



Office of Inspector General | United States Postal Service

## Audit Report

# Negotiated Service Agreement - Contract #50593050

Report Number 20-206-R20 | September 10, 2020

A close-up photograph of a document with a yellow pen pointing to the text "Contract Term:". The document is slightly out of focus, showing other text like "Failure to perform duties", "Contract will commence on the [Year]", and "services listed 1 time".

## Contract Term:

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# Highlights

## Objective

Our objective was to determine mailer compliance with Negotiated Service Agreement (NSA) provisions and evaluate the U.S. Postal Service's oversight of NSA Contract #50593050. We selected the NSA based on the mailer's 2019 volume and revenue.

An NSA is a contractual agreement between the Postal Service and a mailer, whereby the mailer receives customized pricing in exchange for meeting volume and mail preparation requirements. The goal of using NSAs is to retain price sensitive customers and encourage additional mail volume and revenue. While only a small fraction of Postal Service commercial package customers have NSAs, 40 percent of the Postal Service's 5.5 billion domestic package volume is mailed under these agreements.

The Postal Regulatory Commission (PRC) must approve all NSAs. The PRC approved Contract #50593050 in fiscal year 2019. This three-year NSA provides special pricing for the mailer's Priority Mail weight/zone packages, Priority Mail Cubic packages, Priority Mail Flat Rate Envelopes, and Priority Mail Flat Rate Boxes. In return, the mailer agreed to ship [REDACTED] packages annually. The contract also requires the mailer to use a separate permit number for contract packages and pay using an approved manifest system.

This agreement stipulates that the Postal Service, at its sole discretion, has the right to revert to the most current Priority Mail Commercial Plus pricing for packages mailed in the subsequent contract year if the mailer does not meet the annual volume commitment.

We reviewed mail volume in year one of the NSA [REDACTED] 2018 through [REDACTED] 2019), before the President of the United States issued the national emergency declaration concerning the novel coronavirus disease outbreak on March 13, 2020. The results of this audit do not reflect process and/or operational changes that occurred as a result of the pandemic.

## Finding

The mailer was compliant with four of the five key agreement provisions we reviewed, including mail type and zone rates, permit number, and payment system. However, the mailer did not comply with the annual volume commitment. Specifically, in year one of the NSA, the mailer only shipped [REDACTED] [REDACTED] fewer than required. In year two of the NSA (through May 31, 2020), the mailer shipped [REDACTED] [REDACTED] fewer than in the same period the previous year.

The Postal Service provided adequate oversight of the NSA, which included monthly meetings with the mailer to discuss contract performance and expectations, as well as possible contract termination or submission of an exception request. In addition, the Postal Service was attempting to resolve an issue with linking this partner's marketplace platform volume to the NSA. The Postal Service's Contract Administration team presented an [REDACTED] [REDACTED] October 1, 2019, [REDACTED] for the second contract year. Management believed the [REDACTED] was necessary to maintain the customer's mail volume and they expected an uptick in volume during the approaching peak season. The committee approved the request on November 21, 2019.

We estimated that the Postal Service's decision [REDACTED] [REDACTED] [REDACTED] 2019 and May 31, 2020. The Postal Service will evaluate mailer compliance with contract terms, including volume requirements for contract years 2 and 3. As such, we will not make a recommendation in this report.

## Recommendations

We are making no recommendations in this report.

# Transmittal Letter



OFFICE OF INSPECTOR GENERAL  
UNITED STATES POSTAL SERVICE

September 10, 2020

**MEMORANDUM FOR:** TIMOTHY R. COSTELLO  
VICE PRESIDENT, SALES (A)

Janet Sorensen 

**FROM:** Janet M. Sorensen  
Deputy Assistant Inspector General  
for Retail, Delivery and Marketing

**SUBJECT:** Audit Report – Negotiated Service Agreement – Contract  
#50593050 (Report Number 20-206-R20)

This report presents the results of our audit of the Negotiated Service Agreement –  
Contract #50593050.

We appreciate the cooperation and courtesies provided by your staff. If you have any  
questions or need additional information, please contact Joseph Wolski, Director, Sales,  
Marketing and International, or me at 703-248-2100.

Attachment

cc: Postmaster General  
Corporate Audit Response Management  
Sr. Vice President, Finance and Strategy

# Results

## Introduction/Objective

This report presents the results of our self-initiated audit of Negotiated Service Agreement (NSA) – Contract #50593050 (Project Number 20-206). Our objective was to determine whether the mailer is in compliance with NSA provisions and evaluate the oversight of the agreement. We selected the NSA based on the mailer's 2019 volume and revenue. We reviewed mail volume in year one of the NSA [REDACTED], 2018, through [REDACTED], 2019) before the President of the United States issued the national emergency declaration concerning the novel coronavirus disease outbreak on March 13, 2020. The results of this audit do not reflect process and/or operational changes that occurred as a result of the pandemic.

## Background

An NSA is a contractual agreement between the U.S. Postal Service and a mailer, whereby the mailer receives customized pricing in exchange for meeting volume and mail preparation requirements. The goal of an NSA is to retain price sensitive customers and encourage additional mail volume and revenue. NSAs are a tool the Postal Service uses to better meet customer needs when some aspect of its off-the-shelf offerings does not. While only a small fraction of Postal Service commercial package customers have NSAs, 40 percent of the Postal Service's 5.5 billion domestic package volume is mailed under these agreements. The Postal Service's Board of Governors (the Board) authorizes NSAs for submission to the Postal Regulatory Commission (PRC). In 2011, the Board issued a decision approving all competitive NSAs that are estimated to cover their costs.

By law, the PRC approves NSAs. Competitive product NSAs must generate enough revenue to cover the costs directly tied to fulfilling the product or service. The Postal Service must also show that contracts cover their attributable costs,<sup>1</sup> do not cause market dominant products to subsidize competitive products as a whole, and contribute to the Postal Service's institutional costs.<sup>2</sup>

<sup>1</sup> Attributable costs are direct and indirect Postal Service costs that can be clearly associated with a particular mail product. It is the sum of volume-variable cost plus product-specific cost.

<sup>2</sup> Costs that cannot be directly or indirectly assigned to any mail class or product. They can be considered common costs or overhead costs needed for overall operations.



The PRC has approved all of the more than 1,400 domestic package NSA product agreements submitted for review since the program's inception in 2003. The Postal Service can propose NSAs for market dominant products, which include First-Class Mail and Marketing Mail; however, there are currently no NSAs of this type.

Any mailer may apply for an NSA if the mailer meets the requirements of the Postal Service's *Domestic Mail Manual 709*. The number of NSAs increased from 66 in fiscal year (FY) 2012 to 1,144 domestic competitive NSAs in FY 2019. In FY 2019, the PRC approved 191 competitive domestic NSAs.

The PRC approved Priority Mail Contract #50593050 as a competitive product on [REDACTED], 2018, and determined the rates established during the first year of the contract should cover its attributable costs. They also determined that contract price adjustment provisions would help ensure the contract covered attributable costs in subsequent years. The three-year NSA, effective [REDACTED] 2018, includes five key provisions related to mail type and zone rates, permit number,



payment system, and volume commitment. The first two key provisions provide special pricing for the mailer:

- Priority mail weight/zone packages that do not exceed [REDACTED] pounds and are zoned priced;<sup>3</sup> and Priority mail cubic packages that do not exceed [REDACTED] cubic feet and [REDACTED] pounds and are zoned priced.
- Priority mail flat rate envelopes (regular, legal, and padded) and Priority mail flat rate boxes (small, medium, and large).

To receive special pricing, the mailer must also adhere to these three key provisions:

- Use a separate mailing permit (permit) number for contract packages.
- Use PC Postage, Electronic Verification System (eVS),<sup>4</sup> or another Postal Service approved manifest system for payment.
- Ship a “non-binding<sup>5</sup> estimate” of [REDACTED] Priority Mail packages annually.

The agreement stipulates that the Postal Service has the right to suspend the special pricing and revert the mailer to the most current Priority Mail Commercial Plus prices if the mailer does not meet the annual volume commitment. The Contract Administration team within the Field Sales Strategy and Contracts (FSSC) group produces a contract performance report monthly and the FSSC account representative begins reviewing performance after the first month. If there is a concern that the mailer is not going to meet the volume requirement, Contract Administration and the account representative identify shortfalls in performance, discuss the issue with the mailer, and establish a timeline to achieve compliance.

## Finding #1: Annual NSA Volume Commitment Not Met

The mailer was compliant with four of the key agreement provisions we reviewed, including mail type, zone rates, permit number, and payment system. However, the mailer did not comply with the annual volume commitment. Specifically, in year one of the NSA [REDACTED] 2018 through [REDACTED] 2019), the mailer shipped [REDACTED] short of the required annual volume commitment of [REDACTED]. In year two of the NSA (through May 31, 2020) the mailer shipped [REDACTED] percent fewer than in the same period the previous year.

We found that the Postal Service provided adequate oversight of the NSA. A field account representative (FAR) held monthly meetings and reviewed contract performance with the mailer. The FAR discussed with the mailer why performance was not meeting expectations, worked to resolve those issues, and — in consultation with Postal Service management — communicated next steps, including possible contract termination or an exception request. The mailer then informed the FAR that while they did not want to lose the Postal Service as their primary shipper, they would shift 100 percent of their volume to a competitor if their contract was terminated.

The Postal Service chose not to suspend the special pricing and revert the mailer to the most current Priority Mail Commercial Plus prices once the mailer failed to meet their annual volume commitment. Management believed the [REDACTED] was necessary to maintain the customer’s mail volume and they expected an uptick in volume from the approaching peak season. In addition, the Postal Service was attempting to resolve an issue with linking this partner’s marketplace platform volume to the NSA. For these reasons, the Contract Administration team presented an [REDACTED] to the Pricing Committee on October 1, 2019, to [REDACTED] [REDACTED] for the second contract year. The committee approved the request on November 21, 2019.

<sup>3</sup> The Postal Service uses nine zones for domestic postage pricing: one local zone and Zones 1 to 8. Each zone has defined distances based on the mileage between the originating and destinating plant — for example Zone 2 encompasses distances of 51-150 miles, while Zone 3 encompasses distances of 151-300 miles. The larger the zone number, the higher the price charged to the mailer.

<sup>4</sup> Allows commercial mailers to print postage labels and electronically transmit manifests with detailed shipping and payment information to the Postal Service.

<sup>5</sup> Having no legal or binding force.

When the Postal Service extends special pricing to mailers who do not meet their volume commitment, it could set a precedent for future enforcement of NSA volume commitments and undermine one of the key purposes of NSAs, which is to encourage additional mail volume and revenue. If the mailer does not meet volume goals, the Postal Service is not maximizing revenue and mailers shipping similar volumes do not receive special pricing. Lost revenue for any one NSA may be relatively small, but the cumulative effect across all NSAs could be significant.

Postal Service management should consider whether this mailer's ability to obtain the same benefit from its NSA – regardless of whether it meets or fails to meet its volume commitment – ultimately weakens the Postal Service's broader financial position by diluting the perceived strength of NSAs. We estimated the Postal Service's decision not to enforce the revised pricing terms when the mailer failed to reach the volume commitment resulted in revenue shortfalls of [REDACTED] between [REDACTED] 2019, and May 31, 2020. The Postal Service will evaluate mailer compliance with contract terms, including volume requirements for contract years 2 and 3. As such, we will not make a recommendation in this report.

## Management's Comments

Management agreed with the statistics presented in the report but disagreed with the wording related to the monetary impact and program objectives. Specifically, management noted that it is unknown whether the mailer would have kept all of its business with the Postal Service at Priority Mail Commercial Plus prices. Management offered that a more accurate statement would be the Postal Service would have earned additional contribution had it moved the mailer to Commercial Plus prices and managed to retain the mailer's volume. Management also noted that they enter into NSAs to win or retain business that could not be won or retained at publicly available prices and shipping requirements.

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

## Evaluation of Management's Comments

The OIG considers management's comments responsive to the finding in the report. We agree that our conclusion is based on the assumption that the mailer would have continued mailing with the Postal Service after reverting to Priority Mail Commercial Plus pricing. Such an assumption is necessary to show the impact of the decision to continue at the reduced rate.

We also agree with management's assertion that the objective of the NSA program may be to enter into NSAs to win or retain business that could not be won or retained at publicly available prices and shipping requirements. We believe the statement in our report is accurate based on the Postal Service's published information on NSAs.

# Appendices

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# Appendix A: Additional Information

## Scope and Methodology

Our objective was to determine whether the mailer is in compliance with the NSA provisions and evaluate the oversight of the agreement. To accomplish our objective, we:

- Analyzed mailer data from the following Postal Service systems: Marketing Operational Data Store (MODS),<sup>6</sup> Product Tracking and Reporting (PTR),<sup>7</sup> National Meter Accounting and Tracking System (NMATS),<sup>8</sup> and the eVS.
- Obtained and reviewed the current NSA for Contract #50593050 and the PRC order authorizing the NSA to determine contract products, terms, and requirements.
- Interviewed Postal Service officials to discuss the NSA process, including contract performance monitoring and actions taken for non-compliance.
- Reviewed mailer's shipping information for compliance with the NSA provisions on mail type and zone rates, permit number, and payment system.
- Obtained and analyzed volume and price information to determine whether the mailer:
  - Met its volume commitment in contract year one.
  - Paid the correct contract price for each product in contract years one and two.

- Reconciled mailer data in NMATS, PTR, and MODS.
- Calculated monetary impact based on the mailer's volume commitment shortfall in contract year one.
- Interviewed FSSC officials and reviewed supporting documentation to evaluate Postal Service oversight of the NSA.

We conducted this performance audit from April through September 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 August 4, 2020, and included their comments where appropriate.

We assessed the reliability of computer-generated data by tracing the flow of shipping data through Postal Service systems and reviewing it for completeness and accuracy. We determined that the data were sufficiently reliable for the purposes of this report.

<sup>6</sup> The back-end database for the Customer Data Mart that is used to report Postal Service customer revenue and volume performance.

<sup>7</sup> The system of record for all delivery status information for mail and parcels with trackable services and barcodes.

<sup>8</sup> NMATS tracks postage meters, PC postage, customers, settings and their usage. Data reported in this application is transmitted to the Postal Service by the Postage Meter Providers. NMATS was designed to account for the revenue generated by postage meters currently in the hands of the public.

## Prior Audit Coverage

Report Title	Objective	Report Number	Final Report Date	Monetary Impact
<i>Partnership Agreement Compliance</i>	Determine [REDACTED] compliance with agreement provisions and to determine whether opportunities exist to enhance agreement provisions.	19BG004FT000-R20	12/27/2019	None
<i>Self-Certification Process for Domestic Competitive Product Negotiated Service Agreements</i>	Evaluate the Postal Service's self-certification process for domestic Competitive product NSAs.	CP-AR-17-004	12/16/2016	None

# Appendix B: Management's Comments



September 2, 2020

LAZERICK POLAND  
DIRECTOR, AUDIT OPERATIONS

SUBJECT: Project Number 20-206-DRAFT  
Negotiated Service Agreement – Contract # 50593050

The Postal Service management appreciates the opportunity to respond to the  
OIG findings in the draft report dated August 18.

Management agrees with the statistics presented within the Office of Inspector  
General's (OIG) report on Negotiated Service Agreement (NSA) Contract  
#50593050. However, we do not agree with the OIG's conclusion that the Postal  
Service's decision not to revert the customer to Priority Mail Centralized Postage  
Payment (CPP) pricing as a result of failing to meet its annual volume  
commitment resulted in a loss of [REDACTED]. It is unknown whether the  
customer would have kept all of their business with the Postal Service at Priority  
Mail CPP pricing, especially considering competitors were courting the customer  
for their business. Obviously if the Postal Service had the ability to know for sure  
if a customer would keep their business at CPP prices, it would have terminated  
the contract. A more accurate statement would be that the OIG has calculated  
that if the Postal Service had moved the customer to CPP prices and managed to  
retain the customer's volume, then the USPS would have earned [REDACTED] in  
additional contribution. Furthermore, we disagree with the statement that "the  
goal of using NSAs is to retain price sensitive customers and encourage  
additional mail volume and revenue". We enter into NSA's as a means to win or  
retain business that could not be won or retained at publicly available prices and  
shipping requirements.

A handwritten signature in blue ink that reads "Timothy R. Costello".

Timothy R. Costello  
Acting Vice President, Sales

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