Office of Inspector General

January 25, 2005

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SENIOR VICE PRESIDENT, OPERATIONS

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ACTING VICE PRESIDENT, FINANCE, CONTROLLER

KEITH STRANGE
VICE PRESIDENT, SUPPLY MANAGEMENT

SUBJECT: Audit Report – Mail Transport Equipment Service Center Network – Network Realignment – Pittsburgh, Detroit, Cleveland (Report Number NL-AR-05-001)

This report presents results from our audit of the mail transport equipment service center network (Project Number 04YG003NL001). It responds to a Board of Governors' request.

Postal Service officials are realigning the service center network to integrate or consolidate operations, close facilities, and save money. As part of realignment, officials planned to close service centers in Pittsburgh and Detroit, and consolidate operations in Cleveland. On March 12, 2004, an employee of the incumbent Pittsburgh-Detroit contractor wrote to the Board of Governors and asserted that the Postal Service never solicited revised pricing from the incumbent contractor and that retaining operations in Pittsburgh and Detroit would be cheaper than moving to Cleveland. On March 24, 2004, the Board of Governors asked us to examine the plan, and notify them before the Postal Service moved operations to Cleveland. The Cleveland contract award was scheduled for May 7, 2004.

Ultimately, the Postal Service decided not to move consolidated operations to Cleveland. On August 6, 2004, management entered a five-year, [redacted] agreement with the incumbent Pittsburgh-Detroit contractor. The agreement, which included two option periods, will retain existing operations in Pittsburgh and Detroit, and is anticipated to save more than $21.6 million over a five-year period compared to current costs.

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Management's approach to achieving savings began with a belief that creating competition among contractors would place the Postal Service in a strong negotiating position, and ultimately maximize savings. The approach of creating competition between contractors has merit. In the case of the proposed Cleveland move, we believe management could have enhanced competition and the probability of attaining and maximizing savings by conducting thorough analytics in advance, including:

- Gathering data consistently on all potential regional sites.

- Analyzing all potential sites before issuing a solicitation for bids exclusively on Cleveland.

- Putting the incumbent contractor and other potential regional bidders in direct competition.

Postal Service investment policy governing "expense investments" requires major operational changes to be thoroughly analyzed before they are made. Management did not consider closing service centers in Pittsburgh and Detroit, and consolidating those operations in Cleveland, to be major. Consequently, management did not adhere to the rigorous analytical procedures specified by investment policy. We recognize management's need to quickly react to a rapidly changing operational environment; however, we are concerned about a potential policy void covering operational changes when management does not consider such changes major operating expense investments. Consequently, in the context of our process for reviewing proposed policy, we would welcome an opportunity to work with management to clarify investment policy, and establish procedures for operational changes when those changes are not considered "expense investments."

We recommended that Postal Service management (1) clarify investment policy pertaining to expense investments, and (2) establish guidance to clarify the appropriate level of decision analysis and authority, consistent with the magnitude of the business decision being made, when major operational decisions are not covered by investment policy.

Management agreed with our first recommendation, disagreed with our second, and made several additional comments. We have addressed all of management's disagreements and comments. Management's comments and our evaluation of their comments are included in this report.

We view recommendations 1 and 2 as inextricably linked. Beginning in 2002—in response to this and previous audits—management essentially agreed with recommendation 1 by promising to revise and clarify investment policy. Since we consider recommendations 1 and 2 linked, we will monitor the progress of management's proposed policy revision.

The Office of Inspector General (OIG) considers recommendations 1 and 2 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 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 during the review. If you have any questions or need additional information, please contact Joe Oliva Director, Network Operations and Logistics, or me at (703) 248-2300.

/s/ Mary W. Demory

Mary W. Demory
Deputy Assistant Inspector General
for Core Operations

Attachments

cc: Paul E. Vogel
Anthony M. Pajunas
Shibaji Chakraborty
Anthony E. Mazzei
Steven R. Phelps

INTRODUCTION

Background

The mail transport equipment service center network is a system of 22 contractor operated service centers designed to supply mailbags, carts, hampers, and other mail transport equipment to mail processing facilities nationwide. The original plan to create the network was presented to the Postal Service Board of Governors in Decision Analysis Report, Mail Transport Equipment Service Center Network, dated May 13, 1997. The Decision Analysis Report forecast costs exceeding $3.6 billion over ten years, and was approved by the Governors in June 1997. The new network became fully operational in January 2000.

The Pittsburgh Mail Transport Equipment Service Center.

In response to a challenge from the Executive Vice President, Chief Operating Officer, last year, Postal Service Network Operations Management developed a plan to realign the network to integrate or consolidate operations, close facilities, increase efficiency, and save money. The existing Pittsburgh-Detroit five-year cost forecast exceeded [redacted]. Network Operations Management believed that if Pittsburgh and Detroit could be consolidated at a large, newly established service center in Cleveland, the Postal Service could save money.

On March 5, 2004, the Postal Service contracting officer issued a solicitation for bids on the consolidated Cleveland site. On March 12, 2004, an employee of the incumbent Pittsburgh-Detroit contractor wrote to the Board of Governors and alleged or asserted:

- The Postal Service never solicited revised pricing from the incumbent contractor.

- Retaining operations in Pittsburgh and Detroit would be cheaper than moving operations to Cleveland.

The contractor's officials subsequently reiterated their employee's allegations and assertions. On March 24, 2004, the Board of Governors asked us to examine the plan, and

Plastic and cardboard mail containers.

Mail transport equipment service centers are logistical support activities that supply mailbags, carts, and other equipment, like these containers, to mail processing facilities nationwide.

notify them before the Postal Service moved operations to Cleveland. Cleveland contract award was scheduled for May 7, 2004.

Objective, Scope, and Methodology

This report responds to the Board of Governors' request. Its objective is to provide the results of our examination of the proposed Cleveland move.

During our work, we examined contract solicitations, correspondence, media articles, relevant policies and procedures, and assessments prepared by the Postal Service.

We included all relevant comments, where appropriate. We also consulted with economists, financial analysts, and other subject matter experts.

Work associated with this report was conducted from March 2004 through January 2005, in accordance with generally accepted government auditing standards, and included such tests of internal controls as we considered necessary under the circumstances.

Prior Audit Coverage

Our audit report, Mail Transport Equipment Service Center Decision Analysis Report, Performance and Financial Benefit (Report Number TR-AR-01-003, dated May 4, 2001), concluded the network would not achieve the financial benefits anticipated by the Decision Analysis Report and would instead, exceed the ten-year $3.6 billion forecast by more than $1.4 billion. Transportation cost was the most significant cost overrun, accounting for more than $1 billion of the total, and resulted from insufficient analysis of transportation requirements. We recommended, in part, that management develop a Decision Analysis Report Modification Request in accordance with investment policy. Management disagreed. They stated the network was not a

Our 2001 audit report identified $1 billion in potential MTE transportation cost overruns.

The audit concluded that transportation cost overruns were caused, in part, by insufficient analysis of network transportation requirements.

capital investment and consequently, was not subject to investment policy. As a result of management's disagreement, we referred the matter to audit resolution. Postal Service Headquarters Finance, which is the proponent for investment policy, stated that although the network was not a "capital investment," it was a "major operating expense investment," and therefore subject to investment policy. Postal Service investment policy includes rigorous analysis, documentation, and approval requirements. In addition, it requires independent validation by Capital and Program Evaluation officials in Headquarters Finance.

RESULTS

Proposed Service Center Consolidation and Relocation

The Postal Service will retain operations in Pittsburgh and Detroit rather than consolidating operations in Cleveland. Postal Service documents we examined indicate that the new Pittsburgh-Detroit contract will save more than $21.6 million over the five-year contract term including two option periods when compared to current contract costs. Management's approach to achieving savings began with a belief that creating competition among contractors

A mail transport equipment shipment arriving at the Pittsburgh service center.

The service center network has dedicated transportation.

would place the Postal Service in a strong negotiating position, and ultimately maximize savings. The approach of creating competition between contractors has merit. In the case of the proposed Cleveland move, we believe management could have enhanced competition, and increased the probability of attaining and maximizing savings by conducting thorough analytics in advance, including:

- Gathering data consistently on all potential regional sites.
- Analyzing all potential sites before issuing a solicitation for bids exclusively on Cleveland.
- Putting the incumbent contractor and other potential regional bidders in direct competition.

Instead, the competitive effort was initially focused exclusively on Cleveland. On March 5, 2004, the date of the Cleveland solicitation, the contracting officer anticipated the following schedule:

- April 15, 2004 – Cleveland bids due.
- May 7, 2004 – Cleveland contract award.
- June 21, 2004 – Detroit closure.
- August 20, 2004 – Pittsburgh closure.
- August 30, 2004 – Cleveland fully operational.

On March 22, 2004, Postal Service officials met with United States Senator, Carl Levin, from Michigan, and United States Congressman, John D. Dingell, from the Detroit area. Despite the anticipated Cleveland contract award within 47 days, the officials promised Senator Levin and Congressman Dingell that the incumbent Pittsburgh-Detroit contractor would be given an opportunity to reprice existing operations, and no final decision would be made until an analysis was completed and independently validated. After the meeting, the following events took place:

- April 6, 2004 – The contracting office offered the incumbent contractor an opportunity to reprice existing Pittsburgh-Detroit operations.
- April 19, 2004 – The incumbent contractor submitted a reprice offer.
- April 26, 2004 – The contracting officer reported that the repriced Pittsburgh-Detroit operation would be $33 million cheaper than the Cleveland low bid.
- May 6, 2004 – The Office of Inspector General (OIG) provided interim audit results to the Board of Governors.
- May 27, 2004 – Management completed a review of the proposed Cleveland move and concluded any

potential savings in Cleveland were more than offset by a 104 percent increase in transportation costs.

- June 24, 2004 – The contracting officer calculated that repriced Pittsburgh-Detroit operations could save more than $21.6 million over the five-year contract period, including two option periods, when compared to current Pittsburgh-Detroit costs.

- July 6, 2004 – The contracting officer received authorization to make contract award to the incumbent contractor.

- August 6, 2004 – A five-year [redacted] contract was awarded to the incumbent Pittsburgh-Detroit contractor. The contracting officer forecast savings exceeding $21.6 million over the contract term including two option periods.

Decision Analysis Policy

Management could assure savings are attained and maximized by following the concepts and principles of Postal Service investment policy. For example, investment policy requires major decisions to be thoroughly analyzed before they are made. However, the analysis identifying the 104 percent increase in transportation costs was not made until after the decision to solicit bids exclusively on Cleveland. Had the analysis been made in advance, management might have concluded Cleveland was not feasible, and competed Pittsburgh-Detroit instead. Since the analysis was not made in advance, Pittsburgh-Detroit was not directly competed, and it is uncertain whether management's competitive approach was maximized, or the incumbent's reprice minimized.

Postal Service Handbook F-66, General Investment Policies and Procedures, dated February 2002, identifies two investments categories subject to its provisions.

- Capital Investments – This category includes investment in facilities, vehicles, or equipment.

- Expense Investments – This category includes major operational changes that result in operating fund expenditures exceeding $7.5 million.

Analytical procedures specified by Handbook F-66 were not completed in advance of the Cleveland solicitation because it is unclear when the provisions apply. For example, the OIG considers the mail transport equipment service center network a "major operating expense investment" subject to investment policy. The OIG holds that position because:

- The initial ten-year $3.6 billion mail transport equipment service center network plan was presented to the Board of Governors in a Decision Analysis Report in accordance with investment policy.

- In response to our previous audit report, Mail Transport Equipment Service Center Decision Analysis Report, Performance and Financial Benefit (Report Number TR-AR-01-003, dated May 4, 2001), management acknowledged that the network was a "major operating expense investment" subject to investment policy.

During our current audit, we took the position that a decision to restructure the mail transport equipment service center network by closing Pittsburgh and Detroit, and consolidating operations in Cleveland, met the definition of a "major operational change" as defined by investment policy. We believe the decision was "major" because:

- The five-year plan to consolidate Pittsburgh-Detroit operations in Cleveland would cost more than [redacted], and investment policy defines the threshold for a "major operating expense investment" as the expenditure of operating funds in excess of $7.5 million over a project period.

- The plan involved the loss of more than 300 jobs in Detroit and Pittsburgh.

- The plan attracted significant media and Congressional attention.

Consequently, it was our opinion that such a major operational change should be supported by a thorough, structured, and transparent analysis; adequate

	documentation; rigorous independent validation; and a formal written report, which was approved and signed by officials at the appropriate level.
Network Operations Management	Network Operations officials explained that the system of 22 mail transport equipment service centers was not a network in a true sense, and that restructuring was not analogous to the network integration and alignment they now referred to as evolutionary network design. The officials stated that there was no overarching strategy for service center realignment; that the system was established incrementally with different contracts; and that to save money, each contract had to be considered separately. The officials emphasized that in the context of a $6 billion transportation network, closing service centers in Pittsburgh and Detroit, and consolidating operations in Cleveland, was not major. Instead, it was merely an adjustment, and consequently, did not trigger the requirement for a formal Decision Analysis Report. In addition, the officials stated that because technology and the customer base were rapidly evolving, their adjustments would be obsolete in 18 months, and a formal 5-year planning model was not feasible. They explained that rather than a rigorous analytical process, creating a competitive environment based on a certain degree of speculation was the best approach. They also emphasized that because of the rapidly changing environment, every decision could not be brought to the Board of Governors.
Finance	Capital and Program Evaluation officials in headquarters Finance develop and maintain corporate investment policy and procedures. They also manage the Decision Analysis Report process specified by investment policy, and validate Decision Analysis Reports prepared by project sponsors like Network Operations. Capital and Program Evaluation officials emphasized that every business decision does not rise to a level requiring a Decision Analysis Report. They explained that criteria for a Decision Analysis Report was defined in the F-66 Handbook series, and if a project met those criteria, the analysis had to be rigorous, provide supporting documentation that was auditable, and include:

- Analytical assumptions, factors, and financial impacts that were documented and auditable.
- A cost/benefit analysis, consideration of other alternatives, and a risk assessment.
- Detailed backup documentation signed and authenticated by appropriate subject matter experts who were usually independent from the project sponsor.
- Backup documentation organized in a way that allowed review by other organizations such as the Government Accountability Office or the OIG.
- Appropriate concurrences from headquarters functional components and Area Vice Presidents.

Officials explained that they were occasionally asked to review the reasonableness of an assessment other than a Decision Analysis Report, and that such reasonableness reviews, while not cursory, were less in scope than a formal validation. In addition, they explained that they were specifically asked to review the Pittsburgh, Detroit, Cleveland assessment, and that because the assessment was not a Decision Analysis Report, their work was a review, not a validation. The officials also stated that they were not aware of any specific procedural guidance similar to Decision Analysis Report or validation procedures, which applied when a major operating decision was not considered an operating expense investment.

Contracting

The contracting officer stated that normally the contracting office asked sponsors to prepare a detailed cost-benefit analysis before bids were solicited. However, in the case of Cleveland, contracting was presented with a summary transition plan document. The contracting officer explained that after the Cleveland bids were received, officials would analyze the proposed restructuring using actual bid data.

The contracting officer emphasized that to get bids as low as possible, after initial bid receipt, qualified contractors would compete directly against each other in a “reverse auction” to determine which contractor would achieve the lowest bid. However, the contracting officer stipulated:

- The incumbent Pittsburgh-Detroit contactor did not compete in the “reverse auction” because that contractor did not submit a proposal for the original Cleveland solicitation.

- There was no solicitation to re-compete the Pittsburgh-Detroit facilities nor a competitive “reverse auction” procedure focused on Pittsburgh-Detroit.

- Actual data from sites other than Cleveland would not be available for decision analysis since bids on alterative sites were not solicited.

- Normally, reprice opportunities were given to incumbent contractors four to six months before contract termination, and that it was unusual for a rebid opportunity to be offered to an incumbent contractor after a solicitation for bids on an alternate site.

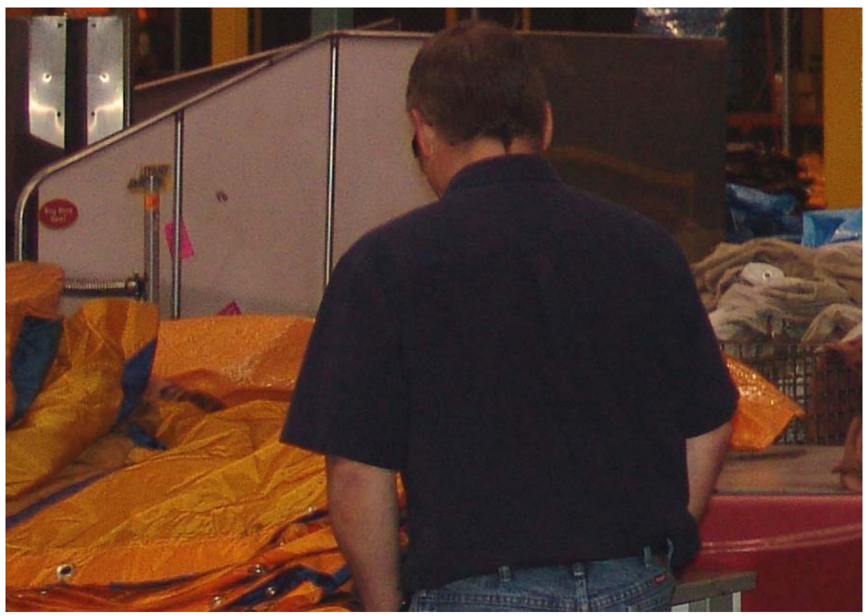
The Pittsburgh, Detroit, Cleveland Assessment

On May 25, 2004, Network Operations completed their assessment of the proposed restructuring. The assessment was a compilation of tables and spreadsheets, it contained no narrative or analytical assumptions, source documents were not referenced or validated, and backup documentation was not organized or readily available. Sites other than Cleveland were not identified, considered, or explored. There were no concurrences from affected functional components or Area Vice Presidents, the document offered no narrative report or conclusion, and the document was not approved or signed.

On May 27, 2004, Capital and Program Evaluation completed their independent review of the Network Operations’ assessment. The review was presented informally on a Capital and Program Evaluation routing slip with four attached worksheets. It did not independently test the accuracy of underlying data, qualified that it was based only on data provided by Network Operations, and it was not signed or approved. However, the review did include a narrative explaining that retaining Pittsburgh-Detroit was economically superior to consolidating in Cleveland.

It is the OIG's position that the analytical, validation, and approval procedures established by Postal Service investment policy for operating expense investments is an excellent framework for analyzing, validating, and approving major operating decisions.

It is also the OIG's opinion that closing, consolidating, and relocating service centers is a major operational change as defined by investment policy, and is consequently subject to that policy. We believe that had management followed the procedures specified by the F-66 Handbook series, they would have thoroughly analyzed the Pittsburgh, Detroit, Cleveland plan, and would have offered the incumbent Pittsburgh-Detroit contractor an opportunity to reprice existing operations before soliciting bids exclusively on the Cleveland location.



Contract employee sorting mailbags.

The service center network is contractor operated.

Notwithstanding our opinion, we recognize management's need to quickly react to rapidly changing requirements in a fluid operational environment. In response to a previous audit, Trailer Lease Justification (Report Number TD-AR-02-002, dated March 29, 2002), management agreed to modify investment policy to clarify certain aspects of investment policy provisions. We believe this is a good strategy, and we would welcome the opportunity to work with management in the context of our process for reviewing proposed policy revisions. We remained concerned about a potential policy void covering major operational changes or initiatives which management does not consider major operating expense investments.

Recommendation

We recommend the Senior Vice President, Operations, in coordination with the Acting Vice President, Finance, Controller, and Vice President, Supply Management:

1. Clarify the provisions of Postal Service investment policy, particularly with regard to the definition of expense investments, so that Postal Service officials and managers have a clearer understanding as to when investment policy applies.

Management's Comments

Management agreed that Postal Service investment policy concerning expense investments needed clarification. They stated that they would re-write the appropriate provisions as part of an entire revision of Postal Service Handbook F-66, General Investment Policies and Procedures. Management also stated that they anticipated issuance of the revised policy not later than September 2006. Management's comments, in their entirety, are included in Appendix A of this report.

Evaluation of Management's Comments

Management's comments were responsive to our recommendation and we consider the planned policy revision sufficient to address the issues we identified. In their response to the 2002 audit we cited earlier, (Report Number TD-AR-02-002, dated March 29, 2002), management made the same commitment by agreeing to immediately modify Handbook F-66. We reiterate that we welcome the opportunity to work with management in the context of our process for reviewing proposed policy revisions.

Recommendation

2. Establish guidance to clarify the appropriate level of decision analysis and authority, consistent with the magnitude of the business decision being made, when major operational decisions are not covered by investment policy.

Management's Comments

Management disagreed with our recommendation. They explained that: (1) it was unlikely guidance could be written that would account for all possible business decisions faced by managers; (2) they empowered managers to make decisions; (3) they expected their managers to make those decisions in a business like manner; and (4) their existing review processes provided the proper level of oversight for decisions being made.

Evaluation of Management's Comments

Management's comments were not responsive to our recommendation. Our recommendation did not contemplate specific written guidance "for all possible business decisions faced by . . .managers." It was intended for "major operational decisions" not covered by policy. For reasons explained earlier, we believe the decision to close service centers in Pittsburgh and Detroit, and consolidate operations in Cleveland, was major. Consequently, we believe the decision warranted formal analysis, documentation, oversight, and approval.

Detroit Mail Transport Equipment Service Center September 16, 2004

However, even if Postal Service officials believe such an operational decision does not meet the "major operating expense investment" criteria specified by their investment policy, federal standards still require analysis, documentation, oversight, and formal authorization protocols. These provisions are intended to help program managers prevent error. Despite management's assertion that existing review processes provide the proper level of oversight for operational decision making, it is not certain current processes are sufficient to prevent error.

For example, in their comments, management acknowledged that their decision to close Pittsburgh and Detroit—and move to Cleveland—was already made before they completed their assessment. Had management executed its original decision, the Postal Service might have spent $33 million too much for an operation now anticipated to cost [redacted]. We believe any decision to spend $33 million more than necessary on a [redacted] program would be a significant error—and as federal internal control standards suggest—well defined policies, procedures, and authorization protocols are needed to prevent such errors.

We view recommendations 1 and 2 as inextricably linked. Beginning in 2002—in response to this and other reports—management essentially agreed with recommendation 1 by promising to revise and clarify policy. Since we consider recommendations 1 and 2 linked, we will monitor the progress of management's proposed policy revision.

Additional Management Comments

Management made several additional comments. In some cases, we discussed the additional comments with management and made minor adjustment to the text of our report. In addition, we addressed management's more significant additional comments in Appendix B

APPENDIX A. MANAGEMENT'S COMMENTS

JOHN A. RAPP
SENIOR VICE PRESIDENT
OPERATIONS

UNITED STATES
POSTAL SERVICE

November 29, 2004

MARY W. DEMORY

SUBJECT: Draft Audit Report-Mail Transportation Equipment Service Center Network-Network Realignment-Pittsburgh, Detroit, Cleveland (Report Number NL-AR-05-DRAFT)

This letter is provided as the combined management response to the above referenced report. Our review of the draft report discovered the following factual inaccuracies:

1. Cover letter, page one, paragraph 3, line 2.

<u>RECOMMENDATION</u>:
Change the sentence to read "On August 6, 2004, management exercised a two-year contract option valued at $27.5 million with the incumbent contractor, and will retain..."

<u>COMMENT</u>:
The Postal Service did not award a new five-year contract to RCI. Instead, it modified the existing contract by exercising an option for two more years in the amount of $27,465,617, with two options period (one two-year option for [redacted] and a one-year option for [redacted]). If both options are exercised, the total contract amount will be [redacted].

2. Draft audit report, page 4.

<u>RECOMMENDATION</u>:
Delete bullet 3.

<u>COMMENT</u>:
The Postal Service pre-qualified suppliers, which included the incumbent and 10 other vendors were invited to submit offers for the Cleveland solicitation. Solicitations were posted on the Federal Business Opportunities website and all pre-qualified suppliers were notified.

3. Draft audit report, page 5, paragraph one, delete the first sentence.

<u>COMMENT</u>:
See comment two above.

4. Draft audit report, page 6, third bullet.

<u>COMMENT</u>:
See comment one above and forecasted savings are $8,110,533 for the base five-year period. The $21.6 million figure assumes all options are exercised.

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5. Draft audit report, page 9.

RECOMMENDATION:
The first full paragraph, after the last sentence "... an operating expense investment." Add "However, these officials did provide OIG with a copy of the Postal Service Purchasing Manual and recommended that it be reviewed for specific analytical guidelines."

6. Draft audit report, page 9.

RECOMMENDATION:
Contracting section, change the paragraph to read "The contracting officer (CO) stated that typically, for a major action such as this, the sponsor or requiring activity would have conducted their own justification analysis. The CO was presented with a summary document of the MTESC transition plan, which indicated the potential benefit of closing Detroit and Pittsburgh."

COMMENT:
The decision to analyze the proposed restructuring using actual bid data was not the CO's position. This position resulted from statements made by Postal Service Officials on March 22, 2004 to members of Congress. This position is more fully explained in the information found on page 5 of the draft report.

7. Draft audit report, page 10.

RECOMMENDATION:
Delete the first bullet.

COMMENT:
This is an inaccurate statement. See comment 2 above.

8. Draft audit report, page 10.

RECOMMENDATION:
Delete the second bullet.

COMMENT:
Since the decision was made to close Detroit and Pittsburgh and relocate the operations to Cleveland, no solicitation for Pittsburgh-Detroit was issued. Therefore, the need for "reverse auction" did not arise at those sites, as they were not considered for continuing operations.

Regarding the recommendations contained in the draft report, management provides the following responses:

We recommend the Senior Vice President, Operations, in coordination with the Acting Vice President, Finance, Controller, and Vice President, Supply Management:

RECOMMENDATION 1:
Clarify the provisions of Postal Service investment policy, particularly with regard to the definition of expense investments, so that Postal Service officials and managers have a clearer understanding as to when investment policy applies.

- 3 –

RESPONSE:
We agree that the F-66 language concerning expense investments needs clarification, and we are working on a re-write of this as part of an entire F-66 revision. We anticipate issuance of the revised F-66 on or before the end of fiscal year 2005.

Moreover, it is this issue which creates the confusion around how the MTESC initiative was or should have been classified and, therefore, all of the downstream disagreements. It is our position that the original MTESC project was not approved as a Decision Analysis Report.

However, all of these issues that existed around the MTESC should not occur in the future when the investment policy language is clarified.

RECOMMENDATION 2:
Establish guidance to clarify the appropriate level of decision analysis and authority, consistent with the magnitude of the business decision being made, when major operational decisions are not covered by investment policy.

RESPONSE:
Management disagrees with the recommendation. It is unlikely that guidance could be written that would account for all possible business decisions faced by our mangers in the performance of their duties. We have empowered them to make decisions and expect them to do so in a business-like manner. We think that our review processes provide the proper level of oversight for decisions being made throughout Operations.

If you have any questions, you may contact [redacted] at [redacted]

John A. Rapp

cc: Keith Strange
Paul Vogel
Tony Mazzei
Tony Pajunas

APPENDIX B

OIG RESPONSE TO ADDITIONAL MANAGEMENT'S COMMENTS

Additional Management's Comments

Management stated that it was their position "the original MTESC project was not approved as a Decision Analysis Report."

Evaluation of Additional Management's Comments

Management's statement is inconsistent with the facts as they exist. The original plan to create the network was presented to the Postal Service Board of Governors in Decision Analysis Report, Mail Transport Equipment Service Center Network, dated May 13, 1997. The Decision Analysis Report anticipated costs exceeding $3.6 billion over ten years, and was approved by the Governors in June 1997. The new network became fully operational in January 2000. On June 6, 2001, Postal Service management agreed the project was a "major operating expense investment" subject to investment policy.

Additional Management's Comments

Management made various suggestions regarding our description of their August 6, 2004 agreement with the incumbent Pittsburgh-Detroit contractor. We described the agreement as a five-year [redacted] contract the contracting officer anticipated would save more than $21.6 million over the five-year contract period.

Evaluation of Additional Management's Comments

Management stipulated that the agreement was not a new five-year [redacted] contract, but the modification of an existing contract with successive renewal options as follows:

Initial 2-year extension	[redacted]
Additional 2-year option	[redacted]
Additional 1-year option	[redacted]
Total 5-year agreement	[redacted]

Management also explained that the contracting officer's $21.6 million saving forecast was only valid if all contract options were exercised.

Management's $21.6 million savings estimate was based on their assessment of the entire five-year agreement, including all renewal options. We understand that if management does not execute all options, the savings they now anticipate will be different, and potentially, may not be achieved at all.

Additional Management's Comments

Management objected to our statement that the incumbent contractor and other regional bidders were not put in direct competition with Cleveland bidders, and were not included in a competitive reverse auction. Management pointed out that the incumbent Pittsburgh-Detroit contractor was free to bid on the Cleveland site, and had the incumbent contractor chosen to do so, the incumbent contractor would have been included in the Cleveland reverse auction.

Regarding a potential Pittsburgh-Detroit reverse auction, management explained that there was no need for such an auction because the decision to close Pittsburgh-Detroit, and move to Cleveland, was already made before the Cleveland solicitation. Management emphasized that before the solicitation on March 5, 2004, both Detroit and Pittsburgh were eliminated from consideration as sites for continuing operations.

Evaluation of Additional Management's Comments

We understand that the incumbent Pittsburgh-Detroit contractor was free to bid on Cleveland—and opted not to do so. Our concern was not about individual contractors bidding against each other on the preselected Cleveland site. Our focus was about putting the incumbent contractor and other potential regional bidders in direct competition in order to optimize potential savings. For example, in addition to Pittsburgh and Detroit, the proposed plan impacted operations in Cincinnati, Chicago, and other locations. We believe management might have increased savings by fully analyzing or competing all affected sites.

Additional Management's Comments

Management requested that we modify our report concerning a statement made by Finance officials. As cited in our report, Finance officials told us that:

> **"they were not aware of any specific procedural guidance similar to Decision Analysis Report procedures or validation procedures, which applied when a major operating decision was not considered an operating expense investment."**

Management requested that we modify our report by adding the following:

> **"However, these officials did provide OIG with a copy of the Postal Service <u>Purchasing Manual</u> and recommended that it be reviewed for specific analytical guidelines."**

Evaluation of Additional Management's Comments

The circumstances of the relevant discussion involved a meeting we had with Finance officials on Wednesday, May 19, 2004. We cannot add the statement management requested because the statement management requested is not accurate. Finance officials did not provide a copy of the Purchasing Manual—nor would doing so have been necessary. At the time of our May 19, 2004, meeting, we had already thoroughly examined the Purchasing Manual.