



August 25, 2010

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SUBJECT: Audit Report – Facility Optimization: New York District  
(Report Number DA-AR-10-010)

This report presents the results of our audit of facility optimization in the New York District (Project Number 09YG049DA000). The U.S. Postal Service Office of Inspector General (OIG) initiated this audit due to the district's high-risk ranking identified through our Real Estate Risk Model (RERM). Our objective was to identify opportunities for the New York District to optimize existing real estate. See [Appendix A](#) for additional information about this audit.

The New York District uses 116 facilities with over 4.4 million interior square feet (SF). While the district employs these facilities, it has experienced a significant reduction in workload over recent years. From fiscal year (FYs) 2005 to 2009, mail volume has dropped 23 percent. Customer traffic has also declined in post office lobbies as retail transactions shift to alternate access locations. From FY 2005 to 2009, alternate access revenue in the New York District has increased by 50 percent. The reduction in workload provides an opportunity to reevaluate space needs and identify potential excess space.

## [Conclusion](#)

The New York District has 2.4 million square feet in excess of what their workload suggests they need. A breakdown of excess space identified at sites visited in the district indicated that 97 percent of the excess space was associated with main post offices and plants. Postal Service has the option to optimize excess real property through:

- Disposals – selling property.
- Outleasing – leasing owned property.
- Subleasing/Assignment – reassigning leased property.
- Development – investing in real estate projects.

With two major efforts underway, the Postal Service has begun taking action to optimize existing space. Specifically the New York District plans to dispose of 227,713 SF of this excess through approved optimization projects, with another 62,000 SF planned for evaluation in FY 2010. Although it has made progress, the Postal Service can do more to dispose of excess interior space in a timelier manner.

Postal Service policy<sup>1</sup> requires installation and district heads to annually review and report excess property. The opportunity to optimize excess interior space in the New York District exists because:

- Postal Service policy requires installation heads to report excess space, but does not provide the necessary guidance to effectively accomplish this task.
- The excess space reporting system does not track metrics such as dates or space conditions to allow for the prioritization of disposal actions.

We estimate that if the New York District initiates disposal<sup>2</sup> action for the excess space we identified, there is a potential opportunity to realize \$446,258,222 over typical and remaining lease terms. We consider this amount to be funds put to better use.<sup>3</sup> See [Appendix B](#) for our detailed analysis of this topic and [Appendix C](#) for our calculation of monetary impact.

We recommend the district manager, New York District, in coordination with the manager, Northeast Facility Service Office:

1. Ensure installation heads have the proper guidance for identifying and reporting excess space.
2. Include additional metrics, such as dates identified and space conditions, to track, monitor, and report excess space within the New York District and initiate disposal actions for excess space identified.

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<sup>1</sup> Per the *Administrative Support Manual (ASM)* 13, Section 517.11, installation heads must review the inventory of Postal Service-owned property at least annually to determine whether there are any properties the Postal Service no longer needs and report that excess property through the Facilities Database. Section 517.34 states that installation heads, district managers, and vice presidents of Area Operations should report all excess space in Postal Service-owned or leased buildings.

<sup>2</sup> Disposal actions available include sale, termination of lease, consolidation, and/or subleasing. At a minimum, the Postal Service can out-lease or initiate a sublet action for owned or leased property, respectively.

<sup>3</sup> Funds that could be used more efficiently by implementing recommended actions. This amount does not include excess square feet that are part of approved node study.

## Management's Comments

Management agreed with both of our recommendations and stated corrective actions to address the recommendations will be in place by the end of Q2, FY 2011. While management agreed to develop a more accurate process and additional metrics to better manage excess space, management did not agree with the amount of excess space or the potential monetary impact reported. Specifically, they disagreed with the methodology used to calculate excess space, the cost factors used to value the excess space, and the calculation of the monetary impact reported.

In reference to the level of excess space reported, management conveyed that our methodology does not include allowances for:

1. Unusable space such as basements and corridors. The audit treats every square foot as usable and leasable.
2. Existing functions not included in standard designs.
3. Inefficiencies in current building layouts and support space due to code requirements.
4. Buildings considered historic property.
5. Parking and dock space requirements.
6. Large inflexible retail lobbies.

Management said that excess space related to the Church Street Station, the Morgan Processing and Distribution Center (P&DC), and the Farley Building should not be included in our calculations. In short, they believe the inclusion of those locations skewed our conclusion because these sites had space that was sub-leased, not subject to our methodology, and subject to sales terms, respectively.

In reference to the cost factors used in our calculations, management disagreed with the:

- Number of facilities in the district.
- Level of approved optimization studies reported.
- Square foot value assigned to excess space.
- Build-out cost factors.

As such, management believes the accurate way to calculate monetary impact is by multiplying usable excess space by sub-lease value less conversion cost. This calculated outcome can then be adjusted for maintenance and utility savings.

Finally, management expressed the challenges facing the Postal Service when disposing of property in poor market conditions and actions they have already taken to reduce excess property. In particular, management has focused its attention on properties that have more than 10,000 interior SF which represents 16 percent of buildings and 76 percent of interior square feet. This allows the Postal Service to capture the largest opportunities for usable excess space. See [Appendix E](#) for management's comments in their entirety.

### Evaluation of Management's Comments

The OIG considers management's comments responsive to the recommendations and management's corrective actions should resolve the issues identified in the audit report. With respect to the methodology used to calculate excess space, we did not determine whether the excess space identified was usable, in part because Postal Service systems do not identify usable areas. We agree that realty management policies and systems need to be updated to define usable areas. According to commercial realty standards,<sup>4</sup> usable areas are generally measured from "paint to paint" inside the permanent walls to the middle of partitions. No deductions are made for columns and projections necessary to the building. Our calculations reflect these standards.

As it relates to the usability of basements, we note that Postal Service Headquarters and many federal agency buildings use basement space. We did not include allowances for existing functions, building layout inefficiencies, and inflexible spaces because the Postal Service's current space standards did not specify these allowances. Our audit focused on interior excess space so excess parking and dock space was outside the scope of the audit.

In reference to issues raised pertaining to the Church Street Station, the Morgan P&DC, and the Farley Building; management said they were collecting rent from the Church Street Station and offered to supply documentation supporting this claim. However, management did not provide us with evidence of this during our audit. For the Morgan P&DC, we did not measure against standards to determine excess space but rather used excess space indentified by engineers selected by the area office. We have previously reported that the Postal Service sold the Farley Building and leased back part of the space. In that report,<sup>5</sup> we questioned the wisdom of leasing back more space than was needed for the delivery unit located there.

Postal Service management also conveyed that we did not consider the historic nature of buildings and that they are possibly restricted in making changes to these buildings. While we agree that there are properties held by the Postal Service that are historic in nature, we do not feel this had a large impact in the presentation of our results. The number of eligible historic buildings listed in the Postal Service's systems account for less than 1 percent of their properties. Also, while the Postal Service is required to

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<sup>4</sup> [www.boma.org](http://www.boma.org)

<sup>5</sup> *Facilities Optimization: Controls Over the Selling of Assets*, Report Number DA-AR-10-004, June 1, 2010

consult with historical organizations, they are not bound by those consultations or decisions.

For clarification, the discrepancy in the number of facilities highlighted by Postal Service is the result of limiting the scope of our audit to buildings classified as post offices in the facilities database. We also included in our review processing plants located near selected sites. The number of facilities conveyed by Postal Service includes all facility classifications or types within the district. The cost factors used in our calculations represent district averages recorded in Postal Service facility databases as of October 2009.

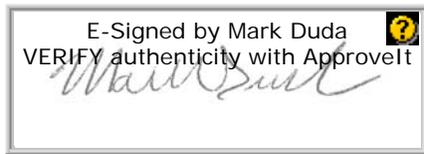
Postal Service management asserted that the audit team did not consider all the node studies from FY 2009. We considered all the “approved” node studies, rather than “completed” node studies. An “approved” node study represents concurrence by area office management and therefore is an active consolidation effort. A “completed” node study is merely a study of consolidation options in which the area office management has yet to agree to a specific course of action.

We requested specific “build-out” costs from the Postal Service for the New York District. The Postal Service responded that they do not have a methodology of determining these costs at a national, area, or district level. As such, to determine build-out cost we used the average build-out costs for the area as presented in their node studies. We note that build out costs are negotiable and lessees, at times, absorb the cost of conversion. We built in several tolerances relating to the size of excess space at sites reviewed and considered the marketability of properties within the districts. We recognized realty market conditions and discounted our excess space calculations by the national commercial vacancy rate of 14 percent. As such, we consider our presentation of monetary impact as fair and conservative.

Finally, we recognize the efforts made to optimize Postal Service real estate and management’s attention to properties greater than 10,000 square feet. We believe that once management modernizes its realty management systems to have greater visibility of excess space, it will be able to better prioritize disposal actions associated with its full building inventory.

The OIG considers all the recommendations significant, and therefore requires OIG concurrence before closure. Consequently, the OIG requests written confirmation when corrective actions are completed. These recommendations should not be closed in the follow-up tracking system until the OIG provides written confirmation that the recommendations can be closed.

We appreciate the cooperation and courtesies provided by your staff. If you have any questions or need additional information, please contact Miguel Castillo, director, Engineering and Facilities, or me at 703-248-4546.



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Deputy Assistant Inspector General  
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Attachment

cc: Steven J. Forte  
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Corporate Audit and Response Management

**APPENDIX A: ADDITIONAL INFORMATION**

**BACKGROUND**

The New York District leases or owns 116 facilities with over 4.4 million interior SF to process the mail. The consolidation or closure of facilities is a widely discussed topic due to declining mail volume and the resulting financial condition of the Postal Service. In response, Postal Service Facilities and Retail Management organizations have implemented initiatives to optimize space, namely, initiation of the Facility Optimization Program and the Station and Branch Optimization Consolidation (SBOC) program.

In April 2008, the vice president of Facilities initiated the Facility Optimization Program to balance the portfolio of existing delivery facilities with the Postal Service’s current and projected space needs. The program’s objectives are to generate revenue and reduce rent obligations and operational costs. The process entails identifying, investigating, analyzing, and approving space before executing the approved optimization action. The Northeast Area has 27 approved optimization studies, with four in the New York District.

Established in May 2009, the SBOC program provides tools and strategies to evaluate the effectiveness of Postal Service retail placement in support of the *Transformation Plan’s* goals of improved service and increased revenue. At the district level, New York initially identified 30 locations for review.

To supplement and expand on existing Postal Service initiatives, the OIG developed a Real Estate Risk Model (RERM) to identify and prioritize emerging facility risk. The risk model measures facility performance results by district for the following nine metrics:

**Table 1. Risk Metrics**

RERM METRICS	
Ratio of Mail Volume to Interior Square Footage	Excess Postal Service Identified Interior Space
Ratio Revenue to Interior Square Footage	Excess Land
Ratio of Total Expense to Interior Square Footage	Facility Condition
Ratio of Employees to Interior Square Footage	Density, Geographic Location
Ratio of Retail Revenue to Total Expense	

The New York District ranked third most at risk of all 74 districts as of Quarter 2, FY 2010.

## OBJECTIVE, SCOPE, AND METHODOLOGY

Our objective was to identify opportunities for the Postal Service's New York District to optimize existing real estate. We visited 39 of 116 facilities in the New York District, which represents 83 percent of OIG-calculated total excess space. The scope of the audit included main post offices, carrier annexes, stations, branches, and mail processing facilities. To accomplish our objective we visited selected facilities, conducted interviews, and examined other relevant materials.

We used Postal Service criteria<sup>6</sup> for new space projects to establish space requirements for post office facilities in the New York District. Our excess space metric subtracts the earned facility size from the actual facility size<sup>7</sup> to calculate the excess space. To determine the earned facility size, we used the Space Requirements Model matrix<sup>8</sup>. The matrix computes earned space based on the delivery and retail workload conducted at each site. We compared workload data from Postal Service databases<sup>9</sup> to the number of carrier routes, the number of rented post office box sections, and peak window usage. Our method differs from existing Postal Service initiatives<sup>10</sup> because it focuses on the total facility size, not specific operations. We designed our metric primarily for customer service facilities. We obtained the measurements for excess space at processing plants from respective industrial engineers.

Facilities management suggested we use detailed facility information available in recently conducted space surveys to calculate our excess space. This approach would provide greater insight into the type and location of space designated as excess. While this method has merit, we were not able to use this approach because the space surveys were conducted only at buildings with 10,000 or more net interior square feet. These buildings — while containing the majority of the Postal Service interior space— only accounted for 16 percent of the total number of facilities nationally. Consequently, we opted to use a global approach and assess excess space at the total facility level.

We modified our metric as follows to address obstacles in applying it to existing real estate resources:

- We established thresholds to remove post offices with less than 100 SF of excess space and carrier annexes with less than 300 SF of excess space.
- We used Non-Flat Sequencing System building standards for customer service sites.

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<sup>6</sup> We used Postal Service criteria established in March of 2007 outlined in a letter issued by the senior vice president of Operations.

<sup>7</sup> Interior square footage obtained from the electronic Facilities Management System (eFMS).

<sup>8</sup> In support of newly established criteria, the Headquarters Facility Group, Planning and Approval, designed matrices to assist with space requirements for planned facilities. We used the Space Requirements Matrix for Non-Flat Sequencing System (FSS) offices.

<sup>9</sup> WebBATS Monthly Summary Data for issued P.O. Box information, Intelligent Mail and Address Quality (IMAQ) Delivery Statistics Summary for route information, and Retail Data Mart for earned peak modeled window staffing.

<sup>10</sup> SBOC and Facilities Optimization Program.

- We provided additional support space by calculating retail and delivery space requirements separately.
- We provided additional delivery space for facilities with more than 51 routes. The additional routes received the space designated for a separate total facility instead of following the Postal Service practice of adding an additional 123 SF per route.
- At facilities with unique functions, we either subtracted the space dedicated to that function from our metric or relied on Postal Service expertise to provide us with an accurate account of the building's excess space.
- Furthermore, we reduced our total monetary impact by 14 percent to address the difficulty in achieving a 100 percent realization of optimization efforts. The reduction correlates directly to the national vacancy rate for commercial real estate.

We conducted this performance audit from September 2009 through August 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 officials on June 14, 2010 and July 15, 2010, and included their comments where appropriate.

We assessed the reliability of facility-related data by verifying the accuracy of computer-generated information by making observations during facility tours and interviewing agency officials knowledgeable about the data. We determined the data used was sufficiently reliable for the purposes of this report.

**PRIOR AUDIT COVERAGE**

The following audit reports are relevant to the Postal Service’s facility infrastructure.

Report Title	Report Number	Final Report Date	Report Results
<i>Restructuring the U.S. Postal Service to Achieve Sustainable Financial Viability</i>	GAO-09-937SP	7/28/2009	The Government Accountability Office added the U.S. Postal Service’s financial condition to the list of high-risk areas needing attention by Congress and the executive branch to achieve broad-based transformation. It recognized the need to reduce the facility infrastructure. There is no Postal Service response in the report.
<i>Federal Real Property: An Update on High-Risk Issues</i>	GAO-09-801T	7/15/2009	Federal agencies have taken some positive steps to address real property issues but some of the core problems that led to the designation of this area as “high-risk” continue to persist. There is no Postal Service response in the report.
<i>Network Rightsizing Needed to Help Keep USPS Financially Viable</i>	GAO-09-674T	5/20/2009	The Postal Service will require actions in a number of areas, such as rightsizing its retail and mail processing networks by consolidating operations and closing unnecessary facilities. The Postal Service generally agreed with the accuracy of the statements and provided technical comments, which we incorporated.
<i>Use of Existing Postal Owned Space – Capping</i>	SA-AR-08-007	3/21/2008	The Pacific, Great Lakes, New York Metro, and Southeast Areas did not monitor or actively track and report underutilized and vacant space. Management agreed with the recommendation.

**APPENDIX B: DETAILED ANALYSIS**

**Excess Space is Significant in the New York District**

Based on facility space requirements,<sup>11</sup> we calculated that the New York District maintains 2.4 million SF more than what is required for its current operational workload, and this amount can be considered potential excess space. As depicted in Chart 1, excess space was 55 percent of the total interior square footage.

**Chart 1 – District Interior and Excess Space Comparison**

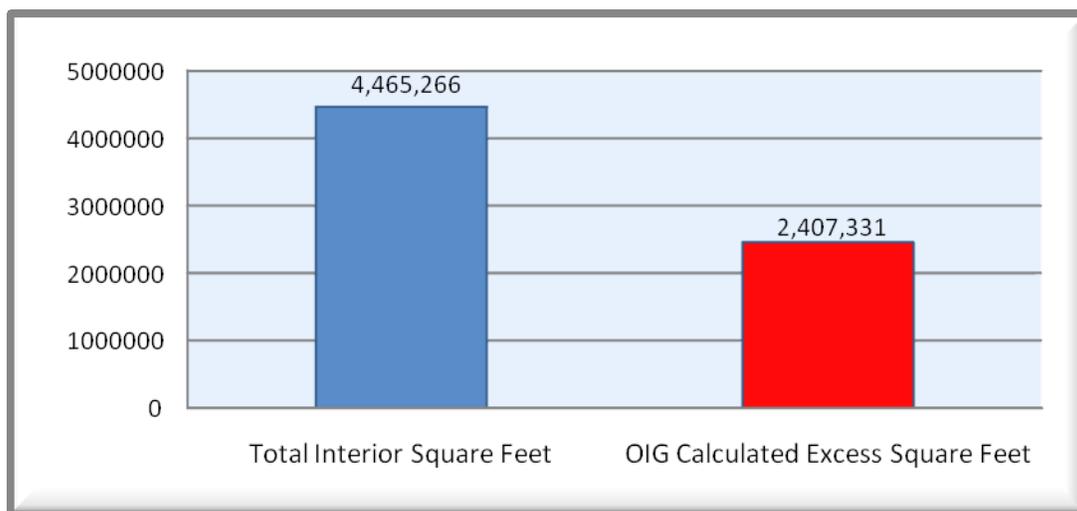


Table 2 shows the breakdown of interior square footage and OIG-calculated excess for the 39 visited facilities in the New York District. Of the excess space at the sites visited, stations (post offices) contributed to 83 percent, while plants contributed to 14 percent, finance stations to 2 percent, and carrier annexes to 1 percent.

<sup>11</sup> We used Postal Service criteria established in March of 2007 outlined in a letter issued by the senior vice president of Operations. In support of this newly established criteria, the Headquarters Facility Group, Planning and Approval, designed matrices to assist with the space requirements of planned facilities.

**Table 2. Excess Space by Facility Type Visited**

Type of Facility	Facility Count	Percentage of Count	Percentage of Excess	OIG Calculated Excess	Interior SF
Stations	20	51%	83%	1,646,671	2,019,171
Plants	2	5%	14%	279,065	1,373,025
Finance Station	14	36%	2%	40,587	82,246
Carrier Annex	1	3%	1%	30,645	266,112
APC Site Only	1	3%	0%	243	943
FND Station (Macy's)	1	3%	0%	-	508
<b>Grand Total</b>	<b>39</b>	<b>100%</b>	<b>100%</b>	<b>1,997,211</b>	<b>3,742,005</b>

To highlight excess space in the New York District, Illustration 1 depicts two facilities with excess interior space. Morgan Processing & Distribution Center (P&DC) is a Postal Service-owned plant with three vacant floors. The Radio City Station is another owned facility which houses delivery and retail operations with one vacant floor. Both are located near other Postal Service facilities also maintaining excess space.

**Illustration 1 – Examples of Excess Space**

<p><b>New York Morgan P&amp;DC</b>                  Interior SF: 1,197,825  <b>OIG Excess SF: 277,785</b></p> 	<p><b>Radio City Station</b>                  Interior SF: 65,229                  Earned SF: 20,000  <b>OIG Excess SF: 45,229</b></p> 
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See [Appendix D](#) for detailed earned space information on each of the facilities visited during fieldwork.

## Causes for Excess Interior Space

The opportunity to optimize excess interior space in the New York District exists because:

- Postal Service policy requires installation heads to report excess space, but does not provide the necessary guidance to effectively accomplish this task.
- Facility systems do not track metrics such as dates identified or space conditions to allow effective management of excess space.

## Guidance Can Be Improved

A review of the *Facility Database User Guide* shows it does not provide sufficient guidance for identifying excess space using the workload-driven space requirements. For example, the facility database space survey asks installation heads to objectively answer “*Do you have any vacant space in your facility that is in leasable condition and has access that does not compromise the security of the operation?*” without providing further guidance or referencing space standards. While we identified excess space at 103 of the 116 Postal Service facilities, only two locations answered “yes” to the vacant leasable space survey question. Further, our interviews revealed that Operations employees were unaware of the method used to identify excess space at their facility.

## Facility Systems Do Not Allow for Effective Management of Excess Space

The Postal Service is experiencing considerable workload decline, which has resulted in significant excess space. However, the electronic systems that manage facility space do not collect or monitor metrics such as length of time space is underutilized or vacant or its condition to efficiently prioritize disposal actions.

For comparison purposes, we benchmarked Postal Service facility practices against the General Services Administration’s (GSA) realty management practices and found that GSA “ages” its available space for tracking, monitoring, and decision-making. The Postal Service does not have the ability to age excess space, as dates on entry are not collected.

The GSA’s Public Buildings Service also manages its leased portfolio by focusing on four primary areas: reducing vacancy, managing lease administration expenses, managing customer requirements, and analyzing market trends.<sup>12</sup> Similarly, owned facilities are monitored and analyzed using performance metrics such as revenue, funds from operations, operating costs, vacancy, net operating income, and return on equity. The Postal Service facility management systems are not able to manage property in this manner. For example, rents from leases or subleases are tracked manually using electronic spreadsheets.

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<sup>12</sup> State of the Portfolio FY 2008 at:

<http://www.gsa.gov/Portal/gsa/ep/channelView.do?pageTypeld=8199&channelPage=%2Fep%2Fchannel%2FgsaOverview.jsp&channelId=-24880>

Additionally, because the Postal Service's eFMS calculates space based on delivery and retail metrics, the excess space reported for processing and distribution plants is inaccurate. Therefore, it is not a reliable source for identifying how much excess space is available in its plants. The Postal Service plans to measure plants and update the facility database. To complete this task for our report, we requested industrial engineers, working with local in-plant support, use blueprints to identify processing equipment, staging areas, manual work areas, and excess space.

We estimate if the New York district initiates disposal actions, there is a potential opportunity to realize \$446,258,222 over typical and remaining lease terms. We consider this amount funds that could be used more efficiently or put to better use. See [Appendix C](#) for the monetary impact calculation and assumptions.

**APPENDIX C: MONETARY IMPACTS**  
**FUNDS PUT TO BETTER USE**

Excess Interior Space  
Monetary Impacts

Project year	0	1	2	3	4	5	6	7	8	9	10
Fiscal year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
<b>Facilities Owned**</b>											
<b><u>Sublease Value</u></b>											
Utility Savings custodial savings	(\$71,647,568)	\$77,103,874	\$77,103,874	\$77,103,874	\$77,103,874	\$77,103,874	\$77,103,874	\$77,103,874	\$19,275,969		
Utility Savings custodial savings		\$3,130,668	\$3,193,281	\$3,257,147	\$3,322,290	\$3,388,735	\$3,456,510	\$3,525,640	\$881,410		
Utility Savings custodial savings		\$2,477,700	\$2,477,700	\$2,477,700	\$2,477,700	\$2,477,700	\$2,477,700	\$2,477,700	\$619,425		
<b><u>Leases Expiring FY 2009**</u></b>											
Utility Savings custodial savings	(\$10,034,487)	\$10,798,662	\$10,798,662	\$10,798,662	\$10,798,662	\$10,798,662					
Utility Savings custodial savings		\$438,461	\$447,230	\$456,175	\$465,298	\$474,604					
Utility Savings custodial savings		\$347,010	\$347,010	\$347,010	\$347,010	\$347,010					
<b><u>Leases Expiring After 10/1/2010</u></b>											
Utility Savings custodial savings	(\$7,870,586)	\$8,469,969	\$8,025,349	\$6,962,977	\$5,651,057	\$3,603,031	\$3,353,827	\$2,862,702	\$2,302,962	\$2,218,917	\$787,222
Utility Savings custodial savings		\$367,103	\$356,031	\$318,273	\$268,110	\$183,461	\$175,958	\$130,899	\$107,411	\$105,561	\$38,200
Utility Savings custodial savings		\$272,179	\$257,891	\$223,752	\$181,594	\$115,782	\$107,774	\$91,992	\$74,005	\$71,304	\$25,297
Subtotal Cash Flows @ Sub Lease Efficiency Rate Discounted at USPS cost of borrowing	(\$87,550,141)	\$101,093,875	\$100,693,529	\$99,630,285	\$98,298,489	\$96,173,896	\$86,675,643	\$86,192,808	\$23,261,182	\$2,395,782	\$850,718
	(\$75,293,121)	\$86,940,733	\$86,596,435	\$85,682,045	\$84,536,700	\$82,709,551	\$74,541,053	\$74,125,815	\$20,004,616	\$2,060,373	\$731,618
	(\$75,293,121)	\$84,000,708	\$80,838,698	\$77,280,296	\$73,668,851	\$69,639,222	\$60,639,195	\$58,262,220	\$15,191,737	\$1,511,759	\$518,657

**Net Present Value: \$446,258,222**

Build-Out Costs SF	\$40.05	Utilities Savings SF per Year	\$1.75
Lease Savings SF per Year	\$43.10	Utility Cost Escalation Rate	2.00%
USPS Cost of Borrowing	3.50%	Custodial Rate SF	\$2.77
Sub-lease Efficiency Rate	86.00%		

**Assumption: \*\*Weighted Average Lease Years = 7.3**

**Value Assigned to Excess Space**

The lease cost per square foot for the New York District is \$43.10. Using Facility Inventory Reports from the eFMS, we calculated this figure by dividing total interior square footage by total lease costs. The value is similar to \$81.63,<sup>13</sup> the average square foot cost for leasing commercial retail and office space in the district.

**Utility Costs Associated with Excess Space**

The utility cost per square foot for the New York District is \$1.75, with a cost escalation rate of 2 percent. Using the Financial Performance Report (FPR), Line 42, we calculated this figure by dividing total annual utility expenses for FY 2009 by the district's total interior square footage.

**Maintenance Costs Associated with Excess Space**

The maintenance cost per square foot for the New York District is \$2.77. We calculated this figure by dividing the total annual maintenance expenses<sup>14</sup> (FY 2009) by the district's total interior square footage. However, we reduced the cost by 50 percent based on previously identified savings in a custodial maintenance audit.<sup>15</sup>

**Build-Out Costs Associated with Implementing Optimization Actions**

The build-out cost per square foot for the New York District is \$40.05. We calculated this figure by dividing the "build-out/Line 63 capital" costs for all approved optimization node studies in the Northeast Area by the total reduction in square footage identified in the approved node studies.

**Ownership of Facility and Term Years**

We categorized all facilities within the district by ownership – leased versus Postal Service-owned. We further grouped the leased properties by the number of term years remaining in the lease.

We calculated leases expiring before the end of FY 2010 based on the assumption the leases would be renewed for the standard 5-year period. We calculated leases expiring after October 1, 2010 for the remaining lease term; and calculated Postal Service-owned facilities over a period of 7.3 years, which was the historical national average lease term.

**Sublease Efficiency Rate**

We obtained the national commercial property vacancy rate of 14 percent from the National Realty Association for industrial and retail space. As such, we reduced the net present value savings realization to an 86 percent "success rate."

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<sup>13</sup> Realtor.com analyzes comparable private sector commercial retail and office space properties to determine average square footage costs.

<sup>14</sup> eFlash (Labor Distribution Code 38, Salary and Benefits) + FPR, Line 3F, Contract Cleaners Costs

<sup>15</sup> *Custodial Maintenance Audit Report*, (Report Number DA-AR-09-011, dated August 13, 2009).

**APPENDIX D: FACILITIES VISITED**

Facility Name	Type of Facility	Interior Square Footage	Total Earned Bldg Size From Matrix	Square Feet In Approved Node Study <sup>16</sup>	Potential Excess Square Footage
JAMES A. FARLEY	Station	250,000	21,500		178,500
LENOX HILL S & N/FDR	Carrier Annex	266,112	25,500		30,645
GRAND CENTRAL STATION	Station	159,051	27,500	150,000	131,551
BRONX/ P&DC	Plant	175,200	-		1,280
MADISON SQUARE	Station	82,113	15,500		66,613
TIMES SQUARE STATION	Station	90,095	21,500		68,595
PECK SLIP STATION	Station	65,372	9,500	30,000	55,872
CANAL STREET STATION	Station	69,200	19,500		49,700
RADIO CITY STATION	Station	65,229	20,000		45,229
MIDTOWN STATION	Station	44,384	12,000		32,384
GRACIE	Station	56,292	28,000		28,292
ANSONIA STATION	Station	44,979	19,000		25,979
COOPER STATION	Station	37,600	17,500		20,100
GREELEY SQUARE	Finance	26,500	4,000		22,500
OLD CHELSEA STATION	Station	41,685	20,000		21,685
LENOX HILL STATION	Station	30,615	15,500		15,115
PETER STUYVESANT STATION	Station	28,000	9,500		18,500
VILLAGE STATION	Station	27,200	11,000		16,200
ROCKEFELLER CENTER	Finance	17,625	8,500		9,125
KNICKERBOCKER STATION	Station	23,025	11,000		12,025
COLUMBUS CIRCLE	Finance	7,900	3,500		4,400
HIGHBRIDGE	Station	12,700	10,000		2,700
BRYANT	Finance	5,977	4,500		1,477
MORRISANIA	Station	10,591	8,500		2,091
MORRIS HEIGHTS	Station	11,262	8,000		3,262
WHITEHALL RETAIL UNIT	Finance	4,300	3,500		800
HANOVER FINANCE STATION	Finance	4,000	3,500		500
APPRAISERS STORES	Finance	3,145	2,000		1,145
CHINATOWN	Finance	2,856	3,500		-
CHEROKEE	Finance	3,800	3,500		300
PATCHIN	Finance	2,152	3,000		-
PITT	Finance	1,391	2,000		-
PORT AUTHORITY CONV	Finance	1,445	2,000		-
MELCOURT	Finance	840	500		340

<sup>16</sup> Prince and Murray facilities were not sampled, however they have 47,713 combined is SF Effected by Node Studies

Facility Name	Type of Facility	Interior Square Footage	Total Earned Bldg Size From Matrix	Square Feet In Approved Node Study <sup>16</sup>	Potential Excess Square Footage
DAG HAMMARSKJOLD	APC	943	700		243
MACYS FINANCE	FND S	508	2,000		-
26 FEDERAL PLAZA STATION	Finance	315	3,000		-
CHURCH STREET STATION	Station	869,778	17,500		852,278
NEW YORK MORGAN P&DC	Plant	1,197,825	-		277,785
<b>TOTALS</b>		3,742,005	397,700	180,000	1,997,211

## APPENDIX E: MANAGEMENT'S COMMENTS

JORDAN M. SMALL  
VICE PRESIDENT, AREA OPERATIONS  
NORTHEAST AREA



August 17, 2010

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SUBJECT: Response to Draft Audit Report Facility Optimization:  
New York District (Report Number DA-AR-10-DRAFT)

Management appreciates the efforts the Office of Inspector General (OIG) has taken in regards to facility optimization in the New York District. We agree that optimization of current facility infrastructure is a critical and an important initiative within the Postal Service. The following is in response to the above subject audit and management's comments on the findings.

Management is in full agreement that excess space exists in a number of facilities and it is the reason why the optimization program was started by the Facilities Department almost two years ago. In addition, management agrees that the policy written in the ASM Section 517 is not followed and is ineffective. This is due to the changes in organizational structure and responsibilities since it was written in 1999 which rendered this section obsolete. A different approach other than the ASM 517 to manage excess space is needed. This section will be revised and we will adjust our systems and the ASM to align to today's structure and processes which addresses the two recommendations made by the audit.

Regarding the findings of the audit, management disagrees with the amount of excess space and potential revenue based on the following:

1. The methodology utilized to determine existing usable excess space in facilities.
2. Inaccurate data and cost factors utilized to calculate the potential revenue.

The following are the basis of management's disagreement as outlined.

### 1. Methodology

As stated in the audit, management disagrees with the methodology utilized in determining excess space. This disagreement was raised in discussions with the OIG prior to the first release of this audit and in meetings that were held with the OIG prior to the reissuance of this audit. The major concern is that the methodology utilized is based on applying the current Small Standard Building Design (SSBD) which is intended for construction of new, under 10,000 sq. ft., one story facilities with today's standards and efficiencies and applying it against existing facilities constructed or leased over the past 80 years with very different standards, construction, layout and utilization. The OIG methodology takes the overall net

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interior square footage of the existing facilities and subtracts the overall net square footage of the SSBD (earned) and calls the delta "excess".

However, this methodology does not include allowances for<sup>1</sup>:

- A. Unusable space such as basements, corridors, etc. The audit treats every square foot in the building as usable and leasable.
- B. Existing functions not included in the SSBD design such as administrative district office, training, caller service, etc.
- C. Inefficiencies in current building layout due to multiple floors, stairs, elevators, columns, redundant support space required on each floor due to code requirements.
- D. Historic nature of some of the buildings that hinders the possibility of making changes.
- E. Parking and dock space requirements.
- F. Large inflexible retail lobbies.

**Example:**



**Church Street:** Administrative space



**FDR Station:** Multi story



**Farley Building:** Historic



**Grand Central:** Structure

**Management Recommended Methodology**

<sup>1</sup> We excluded Morgan P&DC from our analysis because the OIG obtained excess space measurements from respective industrial engineers and no methodology was applied.

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Because every building is different and has a variety of the above items to contend with, management recommends that the OIG review each specific building and determine usable excess space after making allowances for the items listed above.

## 2. Inaccurate Data and Cost Factors

The audit states that 2.4 million square feet of excess space exists in the New York District with a potential to realize \$446,258,222 over typical and remaining lease terms. The OIG also provides two specific recommendations for the \$446,258,222 whereby, "Funds could be used more efficiently by implementing recommended actions."

Management disagrees with these findings because of the following:

- A. The first page of the audit states, "The New York District uses 116 facilities with over 4.4 million square feet (SF). Based on eFMS inventory data this number is inaccurate. It is 121 buildings and utilizes 8.2 million square feet.
- B. Page 3 of the audit states that the Northeast FSO has 27 approved optimization studies..." That number is what was approved in 2010. It did not include the optimization studies completed in 2009 which were 25 more.
- C. The amount of usable excess square footage is not correct due to the methodology as described in section 1 Methodology above.
- D. The OIG states that the Value Assigned to Excess Space is \$43.10. This was calculated by "dividing the total interior square footage by total lease costs" and reaching a number of \$43.10. However, when Facilities calculated this number based on OIG formula, we find the number to be  $\$21,366,803$  (total lease cost) /  $8,234,595$  (total interior square footage) = \$2.59. We believe the correct method to calculate leased per square foot cost is  $\$21,366,803$  (total lease cost) /  $2,420,461$  (total interior LEASED square footage) = \$8.82.
- E. The audit lists Church Street Station as having 869,778 interior square feet with 852,278 square feet as excess (this is 49.5% of the total claimed excess excluding the Morgan P&DC). However the Postal Service only occupies approximately 250,000 square feet. The remainder of the building is controlled by Boston Properties per a 30 year agreement signed in 1995 and rent is paid to the Postal Service for that space.
- F. The audit listed 39 buildings that were reviewed with a total claimed excess square footage of 1,997,211 square feet. However, in depth review shows that 1.3 million of the 1.9 million square feet of excess, or 65.5%, is in just three of the buildings. Those building and the claimed excess square footage are:
  - a. Church Street: 852,278 – Postal Service does not control – see 2E above.
  - b. Morgan P&DC: 277,785 – Mail Processing Facility – methodology not applied.
  - c. Farley Building: 178,500 – Historic lobby, district functions, terms of building sale to NY State

Including these three buildings in the audit, skews the overall results.

- G. Build-Out Cost: To build out the excess space and make it available to sublease, the number utilized was the total line 63 budget numbers from completed node studies divided by the square footage reduction. This is not an accurate method for determining the construction cost, because the node studies are based on

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terminating leases, selling owned buildings, and minimum renovation for the facilities gaining carriers and building alternate retail. The average square foot cost for this work cannot be used for build out cost for subleasing buildings, because the scope of work is completely different in these two scenarios. Management recommends that the OIG review each specific building to determine the following:

- a. The total usable square footage.
- b. The practicality of capturing the usable square footage in one area(s) by moving and consolidating operations in the building and insuring the security of the mail is met.
- c. Cost to accomplish b.

**Potential Revenue:**

Management believes the accurate way to calculate potential revenue is, first applying the following formula we use in our node studies which is:

Potential Revenue = (Usable excess square footage X sublease value per square foot)  
**minus** (Total cost required to achieve this revenue.)

Then adjust for the values of maintenance and utility savings.

We described the correct method to calculate the accurate available excess square footage. When it comes to the value of subleasing the excess square footage, the only way to determine this value is by analyzing the real estate market. This must include the possibility of subleasing, the duration of subleasing, and the square foot value of such a sublease. Also, the cost of tenant improvement must be included. Further discussion of market conditions is covered in a later section of this response.

The correct methodology to calculate the cost of making the space available is described in section 2E above.

The audit states that there is 2.4 million square feet of excess space in the New York District worth \$446,258,222. But 1.3 million square feet is tied up in the 3 building above (Farley, Church, Morgan). As a prorated share this would account for \$240 million of the claimed potential revenue that should not be included.

Since the \$446,258,222 over typical and remaining lease terms was not calculated according to our formula, we are unable to agree or disagree with this number.

**Market Conditions:**

Regardless of how much excess space exists, there needs to be a market for the space. The vast majority of postal facilities fall into the industrial /commercial real estate market. Unfortunately, it is this sector that is experiencing a severe downturn. Vacancy rates are high and demand is low.

Facilities engaged the largest 6 real estate brokerage firms in the country and all have confirmed that the property values are dropping, lease rates and demand are declining. As a result in general, our landlords are not accepting early lease terminations and our excess space must compete in a saturated market. Under this scenario, it makes it impossible for

us in most cases to achieve any positive financial results by subleasing due to the capital improvement required to make the excess space available and the high demand for tenant improvement.

**Conclusions:**

A. Regarding the audit recommendations:

1. Management will develop a more accurate process and proper documentation for identifying and reporting excess space.
  2. Management will include additional metrics to track dates and conditions of excess space. This will be part of a national process.
- Both of these actions will be completed by end of quarter 2 , fiscal year 2011.

B. Actions already taken by management:

1. Management believes that the current facilities optimization approach of focusing on the excess workroom space is an effective method for finding potential excess square footage. By currently focusing on facilities that are 10,000 square feet and greater, as opposed to all buildings in the inventory, it allows us to capture the largest opportunities for excess space that is usable.

National Data	# of Buildings	% of Buildings	Square footage	% of SF
Buildings under 10k SF	28,015	84%	68.1 million	24%
Buildings over 10k SF	5,327	16%	221.6 million	76%

2. This optimization process is a nationwide effort where by we segment and review our facilities for excess space. Our inventory is segmented by:

- a. Leased verses owned buildings
- b. Delivery only facilities
- c. GSA leased space
- d. Expiring leases
- e. Current market conditions

3. Buildings over 10,000 square foot were measured to ascertain the correct square footage per function within the facility. Based on this data, we are now able to determine what space is needed for the current operations in the facility and how much is potential excess space. After finding these candidates for excess space, a node study is developed to verify the feasibility.

The node study standard operating procedure for the optimization program includes:

- a. Establish and schedule a node study to analyzes all alternatives and associated costs/savings and complete schedule for all tasks
- b. Review all market conditions to determine financial viability of utilization of the space, disposal of the facility or sublease excess space
- c. Visit potential sites to verify all applicable costs

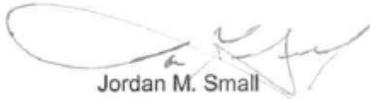
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- d. Determine best financial alternative for utilization or disposal of the excess space and obtain all necessary management approvals.
- e. Track time durations from final study approval of the action to ebuy notification for disposal.
- f. Establish and track disposal schedule.

Generated out of optimization studies nationwide, we currently have over 120 properties on the market for sale and have scheduled to terminate 250 leases. As a positive outcome of node studies in the New York District, the following actions for five facilities that are listed in the OIG audit, and two that were not listed are now complete. The NPV value of these actions is \$43.85 million dollars.

<u>Facility</u>	<u>NPV</u>
Greely Square	5.79 M
Cathedral Station	2.43 M
Radio City Station	5.73 M
Murry Hill	4.19 M
Peck Slip	6.53 M
Grand Central	10.13 M
Canal Street	9.05 M

Management believes the Facilities optimization process, along with other national initiatives, will allow us to identify usable excess space in our portfolio and extract the maximum value for the postal service out of it. Management also looks forward to working with the OIG to accomplish this very important initiative.



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