Office of Inspector General

March 31, 2005

PAUL E. VOGEL
VICE PRESIDENT, NETWORK OPERATIONS MANAGEMENT

SUBJECT: Audit Report – Mail Transport Equipment Service Center Network – Equipment Processing (Report Number NL-AR-05-006)

This report presents results from our self-initiated nationwide audit of the mail transport equipment service center (MTESC) network (Project Number 04YG003NL000). The objective of our audit was to follow up on previous audit recommendations to determine if they were implemented and effective.

On June 30, 1997, the Board of Governors approved a Decision Analysis Report (DAR) recommending a $1.3 million capital investment to implement a contractor-operated MTESC network as a replacement for the Postal Service-operated system. Implementation of the network was scheduled to begin in November 1997, be phased in over 17 months, and be completed by April 1999. However, the network did not become fully operational until January 2000.

Our report, Mail Transport Equipment Service Center Decision Analysis Report, Performance and Financial Benefit (Report Number TR-AR-01-003, dated May 4, 2001), initiated in response to a Board of Governors request, concluded the network would not achieve the financial benefits anticipated by the 1997 DAR. We recommended, in part, that management reduce cost by requiring facilities to reuse serviceable equipment rather than returning it to service centers for processing.

This report focused on whether the Postal Service saved money by requiring facilities to reuse serviceable equipment. We concluded that the Postal Service saved more than $7.2 million in processing costs from March 2002 through September 2004, because headquarters took aggressive and positive action to implement our recommendation, particularly with regard to reusing "over-the-road" containers (OTRs).

However, we also concluded the Postal Service may have missed an opportunity to save an additional $1.4 million because all mail processing facilities did not quickly comply with headquarters' implementing instructions. Notwithstanding the potential missed opportunity, the Postal Service can still save $628,000 over the next two years if all facilities implement headquarters' policy.

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We recommended management reemphasize Postal Service OTR processing policy to all mail processing facilities. Management agreed with our recommendation. They stated the Postal Service executive vice president/chief operating officer had already issued a memorandum to each area vice president reemphasizing the OTR processing policy; that current OTR policy was to be reissued in an upcoming Postal Bulletin; and that Network Operations Management would monitor the receipt of OTRs at mail transport equipment service centers during site reviews. Management's comments in their entirety, including a copy of the executive vice president/chief operating officer's memorandum to the area vice presidents, are included in Appendix D of this report. We will report $7,828,000 in funds put to better use and $1.4 million in unrecoverable costs in our Semiannual Report to Congress.

Management's comments are responsive to our recommendation. We applaud management's rapid reaction to our recommendation and we consider the actions taken sufficient to address the issues we identified. Management's comments and our evaluation of these comments are included in this report.

The Office of Inspector General considers recommendation 1 significant and closed because management's timely corrective actions resolved the identified issues. Consequently, the Postal Service can close the recommendation in their follow-up tracking system.

We appreciate the cooperation and courtesies provided by your staff during the review. If you have any questions or need additional information, please contact Joe Oliva, Director, Transportation, or me at (703) 248-2300.

/s/ Mary W. Demory

Mary W. Demory
Deputy Assistant Inspector General
  for Core Operations

Attachments

cc: Keith Strange
Anthony M. Pajunas
Beverly A. Van Soest
Steven R. Phelps

INTRODUCTION

Background

The Mail Transport Equipment Service Center (MTESC) network is a centrally managed system of 22 contractor-operated service centers designed to supply Postal Service mail processing facilities–and certain large customers–with mailbags, trays, sleeves, pallets, hampers, carts, and "over-the-road" containers (OTRs). The service centers

"Over-the-Road" containers, commonly referred to as OTRs, are large metal rolling containers used in trucks to transport mail.

This picture depicts serviceable OTRs at the Front Royal, Virginia, Mail Transport Equipment Service Center, June 8, 2004.

deliver equipment to users with dedicated transportation, recover it when equipment is no longer needed or serviceable, and then process it for inventory or redelivery. Processing involves receiving, sorting, and inspecting equipment for repair or disposal.

The network was initiated in 1992 as a pilot program, with a prototype center in Greensboro, North Carolina. In 1997, Postal Service management prepared a Decision Analysis Report (DAR) recommending a $1.3 million capital investment to implement the contractor-operated system as a replacement for the Postal Service-operated system in place at the time.

On June 30, 1997, the Board of Governors accepted the recommendation and approved the DAR. Implementation of the network was scheduled to begin in November 1997, be phased in over 17 months, and be completed by April 1999. However, the network did not become fully operational until January 2000. From the outset, the new network was troubled by allegations of poor performance and excessive cost. As a result, the Board of Governors asked the Office of Inspector General (OIG) to evaluate the program.

Our audit report, Mail Transport Equipment Service Center Decision Analysis Report, Performance and Financial Benefit (Report Number TR-AR-01-003, dated May 4, 2001), concluded the network would not achieve the financial benefits anticipated by the DAR. We recommended, in part, that management reduce cost by requiring facilities to reuse serviceable equipment rather than returning it to service centers for processing.

Objective, Scope, and Methodology

This audit is a follow up to our May 4, 2001, report. Our objective was to determine if the Postal Service implemented our recommendations and whether implementation was effective. This report focuses on whether the Postal Service saved money by requiring facilities to reuse serviceable equipment rather than returning it to service centers.

During our work, we interviewed Postal Service Headquarters officials in Network Operations Management and Supply Management, and officials in the Southeast, Southwest, and Pacific Areas. We observed and photographed operations and examined applicable Postal Service policies, procedures, and directives. In addition, we analyzed billing records for mail transport equipment processing at all 22 service centers and examined correspondence and other relevant records. We consulted with statisticians and other subject-matter experts. We also discussed our observations and conclusions with management officials and included their comments where appropriate.

We conducted this audit from November 2003 through March 2005,[1] in accordance with generally accepted government auditing standards and included tests of internal controls considered necessary under the circumstances.

Data and Internal Control Limitation	During our audit, we noted several control weaknesses that delayed and constrained our work. For example, automated billing records were not available and, consequently, we could not use computer-assisted analysis techniques. In addition, complete data for the Chicago MTESC was not available. However, we compensated for data limitations and internal control weaknesses by applying alternate audit procedures, including examination of source documents, observation, and discussions with responsible officials. For a detailed explanation of our methodology, see Appendix A.

[1] Project completion was delayed to address Postal Service MTESC realignment initiatives and to obtain additional billing data.

AUDIT RESULTS

Reusing Serviceable Mail Transport Equipment

The Postal Service saved more than $7.2 million in processing costs from March 2002 through September 2004 because headquarters officials took aggressive and positive action to implement our recommendation, particularly with regard to reusing OTRs. However, the Postal Service may have missed an opportunity to save an additional $1.4 million because all mail processing facilities did not quickly comply with headquarters' policy guidance.

This poster reflects Postal Service policy guidance issued March 1, 2002.

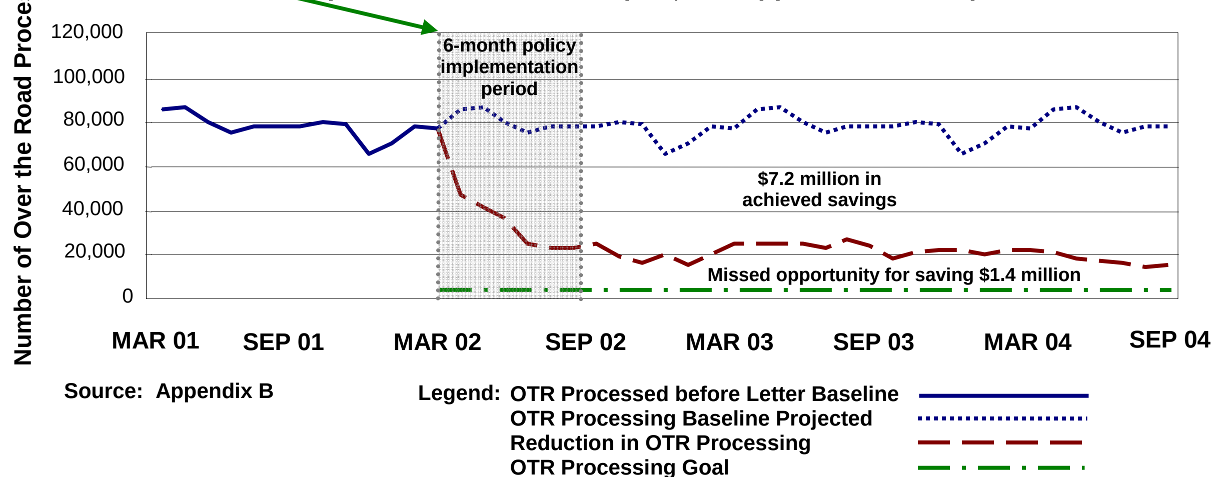
Serviceable over the road containers are to be retained at bulk mail centers and only sent to MTESC when they require repair.

By implementing this policy, the Postal Service saved more than $7.2 million from March 2002 through September 2004.

Notwithstanding the potential missed opportunity, the Postal Service can save an additional $628,000 over the next two years if all facilities follow headquarters' instructions. For a detailed analysis, see Appendix B.

Postal Service officials encouraged the reuse of all types of mail transport equipment and on March 1, 2002, the chief operating officer issued a policy letter specifying that OTRs were for the exclusive use of bulk mail centers and prohibiting facilities from shipping serviceable containers to MTESCs. (See Appendix C.) The letter stipulated that only containers requiring repair could be shipped to the service centers.

Chart 1.
Methodology Illustration of Over the Road (OTR) Container Processing
(For more detailed analysis, see Appendix A and B)

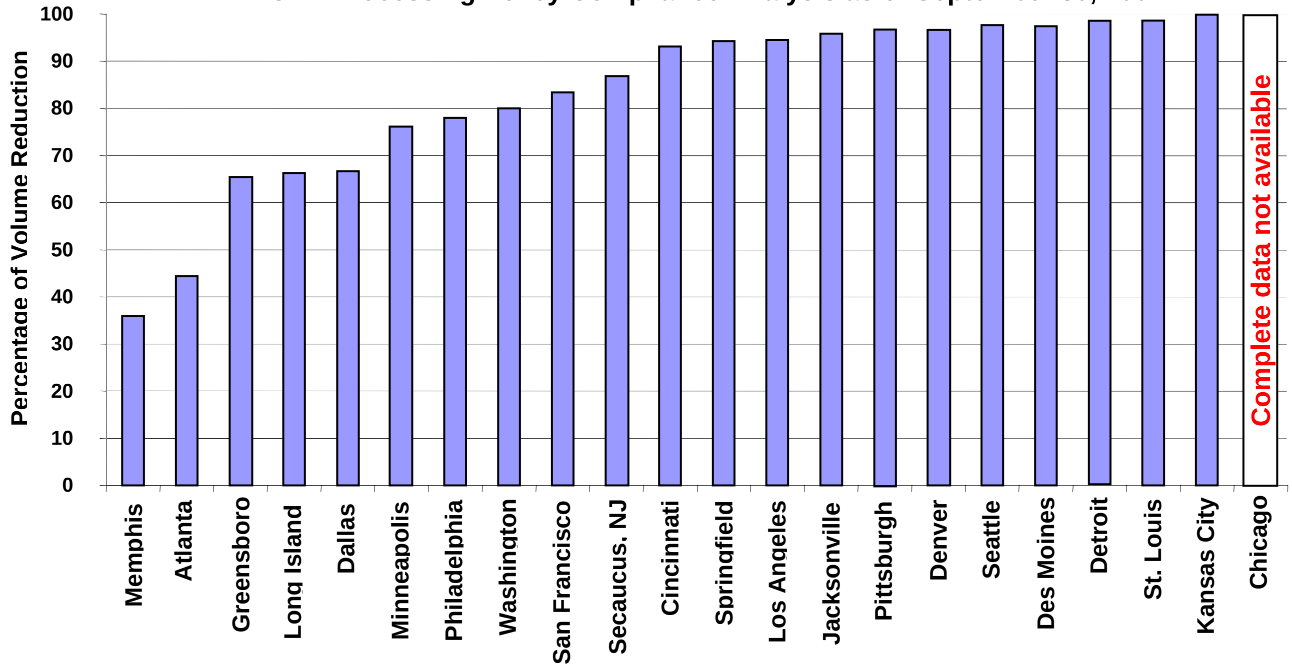


Source: Appendix B

Although Postal Service Headquarters took aggressive and positive action to pursue this savings opportunity, not all mail processing facilities immediately complied with the policy. Our examination of Postal Service records indicated that mail processing facilities serviced by the various MTESCs had varying levels of compliance, ranging from as low as 36 percent for facilities serviced by Memphis, to as high as 100 percent for facilities serviced by Kansas City. The chart on the following page reflects the compliance of facilities serviced by 21 MTESCs. As indicated in the Objective, Scope, and Methodology section of our report, complete data for the Chicago MTESC was not available. Consequently, Chicago was not included in our analysis.

Our analysis indicated that mail processing facilities serviced by the St. Louis MTESC very quickly achieved a 95 percent policy compliance rate. If all facilities could replicate the St. Louis results and achieve 95 percent compliance, the Postal Service could save more than $628,000 over the next two years. (See Appendix A.)

Chart 2.
OTR Processing Policy Compliance Analysis as of September 30, 2004



Source: Appendix B, Column "% Reduction in OTR Equipment Processed as of September 30, 2004."

Postal Service area employees told us that labor issues were a prohibiting factor to fully implementing the OTR container processing policy. However, we did not identify any labor issues or conditions that differentiated locations with high levels of policy implementation from locations with low implementation levels. Consequently, we do not consider labor concerns to be a prohibiting factor.

Recommendation

We recommend the vice president, Network Operations Management:

1. Reemphasize Postal Service OTR processing policy to all mail processing facilities.

Management's Comments

Management agreed with our recommendation. They stated the Postal Service executive vice president/chief operating officer had already issued a memorandum to each area vice president reemphasizing the OTR processing policy; that current OTR policy was to be reissued in an upcoming Postal Bulletin; and that Network Operations Management would monitor the receipt of OTRs at mail transport equipment service centers during site reviews. Management's comments in their entirety, including a copy of the executive vice president/chief operating officer's memorandum to the area vice presidents, are included in Appendix D of this report.

Evaluation of Management's Comments

Management's comments are responsive to our recommendation. We applaud management's rapid reaction to our recommendation, we consider the actions taken sufficient to address the issues we identified, and we consider our recommendation closed.

APPENDIX A

METHODOLOGY AND TECHNICAL DOCUMENTATION MTESC NETWORK – EQUIPMENT PROCESSING

Purpose

The Postal Service implemented the OIG's recommendation to stop unnecessary, routine processing of OTRs containers, issuing a letter to OTR user sites on March 1, 2002. At many MTESCs, the influence of this letter was immediate, with significant drops in the processing of OTRs. At other MTESCs, less dramatic reductions occurred, but the number of OTRs processed has generally decreased since the issuance of the letter. The methodology described here summarizes the monetary impact calculation accrued over a 30-month period (May 2002 – September 2004) as a result of implementation of the OIG recommendation.

Baseline

The number of OTRs processed in the year (March 2001 – February 2002) immediately preceding the letter served as the baseline for OTR processing levels. Data received prior to March 2001 appeared, for many sites, to be still in a "ramp-up" condition or to be missing for several accounting periods (APs). For the Chicago MTESC, the prior data was virtually nonexistent, so Chicago is excluded from the cost avoidance calculations. [MTESC processing at Chicago should be reviewed separately to see if the facilities served by the MTESC are adhering to the letter.]

We repeated the prior-year processing levels over the time following the letter. A few sites actually appeared to have prior processing levels that might have been gradually trending upward, but we decided we had insufficient basis to continue an increase over the next few years. We assumed all sites would continue processing OTRs at about the same levels as the prior year.

The baseline addressed only the number of OTRs processed by MTESC. For the processing unit cost in the post-letter period we used the rate applicable to each period and MTESC.

Actual Processing

We compared the processing levels for the post-letter APs to the baseline extension of the pre-letter APs. The reduction from the baseline is the processing avoided as a result of the recommendation. For the cost avoidance calculation, we applied the processing cost per OTR applicable to a given time period. The implicit assumption is that a corresponding cost would have applied to the number of OTRs processed at the baseline level.

We had originally planned to use an AP-by-AP comparison in case there were seasonal variations in the number of OTRs processed. This became impossible, however, when fiscal year (FY) 2002 had the original 13 APs (September 8, 2001 – September 6, 2002), FY 2003 had 14 (September 7, 2002 – September 30, 2003), and FY 2004 had 12 (October 1, 2003 – September 30, 2004). We ultimately were forced to use annual averages. We calculated the average annual processing cost-per-OTR by dividing the annual total processing cost by the annual total number of OTRs processed.

Processing Target

We noted the facilities using the St. Louis MTESC took immediate action to implement the policy stated in the letter. The St. Louis MTESC very quickly showed a 95 percent reduction in the number of OTRs processed. We adopted the 95 percent reduction level as an achievable target, based on St. Louis's example. We did not push for a 100 percent reduction because we considered that there might still be some legitimate need for some OTR processing.

Unnecessary Cost

Some facilities delayed implementation of the OTR processing guidance, thereby incurring processing expenses they would not have incurred with the guidance. In calculating the number of OTRs processed in excess, we allowed a nominal six-month grace period (March 2002 – September 2002). After that grace period, we consider OTRs processed above the target level to be an unnecessary cost.

Forecast

The cost avoidance forecast is that savings that will accrue in the upcoming two-year period we assumed in Chart 2 (see page 6). We used the number of pieces actually processed in the final AP of FY 2004 as the basis for the forecast. We did not attempt to make tailored forecasts for each site. We noted that some sites were still reflecting some gradual reductions in OTR processing over the last year, some were actually creeping back up, and some were going up and down slightly over the last year. The forecast calculation is a simple flat-line extension–for all sites–of the level for the final AP of FY 2004 (September 1, 2004 – September 30, 2004).

Monetary Impact Illustration

Processing avoidance over a 30-month period is illustrated in the body of the report; the number of OTRs are not for any specific site. The baseline for OTR processing levels is a repetition of the pre-letter year. The number of OTRs processed above the target level after the six-month grace period allowed for implementing the new guidance is what is being questioned. The actual number processed in the illustration shows a moderate initial decline and a gradual leveling off of OTRs processed.

APPENDIX B

SAVINGS SUMMARY ANALYSIS

Facility Site	Achieved Savings Cumulative March 23, 2002 - September 30, 2004[2]	% Reduction in OTR Equipment Processed as of September 30, 2004	Future (2-yr) Cost Avoidance Using September 30, 2004, Processing Cost[3]	Questioned Costs: Costs for Processing More Than Target After March 2002 - September 2002 "Grace Period"	Total Monetary Impact
Atlanta	$ 69,749.26	0.44	$ 106,633.29	$ 228,899.77	$ 405,282.32
Chicago	insufficient data in base year				
Cincinnati	$ 461,988.99	0.92	$ 6,747.78	$ 17,495.44	$ 486,232.20
Dallas	$ 114,229.43	0.68	$ 23,989.89	$ 33,007.26	$ 171,226.58
Denver	$ 422,008.98	0.97	$ -	$ 334.06	$ 422,343.04
Des Moines	$ 173,427.37	0.98	$ -	$ -	$ 173,427.37
Detroit	$ 543,894.99	0.99	$ -	$ 15,478.24	$ 559,373.23
Greensboro	$ 1,103,376.35	0.66	$ 108,566.34	$ 115,175.19	$ 1,327,117.88
Jacksonville	$ 109,839.45	0.96	$ -	$ 30,131.82	$ 139,971.26
Kansas City	$ 185,797.48	1.00	$ -	$ -	$ 185,797.48
Long Island	$ 181,616.93	0.67	$ 86,074.86	$ 133,876.82	$ 401,568.61
Los Angeles	$ 457,391.38	0.94	$ -	$ 12,126.65	$ 469,518.03
Memphis	$ 169,410.46	0.36	$ 93,866.32	$ 56,829.89	$ 320,106.67
Minneapolis	$ 186,496.91	0.77	$ 28,477.35	$ 57,404.36	$ 272,378.62
Philadelphia	$ 652,192.85	0.79	$ 46,352.04	$ 99,038.46	$ 797,583.34
Pittsburgh	$ 286,354.08	0.97	$ -	$ 23,612.35	$ 309,966.43
San Francisco	$ 426,260.03	0.83	$ 60,083.61	$ 65,752.97	$ 552,096.60
Seattle	$ 383,976.20	0.98	$ -	$ 8,975.55	$ 392,951.76
Secaucus	$ 461,633.42	0.87	$ 18,992.61	$ 121,459.12	$ 602,085.15
Springfield	$ 211,496.87	0.93	$ 5,066.51	$ 23,884.29	$ 240,447.67
St. Louis	$ 503,750.27	0.99	$ -	$ -	$ 503,750.27
Washington	$ 112,221.46	0.80	$ 43,079.66	$ 325,050.30	$ 480,351.42
TOTAL	**$ 7,217,113.15**	**0.71**	**$ 627,930.26**	**$ 1,368,532.53**	**$ 9,213,575.94**

Source: Analysis of Postal Service MTESC billing invoices from March 2001 through September 2004.

[2] Funds Put to Better Use.
[3] Funds Put to Better Use.

APPENDIX C

POLICY LETTER FOR OVER–THE-ROAD CONTAINER PROCESSING

PATRICK R. DONAHOE
CHIEF OPERATING OFFICER
AND EXECUTIVE VICE PRESIDENT

UNITED STATES
POSTAL SERVICE

March 1, 2002

VICE PRESIDENTS, AREA OPERATIONS
MANAGER, CAPITAL METRO OPERATIONS

SUBJECT: Bulk Mail Center (BMC) Over-The-Road Container (OTR) Management

Control of bulk mail center (BMC) over-the-road containers (OTR) is being transferred from the mail transport equipment service center (MTESC) network to the BMC network. These containers will either be in continuous use during the normal part of the year or they will be stored when necessary. This will eliminate the redistribution of BMC OTRs by the MTESC network. The MTESC network will retain the responsibility for repair of OTRs. All processing operations must be vigilant about red-tagging damaged and unsafe containers (in accordance with Postal Operations Manual paragraph 583.11).

With more than 216,000 OTRs in service, there is a sufficient supply of containers for each BMC to manage its local operations. Over-the-road containers are for the exclusive use between the BMCs and the processing and distribution centers/facilities (P&DC/F) within the BMC service area. An exception to this rule is the newer P&DC/F sites, which have BMC/OTR processing equipment. Inter-BMC or inter-area dispatches are not authorized, unless adequate and workable "closed loops" have been established. Where imbalances exist, the BMC network will be responsible for relocating OTRs from surplus areas to deficit ones using existing transportation. Transporting mail in OTRs instead of Postal Paks to deficit BMCs will also help to relocate surplus units. Reciprocal agreements also exist between BMCs to exchange non-machineable outsides either in OTRs or cardboard boxes. The MTESC network can provide order information and data to BMC managers concerning "leakage" of OTRs to other operations. Over-the-road containers should not be used for merchandise return operations.

The MTESC network sorts used cardboard boxes in two sizes, small and large. All processing operations should attempt to take advantage of this resource. The MTE organization encourages the return of raw MTE to the MTESC network using these boxes. Using a combination of unprocessed MTE types can maximize truck density.

The MTESC network has previously supplied OTRs nationwide, but the costs (over $9 million for standing transportation and more than $4 million for processing BMC containers) have become prohibitive. Every effort must be made to keep OTRs circulating for the benefit of the entire mail processing and distribution network. The distribution network office must make the appropriate MTESC standing order and highway contract changes. This transfer will be effective March 18.

If you should have further questions, please contact Regina Wesson at (202) 268-4376.

Patrick R. Donahoe

cc: Managers, Operations Support (Area)
Managers, Bulk Mail Centers

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APPENDIX D. MANAGEMENT'S COMMENTS

PAUL VOGEL
VICE PRESIDENT, NETWORK OPERATIONS MANAGEMENT

UNITED STATES
POSTAL SERVICE

March 30, 2005

MARY W. DEMORY

SUBJECT: Draft Audit Report – Mail Transport Equipment Service Center Network – Equipment Processing (Report Number NL-AR-05-DRAFT)

Please find our response to the subject audit which assessed the effectiveness of controls on Over– the– Road (OTR) containers.

Recommendation 1:

We recommend the Vice President, Network Operations Management:

1. Reemphasize Postal Service OTR processing policy to all mail processing facilities.

Response:

We agree with the recommendation and have taken the following actions to reinforce the OTR processing policy:

1. Patrick Donahoe, Executive Vice-President/Chief Operating Officer, issued a memo to each Area Vice President reemphasizing the OTR processing policy. Additionally, the memo provided a synopsis of your most recent audit. See Attachment #1.
2. Current OTR policy information will be reissued in an upcoming Postal Bulletin and posted at USPS facilities. See Attachment #2.
3. We will monitor the receipt of OTRs at the MTESCs through on-site reviews that are being conducted throughout the year.

We appreciate your sharing the findings and providing us an opportunity to address these issues.

For
Paul Vogel

cc: Mr. Strange
Mr. Pajunas
Ms. Van Soest
Mr. Phelps

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Attachment #1

PATRICK R. DONAHOE
CHIEF OPERATING OFFICER
AND EXECUTIVE VICE PRESIDENT

UNITED STATES
POSTAL SERVICE

March 23, 2005

VICE PRESIDENTS, AREA OPERATIONS
MANAGER, CAPITAL METRO OPERATIONS

SUBJCT: Compliance of Bulk Mail Center, Over-The-Road Container Management

The Office of Inspector General recently completed an audit of OTR container usage throughout the Mail Transport Equipment Service Center (MTESC) network. The audit was undertaken to measure compliance to the policy letter issued on March 1, 2002. The policy states that the OTR was designed to be used exclusively within the bulk mail center network and only OTRs requiring repair (those red tagged) should be shipped to the MTESC. The audit completed in February 2005, shows the MTESC network and the percent reduction in OTRs process as of September 2004 (see attached data).

Overall, the data depicts a positive trend in compliance; however, there is still room for improvement and a savings within your areas. Please review the data and ensure postal plants within your area are in compliance with the national policy for OTR usage.

Patrick R. Donahoe

Attachment

cc: Paul Vogel
Tony Pajunas
Walter OTormey
Jaime Fuentes

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SAVINGS SUMMARY ANALYSIS

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TOTAL	**$ 7,217,113.15**	**0.71**	**$ 627,930.26**	**$ 1,368,532.53**	**$ 9,213,575.93**

Source: Analysis of Postal Service MTESC billing invoices from March 2001 through September 2004.

Attachment #2

DO NOT send Over the Road (OTR) containers to the Mail Transport Equipment Service Center (MTESC) unless the containers are **defective** and require **repair.**

All defective containers going to the MTESC must have a container **REPAIR TAG** applied before sending it to the MTESC.