September 29, 2010

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SUBJECT: Audit Report – Management of Mail Transport
Equipment - National Analysis (Report Number NL-AR-10-009)

This report presents the results of our self-initiated audit focusing on the nationwide management of Mail Transport Equipment (MTE) program (Project Number 10XG032NL000). The objective was to assess the effectiveness of the U.S. Postal Service's management and control of MTE from a headquarters perspective. This audit addresses financial and operational risks. See Appendix A for additional information about this audit.

MTE are containers of various types used to hold mail during processing and transportation within or between Postal Service facilities, its contractors, its mailers, and other external customers. The various types of MTE include pallets, containers with wheels, trays, and mailbags. The Postal Service loans MTE to mailers and other external customers as a courtesy to convey mail to and from Postal Service installations. Postal Service policy requires routine audits of mailers and Postal Service facilities to ensure that MTE is not misused or misappropriated and the quantity on-hand is adequate.

Postal Service Headquarters is responsible for establishing policy for managing all aspects of MTE program, and the Postal Service's eight geographical areas are responsible for ensuring compliance with all aspects of the MTE policy at the field level. We estimate the Postal Service purchased about $688 million in MTE over the past 12 years.[1]

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[1] The $688 million in MTE purchases was reconstructed from limited Postal Service system data and represents the best estimate we were able to derive from the limited data.

Conclusion

Although the Postal Service has taken a number of steps to enhance its management of MTE over the last 2 years, we found the following opportunities for Postal Service Headquarters to more effectively manage and control MTE nationwide. Specifically, management could:

- Provide updated, comprehensive policy, guidance, and oversight that support current MTE operational requirements.

- Develop a nationwide comprehensive inventory system for identifying and tracking all MTE throughout the network, including tracking to and from mailers, and for effectively determining annual MTE purchase requirements.

- Ensure that areas have sufficient resources to monitor the management of MTE in the field or at mailers and to ensure appropriate compliance with national MTE requirements.

These systemic issues contributed to conditions identified in our prior MTE reviews in the Pacific and Eastern areas and impact MTE operations in all Postal Service areas. Specifically, in our prior reviews, we concluded the following:

- MTE inventories were inaccurate because management based them on estimated "on-hand counts" and did not include equipment from some plants or any major mailers and other external customers.

- Although plants generally kept records of MTE distributed to mailers and customers, they did not have visibility over the MTE flow once it left the plants and did not use the records for managing, tracking, or reconciling MTE and establishing accountability.

- Plant managers did not always provide sufficient priority, resources, training, and oversight to effectively manage MTE.

- Area management did not assign sufficient resources to monitor MTE activities and ensure compliance with all *Postal Operations Manual* (POM) and Standard Operating Procedures (SOP) requirements.

See Appendix B for our detailed analysis of this topic.

If comprehensive controls over MTE had been in place at facilities and mailers, we estimate the Postal Service could have avoided spending about $14.5 million annually ($29 million total) for MTE in fiscal years (FYs) 2008 and 2009. In addition, if comprehensive controls are established, the Postal Service could better ensure that

only needed MTE is purchased in the future. See Appendix C for our calculation of the questioned costs.

Further, we estimate about $897 million in MTE assets are at risk of loss, theft, and misuse because of the control weaknesses. These conditions also present a potential danger to public safety and security[2] and reflect poorly on the Postal Service's brand and public image.[3] See Appendix D for our calculation of the assets at risk.

Management Actions

Over the last 2 years, Postal Service Headquarters has been assessing and exploring initiatives and taking some action to address nationwide, systemic MTE issues, including the following. Many of these actions are still in process.

- Exploring technological solutions such as an automated MTE management system.[4]

- Assessing the need to reinstitute on hand volume counts[5] to provide the Postal Service with enhanced visibility of MTE at facilities and mailers until an automated MTE management system is fully developed and deployed.

- Implemented an initiative to seed plastic pallets with Global Positioning Satellite technology, which has tracked the movement of Postal Service pallets from mailers to others with no business relationship with the Postal Service.

- Initiated an equipment recovery program in coordination with the U.S. Postal Inspection Service.

- Educated mailers and Postal Service plants by disseminating posters and newsletters and establishing a 1-800 number and national e-mail contact for the recovery of MTE.

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[2] The Postal Service is a recognized presence in cities and communities nationwide and enjoys high public trust. A concern with the widespread unauthorized use and misappropriation of MTE is that criminal elements may use this Postal Service equipment to take advantage of the high public trust, including use of MTE for disguising contraband or other dangerous goods as mail.
[3] The essence of the Postal Service brand is customer perception and the control and management weaknesses above could pose a high risk for the public to negatively perceive the Postal Service's ability to properly manage, account for, and protect its assets.
[4] One option being explored is the MTE On-line Ordering (MTEOR) system and a more recent option is the Solution for Enterprise Asset Management (SEAM) system.
[5] Weekly inventory counts were part of the Equipment Inventory Reporting System (EIRS).

We recommend that the vice president, Network Operations:[6]

1. Further develop, update, and reinforce national Mail Transport Equipment (MTE) policies and procedures contained in the *Postal Operations Manual* and the Postal Handbook PO-502, *Container Methods,* which address MTE inventory and accountability controls, including validating customer MTE needs as well as tracking and reconciling MTE loaned to mailers and other external customers.

2. Continue pursuing implementation of a planned automated Mail Transport Equipment (MTE) management system and ensure its functionality for inventory and accountability processes and for enhancing the Postal Service's visibility into MTE internally and at mailers.

3. Reestablish an on-hand Mail Transport Equipment (MTE) volume count process, both internally and externally, until an automated MTE management system is fully developed, deployed, and operational.

4. Ensure that area Distribution Networks Offices have appropriate resources assigned responsibly to monitor and manage Mail Transport Equipment, and maintain compliance with *Postal Operations Manual* requirements.

Additionally, we recommend the vice president, Network Operations, coordinate with the vice president, Supply Management to:

5. Document the current process for identifying annual, routine Mail Transport Equipment (MTE) purchase requirements, and ensure the process includes Mail Transport Equipment Service Center network information and facility and mailer inventory data, to ensure that only the necessary amount of MTE is purchased.

Management's Comments

Management generally agreed with our findings and recommendations. Management stated they will re-establish equipment inventory counts for Postal Service facilities by January 1, 2011, and will update MTE policies and procedures, to include addressing the roles and responsibilities of local, area, and headquarters, by the end of the second quarter in FY 2011. Management also stated they will assess how best to implement an on-line ordering and fulfillment system solution for mailers by the end of the second quarter in FY 2011. Finally, management stated the addition of EIRS data will enhance the process to determine purchased MTE requirements, and they will determine whether to pursue an external component of on-hand inventory reporting by the end of the second quarter in FY 2011. Management did not agree with the methodology used to determine the potential monetary impact reported for MTE purchases but did agree

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[6] The low individual cost of MTE has been a factor in the decisions made by the Postal Service to limit dollars spent in the controls over these items. The controls implemented based on these recommendations should be cost effective and consider MTE leakage.
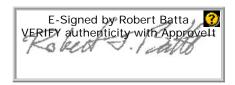
that increased inventory visibility will provide greater control of MTE assets. See Appendix F for management's comments, in their entirety.

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. Regarding management's comments on our monetary impacts, we used the best information available, given data limitations, in calculating the potential monetary impact for unneeded MTE purchases. Further, management did not provide any alternative methodology or estimates, and we believe our estimates are still valid. We will continue to work with management to reach agreement on monetary impacts in closing the significant recommendations.

The OIG considers all 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 Jody Troxclair, director, Transportation, or me at 703-248-2100.

E-Signed by Robert Batta
VERIFY authenticity with ApproveIt

Robert J. Batta
Deputy Assistant Inspector General
  for Mission Operations

Attachment

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APPENDIX A: ADDITIONAL INFORMATION

BACKGROUND

MTE consists of various types of containers used to hold mail during processing and transportation within or between Postal Service facilities, its contractors, its mailers, and other external customers. The various types of MTE include:

- Pallets made of plastic, wood, or chipboard.
- Containers with wheels of varied sizes, shapes, and materials (known as 'rolling stock').
- Trays of varying sizes for letters and flats (known as 'tubs').
- Mailbags (known as 'sacks').

Flat Tray or Tub

Plastic Pallets

Individual MTE items cost the Postal Service anywhere from less than $1 to about $1,400. Generally, the useful life of MTE will vary considerably based on type, and some MTE, such as rolling stock, can be in service for more than 20 years.

Rolling Stock at
Philadelphia Processing and Distribution Center
(P&DC) on November 2, 2009

The Postal Service expenses (rather than capitalizes) MTE in accordance with its accounting policies and practice. Additionally, MTE has been historically viewed as being consumable or expendable and provided to mailers and other external customers as a courtesy. The Postal Service does not carry MTE inventory as an asset for financial reporting purposes and does not know the true size or value of its MTE

inventory. However, we estimate the value of the Postal Service's current on-hand MTE inventory nationwide at approximately $1.2 billion.

<u>MTE Management</u>. Postal Service Headquarters, under the direction of the vice president, Network Operations, is responsible for establishing policy for managing all aspects of MTE, covering the operation, transportation, distribution, delivery, inventory, storage, and reporting of MTE. Postal Service Headquarters manages MTE primarily through the MTESC network, which centralizes MTE processing, repair, and distribution. The MTESC network is a centrally managed system of contractor-operated service centers[7] designed to supply pallets, tubs, mailbags, and other MTE to mail processing facilities and certain large customers nationwide. The MTESC network delivers MTE to users with dedicated transportation, recovers equipment that is no longer needed or serviceable, and then processes it for inventory or redistribution.

Hampers staged for repair work at the Los Angeles MTESC on October 28, 2008

Under the national MTE policy, the Postal Service's geographical areas, through their Distribution Networks Offices (DNOs), are responsible for ensuring compliance with all aspects of the Postal Service's MTE policy at the field level. The area DNOs are required to provide guidance to plants, and each plant is responsible for the daily management of MTE at its facility, ensuring compliance with all national MTE policies. See Appendix E for a flowchart detailing the movement of MTE within the Postal Service.

OBJECTIVE, SCOPE, AND METHODOLOGY

The objective of our self-initiated audit was to assess the effectiveness of the Postal Service's management and control of MTE from a headquarters perspective.

To accomplish our objective, we assessed the management and control weaknesses identified in our audits of the Pacific and Eastern areas to identify issues, actions, and

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[7] At inception, the MTESC network consisted of 23 service centers. In FY 2010, the Postal Service implemented a reengineering plan to close eight of the 23 MTESCs to reduce the overall cost of MTE handling. To date, seven of eight MTESCs scheduled for closure have been closed, with the last remaining service center scheduled for closure in September 2010. An audit addressing the consolidation of the MTESC network is planned for FY 2011.

direction needing nationwide attention, including updating the MTE policies; allocating necessary resources to the field; and gaining visibility into MTE inventory outside of the MTESC network (which covers facilities, MTE in transit, and MTE at mailers and other external customers). We concluded the control weaknesses and ineffective management issues identified in the Pacific and Eastern areas were systemic and impacted all Postal Service areas. Therefore, we determined that additional Postal Service area audit work was unnecessary to address the issues nationwide.

We interviewed representatives from headquarters' Network Operations (Logistics – MTE) and Supply Management (MTE and Spare Parts). In addition, we reviewed national MTE policies and procedures and other documents, including the POM and the Postal Handbook PO-502. We also assessed the status and functionality of the MTEOR system, which is currently being considered to manage MTE. Additionally, we reviewed MTE purchases from FY 1999 to present to calculate an estimated on hand count of MTE by type, adjusting for useful life, condemnation and other variables.[8] Further, we estimated current MTE "rolling stock" inventory, much of which was purchased before FY 1999, based on scanning of Surface Visibility barcodes for a 12-month period.

We assessed the reliability of the computer-generated purchase data used in our analyses by reviewing existing information about the data. We determined that the data were sufficiently reliable for the purposes of this report even though we noted control weaknesses that constrained our work. For example, because there is no inventory system at plants, there was no way to readily determine the universe of MTE throughout the Postal Service. Further, our need to reconstruct an inventory going back 12 years made it difficult to obtain complete data files supporting MTE purchases; the files contained a large amount of records that were not organized by MTE type or by fiscal year purchased; and the files contained duplicate records of some MTE. Additionally, the Postal Service does not require that purchase data be labeled with MTE category classification numbers; therefore, we had to obtain additional clarification from headquarters for a number of MTE purchases. However, we compensated for control weaknesses and data limitations by applying alternate audit procedures including calculation and evaluation of unit costs and discussions with responsible officials.

We conducted this performance audit from March through September 2010 in accordance with generally accepted government auditing standards and included such tests of internal controls, as we considered necessary under the circumstances. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective. We discussed our observations and conclusions with management on August 31, 2010, and included their comments where appropriate.

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[8] During this audit, we gathered information on the cost and use of various cardboard containers used at Network Distribution Centers (NDCs) and P&DCs. However, we will address cardboard issues in a subsequent audit given that cardboard is more perishable than most MTE and has distinct issues and challenges.

PRIOR AUDIT COVERAGE

As reflected in the table below, the U.S. Postal Service Office of Inspector General (OIG) issued three audit reports since December 2008 addressing MTE management. Two of these audits covered the effectiveness of the Postal Service's management and control of MTE. We found the identified control weaknesses in the areas were caused, in part, by the lack of direction and policy from headquarters; the lack of a nationwide comprehensive inventory system for identifying and tracking all MTE; and insufficient MTE resources allocated to the area level.

Report Title	Report Number	Final Report Date	Monetary Impact	Report Results
Management of Mail Transport Equipment – Eastern Area	NL-AR-10-004	3/17/2010	$0	The Eastern area's effectiveness was limited over the management and control of MTE. Area officials did not always ensure adequate controls over inventory and accountability processes required by national MTE policies and procedures. Management agreed with our findings and recommendations.
Management of Mail Transport Equipment – Pacific Area	NL-AR-10-001	10/22/2009	$0	The Pacific area's management and control of MTE was ineffective. The area did not always ensure compliance with inventory and accountability processes nor ensure the safeguarding of assets. Management generally agreed with our findings and recommendations.
Radio Frequency Identification Technology: Asset Management	DA-AR-09-002	12/24/2008	$127 million	The Postal Service has opportunities to adopt Radio Frequency Identification Technology (RFID) to manage MTE inventories and minimize long-standing pallet losses. Management agreed with our findings and recommendations.[9]

In addition, the Postal Service has previously raised concerns and initiated MTE recovery efforts stemming from inadequate MTE inventory, accountability, and safeguarding. For example:

- The Postal Service estimates 3.5 million plastic pallets (with an estimated value of about $70 million) leaked from its network nationwide during the past several years. According to officials, these pallets were unaccounted for over the last few years and are missing from the nationwide network.

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[9] The Postal Service is no longer exploring RFID technology for pallets because of the Postal Service's current financial situation.

- ▪ Two Equipment Recovery Projects in November 2008 and November 2009 coordinated between the Postal Service and the Inspection Service resulted in the identification and recovery of more than 293,000 pieces of MTE nationally valued at about $3.2 million – most of which involved unauthorized use of MTE at external customers or unauthorized possession by other parties, such as recyclers or air cargo warehouses.

APPENDIX B: DETAILED ANALYSIS

Postal Service Headquarters could more effectively manage and control MTE nationwide. We determined that the Postal Service has not:

- Provided updated, comprehensive policy, guidance, and oversight that support current MTE operational requirements.

- Developed a nationwide comprehensive inventory system for identifying and tracking all MTE throughout the network and at mailers and for determining annual MTE purchase requirements.

- Ensured that areas have sufficient resources to monitor the management of MTE in the field or at mailers and to ensure appropriate compliance with national MTE requirements.

We determined that these systemic issues contributed to conditions identified in our prior MTE reviews in the Pacific and Eastern areas and impact MTE operations in all Postal Service areas. We also determined that if comprehensive controls over MTE had been in place at facilities and mailers, that the Postal Service could have spent about $29 million less for MTE in FYs 2008 and 2009. In addition, if comprehensive controls are established to account for and safeguard MTE assets, the Postal Service could better ensure that only needed MTE is purchased in the future. (See Appendix C for our calculation of the questioned costs.) Further, we estimate that about $897 million in MTE assets are at risk of loss, theft, and misuse because of the control weaknesses. These conditions also present a potential danger to public safety and security and reflect poorly on the Postal Service's brand and public image.[10] See Appendix D for our calculation of the assets at risk.

MTE National Policies and Enforcement

Postal Service Headquarters has not developed, updated, nor reinforced adequate and comprehensive national MTE policies. Specifically, Postal Service Headquarters issued national MTE policy and guidelines delineating headquarters, area, plant, and mailer responsibilities for MTE, which are contained in the POM, Chapters 57 through 59, and Postal Handbook PO-502, Container Methods. However, the national MTE policies have not been fully developed and updated[11] to reflect the existing Postal Service operating environment or operational requirements. Additionally, Postal Service Headquarters needs to take steps to ensure compliance in the field with all aspects of national MTE policy, including audits of MTE at mailers.

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[10] The essence of the Postal Service brand is customer perception and the control and management weaknesses above could pose a high risk for the public to negatively perceive the Postal Service's ability to properly manage, account for, and protect its assets.
[11] Based on our discussions with Postal Service officials, it is estimated that the policies have not been updated in nearly 20 years.

Key MTE responsibilities for Postal Service Headquarters are to:

- Ensure that an adequate national inventory of MTE exists and is properly managed.

- Establish procedures for the reporting of empty MTE inventories.

- Develop MTE purchase requirements.

- Coordinate with the field and enforce compliance with MTE policy.

- Establish guidelines for MTE audits of MTE operations and inventory levels at Postal Service facilities and mailers.

We found that Postal Service Headquarters did not always monitor or enforce area compliance with national MTE policies. As we reported in our prior audits, area DNOs did not always ensure compliance with national MTE policies covering inventory and accountability processes nor ensure MTE assets were always safeguarded. Further, Postal Service Headquarters has not monitored and enforced area compliance with critical MTE requirements, such as taking on-hand MTE volume counts; establishing accountability of MTE by tracking and reconciling MTE loaned to mailers; conducting audits of MTE at mailers and Postal Service facilities; and establishing policy to safeguard all MTE.

**Postal Service pallets used as bumpers to prevent wall damage
due to forklift traffic at the Santa Clarita P&DC, January 8, 2009.**

MTE Data and Limited Visibility

The Postal Service does not have a comprehensive nationwide system for identifying, counting, and tracking all MTE to provide for adequate visibility and to support area and local oversight responsibilities. Further, the Postal Service does not have consistent, standardized, and universal collection of MTE use and inventory data within Postal Service facilities and at mailers. As such, Postal Service headquarters does not have comprehensive information (i.e., MTESC network, facility and mailer data) for

forecasting and determining MTE purchase requirements annually. As a result, we estimate the Postal Service could have avoided spending about $14.5 million annually ($29 million total) for MTE in FYs 2008 and 2009.

Although there is no nationwide comprehensive system in place for identifying, counting, and tracking MTE, we determined that the Postal Service does have some visibility of MTE through the existing EIRS and the Mail Transport Equipment Support System (MTESS). However, these systems provide only limited visibility. In addition, the Postal Service has undertaken efforts to identify control weaknesses and to develop an automated management system to improve its visibility and control over MTE. However, action has not yet been taken to address the control weaknesses and implementation of an automated MTE management system, which is on hold.

On-hand Volume Count Process. The Postal Service can partially compensate for its lack of comprehensive MTE data and limited visibility by requiring MTE on-hand volume counts at Postal Service facilities and mailers. The Postal Service initially established a requirement for on-hand volume counts to enable the control and management of MTE by redistributing MTE from areas with a surplus to areas with a deficit. Postal Service headquarters determined that on-hand volume counts were no longer necessary with the implementation of the MTESC network around 1997, and decided to rely on data provided by the MTESC network for visibility into the MTE program.[12] However, Postal Service officials stated the MTESC network only accounts for a small percentage of MTE, and there is limited visibility of MTE outside of the MTESC network. Thus, the Postal Service concluded that they need an automated inventory management solution for tracking MTE at facilities and mailers.

MTESS. Postal Service headquarters' only visibility of MTE inventory is the MTESS. However, MTESS is limited in that it only tracks inventory physically in the possession of the MTESCs and does not provide visibility of MTE at facilities, with mailers and other customers, or in-transit. Although MTESS provides very limited visibility, it is the tool Postal Service headquarters uses to forecast and determine MTE purchase requirements annually.

Recent changes to the Postal Service's MTE handling policy will further reduce the amount of MTE processed by the MTESC network, thereby further narrowing the Postal Service's visibility obtained through MTESS. On November 9, 2009, the Postal Service issued a SOP covering the "reuse" of MTE at plants (processing facilities) and post offices (delivery units). The Postal Service stated that a critical component of the MTESC network reengineering is having plants and post offices "stack and reuse" MTE (such as letter trays, flat tubs, and sleeves). The stated goal of the SOP is to reduce the MTESC network's processing of these types of MTE by 50 percent. The instructions for

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[12] Some Postal Service areas, including the Pacific Area, still require on-hand inventory counts because of the limitations of the MTESC network inventory system. Further, the Postal Service is considering the reestablishment of the requirement for on-hand volume counts nationwide until an automated MTE management solution is developed and fully operational.

plants and post offices are for them to retain a week's inventory of specified MTE types and reuse this MTE rather than returning it for processing. Further, only damaged MTE or MTE in excess of the weekly needs of the facility, its customers, or other supported postal facilities should be returned to the processing facility or MTESC network, as applicable. As such, the Postal Service has and will continue to purchase more MTE than needed, because it does not have visibility of MTE at facilities and mailers and cannot ensure that only MTE needed to support operational requirements is purchased.

Asset Management Integration (AMI) Initiative. Recognizing opportunities to improve its planning and requirements analysis for all assets, including MTE, the Postal Service's Supply Management group undertook the AMI initiative in November 2005. The goal of AMI was to improve the management of inventory and assets, including MTE, to enhance service and reduce costs. The AMI analysis concluded the following as it relates to MTE:

- Demand planning and supply planning processes were either manual or did not exist.

- Technology improvement opportunities existed, including implementing an inventory management solution for tracking MTE that is not at MTESCs (for example, tracking MTE at facilities and mailers), and implementing a demand planning solution to assist in forecasting and data gathering of MTE requirements.

- The Postal Service could reduce MTE purchase costs by 10 to 20 percent annually through MTE management by improving MTE planning and reducing procurement costs.

Although the AMI identified significant control weaknesses corrective action resulting from the initiative has not yet been taken or implemented.

Automated MTE Management System. To address its continued lack of MTE inventory management, controls, and visibility, Postal Service Headquarters has been exploring an automated MTE management system. One option being explored is the MTEOR system,[13] and a more recent option is the SEAM system.[14] Whether the Postal Service pursues MTEOR, SEAM, or some other form of an automated MTE management system, the planned functionality should include tracking MTE at Postal Service facilities and mailers, reconciliation of MTE loaned to mailers, and a requirement to include

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[13]The Postal Service started exploring the development of the MTEOR system in FY 2008. The Postal Service put the MTEOR system initiative on hold in April 2009 because of the Postal Service's financial condition. The Postal Service re-initiated development of the MTEOR system in FY 2010, but is now looking at other system options.

[14] SEAM is a commercial-off-the-shelf application designed to provide centralized asset and warehouse capacity tracking and visibility. It will provide the Postal Service with functional modules that support fulfillment, planning, and service management of all Postal Service inventory and assets. Phase I of SEAM will be implemented over a 3-year period starting in FY 2009. The Postal Service is currently looking at whether SEAM should be expanded to cover the needed MTE tracking and reconciliation information.

recording of MTE on-hand volume at plants and mailers. The Postal Service's planned automated MTE management system has been delayed, leading to continued limited visibility into MTE internally and at mailers, and resulting in continued purchase of MTE in excess of what is needed to support operations.

MTE Management and Monitoring

Areas do not have sufficient resources to monitor the management of MTE in the field or at mailers and to ensure appropriate compliance with national MTE requirements. The Postal Service's eight areas, through their DNOs, are responsible for ensuring compliance with Postal Service MTE policy at the field level. The area DNOs are required to provide guidance to the facilities and each facility is responsible for daily management of its MTE, ensuring compliance with all national policies. Further, the area DNOs are responsible for conducting and monitoring MTE use at mailers and facilities, including conducting audits.

We concluded from our audits of the Pacific and the Eastern areas that the management and oversight over the MTE was ineffective. The facility managers did not always provide sufficient priority, resources, training, and oversight. In addition, management did not assign sufficient resources to monitor MTE activities and compliance with POM requirements and fully address all necessary controls over MTE. We confirmed the lack of oversight during our fieldwork. For example, we observed or were advised of the potential unauthorized possession and improper use of Postal Service MTE by other external parties, including

- One company that had about 250 Postal Service plastic pallets in its yard, that were exposed to elements. It appeared from the company type that there was not an authorized use of the pallets, and the Postal Service subsequently recovered the pallets.

- A national trucking company was picking up plastic pallets for a national retailer. Postal Service officials stated they were advised that a retailer was using the pallets to transport merchandise from its main distribution center to some of its retail stores. Over a 6-month period, the transportation company went to the plant at least five times to pick up anywhere from 500 to 900 pallets.

The area DNO offices are unable to manage and monitor compliance of MTE due to the lack of dedicated resources to oversee these responsibilities. The POM identifies in section 587.1 that Area Mail Transport Equipment Specialist position was established to ensure compliance with all aspects of MTE policy at the field level. These positions - one in each area - would provide guidance to the DNOs and other field units in all aspects of the MTE Program. These positions have been abolished by headquarters for a number of years now, and no other position was established to oversee these MTE responsibilities. Further, with recent reductions in DNO staffing due to the Postal Service's financial position, areas have to assign these MTE responsibilities to a

reduced staff as collateral duties. In addition, headquarters' did not ensure these duties and responsibilities were assigned or absorbed by another position within the area DNO's office.

APPENDIX C: MONETARY IMPACT

Finding	Impact Category	Amount
1	Unrecoverable Questioned Costs[15]	$29,058,088

The OIG identified $29,058,088 in unrecoverable questioned costs as calculated in the table below.

Table 1: Questioned Cost Calculations

Description	2008	2009	Total
MTE Purchases (excluding Postal Paks[16])	$72,347,418	$72,943,023	$145,290,441
Estimated percentage of avoidable MTE purchases	20%	20%	20%
Questioned Costs	**$14,469,484**	**$14,588,604**	**$29,058,088**

We calculated the unrecoverable questioned costs based on the following methodology and assumptions:

- We identified, through Postal Service's Supply Management purchase data, total MTE purchases for the last two complete fiscal years, covering 2008 and 2009.

- We relied on the Postal Service's analysis and estimate of the percentage of avoidable MTE purchases annually from its AMI project if comprehensive controls were in place to enhance MTE asset management and prevent MTE from being lost or misused. We used the AMI project's 20 percent estimate even though the actual percentage of avoidable purchases for some MTE categories, such as plastic pallets, is significantly more than 20 percent because of the ongoing issues with leakage. Our use of the AMI 20 percent estimate resulted in a more conservative questioned cost amount than if we considered the actual leakage rate for some categories, such as plastic pallets.

- Although we did not consider the additional AMI costs covering MTESC network handling, processing and transportation costs related to the purchase of MTE in excess of operational requirements, the Postal Service recognized that there were additional MTE-related costs and, therefore, additional MTE savings opportunities.

- Postal Paks and other cardboard containers have been removed from our calculation of total purchased MTE and will be addressed in a separate audit.

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[15] Unrecoverable costs that are unnecessary, unreasonable or an alleged violation of law or regulation.
[16] The Postal Service uses cardboard boxes of varied sizes and strength specifications to process and transport mail. One type of cardboard box is the Postal Pak which is typically used by Network Distribution Centers.

APPENDIX D: NON-MONETARY IMPACT

Finding	Impact Category	Amount
1	Assets at Risk[17]	$897,254,288
1	Goodwill/Branding[18]	0

The OIG identified $897,254,288 in assets at risk as calculated in the table below.

Table 2: Assets at Risk Calculations

Category	MTE	Low Risk Deduction	Useful Life Deduction	Condemnation Deduction	Total Potential Assets at Risk
Multi-Purpose Mail Containers (A)[19]	$239,897,617	$0	$0	$0	$239,897,617
Over-the-road containers (A)	221,124,880	0	0	0	221,124,880
Pallets (B)[20]	270,069,844	0	48,733,139	3,900,257	217,436,449
Trays/Tubs (B)	159,791,151	31,754,971	48,230,064	1,354,024	78,452,092
Hampers (A)	51,431,832	0	0	0	51,431,832
Other (Con-Cons, Carts) (A & B)	185,228,884	132,380,017	1,507,000	964,334	50,377,533
Wire Containers (A)	38,533,885	0	0	0	38,533,885
Sacks (B)	48,800,250	48,800,250	$0	$0	$0
Sleeves (B)	25,582,547	25,582,547	0	0	0
Total Potential Assets at Risk	**$1,240,460,890[21]**	**$238,517,784**	**$98,470,203**	**$6,218,615**	**$897,254,288**

We calculated the assets at risk based on the following methodology and assumptions:

- The Postal Service classifies annual MTE purchases as an expense for financial reporting purposes. However, the Postal Service considers MTE as an operational asset for non-accounting purposes since it is "an item the Postal Service must purchase and inventory for the fulfillment of external or internal customer needs."

- We identified assets at risk as being the estimated value of all MTE by type, including rolling stock. To accomplish this, we gathered purchase data from FYs 1999 through 2010. As rolling stock was not generally purchased in the last 12

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[17] Assets that are at risk of loss because of inadequate internal controls.

[18] An actual or potential event or problem that could harm the reputation of the Postal Service.

[19] Source (A) - quantity information was obtained from scans of unique Surface Visibility (SV) bar codes for 1year. SV is a technology system that enables the tracking of mail volume between processing plants by scanning bar -coded rolling stock and other MTE.
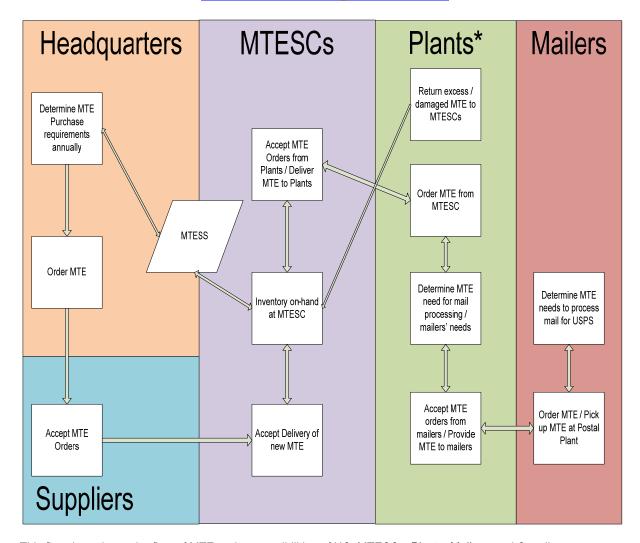
[20] Source (B) - information was obtained from MTE purchase data

[21] The total assets were estimated by reconstructing the data during our audit review due to limitations and insufficient records at the Postal Service. We estimated the value of purchased MTE over the last 12 years to be $688,202,441 based on a review of available purchase data. Additionally, we estimated the "rolling stock" inventory to be about $552,258,449 based on an analysis of Surface Visibility equipment bar code scans over a 12-month period.

years, we estimated the value of rolling stock by collecting unique scanned bar code data from Surface Visibility.

▪ In determining what percentage of MTE purchases were at risk, we removed items, which exceeded their useful life, and items we considered to have low risk of loss, theft, or misuse. To be conservative in our estimate of assets at risk, we also reduced our calculated total by a condemnation percentage, which is based on the amount of equipment the MTESCs remove from service each year due to being damaged or beyond service life.

▪ Postal Paks have been removed from our calculation of total purchased MTE and will be addressed in a separate audit.

▪ Based on our audit observations on MTE misuse and misappropriation, Postal Service experience with MTE "leakage" and the Inspection Service's asset recovery projects, we consider all assets in at risk categories to be at risk of loss, theft, or misuse.

APPENDIX E: MTE FLOWCHART

Headquarters	MTESCs	Plants*	Mailers

- Determine MTE Purchase requirements annually
- Order MTE
- MTESS
- Accept MTE Orders from Plants / Deliver MTE to Plants
- Inventory on-hand at MTESC
- Accept Delivery of new MTE
- Return excess / damaged MTE to MTESCs
- Order MTE from MTESC
- Determine MTE need for mail processing / mailers' needs
- Accept MTE orders from mailers / Provide MTE to mailers
- Determine MTE needs to process mail for USPS
- Order MTE / Pick up MTE at Postal Plant

Suppliers

- Accept MTE Orders

This flowchart shows the flow of MTE and responsibilities of HQ, MTESCs, Plants, Mailers, and Suppliers. An understanding of the data shown in this flowchart was gained from work and research related to the following audits: Management of MTE – Pacific Area; Management of MTE – Eastern Area; and Management of MTE – National Analysis. In addition to showing the flow of MTE and responsibilities of relevant entities, this flowchart shows that HQ currently relies solely on MTESS for visibility of MTE at MTESCs to determine MTE requirements. Until the proposed automated MTE management system is developed and implemented and the POM is revised and enforced, HQ does not have visibility of MTE at Postal Plants and their Mailers, or of MTE in-transit.

*Certain large Mailers order and receive delivery of MTE directly from MTESC, in the same manner as Postal plants .

APPENDIX F: MANAGEMENT'S COMMENTS

UNITED STATES POSTAL SERVICE

September 27, 2010

Lucine M. Willis
Director, Audit Operations
1735 North Lynn Street
Arlington, VA 22209-2020

SUBJECT: Draft Audit Report - Management of Mail Transport Equipment –
                National Analysis (Report Number NL-AR-10-DRAFT)

Thank you for the opportunity to review and comment on the subject draft audit report. The Postal Service appreciates the effort put into this report and the recommendations made.

Overall, management agrees with the recommendations provided.

Recommendation 1:
Further develop, update and reinforce national Mail Transport Equipment (MTE) policies and procedures contained in the *Postal Operations Manual* and the Postal Handbook PO-502, *Container Methods*, which address MTE inventory and accountability controls, including validating customer MTE needs as well as tracking and reconciling MTE loaned to mailers and other external customers.

Management Response
Network Operations is currently in the process of updating both of these manuals. This update is planned for publication by the end of Quarter II, fiscal year (FY) 2011.

Recommendation 2:
Continue pursuing implementation of a planned automated Mail Transport Equipment (MTE) management system and ensure its functionality for inventory and accountability processes and for enhancing the Postal Service's visibility into MTE internally and at mailers.

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- 2 -

<u>Management Response</u>
Network Operations has developed the requirements for an MTE online ordering and fulfillment system. The Postal Service is exploring the best method to implement this solution. This assessment will be completed by the end of Quarter II, FY 2011.

<u>Recommendation 3</u>:
Reestablish an on-hand Mail Transport Equipment (MTE) volume count process, both internally and externally, until an automated MTE management system is fully developed, deployed, and operational.

<u>Management Response</u>
Network Operations is in the process of re-establishing the Equipment Inventory Reporting System (EIRS) reporting requirements for Postal facilities. The targeted completion date is January 1, 2011. External visibility is tied to the development of an online ordering and fulfillment system (referenced in recommendation 2 response). This assessment will be completed by the end of Quarter II, FY2011.

<u>Recommendation 4</u>:
Ensure that area Distribution Networks Offices have appropriate resources assigned responsibly to monitor and manage Mail Transport Equipment, and maintain compliance with *Postal Operations Manual* requirements.

<u>Management Response</u>
The update of the *Postal Operations Manual* (POM) will address the roles and responsibilities of local, area, and headquarters staff. This update of the POM is scheduled for publication by the end of Quarter II, FY2011.

<u>Recommendation 5</u>:
Document the current process for identifying annual, routine Mail Transport Equipment (MTE) purchase requirements, and ensure the process includes Mail Transport Equipment Service Center network information and facility and mailer inventory data, to ensure that only the necessary amount of MTE is purchased.

<u>Management Response</u>
The Postal Service has an extensive process to determine purchased MTE requirements, which includes analyzing historical customer ordering data along with examining condemnation rates, new deliveries of product, production rates at Mail Transport Equipment Service Centers, current inventory levels and leakage. The addition of EIRS data will enhance this process. The determination whether the Postal Service will pursue the external component of on-hand inventory reporting, will be made by the end of Quarter II, FY2011.

- 3 -

We do not agree with the methodology used to determine the estimated value of MTE purchased that was not needed. However, we agree that increased inventory visibility will provide greater control of our assets.

We have reviewed the audit report and do not believe that any portion of the document requires exemption from disclosure under the Freedom of Information Act (FOIA).

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Supply Management

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