



March 20, 2007

LYNN MALCOLM
VICE PRESIDENT, CONTROLLER

SUBJECT: Transmittal of Audit Report — Transportation Cost System
(Report Number MS-AR-07-002)

This report presents the results of our audit of the Transportation Cost System (TRACS) (Project Number 06YG030MS000). We conducted this audit pursuant to the Postal Accountability and Enhancement Act, Public Law 109-435. Section 204 of the act requires the U.S. Postal Service to annually submit a report to the Postal Regulatory Commission analyzing costs, revenues, rates, and quality of service. The U.S. Postal Service Office of Inspector General is required to "regularly audit the data collection systems and procedures utilized" to prepare this report.

Overall, TRACS internal controls were effective and TRACS data was valid and reliable. Our report contains no recommendations. However, management reviewed a draft report for technical accuracy and we incorporated their suggested changes as appropriate.

We appreciate the cooperation and courtesies provided by your staff during the review. If you have any questions or need additional information, please contact Robert Mitchell, Director, Sales and Service, or me at (703) 248-2100.

A digital signature of Darrell E. Benjamin, Jr. is shown in a grey rectangular box. The signature is in cursive and includes a small yellow question mark icon in the top right corner.

Darrell E. Benjamin, Jr.
Deputy Assistant Inspector General
for Revenue and Systems

Attachments

cc: H. Glen Walker
J. Ron Poland
Deborah A. Kendall

INTRODUCTION

Background

The Transportation Cost System (TRACS) is a statistical sampling and data collection system that provides information to estimate purchased transportation costs for major classes and subclasses of mail and type of service. Although the U.S. Postal Service's total purchased transportation costs are available from the accounting records, the records do not indicate how much of the transportation costs should be attributed to each specific class and subclass of mail and special service. Since the characteristics of purchased transportation vary significantly by mode of transportation, TRACS has four separate sampling systems:

- Highway
- Commercial Air
- Network Air
- Rail

In fiscal year (FY) 2005, the Postal Service sampled over 17,000 truck, airline, and rail van trips and used the results to distribute approximately \$4.8 billion in purchased transportation costs to the appropriate classes and subclasses of mail and type of service.

The Postal Service mainframe computer system at the San Mateo Information Technology and Accounting Service Center (IT/ASC) is used to create the TRACS sample frame.¹ Computerized On-Site Data Entry System (CODES) software for TRACS is used to download the sample frame to web-based unit servers at each district. Data collectors conduct TRACS tests and record the results on a laptop computer using the CODES software for TRACS. The completed tests are transferred to the web-based unit servers and transmitted to the San Mateo mainframe computer system for analysis and storage.

Objectives, Scope, and Methodology

We conducted this audit pursuant to the Postal Accountability and Enhancement Act, Public Law 109-435. Section 204 of the act requires the Postal Service to annually submit a report to the Postal Regulatory Commission analyzing costs, revenues, rates, and quality of

¹ A sample frame is a list that identifies all the individual units in a target population.

service. The U.S. Postal Service Office of Inspector General (OIG) is required to “regularly audit the data collection systems and procedures utilized” to prepare this report.

The objectives of this audit were to (1) review the effectiveness of the TRACS internal controls and (2) assess the validity and reliability of the TRACS data.

- Validity refers to whether TRACS data represents purchased transportation costs for major classes and subclasses of mail and type of service.
- Reliable data is complete, accurate and consistent; meets its intended purpose; and is not subject to inappropriate alteration.

The appendix describes the scope and methodology of our review.

Prior Audit Coverage

The OIG and Government Accountability Office (GAO) conducted two audits related to TRACS.

Audit of Statistical Tests for Fiscal Year 2005 – Cost and Revenue Analysis (Report Number FF-AR-06-091, March 6, 2006). This report summarized the results of statistical program audits conducted at 18 Postal Service districts and two postal facilities. The statistical program audits found the Postal Service was generally conducting statistical tests, including TRACS, in accordance with established guidelines. During the course of the audits, we observed 19 TRACS tests and identified testing errors in three of them. The OIG recommended that management reinforce data collection procedures. Management agreed with the findings and recommendations.

U.S. Postal Service: Improving Ratemaking Data Quality through Postal Service Actions and Postal Reform Legislation (GAO Report Number GAO-05-820, July 2005). This audit reviewed the actions the Postal Service took in response to recommendations from a 1999 data quality study that reviewed Postal Service ratemaking data, including TRACS.² The study recommended the Postal

² Data Quality Study, A.T. Kearney Inc., April 16, 1999.

Service evaluate and adjust the TRACS sample design to improve the quality of TRACS data. The study also recommended the Postal Service update TRACS policies and procedures and expand its documentation of TRACS in postal rate cases. The audit found the Postal Service followed the study recommendations and increased the quantity of data collected by TRACS, rewrote the TRACS policies, and expanded the rate case documentation.

Fiscal Year 2005 Information Systems General Controls (Report Number IS-AR-06-004, March 6, 2006). This report summarized the results of audits of information systems general controls at Postal Service IT/ASCs, including San Mateo, for FY 2005. The audit confirmed that general controls over systems, data, and computer-related infrastructure at the San Mateo IT/ASC generally provide reasonable assurance that data were complete, secure, and validated for accuracy, and that data integrity was provided.

AUDIT RESULTS

Effectiveness of Internal Control System

Overall, TRACS internal controls were effective. We used the Treadway Commission's Committee of Sponsoring Organizations (COSO)³ internal control framework to assess the effectiveness of internal controls. We found:

Control Environment: A control environment was in place and included established reporting relationships and duties, a TRACS training program, and supervisory review of data collection procedures.

Risk Assessment: Management identified relevant risks and the Postal Service had taken actions to mitigate the risks and improve the quality of TRACS data.

Control Activities: Internal control activities throughout the TRACS process were in place and functioning. Key processes included creating the sample frames, conducting TRACS tests, and processing the TRACS test results.

Information and Communication: Information and communication systems were in place and functioning.

Monitoring: Monitoring controls over TRACS performance were established and working.

Data Validity and Reliability

TRACS data was valid and reliable. General and application controls over TRACS generally provide reasonable assurance that TRACS data was valid and reliable. Additionally, data validation and edit controls within CODES, the web-based unit, and the mainframe TRACS applications provide additional assurance that TRACS data was valid and reliable.

³ The COSO of the Treadway Commission, Internal Control – Integrated Framework (see the appendix for more details).

APPENDIX. SCOPE AND METHODOLOGY

We conducted this audit from March 2006 through March 2007 in accordance with generally accepted government auditing standards and included such tests of internal controls as we considered necessary under the circumstances. We discussed our observations and conclusions with management officials and included their comments where appropriate.

We used the Treadway Commission's Committee of Sponsoring Organizations (COSO) internal control framework to assess the effectiveness of internal controls. COSO defines internal control as a process designed to provide reasonable assurance that an organization can achieve key objectives related to the effectiveness and efficiency of operations, reliability of financial reporting, and compliance with applicable laws and regulations. Under the COSO framework, five interrelated components of internal control provide a basis against which internal control can be evaluated.

1. **The control environment** sets the tone for the organization and is a foundation for the other internal control components. Key control environment factors include management commitment toward effective internal controls, training, and supervision practices.
2. **Risk assessment** is the identification, analysis, and management of relevant risks to achieving the organization's objectives.
3. **Internal control activities** are the policies and procedures that help ensure management directives are carried out. Control activities include a wide range of diverse activities such as approvals, authorizations, verifications, reconciliations, performance reviews, and documentation.
4. **Information and Communication** systems report on external and internal events, activities, and conditions that make it possible to effectively manage the organization. Effective communication must flow down, across, and up the organization.
5. **Monitoring** occurs in the course of normal operations and includes regular supervisory activities and other actions people take in performing their duties. Monitoring of internal control also includes policies and procedures for ensuring the findings of audits and other reviews are resolved.

To review the effectiveness of the control environment, we interviewed key personnel, reviewed the statistical programs organizational structure and reporting relationships, and assessed the TRACS training program.

To review the risk assessment component, we reviewed the goals and objectives that management established for the TRACS program. We then reviewed management's

assessment of the risks to meeting those goals and objectives and strategies to mitigate those risks.

To examine the effectiveness of control activities, we interviewed personnel, examined TRACS policies and procedures, and reviewed key control activities throughout the TRACS program, including:

- Creating the TRACS highway, commercial air, network air, and rail sample frames.
- Transmitting test schedules to the field.
- Conducting TRACS tests and documenting the test results.
- Supervising review of test results.
- Transmitting and processing test results.

To assess the establishment of an effective information and communications component, we reviewed the flow of information between headquarters and field components.

To assess monitoring, we interviewed key personnel and reviewed key monitoring activities and controls at the headquarters and field level. We also assessed the extent to which the results from prior audits, studies, and postal rate cases had been considered.

To assess the validity and reliability of TRACS data, we interviewed key personnel and reviewed five application controls over TRACS software and hardware. To test data reliability we traced 25 actual tests from the CODES laptop to the web-based unit. We also input simulated test data (some incorrect) for three TRACS tests (rail, highway, and air), traced the data through the CODES laptop to the web-based unit, and observed the functioning of the CODES data edit controls.⁴

⁴ Edit controls are CODES laptop software programs that identify data input errors.