



July 20, 2006

PAUL E. VOGEL  
VICE PRESIDENT, NETWORK OPERATIONS MANAGEMENT

SUBJECT: Audit Report – Mail Transport Equipment Service Center Network –  
Proposed Change to Quality Inspection and Payment Authorization Controls  
(Report Number NL-AR-06-007)

The mail transport equipment service center (MTESC) network is a system of 22 contractor-operated service centers designed to supply mail transport equipment to mail processing facilities nationwide. This report is one in a series of reports that presents results from our self-initiated nationwide MTESC audit (Project Number 06XG008NL001). Our audit objective is to follow-up on previous recommendations and identify opportunities to increase efficiency and save money.

Each MTESC is staffed by an “operating contractor” who runs the facility and an independent “quality contractor” who inspects the operating contractor’s work to ensure work is done properly, equipment meets standards, and payment is appropriate. Each MTESC has many operating processes examined by quality contractor personnel. One such process is the procedure for inspecting and approving palletized products, which include such items as mailbags and mail trays.

Operating contractors believe the current pallet inspection and payment authorization process slows down operations by creating an inspection “bottleneck.” As a result, the U.S. Postal Service is considering a change to the existing process. They are testing the proposed quality assurance change at the Minneapolis, Minnesota, MTESC. During the course of our ongoing MTESC audit, Postal Service officials asked us to examine the proposed change. This report responds to that specific request.

We concluded that the proposed change does not provide the independent quality control needed to assure that the operating contractor’s work is done properly, that equipment meets standards, or that payment should be approved. Although the proposed change document explains it will not modify the inspection criteria currently in place and quality contractors will continue to authorize payment for every pallet produced, it does not sufficiently explain how inspectors will effectively accomplish those important control functions. Further, the change stipulates the manual inspection entries quality clerks currently make will no longer be required. Instead, the computer system will default to automated inspection assumptions such as “serviceable,” “standard pallet quantity,” or “approve.”

We are concerned that the proposed change could significantly erode some of the robust internal controls Postal Service management previously established, possibly resulting in overstated or unsupported invoices or work invoiced as properly completed when not properly performed. We recommended that management postpone the proposed change until they address internal control concerns.

Management agreed with our recommendations. Management stated that they placed the proposed change on hold, and said they would advise us of any additional system modifications. Management's comments and our evaluation of these comments are included in the report.

The U.S. Postal Service Office of Inspector General (OIG) considers all the recommendations significant, and therefore requires OIG concurrence before closure. Consequently, the OIG requests written confirmation when corrective actions are completed. These recommendations should not be closed in the follow-up tracking system until the OIG provides written confirmation the recommendations can be closed.

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

E-Signed by Colleen McAntee   
VERIFY authenticity with Approve!  


Colleen A. McAntee  
Deputy Assistant Inspector General  
for Core Operations

#### Attachments

cc: William P. Galligan  
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## INTRODUCTION

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### Background

The mail transport equipment service center (MTESC) network is a system of 22 contractor-operated service centers designed to supply mail transport equipment to mail processing facilities nationwide.

The Minneapolis, Minnesota, MTESC, February 2006.

The Minneapolis MTESC is one of 22 contractor-operated facilities nationwide.



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### Prior Audit Coverage

Our audit report, *Adequacy of Mail Transport Equipment Center Network Internal Controls* (Report Number TR-AR-01-001, dated October 31, 2000), concluded that controls over contractor work were insufficient. The report identified the following control weaknesses:

- Palletized products such as mailbags, trays, sleeves, and lids were reported as processed when they had not been processed.
- Inspection placards on processed products were erroneously replaced and the errors may have caused additional charges.
- During a 10-day period at one service center the weight of processed mailbags may have been overstated by about 20 percent; the weight of processed trays, sleeves, and lids overstated by more than 30 percent; and the 10-day processing

discrepancies may have resulted in overcharges of about \$13,000.

Our audit concluded that many issues identified were due to insufficient separation of duties and quality assurance, and that the independent quality assurance function was not sufficiently staffed. Our audit also concluded the U.S. Postal Service could reduce the risk of paying for work that was not performed by verifying contractor work. We recommended, in part, that the Postal Service fully staff the independent quality assurance function. Postal Service Headquarters agreed with our recommendation.

**Under current policy, quality assurance clerks are stationed at inspection stations throughout MTESCs, where they inspect the quality of “operating contractor” work and authorize payment for work properly performed.**

**Minneapolis, Minnesota,  
MTESC,  
February 23, 2006.**



As a result, in addition to the “operating contractor” who actually runs the service center, each MTESC is now fully

staffed by a “quality contractor” who provides at least one quality process auditor, plus quality clerks at inspection stations throughout the facility.

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Current Procedure

The quality contractor is independent of the operating contractor. The job of quality contract personnel is to provide assurance that the operating contractors properly do their work, that equipment meets standards, and that payment is appropriate. Quality auditors conduct random quality audits and supervise the quality clerks. The quality clerks inspect all completed operating contractor work and then authorize payment.

Each MTESSC has many operating processes quality auditors and clerks examine. One such quality process is the procedure for inspecting palletized products.

**“Palletized products”  
include mailbags, trays,  
sleeves, and lids.**

**This picture shows letter  
trays shrink-wrapped  
and stacked on a pallet  
at the Dallas MTESSC,  
April 11, 2006.**

**Independent MTESSC  
quality assurance clerks  
are required to inspect  
every pallet to verify that  
piece counts are  
accurate, that equipment  
is serviceable, and that  
pallets are properly  
stacked and packaged.**



The *U.S. Postal Service Mail Transport Equipment Service Center Quality Department Manual*, dated June 30, 2004, currently requires quality clerks to inspect all completed pallets. Specifically, quality clerks must verify that:

- Every pallet has the right number of mailbags, trays, sleeves, or lids.

- The equipment is serviceable.
- Pallets are properly stacked and packaged.

After quality clerks inspect and verify pallet quality, they approve the work and authorize payment by making appropriate entries into the computerized Mail Transport Equipment Support System (MTESS). The quality clerk uses the system to print an inspection placard and authorizes the pallet for payment. The operating contractor then shrink-wraps the pallet, affixes the placard, and stages it for transport.

After quality clerks inspect pallets and authorize payment for work completed, they use the MTESS to print an inspection placard and attach the placard to the shrink-wrapped pallet.

Dallas MTESS,  
April 11, 2006.



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#### Proposed Change

Operating contractors believe the quality assurance inspection process slows down MTESS operations by creating an inspection “bottleneck.” As a result, the Postal Service is considering a proposed change to existing pallet inspection and payment authorization controls and they are testing the proposal at the Minneapolis, Minnesota, MTESS. The change is intended to reduce operational delays, slowdowns, or “bottlenecks” at the quality inspection station. The proposed change document explains:

- The manual inspection entries quality clerks currently make will no longer be required before inspection placards are produced.

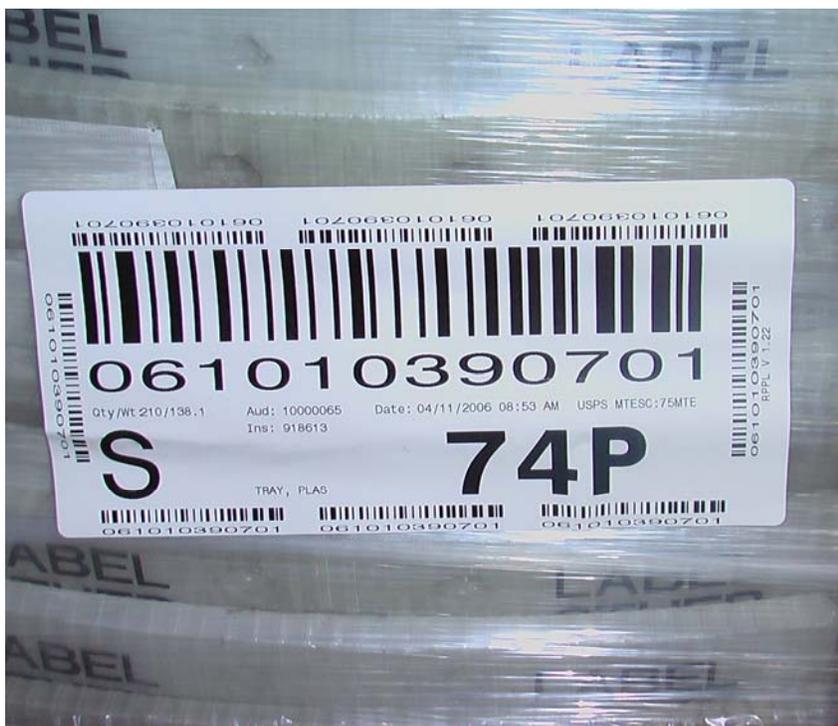
- Instead, the system will default to automated inspection assumptions such as “serviceable,” “standard pallet quantity,” or “approve.”
- Based on the default inspection assumptions, operating contractor employees will use the computer to automatically generate an inspection placard.

The proposed change document asserts that eliminating manual handwritten entries such as inspector identification numbers, pallet quantity, and pallet approval status before inspection placards are produced will improve accuracy and operating contractor efficiency.

Inspection placards contain such information as the type of equipment (plastic trays in this case), the quantity, and weight of the items on the pallet, and the employee identification number of the person who prepared the pallet.

Under current policy, inspection placards are generated only after quality clerks inspect the pallet.

Under the proposed change, quality clerks will not see the pallet until after the inspection pallet has already been generated and the pallet shrink-wrapped.



Postal Service Headquarters is aggressively pursuing opportunities to improve efficiency and reduce MTEC network costs. Accordingly, during the course of our ongoing MTEC audit, officials asked us to examine the proposed change.

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**Objective, Scope, and  
Methodology**

This report responds to that specific request and is one in a series of reports from our MTESSC audit. Our audit objective is to follow-up on previous recommendations and identify opportunities to increase efficiency and save money. We are providing this report to advise management of our opinion regarding the proposed change to quality inspection and payment authorization controls.

We performed our work in close coordination with the Network Operations Management MTESSC assessment team. During our work, we interviewed Postal Service Headquarters officials in Network Operations Management and Supply Management. We examined applicable Postal Service policies, procedures, and directives, including the *Mail Transport Equipment Service Center USPS Quality Department Manual*, dated June 30, 2004, and the draft change to the Postal Service *MTESS Standard Operating Procedure (SOP)*, dated January 19, 2006. We visited the Minneapolis, Minnesota, MTESSC; observed testing of the proposed change; interviewed operating contractor employees; interviewed quality assurance employees; and photographed operations. We consulted with subject-matter experts, discussed our observations and conclusions with management officials, and included their comments where appropriate. We did not audit or comprehensively validate MTESS data; however, we noted several control weaknesses, which we will discuss in the Audit Results section of this report.

We conducted work associated with this report from February through July 2006 in accordance with generally accepted government auditing standards and included such tests of internal controls as we considered necessary under the circumstances.

## AUDIT RESULTS

### Proposed Quality Assurance Change to the Standard Operating Procedure

The proposed change removes the quality clerk from the inspection station and stipulates the manual inspection entries quality clerks currently make will no longer be required. Instead, the computer system will default to automated inspection assumptions such as “serviceable,” “standard pallet quantity,” or “approve.”

Consequently, the proposed change does not provide the independent quality control needed to assure the operating contractors have properly done their work; each pallet has the right number of mailbags, trays, sleeves, or lids; equipment is serviceable; or payment should be approved.

Letter trays,  
shrink-wrapped and  
stacked on a pallet  
shipped by truck from  
the St. Louis, Missouri,  
MTEC  
August 3, 2005.



Although the proposed change document states that it will not modify the inspection criteria currently in place and that quality contractors will continue to authorize payment for every pallet produced, the change document stipulates only that the quality clerks will affix the placard to the pallet after the pallet is shrink-wrapped and banded. It does not sufficiently explain where inspectors will be located or how they will effectively perform their inspection and payment

approval functions. For example, the proposed change document acknowledges the 22 MTESCs in the nationwide network have different layouts, product flows, and equipment setups and that, as a result, the physical location where quality clerks will accept work and authorize payment may differ.

We have other concerns with the proposed pallet inspection and payment authorization change. For example, the current procedure requires quality clerks to inspect, approve, and authorize payment for **every** pallet produced. The proposed change would cause the computer system to default to “approve,” based on the assumption that a quality auditor performed an “in-process” audit prior to the pallet reaching final inspection. However, the approval default is misleading because, unlike quality clerks who are obligated to inspect, approve, and authorize payment for **all** finished pallets, quality auditors are only required to inspect randomly selected samples. Specifically, current policy requires that quality auditors complete 25 “in-progress” audits and 20 “finished goods” audits per shift. The Minneapolis MTESC operates one shift per day. Our analysis of their single-shift operation determined the facility produces an average of 560 pallets per day.

**Minneapolis MTESC Daily Pallet Inspection**

<b>Total Average Daily Pallet Production</b>	<b>560</b>	<b>100%</b>
<b>Required Daily Quality Auditor Inspections</b>	<b>- 45</b>	<b>- 8%</b>
<b>Total Pallets Not Inspected</b>	<b>515</b>	<b>92%</b>

Since 92 percent of daily pallet production is not inspected by independent quality assurance personnel before the pallets are entered into the computer system as “approve,” we believe there is a significant risk the proposed change will allow work to be approved when pallets have not been properly completed.

In response to the report we discussed earlier (*Adequacy of Mail Transport Equipment Center Network Internal Controls*, dated October 31, 2000), management established robust internal controls. We believe the independent quality inspection function needs to remain robust and the proposed change could significantly erode some of the

important controls management established, particularly with regard to the separation of duties between quality contractor personnel and operating contractor personnel. We also believe the system generated defaults such as “serviceable,” “standard pallet quantity,” or “approve” could result in overstated or unsupported invoices and some work invoiced as properly completed when it was not properly performed.

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Cooperative Joint Management – Audit Team Inspection	On May 10, 2006, we met the Postal Service Headquarters Network Operations Mail Transport Equipment manager and toured the Minneapolis, Minnesota, MTESS test facility to call attention to our concerns. As a result of our cooperative inspection, management recognized the problem with separating quality inspectors from the inspection station and agreed with our recommendations.
<b>Recommendation</b>	We recommend the vice president, Network Operations Management:  1. Postpone full implementation of the proposed change to the Mail Transport Equipment Support System pallet inspection and payment authorization procedure until management addresses separation of duty and other internal control concerns.
<b>Management’s Comments</b>	Management agreed with our finding and recommendation. In their formal response to our draft audit report, management stated that they had already placed network-wide implementation on hold, and said they would advise us of any additional system modifications. Management’s comments, in their entirety, are included in the appendix.
<b>Recommendation</b>	2. Require manual input of actual pallet quality or inspection approval in the automated Mail Transport Equipment Support System instead of defaults such as “serviceable,” “standard pallet quantity,” or “approve.”
<b>Management’s Comments</b>	Management agreed with our finding and recommendation. In their formal response to our draft audit report, management stated they would modify the system to enter the true condition, such as serviceable, defective, or

condemned, rather than allowing the system to default to an automated assumed condition. Management also said they would enter the number of units per pallets rather than allowing the system to default to pallet preset quantities. According to the MTESS support team, these changes will be completed by August 2006.

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**Evaluation of  
Management's  
Comments**

Management's comments are responsive to recommendations 1 and 2. Management's actions, taken or planned, should correct the issues identified in the findings.

## APPENDIX. MANAGEMENT'S COMMENTS

PAUL E. VOGEL  
VICE PRESIDENT, NETWORK OPERATIONS MANAGEMENT



July 3, 2006

KIM H. STROUD

SUBJECT: Transmittal of Draft Audit Report – Mail Transport Service Center  
Network – Proposed Change to Quality Inspection and Payment Authorization  
Controls (Report Number NL-AR-06-DRAFT)

Attached you will find responses to the subject draft audit report and your recent evaluation of the proposed change to the Mail Transport Equipment Service Center (MTEESC) our Mail Transport Equipment Support System (MTESS) and the Minneapolis MTEESC pilot test. We concur with your findings and recommendations in the report.

As discussed with your audit team, the MTEESC Program Office will continue to work with the OIG to assure that additional modifications to the pilot program will be reviewed with your organization to assure that we meet the necessary requirements for the quality inspection and payment authorization controls.

Thank you for working so closely with our team to effectively identify potential issues associated with our proposed initiative to reduce network costs.

A handwritten signature in black ink, appearing to read "Paul E. Vogel".

Paul E. Vogel

Attachment

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**Recommendation 1:** Postpone full implementation of the proposed change to the Mail Transport Equipment Support System pallet inspection and payment authorization procedure until management addresses separation of duty and other internal control concerns.

We are in agreement with this recommendation and have placed network wide implementation of these changes on hold pending full review of the MTESS transactional points relative to the current Statement of Work requirements for both the MTESS operating and quality contractors. Since additional system modifications are in the design stage, the MTESS Program Office will provide details to the audit team at the conclusion of design and prior to pilot testing.

**Recommendation 2:** Require manual input of actual pallet quality or inspection approval in the automated Mail Transport Equipment Support System instead of defaults such as "serviceable," "standard pallet quantity," or "approve."

We are in agreement with this recommendation and will make modifications to the Mail Transport Equipment Support System (MTESS) which will require the user to:

1. Enter the true condition (SERVICEABLE, DEFECTIVE, or CONDEMNED) rather than allowing the system to default to a default condition.
2. Enter the number of units per pallet rather allowing the system to default to pallet preset quantities.

According to the MTESS support team these changes will be completed by August, 2006.