



May 13, 2011

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VICE PRESIDENT, OPERATIONS, PACIFIC AREA

SUBJECT: Audit Report – Facility Optimization: Pacific Area Districts
(Report Number DA-AR-11-006)

This report presents the results of our audit of facility optimization in the Pacific Area (Project Number 11YG008DA000). The U.S. Postal Service Office of Inspector General (OIG) initiated this audit from a random sample of districts nationwide. For the Pacific Area, our objective was to identify opportunities to optimize existing real estate in the Bay Valley and Los Angeles Districts. See [Appendix A](#) for additional information about this audit.

The Pacific Area uses 365 facilities with 7,651,122 interior square feet (SF) in the two districts noted previously. Although the area employs these facilities, it has experienced a significant reduction in workload in recent years. From fiscal years (FYs) 2005 to 2010, mail volume in the Pacific Area has dropped 18 percent. Likewise, mail volume in the Bay Valley and Los Angeles Districts has decreased by 34 percent and 36 percent, respectively. This reduction in workload provides an opportunity to reevaluate space needs and identify potential excess space.

Conclusion

The districts analyzed in the Pacific Area have more than 1.7 million SF in excess of what their workload suggests they need. The U.S. Postal Service has the option to optimize excess real property 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 taking action to optimize existing space. Specifically, the Pacific Area plans to dispose of 305,015 SF of this excess through approved optimization projects, with another 49,636 SF scheduled for evaluation in FY 2011 for the two districts selected for our review. Although it has made progress, the Postal Service can do more to dispose of excess interior space more quickly.

The opportunity to optimize 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 effectively accomplish this task.
- 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 Pacific Area initiates disposal¹ action for the excess space we identified, there is an opportunity to realize \$172,248,822² 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 that the Postal Service could be more aggressive in seeking opportunities to fill the space needs of federal entities. In the districts reviewed, our analysis shows that excess space identified at Postal Service facilities may be able to accommodate 84 percent of current federal agencies' space needs. This opportunity exists because the Postal Service has not capitalized on the priority status it has for filling federal agencies' space needs. By capitalizing on this status, the Postal Service has another option for reducing its facility infrastructure size and generating additional revenue. See [Appendix D](#) for more information.

We recommend the vice president, Operations, Pacific Area, district managers, area managers, and the Pacific 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.

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 \$17,224,882.

³ Funds that could be used more efficiently by implementing recommended actions. This amount does not include excess SF that is part of an approved node study.

Management's Comments

Management agreed with our recommendations. They stated they have put in place corrective actions to address the first two recommendations and will complete corrective action to address the third recommendation by the end of Q3, FY 2011. While management agreed with our recommendations, management did not agree with the amount of excess space or the potential monetary impact reported. Specifically, they disagreed with the method we used to calculate existing excess space, in addition to the data and cost factors used to value the excess space and calculate the 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. The audit treats every square foot as usable and leasable.
2. Unique operational functions not included in standard designs, such as administrative, district office, training, caller service, etc.
3. Inefficiencies in current building layout due to multiple floors, stairs, elevators, columns, redundant support space required on each floor due to code requirements.
4. Historic property.
5. Parking and dock space requirements.
6. Large inflexible retail lobbies.
7. Automation support and traffic conditions.

In reference to the data and cost factors used in our calculations, management disagreed with the findings in general as stated in responses to prior audits. Management specifically disagreed with the average build-out cost used in our calculations, citing a range of costs they deem reasonable based on actual project costs.

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 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 square feet, which represents 16 percent of buildings and 76 percent of interior square feet. 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

The OIG considers management's comments responsive to the recommendations, and management's corrective actions 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. According to commercial realty standards, basement space is counted as usable and leasable areas. Mechanical rooms are considered common areas that a proportionate share is allocated to a tenant's area. 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, and thus, enclosed parking and dock spaces, automation support, and traffic conditions 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. Although 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, such as bulk mail entry units or delivery bar code sorters, and allotted the necessary space for those functions. Additionally, we applied the non-Flats Sequencing System (FSS) rate of 123 SF per route to determine the earned delivery space, rather than the post-FSS rate of 95 SF per route. Lastly, we did not consider performance measures such as street efficiency indicator or alternate access sales in the earned space calculation.

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 area as presented in its node studies. We note that

⁴ www.boma.org

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 district. Further, the multiple 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 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 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.

E-Signed by Mark Duda
VERIFY authenticity with e-Sign


Mark W. Duda
Deputy Assistant Inspector General
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Attachments

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APPENDIX A: ADDITIONAL INFORMATION

BACKGROUND

The Pacific Area leases or owns 365 facilities with more than 7 million interior SF to move mail in the Bay Valley and Los Angeles districts. 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, the Postal Service's Facilities and Retail Management organizations have implemented initiatives to optimize space, namely, the 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 Pacific Area has four approved optimization studies in the Bay Valley District and seven in the Los Angeles 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. As of the February 26, 2010, filing, management was considering the following facilities for closure: Kaiser Center, Landscape, Mills College, Niles, Oakland Station B, Park Station, Richmond Station A in the Bay Valley District, Federal Finance Station, Galleria Station, and the Hollywood Pavilion Store in the Los Angeles District.

In addition to the ongoing node studies⁵ and SBOC program, both districts have taken action to use space and provide alternative services by selling Hallmark cards in existing lobby space in several facilities.

In October 2010, the Postal Service consolidated optimization efforts to manage excess space. The goal is to manage the excess space portfolio for 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 mail processing plants, retail facilities, small delivery units, administrative space, and carrier delivery facilities in one overall optimization effort. This integrated effort between Facilities Headquarters and the field offices will use computer modeling and equipment analysis along with local analysis and metro planning to form headquarters and district/area partnerships.

To supplement and expand on existing Postal Service initiatives, the OIG developed a Real Estate Risk Model to identify and prioritize emerging facility risk. The risk model measures facility performance results by district for the following nine metrics in Table 1:

⁵ Studies of consolidation for sites in a geographic radius.

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 interior space nationally; the two districts selected were in the Pacific Area.

OBJECTIVE, SCOPE, AND METHODOLOGY

Our objective was to identify opportunities for the Postal Service’s Pacific Area to optimize existing real estate. We visited 102 of 365 facilities in the Bay-Valley and Los Angeles districts, representing 33 percent of the OIG-calculated excess space when actual interior space is compared to 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 earned⁶ facility size, we compared the workload data from Postal Service databases⁷ to the number of carrier routes, the number of rented post office box sections, and peak window use. We based the earned facility size on Postal Service criteria⁸ for planning new space projects, which differs from existing Postal Service initiatives⁹ because it focuses on the total facility size, not specific retail or delivery operations. We calculated excess space by taking the difference between earned facility size and actual interior square footage reported in the electronic Facilities Management System (eFMS). For the plants, the local in-plant support provided us the excess space data which we assessed for reasonableness.

We conducted this performance audit from December 2010 through May 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

⁶ We used Postal Service criteria established in March 2007, outlined in a letter issued by the senior vice president of Operations. In support of this 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.

our findings and conclusions based on our audit objective. We discussed our observations and conclusions with management on April 5, 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 that 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
<i>Facility Optimization: Western Area Districts</i>	DA-AR-11-001	2/7/2011	\$173,835,881	The OIG identified 4.5 million SF of excess space. The Postal Service agreed with the recommendations but disagreed with the monetary impact.
<i>Facility Optimization: Northern New Jersey District</i>	DA-AR-10-008	8/25/2010	\$157,963,990	The OIG identified 1.98 million SF of excess space. The Postal Service agreed with recommendations but disagreed with the monetary impact.
<i>Facility Optimization: Chicago District</i>	DA-AR-10-009	8/25/2010	\$23,517,019	The OIG identified 740,529 SF of excess space. The Postal Service agreed with recommendations but disagreed with the monetary impact.
<i>Facility Optimization: New York District</i>	DA-AR-10-010	8/25/2010	\$446,258,222	The OIG identified 2.4 million SF of excess space. The Postal Service agreed with recommendations but disagreed with monetary impact.
<i>Restructuring the U.S. Postal Service to Achieve Sustainable Financial Viability</i>	GAO-09-937SP	7/28/2009	None	The Government Accountability Office (GAO) added the U.S. 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 Postal Service response in the report.
<i>Federal Real Property: An Update on High-Risk Issues</i>	GAO-09-801T	7/15/2009	None	Federal agencies have taken some positive steps to address real property issues, but some of the core problems that led to designation of this area as high risk continue to persist. There was no Postal Service response in the report.

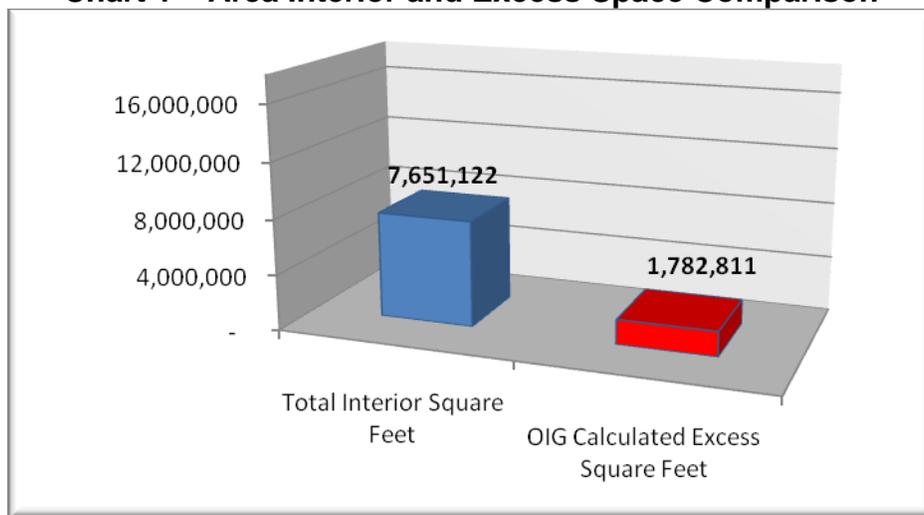
Report Title	Report Number	Final Report Date	Monetary Impact	Report Results
<i>Network Rightsizing Needed to Help Keep USPS Financially Viable</i>	GAO-09-674T	5/20/2009	None	The Postal Service will require action in a number of areas; such as, rightsizing its retail and mail processing networks by consolidating operations and closing unnecessary facilities. The Postal Service generally agreed with the accuracy of the statements and provided technical comments, which were incorporated.

APPENDIX B: DETAILED ANALYSIS

Excess Space is Significant in the Pacific Area

Based on facility space requirements,¹⁰ we calculated that the districts reviewed in the Pacific Area maintain more than 1.7 million SF more than what is required for current operational workload and thus can be considered potential excess space. As depicted in Chart 1, excess space was 23 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 102 visited facilities in the Pacific Area is represented in Table 2. Main post offices contributed 52 percent of the excess space, while stations (23 percent), carrier annexes (12 percent), and plants (7 percent) followed to a lesser degree.

Table 2 – Excess Space by Facility Type Visited

Facility Type	Facility Type Count	Percentage of Count	Percentage of Excess	OIG-Calculated Excess	Interior Square Footage
Main Post Office	46	45%	52%	735,483	1,373,654
Station	29	28%	23%	323,844	918,611
Carrier Annex	13	13%	12%	162,215	318,405
Plant	4	4%	7%	95,291	1,484,230
Finance Station	6	6%	4%	52,724	75,824
Branch	4	4%	3%	36,828	74,028
Total	102	100%	100%	1,406,385	4,244,752

¹⁰ We used Postal Service criteria established in March 2007 outlined in a letter issued by the senior vice president of Operations. In support of this new criteria, the Headquarters Facility Group, Planning and Approval, designed matrices to assist with the space requirements of planned facilities.

To highlight excess space in the Pacific Area, Illustration 1 depicts two facilities with excess interior space. The Alameda Main Post Office is a leased facility with delivery and retail operations and significant vacant space on the workroom floor. The Maywood Branch is a Postal Service-owned facility with retail operations and also maintains significant vacant space on the workroom floor. According to our calculations, 94 percent of the sites visited contained excess space, ranging from 200 to 145,600 SF.

Illustration 1 – Examples of Excess Space

<p>Alameda Main Post Office 2201 Shoreline Dr Alameda, CA 94501 Interior Square Footage: 54,040 OIG Calculated Excess SF: 37,940</p> 	<p>Maywood Branch 4357 S Lauson Ave Maywood, CA 90270 Interior Square Footage: 24,382 OIG Calculated Excess SF: 22,382</p> 
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[Causes for Excess Interior Space](#)

The opportunity to optimize excess interior space in the Pacific Area 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 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. Although we identified excess space at 96 of the 102 Postal Service facilities we visited, only two locations answered “yes” to

the vacant leasable space survey question. As a result, we identified more than 1.7 million of excess square footage in the Bay-Valley and Los Angeles districts.

[Facility Systems Do Not Allow for Effective Management of Excess Space](#)

The Postal Service is experiencing a considerable workload decline that has resulted in significant excess space. However, the electronic system that manages facility space does not collect or monitor metrics, such as whether length-of-time space is underused or vacant and the condition of excess space 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 it does not collect dates on entry.

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 unable to manage property in this manner. 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, 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, industrial engineers, working with local in-plant support, are using blueprints to identify processing equipment, staging areas, and manual work areas and identify excess space.

We estimate if the Pacific Area initiated disposal actions, there is a potential opportunity to realize \$172,248,822¹¹ over typical and remaining lease terms. This amount is considered funds that could be used more efficiently by implementing recommended actions. See [Appendix C](#) for the monetary impact calculation and assumptions.

¹¹ The annualized savings would be \$17,224,882.

Opportunity to Fulfill Federal Space Needs

GSA is the nation's largest public real estate organization. It provides workspace for more than 1 million federal workers through its Public Buildings Service. According to the Code of Federal Regulations (CFR), in situations when GSA-controlled space is not available, federal agencies must extend priority consideration to available space in Postal Service buildings.¹²

Our audit noted that the Postal Service can be more aggressive in seeking opportunities to fill the space needs of federal entities. Table 3 illustrates the potential fulfillment opportunities in both districts reviewed in the Pacific Area. Specifically, it shows that GSA leases on behalf of federal entities primarily from the commercial sector rather than the Postal Service. Space requirements were greater than the excess space identified in Postal Service facilities. GSA paid considerably more per square foot than the value assigned to the Postal Service space.¹³

Table 3 – Postal Service Excess Space Lease Opportunity

Districts	GSA Leased SF	Postal Service Excess SF	GSA Facility Count	Postal Service Facility Count	Existing GSA/ Postal Service Leases	GSA Average SF Cost	Postal Service Average SF Value	Number of GSA Leases Excess Space May Accommodate	
Bay Valley	1,505,154	932,074	94	146	1	\$34.34	\$19.62	79 of 94	84%
Los Angeles	1,381,309	850,737	81	97	0	33.07	23.61	68 of 81	84%
Total	2,886,463	1,782,811	175	243	1	\$33.71	\$21.62	147 of 175	84%

Table 3 and [Appendix D](#) also illustrate the strong correlation between space leased by the GSA and the ability of the Postal Service to significantly accommodate federal space needs. For the districts reviewed, we estimate that Postal Service excess space may accommodate 147 of 175 (or 84 percent) of current federal leases. However, we understand that more information is necessary to determine whether the Postal Service’s excess space would be suitable.

¹² 41 CFR 102-73.20.

¹³ We assigned Postal Service excess space a value based on historical lease rates in the same geographic areas.

APPENDIX C: MONETARY IMPACTS
FUNDS PUT TO BETTER USE¹⁴

Table 4 – Bay Valley Excess Interior Space Monetary Impacts

Project Year	0	1	2	3	4	5	6	7	8	9
Fiscal Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
<u>Owned</u>										
Sublease Value	(\$21,893,826)	\$14,313,791	\$14,313,791	\$14,313,791	\$14,313,791	\$14,313,791	\$14,313,791	\$14,313,791	\$14,313,791	\$3,578,448
Utility Savings		\$2,101,107	\$2,149,432	\$2,198,869	\$2,249,443	\$2,301,180	\$2,354,108	\$2,408,252	\$615,910	
Custodial Savings		\$1,915,071	\$1,915,071	\$1,915,071	\$1,915,071	\$1,915,071	\$1,915,071	\$1,915,071	\$478,768	
<u>Leases Expiring FY 2011</u>										
Sublease Value	(\$1,903,324)	\$1,244,359	\$1,244,359	\$1,244,359	\$1,244,359	\$1,244,359				
Utility Savings		\$182,658	\$186,859	\$191,157	\$195,554	\$200,051				
Custodial Savings		\$166,485	\$166,485	\$166,485	\$166,485	\$166,485				
<u>Leases Expiring After 10/1/2011</u>										
Sublease Value	(\$4,174,391)	\$2,729,142	\$1,673,213	\$1,155,343	\$840,011	\$510,866	\$436,270	\$298,930	\$49,050	\$49,050
Utility Savings		\$400,608	\$251,258	\$177,483	\$132,010	\$82,130	\$71,751	\$50,294	\$8,442	\$8,636
Custodial Savings		\$365,138	\$223,863	\$154,576	\$112,387	\$68,350	\$58,370	\$39,995	\$6,563	\$6,563
Subtotal	(\$27,971,541)	\$23,418,359	\$22,124,332	\$21,517,135	\$21,169,111	\$20,802,284	\$19,149,360	\$19,026,333	\$4,737,181	\$64,249
Cash Flows @ Sublease Efficiency Rate	(\$24,251,326)	\$20,303,717	\$19,181,796	\$18,655,356	\$18,353,619	\$18,035,580	\$16,602,495	\$16,495,831	\$4,107,136	\$55,704
Discounted at Postal Service Cost of Borrowing	(\$24,251,326)	\$19,546,298	\$17,777,357	\$16,644,487	\$15,764,404	\$14,913,341	\$13,216,217	\$12,641,451	\$3,030,057	\$39,563

Net Present Value: \$89,321,849			
Build-Out Costs SF	\$30.01	Utilities Savings SF per Year	\$2.88
Lease Savings SF per Year	\$19.62	Utility Cost Escalation Rate	2.30%
Postal Service Cost of Borrowing	3.875%	Custodial Rate SF	\$5.25
		Sublease Efficiency Rate	86.7%
Assumption: **Weighted Average Lease Years = 7.3			

¹⁴ Funds the Postal Service could use more efficiently by implementing recommended actions.

Table 5 – Los Angeles Excess Interior Space Monetary Impacts

Project Year	0	1	2	3	4	5	6	7	8	9
Fiscal Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Owned										
Sublease Value	(\$23,189,253)	\$14,801,251	\$14,801,251	\$14,801,251	\$14,801,251	\$14,801,251	\$14,801,251	\$14,801,251	\$14,801,251	\$3,700,313
Utility Savings		\$1,172,314	\$1,199,277	\$1,226,861	\$1,255,079	\$1,283,945	\$1,313,476	\$1,343,686		\$343,648
Custodial Savings		\$1,413,673	\$1,413,673	\$1,413,673	\$1,413,673	\$1,413,673	\$1,413,673	\$1,413,673	\$1,413,673	\$353,418
Leases Expiring FY 2011										
Sublease Value	(\$1,267,018)	\$808,713	\$808,713	\$808,713	\$808,713	\$808,713				
Utility Savings		\$64,053	\$65,526	\$67,033	\$68,575	\$70,152				
Custodial Savings		\$77,241	\$77,241	\$77,241	\$77,241	\$77,241				
Leases Expiring After 10/1/2011										
Sublease Value	(\$7,012,490)	\$4,475,937	\$3,493,713	\$2,086,416	\$1,441,367	\$874,703	\$381,467	\$209,421	\$209,421	\$209,421
Utility Savings		\$354,511	\$283,080	\$172,941	\$122,221	\$75,877	\$33,852	\$19,012	\$19,449	\$19,896
Custodial Savings		\$427,498	\$333,686	\$199,274	\$137,665	\$83,543	\$36,434	\$20,002	\$20,002	\$20,002
Subtotal	(\$31,468,762)	\$23,595,191	\$22,476,160	\$20,853,403	\$20,125,785	\$19,489,099	\$17,980,152	\$17,807,044	\$4,646,250	\$249,319
Cash Flows @ Sublease Efficiency Rate	(\$27,283,416)	\$20,457,030	\$19,486,831	\$18,079,900	\$17,449,056	\$16,897,049	\$15,588,792	\$15,438,707	\$4,028,299	\$216,159
Discounted at Postal Service Cost of Borrowing	(\$27,283,416)	\$19,693,892	\$18,060,058	\$16,131,060	\$14,987,451	\$13,971,906	\$12,409,270	\$11,831,333	\$2,971,894	\$153,523

Net Present Value: \$82,926,973			
Build-Out Costs SF	\$36.99	Utilities Savings SF per Year	\$1.87
Lease Savings SF per Year	\$23.61	Utility Cost Escalation Rate	2.30%
Postal Service Cost of Borrowing	3.875%	Custodial Rate SF	\$4.51
		Sublease Efficiency Rate	86.7%
Assumption: **Weighted Average Lease Years = 7.3			

Value Assigned to the Excess Space

Table 6 shows the value per square foot for each district. Using the Facility Inventory Reports from the eFMS, we calculated this figure by dividing total interior square footage by total lease costs.

Utility Costs Associated with the Excess Space

Table 6 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 6 shows the maintenance cost per square foot for each district. We calculated this cost by dividing the total annual maintenance expenses¹⁵ 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.¹⁶

Build-Out Costs Associated with Implementing Optimization Actions

Table 6 shows the build-out cost per square foot for each district. We calculated this figure by dividing the ‘build-out/Line 63 capital’ costs for all approved optimization node studies in each district by the total reduction in square footage identified in the approved node studies.

For both districts, we calculated the average build-out cost and then removed any ‘outliers,’ such as items with no build-out cost or items whose build-out cost per square foot was not in keeping with the emerging range of costs to generate a new build-out cost. However, in the Bay-Valley District, there were not enough node studies with build-out costs to be considered representative of the district. In these cases, we calculated the build-out cost per square foot for the entire Pacific Area, which is \$30.01. We calculated this figure using the same methodology as the district cost but expanded the scope to include node studies for all districts in the Pacific Area.

Table 6 – Square Footage Costs by District

District	Lease Cost/SF	Utility Cost/SF	Maintenance Cost/SF	Build-Out Cost/SF ¹⁷
Bay-Valley	\$19.62	\$2.88	\$5.25	\$30.01
Los Angeles	\$23.61	\$1.87	\$4.51	\$36.99

¹⁵ eFlash (Labor Distribution Code 38, salary and benefits) + FPR Line 3F Contract Cleaners Costs.

¹⁶ *Custodial Maintenance* (Report Number DA-AR-09-011, dated August 13, 2009).

¹⁷ Although build-out costs are negotiable and, at times, paid for by the lessor, these costs ranged from \$0 per square foot to \$139.73 per square foot in the node studies analyzed.

Ownership of Facility and Term Years

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

We calculated 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

Map 1 – Bay Valley District

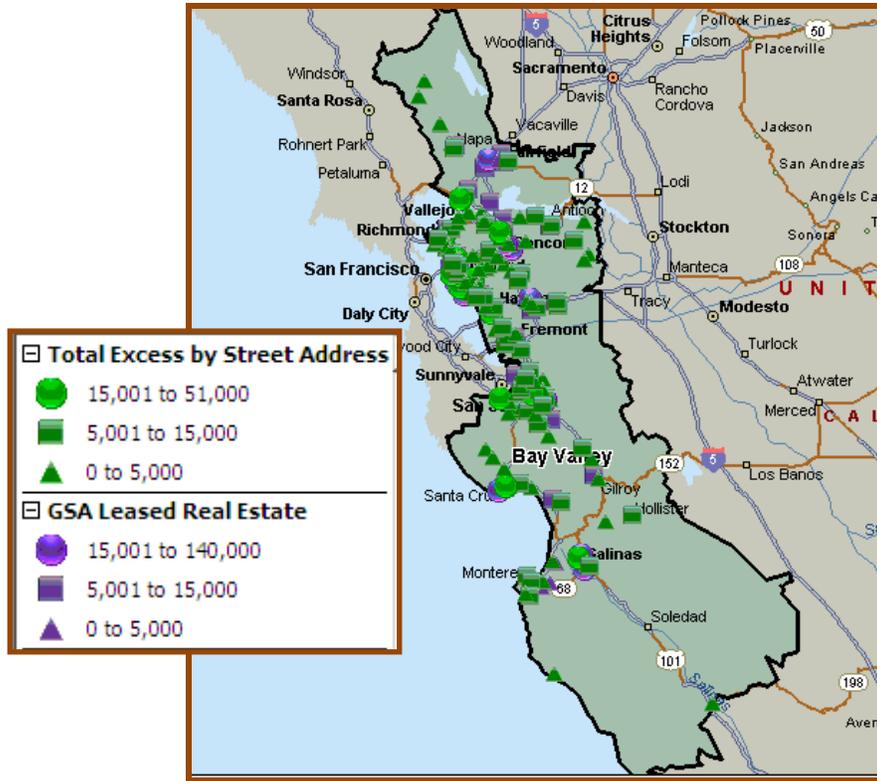
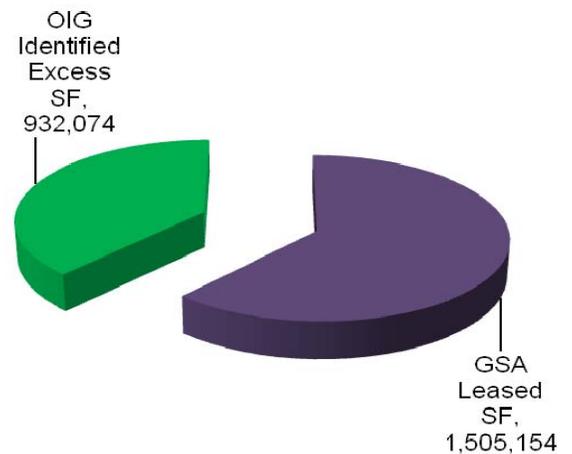


Table 7 – Facilities by Square Footage

Building Size (SF)	GSA Leased Facilities	OIG Identified Excess
1,000	3	36
5,000	21	50
10,000	30	33
20,000	21	17
30,000	6	4
40,000	2	4
50,000	4	1
More	7	1
Total	94	146

Illustration 2 shows the ratio of Postal Service excess space to GSA-leased commercial space. Table 7 provides additional analysis by placing the real estate into size categories to further assess supply vs. demand.

Illustration 2. Ratio of Excess Space to Leased Commercial Space



Map 2 – Los Angeles District

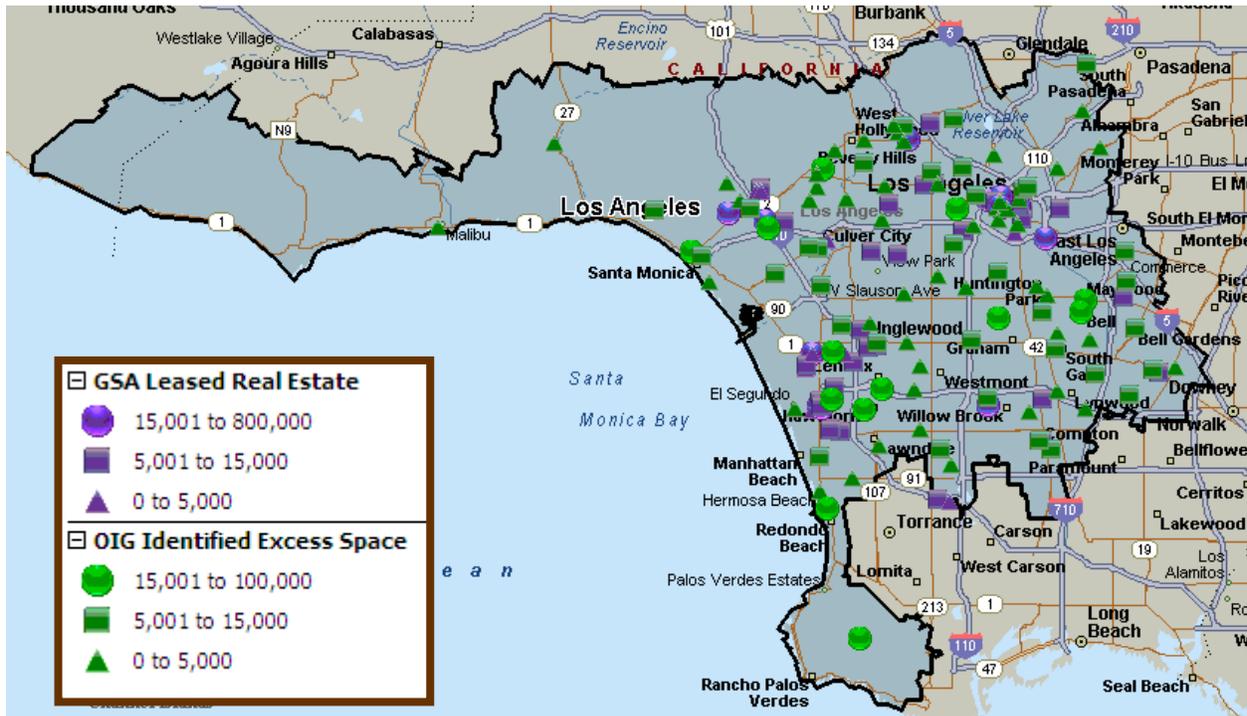
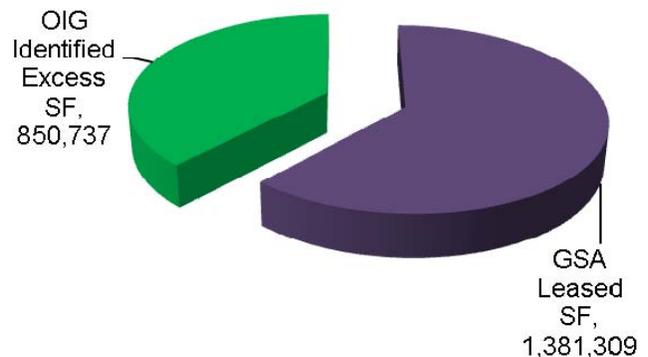


Illustration 3 shows the ratio of Postal Service excess space to GSA-leased commercial space. The following table provides additional analysis by placing the real estate into size categories to further assess supply vs. demand.

Illustration 3 – Ratio of Excess Space to Leased Commercial Space

Table 8 – Facilities by Square Footage

Building Size (SF)	GSA Leased Facilities	OIG Identified Excess
1,000	2	8
5,000	18	41
10,000	22	22
20,000	23	18
30,000	5	5
40,000	3	2
50,000	3	0
More	5	1
Total	81	97



APPENDIX E: MANAGEMENT'S COMMENTS

DREW T. ALPERTO
VICE PRESIDENT, PACIFIC AREA OPERATIONS



April 29, 2011

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

SUBJECT: Facility Optimization: Pacific 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 Pacific 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. In addition, management agrees that the policy written in the ASM section 517 is not followed and is ineffective. Changes to the ASM 517 are in the final edit stage to clarify responsibility for identification of excess space. In addition, a standard operating procedure for useable excess space identification has been released. These two actions effectively address the audit recommendations.

Regarding the findings of the audit, management strongly disagrees with the amount of excess space and methodologies used to calculate potential savings and lease opportunities.

1. The methodology utilized to determine existing usable excess space in facilities, including the use of a lower threshold of only 200 square feet.
2. Inaccurate data and cost factors utilized to calculate the potential revenue

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

1. Methodologies used to determine existing usable excess space in facilities:

As stated in the audit, management disagrees with the methodology utilized in

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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 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, these methodologies do not include reasonable allowances for:

- A. Unusable space such as basements, internal structures, corridors, etc. The audits were too simplistic and serve to treat every square foot in every building as usable and leasable space which is not appropriate.
- B. Existing functions currently exist in many facilities which are not included in the SSBD design such as administrative headquarters office space, area office space, district office space, Inspection Service office space, OIG office space, training rooms, central conference rooms, caller service areas, special service areas, etc.
- C. Inefficiencies in current building layouts due to multiple floors, stairs, elevators, columns, redundant support space required on each floor due to code requirements, etc.
- D. Historic nature of some of the buildings that hinders the possibility of making structural changes.
- E. Parking and dock space requirements.
- F. Large inflexible retail lobbies.
- G. Automation support currently available to the facility's operations units.
- H. Traffic conditions and possible impact on available or replacement space.

Management Recommended Methodology

Because every building is different and has a variety of the unique items to contend with, Management recommends that the OIG review each specific building and determine actual usable excess space after making allowances for the items listed above and any other limitations and operational circumstances that may be appropriate.

2. Inaccurate Data and Cost Factors Utilized to Calculate Potential Savings & Lease Opportunities

The audit states that the two districts audited in the Pacific Area, Bay Valley and Los Angeles, have an excess of over 1.7 million square feet with a potential to realize \$172,248,822 over typical and remaining lease terms. The OIG provided a specific example of excess space in each district; Alameda Main Post Office (Bay Valley), and the Bell-Maywood Branch (Los Angeles).

Management disagrees with these findings in general as we have stated in our previous responses. The calculations do not appropriately consider the following:

- A. Actual current favorable lease values for identified excess space.
- B. Whether or not current suitable replacement facility space is available.
- C. Actual market value for replacement space, including the necessary egress and parking requirements to support efficient postal service operations.
- D. Whether or not the market value of surrounding space would result in a savings.
- E. Whether excess space is located in a community with a need or desire for additional leased space.
- F. Whether or not current suitable replacement facility space is available.
- G. The real costs associated with relocating a postal facility, including de-postalizing space and replacement build-out to newer building code requirements.
- H. Increased operational costs associated with relocation of carrier routes, including employee workhours, increased fuel consumption, vehicle requirements and maintenance.

More specifically, in regard to the two examples, the following is provided:

The Alameda Main Post Office is a leased facility occupied in October of 1972; it has a net interior of 54,040 SF. The OIG states that it has 37,940 of excess space. Management agrees there is excess space in this building. The Alameda Main Post Office is a high-valued property with a favorable lease term of \$148,519 per annum with fixed options at the same rate until the lease end date of July 2022. There is a purchase option of \$2,250,000. Asset Management has been working with developers to ensure that the Postal Service extract the maximum value from this property. The Alameda Main Post Office is located on an island with limited bridge access. There are currently 56 carrier routes and though a search has been in progress for several years, a suitable replacement site to relocate delivery has not become available. Asset Management continues to analyze Letters of Intent from interested developers.

The Bell-Maywood Branch is a USPS owned facility first occupied in June of 1938; it has a net interior of 24,382 SF. Management agrees there is excess space in this building and is in the process of optimizing buildings in the Pacific Area.

Build Out Costs Associated with Implementing Optimization Actions

Management disagrees with the OIG average build out cost of \$41.13. The cost to perform this work will vary greatly but a reasonable actual range for the Pacific area would be from \$100.00 to \$150.00 a square foot depending on the type of work needed. These numbers are based upon actual project costs and include design, construction and construction supervision

The cost to relocate postal operations to an existing postal facility is usually very low. In particular when relocating retail it is sometimes possible to do so with no

capital expenditure. In order to prepare space for outlease, there is considerable additional work that must be performed. Items as listed below must be evaluated and implemented as applicable:

- Separate entrance / exit
- Security walls and partitions
- Life safety upgrades driven by the new walls and egress patterns
- Separate HVAC and electric sub metering
- Separate restrooms
- Segregated parking and fencing

Potential Revenue:

Management believes an appropriate way to calculate potential revenue is to apply the following formula currently used to develop node studies:

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

This value should then be adjusted for any of maintenance and utility costs or savings.

To value the subleasing potential of excess square footage, the real estate market must be analyzed, including the probability of subleasing, the duration of subleasing and the square foot value of such a sublease. Any cost of tenant improvement must also 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 six largest 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 has developed a more accurate process and proper documentation for identifying and reporting excess space.
2. Management has included additional metrics to track dates and conditions of excess space and it is part of the national process.
3. Management will continue to make available our excess property to other federal agencies. This will be completed by the end of quarter 3, 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

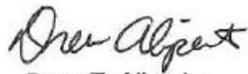
3. Buildings over 10,000 square feet were measured to ascertain the correct square footage per function within the facility. Based on this data, we are now able to determine what space is needed for the current operations in the facility and how much is potential excess space. After finding these candidates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

We do not believe this report contains any proprietary or business information that should not be disclosed and do not believe there are any required exemptions pursuant to the Freedom of Information Act (FOIA).



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