February 11, 2011

JORDAN SMALL
VICE PRESIDENT, EASTERN AREA

SUBJECT: Audit Report – Facility Optimization: Eastern Area
(Report Number DA-AR-11-002)

This report presents the results of our audit of facility optimization in the Eastern Area (Project Number 10YG030DA000). The U.S. Postal Service Office of Inspector General (OIG) initiated this audit from a random sample of districts nationwide. For the Eastern Area, our objective was to identify opportunities to optimize existing real estate in the Appalachian, Western Pennsylvania, and Western New York districts. See Appendix A for additional information about this audit.

The Eastern Area uses 2,244 facilities with almost 11 million interior square feet (SF) in the three districts noted above. While the area employs these facilities, it has experienced a significant reduction in workload in recent years. From fiscal years (FYs) 2008 to 2010, mail volume in the Eastern Area has dropped 22 percent. Likewise, mail volume in the Appalachian, Western Pennsylvania, and Western New York Districts have decreased by 7 percent, 28 percent, and 22 percent, respectively. This reduction in workload provides an opportunity to reevaluate space needs and identify potential excess space.

Conclusion

The districts analyzed in the Eastern Area have 2.8 million more square feet than our review of their workload suggests they need. The Postal Service could reduce interior space through:

- Disposal – selling property
- Outleasing – leasing owned property
- Subleasing/Reassignment – reassigning leased property
- Development – investing in real estate projects

With two major efforts underway, the Postal Service has begun reducing interior space. Specifically, the Eastern Area plans to reduce 1,080,630 SF of excess interior space through approved optimization projects, with another 313,286 SF of excess interior space scheduled for evaluation in FY 2011 for the three districts we reviewed. Although it has made progress, the Postal Service can do more to reduce excess interior space more quickly.

The opportunity to reduce excess interior space in the reviewed districts exists because:

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

We estimate that if the Eastern Area eliminates[1] the excess interior space we identified in the Appalachian, Western Pennsylvania, and Western New York Districts, it could realize $190,656,882[2] over typical and remaining lease terms. We consider this amount to be funds put to better use.[3] See Appendix B for our detailed analysis of this topic and Appendix C for our calculation of monetary impact.

Our audit also noted the Postal Service could more aggressively seek federal entities needing interior space. In the districts reviewed, our analysis shows that excess space identified at Postal Service facilities might accommodate 69 percent of the interior space needs of current federal agencies. This opportunity exists because the Postal Service has not capitalized on the priority status it has for filling federal agencies' space needs, which would allow it to reduce excess interior space and generate additional revenue. See Appendix D for more information.

We recommend the acting vice president, Operations, Eastern Area, district managers, area managers, and the Eastern Facility Service Office manager work in coordination to:

1. Clarify procedures for reporting excess space.

2. Initiate disposal actions for excess space identified.

3. Pursue opportunities with federal agencies as an option to optimize excess property.

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[1] 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.
[2] The annualized savings is $19,065,688.
[3] Funds that could be used more efficiently by implementing recommended actions. This amount does not include excess square footage that is part of an approved node study.

Management's Comments

Management agreed with the finding that excess space exists in a number of facilities, agreed to the recommendations made, and stated that corrective actions to address the first two recommendations will be in place by March 2011. They conveyed that they will complete corrective action to address the third recommendation by June 2011. While management agreed to develop a more accurate process and additional metrics to better manage excess space, as well as continue to make excess property available to other federal agencies, 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 existing excess space, in addition to the data and cost factors used to value the excess space and calculate monetary impact.

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.

2. Unique operational functions not included in standard designs and inefficiencies in the current building layouts.

3. Historic property.

4. Parking and dock space requirements.

5. Large inflexible retail lobbies.

In reference to the data and cost factors used in our calculations, management used the Grafton WV Main Post Office and the Danville VA Courthouse to exemplify their general disagreement with our methodology. They cited excess space existed to some degree but was unusable or inaccessible due to security concerns. In addition, the cost to convert space in poor condition may be impractical. As such, management believes the accurate way to calculate monetary impact is by multiplying useable excess space by sublease value less conversion cost. This calculated outcome should 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 footage. This allows the Postal Service to capture the largest opportunities for excess space that is usable. See Appendix E for management's comments in their entirety.

Evaluation of Management's Comments

Considering the rapid decline of workload and the dynamic nature of excess space, the OIG considers management's comments responsive to the recommendations. Management's corrective actions over time should resolve the issues identified in the 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,[4] 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, thus, enclosed parking and dock spaces were outside the scope of the audit.

Management also conveyed that we did not consider the historic nature of buildings and the challenges or costs associated with making changes to these buildings. While we agree that there are properties of the Postal Service that are historic in nature, we do not feel this has 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 consult with historical organizations, they are not bound by these consultations or decisions.

The standard building design matrix served as the basis for determining earned space. During the on-site visits, we inquired whether there were unique operations conducted at the facility and whether they were allotted the necessary space for those functions. Conservatively, we did not consider performance measures such as street efficiency or alternate access sales channels which would decrease the earned facility size and increase excess space. We acknowledge that security is a factor when optimizing excess space for a site-specific solution. In these cases, security challenges may be mitigated by a comprehensive solution for excess space at sites within an acceptable radius.

The Postal Service does not have a methodology of determining "build-out" costs at a national, area or district level. As such, to determine build-out cost we used the average build-out costs for the district 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 different tolerances relating to the size of excess space at sites reviewed and considered the marketability of properties within the districts. Further, the multiple

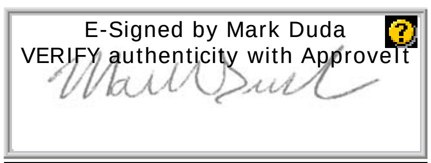
[4] www.boma.org.

actions, such as lease terminations, disposals, and space/lease reductions within the approved node studies were acknowledged and reflected in our monetary impact calculations. We recognized realty market conditions and discounted our excess space calculations by the national commercial vacancy rate of 14 percent. Therefore, we consider our presentation of the level of excess space and value a reasonable estimate of the opportunity loss associated with unproductive assets.

Finally, we recognize the efforts made to optimize Postal Service real estate and management's attention to properties greater than 10,000 SF. 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 A. Castillo, director, Engineering and Facilities, or me at 703-248-2100.



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Attachments

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APPENDIX A: ADDITIONAL INFORMATION

BACKGROUND

The Eastern Area leases or owns 2,244 facilities with more than 11 million interior square feet to move mail in the Appalachian, Western Pennsylvania, and Western New York Districts. Consolidating or closing Postal Service facilities is a widely discussed topic because of declining mail volume and the resulting financial condition of the Postal Service. In response, the Postal Service's Facilities and Retail Management organizations have implemented initiatives to optimize space, namely, 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 Eastern Area has two approved optimization studies in the Appalachian District, eight in the Western Pennsylvania District, and two in the Western 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. In addition to using the ongoing SBOC program and node studies,[5] the districts have begun consolidating space. For example:

- The Appalachian District has initiated reviews of delivery optimization. At the time of our review, the Appalachian District initiated delivery unit optimization, a cross-functional effort to streamline delivery and post office operations.

- The Western Pennsylvania District has moved operations from the Wilkinsburg Branch into the Penn Hills Branch, resulting in cost savings and elimination of a lease. This district has also moved carrier operations from some facilities and placed them in facilities identified as having excess space. Additionally, this district does actively sublease space in some of its facilities and the Downtown Station in Erie, PA is for sale.

In October 2010, the Postal Service consolidated optimization efforts to manage excess space. The goal is to manage the excess space portfolio or all space types in one overall optimization effort.

Currently, the Postal Service has a program in place to optimize carrier delivery facilities through the use of node studies. However, the Postal Service will now include

[5] Studies of consolidation for sites in a geographic radius.

mail processing plants, retail facilities, small delivery units, administrative space, and carrier delivery facilities in one overall optimization effort. The goal is to manage the excess space portfolio for all space types in one overall initiative. This integrated effort between Facilities headquarters and the field offices will use computer modeling and equipment analysis with local analysis and metro planning to form a headquarters and district/area partnership.

To supplement and expand 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 SF	Excess Postal Service Identified Interior Space
Ratio Revenue to Interior SF	Excess Land
Ratio of Total Expense to Interior SF	Facility Condition
Ratio of Employees to Interior SF	Density, Geographic Location
Ratio of Retail Revenue to Total Expense	

We randomly selected 17 districts to study excess space nationally and selected three in the Eastern Area.

OBJECTIVE, SCOPE, AND METHODOLOGY

Our objective was to identify opportunities for the Postal Service's Eastern Area to optimize existing real estate. We visited 72 of 2,209 facilities in the Appalachian, Western Pennsylvania, and Western New York Districts, representing 49 percent of the OIG-calculated excess space when comparing actual interior space to Postal Service space standards. The scope of the audit primarily 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.

To calculate an earned[6] facility size, we compared the workload data from Postal Service databases[7] to the number of carrier routes, the number of rented post office box sections, and peak window use. We based earned facility size on Postal Service criteria[8] for planning new space projects, which differ from existing Postal Service initiatives,[9] because it focuses on the total facility size not specific retail or delivery operations. We

[6] We used Postal Service criteria established in March 2007 and outlined in a letter issued by the senior vice president of Operations. In support of these new criteria, the headquarters Facility Group, Planning and Approval, designed matrices to assist with the space requirements of planned facilities.
[7] WebBATS Monthly Summary Data for issued Post Office Box information, Intelligent Mail and Address Quality Delivery Statistics Summary for route information, and Retail Data Mart for earned peak modeled window staffing.
[8] Space Requirements Matrix for Non-Flat Sequencing System offices.
[9] SBOC and Facilities Optimization programs.

calculated excess space by taking the difference between earned facility size and actual interior square footage reported in the electronic Facilities Management System (eFMS).

We conducted this performance audit from June 2010 through January 2011 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 January 14, 2011, and included their comments where appropriate.

We assessed the reliability of facility-related data by verifying the accuracy of computer-generated information through observations during facility tours and interviewing agency officials knowledgeable about the data. We determined the data 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	Monetary Impact	Report Results
Facility Optimization: Northern New Jersey District	DA-AR-10-008	8/25/2010	$157,963,990	The OIG identified 1.98 million SF of excess space. Management agreed with the recommendations but disagreed with the monetary impact.
Facility Optimization: Chicago District	DA-AR-10-009	8/25/2010	$23,517,019	The OIG identified 740,000 SF of excess space. Management agreed with recommendations but disagreed with the monetary impact.
Facility Optimization : New York District	DA-AR-10-010	8/25/2010	$446,258,222	The OIG identified 2.4 million SF of excess space. Management agreed with recommendations but disagreed with the monetary impact.
Restructuring the U.S. Postal Service to Achieve Sustainable Financial Viability	GAO-09-937SP	7/28/2009	None	The Government Accountability Office (GAO) added the Postal Service's financial condition to the list of high-risk areas needing Congress' attention and the executive branch to achieve broad-based transformation. It recognized the need to reduce the facility infrastructure. There was no management response in the report.

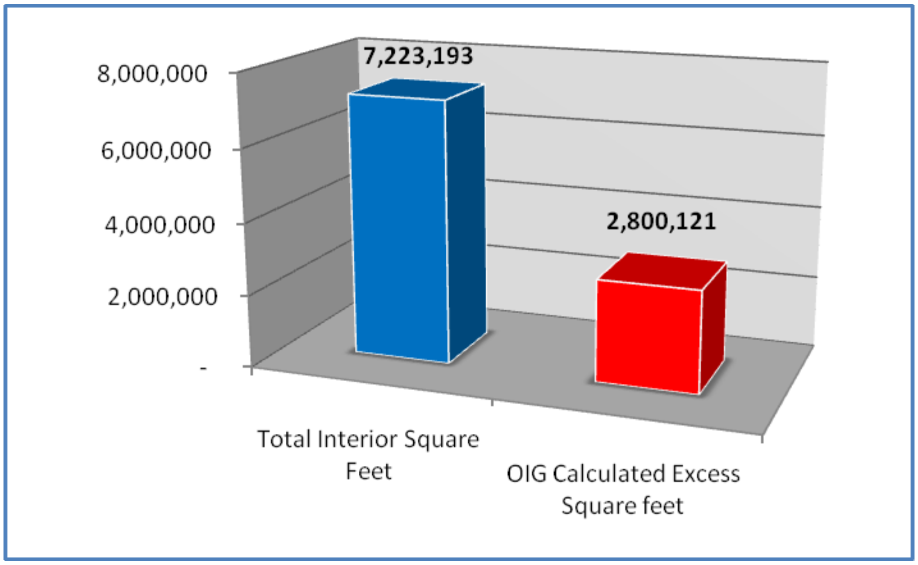
Report Title	Report Number	Final Report Date	Monetary Impact	Report Results
Federal Real Property: An Update on High Risk Issues	GAO-09-801T	7/15/2009	None	Federal agencies have taken some positive steps to address real property issues but some core problems leading to the designation of this area as high risk continue to persist. There was no management response in the report.
Network Rightsizing Needed to Help Keep USPS Financially Viable	GAO-09-674T	6/20/2009	None	In a number of areas, the Postal Service will require actions, such as rightsizing its retail and mail processing networks by consolidating operations and closing unnecessary facilities. Management generally agreed with the accuracy of the statements and provided technical comments, which were incorporated.

APPENDIX B: DETAILED ANALYSIS

Excess Space is Significant in the Eastern Area

Based on facility space requirements, we calculated that the districts reviewed in the Eastern Area maintain 2.8 million more square feet than they need for current operational workload. As depicted in Chart 1, excess space was at least 39 percent of the total interior square footage.

Chart 1 – Area Interior and Excess Space Comparison



The breakdown of interior square footage and OIG-calculated excess for the 72 visited facilities in the Eastern Area is represented in Table 2. Main post offices contributed to 54 percent of the excess space, while branches, stations, carrier annexes contributed to smaller amounts (with 19, 17, and 7 percent, respectively). Plants were optimizing space by integrating workload from surrounding stations.

Table 2 – Excess Space by Facility Type Visited

Facility Type	Facility Type Count	Percentage of Count	Percentage of Excess	OIG-Calculated Excess SF	Interior Square Footage
Main Post Office	39	54%	56%	548,493	960,693
Branch	14	19	15	148,808	280,008
Station	12	17	19	186,225	270,225
Carrier Annex	5	7	9	83,237	451,852
Finance Station	2	3	1%	7,944	10,844
Total	**72**	**100%**	**100%**	**974,707**	**1,973,622**

To highlight excess space in the Eastern Area, Illustration 1 depicts two facilities with vacant offices and excess space. The Grafton Main Post Office is Postal Service-owned and has delivery and retail operations and vacant space. The Courthouse Danville Post Office is another Postal Service-owned facility with delivery operations and significant vacant space on the workroom floor. According to our calculations, sites visited contained excess interior space ranging from 1,393 SF to 64,600 SF.

Illustration 1 – Examples of Excess Space

Grafton Main Post Office 260 W Main St Grafton, WV 26354-9998 Interior Square Footage: 17,575 OIG-Calculated Excess SF: 13,675	**Courthouse Danville** 700 Main St Danville, VA 24541-9993 Interior Square Footage: 47,172 OIG-Calculated Excess SF: 45,172
	
Entire floor of vacant offices	Unused workroom floor

Causes for Excess Interior Space

The opportunity to optimize excess interior space in the Eastern Area exists because:

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

Guidance Can Be Improved

A review of the facility database user guide's workload-driven space requirements show the guide does not provide sufficient guidance for identifying excess space. 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. Although we identified excess interior space at the 72 Postal Service facilities we visited, we found only one location that answered "yes" to the vacant leasable space survey question. Further, interviews revealed that Operations employees were unaware of how to identify excess space at their facilities. As a result, we identified more than 2.8 million SF of excess interior space in the Appalachian, Western Pennsylvania, and Western New York Districts.

Facility Systems Do Not Allow for Effective Management of Excess Space

The Postal Service's workload has declined, resulting in significant excess space. However, the electronic system that manages facility space does not collect or monitor metrics such as length of time that space is underused or vacant and the condition of excess space to prioritize disposal actions efficiently.

For comparison, we benchmarked Postal Service facility practices against the General Services Administration's (GSA's) realty management practices and found the GSA "ages" its available space for tracking, monitoring, and decision-making. The Postal Service is not able to age excess space because it does not collect dates on entry.

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. Similarly, GSA-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's facility management systems are not able to manage property this way. For example, rents from leases or subleases are tracked manually using electronic spreadsheets.

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, eFMS is not reliable for identifying how much excess space is available in postal plants. The Postal Service plans to measure plants and update its facility database. To complete this task, industrial engineers, working with local in-plant support, use blueprints to identify processing equipment, staging areas, and manual work areas as well as to identify excess space.

We estimate that if the Eastern Area initiated disposal actions for the districts we reviewed it could realize $190,656,882[10] over typical and remaining lease terms. We consider this amount funds that could be used more efficiently by implementing recommended actions. See Appendix C for the monetary impact calculation and assumptions.

[10] The annualized savings is $19,065,688.

Opportunity to Fill Federal Space Needs

The GSA is the nation's largest public real estate organization. It provides workspace for more than 1.2 million federal workers through its Public Buildings Service. According to the Code of Federal Regulations (CFR), when GSA-controlled space is unavailable, federal agencies must extend priority consideration to available space in Postal Service buildings.[11]

Our audit noted that the Postal Service could more aggressively seek federal entities to fill excess space. Table 3 illustrates the potential fulfillment opportunities in each of the three districts we reviewed in the Eastern Area. Specifically, it shows that on behalf of federal entities, the GSA leases primarily from the commercial sector rather than from the Postal Service. Space requirements were greater than the excess space identified in Postal Service facilities. The GSA paid considerably more per square foot than the value assigned to the Postal Service space.[12]

Table 3 – Postal Service Excess Space Lease Opportunity

Districts	GSA Leased SF	USPS Excess SF	GSA Count	USPS Count	Existing GSA/ USPS Leases	GSA Average SF Cost	USPS Average SF Value	Number of GSA Leases Excess Space May Accommodate	
Appalachian	2,334,985	933,750	145	416	4	$19.48	$9.32	91 of 145	63%
Western NY	1,448,916	754,500	90	247	1	23.70	11.93	68 of 90	76
Western PA	1,668,874	1,226,187	129	509	1	20.28	19.99	91 of 129	71
Totals	**5,452,775**	**2,914,437**	**364**	**1,172**	**6**	**$20.84**	**$14.48**	**250 of 364**	**69%**

Table 3 and Appendix D also illustrate the strong correlation between space leased by the GSA and the ability of Postal Service to significantly accommodate federal space needs. For the districts reviewed, we estimate that Postal Service excess space may accommodate 250 of 364 current federal leases (69 percent). However, we understand that more information would be needed before determining whether the Postal Service's excess space would be suitable.

[11] 41 CFR 102-73.25
[12] We assigned Postal Service excess space a value based on historical lease rates in the same geographic areas.

APPENDIX C: MONETARY AND OTHER IMPACT FUNDS PUT TO BETTER USE

Western New York Excess Interior Space Monetary Impacts

Project year	0	1	2	3	4	5	6	7	8	9
Fiscal year	**2011**	**2012**	**2013**	**2014**	**2015**	**2016**	**2017**	**2018**	**2019**	**2020**
Owned										
Sublease Value	-$20,047,819	$6,389,254	$6,389,254	$6,389,254	$6,389,254	$6,389,254	$6,389,254	$6,389,254	$1,597,314	
Custodial Savings		$1,054,128	$1,054,128	$1,054,128	$1,054,128	$1,054,128	$1,054,128	$1,054,128	$263,532	
Utility Savings		$1,163,390	$1,190,148	$1,217,521	$1,245,524	$1,274,171	$1,303,477	$1,333,457	$341,032	
Leases Expiring FY 2011										
Sublease Value	-$836,464	$266,582								
Custodial Savings		$43,982								
Utility Savings		$48,541								
Leases Expiring After FY 2011										
Sublease Value	-$7,355,930	$2,344,340	$2,344,340	$2,238,855	$2,104,467	$2,076,375	$432,223	$350,989	$263,540	$156,432
Custodial Savings		$386,780	$386,780	$369,376	$347,204	$342,570	$71,310	$57,908	$43,480	$25,809
Utility Savings		$426,870	$436,688	$426,631	$410,246	$414,079	$88,178	$73,252	$56,267	$34,167
Subtotals	-$28,240,213	$12,123,866	$11,801,338	$11,695,765	$11,550,823	$11,550,576	$9,338,571	$9,258,988	$2,565,164	$216,408
Cash Flows @ Sublease Efficiency Rate	-$24,484,265	$10,511,392	$10,231,760	$10,140,228	$10,014,563	$10,014,350	$8,096,541	$8,027,543	$2,223,997	$187,626
Discounted at Postal Service cost of borrowing	-$24,484,265	$10,119,270	$9,482,618	$9,047,209	$8,601,771	$8,280,710	$6,445,154	$6,151,845	$1,640,763	$133,258

	Net Present Value:	**$35,418,333**	
Build-Out Costs SF	$37.43	Utilities Savings SF per Year	$2.17
Lease Savings SF per Year	$11.93	Utility Cost Escalation Rate	2.30%
Postal Service Cost of Borrowing	3.875%	Custodial Rate SF	$1.97

Western Pennsylvania Excess Interior Space Monetary Impacts

Project year	0	1	2	3	4	5	6	7	8	9
Fiscal year	**2011**	**2012**	**2013**	**2014**	**2015**	**2016**	**2017**	**2018**	**2019**	**2020**
Owned										
Sublease Value	-$10,518,480	$15,848,539	$15,848,539	$15,848,539	$15,848,539	$15,848,539	$15,848,539	$15,848,539	$3,962,135	
Custodial Savings		$1,342,002	$1,342,002	$1,342,002	$1,342,002	$1,342,002	$1,342,002	$1,342,002	$335,500	
Utility Savings		$1,374,782	$1,406,402	$1,438,750	$1,471,841	$1,505,693	$1,540,324	$1,575,752	$402,999	
Leases Expiring FY 2011										
Sublease Value	-$1,375,523	$2,072,545								
Custodial Savings		$175,496								
Utility Savings		$179,783								
Leases Expiring After FY 2011										
Sublease Value	-$4,044,139	$6,093,437	$6,093,437	$4,589,320	$3,698,062	$3,686,910	$595,810	$496,316	$496,316	$460,339
Custodial Savings		$515,972	$515,972	$388,608	$313,140	$312,195	$50,451	$42,026	$42,026	$38,980
Utility Savings		$528,576	$540,733	$416,624	$343,436	$350,276	$57,907	$49,347	$50,481	$47,899
Subtotals	-$15,938,142	$28,131,132	$25,747,085	$24,023,843	$23,017,020	$23,045,615	$19,435,034	$19,353,981	$5,289,457	$547,218
Cash Flows @ Sublease Efficiency Rate	-$13,818,369	$24,389,691	$22,322,723	$20,828,672	$19,955,757	$19,980,548	$16,850,175	$16,779,902	$4,585,959	$474,438
Discounted at Postal Service cost of borrowing	-$13,818,369	$23,479,847	$20,688,313	$18,583,541	$17,140,522	$16,521,604	$13,413,379	$12,859,147	$3,383,311	$336,962

	Net Present Value:	**$112,588,257**	
Build-Out Costs SF	$13.27	Utilities Savings SF per Year	$1.73
Lease Savings SF per Year	$19.99	Utility Cost Escalation Rate	2.30%
Postal Service Cost of Borrowing	3.875%	Custodial Rate SF	$1.69

Appalachian Excess Interior Space Monetary Impacts

Project year	0	1	2	3	4	5	6	7	8	9
Fiscal year	**2011**	**2012**	**2013**	**2014**	**2015**	**2016**	**2017**	**2018**	**2019**	**2020**
Owned										
Sublease Value	-$5,924,703	$4,363,817	$4,363,817	$4,363,817	$4,363,817	$4,363,817	$4,363,817	$4,363,817	$1,090,954	
Custodial Savings		$811,668	$811,668	$811,668	$811,668	$811,668	$811,668	$811,668	$202,917	
Utility Savings		$719,350	$735,895	$752,820	$770,135	$787,848	$805,969	$824,506	$210,867	
Leases Expiring FY 2011										
Sublease Value	-$356,216	$262,370								
Custodial Savings		$48,801								
Utility Savings		$50,547								
Leases Expiring After FY 2011										
Sublease Value	-$4,713,194	$3,471,485	$3,471,485	$3,208,854	$2,877,680	$2,737,118	$1,338,037	$855,447	$531,773	$284,366
Custodial Savings		$645,694	$645,694	$596,845	$535,247	$509,103	$248,874	$159,113	$98,910	$52,892
Utility Savings		$668,803	$684,185	$646,970	$593,543	$577,536	$288,821	$188,899	$120,126	$65,715
Subtotals	-$10,994,113	$11,042,534	$10,712,745	$10,380,975	$9,952,091	$9,787,090	$7,857,187	$7,203,451	$2,255,548	$402,974
Cash Flows @ Sublease Efficiency Rate	-$9,531,896	$9,573,877	$9,287,949	$9,000,305	$8,628,463	$8,485,407	$6,812,181	$6,245,392	$1,955,560	$349,378
Discounted at Postal Service cost of borrowing	-$9,531,896	$9,216,729	$8,607,911	$8,030,159	$7,411,213	$7,016,451	$5,422,755	$4,786,107	$1,442,723	$248,140

	Net Present Value:	**$42,650,292**	
Build-Out Costs SF	$12.65	Utilities Savings SF per Year	$1.79
Lease Savings SF per Year	$9.32	Utility Cost Escalation Rate	2.30%
Postal Service Cost of Borrowing	3.875%	Custodial Rate SF	$1.73

Value Assigned to the Excess Space

Table 4 shows the value per square foot for each district. We calculated this figure by dividing total interior square footage by total lease costs.

Utility Costs Associated with the Excess Space

Table 4 shows the utility cost per square foot for each district. Using the information from line 42 of the financial performance report (FPR), we calculated this figure by dividing the total annual utility expenses by the district's total interior square footage, with a cost escalation rate of 2.3 percent.

Maintenance Costs Associated with the Excess Space

Table 4 shows the maintenance cost per square foot for each district. We calculated this cost by dividing the total annual maintenance expenses[13] 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.[14]

Build-Out Costs Associated with Implementing Optimization Actions

Table 4 shows the build-out cost per square foot for each district. We calculated this figure by dividing the build-out costs for all approved optimization node studies in each district by the total reduction in square footage identified in the approved node studies.

For the Appalachian, Western Pennsylvania, and Western New York Districts, we calculated the average build-out cost and then removed "outliers," such as items with no build-out costs or items whose build-out cost per square foot was not aligned with the emerging range of costs to generate a new build-out cost.

Table 4 – Square Footage Costs by District

District	Lease Cost/SF	Utility Cost/SF	Maintenance Cost/SF	Build-out Cost/SF[15]
Appalachian	$9.32	$1.79	$3.47	$12.65
Western Pennsylvania	$19.99	$1.73	$3.38	$13.27
Western New York	$11.93	$2.17	$3.94	$37.43

[13] eFlash (Labor Distribution Code 38, salary and benefits) + FPR Line 3F Contract Cleaners Costs.
[14] *Custodial Maintenance* (Report Number DA-AR-09-011, dated August 13, 2009).
[15] Although build-out costs are negotiable and at times, paid for by the lessor, these costs ranged from $0 per SF to $52.84 per SF in the node studies analyzed.

Ownership of Facility and Term Years

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

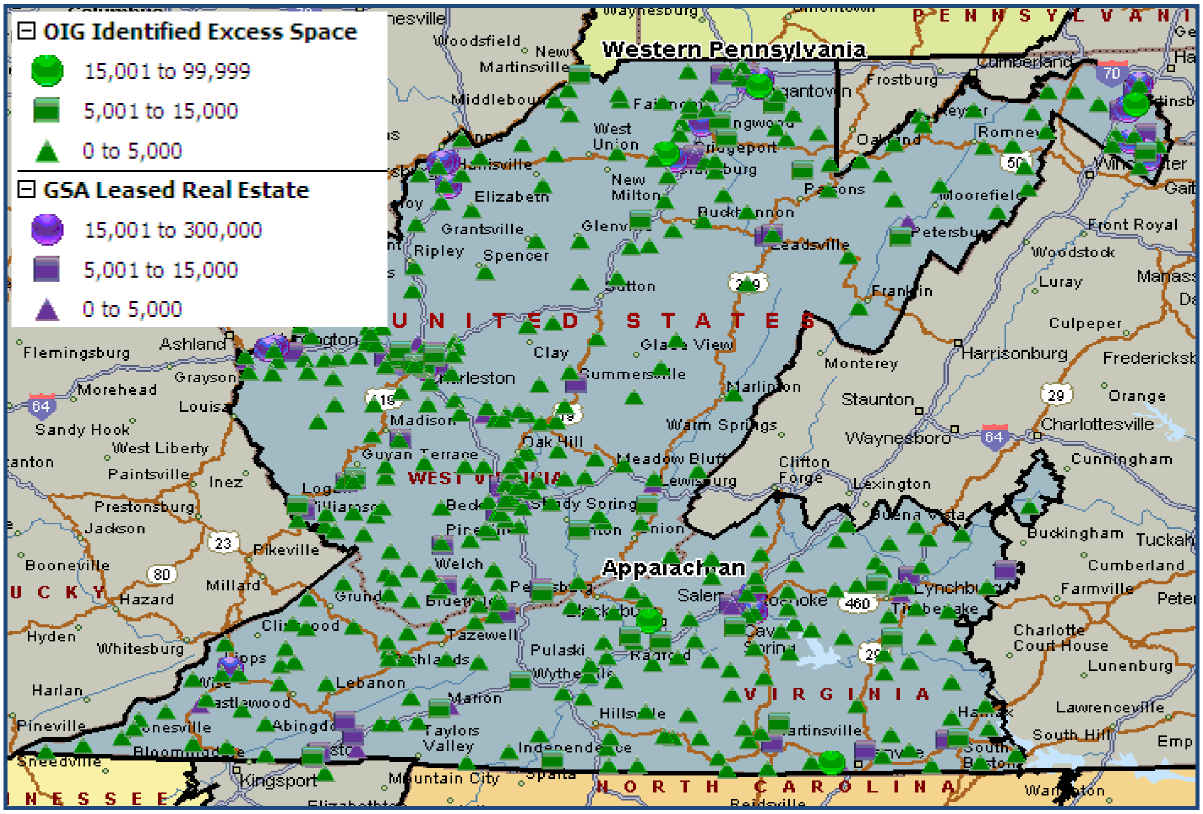
We calculated impact for leases expiring before the end of FY 2011 based on the assumption that these leases would be renewed for the standard 5-year period. We calculated leases expiring after October 1, 2011, for the remaining lease term. We calculated Postal Service-owned facilities over a period of 7.3 years, which was the historical national average lease term.

Sublease Efficiency Rate

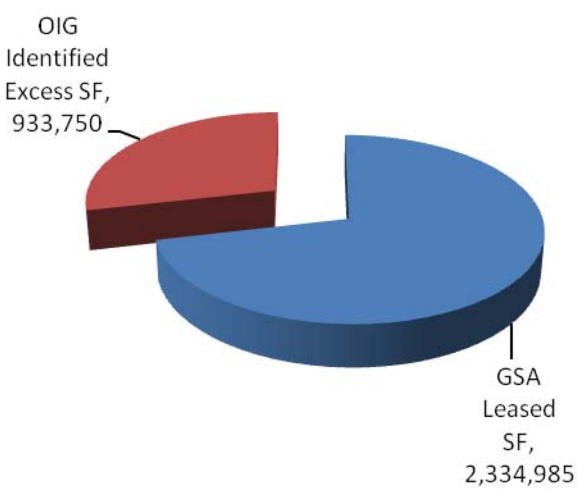
We identified the national commercial property vacancy rate from the National Realty Association for industrial and retail space as 13.3 percent, so we reduced the net present value savings realization to an 86.7 percent "success rate."

APPENDIX D: GSA-LEASED PROPERTIES COMPARED TO POSTAL SERVICE EXCESS SPACE

Appalachian District

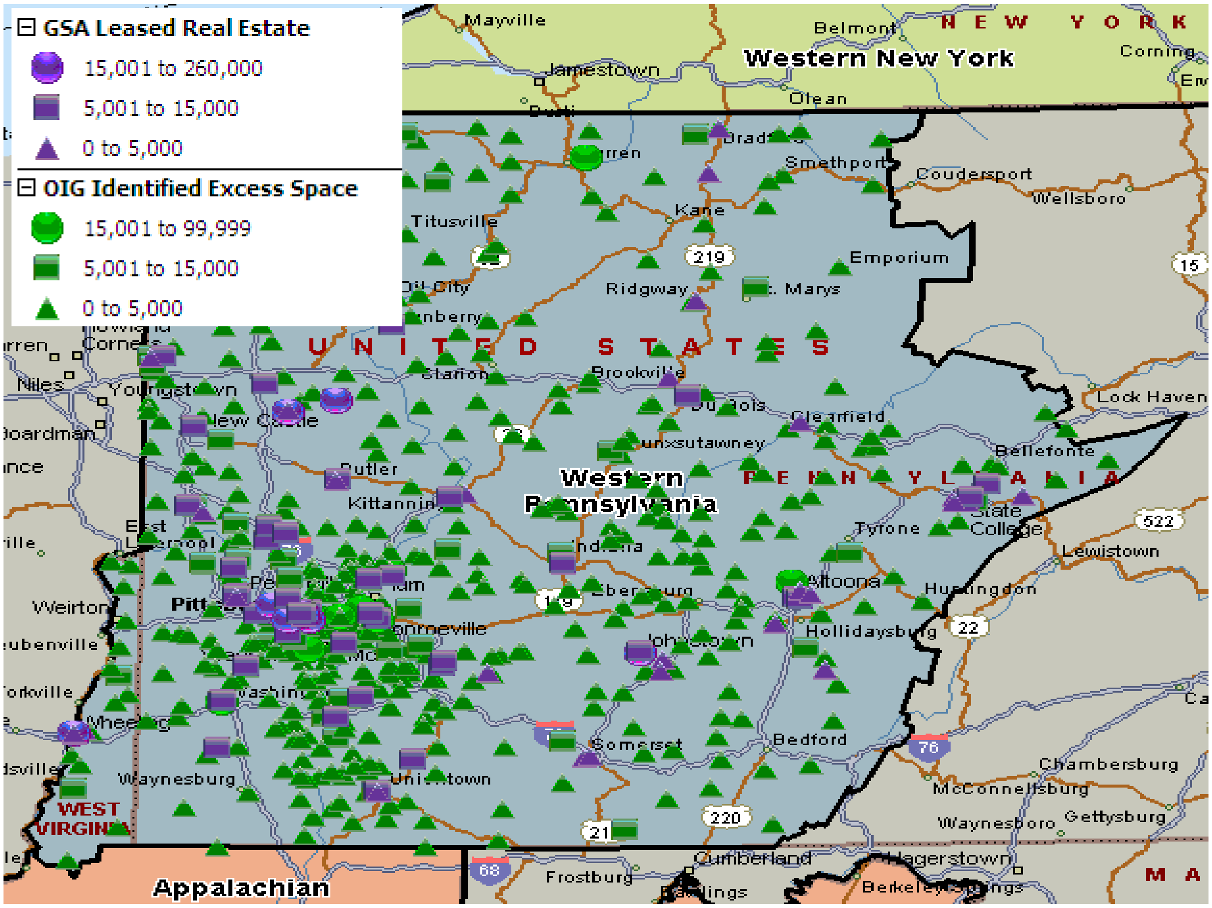


The pie chart illustrates the ratio of Postal Service excess space to GSA-leased commercial space. The following table provides additional analysis by placing the real estate into size categories to further assess supply versus demand.

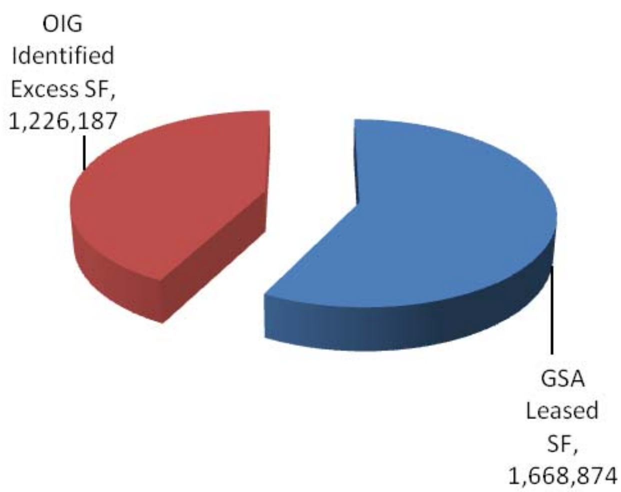


Building Size	GSA Leased Facilities	OIG Identified Excess
1,000	14	217
5,000	42	164
10,000	42	19
20,000	21	11
30,000	9	2
40,000	5	1
50,000	1	1
More	11	1
Total Count	145	416

Western Pennsylvania District

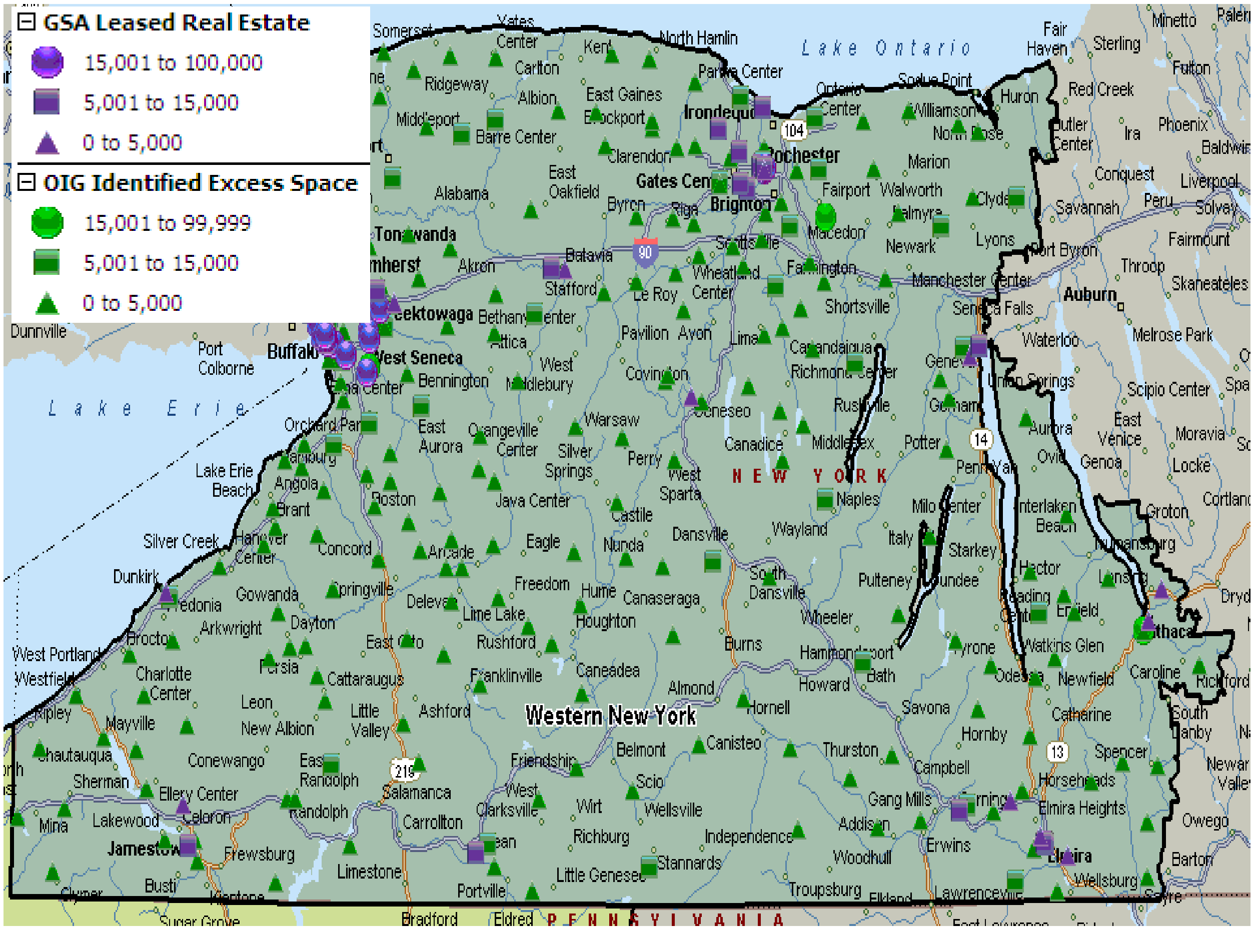


The pie chart illustrates the ratio of Postal Service excess space to GSA-leased commercial space. The following table provides additional analysis by placing the real estate into size categories to further assess supply versus demand.



Building Size	GSA Leased Facilities	OIG Identified Excess
1,000	19	325
5,000	37	125
10,000	42	35
20,000	16	16
30,000	6	2
40,000	1	1
50,000	1	3
More	7	2
Total Count	**129**	**509**

Western New York District



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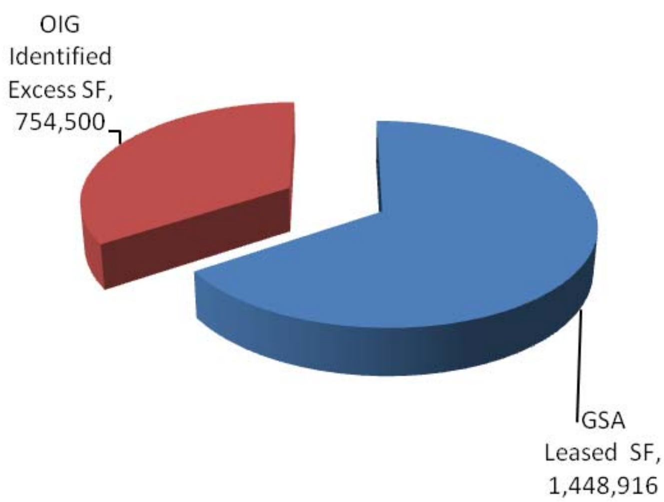

Building Size	GSA Leased Facilities	OIG Identified Excess
1,000	9	109
5,000	20	94
10,000	24	25
20,000	11	15
30,000	9	3
40,000	9	1
50,000	0	0
More	8	0
Total Count	90	247

APPENDIX E: MANAGEMENT'S COMMENTS

JORDAN M. SMALL
VICE PRESIDENT, AREA OPERATIONS
EASTERN AREA

UNITED STATES POSTAL SERVICE

February 4, 2011

LUCINE M. WILLIS, DIRECTOR
AUDIT OPERATIONS @ audittracking@uspsoig.gov

SUBJECT: Facility Optimization: Eastern Area
Report Number DA-AR-11-DRAFT

Management appreciates the efforts the Office of Inspector General (OIG) has taken in regards to facility optimization in the Eastern Area. 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 2 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 updated in 2005, 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

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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 sf 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 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:

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

Management Recommended Methodology

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 2.8 million square feet of excess space exist in the Eastern Area with a potential to realize $190,656,882 over typical and remaining lease terms. The OIG also provides two specific examples of excess space; Grafton, WV Main Post Office and the Danville, VA Courthouse.

Management disagrees with these findings in general as we have stated in our responses to DA-AR-10-010 and DA-AR-10-011. More specifically in regard to the two examples, the following is provided:

The Grafton, WV MPO is a USPS owned facility with a net interior of 17,575 SF. The OIG states it has 13,675 SF of excess space. This is a four story building first occupied in 1914. Management agrees there is excess space but estimates it to be ~9,600 SF, not 13,675. Part of the difference may be attributable to the 1,660 feet of unusable basement space.

Primary challenges to outleasing this space includes the following:

- The vacant space is primarily on upper floors of the building. In order to access this space, it is necessary to pass through the USPS space. This is not acceptable for security reasons. It would be necessary to spend considerable

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expense to build an alternative entrance to access this space. Note this access must be handicap accessible which would require an elevator.

- This building is on the historic register. Any improvements would be required to meet historic preservation requirements which greatly adds to the cost. See photos below.
- The vacant spaces do not currently meet current building codes. Significant expense would be required to update restrooms and life safety systems. See photos below.
- The vacant space is in relatively poor condition.
- The OIG estimates $12.65/SF to build out this space to leasable condition. Management estimates the cost closer to a minimum of $100/SF given the current condition, age, and need for alternative access. With further evaluation, it may be found to be impractical even at this cost.

The Danville Courthouse (Danville Downtown Station) is a USPS owned facility first occupied in 1934. Management agrees there is excess space in this facility. The USPS has been aggressively working to dispose of this building for over three years. Although GSA has courts in this building, GSA has repeatedly stated they are not interested in purchasing.

Potential Revenue:

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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.

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.
3. Management will continue to make available our excess property to other federal agencies.

Actions 1&2 will be completed by end of quarter 2, fiscal year 2011. Action 3 will be completed by end of quarter 3, fiscal year 2011. Regarding the audit recommendations:

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

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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
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 180 properties identified for disposal and 326 leases that we have or will terminate.

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.

Jordan M. Small

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