



OFFICE OF INSPECTOR GENERAL

UNITED STATES POSTAL SERVICE

Contract Postal Units

Audit Report

Report Number
DR-AR-15-001

November 13, 2014



Hours of Operation

Monday - Friday	8:00am - 5:00pm
Saturday	8:00am - 5:00pm
Sunday	Closed
Holiday	Closed

Collection Times

Monday - Friday	11:45 am - 4:45 pm
Saturday	4:00 pm
Sunday	No Collection
Holiday	No Collection

Expedited Services
Certified/Registered Mail
Insured Mail





OFFICE OF INSPECTOR GENERAL

UNITED STATES POSTAL SERVICE

Highlights

Officials did not always conduct annual evaluations or assess contract types to optimize revenue performance.

The Postal Service could save an estimated \$2,324,403 by improving oversight and converting CPU firm-fixed-price contracts.

Background

A Contract Postal Unit (CPU) is a Postal Service retail unit located inside a private business and operated by nonpostal employees. CPU suppliers operate under either a firm-fixed-price or performance-based contract to provide a range of retail products and postal services. Management prepares revenue forecast and cost estimates to determine contract type. CPU services include selling stamps and providing domestic mailing services such as First-Class Mail. In fiscal year (FY) 2013, over 2,700 CPUs generated about \$539 million.

Postal Service policy requires officials to evaluate CPUs annually to ensure they are cost effective and increase the return on investment. Officials should mainly consider performance-based/automated CPUs with annual revenue of less than \$100,000. The evaluations should identify non-productive CPUs, changing market conditions, and return on investment.

Our objective was to assess CPUs' revenue performance for FYs 2011 through 2013.

What The OIG Found

An average of 98 percent of CPUs reviewed either broke even

or generated a positive cash flow during the past 3 fiscal years. However, an average of 2 percent of CPUs (49 of 2,337) had a negative cash flow totaling \$1,257,742. Further, 469 CPUs generated less than \$100,000 in annual revenue for the 3 fiscal years reviewed.

Officials did not always conduct annual evaluations or assess contract type to optimize revenue performance. The Postal Service could save an estimated \$2,324,403 by improving oversight and converting firm-fixed-price CPUs, where cost effective, to performance-based CPUs.

We also informed management that payments were made totaling \$160,425 to one CPU supplier for 1 year after the contract termination date. District and Category Management Center officials did not stop contract payments. The Postal Service and the supplier negotiated a settlement of \$112,506, which the Postal Service received on June 11, 2014.

What The OIG Recommended

We recommended the vice president, Retail and Customer Service Operations, conduct annual evaluations and convert firm-fixed-price CPU contracts to performance-based contracts when it is cost effective.

Years Studied **2011** **2012** **2013**

CONTRACT POSTAL UNIT

A Contract Postal Unit (CPU) is a Postal Service retail unit located inside a private business and operated by nonpostal employees.



In fiscal year (FY) 2013, over 2,700 CPUs generated about \$539 million.

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of CPUs broke even or generated a positive cash flow during the past 3 fiscal years.

2% of CPUs (49 of 2,337) had a negative cash flow totaling \$1,257,742.

469 CPUs generated less than \$100,000 in annual revenue for the 3 fiscal years reviewed.



The Postal Service could save an estimated \$2,324,403 by improving oversight and converting firm-fixed-price CPUs, where cost effective, to performance-based CPUs.

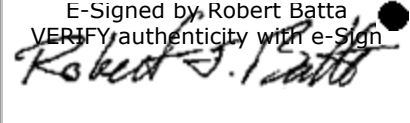
Transmittal Letter



OFFICE OF INSPECTOR GENERAL
UNITED STATES POSTAL SERVICE

November 13, 2014

MEMORANDUM FOR: KELLY SIGMON
VICE PRESIDENT, RETAIL AND CUSTOMER SERVICE
OPERATIONS

E-Signed by Robert Batta
VERIFY authenticity with e-Sign


FROM: Robert J. Batta
Deputy Assistant Inspector General
for Mission Operations

SUBJECT: Audit Report – Contract Postal Units
(Report Number DR-AR-15-001)

This report presents the results of our audit of Contract Postal Units
(Project Number 13XG044DR000).

We appreciate the cooperation and courtesies provided by your staff. If you have any
questions or need additional information, please contact Rita F. Oliver, director, Delivery
and Post Office Operations, or me at 703-248-2100.

Attachment

cc: Corporate Audit and Response Management

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Findings

On average, 98 percent of CPUs reviewed broke even or generated a positive cash flow. An average of 2 percent of the CPUs had a negative cash flow, totaling \$1,257,742.

Introduction

This report presents the results of our self-initiated audit of Contract Postal Units (CPU)¹ (Project Number 13XG044DR000). Our objective was to assess CPU revenue performance. See [Appendix A](#) for additional information about this audit.

CPUs are located inside private businesses and operated by the businesses' employees. CPU suppliers operate either under a firm-fixed-price² or a performance-based³ contract to provide the public with access⁴ to postal services at U.S. Postal Service prices (see [Appendix B](#) for a comparison of performance-based and firm-fixed-price contracts). Postal services include selling stamps and money orders, renting out Post Office (PO) boxes, and providing domestic mailing services, such as Priority Mail, First-Class Mail, and Parcel Post.⁵ The Postal Service reported that over 2,700 CPUs generated revenue of about \$539 million in fiscal year (FY) 2013.⁶ Postal Service policy⁷ requires officials to evaluate CPUs annually to ensure they are cost effective.

Conclusion

An average of 98 percent of CPUs we reviewed either broke even or generated a positive cash flow⁸ during the past 3 fiscal years; however, an average of 2 percent of CPUs had a negative cash flow, totaling \$1,257,742. Further, 469 CPUs generated less than \$100,000 in annual revenue for the 3 fiscal years reviewed. These conditions occurred because officials did not consistently conduct annual CPU revenue performance evaluations or assess contract type to optimize revenue performance. The Postal Service could save an estimated \$2,324,403 by improving oversight and converting CPU firm-fixed-price contracts, where cost effective, to performance-based contracts.

We also informed management that the Postal Service made payments totaling \$160,425 to one CPU supplier for 1 year after the contract termination date. District and Category Management Center officials did not coordinate to stop contract payments. The Postal Service and the supplier negotiated a settlement of \$112,506, which the Postal Service received on June 11, 2014.

Contract Postal Units

Overall, CPU revenue performance was adequate, with an average of 98 percent of CPUs breaking even or generating a positive cash flow during the past 3 fiscal years (see [Table 1](#)).

¹ In the FY 2013 *Annual Report*, the Postal Service reported on 2,718 CPUs, including CPUs that were only open for 1 day. U.S. Postal Service Office of Inspector General (OIG) analysis from the Contract Postal Unit Technology (CPUT) system identified 2,581 CPUs as of August 2013.

² Firm-fixed-price CPU contracts stipulate a fixed annual amount to the supplier over a 12-month period. Compensation does not depend on the amount of revenue the CPU generates.

³ Performance-based CPU contracts pay the supplier for revenue generated from the sale of Postal Service products and services. This compensation can consist of a percentage of all the revenue, a split percentage of all the revenue, or a fixed flat monthly fee and a percentage of stipulated revenue.

⁴ We removed village post offices, fee for service, public service, and seasonal CPUs because their basic function in the CPU program is to provide access and universal service to customers.

⁵ Extra services such as Certified Mail, Collect on Delivery (COD), Confirm, USPS Tracking, Insured Mail, Registered Mail, Restricted Delivery, Return Receipt, Return Receipt for Merchandise, Signature Confirmation, and Special Handling are also sold.

⁶ The Postal Service's *Five-Year Business Plan* established a plan for increasing alternative access retail revenue from 40 to 60 percent by FY 2017. In FY 2013, the Postal Service established a 45 percent goal for alternative channel access revenue. Alternative channel access is a customer access point to postal products and services such as Automated Postal Center kiosks; CPUs; USPS.com; Stamps on Consignment; Stamps by Mail service; and USPS Approved Shipper. As of April 2014, 41 percent of the Postal Service's retail revenue came from alternative channel access.

⁷ Postal Service policy requires management to evaluate all CPUs annually and particularly consider those with annual revenue less than \$100,000 (Postal Service Publication 156, *Guide to Contract Postal Units for Postal Service Employees*, Section 10.3.5.1, updated January 2014). Postal Service officials indicated that while it might appear that the criteria apply to all CPUs, this evaluation factor only applies to automated CPUs.

⁸ A timeline that shows the anticipated flow of investments, costs, and savings.

On average, 34 percent of automated CPUs generated less than \$100,000 in annual revenue.

Table 1: Positive Cash Flow Analysis

FY	CPUs With Positive Cash Flow/Break Even	Positive Cash Flow/Break Even Percentage	Universe⁹ of CPUs
2011	2,295	98%	2,337
2012	2,289	98%	2,337
2013	2,279	98%	2,337
Average	2,288	98%	2,337

Source: OIG analysis of CPUT system data as of August 2013.

The remaining 2 percent of CPUs had a negative cash flow for FYs 2011 through 2013 (see Table 2).

Table 2: Negative Cash Flow Analysis¹⁰

FY	Number of CPUs	Percentage of CPUs	Revenue	Payment	Profit/(Loss)	Universe of CPUs
2011	42	1.80%	\$721,416	\$1,056,863	(\$335,447)	2,337
2012	48	2.05%	890,040	1,316,971	(426,931)	2,337
2013	58	2.48%	707,447	1,202,811	(495,364)	2,337
Total	148		\$2,318,904	\$3,576,646	(1,257,742)	

Source: OIG analysis of CPUT system data as of August 2013.

In addition, we evaluated the CPUs using the specified evaluation factor outlined in Postal Service policy.¹¹ We found that an average of 34 percent of automated CPUs (or 469) generated less than \$100,000 in annual revenue for the 3 fiscal years we reviewed¹² (see Table 3).

Table 3: CPU Revenue Analysis

FY	Universe of CPUs	Revenue Greater Than \$100,000		Revenue Less Than \$100,000	
		Number	Percentage	Number	Percentage
2011	1,280 ¹³	885	69%	395	31%
2012	1,390 ¹⁴	926	67%	464	33%
2013	1,439	891	62%	548	38%
Average	1,370	901	66%	469	34%

Source: OIG analysis of CPUT system data as of August 2013.

⁹ The number of CPUs fluctuates; therefore, for our analysis we performed a comprehensive review of CPUs active as of August 2013. Our original universe was 2,581 CPUs. We subsequently removed village post offices, fee for service, public service, seasonal, and terminated CPUs to arrive at 2,337 facilities.

¹⁰ Revenue and payment totals may vary slightly due to rounding.

¹¹ Publication 156.

¹² We applied this evaluation factor to CPUs using the automated Contract Access Retail System (CARS) to report revenue. We eliminated the 901 CPUs that reported revenue via the non-automated system, Postal Service (PS) Form 1412, Financial Reporting. Thus, there were 1,439 CPUs that reported revenue via CARS.

¹³ Revenue and payment data were not shown for 159 CPU suppliers.

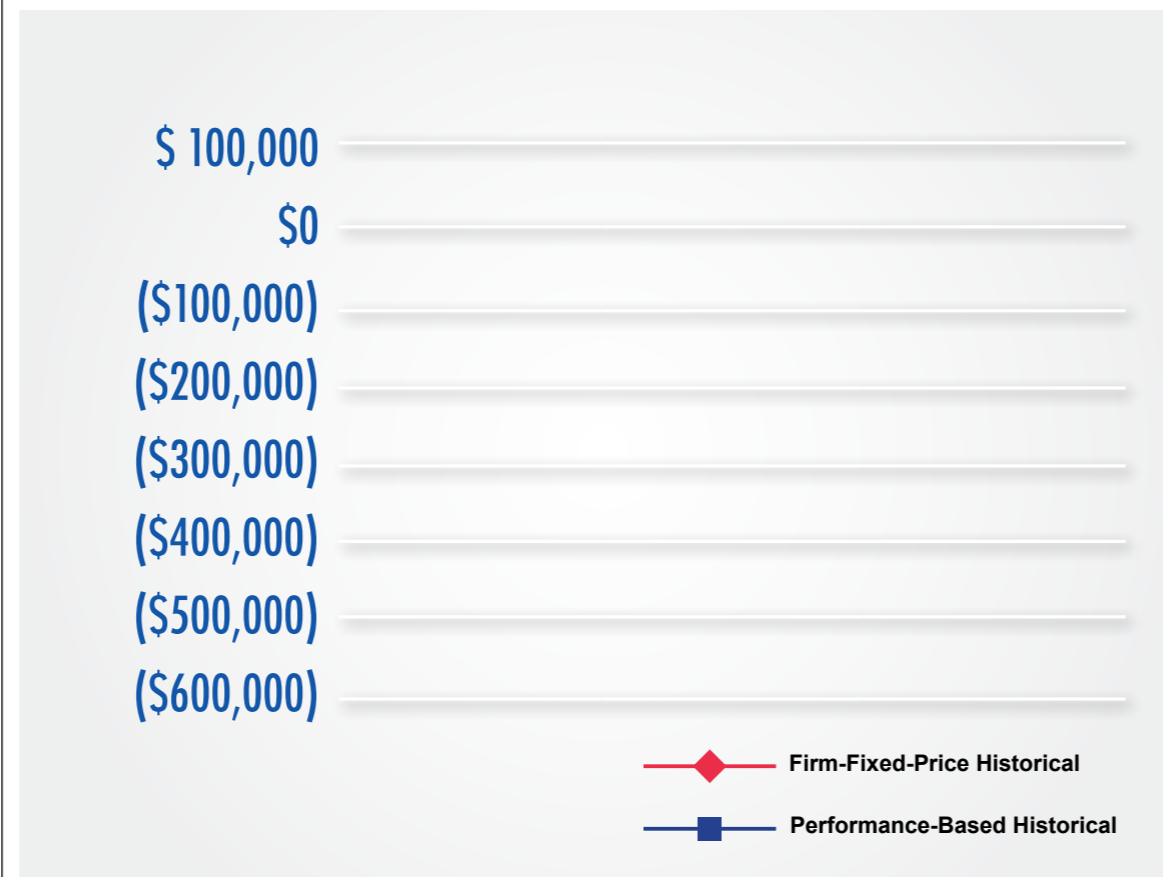
¹⁴ Revenue and payment data were not shown for 49 CPU suppliers.

District personnel did not conduct annual revenue performance evaluations or assess contracts to modify and optimize revenue performance.

These conditions occurred for several reasons:

- District personnel did not conduct annual revenue performance evaluations in the seven districts¹⁵ we reviewed. This occurred for various reasons. One official stated their focus was primarily on opening new CPUs and providing access to developing communities. Another official cited limited resources. Several officials stated they only conducted annual revenue performance evaluations after CPU suppliers requested increased contract fee payments.¹⁶
- Officials did not always assess contracts to modify and optimize revenue performance. However, our analysis of 70 CPUs with revenue loss showed revenue for CPU suppliers with performance-based contracts improved between FYs 2011 and 2013 while revenue for firm-fixed-price contract CPUs steadily declined (see Figure 1).

Figure 1: Analysis of CPUs with Revenue Loss



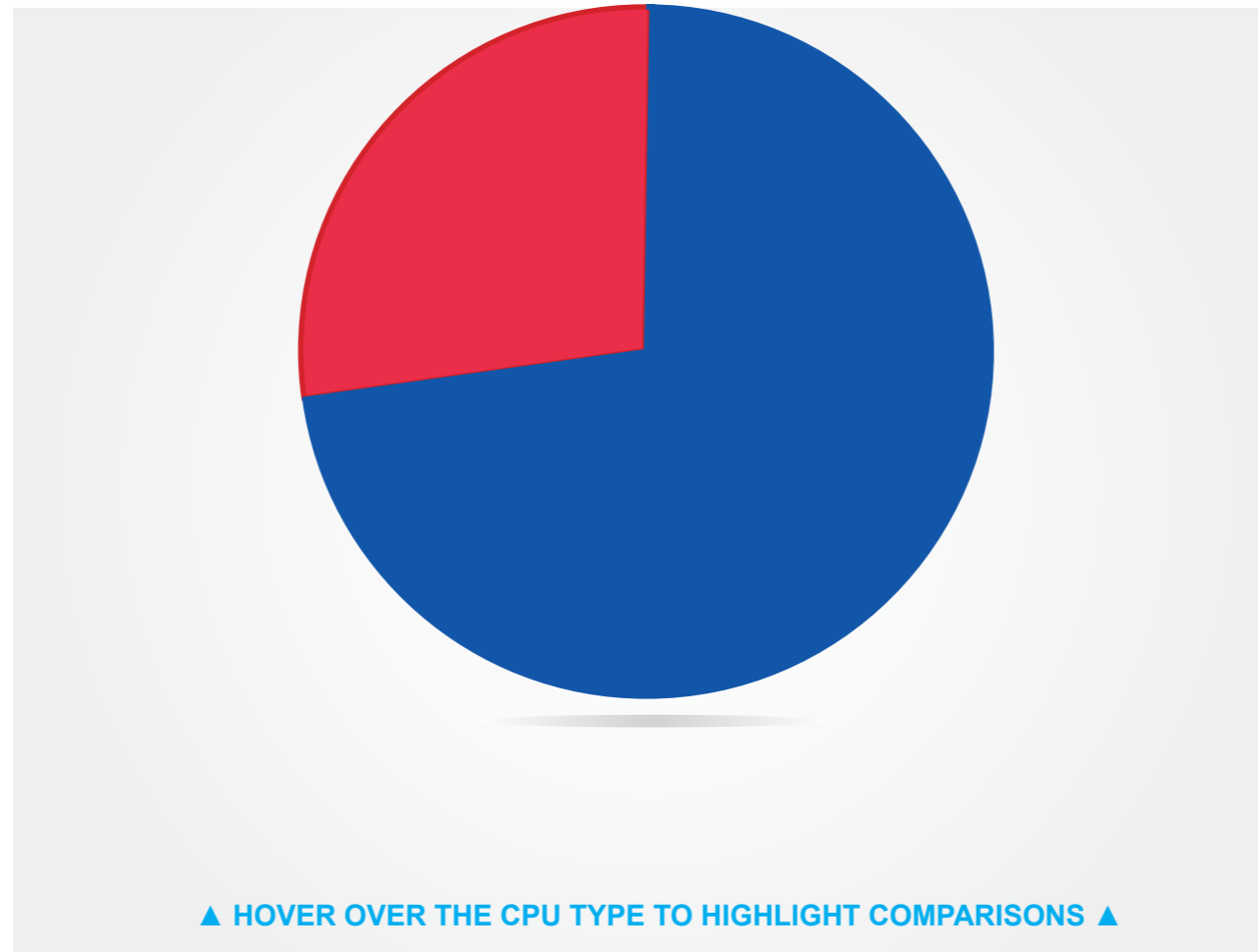
Source: OIG analysis of CPUT system data as of August 2013.

Additionally, 73 percent of these CPUs (or 51) with losses for the fiscal years reviewed were firm-fixed-price contracts and 27 percent of the CPUs (or 19) were performance-based contracts (see Figure 2).

¹⁵ We judgmentally selected the Arizona, Central Illinois, Mid-Carolinas, Northern New England, Northern Ohio, Sacramento, and Suncoast districts so we would cover all seven Postal Service areas.

¹⁶ The Sacramento District did not conduct annual revenue reviews; however, the Pacific Area implemented a Lean Six Sigma study to identify high-cost, non-productive CPUs. The area plans to transition firm-fixed-price contracts to other expanded access channels that are more cost effective for the Postal Service.

Figure 2: CPU Contract Type with Revenue Loss



Source: OIG analysis of CPUT system data as of August 2013.

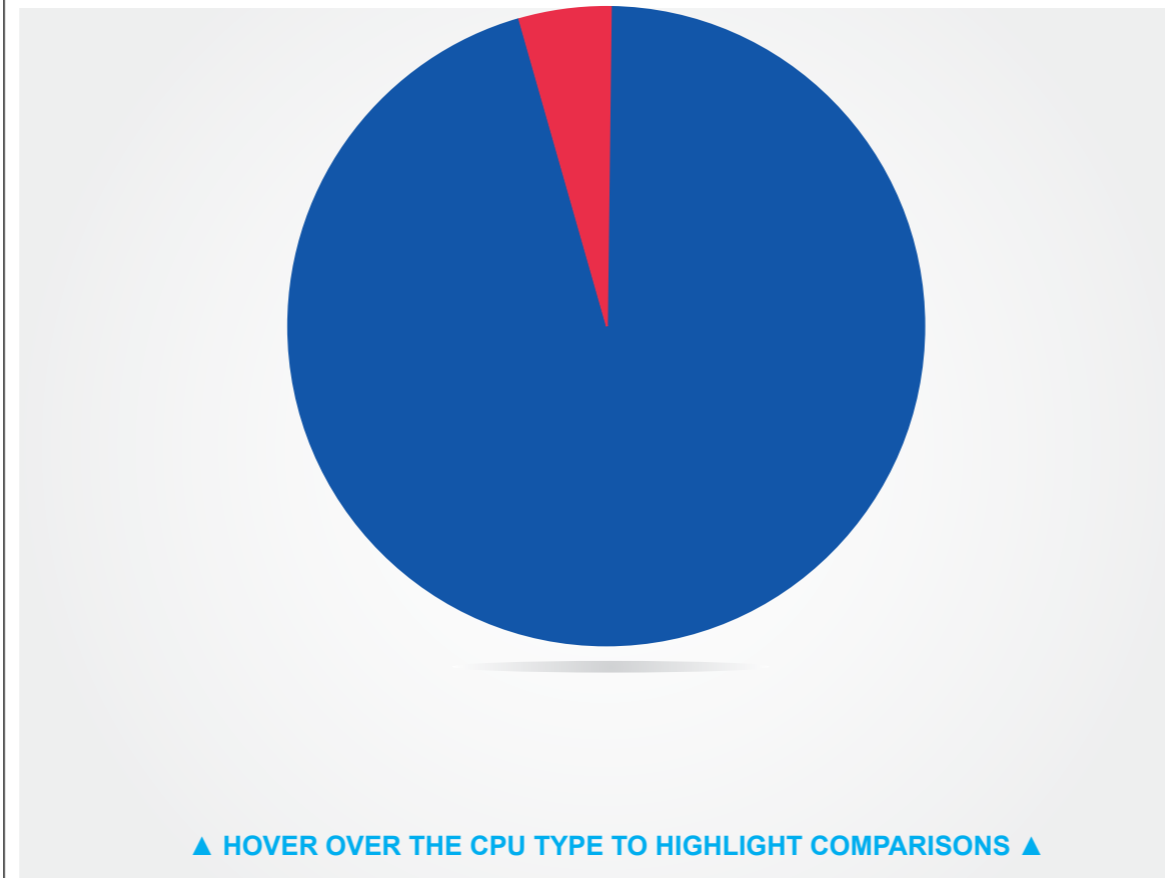
Further, 97.2 percent of firm-fixed-price CPU contracts contributed to revenue loss, while 2.8 percent of performance-based CPU contracts contributed to revenue loss (see Figure 3).

Specifically:

- 32 of 70 CPU suppliers (46 percent) had losses in all 3 years, ranging from \$283 to over \$269,000 annually for each CPU.
- 14 of 70 CPU suppliers (20 percent) had losses for 2 years, ranging from \$125 to over \$74,000 per CPU annually.
- 24 of 70 CPU suppliers (34 percent) had losses in 1 year, ranging from \$27 to over \$15,000 per CPU annually.

Figure 3: Contribution to Revenue Loss

The Postal Service made payments totaling \$160,425 to one non-productive CPU supplier for 1 year after the contract termination date.



Source: OIG analysis of CPUT system data as of August 2013.

Publication 156 requires officials to evaluate CPUs annually to ensure they are cost effective. The reviews should identify non-productive CPUs,¹⁷ changing market conditions, and increasing return on investment.

The Postal Service could save an estimated \$2,324,403 by improving oversight and converting CPU firm-fixed-price contracts, where cost effective, to performance-based contracts.

Other Matters

We also informed management that the Postal Service made payments totaling \$160,425 to one non-productive CPU supplier for 1 year after the contract termination date in July 2012.¹⁸ District and CMC officials did not coordinate to stop contract payments. Postal Service officials and the CPU supplier negotiated a settlement totaling \$112,506. The Postal Service received the settlement amount on June 11, 2014; therefore, we are not making a recommendation regarding this issue.

¹⁷ According to Postal Service Supply Management officials, non-productive CPUs do not generate substantial revenue or are no longer needed. The CPUT system is unable to identify non-productive CPUs; therefore, CPUs must be evaluated individually.

¹⁸ We plan to refer this issue to data analytics for further analysis.

Recommendations

We recommend management conduct annual evaluations and convert firm-fixed-price CPU contracts to performance-based contracts when it is cost effective.

We recommend the vice president, Retail and Customer Service Operations:

1. Conduct annual evaluations of contract postal units to ensure they are cost effective.
2. Convert firm-fixed-price contracts for contract postal units, where cost effective, to performance-based contracts to optimize revenue performance.

Management's Comments

Management agreed with the findings, recommendations, and monetary impact.

Regarding recommendation 1, management stated that annual evaluations of firm-fixed-price and performance-based contracts are a valuable tool which will allow CPUs to achieve their program and revenue goals at the best value. Management stated they will work with the Denver Category Management Center team, San Mateo Contract Postal Unit Technology Information Technology team, and area and district officials to develop a process and tools to review, analyze, and recommend changes to specific supplier contracts. Management has a target implementation date of FY 2015, Q3.

Regarding recommendation 2, management stated that when they complete annual evaluations and periodic reviews of firm-fixed-price contracts, they will convert firm-fixed price contracts to optimize revenue performance. Management stated the conversions will occur where practical and mutually agreeable by the host district. Management has a target implementation date of FY 2015, Q3.

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

Evaluation of Management's Comments

The OIG considers management's comments responsive to the recommendations in the report. The OIG considers both 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.

Appendices

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Appendix A: Additional Information

Background

A CPU is a postal unit that is located inside a private business and operated by the businesses' employees. CPUs are under contract and generally provide a broad range of retail products and postal services to customers. Services include selling stamps and money orders, renting out PO boxes, and providing domestic mailing services such as Priority Mail, First-Class Mail, and Parcel Post.

Suppliers are compensated through either a firm-fixed-price or a performance-based contract to provide the public with access to postal services at Postal Service prices. Postal Service officials prepare a revenue forecast and estimate the cost to determine the type of contract to award. These contracts are valid for an indefinite period; however, CPU contracts specify that either the operator or the Postal Service can terminate the contract and close the CPU at any time within 120 days of a termination notice.

In FY 2013, the Postal Service reported that over 2,700 CPUs generated revenue of about \$539 million. The Postal Service's *Five-Year Business Plan* established a plan to increase alternative access retail revenue from 40 to 60 percent by FY 2017. In FY 2013, the Postal Service established a 45 percent goal for alternative channel access revenue and, as of April 2014, 41 percent of the Postal Service's retail revenue came from alternative channel access.

Objective, Scope, and Methodology

Our objective was to assess CPU revenue performance. Our audit scope included CPU operations in effect from FYs 2011 through 2013. The OIG analyzed the CPUT system as of August 2013. Specifically, we:

- Reviewed policies and procedures and Delivery, Results, Innovation, Value, and Efficiency Initiative 3, Transforming Access for CPUs.¹⁹
- Interviewed Postal Service Headquarters Retail Channel Operations, Supply Management, and district retail officials regarding CPU processes and procedures.
- Analyzed payment and revenue data for 2,581 CPUs from the CPUT system. We identified 70²⁰ firm-fixed-price and performance-based CPU contracts with Postal Service payments greater than the revenue generated for 1 or more of the 3 years reviewed.

We conducted this performance audit from September 2013 through November 2014, 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 finding and conclusions based on our audit objective. We discussed our observations and conclusions with management on September 18, 2014, and included their comments where appropriate.

We relied on the revenue and payment data reported in the CPUT system. We performed a limited data integrity review to support our data reliance. We compared the revenue and payment data in the CPUT system to data in the Retail Data Mart and

¹⁹ The objective is to reduce the Postal Service's cost to serve, maximize revenue, and improve customer experience.

²⁰ Our original universe was 2,581 CPUs. We subsequently removed village post offices, fee for service, public service, seasonal, and terminated CPUs to arrive at the universe of 2,337.

we interviewed Postal Service officials knowledgeable about the data. We found differences in the data from these two systems; however, the Postal Service relies on the data in CPUT system to manage the CPU program. We determined that the data are sufficiently reliable for the purposes of this report.

Prior Audit Coverage

Report Title	Report Number	Final Report Date	Monetary Impact (in millions)
<i>Contract Postal Units: Analysis of Location, Service, and Financial Characteristics</i>	GAO-13-41	11/14/2012	None
<p>Report Results: The Government Accountability Office (GAO) found the number of CPUs has declined and their nationwide presence in urban and rural areas supplements the Postal Service's network of post offices by providing additional locations and hours of service. The Postal Service has no strategic plan to increase CPUs as part of the retail network strategy. The GAO did not make any recommendations in this report but made retail network recommendations in a previous report.</p>			
<i>Closure of Contract Postal Units</i>	CI-MA-12-001	8/16/2012	Net loss could range from \$284,658 to \$1,423,289
<p>Report Results: While CPUs are part of the Postal Service's overall strategy to expand retail alternatives, management stated the 20 CPU closures were needed to facilitate the 2010-2015 collective bargaining agreement negotiation. Accordingly, the Postal Service closed the CPUs in compliance with a Memorandum of Understanding (MOU), CPU contract termination clauses, and Postal Service guidance. The impact on retail alternatives was minimal and the report estimated a range for the potential annual net revenue loss. Because the closures were part of the MOU, the report did not provide any recommendations.</p>			
<i>U.S. Postal Service: Action Needed to Maximize Cost-Saving Potential of Alternatives to Post Offices</i>	GAO-12-100	11/17/2011	None
<p>Report Results: The Postal Service expanded access to its services through retail alternatives to improve service and financial performance; however, oversight of retail partners, which includes entering into written agreements and providing training and guidance, could be improved with modification to monitoring compliance with its procedures. Management agreed with the GAO's findings and recommendations to develop a plan for retail network restructuring and monitoring retail partners.</p>			
<i>Contract Postal Units Contract Oversight</i>	CA-AR-11-007	9/30/2011	\$162,687,742
<p>Report Results: The Postal Service must improve oversight of CPU contracts to ensure it is billed appropriately and services are received in accordance with contract terms. Specifically, Postal Service contracting officials did not certify payments to CPUs during FYs 2009 and 2010. In addition, contracting officials did not perform all assigned duties and responsibilities as required based on contract administrative files reviewed. Finally, contracting officials did not always perform financial audits of CPUs as required. Management disagreed with the recommendations to require and certify invoices and the associated monetary impact. Management agreed to the recommendations regarding providing training and oversight.</p>			

**Appendix B:
Performance-Based vs.
Firm-Fixed-Price Contracts**

Performance-Based		Firm-Fixed-Price
Non-automated	Automated	Non-automated
No minimum revenue requirement	Required to generate \$100,000 in annual revenue	No minimum revenue requirement
Transactional data is reported daily on PS Form 1412	Transactional data/financial data is uploaded daily from CARS System	Transactional data is reported daily on PS Form 1412
Suppliers are paid a percentage of the revenue from the sale of Postal Service products and services for each month	Suppliers are paid a percentage of the revenue from the sale of Postal Service products and services for each month	Suppliers are paid a fixed annual rate in 12 equal monthly installments
Required to comply with brand image of a retail facility	Required to comply with brand image of a retail facility	Not required to comply with brand image of retail facility
Requires financial examinations	Financial examinations are not required	Financial examinations are required
Required to maintain separation of revenue between Postal Service sales and normal business sales	Not required to maintain separation of revenue between Postal Service sales and normal sales	Required to maintain separation of revenue between Postal Service sales and normal sales
Offers PO Boxes	Does not offer PO Boxes	Offers PO Boxes
Does not offer money orders	Does not offer money orders	Offers money orders

Source: OIG analysis as of April 2014.

Appendix C: Management's Comments

KELLY M. SIGMON
VICE PRESIDENT, RETAIL AND CUSTOMER SERVICE OPERATIONS



October 31, 2014

To: LORI LAU DILLARD
DIRECTOR, AUDIT OPERATIONS

SUBJECT: Draft Contract Postal Units (Report Number [DR-AR-14-DRAFT])

The Postal Service agrees with the OIG findings and monetary impacts in this report.

Recommendation 1:

We recommend the Vice President, Retail and Customer Service Operations, conduct annual evaluations and convert firm-fixed price CPU contracts to performance-based contracts when it is cost effective.

Management Response/Action Plan:

Agree. Annual evaluations of CPU firm-fixed and performance based contracts are valuable tools which will allow the CPU program to achieve our program and revenue goals at the best value. We will work cross-functionally with the Denver Category Management Center team, San Mateo CPUT IT team and USPS Area and District representatives to develop tools and implement processes within the CPUT IT Team and USPS Area and District representatives to develop tools to and implement processes within the CPUT (Contract Postal Unit Technology) system that will provide review, analyst and recommendation for changes with specific supplier contracts.

Target Implementation Date:

Third Quarter, FY2015

Responsible Official:

Kelly M. Sigmon, Vice President, Retail and Customer Service Operations

475 L'ENFANT PLAZA SW
WASHINGTON DC 20260
202-268-2252
FAX: 202-268-3331
WWW.USPS.COM

Recommendation 2:

We recommend the Vice President, Retail and Customer Service Operations, convert firm-fixed price contracts for contract postal units, where cost effective, to performance-based contracts to optimize revenue performance.

Management Response/Action Plan:

Agree. Upon the completion of annual evaluations and periodic reviews of firm-fixed price CPU suppliers, where practical and mutually agreeable with the needs of the host District, we will convert existing firm-fixed price contracts to performance-based contracts to optimize revenue performance.

Target Implementation Timeline:

Third Quarter, FY2015

Responsible Official:

Kelly M. Sigmon, Vice President, Retail and Customer Service Operations

This report and management response does not contain any information that may be exempt from disclosure under FOIA



Kelly M. Sigmon
Vice President, Retail and Customer Service Operations

cc: *Sally Haring*
Manager, Corporate Audit Response Management
Megan Brennan
Chief Operating Officer



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1735 North Lynn Street
Arlington, VA 22209-2020
(703) 248-2100