Office of Inspector General | United States Postal Service

Audit Report

Professional Services Contract Rates

Report Number 20-143-R20 | August 20, 2020

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Highlights

Objective

The U.S. Postal Service has used the same independent public accounting firm (supplier) since 1972 for professional services, which included providing an opinion on the Postal Service's financial statements. The supplier was last non-competitively awarded a time and materials contract for professional services on March 1, 2014. This type of contract is most commonly used when the quantity of labor required for the work to be accomplished cannot be adequately estimated in advance. The contract consisted of a two-year base period, with five one-year renewable options.

In addition to professional services, the Postal Service required the supplier to develop a formal Continuous Process Improvement Plan (improvement plan). The improvement plan deliverables consisted of a one-time draft improvement plan, a semiannual continuous improvement performance review report (review report), and an annual improvement plan update.

The draft improvement plan required the supplier to identify the methodology, goals, objectives, significant cost drivers, and planned actions to improve efficiency and reduce costs. The review reports required the supplier to identify specific actions taken and progress achieved during the reporting period to meet improvement plan goals. The annual improvement plan update required the supplier to quantify targeted hour reductions, efficiencies gained, and resulting decreases in total fees.

On November 10, 2014, we issued a report that found the supplier's labor rates exceeded General Services Administration Schedule rates (government-wide contracts that provide products and services at fair and reasonable prices). Subsequent to our review, the supplier submitted an unsolicited proposal to the Postal Service. The proposal reduced hours over five years and offered a reduction in the five-year average blended labor rate in exchange for the Postal Service exercising all five one-year options simultaneously.

On November 20, 2015, the Postal Service modified the contract to incorporate a lower blended labor rate and exercised all five one-year options concurrently. This modification extended the period of performance to February 28, 2021 and incorporated one additional two-year renewable option that would extend the period of performance to February 28, 2023, if exercised.

Our objective was to determine if potential cost savings exist for the supplier's professional services contract. We began our fieldwork before the President of the U.S. issued the national emergency declaration concerning the novel coronavirus disease (COVID-19) outbreak on March 13, 2020. The results of this audit do not reflect any supply management or financial management process changes that may have occurred as a result of the pandemic.

Findings

The Postal Service has opportunities to obtain additional cost savings for the professional services contract. Renegotiating the contract achieved a lower blended labor rate; however, the rate is still, on average, [redacted] higher than the General Services Administration Schedule industry standard.

The Postal Service contracted for higher labor rates because of concerns over lost efficiencies if the work was awarded to a new supplier. Had the Postal Service followed GSA Schedule labor rate standards, it could have saved an estimated $1.9 million annually. Furthermore, if the Postal Service remains in the current contract and exercises the optional two-year extension, it would pay an additional annual cost of $3,630,165.

The Postal Service contracted for these services using a time and materials contract (a contract that obligates the supplier to deliver the product or service specified by the contract for a fixed hourly rate) rather than a firm-fixed price contract. Postal Service policy states that a time and materials contract should only be used when it is not possible to accurately estimate the extent or duration of the work or anticipate project cost with a reasonable degree of certainty. We benchmarked other government agencies and quasi-government agencies similar to the Postal Service and found that 12 of 14 agencies used firm-fixed priced contracts for similar services.

The Postal Service considered using a firm-fixed price contract but believed it had more flexibility and limited liability for termination and settlement costs with a time

and materials contract. As a result, the Postal Service assumed greater risk by using a time and materials contract for professional services.

Finally, the supplier did not comply with the contract to submit improvement plan deliverables. Specifically, the supplier did not provide the draft improvement plan and semiannual review reports. Furthermore, the annual improvement plan updates did not quantify targeted hour reductions, efficiencies gained, and resulting decreases in total fees. The supplier claimed additional efficiencies led to cost savings but did not include the supporting documentation required in the improvement plan. Because the Postal Service did not enforce these contract requirements, it missed opportunities for cost savings.

Recommendations

We recommended management:

- Compete the professional services contract at the end of the current performance period and negotiate labor rates considering the General Services Administration Schedule.
- Explore the benefits of awarding a firm-fixed priced professional services contract and implement, as warranted.
- Obtain semiannual review reports, annual improvement plans, and supporting documentation from the supplier, as required in the contract, and review the improvement plan to validate specific actions are taken to increase efficiencies and reduce costs.

Transmittal Letter

OFFICE OF INSPECTOR GENERAL
UNITED STATES POSTAL SERVICE

August 20, 2020

MEMORANDUM FOR: MARK A. GUILFOIL
VICE PRESIDENT, SUPPLY MANAGEMENT

E-Signed by Jason Yovich
ERIPX authenticity with eSign Deskto

FROM: Jason Yovich Deputy Assistant Inspector General
for Supply Management & Human Resources

SUBJECT: Audit Report – Professional Services Contract Rates
(Report Number 20-143-R20)

This report presents the results of our audit of Professional Services Contract Rates.

We appreciate the cooperation and courtesies provided by your staff. If you have any questions or need additional information, please contact Shirian Holland, Director, Supply Management and Facilities, or me at 703-248-2100.

Attachment

cc: Postmaster General
Corporate Audit Response Management

Results

Introduction/Objective

This report presents the results of our self-initiated audit of Professional Services Contract Rates (Project Number 20-143-R20). Our objective was to determine if potential cost savings exists for the supplier's professional services contract.

We began our fieldwork before the President of the U.S. issued the national emergency declaration concerning the novel coronavirus disease (COVID-19) outbreak on March 13, 2020. The results of this audit do not reflect any supply management or financial management process changes that may have occurred as a result of the pandemic.

"Our objective was to determine if potential cost savings exists for the supplier's professional services contract."

Background

The U.S. Postal Service has used the same independent public accounting firm (supplier) since 1972 for professional services. The supplier was last non-competitively awarded a time and materials contract[1] for professional services on March 1, 2014. Specifically, the supplier was contracted to perform professional services that include an annual audit of the Postal Service's annual financial statements for each of the fiscal years and report on the Postal Service's internal controls over financial reporting under Sarbanes-Oxley (SOX)[2] for each of the fiscal years.

The contract consists of a two-year base period with five one-year renewable options and a negotiated contract ceiling amount of $48.6 million. The U.S. Postal Service Board of Governors (Governors) approved the contract and it is managed by the Postal Service. The Postal Service and U.S. Postal Service Office of Inspector General (OIG) are responsible for administrative functions and are appointed as contracting officer representatives (COR).[3]

In addition to professional services, in March 2014 the Postal Service required the supplier to develop a formal Continuous Process Improvement Plan (improvement plan) with the primary goal of increasing efficiencies, reducing the hours incurred, and decreasing total fees over the extended term of the contract. The improvement plan also requires the supplier to provide a continuous improvement performance review report (review report) every six months over the term of the contract.

We issued a report in November 2014 that compared Postal Service's labor rates for financial, accounting and consulting services with federal government rates (General Services Administration (GSA) Schedule[4] rates) for comparable services.[5] COs were aware of the GSA Schedule rates but considered them incomparable because the supplier is required to provide an opinion on the Postal Service's internal controls over financial reporting. At that time, had the Postal Service awarded the contract using the supplier's GSA Schedule rates, it could have saved about $2.8 million annually.

We recommended management compete the independent accounting services contract before exercising the option to renew the contract. However, management decided not to compete the contract to avoid interrupting service while implementing operational changes, despite receiving indications that other suppliers could potentially perform the same services using labor rates at or below the GSA Schedule rates. Management stated that switching suppliers could cost as much as 50 percent more during the first year of transition.

Subsequent to that audit, the supplier submitted an unsolicited proposal to the Postal Service. The proposal reduced hours over five years and offered

1 A contract in which the buyer and supplier agree on a fixed hourly rate for each labor category required and quantity of labor required for the work to be accomplished cannot be adequately estimated in advance.
2 The SOX Act of 2002 is a law the U.S. Congress passed to help protect investors from fraudulent financial reporting by corporations. It mandated strict reforms to existing securities regulations and imposed tough new penalties on lawbreakers.
3 Appointed by the contracting officer (CO) and responsible for day-to-day administration of the contract, CORs serve as the Postal Service's point of contact with the supplier on all routine matters.
4 Long-term government-wide contracts with commercial companies that provide access to millions of commercial products and services at fair and reasonable prices to the government.
5 *Professional Services Contract Rates* (Report Number SM-AR-15-001, dated November 10, 2014).

a reduction in the five-year average blended labor rate[6] in exchange for the Postal Service simultaneously exercising all five one-year options (see Table 1).

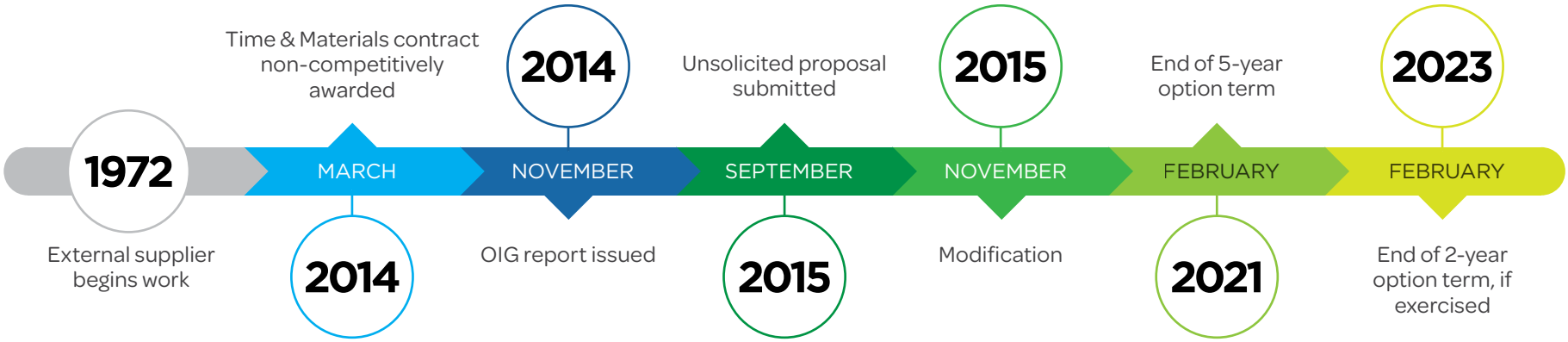
Table 1. Unsolicited Proposal

	Original Contract	Modification[7]	Difference	Percentage
Hours	[redacted]	[redacted]	[redacted]	[redacted]
Blended Rate	[redacted]	[redacted]	[redacted]	[redacted]
Fee	$61,287,612	$48,610,211	($12,677,401)	22%

Source: OIG analysis of the unsolicited proposal for the period of performance 2016 to 2020.

Postal Service management entered rate negotiations with the supplier and outsourced SOX-related work to another supplier while maintaining the responsibility of providing an opinion on the Postal Service's financial statements and internal controls over financial reporting. This increased the supplier's reliance on the other supplier's work and reduced their level of effort for the contract. The Governors estimated these actions should save the Postal Service over $3.7 million annually. On November 20, 2015, the Postal Service modified the contract to incorporate a lower blended rate [redacted] and exercised all five one-year renewable options simultaneously for a new period of performance ending February 28, 2021. The modification also incorporated one two-year renewable option to extend the period of performance through February 28, 2023, if exercised. See Figure 1 for a timeline of the contract.

Figure 1. Contract Timeline



Source: OIG analysis.

The negotiated contract ceiling amount for fiscal year (FY) 2016 through FY 2020 option periods was valued at $48.6 million. However, that ceiling was increased by $21.7 million (45 percent) to $70.3 million which includes additional audit requirements related to cybersecurity and new Financial Accounting Standards Board standards for revenue recognition and lease accounting. As of February 2020, the Postal Service spent $59 million over the life of the contract.

6 An average blended rate is the weighted average of all labor categories rates.
7 Modification to incorporate negotiated unsolicited proposal.

Finding #1: Labor Rates

The Postal Service has opportunities to obtain additional cost savings for the professional services contract. The Postal Service simultaneously exercised five one-year contract options to extend the non-competitive time and materials contract although it was awarded with higher labor rates than the GSA Schedule industry standard. Renegotiating the labor rates over the contract extension achieved a lower blended labor rate; however, the rate is still on average [redacted] higher than the GSA Schedule industry standard (see Figure 2).

Figure 2. Rates Comparison

[redacted]

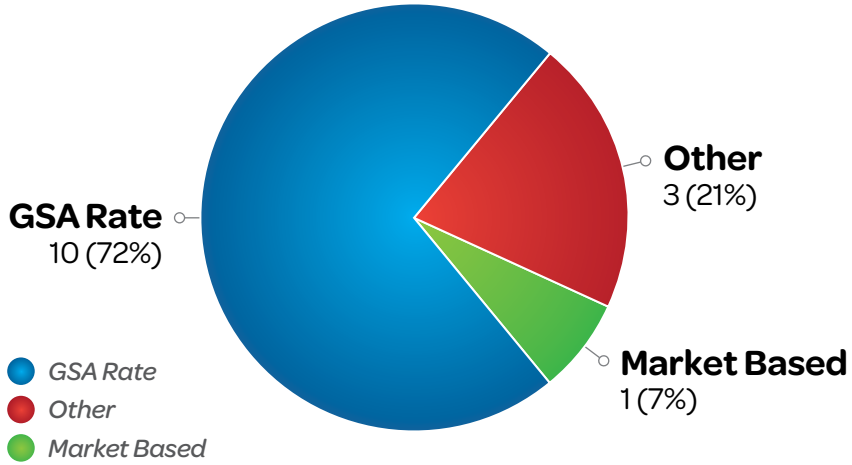
Source: OIG analysis.

Postal Service policy requires some form of price analysis for every purchase.[8] Price analysis is the process of examining and evaluating a proposed price against reasonable price benchmarks, without evaluating the separate cost elements and profit that make up the price. Furthermore, the policy states a cost is reasonable if it is a type of cost and amount that does not exceed what a prudent person would incur conducting competitive business.[9]

We benchmarked 18 government agencies[10] and three quasi-government agencies[11] that contracted for integrated audit services similar to those of the Postal Service. We found 12 of 18 government agencies (67 percent) and two of three quasi-government agencies (67 percent) outsourced their integrated financial statement audits to other suppliers. The remaining seven agencies performed their audits internally.

We found ten of the 14 (72 percent) agencies that outsourced their integrated audit used the GSA Schedule rates for price negotiation (see Figure 3).

Figure 3. Benchmarked Agencies Labor Rates[12]



Source: OIG analysis.

8 Supplying Principles & Practices (SP&P) 2-34 Conduct Price/Cost Analysis.
9 SP&P 2-34.8 Reasonableness.
10 We benchmarked with the following government agencies: Nuclear Regulatory Commission, Department of Homeland Security, Department of Energy, Department of Interior, Department of Justice, Department of Labor, Department of Transportation, Department of Education, Federal Election Commission, Government Publishing Office, National Archives, National Aeronautics and Space Administration, National Geospatial Intelligence Agency, Social Security Administration, Defense Intelligence Agency, Peace Corps, Federal Reserve System, and Department of Housing and Urban Development.
11 We benchmarked with the following quasi-government agencies: Pension Benefit Guaranty Corporation, Railroad Retirement Board, and Tennessee Valley Authority.
12 Other includes contracts without labor rates or we could not determine if the agency used GSA rates or market rates.

Upon review of the unsolicited proposal documentation, we determined the supplier's position was that the GSA Schedule rates did not apply to the integrated financial statement audit requirement and that the Postal Service was similar to a commercial customer and not government. The Postal Service contracted for higher labor rates above the GSA Schedule rates because they accepted the supplier's position that the GSA Schedule rates did not apply.

We compared GSA Schedule labor categories and required qualifications to the supplier's labor categories and qualifications. We determined the qualifications to be very similar. For example, the GSA Schedule senior manager description includes eight to 10 years experience planning, supervising, reviewing audit and financial engagements, with generally at least two years of experience as managers of engagements for the private sector, the federal government or in another specialized area. The supplier's corresponding labor category description includes eight to 10 years of experience supervising and managing audits. However, the supplier's average labor rate is [redacted] than the GSA Schedule labor rate for a senior manager. Accordingly, we found no justification to explain the supplier's significantly higher rate for this labor category.

> *"We compared GSA Schedule labor categories and required qualifications to the supplier's labor categories and qualifications. We determined the qualifications to be very similar."*

Additionally, the Postal Service stated it did not compete the contract because of concerns over lost efficiencies in accomplishing the work if the contract was competed and awarded to another supplier. However, by repeatedly using the same supplier, the Postal Service may miss opportunities to identify new methods of accomplishing the work, make quality improvements, or gain efficiencies.

We estimate the Postal Service overpaid the supplier by $3,902,824 for 2018 and 2019 by not negotiating contract labor rates commensurate to the GSA Schedule industry standard. Furthermore, if the Postal Service remains in the current contract and exercises the additional two-year option to extend the contract, we estimate the additional cost will be $7,260,329.

Recommendation #1

We recommend the **Vice President, Supply Management**, compete the contract at the end of the current performance period and negotiate labor rates considering the General Services Administration Schedule.

Finding #2: Contract Type

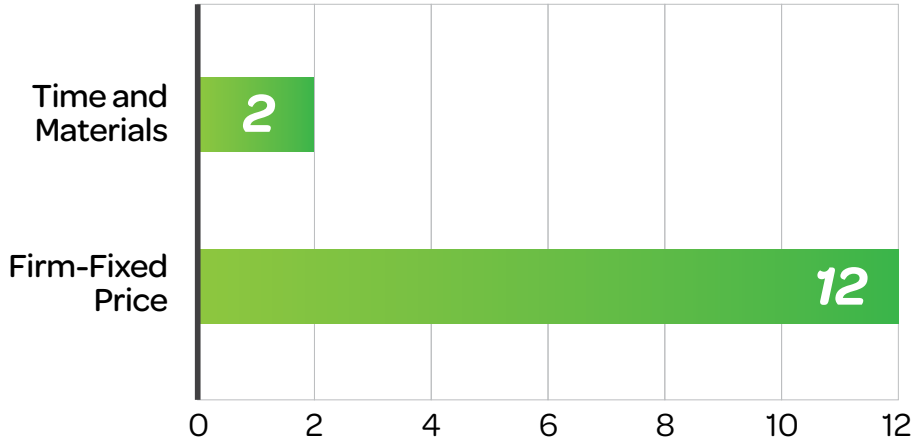
The Postal Service contracted for professional services using a time and materials contract rather than a firm-fixed price contract. Furthermore, the Postal Service awarded the time and materials contract although it should only be used when project durations or costs cannot be estimated accurately, despite the supplier performing the services since 1972.

A time and materials contract is also appropriate when an organization can provide adequate monitoring to ensure that inefficient work methods are not used. Overall, time and materials contracts do not encourage effective cost control or labor efficiency by the supplier. Firm-fixed price contracts obligate the supplier to deliver the product or service specified by the contract for a fixed price and places full responsibility on the supplier for all costs. This contract type also maximizes the supplier's incentive to control costs and perform effectively. Additionally, a firm-fixed price contract is the least burdensome type of contract for the Postal Service to administer.[13]

Based on our benchmarking, we determined 12 of 14 (86 percent) government agencies that contracted for similar professional services used firm-fixed priced contracts (see Figure 4). We also determined the Postal Service's professional services supplier has a firm-fixed priced contract with one of the benchmarked government agencies for similar services.

13 SP&Ps, Practices, 2-18.3 Firm-Fixed Price Contract.

Figure 4. Benchmarked Contract Types



Source: OIG analysis.

The Postal Service considered using a firm-fixed price contract but believed it had more flexibility and limited liability for termination and settlement costs with a time and materials contract. Additionally, the supplier did not feel comfortable transitioning to a firm-fixed price contract and felt it would be inconsistent with their standard commercial engagement arrangements. Nevertheless, in November 2015, the Postal Service exercised all five one-year options simultaneously as part of the negotiation, effectively obligating them into a long-term contract, which negate the benefits they believed a time and materials contract would have provided. As a result, the Postal Service also assumed greater risk utilizing a time and materials contract for these professional services.

Recommendation #2

We recommend the **Vice President, Supply Management**, explore the benefits of awarding a firm-fixed priced professional services contract and implement, as warranted.

Finding #3: Continuous Process Improvement Plan

The supplier did not comply with the contract to submit improvement plan deliverables. Specifically, the supplier did not provide the draft improvement plan and semiannual review reports. Additionally, the annual improvement plan updates did not quantify targeted hour reductions, efficiencies gained, and resulting decreases in total fees. The supplier claimed additional efficiencies led to cost savings but did not include the supporting documentation required in the improvement plan.

The Postal Service required the supplier to develop a formal Continuous Process Improvement Plan (improvement plan). The improvement plan deliverables consisted of a one-time draft improvement plan, a semiannual continuous improvement performance review report (review report), and an annual improvement plan update. The draft improvement plan required the supplier to identify the methodology, goals, objectives, significant cost drivers, and planned actions to improve efficiency and reduce costs. The review reports required the supplier to identify specific actions taken and progress achieved during the reporting period to meet improvement plan goals. The annual improvement plan update required the supplier to quantify targeted hour reductions, efficiencies gained, and resulting decreases in total fees. The supporting documentation should include quantification and rationale to validate the claimed results. The improvement plan update was part of the annual presentation of the audit plan to the CORs, Chief Financial Officer, and Postal Service Audit and Finance Committee (see Table 2).

Table 2. Improvement Plan Deliverables

Deliverable	Timing	Recipient	Submitted
Draft Improvement Plan	90 Days from Contract Award	CO	No
Review Report	Semiannually	CO	No
Improvement Plan	Annually	CORs Chief Financial Officer Audit and Finance Committee	Yes[14]

Source: OIG analysis.

The supplier claimed a 21,750 hour reduction by leveraging the work of the other supplier performing the SOX work. In the unsolicited proposal, the supplier stated, as the work of the other supplier performing the SOX work matured, the supplier's reliance increased over time. This reliance strategy depends on the learning curve of the other supplier's SOX group and should be considered a natural progression[15] and not part of the improvement plan that leads to a reduction in cost based on improved supplier efficiencies. Additionally, the supplier claimed a reduction in hours due to quarterly review procedures, audit procedures, staffing mix, and the use of digital tools. However, they did not provide adequate supporting documentation to quantify how each of these contributed to cost savings, as required in the improvement plan. As a result, the contract ceiling has increased to $70 million (45 percent) and as of February 2020 contract spend was $59 million.

"The contract ceiling has increased to $70 million (45 percent) and as of February 2020 contract spend was $59 million."

The CO did not enforce contract requirements for the supplier to submit improvement plan deliverables. Specifically, the CO did not ensure the supplier submitted a draft improvement plan or review reports and supporting documentation to quantify targeted hour reductions and efficiencies gained to support the specific actions for the improvement plan goals. Additionally, the annual status update of the improvement plan was not included within the annual presentations to the CORs. We were unable to determine if the annual status update of the improvement plan was presented to the Chief Financial Officer and Postal Service Audit and Finance Committee, as required. Moreover, the CO did not provide the plans to either the OIG or Postal Service CORs.[16] The OIG COR did not receive the improvement plan from the supplier or CO and the Postal Service COR also stated they had not been involved with the contract since 2013. Furthermore, the CO did not know who was fulfilling the Postal Service's COR role and was unable to provide us the name of the Postal Service representative responsible for reviewing improvement plans.

As a result of the Postal Service not reviewing and validating the supplier's improvement plan goals, the Postal Service missed opportunities to achieve cost savings through increased efficiencies, reduce hours, and decrease total fees.

Recommendation #3

We recommend the **Vice President, Supply Management**, obtain semiannual review reports, annual improvement plans, and supporting documentation from the supplier, as required in the contract, and review the improvement plan to validate specific actions are taken to increase efficiencies and reduce costs.

14 Improvement plan provided did not contain sufficient information which would allow the Postal Service to validate claimed efficiencies and cost reductions.
15 Natural progression is the supplier's reliance strategy that the SOX work performed by the other supplier will improve over the course of time.
16 The OIG COR reviews the supplier's audit professional fees and travel expenses and the Postal Service COR is responsible for providing the appropriate level of contract management and ensure financial interests are fully protected.

Management's Comments

Management agreed with recommendations 2 and 3; however, they disagreed with recommendation 1 and the monetary impact.

Regarding recommendation 1, management stated the OIG's reliance on GSA Schedule rates does not recognize the specific expertise of the supplier and focuses solely on labor rates versus the efficiencies demonstrated due to the supplier's understanding of Postal Service accounts. The Postal Service applies a best value approach in all procurements and considers the price analysis techniques used in negotiating the contract's accounting service labor rates to have resulted in a fair and reasonable price.

Under the applicable regulations of 39 CFR §3.4(n), the Governors have authority over the selection of the outside auditor, including any decision about whether to maintain, change, or provide for competition, and the process for selecting the auditor.

Pursuant to its Charter, BOG Resolution 19-22, the Audit and Finance Committee (AFC) makes recommendations to the Governors regarding the selection, retention, and termination of the outside auditor's contract. The Governors, through the AFC, recently conveyed their decision to maintain the existing relationship with the supplier without further competition; however, labor rates are still to be negotiated for the upcoming option period. Supply Management will take the lead in negotiating rates, terms, and conditions for the option. In negotiating pricing, Supply Management will consider GSA rates as a potential benchmark.

Regarding recommendation 2, management stated they will review the benefits and administration of a firm-fixed price contracting structure and implement it if warranted. Should a change from the existing contract structure be determined, Supply Management will convey this recommendation to the AFC. Any change will require approval of the AFC and the Governors. Management plans to implement this action by February 2021.

Regarding recommendation 3, management stated they will obtain semiannual review reports, annual improvement plans, and supporting documentation from the supplier, as required in the contract, and review the improvement plan to validate that specific actions are taken to increase efficiencies and reduce costs. Management plans to implement this action by January 2021.

Regarding monetary impact, management disagrees with the OIG's assertion that the Postal Service had opportunities to obtain additional cost savings by renegotiating the contract based solely on the GSA labor rate schedules. As discussed, based on SOX requirements, the size and scope of the Postal Service, the learning curve and transitioning aspect of an incoming auditing firm, and the skillset and experience of current auditors, they believe they contracted at fair and reasonable pricing and achieved best value.

See Appendix B for management's comments in their entirety.

Evaluation of Management's Comments

The OIG considers management's comments responsive to recommendations 2 and 3 in the report and corrective actions stated should improve the issues identified in the report.

Regarding recommendation 1, management's comments are responsive. Our analysis used the GSA rates as a benchmark. However, by continuing to use the same supplier, the Postal Service may miss opportunities to identify new methods of accomplishing the work, make quality improvements, or gain efficiencies as part of our conclusion to obtain more favorable rates.

The OIG acknowledges the decision that the Board of Governors exercised their authority under the applicable regulations of 39 CFR §3.4(n) to maintain the relationship with existing supplier without further competition. The OIG would need to obtain supporting documentation of the decision to sole source this contract in order to close this recommendation.

Regarding the calculation of the monetary impact, management stated they disagree with the OIG's assertion that the Postal Service had opportunities to obtain additional cost savings by renegotiating the contract based solely on the GSA labor rate schedules. We benchmarked government agencies and found 72 percent used GSA schedule rates for price negotiations. Our analysis compared the labor qualifications of the contract SOW, the supplier, and the GSA schedule and found they were similar. We calculated the monetary impact by comparing

the supplier's fees to the estimated GSA Schedule fees. Moreover, regarding the learning curve and transitioning aspect of an incoming auditing firm and the skillset and experience of the current auditors being a concern, in subsequent conversations management indicated that very few of the largest 500 companies have switched auditors in the last eight years. We note that the Postal Service has used the same independent auditor since 1972.

All recommendations require OIG concurrence before closure. Consequently, the OIG requests written confirmation when corrective actions are completed. All recommendations should not be closed in the Postal Service's follow-up tracking system until the OIG provides written confirmation that the recommendations can be closed.

Appendices

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Appendix A: Additional Information

Scope and Methodology

The specific scope of this project is identifying cost savings for contract # 2BFAAS-13-B-0012. Our objective was to determine if potential cost savings exists for the supplier's professional services contract.

To accomplish our objective, we:

- Interviewed the CO and other personnel responsible for contract administration to gain an understanding of the decisions made regarding contract labor rates and why the Postal Service has not competed the contract.
- Obtained and reviewed supplier contract labor rates, labor category qualifications and descriptions and compared them to GSA Schedule rates and qualifications.
- Obtained and reviewed responses from other government and quasi-government agencies regarding integrated audits to analyze labor rates, contract type, and accounting firms used.
- Benchmarked GSA Schedule rates to the supplier's current labor rates to determine the opportunity of cost savings.
- Analyzed the labor/blended labor rates to determine if the Postal Service realized the cost savings as stated in the Board of Governors' response dated September 29, 2015.
- Calculated the potential cost savings by identifying the potential average blended labor rate and applying it to budgeted contract hours.

We conducted this performance audit from January through August 2020 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 June 26, 2020 and included their comments where appropriate.

We based this report on the analysis of a single contract and did not obtain any computer-generated data to meet our objective. As a result, assessing the reliability of computer-generated data was not required.

Prior Audit Coverage

Report Title	Objective	Report Number	Final Report Date	Monetary Impact (in milliions)
Professional Services Contract Rates	Compare the Postal Service's labor rates for financial, accounting, and professional consulting services with federal government rates for comparable services.	SM-AR-15-001	11/10/2014	$5.6

Appendix B: Management's Comments

MARK A. GUILFOIL
VICE PRESIDENT, SUPPLY MANAGEMENT

UNITED STATES POSTAL SERVICE

August 7, 2020

LAZERICK POLAND
DIRECTOR, AUDIT OPERATIONS

SUBJECT: Professional Services Contract Rates
(Project Number 20-143- DRAFT)

Thank you for providing the United States Postal Service (Postal Service) with the opportunity to review and comment on the subject draft audit report, "Professional Services Contract Rates", dated June 30, 2020. Management disagrees with the findings and Recommendation 1 and the monetary impact. Management agrees with both Recommendation 2 and 3.

Central to this audit, as presented by management during the audit process and again at the exit conference, is the applicable regulation of 39 C.F.R. 3.4(n) which provides that the Postal Service Governors have authority over the "selection of an independent, certified public accounting firm to certify the accuracy of Postal Service financial statements." This authority includes the decision as to whether to maintain the current contractual relationship with the existing supplier, and if applicable, the process to provide for any replacement. The subject report, while noting the Governors as a component of prior actions, does not discuss this reserved authority which directly bears on managements disagreement with Recommendation 1.

Finding 1 – Labor Rates

The report asserts that had the Postal Service followed General Services Administration (GSA) schedule labor rate standards, we could have achieved greater contract savings. The Postal Service applies a best value approach in all procurements and considers the price analysis techniques used in negotiating the contract's accounting service labor rates to have resulted in a fair and reasonable price. The OIG's reliance on GSA Schedule rates does not recognize the specific expertise of the supplier, and focuses solely on labor rates versus the efficiencies demonstrated due to the supplier's understanding of Postal Service accounts.

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MARK A. GUILFOIL
VICE PRESIDENT, SUPPLY MANAGEMENT

UNITED STATES POSTAL SERVICE

August 7, 2020

LAZERICK POLAND
DIRECTOR, AUDIT OPERATIONS

SUBJECT: Professional Services Contract Rates
(Project Number 20-143- DRAFT)

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Finding 1 – Labor Rates

The report asserts that had the Postal Service followed General Services Administration (GSA) schedule labor rate standards, we could have achieved greater contract savings. The Postal Service applies a best value approach in all procurements and considers the price analysis techniques used in negotiating the contract's accounting service labor rates to have resulted in a fair and reasonable price. The OIG's reliance on GSA Schedule rates does not recognize the specific expertise of the supplier, and focuses solely on labor rates versus the efficiencies demonstrated due to the supplier's understanding of Postal Service accounts.

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The OIG noted they benchmarked 18 government agencies and three quasi-government agencies and found that 12 of 18 government agencies (67 percent) and two of three quasi-government agencies (67 percent) outsourced their integrated financial statement audits to other suppliers. The remaining seven agencies performed their audits internally.

The OIG in comparing rates did not identify which, if any, of the benchmarked government agencies under GSA contract are under the same Sarbanes-Oxley (SOX) compliance requirements as the Postal Service. This is a critical distinction in terms of assigned resources and the level of risk associated with performing the work by the supplier. In addition, as noted above, the OIG only compared the rates of similar labor categories and did not compare the level of effort of the Postal Service's audit engagement with the engagements of other agencies.

The complexity introduced because of SOX and regulatory agency oversight represents a greater level of complexity of a publicly traded commercial level audit versus a dissimilar and lower level of complexity and effort GSA government agency audit. SOX testing is an integral part of monitoring the effectiveness of financial controls and has added a significant layer of complexity and cost to Postal Service external audit services. Although the Postal Service is not a public company and does not have investors (shareholders), it is by statute deemed a "registrant" for purposes of certain SEC financial reporting and controls requirements. A registrant is required to include in its annual report, management's report on the company's internal controls over financial reporting. Public Company Accounting Oversight Board (PCAOB) auditing standards establish requirements and provide direction that apply when an auditor is engaged to audit both a company's financial statements, and management's assessment of the effectiveness of internal controls over financial reporting. The audit process involving SOX affects the cost of Postal Service professional external audit services and is an important distinction to direct GSA rate comparisons.

Finding 2 – Contract Type

The OIG notes that other agencies have contracted for audit services using firm fixed price contracts. While a firm fixed-price contract was previously considered, management determined to incorporate a hybrid approach which includes a both a fixed component and a time and material (T&M) component. This approach provides flexibility to the Postal Service and has resulted in reduced costs for the services. The T&M aspect has been necessary as estimating total audit needs have seen changes due to the implementation of additional accounting standards and SOX controls during performance.

The contracting officer put into place measures to mitigate the risks of a T&M contract. A ceiling price was placed on the contract for the yearly financial

statements audit and actively tracked the amount of supplier hours. Utilizing a T&M contract has allowed the Postal Service to capture cost savings as the supplier was able to begin relying on SOX IT reports, thus reducing the yearly audit hours.

Finding 3 – Continuous Process Improvement Plan

The supplier committed to reductions in base hours for 2016 and future periods which resulted in revised targets for all years. These reductions represented the supplier's commitment to continuous improvement and represented a multi-year Continuous Process Improvement Plan (CPI Plan) in accordance with the contract. We achieved the reduction in hours through leveraging the work of the SOX Compliance group. This SOX work had transitioned to external consultants with extensive experience, and streamlined the work in certain areas, providing for lower risk and/or stability.

As was communicated in both the team interview with the OIG and the pre-exit meeting, the supplier did fully comply with the improvement plan's primary goal of decreasing total fees in accordance with the contract, however did not always provide documentation required under the contract. Documentation was provided to the OIG in October 2019. This documentation confirmed compliance resulting in substantial financial benefit to the Postal Service from a total reduction in fees since 2015 of $13.8 million.

Monetary Impact

Management disagrees with the OIG's assertion that the Postal Service had opportunities to obtain additional cost savings by renegotiating the contract based solely on the GSA labor rate schedules. As discussed, based on SOX requirements, the size and scope of the Postal Service, the learning curve and transitioning aspect of an incoming auditing firm, and the skillset and experience of the current auditors, we contracted at fair and reasonable pricing and achieved best value.

OIG Recommendations:

We recommend the Vice President, Supply Management:

Recommendation 1: Compete the contract at the end of the current performance period and negotiate labor rates considering the General Services Administration Schedule.

Management Response/Action Plan: Management disagrees with this recommendation on the basis of the Governors reserved authority. Under the applicable regulations of 39 C.F.R. 3.4(n), the Governors have authority over the selection of the outside auditor. That authority includes any decision as to whether to maintain, change, or provide for competition, and the process to select the auditor.

Pursuant to its Charter, BOG Resolution 19-22, the Audit and Finance Committee (AFC) makes recommendations to the Governors regarding the selection, retention and termination of the outside auditor's contract. The Governors, through the AFC, recently conveyed their decision to maintain the existing relationship with the supplier without further competition; labor rates are still to be negotiated for the upcoming option period. Supply Management will take the lead in negotiating rates, terms and conditions for the option. In negotiating pricing, Supply Management will consider GSA rates as a potential benchmark.

Target Implementation Date: N/A

Responsible Official: Manager, Employee, Financial & Tactical Services CMC

Recommendation 2: Explore the benefits of awarding a firm-fixed priced professional services contract and implement, as warranted.

Management Response/Action Plan: Management agrees with this recommendation. Supply Management will review the benefits and administration of a firm-fixed price contracting structure and implement if warranted. Should a change from the existing contract structure be determined, Supply Management will convey this recommendation to the AFC. Any change will require approval from the AFC and the Governors.

Target Implementation Date: February 2021

Responsible Official: Manager, Employee, Financial & Tactical Services CMC

Recommendation 3: Obtain semi-annual review reports, annual improvement plans and supporting documentation from the supplier, as required in the contract and review the improvement plan to validate specific actions are taken to increase efficiencies and reduce costs.

Management Response/Action Plan: Management agrees with this recommendation. We will obtain semi-annual review reports, annual improvement plans and supporting documentation from the supplier, as required in the contract and review the improvement plan to validate specific actions are taken to increase efficiencies and reduce costs.

Target Implementation Date: January 2021

Responsible Official: Manager, Employee, Financial & Tactical Services CMC

E-SIGNED by MARK GUILFOIL
on 2020-08-07 15:03:56 CDT

Mark A. Guilfoil

cc: Manager, Corporate Audit Response Management

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