

February 14, 2003

STEPHEN M. KEARNEY
VICE PRESIDENT, PRICING AND CLASSIFICATION

SUBJECT: Audit Report – Review of Nonprofit Authorizations
(Report Number AC-AR-03-003)

This report presents the results of our self-initiated audit of authorizations to mail at nonprofit rates (Project Number 02YG011AC001).

Background

Authorization to mail at Nonprofit Standard Mail rates is a privilege reserved by law to authorized organizations. The Domestic Mail Manual, paragraph E670.7.3, states that if an organization submits proof that it has been granted tax-exempt status under Title 26, United States Code, Sections 501(c)(3), 501(c)(5), 501(c)(8) or 501(c)(19), it is qualified for nonprofit mailing rates. An exemption from the payment of federal income tax is not required to qualify for Nonprofit Standard Mail rates, but is considered as evidence of qualification for nonprofit rates. For organizations that qualify and obtain authorization, a reduced Standard Mail (A)¹ bulk rate is available. Authorization to mail at nonprofit rates can be revoked for cause when it is determined an organization is no longer qualified. A revenue deficiency may be assessed in the amount of unpaid postage against any organization that mailed ineligible matter at the Nonprofit Standard Mail rates.

Objective, Scope, and Methodology

Our objective was to determine whether the Postal Service had reviewed the eligibility to mail at nonprofit rates for organizations whose tax-exempt status had been revoked by the Internal Revenue Service.

We reviewed Internal Revenue Service Bulletins for 2000, 2001, and 2002 through September 30, 2002. We compared those organizations whose tax-exempt status had been revoked to organizations listed in the Postal Service's nonprofit authorization database. We contacted the Nonprofit Service Center to determine whether reviews

¹ Standard Mail (A) is a class of mail matter that weighs less than 16 ounces and is not required to be mailed as First-Class Mail.

had been conducted on the continued eligibility for nonprofit authorizations based on the loss of tax-exempt status. We searched the Permit System for those organizations listed as active in the authorization database. For an organization authorized to mail at nonprofit rates at a Postal Service facility that did not have access to the Permit System, we contacted the facility to determine if the organization was mailing at nonprofit rates. For those organizations with permits to mail at nonprofit rates, we determined the amount of nonprofit revenue generated since the organization's tax-exempt status was revoked and what the regular Standard Mail (A) rate would have been.

This audit was conducted from September 2002 through February 2003, in accordance with generally accepted government auditing standards and included such tests of internal controls, as were considered necessary under the circumstances. We discussed our conclusions and observations with appropriate management officials and included their comments, where appropriate.

Prior Audit Coverage

On September 30, 2002, the Office of Inspector General (OIG) issued a management advisory report, Review of Nonprofit Standard Mail (Report Number AC-MA-02-002). This review disclosed that the authorization process and database management for nonprofit mailers needed improvement. We made six recommendations including the Postal Service conduct periodic reviews of nonprofit authorizations at the Nonprofit Service Center. Management disagreed with this recommendation, but indicated they were considering alternative methods of reviewing the continued eligibility of authorized nonprofit organizations.

Results

The Postal Service did not review the continued eligibility of nonprofit mailers whose tax-exempt status had been revoked by the Internal Revenue Service. An organization whose tax-exempt status had been revoked by the Internal Revenue Service was still mailing at nonprofit rates, even though it appeared the mailer may no longer be eligible to mail at nonprofit rates. This occurred because the Postal Service did not have procedures for reviewing revocations of the tax-exempt status of nonprofit mailers. As a result, the Postal Service did not collect approximately \$304,000 in revenues that it may have been entitled.

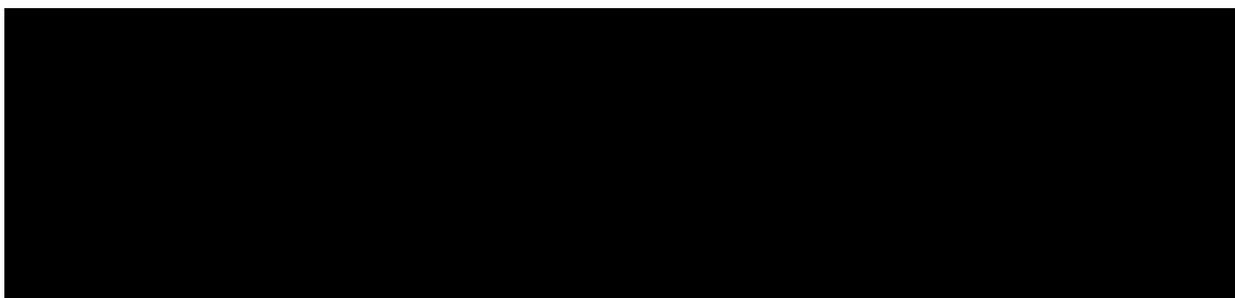
Controls to Review the Continued Eligibility of Nonprofit Mailers Need Improvement

The Postal Service had not conducted reviews to determine whether organizations whose tax-exempt status had been revoked by the Internal Revenue Service remained eligible for nonprofit rates. The Postal Service uses the tax-exempt status issued by the Internal Revenue Service as a criterion for most organizations to obtain nonprofit mailing status. Postal Service officials stated they review nonprofit authorizations when

they receive complaints from other organizations or members of the general public or when an applicant that may not qualify for the privilege alleges that another similar organization is already authorized nonprofit privileges. However, the Postal Service does not review revocations of tax-exempt status to determine if an organization still qualifies for nonprofit mailing rates.

From January 2000 to September 2002, the Internal Revenue Service revoked the tax-exempt status of 70 organizations. We identified three organizations that had active authorizations to mail at nonprofit rates although their tax-exempt status had been revoked. These organizations were: [REDACTED]

[REDACTED] See Appendix A for the addresses and mailing locations for these organizations.



The Domestic Mail Manual states that an organization may be authorized to mail at nonprofit rates if it is not organized for profit and none of its net income benefits any individual. Therefore, it appears [REDACTED] does not meet the requirements for nonprofit mailing rates. From April 15, 1999, through October 17, 2002, [REDACTED] had 339 mailings, totaling \$480,079, all at nonprofit rates. However, using Standard Mail (A) regular rates, the Postal Service should have received \$784,743 for these mailings, a difference of approximately \$304,000.

We previously recommended the Nonprofit Service Center conduct periodic reviews of nonprofit authorizations. We realize the risk of revenue loss must be weighed against the cost of establishing controls to prevent and detect such losses. However, conducting these periodic reviews on organizations that have lost their tax-exempt status from the Internal Revenue Service will target Postal Service efforts based on potential risk.

Recommendation

We recommend the vice president, Pricing and Classification:

1. Establish policies and procedures for reviewing the continued eligibility for nonprofit authorizations based on the loss of tax-exempt status.

Management's Comments

Management agreed with the recommendation. Personnel at the Nonprofit Service Center are now reviewing Internal Revenue Service Bulletins for organizations with nonprofit authorizations that have lost their tax-exempt status. Management's comments, in their entirety, are included Appendix B of this report.

Recommendation

We recommend the vice president, Pricing and Classification:

2. Review the nonprofit mailing authorizations for [REDACTED] to [REDACTED] to determine whether these organizations remain eligible to mail at nonprofit rates.

Management's Comments

Management agreed with the recommendation. A review of these organizations eligibility to mail at Nonprofit Standard Mail rates will be completed and actions taken to revoke said authorizations if found not to be in compliance with Postal Service standards.

Recommendation

We recommend the vice president, Pricing and Classification:

3. Determine whether to initiate action for assessment and collection of shortages in postage paid by [REDACTED] or to refer this issue to the Inspection Service for action as appropriate.

Management's Comments

Management agreed with the recommendation. Personnel at the Nonprofit Service Center are reviewing this organization's nonprofit authorization. If appropriate, action will be initiated to revoke this authorization and if any indications of fraud are detected, the case will be referred to the Postal Inspection Service.

Evaluation of Management's Comments

Management's comments are responsive to recommendations 1, 2, and 3. Management's actions taken or planned should correct the issues identified in the report.

The OIG considers recommendation 1 significant and, therefore, requires OIG concurrence before closure. Consequently, the OIG requests written confirmation when

corrective action(s) are completed. This recommendation should not be closed in the follow-up tracking system until the OIG provides written confirmation that the recommendation can be closed.

We appreciate the cooperation and courtesies provided by your staff during our review. If you have any questions or need additional information, please contact Larry Chisley at (813) 261-5200 or me at (703) 248-2300.

B. Wayne Goleski
Assistant Inspector General
for Core Operations

Attachment

cc: Anita J. Bizzotto
Sherry L. Freda
Edward S. Walker
Angelo Wider
Danny R. Neal
Susan M. Duchek

**APPENDIX. A
ORGANIZATIONS AUTHORIZED TO MAIL AT NONPROFIT RATES
BUT NO LONGER HAVE INTERNAL REVENUE SERVICE
TAX-EXEMPT STATUS**

Organization	Postal Service Facility	Nonprofit Authorization Number	Permit Number
[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]

APPENDIX. MANAGEMENT'S COMMENTS

STEPHEN M. KEARNEY
VICE PRESIDENT
PRICING AND CLASSIFICATION



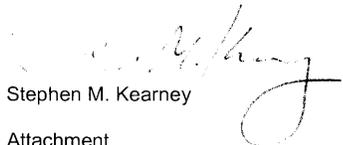
January 17, 2003

B. WAYNE GOLESKI
ASSISTANT INSPECTOR GENERAL FOR CORE OPERATIONS

SUBJECT: Draft Audit Report – Review of Nonprofit Authorizations
(Report Number AC-AR-03-Draft)

Attached is management's response to the findings and recommendations of the Office of the Inspector General in this matter.

If you have any questions or require further information, please contact Sherry Freda, manager, Mailing Standards at (703) 292-3651.


Stephen M. Kearney
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Response to OIG Report
Review of Nonprofit Authorizations
(Report Number AC-AR-03-Draft)

RECOMMENDATION #1

- Establish policies and procedures for reviewing the continued eligibility for nonprofit authorizations based on the loss of tax-exempt status.

RESPONSE

We agree with this recommendation. The recommended review procedure using information to be obtained from the Internal Revenue Service and reviewed regularly has been instituted by the Memphis Nonprofit Service Center which has already begun reviewing IRS Bulletins.

RECOMMENDATION #2

- Review the nonprofit authorizations for [REDACTED] to determine whether these organizations remain eligible to mail at nonprofit rates.

RESPONSE

We agree and will initiate review of the authorizations named immediately taking action to revoke said authorizations if found to be not in compliance with Postal Standards of evidence to be furnished necessary to demonstrate eligibility to mail at Nonprofit Standard mail rates.

RECOMMENDATION #3

- Determine whether to initiate action for assessment and collection of shortages in postage paid by [REDACTED] or to refer this issue to the Inspection Service for action as appropriate.

RESPONSE

We concur with the recommendation. The Memphis NSC is currently reviewing the authorization previously granted to the organization and, if appropriate, the action will be initiated to revoke the authorization. In addition, any indication of suspected fraud will be appropriately referred to the Postal Inspection Service once detected.