June 8, 2011

HELEN R. GRANT
ASSOCIATE GENERAL COUNSEL

TOM A. SAMRA
VICE PRESIDENT, FACILITIES

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SUBJECT: Audit Report – Conflicts of Interest: Facility Leases and Contract Delivery Services (Report Number DA-AR-11-008)

This report presents the results of our audit of facility leases and Contract Delivery Service (CDS) agreements that represent potential conflicts of interest to the U.S. Postal Service (Project Number 10YG016DA000). Our audit objective was to assess whether leasing facilities from employees or their relatives or contracting with employees for delivery services resulted in actual or apparent conflicts of interest. We conducted this audit based on concerns brought to our attention and risks to organizational branding.

Federal regulations and Postal Service policies[1] seek to minimize conflicts of interest to ensure that every citizen can have confidence in the integrity of the federal government. Postal Service policies encourage employees to avoid creating the appearance that they are violating the law or ethical standards.

At the end of fiscal year 2010, the Postal Service leased over 24,000 properties that represent about $1 billion[2] in annual rent. During the same period, the Postal Service also maintained 7,797 mail delivery service contracts with individuals at an annual value of $318,658,027. See Appendix A for additional information about this audit.

[1] Acts affecting a personal financial interest (Title 18 U.S.C. §208),*Standards of Conduct for Employees of the Executive Branch* (5 U.S.C., §2635), Use of Public Office for Private Gain (5 CFR.2635.702), Use of nonpublic information (5 CFR.2635.703), Supplying Principles & Practices – Section 7-12, General Practices; and Supplying Principles & Practices – Principles – Ethics and Social Responsibility – Conflicts of Interest.
[2] Source: Postal Service 2010 Annual Report.

Conclusion

Our audit determined the Postal Service entered into leases that resulted in financial conflicts.[3] We identified 1,202 of 24,582 total leased properties that were obtained from current or former Postal Service employees with an annual rent value of $8.2 million. Of these properties, 982 were active leases with an annual rent value of $5.4 million. One-hundred seventy of the active properties were leased from current employees with an annual rent value of $490,375. Some pose risks of violations while others give the appearance of impropriety.

Similarly, the Postal Service entered into 78 of the 7,797 total CDS contracts (valued at $3,005,818 annually) with current or former employees that, in some cases, resulted in apparent violations of federal regulations and Postal Service policies. Others also give the appearance of impropriety.

Real Estate Leases – Conflicts of Interest

We randomly sampled 59 of the 1,202 leases that we associated with employees or their relatives. As presented in Table 1, we identified 11 (or 19 percent) with financial conflicts because they were owned by employees who have the authority to exert significant influence in the lease process. These employees consisted of postmasters and their reliefs. For eight of these 11 leases, we confirmed that employees did, in fact, exert significant influence during negotiations in their roles as postmasters.

For example, in one instance the Postal Service decided to move operations from the postmaster's property due to the poor condition of the facility. The postmaster subsequently solicited community support to discourage the move but once unsuccessful, she was able to lease land for the new post office location. This instance, among others, are apparent violations of Title18 U.S.C. §208 because employees participated personally and substantially in the Postal Service's decision to lease property they own and represent illegal actions that, in the absence of an approved waiver, are subject to criminal prosecution. We were unable to confirm apparent Section 208 violations for the remaining three leases because there was insufficient evidence in lease files to assess employee participation.

[3] Per Title 18 U.S.C. §208, a financial conflict exists when an employee participates personally and substantially in a particular matter where he, his spouse, minor child, or member of his household has a financial interest.

Table 1 – Results of Reviewing Active Leases With Potential Conflicts

Category	Sampled Leases	Projections[4]
Financial Conflicts – Apparent Section 208 Violations	8	103
Financial Conflict	3	16
Active Lease Conflicts	11	119

In addition, we identified 27 (46 percent) leases that were not conflicts of interest per Postal Service or federal guidelines. However, they give the appearance of impropriety. These lease renewals include former employees who have insider knowledge into the Postal Service's leasing practices, current employees not assigned to the leased location, and instances where the lessor was a permitted relative of a Postal Service employee. The remaining 21 leases were no longer conflicts of interest due to termination or ownership transfer to individuals other than Postal Service employees.

Apparent violations of Section 208 and federal ethics standards exist because Postal Service policy allows employees or their relatives to lease smaller properties to the Postal Service, self-disclosure of potential conflicts is ineffective, and the Postal Service does not match lessor information to payroll records. For example, in four of the 11 financial conflicts, the lessors did not disclose their relationships with the Postal Service as required.

As a result, we estimate that 119 of the 982 active leases (or 12 percent) are at risk for conflict and 103 of them (or 10 percent) are possible in violation of Section 208. Section 208 does provide exceptions that require obtaining a waiver from the Postal Service's Designated Agency Ethics Official (DAEO). None of the lease files we reviewed that were subject to Section 208 violations contained a waiver. See Appendix B for our detailed analysis of this topic.

CDS – Conflicts of Interest

Of the 78 delivery contracts with potential conflicts, we confirmed that the Postal Service awarded 15 of 78 contracts (19 percent) valued at $591,210 to current employees. In one instance a rural carrier associate was awarded a delivery service contract in July 2006 and remained an employee. The employee contractor did not disclose the Postal Service relationship as required. This instance, among others, are not violations of Section 208 because employees did not participate personally and substantially in

[4] We derived the projections based on the lower limit of a 90 percent confidence level. We are 95 percent confident that the actual populations are at least as great as the projections.

the contracting decision from which they or their relative received a financial benefit. Rather, these contract awards are apparent violations of Title 18 U.S.C. §440 that prohibits Postal Service employees from entering into contracts for mail delivery and Postal Service policy that does not allow CDS contracting with current employees.[5] Section 440 violations are also illegal actions subject to criminal prosecution.

In addition, we determined that 27 of 78 (35 percent) contracts were awarded to employees within days of separation from the Postal Service. Per discussion with Postal Service contracting personnel, employees were advised to resign before receipt of contract awards. Another 25 contracts (32 percent) were awarded to employees after 30 days of separation from the Postal Service. Although contracts with former employees are not violations of Postal Service or federal conflicts of interest guidelines, they do give the appearance of impropriety and may create the appearance that former employees violated Title 5 CFR.2635.703 by using their insider knowledge of the Postal Service to secure contract awards. This is particularly applicable to the 27 contracts negotiated during the employees' tenures and awarded shortly after separation. The remaining 11 contracts were not financial conflicts due to contract termination or changes in contractors.

Table 2 – Results of Reviewing CDS Contracts With Potential Conflicts

Category	Number of Contracts
Financial Conflict (Apparent Section 440 Violations)	15
Appearance of Impropriety – Former Employees	52
No Longer Conflict – Termination or Contractor Changes	11

Postal Service policies are implemented to minimize situations in which a supplier has an unfair competitive advantage.[6] Awarding employees delivery service contracts presents an appearance of impropriety and an unfair competitive advantage. CDS conflicts existed because:

- The Postal Service does not match its contractor information to payroll records.
- Contractor self-disclosure is ineffective. Ten of the 15 contractors associated with apparent Section 440 violations did not disclose their Postal Service relationship as required.

[5] *Supplying Principles & Practices*, Section 7-12, General Practices.
[6] *Supplying Principles & Practices* – Principles – Ethics and Social Responsibility – Conflicts of Interest.

We consider $146,149[7] as questioned costs associated with apparent Section 208 violations for leases, as the Postal Service should not have entered into questionable agreements. In addition we associated $591,210 in unrecoverable questioned costs for CDS contracts awarded to current employees in apparent violation of federal regulations and Postal Service policies. Although these amounts are not materially significant, transactions with financial conflicts erode the integrity and brand of the Postal Service. See Appendix B for our detailed analysis of this topic. Appendix C details our monetary impact calculations.

We recommend the associate general counsel, in coordination with the vice president, Facilities:

1. Revise the Postal Service's policy for leasing property under 3,000 square feet from employees or relatives to include an ethics review.

2. Evaluate the universe of potential facility lease conflicts and develop an action plan to minimize active and future conflicts.

3. Implement a control to systemically identify, monitor, and resolve potential conflicts of interest with facility leases and, if necessary, request waivers for leases that represent conflicts.

We recommend the associate general counsel, in coordination with the vice president, Supply Management:

4. Evaluate the universe of potential delivery service contract conflicts and develop an action plan to minimize active and future conflicts.

5. Implement a control to systemically identify, monitor, and resolve contract delivery service regulatory and policy violations in a timely manner.

[7] We derived the monetary impact projection based on the lower limit of a 90 percent confidence level. We are 95 percent confident that the actual population amount is at least as great as the monetary impact of $146,149.

Management's Comments

Management agreed with all five recommendations. In reference to facility leases, management will revise Handbook RE-1, *U.S. Postal Service Facilities Guide to Real Property Acquisitions and Related Services,* to require an ethics review and examine the 982 leases we identified as potential conflicts of interest. If the examination leads to risks of ethics violations they will seek the advice of ethics counsel. Management believes that their planned actions — to be completed by December 2011 and June 2012, respectively — will provide a system to monitor and resolve leases with potential conflicts. In addition, management will review disclosure language in lease agreements and strengthen it as necessary.

In reference to delivery service contracts, management planned to implement several controls to minimize conflicts. By September 2011, management will review and make necessary changes in their pre-award evaluation policies and processes to require offerers to disclose whether they are current employees. This should enhance controls for complying with the current prohibition to contracting with employees. In addition, management will provide training corresponding to Title 18 USC §440 requirements to contracting officers.

While management agreed with the recommendations and that financial conflicts occur when an employee participates personally and substantially in business decisions, they noted a fundamental disagreement about the application of certain ethics laws in the draft report. In particular, they rejected the assertion that conflict of interest laws and impartiality provisions applied to former employees and relatives. In addition, current employees who do not have official duties involving lease decisions, such as employees assigned to another location, do not legally give rise to a violation of the impartiality provision of the Standards of Ethical Conduct for Employees of the Executive Branch (Standards of Conduct).

Management also disagreed with our assessment of unrecoverable questioned costs. Specifically, due to the pending investigation of leases, they did not agree with the monetary impact presented at this time. Although they agree that delivery service contracts with current employees are violations, they do not believe the contract dollars represent a monetary loss or risk. Management comments, in their entirety, are included in Appendix D.

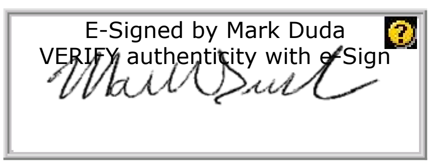
Evaluation of Management's Comments

The U.S. Postal Service Office of Inspector General (OIG) considers management's comments responsive to the recommendations and management's corrective actions should resolve the issues identified in the report.

We agree that financial conflicts of interest laws and impartiality provisions in the Standards of Conduct do not apply to former employees or family members who are not the spouses or minor children of current employees. The same is true for current employees who do not influence lease decisions. Although the contractual and leasing relationships we noted for these individuals were not conflicts of interest, we determined that the transactions, in substance, gave the “appearance of impropriety” and have revised the report accordingly. Given the financial condition and increased visibility of the Postal Service, appearance issues are critical and should not be readily dismissed. Individuals with these appearance issues have a competitive advantage because of their access to Postal Service insiders and knowledge of Postal Service operations.

The OIG considers all the recommendations significant and, therefore, requires OIG concurrence before closure. Consequently, the OIG requests written confirmation when corrective actions are completed. These 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.

We appreciate the cooperation and courtesies provided by your staff. If you have any questions or need additional information, please contact Miguel A. Castillo, director, Engineering and Facilities, or me at 703-248-2100.



Mark W. Duda
Deputy Assistant Inspector General
for Support Operations

Attachments

cc: Mary Anne Gibbons
Corporate Audit and Response Management

APPENDIX A: ADDITIONAL INFORMATION

BACKGROUND

Facilities is an enabling organization within the Postal Service whose primary mission is to (1) provide quality real estate to meet present and future needs of Postal Service organizations and (2) realize optimum value from facilities assets and transactions. The facility management function is headquartered in Arlington, VA, and has Facility Service Offices (FSO) throughout the country. Facilities administers over 24,000 leases that represent about $1 billion in annual rent. The Postal Service has various levels of approval and decision requirements based on the nature of the lease. The lease approval levels depend on the lease amount and whether they are entering into a new lease or exercising the renewal option of a current lease.

The Postal Service is required to provide retail and delivery services to customers in rural areas. The FSO works with Postal Service Operations to identify suitable facilities in these areas in accordance with Handbook RE-1. The cost of building a facility in a rural area can be cost prohibitive for the Postal Service, thus, the agency does not prohibit leasing property under 3,000 square feet (SF) from employees or relatives . For these leases, the Postal Service's long-standing practice is to balance the economic advantage with the highest standard of ethical conduct and the best interests of the Postal Service. The practice of leasing to employees dates back to the early years of the Postal Service. Postmasters were allowed to conduct retail and delivery operations in their homes and as an incentive for providing services. The Postal Service offered postmasters an allowance as part of their compensation. In the late 1970s, the Postal Service discontinued the allowance program and began a leasing relationship with postmasters. The leasing relationship is not limited to Postal Service employees' homes and can also include employee-owned property.

A federal conflict of interest statute (Title 18 U.S.C, §208) forbids employees of the federal government to participate personally and substantially as a government officer or employee through decision, approval, or recommendation of a contract in which, to his knowledge, he, his spouse, or minor child or any person or organization with whom he is associated as an officer, director, trustee, general partner or employee, has a financial interest. The statute and implementing regulations provide for Section 208 waivers with notification to the director of the Office of Government Ethics. Alleged violations of Section 208 may be subject to criminal prosecution.

Current employees are also required to adhere to Title 18 U.S.C. §440 for mail delivery contracts which states that whenever a person employed by the Postal Service becomes interested in any contract for carrying the mail or acts as agent, with or without compensation, for any contractor or person offering to become a contractor in any business before the Postal Service shall be fined under this title or imprisoned not more than 1 year or both.

CDS agreements are contracts between the Postal Service and an individual or company for the delivery and collection of mail from homes and businesses.[8] The services a CDS carrier provides are similar to those postal rural letter carriers provide, including delivery of mail and sale of stamps.

To initiate a CDS contract, a contract representative issues a memorandum announcing the solicitation request to the affected postmaster or local administrative official. The local official subsequently posts a notice of "Solicitation Availability" for public viewing in the post office. The official is also encouraged to use personal contacts, post brief announcements in publications, and use radio and television stations to share the contract solicitation, as long as the means used do not result in cost to the Postal Service.

The contracting office handles questions regarding solicitation requests along with the completed proposal documents. The contracting representative uses the following criteria to evaluate the applicants:

- Offer submission/bidding price (annual rate).
- Prior experience (transportation).
- Equipment availability (vehicle).

The contracting office assesses the supplier's capability based on the aforementioned criteria and awards the contract.

OBJECTIVE, SCOPE, AND METHODOLOGY

Our objective was to determine whether the Postal Service has adequate controls over the execution of lease agreements and contracting of delivery services to avoid actual or apparent conflicts of interest. In order to identify leases specifically related to conflicts of interest, we compared Social Security numbers from the Postal Service's Employee Master File (EMF) to corresponding social security numbers for leases in the electronic Facilities Maintenance System (eFMS). We randomly selected a statistical sample of 59 of 1,202[9] leases that matched for further study. Table 3 details the breakdown of our sample.

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[8] Publication 33, *Mail Transportation Contracting Guide*, February 2009.
[9] Twenty-two leases in this population were for spaces larger than 3,000 SF.

Table 3 – Lease Sample Section by Area Office

Area	Number of Leases
Western Area	24
Eastern Area	18
Southwest Area	7
Northeast Area	5
Great Lakes Area	3
Southeast Area	2
Total	59

To determine if employee lessors used their Postal Service relationships to their advantage, we visited a limited number of sites in the Western Area, conducted interviews, and assessed their span of influence for lease decisions. In addition, we reviewed lease files for award justification and reviewed negotiation notes. In coordination with OIG Office of Investigations, we analyzed whether leases were held by relatives or spouses of active or inactive Postal Service employees. A forensic examiner performed background investigations of lessors and confirmed employee status.

To identify CDS contract statutory, regulatory, and policy violations, we similarly matched electronic contract data to employee records. Specifically, we matched data from the Transportation Contract Support System to the EMF. We identified 78 CDS contracts with current or former employees that were awarded by the five contract offices presented in Table 4.

Table 4 – Offices Awarding CDS Contracts to Postal Service Employees

Area	Number of Contracts
Western Contracting Office	8
Eastern Contracting Office	22
Southern Contracting Office	15
Northern Contracting Office	13
Central Contracting Office	20
Total	78

To determine whether the contractor had influence in the award process, we reviewed contract files. In particular, we reviewed award justification and pre-award conference notes to assess influence and determine if the agreement was properly approved per Postal Service policies.

We conducted this performance audit from March 2010 through June 2011 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 officials on March 11, 2011, and included their comments where appropriate.

We assessed the reliability of computer generated data by comparing eFMS and TCSS information to the applicable lease and CDS contract documentation, respectively, without exception. We determined the data was sufficiently reliable for the purposes of this report. We based our audit conclusions on a review of applicable federal statues, regulations, and discussions with Postal Service and OIG counsel. Apparent violations of applicable laws were referred to our Office of Investigations to determine whether a referral to the Attorney General is warranted.

PRIOR AUDIT COVERAGE

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

APPENDIX B: DETAILED ANALYSIS

Real Estate Leases – Conflicts of Interest

Our review noted the Postal Service engages employees or their relatives for its real estate needs. These transactions create the need to manage potential conflicts of interest for leased property. While federal statute and regulations and Postal Service policies[10] control these potential conflicts, as indicated in Table 5, there are 1,202 potential conflict of interest leases held by current or former Postal Service employees. Specifically, there are 982 active leases and 220 discontinued leases in which vendor tax identification numbers match Postal Service employee Social Security numbers. Seventy-eight percent of these leases were obtained from postmasters or their relief; 7 percent from rural carriers; and the balance from casuals, clerks, and city carriers.

Of most concern are leases associated with postmasters as they have authority[11] to approve leases, repairs, emergency space, maintenance, and custodial services. At a minimum, this relationship would cause a reasonable person to question an appearance of impropriety as the lease arrangement is likely to have a direct and predictable effect on the financial interests of the Postal Service employee. Active leases with potential conflicts represented about 4 percent of leases, accounting for $5,437,344 of total lease payments (or less than 1 percent).

Table 5 – Status of Facilities Leased From Postal Service Employees

Facility Status	Leased	Owned[12]	Total
Active	981	1	982
Cancelled	59	11	70
Disposed	39	13	52
New/Planned	2	0	2
Terminated	96	0	96
Total	1,177	25	1,202

In addition, as depicted in Table 6, 11 of 59 leases (19 percent) randomly sampled from this population had financial conflicts associated with active leases. Based on the 11 sampled financial conflicts of concern, we estimate that at least 119 of the 982 active leases in our universe represent financial conflicts.

[10] Federal guidance related to conflicts of interest is included in Title 18 U.S.C., §208 and Executive Order 12731,*Principles of Ethical Conduct for Government Officers and Employees*. Postal Service guidance related to conflicts of interest are included in Handbook RE-1.
[11] *Administrative Services Manual*, Chapter 5.
[12] The Postal Service owns the building and leases the land.

Table 6 – Results of Reviewing 59 Leases

Category	Universe of Leases Matched to Employees	Sampled Leases	Projections
Apparent Section 208 Violations		8	103
Could Not Determine Employee Influence as Prescribed in Section 208		3	16
Subtotal Active Lease Conflicts		11	119
Active Leases with Current Employees Assigned to Another Location		2	7
Appearance of Impropriety – Former Employees		25	343
No Longer Employee Owned / Conflict		16	195
Subtotal Active Leases	982	54	[redacted]
Terminated Leases – No Longer Conflicts	220	5	[redacted]
Total Leases	1202	59	[redacted]

Our review also confirmed that eight of the 11 active leases with financial conflicts were apparent violations of Section 208 because employees personally and substantially participated in the lease decision in which they had a financial interest. For example, in one instance, the Postal Service decided to move from the postmaster's facility due to poor conditions. The postmaster subsequently solicited community support to discourage the move. When she was unsuccessful, she submitted a bid for a leasing land for the new Post Office location and her lease bid was selected. In other instances the postmasters appear to use their leasing relationship as a condition of employment.

Based on these eight leases, we estimate that at least 103 of the 982 active leases in our initial universe are also subject to Section 208 violations. Office of Government Ethics regulations[13] require a waiver for potential Title 18 U.S.C. §208 violations from the government official delegated the authority to issue a waiver. At the Postal Service, the DAEO would issue the waiver, in consultation with the Office of Government Ethics. Lease documentation did not contain a waiver for these leases. In the absence of a waiver, Section 208 violations represent illegal actions that are subject to criminal prosecution. As such, we have referred these cases to our Office of Investigations. The other three leases owned by postmasters or postmaster relief were at risk for violations of Section 208; however, lease files did not provide sufficient evidence to determine employee influence on the lease decision.

[13] Standards of Conduct for Employees of the Executive Branch (5 U.S.C. 2635.402(d)).

Another 25 active leases sampled correspond to former employees and relatives. Although there appear to be conflicts due to their Postal Service relationships, by definition they are not violations of federal ethics standards, which apply to current employees. Furthermore, federal conflict of interest statutes do not apply to relatives who are not spouses or minor children of federal employees. In our sample, the relatives of employees associated with an active lease were not spouses or minor children. Former employees and relatives have insider knowledge of Postal Service leasing practices and despite compliance with federal and Postal Service policy, these lease renewals give the appearance of impropriety. In addition, two lease renewals were associated with active employees assigned to another location which also gives an appearance of impropriety. The remaining 21 leases were no longer apparent conflicts of interest as the Postal Service had either terminated them or ownership had changed.

Postal Service Handbook RE-1, Chapter 3, provides guidance on leasing from Postal Service employees or immediate family members and is in compliance with federal Executive Order 12731. Handbook RE-1, Chapter 3, generally prohibits the Postal Service from entering into new agreements to option, purchase, or lease real property or contract real estate services from:

1) Any member of the Postal Service or member of the employee's immediate family.

2) Any individual bound by a personal services contract to the Postal Service or members of the individual's immediate family.

3) Any business substantially owned or controlled by Postal Service employees, personal service contractors, or members of their immediate families.

4) Any former Postal Service officer, executive, or employee.

Conditions of financial conflicts and apparent violations exist because:

- Postal Service policy allows property to be leased from employees or relatives for properties under 3,000 SF.

- The Postal Service does not match lessor information to payroll records.

- Self-disclosure of conflicts is ineffective. We consider self-disclosure alone ineffective to mitigate apparent conflicts as lease documentation did not show disclosure of the lessor's relationship with the Postal Service for four of the 11 active leases sampled with financial conflicts.

While these leases do not represent material annual rents to the Postal Service, lessors who are employees may take advantage of their insider knowledge and erode the integrity and brand of the Postal Service. As presented in Appendix C we will report $146,149 as monetary impact for Section 208 lease violations.

CDS – Conflicts of Interest

Our analysis of delivery contract and employee data showed the Postal Service awarded 78 CDS contracts to current and former Postal Service employees. As presented in Table 7, 15 of 78 CDS contracts (19 percent) were awarded to current employees. Fifty-two CDS contracts (67 percent) were awarded to former Postal Service employees and did not represent regulatory or policy violations. The remaining 11 were also no longer regulatory or policy violations due to termination of the contract or a change in the contractor.

Table 7 – Results of Reviewing 78 CDS Contracts

Category	CDS Classification	Number of Contracts
Section 440 (Financial Conflict)	Contracts to Current Employees	15
Appearance of Impropriety	Former Employees Awarded CDS Contracts	52
No Longer Conflict	Contracts Termination or Change in Contractor	11
	Total	78

We confirmed that 15 delivery contracts valued at $591,210 with apparent statutory, regulatory, or policy violations were awarded to current employees while substantially engaged with the Postal Service. In one instance, a rural carrier associate was employed by the Postal Service in December 2000 and was awarded a delivery service contract in July 2006 while remaining employed. The employee contractor did not disclose the Postal Service relationship as required. We noted other instances where current employees were awarded contracts and where employees held contracts for a significant time period prior to separation. Employees in this classification risk violations of Title 18 U.S.C. §440 because it prohibits Postal Service employees from entering into contracts for delivery of mail. Section 440 violations are also illegal actions subject to criminal prosecution. As such, we have also referred these cases to our Office of Investigations.

In addition, according to Postal Service policies, CDS contracts are not to be awarded to current employees.[14] The Postal Service's *Supplying Principles and Practices* clearly state that the, ". . .Postal Service will attempt to avoid situations in which a supplier has

[14] Supplying Principles & Practices – General Practices, Section 7-12.

an unfair competitive advantage. . ."[15] Awarding employees contracts during active service or prior to separation presents a potential conflict and an unfair competitive advantage. These 15 contracts are not violations of Section 208 because the employees did not participate personally and substantially in the contracting decision for which they have a financial interest.

We further noted that 52 contracts valued at $2,005,676 were awarded to former employees and, by definition, are not violations of Postal Service and federal ethics standards because these standards do not apply to former employees. Twenty-seven of 52 contracts were awarded to employees within days of separation from the Postal Service. Per discussion with Postal Service contracting personnel, employees are advised to resign before receipt of contract awards. The remaining 25 contracts were awarded to employees 30 days after separation from the Postal Service. The Postal Service allows for contracting delivery services with former employees when their expertise will further the success of the business and competitive interests of the Postal Service. However, former employees may use their insider knowledge of the Postal Service's process to their advantage when bidding for contracts. Although contracts with former employees are not violations of Postal Service or federal conflicts of interest guidelines; they give the appearance of impropriety.

Delivery service contract conflicts also existed because:

- The Postal Service does not match its contractor information to payroll records.
- Employees did not disclose their relationship as required.[16] For 10 of the 15 apparent Section 440 violations, employees did not disclose their Postal Service relationships.

While delivery service conflicts are not financially material to the Postal Service, contractors, who are employees may take advantage of their insider knowledge and also erode the integrity and brand of the Postal Service. As presented in Appendix C, we will report $591,210 as monetary impact for apparent Section 440 violations.

[15] Supplying Principles & Practices – Principles – Ethics and Social Responsibility – Conflicts of Interest.
[16] Supplying Principles & Practices – Provision 1-5, Proposed Use of Former Postal Service Employees.

APPENDIX C: MONETARY IMPACTS

Monetary Impacts

Finding	Impact Category	Amount
Section 208 Lease Violations	Questioned Costs	$146,149
Section 440 CDS Violations	Questioned Costs	591,210
	Total	**$737,359**[17]

Questioned Costs
Costs that are unnecessary, unreasonable, or an alleged violation of law or regulation.

[17] Based on annual value of lease and contract amounts.

APPENDIX D: MANAGEMENT COMMENTS

UNITED STATES
POSTAL SERVICE

May 26, 2011

LUCINE M. WILLIS

SUBJECT: Draft Audit Report – Conflicts of Interest: Facility Leases and Contract Delivery Services (Report Number DA-AR-11-DRAFT)

Thank you for the opportunity to review and comment on the subject draft audit report. Below, please find our responses to the findings of this audit, the recommendations, and our position on the accuracy of the monetary impact statements.

However, before responding to the findings and recommendations set forth in this audit report, it is important to note that we have a fundamental disagreement about the application of certain ethics laws in this report. The financial conflict of interest laws and the impartiality provisions in the Standards of Ethical Conduct for Employees of the Executive-Branch (Standards of Conduct) do not apply to former government employees or family members of current employees. Accordingly, management requests a deletion from page 2 of the audit report, in the paragraph entitled "Conclusion," because it is legally incorrect to state that there is a "lack of impartiality by primarily former employees." When discussing family members of current employees or former employees, the focus should shift to any applicable postal policies at issue and not the ethics laws or ethical obligations.

REAL ESTATE LEASES

Financial Conflicts of Interest

The Postal Service agrees that current postmasters or postmasters relief who own the real property that houses the post office(s) they manage could be at risk of violating the financial criminal conflict of interest law. However, it is important to note that the mere ownership of the building or property is not enough to give rise to an actual violation of this criminal law. A critical element of a violation of the financial conflict of interest law requires that the employee must have acted "personally and substantially" in an official action that involved the facility lease at issue. Postmasters or postmasters relief who own the property that houses their post office may avoid violating this law if they disqualify ("recuse") themselves from all official duties related to the lease and delegate all related responsibility to another postal official.

The OIG concluded that there were 11 situations in which there was a potential financial conflict of interest violation present because a postmaster or postmaster relief leased their real property to the Postal Service to house a post office facility. The OIG concluded that there was evidence to suggest that 8 of these 11 postmasters or postmaster relief employees exerted significant influence in the leasing process. In that the OIG's investigative arm is currently investigating these matters, management will defer taking a position on this finding until the investigations are complete.

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Washington DC 20260

Appearance of the Loss of Impartiality in Performance of Official Duties

The Postal Service rejects the finding of this audit report that 27 leases contained in the audit sample present an ethics violation involving an appearance of the loss of impartiality based on the following.[1]

Former Employees and Relatives of Current Employees:

The impartiality provision of the Standards of Conduct prohibits current employees from participating *in a particular matter involving specific parties which he knows is likely to affect the financial interests of a member of his household, or in which he knows a person with whom he has a covered relationship is or represents a party, if he determines that a reasonable person with the relevant facts would question his impartiality in the matter.*[2]

We disagree with the ethics analysis performed in this area. The audit found that there was a violation of the impartiality provision of the Standards of Conduct where a *former employee or a relative of a current employee was a lessor* to the Postal Service. The acts or omissions of a non-government employee cannot give rise to an impartiality violation. In other words, the impartiality provision of the ethics laws only focuses on what a current employee does while acting in their governmental capacity. Therefore, it is not legally correct to find an ethics violation of this provision on the part of anyone other than a current employee.[3]

Therefore, as to the 25 leases identified as giving rise to a "loss of partiality" on the part of former employees, the Postal Service rejects this conclusion on legal grounds.

Current Employees

Furthermore, the impartiality provision of the Standards of Conduct does not prohibit a current employee, *who does not have any official duties involving the lease (i.e., the particular matter)*, from leasing real property to the Postal Service. In other words, an employee who has no postal duties involving the execution of a lease or the events leading up to the execution of the lease, and who has no official duties related to the maintenance of the building or the lease oversight, by law, cannot be in violation of this provision of the Standards of Conduct. For example, a letter carrier would not have any lease related duties. Therefore, assuming there are no other legal concerns or leasing irregularities, there is no ethics concern with a letter carrier leasing a building to the Postal Service for use as a post office.

For the same reasons discussed above, the Postal Service rejects the conclusion that 2 of the leases at issue— where the current employee is assigned to another location— legally give rise to a violation of the impartiality provision of the Standards of Conduct.

However, the Postal Service agrees that our review of these findings does not stop with the ethics laws or regulations. Rather, there may be violations of Postal Service policies at issue. As noted in the audit report, the RE-1[4] sets out the policies that should be considered for such an analysis.

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[1] Page 3 of the report states: These lease renewals include former employees who have insider knowledge into [the] Postal Service's leasing practices, current employees not assigned to the leased location, and instances where the lessor was a permitted relative of a Postal employee.
[2] See 5 CFR 2635.501.
[3] Nothing in this OIG Audit report suggests that any postal official improperly awarded a leasing agreement to a party with whom the employee has a covered relationship or a party that lives in his/her household.
[4] U.S. Postal Service Facilities Guide to Real Property Acquisitions and Related Services

Real Estate Policies.

Section 332.1 of the RE-1 has a general prohibition against entering into "new agreements to option, purchase, or lease real property or contract for real estate services from (a) [a]ny employee of the Postal Service or member of the employee's immediate family;...(d) [a]ny former Postal Service officer, executive or employee." There are exceptions to this policy, however, when management believes it is in the best interests of the Postal Service to lease a facility despite the general prohibitions identified above. (See RE-1 332.2). The level of authority needed to grant such an exception to the general prohibitions vary and depend on whether it is an occupied post office at the time the lease is executed and the square footage of the facility.[5]

It is not clear if the 8 situations identified in the audit report that involve postmasters or postmasters relief, who own the real property that houses their post office, involve rental space of more or less than 3,000 square feet. Therefore, management is not clear if the requisite considerations were given to these situations. Nonetheless, management agrees that an ethics review is necessary whenever such a potential conflict exists and that neither the size of the facility or the state of occupancy should be a factor in determining whether an ethics review is warranted. Therefore, management agrees that the policies in the RE-1 need to be revised to include an ethics review anytime a postal employee owns the property at issue.

Real Estate Leases - Monetary Impact:

Until the investigation of these potential 18 USC § 208 violations is concluded by the OIG, management cannot determine if there are violations present. Therefore, management cannot agree at this time that there is a $146,149 monetary impact for 18 USC § 208 violations. (See page 12 of the audit report.)

REAL ESTATE LEASES—AUDIT RECOMMENDATIONS

We recommend the associate general counsel in coordination with the vice president, Facilities:

Recommendation 1. Revise the Postal Service's policy for leasing property under 3,000 square feet from employees or relatives to include an ethics review.

Management Response/Action Plan: Management agrees to revise Handbook RE-1 to require an ethics review whenever any lease agreement involves any current postal employee, regardless of post office size.

Target Implementation Date: December 2011.

Responsible Official: Actions will be completed by Vice President, Facilities, and the Associate General Counsel and Chief Ethics Officer.

Recommendation 2. Evaluate the universe of potential facility lease conflicts and develop an action plan to minimize active and future conflicts.

Management Response/Action Plan: As to the existing leases identified by the OIG as the universe of potential facility lease conflicts, management agrees to examine the 982 leases that the OIG matched for further study and determine if there is a basis to conclude that the postal employee who also serves as a lessor is in risk of violating his ethics obligations. If so, ethics counsel will advise management of the appropriate remedy.

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[5] The audit team acknowledged these exceptions on page 6 of the report.

Following the revision of the RE-1, in any situation where a lease involves a Postal Service employee, the lease will not be executed or renewed until an ethics review has been conducted and appropriate action, if any, is taken to remedy any ethics violation that such ownership presents.

Target Implementation Date: June 2012 for review of all existing leases noted above.

Responsible Official: Actions will be completed by Vice President, Facilities, and the Associate General Counsel and Chief Ethics Officer.

Recommendation 3. Implement a control to systemically identify, monitor, and resolve potential conflicts of interest with facility leases and, if necessary, request waivers for leases that represent conflicts.

Management Response/Action Plan: The steps identified in Recommendations 1 and 2 will provide the appropriate system to identify, monitor and resolve potential conflicts of interest with facility leases. Further, Management agrees to review the disclosure language in the standard lease agreement and strengthen as necessary. However, the Chief Ethics Officer disagrees with the recommendation insofar as it suggests granting waivers for existing violations in that a waiver may only be granted to allow for future participation in official duties that are otherwise in violation of 18 USC § 208.

Target Implementation Date: Revisions to the RE-1 and updating of standard lease agreement language are projected for December 2011.

Responsible Official: Actions will be completed by Vice President, Facilities, and the Associate General Counsel and Chief Ethics Officer.

CONTRACT DELIVERY SERVICES—CONFLICTS OF INTEREST

Contracting with Former Employees

We disagree with the analysis performed in this area insofar as it found an ethics violation in the award of a delivery contract to a former employee. The audit found that there was a violation of the impartiality provision of the Standards of Conduct where a *former employee* was awarded a delivery contract. The acts or omissions of a non-government employee cannot give rise to an impartiality violation. In other words, as discussed in the introduction and in the above section addressing real estate leases, the impartiality provision of the ethics laws only focuses on current employees and only while acting in their governmental capacity. Therefore, it is not legally correct to find an ethics violation of this provision on the part of anyone other than a current employee.[6]

Therefore, the Postal Service rejects the finding that there is any appearance of a loss impartiality violation present insofar as the 52 delivery contracts cited in this audit report that were issued to former employees.

Management asserts that such awards are not only ethically permissible appropriate but are most often fiscally prudent and operationally efficient business decisions. The contracts under examination are those that serve postal customers who live in rural areas. Contract Delivery Services are competitively solicited – that is, they are awarded based on "best value." In these remote delivery areas, former employees very well may be the most qualified and, therefore, offer the best value

[6] There is nothing in this audit report to suggest that any current employee engaged in any ethical misconduct in the award of the delivery services contracts at issue.

to the Postal Service. Particularly where a route was converted to a Contract Delivery Service pursuant to Article 32, the most obvious benefits of engaging a former employee include increased operational flexibility, reduced costs, and the ability to manage cost growth over time.

Contracting with Current Employees

Management agrees that current employees may not "become interested in any contact for carrying the mail." Pursuant to 18 USC § 440 current employees risk prosecution for violating this federal statute. Therefore, management agrees that action is warranted in response to the 15 delivery services contracts that were awarded to active Postal Service employees.

Contract Delivery Services—Monetary Impact

Although management agrees that delivery contracts should not have been awarded to current employees, there is no basis to conclude that the value of the contracts represent any monetary loss or risk to the Postal Service and, therefore, we respectfully disagree that with the assessment of $591,210 as unrecoverable questioned costs.

CONTRACT DELIVERY SERVICES AUDIT RECOMMENDATIONS

Recommendation 4. Evaluate the universe of potential delivery service contract conflicts and develop an action plan to minimize active and future conflicts.

Management Response/Action Plan: Management agrees in part with this recommendation and in conjunction with our action plan for recommendation 5 below will implement several controls to minimize conflicts.

Target Implementation Date: See implementation dates for recommendation 5.

Responsible Official: The responsible official is the Manager, Surface Transportation, with the advice and support of the appropriate legal counsel.

Recommendation 5. Implement a control to systemically identify, monitor, and resolve contract delivery service regulatory and policy violations in a timely manner.

Management Response/Action Plan: Management agrees with this recommendation. Self certification has been an effective process that is commonly used in both government and commercial sectors to review offeror's representations before contract award. However, we are concerned that there were instances of nondisclosure as noted within the OIG's report. We will review and make necessary changes in our preaward evaluation policies and processes to require offerors to disclose if they are current Postal Service employees. This will enhance our controls and ensure compliance with our policies prohibiting contracting with current employees.

Training and communication will be provided to our contracting officers regarding the requirements of 18 USC § 440 and the current policy prohibition against contracting with current employees.

Target Implementation Date: Communications and policy changes September 2011.

Responsible Official: The responsible officials for the communication are the Manager, Surface Transportation and Chief Ethics Officer. For the policy changes the responsible official is the Manager, Supply Management Infrastructure.

We do not believe that this report contains any proprietary or business information and may be disclosed pursuant to the Freedom of Information Act. If you have any questions about this response, please contact Susan Witt at 202 268-4833.

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Corporate Audit and Response