise, the Postmaster General should consider ceasing the service so that the resources can be redeployed to provide other more profitable services.**

### **Response from the Administration**

**2.30 The Postmaster General has said that:**

- (a) the remittance service is part and parcel of the PO's various initiatives introduced to achieve the objective of widening the scope of business in branch post offices so that they would become financially more viable and productive over time;**
- (b) the operating results of the remittance service mentioned in paragraph 2.26 above have been extracted from the PO's Service Cost Statement. This Statement shows the full cost of providing the service as a "stand alone" project. The full cost includes an allocation of fixed costs such as accommodation and counter staff costs incurred in maintaining the postal infrastructure with or without the operation of the service; and**
- (c) during the period April to December 2001, a total of 4,017 transactions were made under the remittance service. The service provides a convenient alternative to a certain sector of the community who wish to remit small sums of money. However, the PO will, as recommended by Audit, conduct a review on the competitiveness of the service, taking into account the service offerings of both existing and potential competitors of the PO, the outcome of the PO's further negotiations with other postal administrations and the PO's efforts to expand the service network to more destinations.**

## **PART 3: SCOPE FOR REDUCING OPERATING COSTS**

### **Potential for reducing operating costs**

3.1 The financial performance of the PO can be improved by reducing its operating costs. Audit has found that there is scope for the PO to do so by:

- (a) reducing the delivery frequency of its delivery beats (see paras. 3.2 to 3.16 below); and
- (b) strengthening the control over overtime (OT) work of its delivery postmen and their claims for OT allowance (see paras. 3.19 to 3.36 below).

### **Delivery frequency**

3.2 As at 31 August 2001, the PO operated 1,690 delivery beats in 21 delivery offices (DOs) covering the entire territory. Each delivery beat was served by one delivery postman. Among these delivery beats:

- (a) 1,238 delivery beats made one delivery a day. These delivery beats are hereinafter referred to as once-delivery beats; and
- (b) the remaining 452 delivery beats made two deliveries a day. These delivery beats are hereinafter referred to as twice-delivery beats (see Appendix A).

In total, the PO deployed about 1,850 delivery postmen (including about 160 delivery postmen as leave reserve) to provide the delivery service.

3.3 The PO's aim is to provide residential areas with one delivery a day and commercial and industrial areas with two deliveries a day. The frequency of delivery is laid down in the PO's Departmental Rules. According to the rules:

- (a) areas which are almost entirely residential will receive one delivery a day;
- (b) areas which are receiving two deliveries a day will continue to receive two deliveries a day, even though they are largely residential; and

- (c) new housing developments will receive the same number of deliveries a day as the areas nearby.

### **Reduction of delivery frequency of some delivery beats in 1989**

3.4 In the late 1980s, many residential areas still received two deliveries a day. This was because:

- (a) some commercial establishments were located in the residential areas; and
- (b) areas which were receiving two deliveries a day for historical reasons continued to receive two deliveries a day.

3.5 In 1989, the PO conducted a trial in Mei Foo Sun Chuen and Wah Fu Estate to ascertain the feasibility of converting the twice-delivery beats in these two areas to once-delivery beats. The results of the trial indicated that:

- (a) the reduction in delivery frequency was accepted by both the customers in these two areas and the delivery postmen concerned; and
- (b) converting twice-delivery beats to once-delivery beats could reduce the manpower involved in providing the delivery service by 17%.

3.6 In May 1990, in view of the success of the trial, the PO converted 514 twice-delivery beats which were at that time serving areas that were largely residential, out of a total of 971 twice-delivery beats, to once-delivery beats. In doing so, the PO:

- (a) did not receive strong public complaints (although there were some complaints from customers in the Wan Chai district);
- (b) did not receive any complaints from the delivery postmen concerned; and
- (c) was able to release 151 delivery postmen from delivery duties.



## Delivery frequency and service standard

3.7 The PO's performance pledge is that 98% of locally posted letters are delivered to addressees by the working day following the day the letters are posted. Every month it conducts Quality of Service Surveys on about 20 delivery beats at various DOs to ascertain whether the performance pledge is achieved.

3.8 The actual performance of delivering locally posted letters during the two-year period January 2000 to December 2001 is summarised in Table 4 below. It can be seen from this table that during this period, nearly all of these letters were delivered to addressees by the following day. Therefore, the PO had achieved its performance pledge. However, the performance of twice-delivery beats was only slightly better than that of once-delivery beats by 1.2%.

**Table 4**

**Percentages of locally posted letters delivered  
to addressees by the following working day  
during the period January 2000 to December 2001**

<b>Period</b>	<b>Once-delivery beats</b>	<b>Twice-delivery beats</b>	<b>Performance improvement of twice-delivery beats</b>
	<b>(a)</b>	<b>(b)</b>	<b>(c) = (b) - (a)</b>
	<b>(Percentage)</b>	<b>(Percentage)</b>	<b>(Percentage)</b>
January to June 2000	99.4%	99.8%	0.4%
July to December 2000	99.0%	99.9%	0.9%
January to June 2001	98.1%	99.9%	1.8%
July to December 2001	98.3%	99.9%	1.6%
<b>Average</b>	<b>98.7%</b>	<b>99.9%</b>	<b>1.2%</b>

*Source: PO's records*

### **Volume of mail items delivered in second delivery of twice-delivery beats**

3.9 During the period April to September 2001, the PO carried out Quality of Service Surveys (see para. 3.7 above) on 46 twice-delivery beats. The results of the Surveys are summarised in Appendices B and C. It can be seen that:

- (a) 24% of the twice-delivery beats delivered not more than 50 mail items daily in the second delivery (see Appendix B); and
- (b) 30% of the twice-delivery beats delivered not more than 5% of the daily mail items in the second delivery (see Appendix C).

### **Opinion survey of commercial customers on delivery frequency**

3.10 In 1999-2000, the PO conducted a survey on the opinions of commercial customers about delivery frequency. It interviewed 630 commercial customers in five districts, namely Cheung Sha Wan, Kowloon Central, Shatin, Tsuen Wan and Yuen Long. Only two customers objected to reducing the daily delivery frequency to once a day.

### **Potential saving if all twice-delivery beats are converted to once-delivery beats**

3.11 As mentioned in paragraph 3.6 above, in May 1990, the PO was able to release 151 delivery postmen from delivery duties by converting 514 twice-delivery beats to once-delivery beats. Applying this amount of manpower saving to the existing 452 twice-delivery beats (see Appendix A), Audit has estimated that, if the PO adopted only once-delivery beats throughout Hong Kong, 133 ( $151 \times 452/514$ ) delivery postmen could be redeployed to perform other duties. The resultant potential annual saving in staff costs would be \$38.2 million (\$287,323 per delivery postman  $\times$  133 delivery postmen).

### **Audit observations on delivery frequency**

3.12 **Audit has found that:**

- (a) **during the period January 2000 to December 2001, the performance of twice-delivery beats was only slightly better than that of once-delivery beats by 1.2% (see para. 3.8 above); and**
- (b) **during the period April to September 2001:**

- (i) **24% of the twice-delivery beats delivered not more than 50 mail items daily in the second delivery; and**
- (ii) **30% of the twice-delivery beats delivered not more than 5% of the daily mail items in the second delivery (see para. 3.9 above).**

3.13 In response to Audit's enquiry, in February 2002, the PO informed Audit that:

- (a) twice-delivery was only provided to mainly commercial and industrial areas, which provided the life line of the business community. To better serve its customers and to increase its productivity, the PO's delivery arrangement was such that 80% of mail items for the commercial and industrial areas were delivered in the morning. In the afternoon session, non-time sensitive and relatively heavy items were delivered. This would ensure that the business community was able to respond to any incoming mail items at the end of the working day. The mail traffic in commercial and industrial areas, in terms of both quantity and weight, was significantly heavier than that in residential areas; and
- (b) bulky packets and printed matters made up a significant portion of the mail delivery load. The average load for a delivery postman ranged from 45 to 90 kilogrammes in the morning. It was extremely difficult for a delivery postman to completely deliver all the mail items in one delivery round. On a practical basis, supplementary afternoon delivery would be required in commercial and industrial areas in order to clear all the mail items of the day.

3.14 However, Audit's further analysis indicates that, out of the 120 delivery beats covered by the PO's Quality of Service Surveys during the period April to September 2001 (see para. 3.9 above), the average weight of mail delivered by each of the 46 twice-delivery beats exceeded that delivered by each of the remaining 74 once-delivery beats by only 2%. The average number of mail items delivered by each of the 74 once-delivery beats exceeded that delivered by each of the 46 twice-delivery beats by 29%.

3.15 Audit has also noted that, in order to avoid causing physical strain to delivery postmen and to improve work efficiency, the PO has, among others:

- (a) installed pouch boxes along the delivery beats. Delivery postmen do not have to carry heavy mail items from the DOs to the delivery beats because such mail items are lodged in the pouch boxes prior to delivery; and
- (b) provided delivery postmen with delivery vehicles and handcarts, where necessary.

3.16 Based on the above findings, Audit considers that it is feasible for the PO to reduce its delivery frequency from twice to once a day. There is a need for the PO to consider converting its existing twice-delivery beats to once-delivery beats. If the PO adopted once-delivery beats throughout Hong Kong, 133 delivery postmen could be redeployed to perform other duties. The resultant potential annual saving in staff costs would be \$38.2 million (see para. 3.11 above).

### **Audit recommendations on delivery frequency**

3.17 Audit has *recommended* that the Postmaster General should:

- (a) conduct a comprehensive review of the existing twice-delivery beats so as to identify those delivery beats which can be converted to once-delivery beats, taking into account:
  - (i) the number and percentage of mail items delivered in the second delivery; and
  - (ii) the possible effects of the conversion on the service standard;
- (b) for those twice-delivery beats which cannot be converted to once-delivery beats, review the workload of the delivery postmen in the second delivery and improve the efficiency of the second delivery by combining the delivery beats for the second delivery; and
- (c) redeploy those delivery postmen, who have become surplus to requirement as a result of the conversion exercise, to perform other postal duties.

### **Response from the Administration**

3.18 The Postmaster General has said that:

- (a) the potential annual saving of \$38.2 million is calculated on the assumption that all the existing 452 twice-delivery beats will be converted to once-delivery beats. This means that after the conversion, there will be no twice-delivery beats throughout the territory. This reduction in delivery frequency will seriously impede the efficiency and competitiveness of the business community because a substantial portion of the daily mail

in commercial and industrial areas would, in the circumstances, be received in the afternoon (Note 3). It will also render the operation of the PO's Speedpost and Local CourierPost by the regular delivery beats impossible. This is because these services have a half-day delivery standard and require the delivery postmen in commercial and industrial areas to make two deliveries a day. The alternative is to arrange special teams to deliver these time-sensitive Speedpost and Local CourierPost items at much higher costs (Note 4);

- (b) Audit's calculations of the average weight and number of mail items delivered by the 46 twice-delivery beats and 74 once-delivery beats in question, based on the data of the days of survey (see para. 3.14 above), are correct. However, the PO would like to point out that it is inappropriate to compare directly average daily mail volume figures for these two types of delivery beats in the manner Audit suggested, for the purpose of assessing the difference in their daily workload. Allowance has to be made for the fact that the delivery postmen perform indoor mail preparation work and travel outdoor twice for twice-delivery beats and once only for once-delivery beats (Note 5);
- (c) although the delivery workload of twice-delivery beats in the afternoon is lighter, the PO ensures that upon completion of their delivery duties, the delivery postmen will continue to be gainfully employed. They are required to perform indoor duties (e.g. documentation of registered items) so as to reduce the mail preparation time for the following morning (Note 6);

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**Note 3:** *In Audit's view, the PO should convert the existing twice-delivery beats to once-delivery beats as far as possible. Some twice-delivery beats can be retained if the number and percentage of mail items which must be delivered in the second delivery justify this practice (see para. 3.17(a) and (b) above). Furthermore, it is worth noting that according to the PO's survey conducted in 1999-2000, only two commercial customers (out of 630) objected to reducing the daily delivery frequency to once a day (see para. 3.10 above).*

**Note 4:** *According to Audit's analysis of the 46 twice-delivery beats covered by the PO's Quality of Service Surveys during the period April to September 2001 (see para. 3.9 above), only 11 delivery beats delivered Speedpost and Local CourierPost items in the second delivery on the day of survey and the total number of such items delivered was 19. Audit considers that it is not cost-effective to retain so many twice-delivery beats for delivering such a small number of Speedpost and Local CourierPost items. Special arrangements could be made to deliver such urgent mail items.*

**Note 5:** *In Audit's view, converting twice-delivery beats to once-delivery beats should reduce the time taken for mail preparation work and outdoor travelling because the work would be completed in one delivery round instead of two delivery rounds and hence should increase the efficiency of the delivery beats.*

**Note 6:** *In Audit's view, converting twice-delivery beats to once-delivery beats will enable the delivery postmen to have more time to perform other postal duties.*

- (d) for the reasons mentioned in paragraph 3.13 and insets (a) to (c) above, it may not be in the community's interest to further reduce the number of twice-delivery beats at this stage. However, as and when there are changes in the mail pattern, the PO will certainly conduct another review to determine the optimum delivery frequency. In August 2001, the PO started another delivery beat revision at DOs (Note 7). Audit's suggestion will be considered in the exercise; and
  
- (e) the PO considers that Audit's recommendation on combining the delivery beats in the afternoon session will cause supervisory and operational difficulties (Note 8). The reshuffling of the postman delivery routes and boundary necessitates changes in mail sorting plans during the day, thus adversely affecting the accuracy and efficiency of the mail delivery service. This is because, even though a delivery point may be served by different delivery postmen on a daily basis depending on the actual workload, this will cause confusion to the supervisor and members of the public alike and may likely disrupt the "postman ambassador" image which the PO is trying very hard to establish.

### **OT work of delivery postmen**

#### **Government's guidelines on administration and control of OT**

3.19 In May 1998, following a number of reviews completed by the Independent Commission Against Corruption, the Civil Service Bureau (CSB) issued a set of revised guidelines on the administration of OT by Circular No. 10/98. According to the guidelines:

- (a) OT work may only be undertaken when it is strictly unavoidable;
  
- (b) it is the personal responsibility of a Head of Department to ensure that:
  - (i) OT work is kept to the minimum compatible with operational requirements; and
  
  - (ii) at all times, OT work is strictly controlled and properly supervised;

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**Note 7:** *Up to 31 January 2002, this delivery beat revision had not been completed.*

**Note 8:** *Audit considers that, if the PO's management is committed to actively enhancing productivity and reducing operating costs (see para. 1.10(a) above), the supervisory and operational difficulties arising from the combination of the twice-delivery beats in the afternoon session should not be insurmountable.*

- (c) a minimum period of one hour of OT in respect of any one shift must be worked before OT allowance is payable. The allowance is payable on a half-hourly basis thereafter; and
- (d) to ensure close supervision of OT work, the work output during the OT period should be monitored, preferably against established work measurement standards.

3.20 In November 2000, following a review of the OT policy, the CSB issued Circular No. 18/2000 (which replaced CSB Circular No. 10/98) on the administration and control of OT. CSB Circular No. 18/2000 restates the guidelines referred to in paragraph 3.19 above and provides additional guidelines to strengthen controls on OT work.

### **Components of duty time of delivery postmen**

3.21 As mentioned in paragraph 3.2 above, as at 31 August 2001, the PO operated 1,690 delivery beats covering areas on Hong Kong Island and in Kowloon and the New Territories. Each delivery beat was served by one delivery postman.

3.22 Letters collected locally or received from overseas are sent to the three sorting centres, namely the GPO, the International Mail Centre and the Air Mail Centre. At the sorting centres, the letters are sorted according to the DOs. After sorting, letters are sent to the DOs. At the DOs, letters are further sorted according to the delivery beats before they are passed to the delivery postmen. Delivery postmen then sort the letters according to the delivery sequence along the delivery beat. The time required by delivery postmen to sort the letters according to the delivery sequence is referred to as preparation time. After sorting the letters, delivery postmen deliver them to the addressees. The time taken is referred to as delivery time (which includes travelling time). The duty time of delivery postmen is made up of preparation time and delivery time. Audit's analysis of the duty time of delivery postmen has revealed that there is scope for reducing the OT work of delivery postmen.

### **New work standards for preparation work**

3.23 In March 1999, the PO completed a study to establish the standards for the preparation work of delivery postmen. During the study, the PO's Beat Survey Team surveyed 80 randomly selected delivery beats covering all DOs and all delivery patterns (such as delivery to the letter boxes on the ground floor of multi-storey buildings, door-to-door delivery and rural area delivery). In setting the work standards, the Beat Survey Team had included:

- (a) a 15% rest allowance in the preparation time to take account of normal fatigue element, and the time for personal needs of delivery postmen; and

- (b) the time required for sorting letters, handling registered items and mail redirection, and bundling and packing pouches.

3.24 After consultation with the staff unions, in August 2000, the PO formally promulgated the work standards.

#### **Beat revision exercise of 1999 using new work standards**

3.25 In May 1999, the PO commenced an extensive beat revision exercise. In this exercise, its Beat Survey Team studied the work of delivery beats. The Beat Survey Team recorded, for each delivery beat, the number of mail items delivered and the delivery time required. The Beat Survey Team then revised the delivery beats so as to even out the workload of the delivery beats. The revision was based on the mail traffic, the new work standards for preparation work and the delivery time recorded. The PO considered that:

- (a) after the revision of the delivery beats, delivery postmen should not have difficulties in finishing their daily work within the scheduled working time, unless there was a sudden large increase in the mail volume; and
- (b) for handling any unexpected additional mail volume, the extra time would be largely incurred in carrying out mail preparation work. The extra delivery time would be insignificant.

The PO's senior management has pledged that every effort would be made to assist individual delivery postmen to meet the work standards. However, it also announced that it would take disciplinary action against those delivery postmen who deliberately slowed down their work pace.

#### **Assessment and approval of OT work**

3.26 The Superintendent of Posts in charge of a DO monitors the workload of the DO and, if necessary, recommends OT work. The Assistant Controller of Posts of the DO then checks the request. If the Assistant Controller of Posts is satisfied that the requested OT work is justified, he will endorse the recommendation and forward the recommendation to the Controller of Posts for approval.

3.27 Some delivery postmen are required to report for duty earlier than the start time of their official working hours (hereinafter referred to as conditioned working hours). The extra working time (usually one hour daily before the start of the day's conditioned working hours) qualifies the delivery postmen to claim OT allowance.



3.28 From the PO management's point of view, OT work can only be justified if:

- (a) there is sufficient work to be performed by the delivery postmen; and
- (b) the work is performed according to the PO's established work standards.

3.29 In assessing the OT work of a delivery postman and to ensure that all approved OT work follows the guidelines of the CSB (see paras. 3.19 and 3.20 above), the PO's management:

- (a) is required to regularly monitor the actual mail traffic of each delivery beat; and
- (b) is required to assess the time required by a delivery postman to finish the daily mail delivery work based on the PO's work standards.

3.30 However, if on a particular day, the mail volume of a delivery beat drops to a level significantly below the original expectation of the PO's management, the total time needed by the delivery postman to finish his work (i.e. preparation work and delivery work) would decrease considerably. The delivery postman would be able to finish the work required of him within the conditioned working hours. The OT claim for that day can no longer be justified, unless other work can immediately be assigned to him before the end of the working hours.

#### **Audit's assessment of the workload of delivery beats**

3.31 In order to ascertain whether the OT claims of delivery postmen were justified, Audit used the same mathematical model adopted by the PO's Beat Survey Team to assess the workload of the 120 (6 × 20) delivery beats covered by the PO's Quality of Service Surveys (see para. 3.7 above) during the period April to September 2001. Based on the PO's new work standards (see para. 3.23 above), Audit calculated the time required by the delivery postmen to sort the mail items and deliver them to the addressees according to the mail counts recorded in the Surveys. Regarding the delivery time, if the mail counts indicated that the actual number of mail items was larger than the number of mail items which had been used by the PO for the delivery beats in the beat revision exercise (see para. 3.25 above), Audit allowed additional delivery time (excluding travelling time) for the delivery postmen to handle the additional mail items. Audit then calculated the total time required by the delivery postmen to finish their daily work, and ascertained whether OT work was really required. The results of Audit's analysis are summarised in Appendix D.

3.32 Audit's analysis indicated that, on the basis of the PO's mail counts, out of the 120 delivery beats covered in the PO's Survey, there were 52 delivery beats (43.3%) in which the OT claimed by the delivery postmen could not be justified by the workload (see the case illustration

in Appendix E). Upon further analysis of the OT claimed by the delivery postmen of these 52 delivery beats, Audit found that:

- (a) 9.1% of the delivery postmen of the 120 delivery beats claimed OT allowance for one hour per day. However, their workload did not justify any OT work;
- (b) 30% of the delivery postmen of the 120 delivery beats claimed OT allowance for one to two hours per day. However, their workload only justified less than one hour of OT work; and
- (c) 4.2% of the delivery postmen of the 120 delivery beats claimed OT allowance for more than one hour per day. However, their workload only justified 1 to less than 1.5 hours of OT work (see paras. 3.19(c) and 3.20 above).

Based on these findings, Audit further estimated that the total number of OT hours claimed by delivery postmen of all the 1,690 delivery beats, which could not be justified by workload, was 766 hours per day (see Appendix F). The annual OT allowance claimed by delivery postmen, which could not be justified by workload, would amount to \$21.3 million at 2001-02 prices (Note 9).

### **Audit observations on OT work of delivery postmen**

#### **3.33 Audit has found that:**

- (a) **based on the PO's mail counts, the OT claimed by some delivery postmen could not be justified by the workload; and**
- (b) **the estimated annual OT allowance claimed by delivery postmen of all the 1,690 delivery beats which could not be justified by workload would amount to \$21.3 million at 2001-02 prices (see para. 3.32 above).**

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**Note 9:** *Annual OT allowance which could not be justified by delivery postmen's workload at 2001-02 prices*

= *Hourly OT allowance rate × Unjustified number of OT hours claimed per day × Number of working days a year (excluding working days following a Sunday or a public holiday — as the mail traffic on these working days is not typical)*

= *\$120 per hour × 766 hours per day × 232 days*

= \$21,325,440 (say \$21.3 million)

3.34 In response to Audit's enquiry on the assessment of daily workload of the delivery postmen, in February 2002, the PO informed Audit that:

- (a) in the real situation, the assessment of daily workload for a delivery postman was more complicated than the application of a mathematical formula based on predetermined ordinary mail preparation work standards (Note 10). Apart from the mail preparation work standards, supervisors were required to make on-the-spot judgement taking into account:
  - (i) the weight of the total mail volume. Heavy items warranted a longer handling time per item. The standard preparation work standards were not applicable;
  - (ii) unexpected increase in the volume of items requiring the proof of delivery (such as registered mail, Speedpost and Local CourierPost items) which would affect the pre-determined work schedule for delivery postmen (Note 11). The PO was committed to completing the delivery of the above time-sensitive items within half a day. In order to meet the target, supervisors were required to make on-the-spot decisions to change the delivery routes of delivery postmen. Such changes normally required both additional delivery time and travelling time. These factors should be assessed by the supervisors case by case, using their experience and local knowledge. There were no ready and simple guidelines for the supervisors to follow; and
  - (iii) contingencies such as unexpected late arrival of mail from sorting centres which would hinder the smooth mail preparation work by the delivery postmen and affect their output; and
- (b) estimating the delivery postmen's workload by simply applying the mail preparation work standards without taking into account the factors elaborated in inset (a) above was an over-simplification.

3.35 However, Audit's further analysis indicated that:

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**Note 10:** *The mathematical model used by Audit to assess the workload of the delivery postmen is the same as that used by the PO's Beat Survey Team. Furthermore, Audit has allowed additional time for the delivery postmen to deliver the additional mail items, although the PO considers that the extra delivery time for handling the additional mail volume is insignificant (see paras. 3.25(b) and 3.31 above).*

**Note 11:** *During the overall beat revision exercise, the PO's Beat Survey Team has already taken into account the time required for handling items which require the proof of delivery.*

- (a) out of the 120 delivery beats covered by the PO's Quality of Service Surveys during the period April to September 2001 (see para. 3.9 above), the average weight of mail delivered by each of the 52 delivery beats (in which the OT claimed by the delivery postmen could not be justified by their workload) exceeded that delivered by each of the 32 delivery beats (in which the delivery postmen did not claim any OT) by only 2%; and
- (b) the actual number of items which required the proof of delivery and which were delivered by the 52 delivery beats with unjustified OT was 6% less than the estimated number of items used by the Beat Survey Team for assessing the workload of the delivery postmen.

Audit has noted that the PO does not have records to show that the unjustified OT identified by Audit was due to the provision for contingencies such as unexpected late arrival of mail from sorting centres.

**3.36 Based on the above findings, Audit considers that there is a need for the PO to strengthen its control over the OT work of delivery postmen and their claims for OT allowance.**

#### **Audit recommendations on OT work of delivery postmen**

**3.37 Audit has *recommended* that the Postmaster General should:**

- (a) **review the PO's system of controlling and monitoring the OT work of delivery postmen to ensure that the guidelines in CSB Circular No. 18/2000 are fully complied with;**
- (b) **ensure that all approvals for OT work are based on the proper assessment of workload and that all delivery postmen perform their work strictly according to the PO's established work standards; and**
- (c) **ensure that a proper system of internal control is in place to regularly check the OT claims of delivery postmen against the workload of their delivery beats.**

#### **Response from the Administration**

**3.38 The Postmaster General has said that:**

- (a) the PO exercises very stringent control over the use of resources including OT. The PO has strictly followed the guidelines laid down by the CSB. All the requirements are clearly stipulated in the Departmental Rules. Instructions are periodically circulated to all staff serving as a reminder. Apart from well-defined approval procedures, there are many other rigorous control measures in place such as outdoor surprise checks by immediate supervisors, different types of supervisory checks by managers, and follow-up checks by a team of workload assessment staff from the Headquarters. All these measures are to ensure that there are full justifications for claiming OT;
- (b) the Independent Commission Against Corruption has also conducted periodical reviews on the PO's management control of OT. The last review was conducted in November 2000. It was a very comprehensive study which focused on the administration of staff attendance and OT. It examined all the existing controlling measures for granting OT and found that they conformed to the CSB's guidelines;
- (c) in the overall beat revision exercise conducted in 1999-2000, the PO further revised mail preparation work standards of delivery postmen, according to the nature of the delivery area and the mode of delivery. As a result, a set of more realistic mail preparation work standards for delivery postmen serving different types of buildings (rather than a generic work standard) has been adopted. With the introduction of the new work standards for mail preparation, the PO has been able to reduce the OT incurred for mail delivery by 35.5% (from 1,351,449 hours in 1998-99 to 871,298 hours in 2000-01) despite an increase of 7.6% (96 million items) in total mail traffic handled during the same period;
- (d) the mail preparation work standards mentioned in inset (c) above apply to indoor activities such as preparation and sorting of ordinary mail before the delivery postman departs for delivery work. They are not applicable to outdoor activities such as delivery of registered mail, Speedpost and Local CourierPost items which require delivery at door and the addressee's signature. These activities are quite time-consuming and normally require 4 to 6 minutes to complete the delivery of an item. Besides, when a delivery postman returns to the DO after delivery work, he also needs to handle those undeliverable items and return the signed delivery receipts to the sections concerned for record (Note 12);

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**Note 12:** *During the overall beat revision exercise, the PO's Beat Survey Team has already taken into account the time required for handling undeliverable items and items which require the proof of delivery. Furthermore, Audit's analysis indicated that the actual number of items which required the proof of delivery and which were delivered by the 52 delivery beats with unjustified OT was 6% less than the estimated number of items used by the Beat Survey Team for assessing the workload of the delivery postmen (see para. 3.35(b) above).*

- (e) the new mail preparation work standards have only provided a general yardstick to assess the standard time required for the indoor work. It is the responsibility of the field supervisors to exercise their discretion in scheduling duties for delivery postmen, including allocation of OT;
- (f) Audit's calculations of the average weight of mail delivered and the number of mail items requiring the proof of delivery (see para. 3.35 above) are correct. However, the PO would like to point out that it is inappropriate to compare the workload of the 52 delivery beats where OT was incurred on the days of survey and the 32 delivery beats where OT was not incurred on the days of survey based on these figures of average daily mail volume. The weight of mail delivered and the number of mail items requiring the proof of delivery represent only two of the many components which add up to the total workload of the delivery postmen (Note 13). Otherwise, some of the 32 delivery beats should have been allocated OT, just based on the weight of mail delivered on the days of survey;
- (g) the review of the workload of delivery postmen is a continuous process. The PO has recently introduced the following measures:
  - (i) shortening the review period from once every five years to once every two to three years;
  - (ii) introducing quarterly mail count to monitor the mail volume of individual delivery beats;
  - (iii) following up on individual delivery beats where there have been changes in delivery mode;
  - (iv) enhancing the PO's Beat Revision Analysis System that stores and computes relevant workload data for the review process; and

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**Note 13:** *The PO informed Audit that in assessing the workload of delivery postmen, apart from the mail preparation rates, there were three factors which the PO had to take into account, namely the weight of the total mail volume, the number of mail items requiring the proof of delivery, and contingencies such as unexpected late arrival of mail from sorting centres (see para. 3.34(a) above). Regarding the weight of mail and the number of mail items requiring the proof of delivery, the PO has not provided valid arguments to justify the claims for OT by delivery postmen. Regarding contingencies, the PO has not provided records to show that the OT claims were justified under this category (see para. 3.35 above). Furthermore, the PO has not spelt out the "many components" referred to above.*

- (v) reminding the supervisors to follow the CSB's requirement in granting OT work;  
and
  
- (h) the PO agrees that continuous work improvement and close monitoring of OT claims are essential. Hence in the long run, the PO also has the following improvement plans in hand:
  - (i) introducing new initiatives to standardise its work methods so as to set realistic and accurate work standards for delivery postmen. Specifically:
    - an implementation plan for adoption of an ergonomically-designed office fitting to facilitate the preparation work has been drawn up; and
  
    - letter trays will be used to contain sorted mail passed to delivery postmen, with a view to reducing the handling activities in mail preparation and facilitating daily mail count; and
  
  - (ii) developing a Delivery Management Information System to record the daily mail volume of individual delivery beats and to control the use of resources.

3.39 The **Secretary for the Civil Service** welcomes the audit report. The Secretary has said that, in the light of Audit's recommendations, he would urge the PO to review its system of controlling and monitoring of OT work, with a view to identifying improvement measures.

## **PART 4: THE PO's CHALLENGES**

### **Changing business environment**

4.1 With the growing trends of globalisation, deregulation and liberalisation in the communication market, the PO faces growing challenges in three areas, namely international mail, local mail, and an increasing use of electronic communication instead of traditional mail.

### **International mail**

4.2 The international mail service of the PO is a profitable service and cross-subsidises the local mail service. However, it is well known that one overseas postal administration and some overseas mailers have bypassed the international mail system by making their own arrangements to deliver mail items to addressees in Hong Kong. Consequently, the PO is facing the threat of losing profit from the international mail service. Details are elaborated in paragraphs 4.3 to 4.8 below.

### **An overseas postal administration bypasses the international mail system**

4.3 Traditionally, overseas postal administrations sent all their international mail items destined for Hong Kong to the PO for delivery via the international mail system. The PO charges these overseas postal administrations terminal dues (Note 14) for delivery of the mail received. The terminal dues are determined, largely based on the weight of mail delivered. Hence, the PO receives less terminal dues for handling a light-weight item than a heavy one. As an illustration of the price differential between the domestic postage and the terminal dues, the PO's postage is \$28 for delivering a first class packet weighing 2 kilogrammes posted locally. However, under the international mail system, the PO can charge the overseas postal administration about \$70 as terminal dues for delivering locally a similar item received. On the other hand, the PO only receives about \$0.7 as terminal dues to receive, sort and deliver an overseas mail item weighing 20 grammes, which is much less than the postage of \$1.3 for a local first class letter.

4.4 Since December 2000, one overseas postal administration has changed its arrangement for sending mail items to Hong Kong. Under this new arrangement, the overseas postal administration sends directly part of the mail items destined for Hong Kong to its agent here. The postal administration selects for delivery to its agent in Hong Kong those mail items which are heavier in weight and those mail items which are destined for the major business areas or high-density residential areas. The agent delivers such mail items to the addressees. However, the overseas postal administration delivers to the PO via the international mail system those light-weight items and those mail items which are costly to deliver by its agent (e.g. letters addressed to remote villages in the New Territories). In doing so, this overseas postal

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**Note 14:** *Terminal dues were introduced by the 1969 Tokyo Congress of the Universal Postal Union as a means of compensating postal administrations for the costs incurred in handling mail received.*



administration has deprived the PO of the chance of handling those mail items which are relatively more profitable to deliver.

4.5 The PO is worried that if other overseas postal administrations follow the practice of this overseas postal administration, it will further erode the PO's profit from the international mail service.

#### **Overseas mailers bypass the international mail system**

4.6 Some overseas mailers also bypass the international mail system to reduce their delivery costs. The overseas mailers transport mail items to their agents in Hong Kong as cargo. For those mail items which are of heavy weight and those mail items which are destined for the major business areas or high-density residential areas, the agents in Hong Kong will deliver them to the addressees. For those mail items which require costly delivery work, the local agents will pass them to the PO as local mail. In doing so, these overseas mailers make use of the subsidised local postal service, resulting in further operational losses to the PO.

4.7 Such overseas mailers pose a threat to the PO's profit from the international mail service because they initially send mail items to Hong Kong as cargo. Similar to the practice of the overseas postal administration mentioned in paragraph 4.4 above, they choose to give the PO those mail items which are costly to deliver. The PO has stated that it is very difficult to deter this practice because mail items brought into Hong Kong as cargo and then posted as local mail are not readily distinguishable from bona fide local mail in appearance.

#### **Loss of revenue**

4.8 A sizeable volume of the inward international mail is made up of heavy-weight items. If overseas postal administrations and mailers continue to bring international mail into Hong Kong as cargo, they exploit the local postage system and bypass the international mail system. The PO will lose a large sum of income in the form of terminal dues received from its international mail service. According to the PO's estimation in 2001, the loss of annual revenue from this source amounts to \$24 million.

#### **Local mail**

4.9 According to the Post Office Ordinance, the Postmaster General has the "exclusive privilege" of:

- (a) conveying letters from one place to another within Hong Kong;
- (b) sending letters out of Hong Kong for delivery outside Hong Kong; and

- (c) receiving letters brought into Hong Kong for delivery in Hong Kong or for transmission to some places outside Hong Kong.

4.10 The local mail service has been operating at a loss (see Table 5 below). The PO considers that the loss is caused not only by its high cost of maintaining a universal postal service because of its obligation to the community, but also by a noticeable increase in the scope and extent of competition.

**Table 5**  
**Financial performance of**  
**local mail service for the period 1996-97 to 2000-01**

Year	Operating profit/(loss) (\$ million)
1996-97	(83.8)
1997-98	(212.4)
1998-99	(411.5)
1999-2000	(444.0)
2000-01	(216.8)

*Source: PO's records*

4.11 The PO is aware that:

- (a) the barrier of entry to the local mail delivery industry is low. The PO's competitors have been successful in seizing the profitable mail delivery service covering the more densely populated areas, while leaving the PO to serve the remote areas at higher costs;
- (b) many courier firms are providing mail delivery service in Hong Kong. In recent years, the growth rate of the PO's local mail traffic in business districts and densely populated residential areas has been adversely affected, as a result of competition not only from local couriers but also from utility companies. According to the market information collected by the PO in mid-2001, the utility companies delivered 42% of their bills; and

- (c) consequently, the PO's market share in local mail service, particularly in respect of those mail items destined for major business areas or densely populated residential areas, may gradually decrease because the competitors have a strong competitive edge over the PO due to their flexible mode of operation.

### **Electronic communication replacing traditional mail**

4.12 The financial performance of the PO is also affected by the use of electronic communication which is growing steadily. Fax, electronic mail, electronic billing and electronic payment all have adverse impacts on the traditional mail service of the PO. Electronic communication erodes the mail volume handled by the PO and increases the unit cost of its mail service. Many companies, including financial institutions and utility companies, are striving to reduce paperwork and to use electronic billing and electronic payment. Audit expects that a significant proportion of bills and payments which are currently mailed will eventually be replaced by electronic billing and electronic payment methods. It is difficult to predict the timing and magnitude of mail being replaced by electronic communication and the financial consequences. However, this trend is detrimental to the PO's financial performance.

### **Audit observations**

4.13 **Audit has found that:**

- (a) **the PO loses \$24 million in annual revenue because one overseas postal administration and some overseas mailers exploit the low local postage rates and bypass the international mail system by bringing international mail into Hong Kong as cargo (see paras. 4.4, 4.6 and 4.8 above);**
- (b) **in recent years, the growth rate of the PO's local mail traffic in business districts and densely populated residential areas, which is a profitable business for the PO, has been adversely affected by the competition from local couriers and utility companies delivering their own bills (see para. 4.11(b) above); and**
- (c) **electronic communication will increasingly replace traditional mail to the detriment of the PO's income (see para. 4.12 above).**

4.14 **Audit noted that in January 2002, the Economic Services Bureau (ESB) and the PO were conducting a comprehensive review on postal policy and services. Audit considers that there is a need for the PO to find ways of addressing the threats it is facing.**

## **Audit recommendation**

4.15 Audit has *recommended* that in the comprehensive review on postal policy and services currently being conducted, the Postmaster General should, in conjunction with the ESB, critically examine the following threats posed to the PO and find practical ways of addressing them. The threats are:

- (a) overseas postal administrations transporting mail items to Hong Kong as cargo and arranging their agents in Hong Kong to deliver them locally;
- (b) overseas mailers transporting mail items to Hong Kong as cargo and arranging their agents in Hong Kong to deliver them or mail them locally;
- (c) the loss in volume of the PO's local mail in business districts and densely populated residential areas as a result of the competition from local couriers and utility companies delivering their own bills; and
- (d) the increasing use of electronic communication as an alternative to traditional mail.

## **Response from the Administration**

4.16 The Postmaster General agrees with Audit's recommendation.

4.17 The Secretary for Economic Services has said that the ESB will, in the comprehensive review on postal policy and services, address the issues raised by Audit.

## **PART 5: CROSS-SUBSIDISATION AMONG MAIL SERVICES**

### **Problem of cross-subsidisation raised in early 1990s**

5.1 In Report No. 20 of the Director of Audit of March 1993 on the PO's pricing strategy and service standards for local mail service and surface mail service, Audit pointed out that it was doubtful whether it was appropriate to continue subsidising the local mail service and the surface mail service. Audit recommended that the Postmaster General should review the pricing strategy of local mail service and surface mail service with a view to eliminating cross-subsidisation among different types of mail services.

5.2 In response to Audit's observations and recommendation:

- (a) the Postmaster General said that:
  - (i) the need to reduce cross-subsidisation as far as possible among mail services served as a guideline for determining the postage rates of individual services. This represented a long-term aim rather than a short-term aim; and
  - (ii) in the determination of postage rates, the guideline had to be applied with due regard to the political and social climate in Hong Kong and to public acceptability;
- (b) the Secretary for the Treasury said that cross-subsidisation among different types of services should be eliminated; and
- (c) the Secretary for Economic Services said that a review of the postal policy would be carried out soon.

5.3 In its Report No. 20 of July 1993, the Public Accounts Committee:

- (a) noted that a review of the postal policy, including the question of cross-subsidisation and the pricing strategy of the PO, would be conducted soon; and

- (b) saw no objection in principle to some cross-subsidisation among different types of mail services provided by the PO for so long as fees and charges were set at levels acceptable to the public and yet could produce a reasonable return on turnover.

5.4 In October 1993, in the Government Minute in response to the Public Accounts Committee's Report, the Administration stated that:

- (a) a review of the postal policy and a review on the rate of return of Government utilities were in progress; and
- (b) the issue of cross-subsidisation would be examined in the light of the conclusions of the reviews.

### **Measures to eliminate cross-subsidisation**

5.5 In April 1995, after reviewing the postal policy, the ESB pointed out that universal letter service, like most other universal public services, was traditionally provided on a loss-making basis, because of the need to keep the charges at a level affordable to all and of the disproportionate high costs of maintaining services to remote and low demand areas. The ESB accepted that elimination of cross-subsidisation to bring the charges more in line with the costs of providing the service was a good financial management discipline. Although the ESB considered that some element of cross-subsidisation was inevitable, on balance, it recommended that the PO should set, as a long-term postal pricing policy, the objective of gradually reducing the extent of cross-subsidisation.

5.6 Since 1995, the postage rates have been increased twice: once in June 1995 and once in September 1996. In these two revisions, despite the fact that the PO implemented higher percentages of postage rate increase for those services incurring losses than those services generating profits, cross-subsidisation still has not been eliminated. Audit has noted that, while the PO considers that the reduction of cross-subsidisation among different types of mail services represents a long-term aim rather than a short-term aim (see para. 5.2(a)(i) above), in 1996, the PO decided to achieve breakeven for the bulk bag service within three to four years (see para. 5.10 below).

5.7 Recently, the PO and the ESB have recognised that as revenue from the profitable services decreases, continuation of cross-subsidisation among mail services becomes increasingly untenable and needs to be phased out. In July 2001, in order to gradually eliminate cross-subsidisation and to achieve full-cost recovery for its loss-making mail services, the PO

decided to increase the postage rates of the local mail and the surface mail and to reduce those of the airmail with effect from 1 April 2002. Following this postage revision, the PO projected in mid-2001 that its operating loss in 2002-03 would be \$67 million. Nevertheless, even after this increase in postage rates, cross-subsidisation among mail services will still continue. An example of a heavily cross-subsidised mail service is the bulk bag service (see paras. 5.8 to 5.13 below).

### **Bulk bag service**

5.8 The bulk bag service provides for posting of printed matter in bulk quantity by surface mail to places abroad. Users of the service have to sort their mail items into mail bags provided by the PO. Each mail bag should contain mail items destined for one country only. Items which can be accepted under the bulk bag service are:

- (a) newspapers or periodicals printed and published in Hong Kong; and
- (b) books, pamphlets (except articles of commercial nature such as catalogues) or maps printed and published in Hong Kong or elsewhere.

### **Bulk bag service heavily subsidised by other postal services**

5.9 The bulk bag service has been incurring heavy operating losses and has been heavily subsidised by other profitable services. In 2000-01, the operating loss of the service was \$20.5 million, representing 65% of the PO's overall operating loss of \$31.5 million (see Table 1 in para. 1.6 above). The operating results of the bulk bag service for the period 1996-97 to 2000-01 are summarised in Table 6 below. It can be seen that during this period, the postage received from the service was insufficient to cover the total costs made up of:

- (a) the terminal dues paid by the PO to the postal administrations abroad;
- (b) the conveyance charges paid by the PO to the shipping companies; and
- (c) the local handling costs incurred by the PO on the service.

**Table 6**

**Operating results of bulk bag service for the period 1996-97 to 2000-01**

<b>Period</b>	<b>Postage received</b>	<b>Terminal dues paid by PO</b>	<b>Conveyance charges paid by PO</b>	<b>PO's local handling costs</b>	<b>Operating profit/(loss)</b>
	<b>(a)</b>	<b>(b)</b>	<b>(c)</b>	<b>(d)</b>	<b>(e) = (a) - (b) - (c) - (d)</b>
	<b>(\$ million)</b>	<b>(\$ million)</b>	<b>(\$ million)</b>	<b>(\$ million)</b>	<b>(\$ million)</b>
1996-97	123.4	127.3	4.9	6.1	<b>(14.9)</b>
1997-98	85.5	97.6	5.7	6.2	<b>(24.0)</b>
1998-99	72.5	69.4	4.5	8.3	<b>(9.7)</b>
1999-2000	56.3	54.2	2.9	10.3	<b>(11.1)</b>
2000-01	58.2	67.6	3.1	8.0	<b>(20.5)</b>
				<b>Total</b>	<b><u>(80.2)</u></b>

*Source: PO's records*

**Users of bulk bag service**

5.10 In mid-1996, the PO reported to the ESB and the Finance Bureau (FB) that:

- (a) there were only a few users of the bulk bag service;
- (b) the top four users of the service accounted for over 75% of the total traffic volume. The largest user of the service accounted for almost half of the total traffic volume; and
- (c) any increase in postage rates for the service would only affect a small number of users.

The PO, the ESB and the FB decided that the small group of business users of the bulk bag service should not be subsidised. They also set a target that the service would achieve breakeven within three to four years by increasing the postage rates for the service by six to seven percent above inflation each year.



5.11 In September 1996, the PO increased the postage rate of the bulk bag service by 15.5% (i.e. higher than the inflation rate of 9.1% since June 1995).

5.12 In 1998, the PO carried out a review on the bulk bag service for the period October 1997 to January 1998. The results of the review indicated that a few large users of the service still accounted for a very large percentage of the total postage. The top ten users accounted for 92.2% of the total postage.

5.13 Audit's review of the postage received from the major users of the bulk bag service indicated that during the period August to October 2001, the top ten users of the service accounted for 97.6% of the total postage (see Appendix G).

### **Audit observations**

5.14 In March 1993, Audit recommended that the Postmaster General should review the pricing strategy of local mail service and surface mail service with a view to eliminating cross-subsidisation among different types of mail services (see para. 5.1 above). In April 1995, after reviewing the postal policy, the ESB recommended that the PO should set, as a long-term postal pricing policy, the objective of gradually reducing the extent of cross-subsidisation among mail services, notwithstanding that the ESB considered that some element of cross-subsidisation was inevitable (see para. 5.5 above). **However, Audit has found that:**

- (a) **the PO implemented higher percentages of postage rate increase for those services incurring losses than those services generating profits in June 1995 and September 1996. However, the PO still has not been able to eliminate cross-subsidisation (see para. 5.6 above); and**
- (b) **the bulk bag service continued to be heavily subsidised by other profitable services. In 2000-01, the service's operating loss of \$20.5 million constituted 65% of the PO's overall operating loss of \$31.5 million (see para. 5.9 above). The PO's aim in 1996 of achieving breakeven for the service within three to four years has not materialised (see para. 5.10 above). The service to a few large customers has been heavily subsidised. For the period August to October 2001, the top ten users of the service accounted for 97.6% of the total postage (see para. 5.13 above).**

5.15 **Audit notes that:**

- (a) **in 1996-97 and 1997-98, the PO's windfall profits from the philatelic activities made it difficult for the PO to justify increasing the postage rates of the loss-making services in order to reduce the extent of cross-subsidisation;**

- (b) **during the years from 1998-99 to 2000-01, due to the adverse financial climate in Hong Kong, the PO froze its postage rates; and**
- (c) **in July 2001, in order to gradually eliminate cross-subsidisation and to achieve full-cost recovery for its loss-making mail services, the PO announced that the postage rates of the local mail and the surface mail would be increased and those of the airmail would be reduced with effect from 1 April 2002 (see para. 5.7 above).**

**In Audit's view, there is a need for the PO to continue its efforts to reduce cross-subsidisation among its different mail services.**

### **Audit recommendations**

**5.16 Audit has *recommended* that the Postmaster General should, in conjunction with the ESB and the FB:**

- (a) **continue taking action to reduce cross-subsidisation among the PO's different mail services, especially by improving the financial performance of those mail services which are currently incurring heavy losses; and**
- (b) **draw up a definite timetable to increase the postage rates for the bulk bag service so as to enable the service to achieve breakeven as soon as possible.**

### **Response from the Administration**

**5.17 The Postmaster General agrees with Audit's recommendations.**

Distribution of delivery beats as at 31 August 2001

Delivery Office	Number of once-delivery beats	Number of twice-delivery beats	Total number of delivery beats
Aberdeen	48	5	53
Cheung Sha Wan	74	16	90
Eastern	115	17	132
GPO	31	126	157
Kowloon Central	106	33	139
Kowloon City	113	21	134
Kowloon East	84	54	138
Ma On Shan	24	0	24
Outlying islands	28	1	29
Sai Kung	26	0	26
Sai Ying Pun	37	0	37
Shatin Central	72	15	87
Shek Wu Hui	47	0	47
Tai Po	46	3	49
Tseung Kwan O	33	1	34
Tsim Sha Tsui	0	70	70
Tsuen Wan West	113	48	161
Tuen Mun Central	67	8	75
Wah Fu	9	0	9
Wan Chai	84	33	117
Yuen Long	81	1	82
<b>Total</b>	<b><u>1,238</u></b>	<b><u>452</u></b>	<b><u>1,690</u></b>

Source: PO's records

**PO's survey results: Volume of mail items delivered daily  
in the second delivery of twice-delivery beats of some DOs  
during the period April to September 2001**

Delivery Office	Number of delivery beats which delivered the following numbers of mail items in the second delivery				Number of delivery beats surveyed
	1 to 50 items	51 to 100 items	101 to 200 items	201 to 600 items	
Cheung Sha Wan	-	1	1	-	2
Eastern	2	-	-	-	2
GPO	-	8	4	6	18
Kowloon Central	-	-	2	2	4
Kowloon City	1	1	-	-	2
Kowloon East	-	-	-	4	4
Shatin Central	-	-	1	1	2
Tsim Sha Tsui	8	-	-	-	8
Wan Chai	-	-	1	3	4
<b>Total</b>	<b><u>11 (24%)</u></b>	<b><u>10 (22%)</u></b>	<b><u>9 (19%)</u></b>	<b><u>16 (35%)</u></b>	<b><u>46 (100%)</u></b>

Source: Audit's analysis of PO's records

**PO's survey results: Percentage of mail items delivered daily  
in the second delivery of twice-delivery beats of some DOs  
during the period April to September 2001**

Delivery Office	Number of delivery beats which delivered the following percentages of mail items in the second delivery				Number of delivery beats surveyed
	0.1% to 5%	5.1% to 10%	10.1% to 20%	20.1% to 40%	
Cheung Sha Wan	2	-	-	-	2
Eastern	2	-	-	-	2
GPO	-	12	6	-	18
Kowloon Central	-	-	2	2	4
Kowloon City	2	-	-	-	2
Kowloon East	-	-	2	2	4
Shatin Central	-	-	2	-	2
Tsim Sha Tsui	8	-	-	-	8
Wan Chai	-	-	2	2	4
<b>Total</b>	<b><u>14</u> (30%)</b>	<b><u>12</u> (27%)</b>	<b><u>14</u> (30%)</b>	<b><u>6</u> (13%)</b>	<b><u>46</u> (100%)</b>

Source: Audit's analysis of PO's records

**Audit's analysis of workload of 120 delivery beats and  
OT claimed by the delivery postmen for the period April to September 2001**

<b>Delivery Office</b>	<b>Total number of delivery beats</b>	<b>Number of delivery beats analysed in the PO's surveys (Note)</b>	<b>Number of delivery postmen whose OT claims could not be justified by workload</b>
Aberdeen	53	4	4
Cheung Sha Wan	90	10	2
Eastern	132	8	3
GPO	157	18	2
Kowloon Central	139	8	6
Kowloon City	134	10	6
Kowloon East	138	10	1
Ma On Shan	24	2	0
Outlying islands	29	0	0
Sai Kung	26	2	1
Sai Ying Pun	37	0	0
Shatin Central	87	6	5
Shek Wu Hui	47	2	2
Tai Po	49	2	0
Tseung Kwan O	34	2	0
Tsim Sha Tsui	70	8	4
Tsuen Wan West	161	8	3
Tuen Mun Central	75	4	3
Wah Fu	9	2	1
Wan Chai	117	10	5
Yuen Long	82	4	4
<b>Total</b>	<b><u>1,690</u></b>	<b><u>120</u></b>	<b><u>52</u></b>

Source: *Audit's analysis of PO's records*

Note: *Every month, the PO conducts Quality of Service Surveys on about 20 delivery beats (see para. 3.7). Audit used the data of these surveys to assess the justifications for OT claims of delivery postmen.*

**A case to illustrate an unjustified OT claim of a delivery postman**

- (a) Total number of working hours of the delivery postman on the working day selected for audit review (including 7 conditioned working hours and 1 hour of OT claimed but excluding 1 hour lunch break) = 8
- (b) Actual mail volume of the delivery beat for that day as counted in the PO's Quality of Service Survey = 1,469 mail items
- (c) Audit's analysis of the time needed by the delivery postman (based on the PO's work standards) to finish his tasks on 1,469 mail items on that day
- = Preparation time (including allowance for normal fatigue and time for the personal needs of the delivery postman) + Delivery time (including travelling time)
- = 2 hours 2 minutes + 4 hours 18 minutes
- = **6 hours 20 minutes**

**Audit conclusion**

*The delivery postman needed 6 hours and 20 minutes to finish all his tasks. This is less than the 7 conditioned working hours of that day. Therefore, his one-hour OT claim for that day could not be justified.*

Audit's analysis of OT claimed by  
delivery postmen which could not be justified by workload

OT claimed per delivery beat	Unjustified OT claimed per delivery beat	Number of delivery beats with unjustified OT claims	Percentage of delivery beats with unjustified OT claims	Projected total unjustified OT claimed by delivery postmen of all 1,690 delivery beats
(a)	(b)	(c)	(d) = $\frac{(c)}{120} \times 100\%$	(e) = 1,690 × (d) × (b)
(Hours)	(Hours)		(Percentage)	(Hours)
<b>(A) Delivery beats whose workload could not justify any OT work</b>				
1.0	1.0	11	9.1%	154
		—	—	—
		<b>Subtotal</b>	<b>9.1%</b>	<b>154</b>
<b>(B) Delivery beats whose workload justified less than 1 hour of OT work</b>				
1.0	1.0	31	25.8%	436
1.5	1.5	3	2.5%	63
2.0	2.0	2	1.7%	57
		—	—	—
		<b>Subtotal</b>	<b>30.0%</b>	<b>556</b>
<b>(C) Delivery beats whose workload justified 1 to less than 1.5 hours of OT work</b>				
1.5	0.5	2	1.7%	14
2.0	1.0	3	2.5%	42
		—	—	—
		<b>Subtotal</b>	<b>4.2%</b>	<b>56</b>
		<b>Total</b>	<b>43.3%</b>	<b>766</b>

Source: Audit's analysis of PO's records



**Postage paid by top ten users  
of the bulk bag service for the period August to October 2001**

<b>User</b>	<b>Postage paid</b>	<b>Percentage of total postage paid</b>	<b>Cumulative percentage of total postage paid</b>
	<b>(\$ million)</b>	<b>(Percentage)</b>	<b>(Percentage)</b>
User 1	9.7	59.7%	59.7%
User 2	3.0	18.8%	78.5%
User 3	1.1	7.1%	85.6%
User 4	0.8	4.7%	90.3%
User 5	0.4	2.5%	92.8%
User 6	0.3	2.0%	94.8%
User 7	0.1	0.7%	95.5%
User 8	0.1	0.7%	96.2%
User 9	0.1	0.7%	96.9%
User 10	0.1	0.7%	<b>97.6%</b>

*Source: Audit's analysis of PO's records*

**Acronyms and abbreviations**

CSB	Civil Service Bureau
DO	Delivery Office
ESB	Economic Services Bureau
ExCo	Executive Council
FB	Finance Bureau
GPO	General Post Office
OT	Overtime
PO	Post Office
POTF	Post Office Trading Fund
RVD	Rating and Valuation Department
WSD	Water Supplies Department