September 24, 2004

JOHNRAY EGELHOFF
MANAGER, NEVADA-SIERRA DISTRICT

SUBJECT: Audit Report – Self-Service Vending Program – Nevada-Sierra District (Report Number DR-AR-04-009)

This is one of a series of audit reports on the Self-Service Vending Program in the Pacific Area. The report presents the results of our self-initiated audit on the Self-Service Vending Program in the Nevada-Sierra District (Project Number 04YG016DR004). The information in this district report will be included in a report to the Pacific Area Vice President.

Background

The Self-Service Vending Program, implemented in October 1964, is one of the Postal Service's major programs. It provides Postal Service customers with a convenient alternative for purchasing stamps and other basic Postal Service products after business hours and without the need to stand in line during business hours.

Nationwide, the Postal Service maintains approximately 30,000 vending machines (27,000 self-service postal centers and 3,000 other types of vending equipment) that generated over $1.9 billion in revenue during fiscal years (FY) 2001 through 2003. During FY 2003, the Pacific Area had 3,325 pieces of vending equipment that generated over $145 million in revenue. The Nevada-Sierra District maintained 7 percent (221) of the total area machines that generated over 6 percent ($9 million) of the total area vending revenue. During the first quarter of FY 2004, the Pacific Area had 3,395 pieces of vending equipment that generated over $37.3 million in revenue. The Nevada-Sierra District maintained 7 percent (226) of the total area machines that generated over 6 percent ($2.4 million) of the total area vending revenue.[1]

Objective, Scope, and Methodology

The objective of our audit was to determine whether the Self-Service Vending Program was effectively and efficiently meeting program goals of increasing revenue and

[1] During the first quarter of FY 2004, the Pacific Area had 70 additional vending machines and the Nevada-Sierra District had 5 additional vending machines.

1735 N Lynn St..
Arlington, VA 22209-2020
(703) 248-2100
Fax: (703) 248-2256

reducing operating costs. Specifically, in this review, we determined whether Self-Service Vending Program managers have effectively redeployed vending equipment that does not meet minimum revenue requirements in order to maximize revenue, and discontinued the use of obsolete vending equipment. We also physically observed a judgmental sample of 17 vending machines to determine whether the machines were operational and easily accessible. For the 221 vending machines operating in the Nevada-Sierra District in FY 2003, 34 were classified as obsolete based on Postal Service guidance, while the remaining 187 were classified as current equipment. For the first quarter of FY 2004, 226 vending machines were operating in the Nevada-Sierra District, of which 34 were classified as obsolete, and the remaining 192 were classified as current equipment.

During our audit, we visited Postal Service facilities and interviewed managers and employees; reviewed documentation and applicable policies and procedures; and analyzed data in the Postal Service's Vending Equipment Sales and Service System (VESS) for FY 2003 and the first quarter of FY 2004 to identify obsolete equipment and equipment that did not meet the minimum revenue requirements.[2] Although we relied on data obtained from VESS, we did not test the validity of the data and controls over the system.

Audit work associated with the Nevada-Sierra District was conducted from March through September 2004 in accordance with generally accepted government auditing standards and included such tests of internal controls as were considered necessary under the circumstances. We discussed our observations and conclusions with appropriate management officials and included their comments, where appropriate.

Prior Audit Coverage

The Office of Inspector General (OIG) has issued three reports related to the objective of this audit.

Self-Service Vending Program - Tennessee District (Report Number DR-AR-04-003, June 30, 2004), Self-Service Vending Program - Alabama District (Report Number DR-AR-04-004, June 30, 2004), and Self-Service Vending Program - Atlanta District (Report Number DR-AR-04-002, July 1, 2004). The reports stated that district officials could improve their process for redeploying vending equipment that does not meet minimum revenue requirements. In FY 2003, 54 percent (857 of 1,573 machines) of the vending machines in the Tennessee, Alabama, and Atlanta, Districts did not meet the minimum revenue requirements and the districts may have missed revenue opportunities totaling approximately $2.7 to $8.5 million by not redeploying this equipment. Additionally, these districts continued to use 250 obsolete machines and possibly incurred maintenance and repair expenses. Management agreed with all

[2] Obsolete equipment was not included in the minimum revenue analysis.

recommendations and the actions taken and planned were responsive to the recommendations.

Audit Results

Opportunities exist for Nevada-Sierra District officials to improve the effectiveness and efficiency of the Self-Service Vending Program and to meet or exceed program goals of increasing revenue and reducing operating costs. Specifically, Nevada-Sierra officials could increase revenue opportunities by redeploying equipment that does not meet minimum revenue requirements. Further, Nevada-Sierra District officials could possibly reduce maintenance and repair costs by discontinuing the use of obsolete equipment. However, our physical observation of vending machines in the Nevada-Sierra District indicated that overall the machines were operational and easily accessible.

Redeployment of Vending Equipment

Nevada-Sierra District officials could improve their process for redeploying vending equipment that does not meet Postal Service minimum revenue requirements. Specifically, during FY 2003, our review of the vending equipment revenue reports indicated that 55 percent (102 of 187) of the vending machines did not meet the minimum revenue requirements during FY 2003. Vending equipment sales were approximately $1.6 million, which was significantly less than the minimum revenue requirement of $3.2 million. As a result, the Nevada-Sierra District may have missed revenue opportunities of approximately $400,000 to $1.5 million by not redeploying this equipment.[3]

Additionally, during the first quarter of FY 2004, our review of vending equipment revenue reports indicated that 52 percent (100 of the 192 machines) of the vending machines did not meet the minimum revenue requirements. Vending equipment sales were approximately $336,000, which was significantly less than the minimum revenue requirement of $653,000. As a result, the Nevada-Sierra District may have missed revenue opportunities of approximately $317,000 by not redeploying this equipment.

One of the Self-Service Vending Program's goals is to increase revenue through the redeployment of equipment. The Postal Service should redeploy equipment that does not meet minimum revenue requirements to other locations. Postal Service policy, Handbook PO-102, Self-Service Vending Operational and Marketing Program, Chapter 2, Section 256, May 1999 (updated with Postal Bulletin revisions through December 25, 2003), establishes the minimum revenue requirements for vending

[3] For each vending machine, we calculated the shortfall in revenue compared to the established minimum for a particular machine type and referred to this shortfall as "missed revenue opportunities." The $400,000 represents the minimum total possible missed revenue opportunities after giving consideration to Postal Service guidance, which requires district officials to review revenue reports and take appropriate actions if a vending machine's revenue does not reach plan in three to six accounting periods. The $1.5 million represents the maximum total possible missed revenue opportunities for FY 2003 and is calculated by subtracting actual revenues generated from the total of all machine minimum revenue requirements.

machines. The district retail office is responsible for evaluating equipment revenue to find the right location for the right machine. If self-service vending equipment is located in an area where it is unable to generate enough revenue to meet the minimum requirement, the equipment must be considered for redeployment. If revenue does not meet the minimum requirement in three to six accounting periods, the district retail office should place the equipment on a list for redeployment; notify any office where changes will be made; prepare a typewritten or computer-generated notice, approved through the district retail office, to be posted in the lobby informing customers 30 days before removing the equipment; and complete Postal Service Form 4805, Maintenance Work Order*,* and move the equipment to a better location.

District officials took action to redeploy six vending machines that did not meet minimum revenue requirements during FY 2003.[4] For the remaining 181 machines, district officials did not initiate any redeployment action. Additionally, during the first quarter of FY 2004, district officials did not initiate any redeployment actions for the 100 underperforming machines. District officials did not initiate any redeployment action for the underperforming vending machines during FY 2003 and the first quarter of FY 2004 because of concern for the potential adverse impact on customer service due to the nonavailability of machines. District officials also indicated that the required replacement equipment needed for the redeployable locations had not yet been allocated to the district location. By not taking action to redeploy under performing equipment, the district could miss revenue opportunities during the remainder of FY 2004.

We discussed the results with Nevada-Sierra District officials and they agreed they could improve their redeployment process for equipment that does not meet the Postal Service's minimum revenue requirements. District officials stated that plans are being made to reassess vending machine locations based on trend analysis of historical vending data, communication with the self-service postal center technicians, and receipt of 20 automated postal centers.[5]

Recommendation

We recommend the Manager, Nevada-Sierra District, direct the Retail Manager to:

1. Review revenue reports to identify underperforming equipment; notify postmasters of vending equipment that generates low revenue; and giving consideration to all feasible alternatives, complete all necessary actions to redeploy underperforming equipment as often as possible.

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[4] Our review of the revenue reports for the first quarter of FY 2004 indicated that three of the six machines did not meet minimum revenue requirements.
[5] Automated postal centers are a newly developed kiosk that provides convenient 24-hour automated access to purchase stamps as well as many premium delivery services such as Express and Priority Mail.

Management's Comments

Management agreed with the finding and recommendation and issued an action plan July 1, 2004, to redeploy vending machines as they become available beginning August 4, 2004. In addition, 18 vending machines will be redeployed beginning November 11, 2004, when the new automated postal centers are deployed. Management will continue to review revenue reports to identify machines not meeting minimum revenue requirements and place them in locations that provide the opportunities to reach minimum revenue goals. Management's comments, in their entirety, are included in the appendix of this report.

Evaluation of Management's Comments

Management's comments are responsive to our recommendation. Management's planned actions should correct the issues identified in the finding.

Use of Obsolete Equipment

In FY 2003, Nevada-Sierra District officials continued to use 34 obsolete machines and possibly incurred maintenance and repair expenses, even though Postal Service policy discontinued the maintenance and repair support for the machines in June 2000.[6] Our review of vending equipment revenue reports indicated that 97 percent (33 of 34) of the machines during FY 2003 and all of the machines during the first quarter of FY 2004 did not meet minimum revenue requirements.

District officials stated they continued to use and maintain the obsolete equipment because of the potential adverse impact on customer service. As a result, during FY 2003 and the first quarter of FY 2004, the district possibly incurred maintenance and repair expenses that may have exceeded the revenue generated by continuing to operate and maintain the obsolete machines. We were unable to determine the amount of repair and maintenance expenses associated with the machines because the Postal Service does not capture the data for each machine. [7]

Periodically, the Postal Service lists vending equipment as obsolete, meaning the equipment has exceeded its expected life cycle and will no longer receive support from maintenance organizations. All inactive retail vending equipment items must be reported to the district material management specialist. When retail vending equipment items are obsolete or listed as excess, the Postal Service may consider them for disposal action. Parts from obsolete machines may be salvaged and stored for maintenance or repair of other compatible equipment. In June 2000, Postal Service

[6] This policy supplements Maintenance Management Order, MMO-018-96, June 21, 1996, Discontinuance of Support for Obsolete Vending Machines. This MMO includes discontinuance of support for recently obsolete models of vending machines announced in the Material Logistics Bulletin (MLB-PP-00-004), issued on May 18, 2000.
[7] We plan to address this issue in a capping report to Postal Service Headquarters officials.

policy listed the obsolete vending equipment that should no longer receive support from maintenance organizations.

By continuing to use and maintain obsolete machines, the district will possibly incur repair and maintenance costs that may exceed the revenue generated. We recognize management's desire to provide customer service; however, because the Postal Service does not capture repair and maintenance, management has no means of assessing whether the benefits of operating the obsolete equipment outweigh the cost to operate it. District officials stated that plans will be made to replace the obsolete machines when the new automated postal center machines are deployed to the district location.

Recommendation

We recommend the Manager, Nevada-Sierra District, direct the Retail Manager to:

2. Consider all feasible alternatives, and complete all necessary actions to eliminate repair and maintenance cost for the obsolete equipment.

Management's Comments

Management agreed with the finding and recommendation and stated that even though the obsolete machines require very little maintenance, they plan to remove the equipment beginning August 4, 2004, as equipment fails. This will be an on-going process until all 34 machines are removed.

Evaluation of Management's Comments

Management's comments are responsive to our recommendation. Management's planned actions should correct the issues identified in the finding.

The OIG considers recommendations 1 and 2 significant, and therefore requires OIG concurrence before closure. Consequently, the OIG requests written confirmation when corrective action(s) are completed. These recommendations should not be closed in the follow-up tracking system until the OIG provides written confirmation that the recommendations can be closed**.**

We appreciate the cooperation and courtesies provided by your staff. If you have any questions or need additional information, please contact Debra D. Pettitt, Director, Delivery and Retail, or me at (703) 248-2300.

/s/ Mary W. Demory

Mary W. Demory
Deputy Assistant Inspector General
for Operations and Human Capital

Attachment

cc: John A. Rapp
Alfred Iniguez
Lani R. Meneses
Charlene B. McComb
Ralph G. Lindsey
Steven R. Phelps

APPENDIX. MANAGEMENT'S COMMENTS

UNITED STATES
POSTAL SERVICE

July 26, 2004

Office of Inspector General

Subject: Response to Review of Self-Service Vending Program Audit for Nevada Sierra District (Report Number DR-AR-04)

The Nevada-Sierra District is in concurrence with your findings and recommendations on the above mentioned document. The Action Plan for self service vending equipment was submitted July 1, 2004.

Redeployment of Vending Equipment (On-going process as equipment becomes available beginning 8/04. Redeploy 18 self service vending machines beginning 11/04 when APC equipment is placed at 18 new locations.)

Nevada-Sierra District has no excess self service vending equipment. Equipment Relocation Analysis (ERA) provides us the tool to relocate equipment that is not meeting the minimum revenue requirements. Most times what is recommended is not able to happen as we do not have the suggested equipment to place at the location that is not meeting minimum requirements.

Retail will continue to review revenue reports to identify equipment not meeting minimum revenue requirements and place it in a location that provides the opportunity to reach the minimum revenue goals.

Use of Obsolete Equipment (Will be removed when equipment fails beginning 8/04.)

The obsolete equipment that is still located in the field requires very little maintenance. If the machine requires maintenance, we are unable to get the parts and the equipment is then removed after it completely breaks down. The only maintenance required is when the equipment is removed and the hole in the wall needs to be replaced. At that time the wall is repaired and equipment is returned to Supply and treated as obsolete equipment. We then follow the procedures to destroy the obsolete equipment.

We will continue the process to remove the 34 machines that are obsolete equipment.

Johnray Egelhoff
District Manager

1001 E. Sunset Rd Rm 1030
Las Vegas, NV 89199-9616
Phone: 702-361-9328
FAX: 702-361-9471