



OFFICE OF INSPECTOR GENERAL

UNITED STATES POSTAL SERVICE

Market Dominant Billing Determinants: Periodicals

Audit Report

Report Number
CP-AR-15-004

September 14, 2015



1.426,	989,69	317
1.83	536,15	214
1.752,60	293,05	221
1.230,18	265,82	100
406,12	878,94	
1.649,21	577,41	
1.573,66	-187,74	
1.150,13	-152,81	
330,72	1.357,65	
1.641,01	681,62	
2.114,51	-161,62	
1.624,95	-290,71	
	203,15	

20	56,	10	21	174	188	289	317	214	221	100
	82,7									
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UNITED STATES POSTAL SERVICE

Highlights

The Postal Accountability and Enhancement Act requires the Postal Service to produce an Annual Compliance Report within 90 days of the end of each fiscal year. Billing determinants are filed in support of this report and used to ensure that price adjustments do not exceed price caps for each market dominant class of mail.

Background

Billing determinants are spreadsheets that U.S. Postal Service employees manually produce to report volume and revenue for every price in the five market dominant classes of mail: First-Class Mail, Periodicals, Standard Mail, Package Services, and Special Services. Periodicals primarily consist of flat-shaped mail that contains educational, cultural, or scientific information, such as magazines and newspapers. The Postal Service obtains data for Periodicals billing determinants from the following sources: its published price list, the Shape Indicia Report, and the Revenue, Pieces, and Weight Report. This is the second in a series of audits on billing determinants. The first audit looked at First-Class Mail.

The Postal Accountability and Enhancement Act requires the Postal Service to produce an Annual Compliance Report within 90 days of the end of each fiscal year. The report analyzes costs, revenue, pricing, and quality of service for all products. Billing determinants are filed in support of this report and used to ensure that price adjustments do not exceed price caps for each market dominant class of mail. The manual preparation and complexity of the spreadsheets create a risk of data entry errors.

Our objective was to assess the accuracy and completeness of data used to prepare fiscal year (FY) 2013 and FY 2014 Periodicals billing determinants.

What the OIG Found

We did not find issues with completeness of data; however we did identify data inaccuracies that could be prevented by improving the procedures used to prepare Periodicals billing determinants. Specifically, there were errors in the FY 2013 and FY 2014 determinants because employees used outdated and mislabeled source data and made incorrect calculations. Further, the Postal Service did not establish adequate controls over the Periodicals billing determinant process. As a result of our First-Class Mail billing determinants audit, the Postal Service began to document repeatable processes for preparing billing determinant spreadsheets. Although these procedures are being developed, there were no internal reviews conducted of Periodical billing determinants prior to FY 2015. As a result, the Postal Service incorrectly calculated an absolute value of \$7.6 million in revenue for FYs 2013 and 2014. Although these errors did not impact compliance with 2015 price cap requirements, future errors may do so.

What the OIG Recommended

We recommended the vice president, Pricing, file corrected Periodicals billing determinants for FYs 2013 and 2014 with the Postal Regulatory Commission no later than December 2015; ensure source data is labeled correctly and labeling errors are not repeated; increase transparency by disclosing the methodology for calculating editorial discounts; and complete ongoing internal efforts to ensure all Periodicals billing determinants are produced using documented and repeatable processes that include an in-depth internal review process.

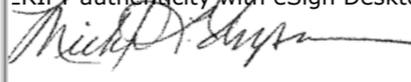
Transmittal Letter



OFFICE OF INSPECTOR GENERAL
UNITED STATES POSTAL SERVICE

September 14, 2015

MEMORANDUM FOR: CYNTHIA SANCHEZ-HERNANDEZ
VICE PRESIDENT, PRICING

E-Signed by Michael Thompson
VERIFY authenticity with eSign Desktop


FROM: Michael L. Thompson
Acting Deputy Assistant Inspector General
for Technology, Investment and Cost

SUBJECT: Audit Report – Market Dominant Billing Determinants: Periodicals
(Report Number CP-AR-15-004)

This report presents the results of our audit of the Market Dominant Billing Determinants: Periodicals (Project Number 15TG028CP000).

We appreciate the cooperation and courtesies provided by your staff. If you have any questions or need additional information, please contact Guy Sergi, acting director, Cost and Pricing, or me at 703-248-2100.

Attachment

cc: Corporate Audit and Response Management

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Findings

Opportunities exist to improve the accuracy of the Postal Service's billing determinant calculations for Periodicals. Specifically, we identified errors resulting from the use of outdated and mislabeled source data and other incorrect calculations. The combined effect of these errors resulted in the Postal Service incorrectly reporting \$7.6 million in calculated revenue for FY 2013 and FY 2014.

Introduction

This report presents the results of our self-initiated audit of the U.S. Postal Service's Market Dominant Billing Determinants: Periodicals (Project Number 15TG028CP000). This is the second in a series of audits on billing determinants. Our audit objective was to assess the accuracy and completeness of the data used to prepare fiscal year (FY) 2013 and FY 2014 Periodicals billing determinants. See [Appendix A](#) for additional information about this audit.

Billing determinants are spreadsheets that Postal Service employees manually produce to report volume and calculated revenue¹ for every price in the five market dominant classes of mail:

Hover over an icon to reveal the market domain classes of mail.

The Postal Service and the Postal Regulatory Commission (PRC) use billing determinants to ensure that price adjustments do not exceed price caps² for each market dominant class of mail. The Postal Service also uses billing determinants in its *Annual Compliance Report* (ACR) as part of the process to develop avoided cost estimates, which the Postal Service uses to set workshare discounts.

Conclusion

While we did not find any issues with the completeness of billing determinant procedures for Periodicals³, there are opportunities to improve their accuracy. Specifically, we identified errors resulting from the use of outdated⁴ and mislabeled source data and other incorrect calculations. Further, the Postal Service did not establish adequate controls over the Periodicals billing determinant process. As a result of our First-Class Mail billing determinants audit, the Postal Service began documenting repeatable processes for preparing billing determinant spreadsheets. Although these procedures are being developed, there were no internal reviews conducted of Periodical billing determinants prior to FY 2015. The combined effect of these errors resulted in the Postal Service incorrectly reporting \$7.6 million in calculated revenue for FYs 2013 and 2014.⁵ Although these errors did not result in the Postal Service having to adjust prices, there is a risk that future billing determinant calculation errors could result in prices that exceed the price cap.

¹ Calculated revenue equals volume multiplied by price, as opposed to actual revenue, which is revenue the Postal Service receives.

² The inflation-based limit on Postal Service prices as described in the Postal Accountability and Enhancement Act (PAEA).

³ To assess completeness of data we compared the data on the Periodical billing determinant spreadsheets with data listed on the Public Cost and Revenue Analysis (CRA). We determined that the data from the CRA was included in the billing determinant spreadsheets.

⁴ The following source data is used to prepare the Periodicals billing determinants: published price list, the Shape Indicia Report, and Revenue, Pieces, and Weight (RPW) Report.

⁵ The amount cited is the absolute value of our calculations which is the sum of the figures regardless of whether they are positive or negative. The net value is an understatement of revenue of \$2.2 million.

Billing Determinant Accuracy

Opportunities exist to improve the accuracy of Periodicals billing determinant procedures. We found inaccuracies due to use of outdated or mislabeled source data and calculation errors. Overall these errors occurred because the Postal Service did not establish adequate controls over the Periodicals billing determinant process. Prior to FY 2015, the Postal Service did not have documented and repeatable processes for preparing billing determinant spreadsheets and did not review billing determinants prior to publication. Although these procedures are currently being developed, there were no internal reviews conducted of Periodical billing determinants prior to FY 2015. As a result, the Postal Service incorrectly reported \$7.2 million in calculated revenue for FY 2013 and \$0.4 million for FY 2014 on the billing determinants spreadsheets. These errors did not result in the Postal Service having to adjust postage prices; however, there is a risk that future billing determinant calculation errors could result in prices that exceed the price cap.

In addition, we noted the methodology used to calculate billing determinants for editorial discounts was not consistent with the overall Periodicals billing determinant calculation methodology. Although the difference in methodologies is reasonable, there is less transparency for users⁶ of Periodicals billing determinants because the difference is not explained.

Inaccurate Source Data

Inaccurate source data resulted in employees making errors in Periodicals billing determinant spreadsheets. We found two types of errors that resulted from using inaccurate source data.

In Quarter (Q) 2, FY 2013, the Postal Service instituted a price adjustment. When a price adjustment occurs in the middle of a quarter, the Postal Service must request two sets of source data for that quarter; one for the pre-adjusted price and one for the post-adjusted price. This is known as “split quarter” source data. In FY 2013, the Postal Service used Q2 source data; however it did not receive the updated “split-quarter” source data from its contractor because of a Postal Service oversight. Therefore, the Q2, FY 2013, billing determinants did not reflect the updated source data file. As a result, there was a \$6.3 million error in the FY 2013 Periodicals billing determinants.

We also found four mislabeled rows for each quarter in the FY 2014 Periodicals source data file. The source data mislabeled Origin ADC⁷ as Origin NDC.⁸ These errors did not impact calculated revenue because the Postal Service’s pricing economist identified them. If these errors occur again, they may not be identified and could lead to billing determinant spreadsheet inaccuracies.

Other Calculation Errors

We found 15 calculation errors in the FY 2013 and 2014 Periodicals billing determinant spreadsheets that resulted from using incorrect values or making mathematical errors. Four of the errors found in Q3, FY 2013, were repeated in Q4, FY 2013, and again in Q1, FY 2014. Examples include:

- Misclassified mailpieces. In FYs 2013 and 2014 Mixed ADC Sack Origin ADC Entry pieces were reported as Mixed ADC Sack Origin NDC Entry pieces and vice versa.
- Volume multiplied by an incorrect price as a result of retrieving incorrect figures from the price list.

⁶ Users include business mailers, the PRC, stakeholders and anyone interested in Periodicals pricing.

⁷ A mail processing facility that receives, processes, and distributes mail destined for specific ZIP Code areas under the Managed Mail Program.

⁸ A highly mechanized mail processing plant (formerly called a Bulk Mail Center) that distributes Standard, Periodicals, and Package Services Mail in bulk volume.

- Spreadsheet formula errors such as linking formulas to an incorrect cell.

The total impact of general calculation errors was about \$900,000 in FY 2013 and \$400,000 in FY 2014.

Review of Editorial Discount

The methodology used to calculate billing determinants for editorial discounts was not transparent. The Postal Service did not disclose the difference between the editorial discount billing determinant formula and the formula used for all other Periodicals billing determinants. The Postal Service uses actual volume to calculate all other Periodicals billing determinants, but uses a calculated figure⁹ for editorial discount volume.

The reporting of a calculated volume, as opposed to the actual volume, is necessary for two reasons. First, if the actual volume of publications receiving editorial discounts were reported it would nearly equal the total number of Periodicals. Therefore, using actual volume would result in unnecessary work to eliminate only a fraction of periodicals. Second, using actual volume in the price adjustment calculations would result in a price per publication, which would be unrealistic. Assuming a volume that corresponds to the maximum editorial discount is optimal because it eliminates this concern.

We found no indication in the billing determinant spreadsheets that the editorial discount volume was not an actual volume. Furthermore, the Postal Service does not disclose why it calculates editorial discount volume differently. Although we determined the difference in methodology is reasonable, the lack of disclosure reduces transparency for Periodicals billing determinant users.

Billing Determinant Controls

Prior to FY 2015, the Postal Service did not have documented and repeatable processes for preparing billing determinant spreadsheets and did not conduct internal reviews of billing determinants prior to publication. The Pricing department has only 10 calendar days from when source data is obtained to compile billing determinant spreadsheets because of PRC filing timeline requirements. The current manual process allows the preparer of billing determinants to visually verify that the correct source data is used, rather than inspecting computer code for accuracy. The current process, with the amount of judgement required and the tight timeframes would be difficult to automate; however, as business processes change, opportunities for automation may increase and should be pursued.

During our audit of First-Class Mail[®] billing determinants,¹⁰ the Pricing department instituted billing determinant internal controls that require a review of billing determinant accuracy. During the current audit the Pricing department began documenting the billing determinant calculation process. While these controls are helping to reduce reporting errors, improved controls over the billing determinant process could have prevented errors found in this audit.

Improved controls for billing determinants could be an internal system of written procedures and practices to assess the accuracy and completeness of the volume, price, and revenue data reported in Periodicals billing determinants. Additionally, the Postal Service could incorporate Microsoft Excel tools to identify data changes and adopt a review process for billing determinant spreadsheets.

⁹ The calculated volume figure represents the number of pieces that would exist if every piece received the maximum editorial discount.

¹⁰ *Market Dominant Billing Determinants: First-Class Mail* (Report Number CP-AR-15-003, June, 11, 2015).

Recommendations

We recommend management file corrected Periodicals billing determinants for fiscal years 2013 and 2014; ensure source data is labeled correctly and labeling errors are not repeated; disclose the methodology used to calculate editorial discounts and the reason for the different calculation method; and complete ongoing internal efforts to ensure that all Periodicals billing determinants are produced using documented and repeatable processes.

We recommend the vice president, Pricing:

1. File corrected Periodicals billing determinants for fiscal years 2013 and 2014 with the Postal Regulatory Commission no later than December 2015.
2. Ensure the source data is labeled correctly and labeling errors are not repeated while preparing billing determinants.
3. Disclose the methodology used to calculate editorial discounts and the reason for the different calculation method.
4. Complete ongoing internal efforts to ensure that all Periodicals billing determinants are produced using documented and repeatable processes that include an internal review process no later than December 2015.

Management's Comments

Management agrees there are opportunities to strengthen the billing determinants process. Management believes that a \$2.2 million net value is a more accurate depiction of the revenue impact than the OIG's \$7.6 million absolute value. Management also stated that, while the audit was underway, they completed the documentation of the billing determinants process for Periodicals and the activities are ongoing.

Management disagreed with recommendation 1 and views the level of change as de minimis or immaterial when based on the net value amount.

Management disagreed with recommendation 2 because it does not fall under the purview of Pricing. However, Pricing personnel notified preparers of the source data of the labeling errors identified in this report and appropriate corrections have been made.

Management agreed with recommendation 3 and, in the future, will provide a footnote to explain how they account for the editorial discount.

Management agreed with recommendation 4 and continues to strengthen internal controls over the billing determinants process.

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

Evaluation of Management's Comments

The U.S. Postal Service Office of Inspector General (OIG) generally considers management's comments responsive to the recommendations in the report.

Management disagreed with our recommendation to file corrected Periodicals billing determinants for FYs 2013 and 2014 because it is immaterial when using net value. While we understand the Postal Service's perspective on net value, we believe absolute value is a more appropriate measurement. Net value understates the total financial impact of each exception on the billing determinant calculations. While we believe that the FY 2014 billing determinants correction should be filed to ensure accuracy, we understand that the amount is minimal, therefore we agree with the Postal Service's decision not to revise FY 2014 billing determinants. However, we believe the Postal Service should file the FY 2013 billing determinants corrections with the PRC to ensure accuracy.

While management disagreed with our recommendation to ensure that source data is labeled correctly and labeling errors are not repeated, they did cite actions they have taken and are taking to address the concern we identified. In addition, the Postal Service has taken the initiative to footnote the editorial discount calculation and proactively begin documenting the process for preparing billing determinants. We will evaluate these actions in future audit work.

Appendices

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Appendix A: Additional Information

Background

Billing determinants are spreadsheets that Postal Service employees manually produce to report volume and revenue for every Postal Service price in each class of market dominant mail. The Postal Service primarily obtains data for Periodicals billing determinants from its published price list, the Shape Indicia Report, and the RPW report.¹¹

Employees primarily use volume and price data for the spreadsheets from RPW data and the Postal Service's Notice 123.¹² Billing determinants are produced for five market dominant classes of mail: First-Class Mail, Periodicals, Standard Mail, Package Services, and Special Services. This audit focuses on Periodicals billing determinants. Periodicals are defined as "a class of mail consisting of magazines, newspapers, or other publications formed of printed sheets that are issued at least four times a year at regular, specified intervals (frequency) from a known office of publication." The Postal Service maintains four different types of Periodicals mailings for billing determinants: Inside County vs. Outside County; Classroom; Science; and Agriculture and Nonprofit.

The Postal Service uses billing determinants to ensure that price adjustments do not exceed the price cap for each market dominant class of mail and to employ economic forecasting to produce price indices. Furthermore, the Postal Service uses billing determinants in the ACR as a part of the process to develop avoided cost estimates, which the Postal Service uses to set workshare discounts. The PAEA requires the OIG to regularly audit data collection systems and procedures the Postal Service uses to collect information and prepare the ACR.

The ACR is due within 90 days of the end of each fiscal year; and analyzes costs, revenue, pricing, and quality of service for all products. Billing determinants are presented in the ACR as a part of the process to develop avoided cost estimates, which the Postal Service uses to set workshare discounts

Billing determinants are filed in support of the ACR. Given the manual preparation and complexity of the spreadsheets, there is a risk of data entry errors. These errors increase the risk of incorrect annual price adjustments. Billing determinant calculation errors could cause proposed prices to exceed price caps and cause the Postal Service to violate the PAEA. Conversely, inaccurate billing determinants could prevent the Postal Service from increasing prices as much as the law permits.

Objective, Scope, and Methodology

Our objective was to assess the accuracy and completeness of data used to prepare FY 2013 and FY 2014 Periodicals billing determinants. To accomplish our objective we:

- Reviewed and evaluated FY 2013 and FY 2014 Periodicals billing determinants to identify errors and ensure accuracy and completeness.
- Identified and reviewed inputs to billing determinants, including the shape indicia report and the special weight report and determine adequacy of inputs.
- Interviewed Postal Service Pricing department employees to determine the process they used to compile Periodicals billing determinants.

¹¹ The Postal Service uses information collected from this system to develop proposals for new Postal Service rates, assist in budget preparation, conduct management studies, and support management decisions concerning mail flow and service performance in transportation and operations.

¹² Price List that includes a 44-page publication that contains domestic and international prices and is used as part of the billing determinant preparation process.

- Reviewed and evaluated documentation used to compile Periodicals billing determinants.
- Interviewed PRC staff members who use Periodicals billing determinants for their perspective on billing determinants and the existence of any inadequacies.
- Recalculated volume and revenue to identify errors and ensure completeness.
- Evaluated other data sources to determine whether the Postal Service could use them to compile Periodicals billing determinants.
- Analyzed price adjustment calculations to determine whether identified errors impact percentage change in Periodicals prices.

The scope of this project included a review of the data and processes used to calculate billing determinants information, including domestic market dominant Periodicals Mail.

We conducted this performance audit from April through September 2015, 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 findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective. We discussed our observations and conclusions with management on August 18, 2015, and included their comments where appropriate.

We did not assess the reliability of any computer-generated data for the purposes of this report.

Prior Audit Coverage

We identified one prior audit report related to the objective of this audit. On June 11, 2015, the OIG issued *Market Dominant Billing Determinants: First-Class Mail* (Report Number CP-AR-15-003). Management agreed there are opportunities to strengthen the billing determinants process; however, while management understands the absolute value method used to calculate the \$156.8 million of other impact, they believe the net value of \$37.9 million is a more accurate depiction of the results.

Appendix B: Management's Comments

CYNTHIA SANCHEZ-HERNANDEZ
VICE PRESIDENT PRICING



September 3, 2015

Lori Lau Dillard
Director, Audit Operations

SUBJECT: Market Dominant Billing Determinants: Periodicals (Report Number CP-AR-15-DRAFT)

Management agrees that there are opportunities to strengthen the billing determinants process and appreciates the thorough review by the USPS Office of Inspector General (OIG). Although management understands the "absolute value" method used by the OIG to calculate the value of the potential differences in the billing determinants revenue of \$7.6 million, management believes that the net value of \$2.2 million is a more accurate depiction of the revenue impact from the anomalies identified by the OIG (out of \$3.2B in total revenue). Management would also like to point out that we completed the documentation of our Periodicals processes for billing determinants while this audit was under way and continue to refine our quality review process. These activities are ongoing.

Recommendation 1:

File corrected Periodicals billing determinants for fiscal years 2013 and 2014 with the Postal Regulatory Commission no later than December 2015.

Management Response:

Management disagrees with the need to file corrected versions of the fiscal year 2013 and 2014 Periodicals billing determinants. We view the level of change as diminimus and therefore not necessary. On the 2013 Billing Determinants, the net amount of the changes is \$2.2 million which represents just over one tenth of one percent of the revenue in the fiscal year. The 2014 billing determinants suggested changes are even smaller, a net of \$25 thousand dollars on revenues of \$1.6 billion.

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Recommendation 2:

Ensure the source data is labeled correctly and labeling errors are not repeated while preparing billing determinants.

Management Response:

Disagree: This recommendation does not fall under the purview of the Pricing function. However, Pricing notified the providers of the source data with the labeling errors identified in this report and the appropriate corrections have been made. Pricing will continue to work with data providers as issues are identified.

Recommendation 3:

Disclose the methodology used to calculate editorial discounts and the reason for the different calculation method.

Management Response:

Agree. Pricing will provide a short footnote in future billing determinants that explain how the discount is accounted for in the report.

Target Implementation Date:

Q3 FY 2015 billing determinants

Responsible Management Official:

Manager, Pricing

Recommendation 4:

Complete ongoing internal efforts to ensure that all Periodicals billing determinants are produced using documented and repeatable processes that include an internal review process no later than December 2015.

Management Response:

Management concurs with this finding. In fact, management had already started down this path prior to the start of the audit and provided the OIG with the documented Periodicals billing determinants preparation documentation during the completion of the audit process. Management also initiated a high level review of billing determinants and exigent surcharge reporting with the Quarter 4 fiscal year 2014 reporting cycle. This review process has been enhanced with

additional layers of review with each successive reporting cycle. The review process will be part of the documented process when completed.

Target Implementation Date:

Management will document a repeatable process that includes a quality review process for Periodicals billing determinants preparation by Fiscal Year 2016 Quarter 2.

Responsible Management Official:

Manager, Pricing



Cynthia Sanchez-Hernandez

cc: Manager, Corporate Audit Response Management



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