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SUBJECT: Audit Report – Facility Optimization: Former Southeast Area Districts
(Report Number DA-AR-11-007)

This report presents the results of our audit of facility optimization in the former Southeast Area (Project Number 11YG007DA000). The U.S. Postal Service Office of Inspector General (OIG) initiated this audit from a random sample of districts nationwide. For the former Southeast Area, our objective was to identify opportunities to optimize existing real estate in the North Florida, South Florida, and Tennessee Districts. See Appendix A for additional information about this audit.

The three districts analyzed in the former Southeast Area use over 1,114 facilities covering nearly 11 million square feet (SF) of interior space for its retail and delivery operations. While 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 former Southeast Area has dropped 8 percent annually on average. Likewise, mail volume in the North Florida, South Florida, and Tennessee Districts has decreased by about 10 percent annually on average. This reduction in workload provides an opportunity to reevaluate space needs and identify potential excess space.

Conclusion

In the former Southeast Area, the North Florida, South Florida, and Tennessee Districts have nearly 3 million more SF than 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/Redevelopment – investing in real estate projects.

With two major efforts underway, the Postal Service has begun optimizing existing space. Specifically, the former Southeast Area plans to dispose of 934,155 SF of this excess space through approved optimization projects, with another 292,293 SF scheduled for evaluation in FY 2011 for the three 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 former Southeast Area initiates disposal[1] action for the excess space we identified in the North Florida, South Florida, and Tennessee Districts, there is a potential opportunity to realize $151,624,144[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 monetary impact calculation.

Our audit also noted that the Postal Service could more aggressively seek federal entities needing space. In the districts reviewed, our analysis shows that excess space identified at Postal Service facilities may be able to accommodate 72 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, which would allow it to reduce its facility infrastructure size and generate additional revenue. See Appendix D for more information.

We recommend the vice presidents, Operations, Southwest and Eastern areas; district managers; area managers; and Southwest and Eastern Area Facility Service Office managers work in coordination to:

1. Clarify procedures for reporting excess space.

2. Initiate disposal actions for excess space identified.

3. Pursue rental 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 $15,162,414.
[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 our recommendations. They stated they have put corrective actions in place to address the first two recommendations and will complete corrective action to address the third recommendation by the end of Quarter 3, 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, and caller service.

3. Inefficiencies in current building layout due to multiple floors, stairs, elevators, columns, and 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.

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 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 usable excess space. See Appendix E for management's comments, in their entirety.

Evaluation of Management's Comments

The OIG considers management's comments responsive to the recommendations and 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 the Postal Service needs to update its realty management policies and systems 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, a proportionate share of which 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, 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 on 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 any decisions resulting from the consultations.

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 indicators or alternate access sales in the earned space calculation.

The Postal Service does not have a methodology for 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 build-out costs are negotiable and lessees, at times, absorb the cost of conversion. We

[4] www.boma.org

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 of more 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 Postal Service's follow-up tracking system until the OIG provides written confirmation that the recommendations can be closed.

We appreciate the cooperation and courtesies provided by your staff. If you have any questions or need additional information, please contact 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 former Southeast Area leases or owns over 1,114 facilities with nearly 11 million SF to move mail in the North Florida, South Florida, and Tennessee 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, 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 former Southeast Area has four approved optimization studies in the North Florida District, 11 in the South Florida District, and seven in the Tennessee 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:

- JAX-Airport Station.
- JAX-Cecil Field FSTA.
- PFN-Eastside STA.
- MIA-International Airport Finance.
- MIA-Edison Center FSTA.
- FMY-Miracle Mile STA.
- KIS-Good Samaritan BR.
- NPS-Golden Gate Finance.
- NPS-Vanderbilt Beach.
- ORL-Lee Vista Station.
- SPT-Central STA.
- SPT-Pass A Grille.
- TPA-Port Tampa.
- TPA-Seminole Heights.
- MEM-Lee Finance Unit.

In addition to the ongoing node studies[5] and SBOC program, the three districts have taken action to utilize space and provide alternative services by selling Hallmark cards in existing lobby space at several facilities.

In October 2010, the Postal Service consolidated optimization efforts to manage excess space. Currently, the Postal Service has a program in place to optimize carrier delivery facilities through the use of node studies. The goal is to manage the excess space portfolio for all space types in one overall optimization initiative. 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 (RERM) to identify and prioritize emerging facility risk. The risk model measures facility performance results by district for the following nine metrics:

[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 on a national basis. The three districts we selected were in the former Southeast Area.

OBJECTIVE, SCOPE, AND METHODOLOGY

Our objective was to identify opportunities for the Postal Service's former Southeast Area to optimize existing real estate. We visited 118 of 1,114 facilities in the North Florida, South Florida, and Tennessee Districts, representing 43 percent of OIG-calculated excess space when actual interior space is compared to space standards. The scope of the audit included main post offices, carrier annexes, stations, branches, and mail processing facilities. To accomplish our objective we visited selected facilities, conducted interviews, and examined other relevant materials.

To calculate the 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 the earned facility size on Postal Service criteria[8] for planning new space projects, which differs from existing Postal Service initiatives[9] 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 to 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 our findings and conclusions based on our audit objective. We discussed our

[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.

observations and conclusions with management officials on April 13, 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
Facility Optimization: Southwest Area Districts	DA-AR-11-003	03/01/2011	$99,618,007	The OIG identified 2.3 million SF of excess space. Management agreed with the recommendations but disagreed with the monetary impact.
Facility Optimization: Eastern Area Districts	DA-AR-11-002	2/11/2011	$190,656,882	The OIG identified 2.8 million SF of excess space. Management agreed with the recommendations but disagreed with the monetary impact.
Facility Optimization: Capital Metro Area Districts	DA-AR-11-004	2/25/2011	$36,312,795	The OIG identified 1.7 million SF of excess space. Management agreed with the recommendations but disagreed with the monetary impact.
Facility Optimization: Western Area Districts	DA-AR-11-001	2/7/2011	$173,835,881	The OIG identified 4.5 million SF of excess space. Management agreed with the recommendations but disagreed with the monetary impact.
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 recommendations but disagreed with the monetary impact.
Facility Optimization: Chicago District	DA-AR-10-009	8/25/2010	$23,517,019	The OIG identified 740,529 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 the recommendations but disagreed with the monetary impact.

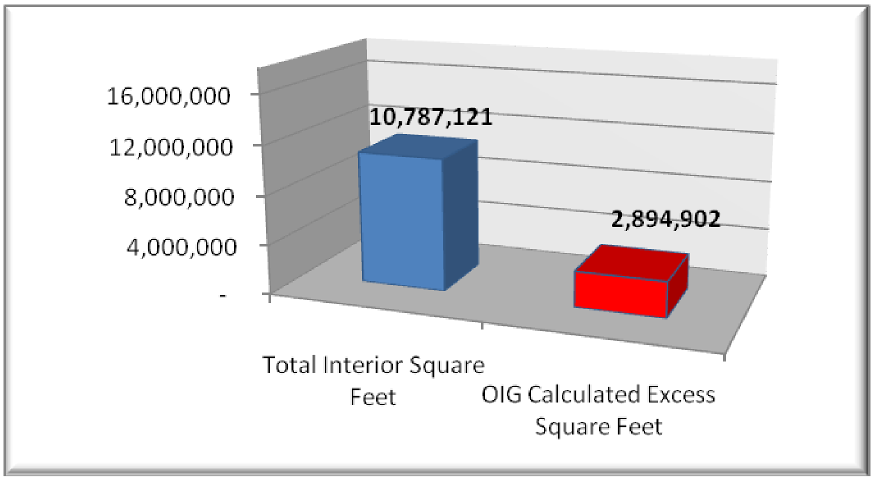
Report Title	Report Number	Final Report Date	Monetary Impact	Report Results
Restructuring the U.S. Postal Service to Achieve Sustainable Financial Viability	GAO-09-937SP	7/28/2009	None	The Government Accountability Office (GAO) added the U.S. Postal Service's financial condition to the list of high-risk 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.
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 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.
Network Rightsizing Needed to Help Keep USPS Financially Viable	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 former Southeast Area

Based on facility space requirements[10], we calculated that the districts reviewed in the former Southeast Area maintain nearly 3 million SF more than they need for current operational workload. As depicted in Chart 1, excess space was 27 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 118 visited facilities in the former Southeast Area is represented in Table 2. Stations contributed 38 percent of the excess space, while branches (17 percent), main post offices (16 percent), and plants (12 percent) followed to a lesser degree.

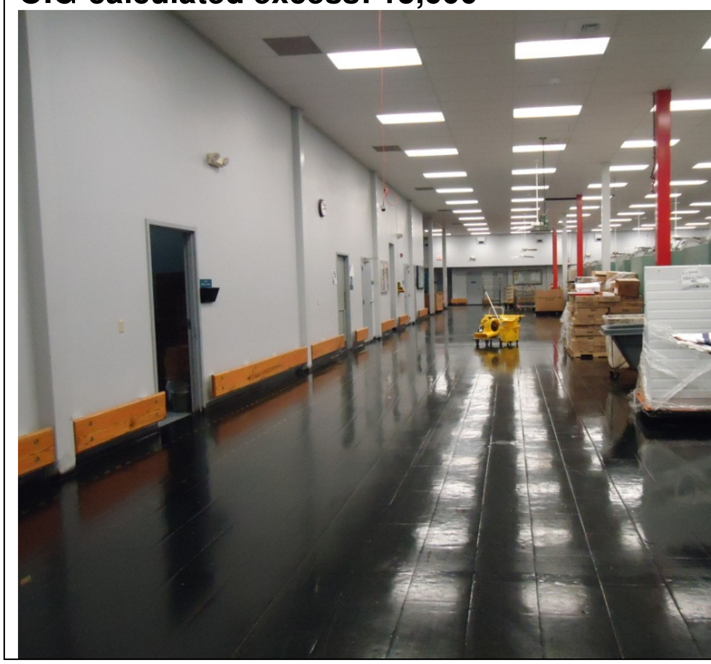
Table 2 – Excess Space by Facility Type Visited

Facility Type	Facility Type Count	Percentage of Count	Percentage of Excess	OIG calculated Excess	Interior Square Footage
Stations	45	38%	38%	355,609	896,386
Branches	19	16%	17%	162,168	405,695
Main Post Offices	24	20%	16%	151,910	855,058
Plants	13	11%	12%	116,326	2,347,225
Carrier Annexes	10	8%	10%	98,106	212,374
Finance Centers	7	6%	6%	52,438	108,494

[10] We used Postal Service criteria established in March of 2007 outlined in a letter issued by the senior vice president of Operations. In support of this 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 former Southeast Area, Illustration 1 depicts two facilities with excess interior space. The Monument Station Post Office is a Postal Service-owned facility with delivery and retail operations. It maintains significant vacant space on the workroom floor. Likewise, the Father Felix Varela Branch is a Postal Service-owned facility with delivery and retail operations. It also maintains significant vacant space on the workroom floor. According to our calculations, 92 percent of the sites visited contained excess space, ranging from 1,865 to 84,056 SF.

Illustration 1 – Examples of Excess Space

Monument Station 10990 Fort Caroline Road Jacksonville, FL 32225 Interior Square Footage: 25,100 **OIG-calculated excess: 15,600**	**Father Felix Varela Branch** 14310 SW 8th Street Miami, FL 33184 Interior Square Footage: 26,888 **OIG-Calculated Excess SF: 15,888**
	

Causes for Excess Interior Space

The opportunity to optimize excess interior space in the former Southeast 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.
- 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. While we identified excess space at 109 of the 118 Postal Service facilities we visited, only four locations answered "yes" to the vacant leasable space survey question. As a result, we identified nearly 3 million SF of excess interior space in the North Florida, South Florida, and Tennessee 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 systems that manage facility space do 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 purposes, we benchmarked Postal Service facility practices against the General Services Administration's (GSA) realty management practices and found the 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.

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 in 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 a reliable source 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 former Southeast Area initiated disposal actions, there is a potential opportunity to realize $151,624,144[11] over typical and remaining lease terms. We consider this amount funds that could be used more efficiently by implementing

[11] The annualized savings would be $15,162,414.

recommended actions. See Appendix C for the monetary impact calculation and assumptions.

Opportunity to Fulfill Federal Space Needs

The 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), 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 could more aggressively seek federal entities to excess space. Table 3 illustrates the potential fulfillment opportunities in both districts reviewed in the former Southeast 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. The GSA paid considerably more per square foot than the value assigned to Postal Service space.[13]

Table 3 – Postal Service Excess Space Lease Opportunity

Districts	GSA Leased SF	Postal Service OIG Excess SF	GSA Count	Postal Service Count	Existing GSA/ Postal Service Leases	GSA Average SF Cost	Postal Service OIG Average SF Value	GSA Annual Opportunity Rent	
South Florida	3,377,964	879,421	181	141	0	$32.15	$26.64	**116 of 181**	64%
North Florida	1,533,720	861,934	135	192	1	22.93	16.67	**110 of 135**	81
Tennessee	1,894,567	1,153,547	183	371	1	20.27	9.16	**132 of 183**	72
Totals	**6,806,251**	**2,894,902**	**499**	**704**	**2**	**$26.81**	**$16.71**	**358 of 499**	**72%**

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 358 of 499 (or 72 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] Title 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 IMPACT FUNDS PUT TO BETTER USE[14]

North Florida District Monetary Impact

Project Year			1	2	3	4	5	6	7	8	9
Fiscal Year		2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Owned**											
Sublease Value		($17,208,040)	$7,161,220	$7,161,220	$7,161,220	$7,161,220	$7,161,220	$7,161,220	$7,161,220	$1,790,305	
Custodial savings			$1,322,865	$1,322,865	$1,322,865	$1,322,865	$1,322,865	$1,322,865	$1,322,865	$330,716	
Utility Savings			$1,281,347	$1,310,818	$1,340,967	$1,371,809	$1,403,360	$1,435,638	$1,468,657	$375,609	
Leases Expiring After FY 2011											
Sublease Value		($5,599,282)	$2,330,172	$2,271,193	$2,113,186	$1,899,316	$1,883,789	$882,062	$839,194	$614,719	$415,275
Custodial savings			$430,444	$419,549	$390,361	$350,853	$347,985	$162,940	$155,021	$113,555	$76,712
Utility Savings			$416,934	$415,728	$395,702	$363,834	$369,160	$176,830	$172,106	$128,969	$89,129
Subtotals	**$66,915,219**	**-22,807,322**	**$12,942,982**	**$12,901,373**	**$12,724,301**	**$12,469,897**	**$12,488,380**	**$11,141,556**	**$11,119,063**	**$3,353,874**	**$581,116**
Discounted at Postal Service Cost of Borrowing	**$54,276,681**	-$22,807,322	$12,460,151	$11,956,770	$11,352,743	$10,710,722	$10,326,447	$8,869,101	$8,521,007	$2,474,334	$412,728
Cash Flows @ Sub Lease Efficiency Rate	$47,057,883	-$19,773,948	$10,802,951	$10,366,519	$9,842,828	$9,286,196	$8,953,029	$7,689,511	$7,387,713	$2,145,248	$357,835

Net Present Value: $47,057,883

Build-out cost SF	**$26.46**	**Custodial rate SF**	**$2.03**
Lease savings SF per Year	**$11.01**	**Postal Service cost of borrowing**	**3.875%**
Utilities savings SF per Year, FY 2010	**$1.97**	**Sub-lease efficiency rate**	**86.7%**
Utility cost escalation rate	**2.30%**		
	Assumptions	****Weighted Average Lease years = 7.3**	

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

South Florida District Monetary Impact

Project Year			1	2	3	4	5	6	7	8	9
Fiscal Year		2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Owned**											
Sublease Value		($14,858,970)	$9,312,856	$9,312,856	$9,312,856	$9,312,856	$9,312,856	$9,312,856	$9,312,856	$1,790,305	
Custodial Savings			$1,119,953	$1,119,953	$1,119,953	$1,119,953	$1,119,953	$1,119,953	$1,119,953	$330,716	
Utility Savings			$1,276,015	$1,305,363	$1,335,386	$1,366,100	$1,397,521	$1,429,664	$1,462,546	$375,609	
Leases Expiring After FY 2011											
Sublease Value		($8,411,069)	$5,271,635	$4,762,583	$3,765,044	$2,470,863	$2,205,947	$524,608	$319,876	$259,261	$259,261
Custodial Savings			$633,960	$572,742	$452,780	$297,143	$265,284	$63,089	$38,468	$31,178	$31,178
Utility Savings			$722,301	$667,561	$539,876	$362,450	$331,032	$80,535	$50,235	$41,652	$42,610
Subtotals	**$87,377,615**	**-23,270,039**	**$18,336,719**	**$17,741,058**	**$16,525,894**	**$14,929,364**	**$14,632,592**	**$12,530,704**	**$12,303,933**	**$3,314,340**	**$333,049**
Discounted at Postal Service Cost of Borrowing	**$72,577,641**	-$23,270,039	$17,652,678	$16,442,106	$14,744,561	$12,823,222	$12,099,463	$9,974,916	$9,429,023	$2,445,168	$236,543
Cash Flows @ Sub Lease Efficiency Rate	$62,924,815	-$20,175,124	$15,304,872	$14,255,306	$12,783,535	$11,117,734	$10,490,234	$8,648,252	$8,174,963	$2,119,961	$205,082

Net Present Value: $62,924,815

Build-out cost SF	$26.46	Custodial rate SF	$1.99
Lease savings SF per Year	$16.58	Postal Service cost of borrowing	3.875%
Utilities savings SF per Year, FY 2010	$2.27	Sub-lease efficiency rate	86.7%
Utility cost escalation rate	2.30%		
	Assumptions	**Weighted Average Lease years = 7.3	

Tennessee District Monetary Impact

Project Year			1	2	3	4	5	6	7	8	9
Fiscal Year		2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Owned**											
Sublease Value		($19,416,153)	$6,475,038	$6,475,038	$6,475,038	$6,475,038	$6,475,038	$6,475,038	$6,475,038	$1,618,760	
Custodial Savings			$1,205,707	$1,205,707	$1,205,707	$1,205,707	$1,205,707	$1,205,707	$1,205,707	$301,427	
Utility Savings			$1,309,545	$1,339,665	$1,370,477	$1,401,998	$1,434,244	$1,467,232	$1,500,978	$383,875	
Leases Expiring After FY 2011											
Sublease Value		($11,107,434)	$3,704,187	$3,284,875	$3,051,746	$2,500,625	$2,469,131	$1,010,151	$924,097	$641,543	$400,437
Custodial Savings			$689,751	$611,672	$568,261	$465,638	$459,773	$188,099	$172,075	$119,461	$74,565
Utility Savings			$749,154	$679,630	$645,919	$541,444	$546,921	$228,898	$214,215	$152,136	$97,144
Subtotals	**$60,561,376**	**-30,523,587**	**$14,133,382**	**$13,596,586**	**$13,317,148**	**$12,590,450**	**$12,590,815**	**$10,575,125**	**$10,492,109**	**$3,217,202**	**$572,146**
Discounted at Postal Service Cost of Borrowing	**$48,029,349**	-$30,523,587	$13,606,144	$12,601,081	$11,881,687	$10,814,268	$10,411,149	$8,418,201	$8,040,546	$2,373,504	$406,357
Cash Flows @ Sub Lease Efficiency Rate	$41,641,446	-$26,463,950	$11,796,527	$10,925,137	$10,301,423	$9,375,970	$9,026,466	$7,298,580	$6,971,153	$2,057,828	$352,312

Net Present Value: $41,641,446

Build-out cost SF	**$26.46**	**Custodial rate SF**	**$1.64**
Lease savings SF per Year	**$8.82**	**Postal Service cost of borrowing**	**3.875%**
Utilities savings SF per Year, FY 2010	**$1.78**	**Sub-lease efficiency rate**	**86.7%**
Utility cost escalation rate	**2.30%**		
	Assumptions:	****Weighted Average Lease years = 7.3**	

Value Assigned to the Excess Space

Table 4 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 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[15] 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 4 shows the build-out cost per square foot for the former Southeast Area. We calculated this figure by dividing the "build-out/Line 63 capital" costs for all approved optimization node studies in the former Southeast Area by the total reduction in square footage identified in the approved node studies. 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.

Table 4 – Square Footage Cost by District

District	Lease Cost/SF	Utility Cost/SF	Maintenance Cost/SF	Build out Cost/SF[17]
South Florida	$16.58	$2.27	$3.99	$33.60
North Florida	11.01	1.97	4.07	14.25
Tennessee	8.82	1.78	3.29	14.63

[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] While build-out costs are negotiable and, at times, paid for by the lessor, these costs ranged from $0 per square footage to $121.95 per square foot in the node studies analyzed.

Ownership of Facility and Term Years

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

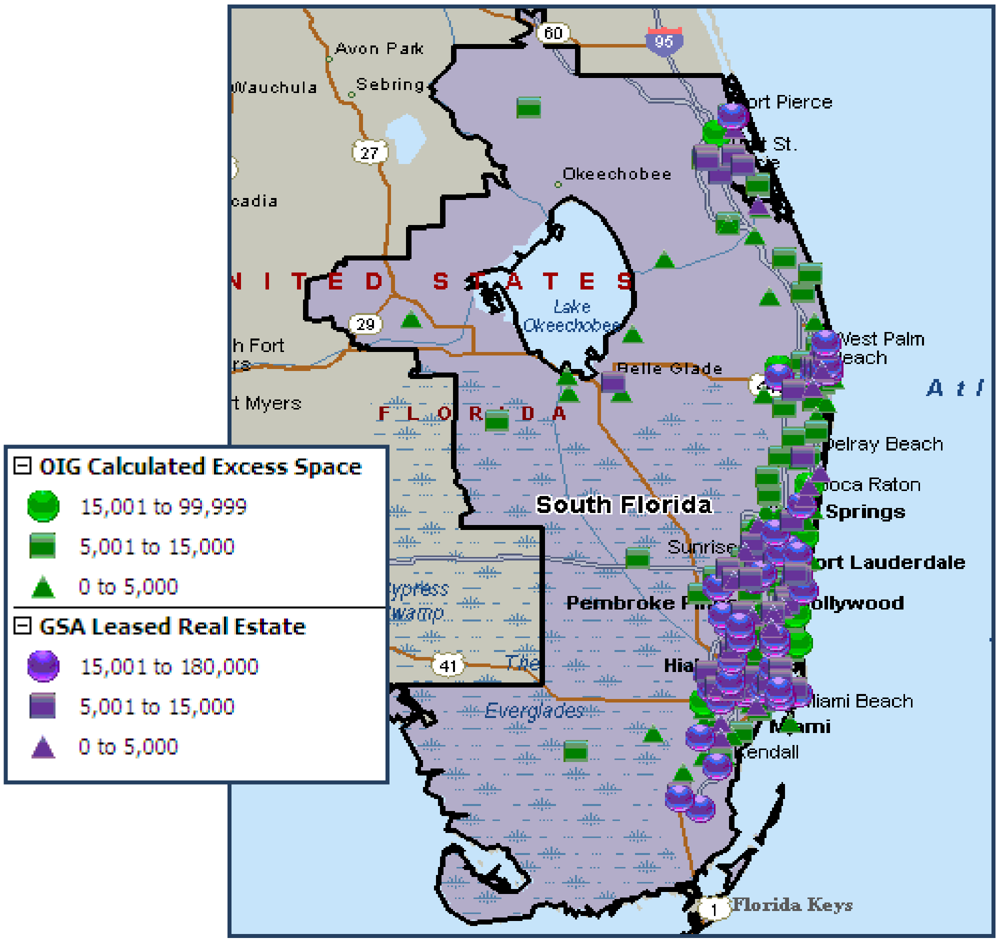
We calculated leases expiring before the end of FY 2011 based on the assumption that these leases would be renewed for the standard 5-year period. We calculated leases expiring after October 1, 2011, for the remaining lease term. We calculated Postal Service-owned facilities over a period of 7.3 years,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

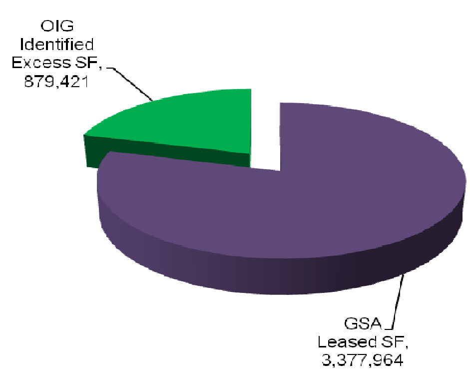
APPENDIX D: GSA-LEASED PROPERTIES COMPARED TO POSTAL SERVICE EXCESS SPACE

South Florida District

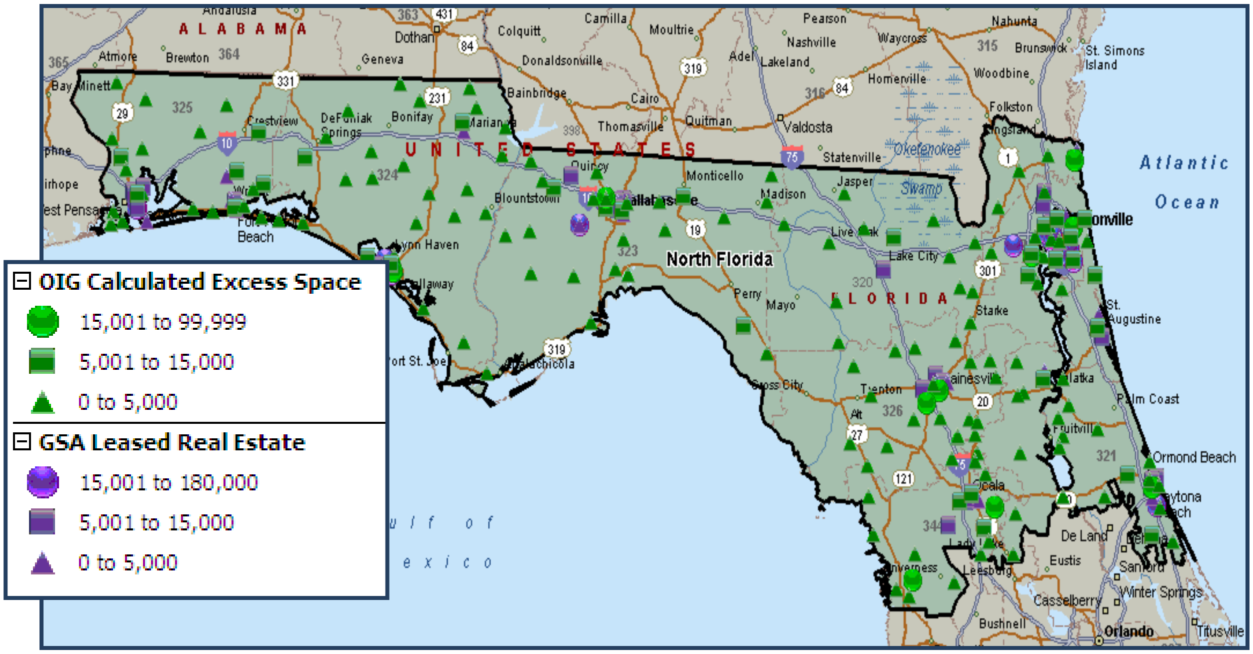


Building Size	GSA Leased Facilities	OIG Identified Excess
1,000	8	19
5,000	48	52
10,000	35	45
20,000	39	22
30,000	17	2
40,000	14	1
50,000	9	0
More	11	0
	181	141

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

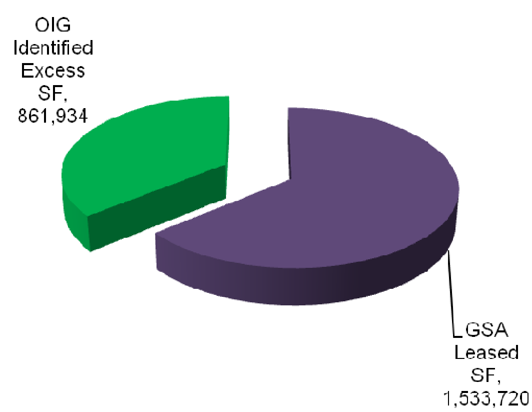


North Florida District

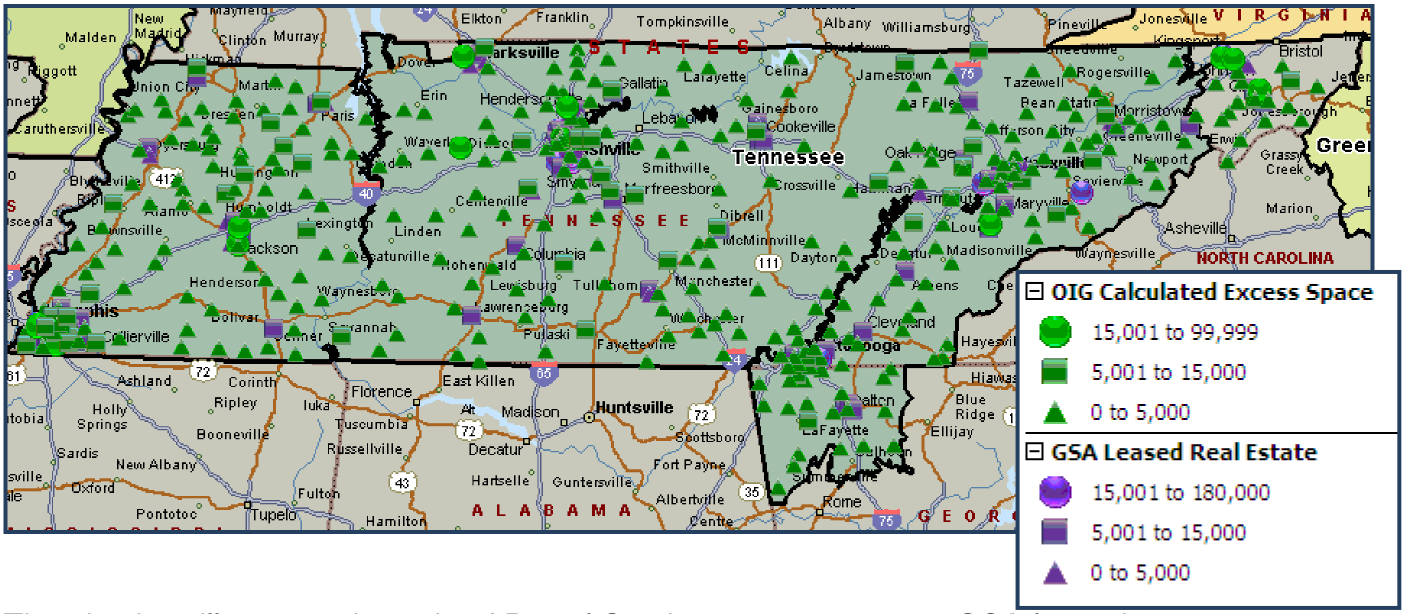


The pie chart illustrates the ratio of Postal Service excess space to GSA-leased commercial space. The table below provides additional analysis by placing the real estate into size categories to further assess supply versus demand.

Building Size	GSA Leased Facilities	OIG Identified Excess
1,000	12	68
5,000	50	76
10,000	38	22
20,000	21	20
30,000	8	5
40,000	1	0
50,000	0	0
More	5	1
Total Count	135	192

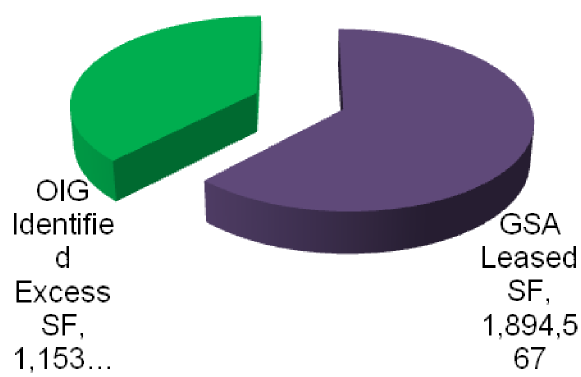


Tennessee District



The pie chart illustrates the ratio of Postal Service excess space to GSA-leased commercial space. The table below 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	9	160
5,000	59	147
10,000	62	39
20,000	25	18
30,000	18	3
40,000	4	2
50,000	2	1
More	4	1
Total Count	183	371



APPENDIX E: MANAGEMENT'S COMMENTS

UNITED STATES
POSTAL SERVICE

May 9, 2011

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

SUBJECT: Facility Optimization: Former Southeast 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 former Southeast 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 two years ago. In addition, management agrees that the policy written in the ASM, section 517, is not followed and is ineffective. Changes to the ASM 517 have been made 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 disagrees with the amount of excess space and potential revenue based on the following:

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

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

1. Methodology

As stated in the audit, management disagrees with the methodology utilized in determining excess space. This disagreement was raised in discussions with the OIG prior to the first release of this audit and in meetings that were held with the OIG prior to the reissuance of this audit. The major concern is that the methodology utilized is based on applying the current Small Standard Building Design (SSBD) which is intended for construction of new, under 10,000 square feet (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."

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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 with which to contend, 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 the three districts audited in the former Southeast Area -- North Florida, South Florida and Tennessee -- have an excess of nearly 3 million SF with a potential to realize $151,624,144 over typical and remaining lease terms. The OIG provided specific examples of excess space in the North Florida and South Florida Districts.

The first page of the audit states, "The three districts analyzed in the Southeast Area use 1,114 facilities covering nearly 11 million SF of interior space for its delivery and retail operations." Based on eFMS inventory data, this number should be 1,300 buildings and utilizes 14,212,899 square feet.

Management disagrees with these findings in general, as we have stated in our previous responses.

Management agrees there is excess space in the two specific examples and is actively working to find opportunities to best utilize this space.

Build Out Costs Associated with Implementing Optimization Actions

Management disagrees with the OIG average build out cost of $26.46. The cost to perform this work will vary greatly but a reasonable actual range for the Southeast 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 the accurate way to calculate potential revenue is first applying the following formula we use in our node studies:

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 six largest real estate brokerage firms in the country and all have confirmed that the property values are dropping and 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 SF 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 have been or will be terminated.

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.

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