



# OFFICE OF INSPECTOR GENERAL

UNITED STATES POSTAL SERVICE

## Fuel Consumption and Cost Risk Mitigation

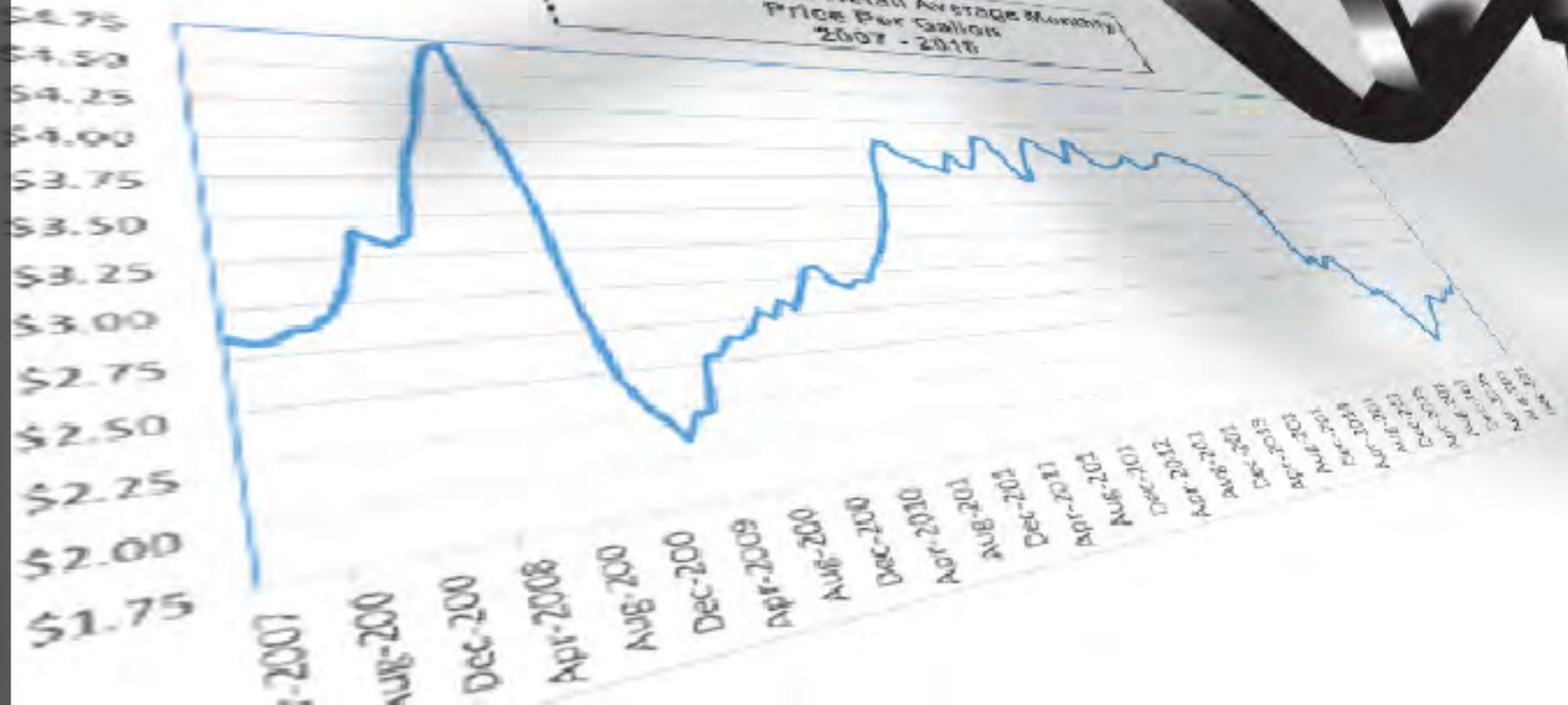
### Audit Report

Report Number  
NL-AR-17-004

April 24, 2017



U. S. Number 2 Retail Average Monthly  
Price Per Gallon  
2007 - 2016





# OFFICE OF INSPECTOR GENERAL UNITED STATES POSTAL SERVICE

## Highlights

*Diesel fuel has been an extremely unstable cost for businesses to manage.*

### Background

The U.S. Postal Service has a surface transportation network that, in fiscal year (FY) 2016, consisted of almost 16,000 supplier-operated highway contract routes (HCR) and about 7,600 Postal Service-owned mail transport vehicles. This fleet makes the Postal Service one of the largest users of diesel fuel in the U.S., purchasing about 251 million gallons in FY 2016 at a cost of more than \$570 million.

Unanticipated events domestically and globally, including natural disasters, disruptions of or reductions in fuel supply, and increased taxes can significantly affect fuel prices. Diesel fuel has been an extremely unstable cost for businesses to manage.

The Postal Service has already experienced the effects of diesel fuel price instability. When diesel fuel prices increased by \$2.03 from March 2009 to March 2012, the Postal Service's fuel costs increased by \$341 million. Conversely, when diesel fuel prices decreased by \$2.00 from March 2014 to February 2016, the Postal Service's fuel costs decreased by \$413 million.

Our objective was to determine whether the Postal Service is positioned to mitigate the risks associated with increased fuel consumption and projected diesel fuel cost increases.

Consisting of almost



**16,000**  
supplier-operated  
highway contract routes

and

**7,600**

Postal Service-owned  
mail transport vehicles



in FY 2016, this fleet makes the Postal Service one of the largest users of diesel fuel in the U.S.

## Purchasing

**251** million gallons  
in FY 2016



at a cost of  
more than  
**\$570**  
million



# OFFICE OF INSPECTOR GENERAL

## UNITED STATES POSTAL SERVICE

### What the OIG Found

We found the Postal Service is not financially or contractually positioned to mitigate risks of increasing diesel fuel prices or consumption.

Despite declines in diesel fuel costs and mail volume, HCR miles and costs continue to increase. Specifically, between FYs 2013 and 2016, mail volume declined by 4.3 billion pieces and surface transportation fuel costs decreased by over \$410 million. However, HCR miles increased by 183 million and HCR costs (excluding fuel) increased by \$797 million. The Postal Service has identified multiple reasons for the increase in HCR costs and miles to include growth in package volume and changes in service standards. This substantial increase in HCR mileage subjects the Postal Service to major financial exposure if diesel fuel prices increase.

The Postal Service does not have a comprehensive strategic plan to address the risk of increasing diesel fuel prices. However, it has taken some interim steps to reduce risk by using fuel efficiency as best value criteria, requiring a sustainability clause in HCR contracts from FY 2016 forward, and encouraging suppliers to convert vehicles to alternative fuels.

In FY 2008, the Postal Service established a goal of reducing HCR diesel fuel use by 20 percent by 2020. It is not currently on target toward meeting this goal, having achieved only a 0.1 percent reduction as of FY 2015.

Management continues to work with HCR suppliers to promote the use of alternative fuels, specifically compressed natural gas (CNG). In 2015 and 2016, HCR suppliers converted about 178 vehicles to alternative fuel without Postal Service incentives. An incentive plan could include such things as sharing CNG conversion costs or a tiered pricing strategy based on fuel type and miles per gallon.

HCR contracts require the Postal Service to pay for diesel fuel increases; however, unlike other shippers, the Postal Service is prohibited by law from using fuel surcharges to recover increased fuel costs from ratepayers.

The U.S. Department of Energy projects a diesel fuel cost increase of \$0.74 per gallon over the next five years from an average price of \$2.63 in 2017 to \$3.37 in 2022. Based on these projections, fuel costs for HCRs will increase by \$600 million over the next five calendar years. With effective strategic planning, the Postal Service has an opportunity to put about \$80 million to better use annually in calendar years 2018 and 2019.



# OFFICE OF INSPECTOR GENERAL

## UNITED STATES POSTAL SERVICE

### What the OIG Recommended

We recommended management develop a comprehensive plan to mitigate the risk of projected fuel price increases. This plan could include the following:

- Enhancing contract negotiations to achieve the lowest price per gallon as well as minimum gallons needed;
- Incentivizing HCR suppliers to convert to alternative fuels by sharing cost savings;
- Establishing a tiered contract pricing strategy based on fuel type and miles per gallon;
- Establishing a fuel fund reserve, and
- Seeking congressional approval for fuel surcharges.

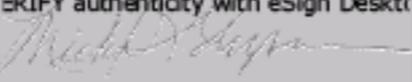
# Transmittal Letter



OFFICE OF INSPECTOR GENERAL  
UNITED STATES POSTAL SERVICE

April 24, 2017

**MEMORANDUM FOR:** ROBERT CINTRON  
VICE PRESIDENT, NETWORK OPERATIONS

E-Signed by Michael Thompson  
VERIFY authenticity with eSign Desktop  


**FROM:** Michael L. Thompson  
Deputy Assistant Inspector General  
for Mission Operations

**SUBJECT:** Audit Report – Fuel Consumption and Cost Risk Mitigation  
(Report Number NL-AR-17-004)

This report presents the results of our audit of the U.S. Postal Service's Fuel Consumption and Cost Risk Mitigation (Project Number 17XG013NL000).

We appreciate the cooperation and courtesies provided by your staff. If you have any questions or need additional information, please contact Daniel Battitori, Director, Transportation, or me at 703-248-2100.

Attachment

cc: Corporate and Audit Response Management  
Postmaster General

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# Findings

## Introduction

This report presents the results of our audit of the U.S. Postal Service's fuel consumption and cost risk mitigation (Project Number 17XG013NL000). Our objective was to determine whether the Postal Service is positioned to mitigate the risks associated with increased fuel consumption and projected diesel fuel cost increases. See [Appendix A](#) for additional information about this audit.

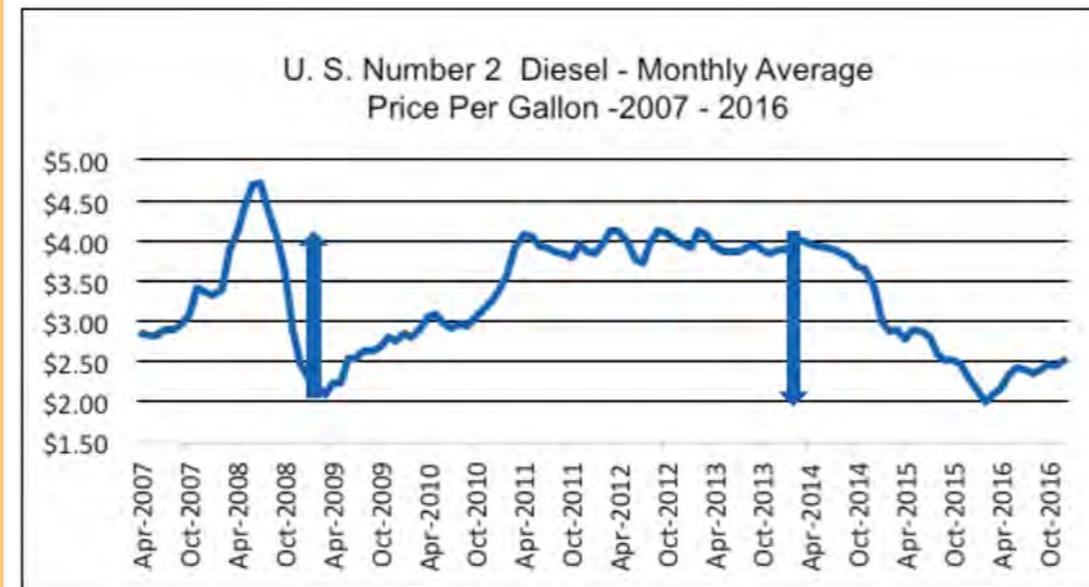
The Postal Service has a surface transportation network that, in fiscal year (FY) 2016, consisted of almost 16,000 supplier-operated highway contract routes (HCR)<sup>1</sup> and about 7,600 Postal Service-owned mail transport vehicles.<sup>2</sup> As a result, it is one of the largest users of diesel fuel<sup>3</sup> in the U.S., purchasing about 251 million gallons for surface transportation at a cost of over \$570 million in FY 2016.

Diesel fuel has been an extremely unstable cost for businesses to manage. Unanticipated events both domestically and globally – including natural disasters, disruptions or reductions in fuel supply, and increased taxes – can significantly affect fuel prices.

The Postal Service has already experienced the effects of diesel fuel price instability. When diesel fuel prices increased by \$2.03 from March 2009 to March 2012, the Postal Service's fuel costs increased by \$341 million. Conversely, when diesel fuel prices decreased by \$2.00 from March 2014 to February 2016, the Postal Service's fuel costs decreased by \$413 million.

Figure 1 depicts the instability of diesel fuel prices from calendar years (CY) 2007 through 2016.

**Figure 1. Fuel Price Instability<sup>4</sup>**



Source: U. S. Department of Energy (DOE), Energy Information Administration.

- 1 HCRs include Transportation and Contract Delivery Service routes and make up the largest single group of transportation services the Postal Service uses.
- 2 Transportation using Postal Service employees and postal-owned vehicles is called Postal Vehicle Service (PVS).
- 3 Ninety-three percent of all HCR fuel is diesel.
- 4 Diesel fuel prices are graphed monthly; however, labels are graphed every four months due to the number of data points.

**The Postal Service is not financially or contractually positioned to mitigate risks of increasing diesel fuel prices or consumption.**

## Summary

We found the Postal Service is not financially or contractually positioned to mitigate risks of increasing diesel fuel prices or consumption.

Despite declines in diesel fuel costs and mail volume, HCR miles and costs (excluding fuel) continue to increase. Specifically, between FYs 2013 and 2016, mail volume declined by 4.3 billion pieces and surface transportation fuel costs decreased by over \$410 million. However, HCR miles have increased by 183 million and HCR costs (excluding fuel) have increased by \$797 million. The Postal Service has identified multiple reasons for the increase in HCR costs and miles to include growth in package volume and changes in service standards. This substantial increase in HCR mileage subjects the Postal Service to major financial exposure if diesel fuel prices increase as projected.

While, the Postal Service does not have a comprehensive strategic plan to manage and fund increasing diesel fuel prices, it has taken steps to manage and mitigate increased fuel consumption and prices by using fuel efficiency as best value criteria, requiring a sustainability clause in FY 2016 and newer HCR contracts, and converting HCR vehicles to alternative fuels.<sup>5</sup>

The Postal Service reported in its annual *Energy Expense Reports*<sup>6</sup> a decline in diesel fuel consumption of about 12 million gallons from FY 2015 to FY 2016; however, the Postal Service was not able to explain the decline because it does not manage and track HCR fuel consumption<sup>7</sup>. In FY 2008, the Postal Service established a goal of reducing HCR diesel fuel usage by 20 percent by 2020, but is not currently on target to achieving that goal, having only achieved a 0.1 percent reduction as of FY 2015.

Management continues to work with HCR suppliers to promote the use of alternative fuels, specifically compressed national gas (CNG). CNG provides better gas mileage, reduces maintenance costs and emissions, and is about \$0.40 cheaper per gallon than diesel. In 2015 and 2016, HCR suppliers converted about 178 vehicles to alternative fuel<sup>8</sup>.

- 5 The manager, Surface Transportation Category Management Center, said that the Postal Service is making conversion to alternative fuel vehicles for HCR suppliers a priority. The manager stated that suppliers that convert to alternative would be given priority. However, the Postal Service is not incentivizing or funding the conversion.
- 6 *Energy Expense Reports* are generated from the Postal Service's Corporate Energy Interface (CEI). The CEI is part of the Postal Service Sustainability organization and enables it to provide end users the ability to generate energy reports for managing utilization and consumption
- 7 The manager, Surface Transportation Category Management Center, stated that HCR fuel gallons between FYs 2015 and 2016 actually increased. Further, they report that FY 2015 HCR gallons captured by their *Energy Expense Report* for FY 2015 were in error.
- 8 Suppliers converted these diesel trucks to alternative fuel vehicles using CNG, liquid natural gas, and hybrid electric. Most of the conversions were to CNG vehicles because of its growing infrastructure.

**Despite declines in diesel fuel costs and mail volume, HCR miles and costs (excluding fuel) continue to increase.**

## Specifically

between FYs 2013 and 2016, mail volume declined by **4.3 billion pieces**



and



surface transportation fuel costs decreased by over **\$410 million.**

## However

HCR miles have increased by **183 million**



and HCR costs (excluding fuel) have increased by **\$797 million.**



The HCR contract requires the Postal Service to pay for HCR diesel fuel increases; however, unlike other shippers, the Postal Service is prohibited by law from using fuel surcharges to recover increased fuel costs from rate payers.

The DOE projects a diesel fuel cost increase of about \$0.74 per gallon over the next five years, from an average cost of \$2.63 in 2017 to \$3.37 in 2022. Based on these projected fuel price increases, the HCR fuel costs will rise by over \$600 million in the next five calendar years. We concluded that the Postal Service has an opportunity to put about \$80 million to better use annually in CYs 2018 and 2019, by implementing a comprehensive strategic plan to manage and fund future increasing diesel fuel prices.

## Financial Exposure to Rising Diesel Fuel Costs

We found the Postal Service is not financially or contractually positioned to mitigate the risk of increasing diesel fuel prices or consumption.

### Trends in Mail Volume, Fuel Gallons, and HCR Miles and Costs

Despite declines in diesel fuel costs and mail volume, HCR miles and costs (excluding fuel) continue to increase. Specifically, between FYs 2013 and 2016, mail volume has declined by 4.3 billion pieces and surface transportation fuel costs decreased by over \$410 million.<sup>9</sup> However, HCR miles have increased by 183 million and HCR costs (excluding fuel) have increased by \$797 million (see Table 1). This substantial increase in HCR mileage subjects the Postal Service to major financial exposure when diesel fuel prices increase.

**Table 1. Mail Volume, Surface Transportation Fuel, and HCR Miles and Costs<sup>10</sup>**

Fiscal Year	Mail Volume (in millions)	Surface Transportation Fuel Costs <sup>11</sup>	HCR Fuel Gallons	HCR Miles	HCR Costs (excluding fuel) <sup>12</sup>
2013	158,222	\$980,129,441	231,276,831	1,451,874,210	\$2,445,807,212
2014	155,539	\$983,395,452	237,983,661	1,500,857,500	\$2,596,726,421
2015	154,035	\$776,329,935	239,290,531	1,553,467,582	\$2,881,239,739
2016	153,941	\$570,453,494	227,013,822	1,634,984,310	\$3,243,125,073
Change: 2013 to 2016	(4,281)	(\$409,675,947)	(4,263,009)	183,110,100	\$797,317,861

Source: Various Postal Service sources.<sup>13</sup>

<sup>9</sup> The Postal Service's Fuel Price Index program for HCR suppliers adjusts fuel prices monthly, which has driven fuel cost savings in FYs 2015 and 2016. Specifically, the Postal Service negotiates and establishes the contract's baseline fuel price per gallon (ppg). The Postal Service subsequently uses the DOE's regional fuel indexes to adjust the monthly fuel ppg when the regional fuel index prices fluctuates by \$.05 or more in a single month.

<sup>10</sup> Surface Transportation costs cover both HCR and PVS.

<sup>11</sup> HCRs account for over 91 percent of Postal Service fuel costs.; therefore, we focused our assessment on HCR fuel costs.

<sup>12</sup> We started with HCR costs reported on Forms 10-K and reconciled with data in the Enterprise Data Warehouse (EDW). We then removed fuel costs as reported in the Postal Service's *Energy Expense Reports*.

<sup>13</sup> Information came from the Postal Service's Forms 10-K, *Energy Expense Reports*, Excel workbooks, and EDW expense summaries.

The manager, Surface Transportation Category Management Center, questioned the fuel gallons that we are reporting based upon the HCR data in the Transportation Contract Support System (TCSS). We used the Postal Service's Form 10-K for FYs 2013 through 2016 to identify total HCR costs and the Postal Service's *Energy Expense Report* for HCR fuel costs and gallons for FYs 2013 through 2016. The manager stated that the *Energy Expense Reports* we used to capture HCR fuel gallons are based on actual gallons used under the HCR Voyager Card Program,<sup>14</sup> which, in many cases, exceeded the number of gallons authorized in the contracts. Further, she said that the *Energy Expense Report* for FY 2015 may have double counted HCR fuel gallons during the transition from HCR Voyager<sup>15</sup>, thereby overstating FY 2015 HCR gallons by as much as 25 million. However, she was not able to provide any support for her opinion. We are not making a recommendation concerning this matter because it is outside the scope of this audit. The manager later confirmed that the HCR gallons reported for FY 2016 were accurate.

The Postal Service has identified multiple reasons for the increase in HCR costs and miles. Per its FY 2016 Form 10-K, shipping and packages volume has grown, which has changed the mail mix, cubic volume, and weight. In addition, the Postal Service manager for Surface Transportation said that the HCR miles increased as a result of the changes in service standards and the operational window for processing mail. Additionally, he said moving mail from air to surface transportation increased the use of HCR long-haul transportation, which also contributed toward the increase in HCR costs and miles.

### **Mitigation Plan**

The Postal Service does not have a comprehensive strategic plan to manage and fund increasing diesel fuel prices, but has taken some interim steps to manage and mitigate increased fuel consumption and prices, such as using fuel efficiency as best value criteria<sup>16</sup>, requiring a sustainability clause in newer HCR contracts (FY 2016 and later), and supporting HCR supplier conversion of vehicles to alternative fuels.

The Postal Service reported a decline in diesel fuel consumption of about 12 million gallons from FY 2015 to FY 2016, but was not able to explain the decline because it does not manage and track HCR fuel consumption.

The Postal Service established a goal in FY 2008 of reducing HCR diesel fuel use by 20 percent by 2020, but is not currently on target to achieve the goal and had only achieved a 0.1 percent reduction as of FY 2015. Management continues working with HCR suppliers to promote using alternative fuels, specifically CNG. CNG provides better gas mileage, reduces emissions, and is \$0.40 cheaper per gallon than diesel fuel.

In 2015 and 2016, HCR suppliers converted about 178 vehicles to alternative fuel vehicles without Postal Service incentives. The conversions reduced diesel consumption and the size of the carbon footprint and saved fuel costs; however, the number of vehicles converted out of a total contracted HCR fleet of about 20,500 vehicles is less than 0.9 percent.

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<sup>14</sup> The Postal Service terminated the HCR Voyager Card Program effective June 30, 2015, in response to a series of U.S. Postal Service Office of Inspector General (OIG) audits and investigative work.

<sup>15</sup> During the conversion from HCR Voyager, the Postal Service had to move the contracted gallons, which were under HCR Voyager to the fuel price indexing program.

<sup>16</sup> Contracting officers are to consider the supplier's sustainability plan to determine which offeror provides the best overall value for the Postal Service.

Without an actionable and comprehensive plan, including executing the HCR contract sustainability clause and requiring and incentivizing for alternative fuel vehicles, the Postal Service will not be able to transition HCR supplier vehicles to alternative fuels to achieve lower and more stable prices. Additionally, the comprehensive plan should ensure that the Postal Service is negotiating the lowest price per gallon as well as gallons needed.

In addition to the steps or initiatives addressed above, management has recently initiated action to help mitigate increased fuel prices and consumption, including:

- Using tools, such as an Excel-based predictive model developed in September 2016, and fuel forecast data from a national market research firm; and
- Setting aside, when financially viable, a contingency to cover unexpected cost increases, including fuel, which exceed annual inflationary targets obtained from an outside economic and risk management leader. This contingency does not carry over from year to year.

### **Fuel Surcharges**

Fuel surcharges are common in the transportation industry (trucking companies and airlines) when fuel prices increase beyond an expected or budgeted level. Surcharges allow transportation operators to pass the additional fuel price fluctuations to their customers. However, HCR contracts require the Postal Service to pay for HCR diesel fuel increases and it is prohibited by law<sup>17</sup> from using fuel surcharges to recover increased fuel costs from ratepayers.

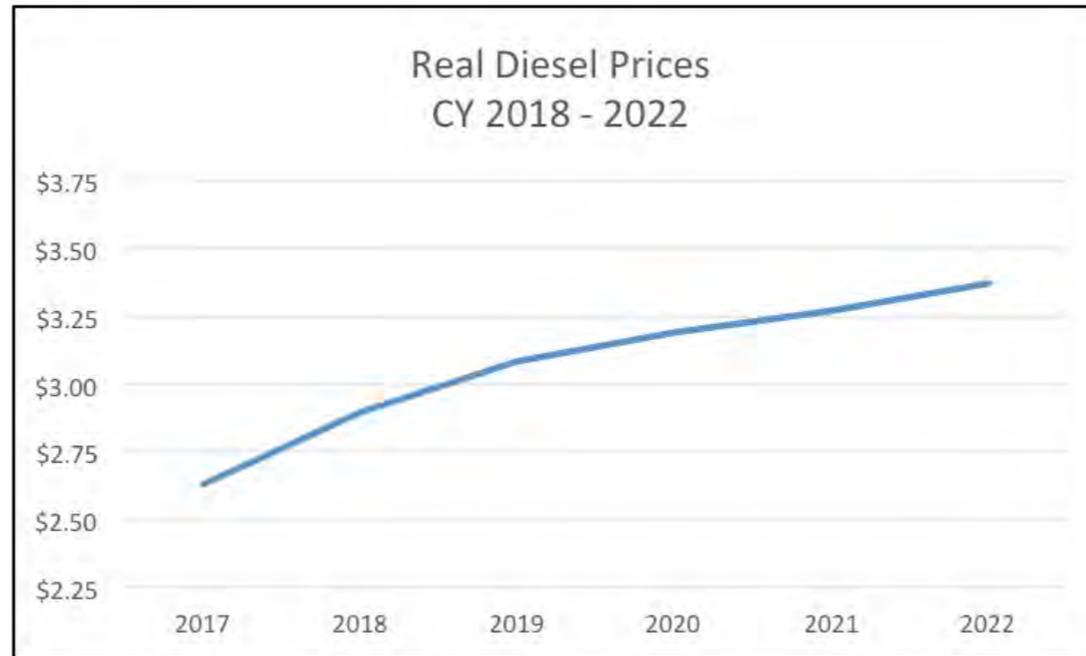
### **Fuel Price Volatility and Risk Mitigation**

The price of diesel fuel increased from \$2.00 per gallon in February 2016, to \$2.51 in December 2016. Additionally, the DOE projects a diesel fuel cost increase of \$0.74 per gallon over the next five years from an average of \$2.63 in 2017 to \$3.37 in 2022 (see [Figure 2](#)).

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<sup>17</sup> Postal Accountability and Enhancement Act of 2006, Public Law No. 109-435, in which Congress imposed a price cap on Postal Service charges to “create predictability and stability in rates” and limited increases in most products (e.g., First-Class Mail and periodicals) to the rate of inflation. A narrow exception to the price cap exists for “extraordinary or exceptional circumstances,” but this exception does not entail the market responsiveness ordinarily expected of a fuel surcharge mechanism. 39 U.S.C. §3622(d)(1)(E).

**Figure 2. Forecasted Fuel Price Increases<sup>18</sup>**



Source: DOE's Annual Energy Outlook 2017 - Data (dated January 5, 2017).

Based on these projected fuel price increases, the Postal Service will need to fund over \$600 million in additional fuel costs for HCRs over the next five calendar years based on existing mileage. We concluded that the Postal Service should mitigate these risks by implementing a comprehensive strategic plan to manage and fund future increasing diesel fuel costs.

<sup>18</sup> We show the DOE projected diesel fuel prices for the five-year period covering CYs 2018–2022. DOE defines “real” prices as a price that has been adjusted to remove the effect of changes in the purchasing power of the dollar (i.e., it is expressed in constant dollars). Additionally, we use CY 2017 as the base and implementation year in which the Postal Service can take corrective actions.

# Recommendation

***We recommend management develop a comprehensive fuel risk mitigation plan, which could include negotiations for the best fuel prices and gallons, incentives for alternative fuels, tiered contract pricing, a fuel fund reserve and potential fuel surcharges.***

We recommend the vice president, Network Operations, in coordination with the vice president, Supply Management:

1. Develop a comprehensive plan to mitigate risk of projected future fuel price increases, which could include:
  - Enhancing contract negotiations to achieve the lowest price per gallon and minimum gallons needed;
  - Incentivizing highway contract route suppliers to convert to alternative fuels by sharing cost savings;
  - Establishing a tiered contract pricing strategy based on fuel type and miles per gallon;
  - Establishing a fuel fund reserve; and
  - Seeking congressional approval for fuel surcharges.

## Management's Comments

Management said they generally agree with the finding and they agree with the recommendation. The Postal Service acknowledged that strategic planning for fuel is important and recognizes that diesel fuel represents a significant share of network transportation costs.

However, management disagrees with the monetary impact because it focuses on fuel consumption and projected fuel prices without considering ongoing initiatives to reduce total transportation costs. These initiatives include current solicitation for the Transportation Management System and the Dynamic Route Optimization pilot. The Postal Service also notes that the monetary impact calculation assumes that total fuel consumption through FY 2019 will remain flat despite a reported decline in fuel consumption from FY 2013 to FY 2016. Management also disagrees with the funds put to better use because these expenses have not occurred.

Regarding the recommendation, management stated that they will develop a comprehensive risk mitigation plan by August 2017. The plan will have multiple initiatives including incentivizing HCR suppliers to convert to alternative fuels. Management also stated that the recommendation includes suggestions for items to be included in a comprehensive plan and they understand these items are for management's consideration only.

See [Appendix B](#) for management's comments in their entirety.

## Evaluation of Management's Comments

The OIG considers management's comments responsive to the recommendation in the report.

The OIG believes that the monetary impact analysis is reasonable because we based it on the most recent fuel gallon usage and the DOE's projected diesel fuel prices, which the Postal Service uses and which have been identified as an industry best practice. The OIG believes that by strategically managing for projected increases in diesel fuel prices, the Postal Service will be in a better position to mitigate any realized increases, which will provide an opportunity to put funds to better use instead of incurring increased fuel costs. The OIG did not factor in the decline in fuel gallons because while the Postal Service did report a decline, management disagreed with their own energy expense report. As a result, management could not explain the decline and identified it as a trend. Further, we did not include the Transportation Management System and the Dynamic Route Optimization initiatives the Postal Service identified because they are new initiatives and their effect on fuel is unknown.

The recommendation requires OIG concurrence before closure. Consequently, the OIG requests written confirmation when corrective action is completed. The recommendation should not be closed in the Postal Service's follow-up tracking system until the OIG provides written confirmation that the recommendation can be closed.

# Appendices

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## Appendix A: Additional Information

### Background

The Postal Service had a surface transportation network for FY 2016 that consisted of almost 16,000 supplier-operated HCRs and about 7,600 postal-owned mail transport vehicles. As a result, the Postal Service is one of the largest users of diesel fuel in the U.S., purchasing about 251 million gallons for surface transportation at a cost of over \$570 million in FY 2016.

Diesel fuel is an extremely unstable cost for businesses to manage. Unanticipated events domestically and globally, including natural disasters, disruption of or reduction in fuel supply, and increased taxes, can significantly affect fuel prices.

The Postal Service has already experienced the effects of diesel fuel price instability. When diesel fuel prices increased by \$2.03 from March 2009 to March 2012, the Postal Service's fuel costs increased by \$341 million. Conversely, when diesel fuel prices decreased by \$2.00 from March 2014 to February 2016, Postal Service fuel costs decreased by \$413 million (see Table 2 for total costs and Figure 3 for high and low average ppg by fiscal year).

**Table 2. Total Surface Transportation Fuel Costs**

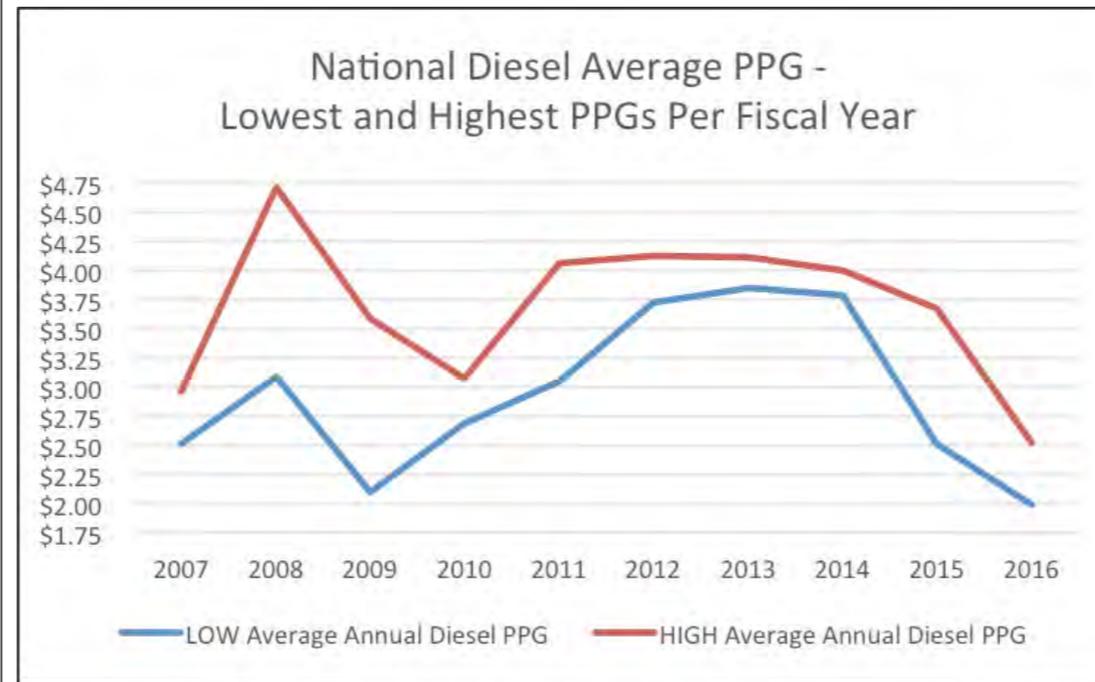
Fiscal Year	Low Average PPG	High Average PPG	Total Surface Fuel Costs
2007	\$2.51	\$2.96	\$733,789,747
2008	\$3.09	\$4.71	\$1,020,683,079
2009	\$2.10	\$3.59	\$670,374,769
2010	\$2.68	\$3.07	\$783,015,906
2011	\$3.05	\$4.06	\$962,106,477
2012	\$3.72	\$4.13	\$1,011,003,016
2013	\$3.85	\$4.11	\$980,129,441
2014	\$3.79	\$4.00	\$983,395,452
2015	\$2.51	\$3.68	\$776,329,935
2016	\$2.00	\$2.52	\$570,453,494

Total fuel costs rose by \$341 million as fuel prices increased between 2009 and 2012

Total fuel costs dropped by \$413 million as fuel prices declined between 2014 and 2016

Source: DOE's monthly average diesel ppg and the Postal Service's *Energy Expense Report*.

**Figure 3. High and Low Average Diesel Prices by Fiscal Year**



Source: DOE's monthly average diesel ppg.

In FY 2008, the Postal Service established a sustainability program to meet the spirit of federal energy management and emissions requirements, although it is exempt from specific federal executive orders and renewable energy provisions.<sup>19</sup> Specifically, the Postal Service voluntarily pursues increased use of renewable energy through projects that reduce the use of fossil fuels and have a favorable return on investment. Management established a goal of reducing the use of petroleum fuel for its owned and contracted fleet by 20 percent by 2020.<sup>20</sup>

### Objective, Scope, and Methodology

Our objective was to determine whether the Postal Service is positioned to mitigate the risks associated with increased fuel consumption and projected diesel fuel cost increases. Our audit focused on HCR and PVS costs and gallons used during FYs 2007 through 2016, and potential fuel price increases over the next five years.

To accomplish our objective, we:

- Obtained and analyzed HCR and PVS gallons used; HCR costs and miles; and mail volume and revenue and expenses covering 2007 through 2016 from Forms 10-K, *Energy Expense Reports*, Excel workbooks, and the EDW to identify patterns and trends.
- Reviewed Postal Service policies and procedures relating to reducing surface transportation fuel consumption and planning for fuel price increases.

<sup>19</sup> Executive Orders 13423 and 13514 and the Energy Policy Act of 2005.

<sup>20</sup> The baseline for measuring sustainability performance for both contracted transportation and Postal Service vehicles is FY 2008.

- Obtained the DOE's monthly and annual regional fuel index prices for 2007 through 2016 and trended fuel price fluctuations.
- Obtained the DOE's projected fuel prices for the next five years (CYs 2018 through 2022) and calculated the potential impact on Postal Service HCR transportation costs.
- Interviewed Postal Service Headquarters Supply Management, Network Operations, and Sustainability and Budgeting Initiatives managers to discuss HCR policies and procedures and fuel contract provisions and strategies related to mitigating increased fuel prices and consumption (including the use of alternative fuel vehicles in its contracted and owned fleets). We also discussed how they would fund significant fuel increases in fuel costs for surface transportation.

We conducted this performance audit from February through April 2017, in accordance with generally accepted government auditing standards and included such tests of internal controls, as we considered necessary under the circumstances. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our finding and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our finding and conclusions based on our audit objective. We discussed our observations and conclusions with management on March 21, 2017, and included their comments where appropriate.

We did not assess the reliability of any computer-generated data for the purposes of this report. We reviewed the Postal Service's *Energy Expense Reports*, Excel workbooks, and EDW summary expense reports to trend ten years. We did analysis to determine how the data were collected and followed up with managers to understand data collection. In addition, mail volume and mail mix data and high-level transportation cost data used for analysis were public reports provided by the Postal Service to the Postal Regulatory Commission.<sup>21</sup> We determined that the data used were sufficiently reliable for the purposes of this report.

### **Prior Audit Coverage**

The OIG did not identify any prior audits related to the objective of this audit.

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<sup>21</sup> Form 10-K, Annual Report and Revenue, Pieces and Weight reports.

## Appendix B: Management's Comments



April 14, 2017

LORI LAU DILLARD

SUBJECT: Fuel Consumption and Cost Risk Mitigation (Report Number NL-AR-17-DRAFT)

Thank you for providing the United States Postal Service with an opportunity to review and comment on the subject draft audit report "Fuel Consumption and Cost Risk Mitigation". Management generally agrees with the findings included in the draft report. Accordingly, management agrees with the recommendation; however, disagrees with the monetary impact in total.

At the outset of our response, we share the view of the OIG that strategic planning around the area of fuel cost is important, and that the Postal Service recognizes the significant share that diesel fuel represents of our expense budgets for network transportation.

The OIG suggests that the Postal Service is not positioned to either mitigate increased diesel fuel prices or reduce consumption. In fact the Postal Service is already implementing strategies to reduce the number of Highway Contract Route (HCR) miles driven and fuel gallons required within our transportation network. As an example, while not referenced in the OIG's report, the Postal Service is currently soliciting for an enterprise-wide Transportation Management System (TMS), has already completed a pilot and is now executing on the strategy to solicit and establish multiple sites under a Dynamic Route Optimization (DRO) Initiative. All of these projects are part of existing management initiatives and also have added benefits of reducing environmental impacts allowing the Postal Service to become more sustainable.

Management disagrees with the OIG's monetary impact which focuses exclusively on fuel consumption and projected fuel price per gallon increases without consideration of the impact of any ongoing initiatives to reduce our total cost of mail transportation. The OIG characterizes the monetary impact as "funds put to better use"; however, such funds are for expenses which have not occurred. Any future impacts will be dependent on market conditions and the results of our ongoing strategies. Management has previously noted in responses to OIG reviews, that fuel price is just one element considered as part of the Postal Service's overall objective to manage expenses. Finally, while future events are unknown, the OIG's calculation assumes that total fuel consumption will remain flat between Fiscal Years 2016 and 2019. However, the OIG's report actually documents the reduction in HCR fuel gallons between Fiscal Years 2013 and 2016.

Management's response to the recommendation included in the draft report may be found below.

We recommend the Vice President, Network Operations, in coordination with the Vice President, Supply Management:

Recommendation 1: Develop a comprehensive plan to mitigate risk of projected future fuel price increases, which could include:

- Enhancing contract negotiations to achieve the lowest price per gallon and minimum gallons needed;
- Incentivizing highway contract route suppliers to convert to alternative fuels by sharing cost savings;
- Establishing a tiered contract pricing strategy based on fuel type and miles per gallon;
- Establishing a fuel fund reserve; and
- Seeking congressional approval for fuel surcharges.

Management Response to Recommendation 1: Management agrees with this recommendation. Management will aggregate and develop a comprehensive risk mitigation plan. The Postal Service, as previously described, has already enacted multiple initiatives to mitigate the risk of future fuel price increases. These actions include implementing procedural guidance on determining fuel mileage and offerors' proposed initial fuel price per gallon as a starting point for negotiations, as well as incentivizing HCR suppliers to convert to alternative fuels. We note that the OIG's recommendation includes suggestions for inclusion within the comprehensive plan. We understand these to be items for management consideration only.

Target Implementation Date: August 2017

Responsible Officials: Acting Manager, Surface Transportation Operations, Network Operations, and Manager, Surface Transportation Category Management Center, Supply Management



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Vice President  
Network Operations



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Supply Management

cc: Manager, Corporate Audit Response Management



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