August 25, 2010

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VICE PRESIDENT, OPERATIONS, NORTHEAST AREA

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SUBJECT: Audit Report – Facility Optimization: Northern New Jersey District (Report Number DA-AR-10-008)

This report presents the results of our audit of facility optimization in the Northern New Jersey District (Project Number 09YG051DA000). The U.S. Postal Service Office of Inspector General (OIG) initiated this audit due to the district's high-risk ranking identified through our Real Estate Risk Model (RERM). Our objective was to identify opportunities for the Northern New Jersey District to optimize existing real estate. See Appendix A for additional information about this audit.

The Northern New Jersey District uses 432 facilities with over 7.8 million interior square feet (SF). While the district employs these facilities, it has experienced a significant reduction in workload over recent years. From fiscal year (FYs) 2005 to 2009, mail volume has dropped 20 percent. Customer traffic has also declined in post office lobbies as retail transactions shift to alternate access locations. From FYs 2005 to 2009, alternate access revenue in the Northern New Jersey District has increased by 102 percent. This reduction in workload provides an opportunity to reevaluate space needs and identify potential excess space.

Conclusion

The Northern New Jersey District has 1.98 million square feet in excess of what their workload suggests they need. A breakdown of excess space identified at sites visited in the district indicated that 81 percent of the excess space was associated with main post offices and plants. Postal Service has the option to optimize excess real property through:

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

With two major efforts underway, the Postal Service has begun taking action to optimize existing space. Specifically, the Northern New Jersey District plans to dispose of 44,000 SF of this excess through approved optimization projects, with another 571,590 SF planned for evaluation in FY 2010. Although it has made progress, the Postal Service can do more to dispose of excess interior space in a timelier manner.

Postal Service policy[1] requires installation and district heads to annually review and report excess property. The opportunity to optimize excess interior space in the Northern New Jersey District exists because:

- Postal Service policy requires installation heads to report excess space, but does not provide the necessary guidance to effectively accomplish this task.

- The excess space reporting system does not track metrics such as dates or space conditions to allow for the prioritization of disposal actions.

We estimate that if the Northern New Jersey District initiates disposal[2] action for the excess space we identified, there is a potential opportunity to realize $157,963,990 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.

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

1. Ensure installation heads have the proper guidance for identifying and reporting excess space.

2. Include additional metrics, such as dates identified and space conditions, to track, monitor, and report excess space within the Northern New Jersey District and initiate disposal actions for excess space identified.

[1] Per the *Administrative Support Manual* (ASM) 13, Section 517.11, installation heads must review the inventory of Postal Service-owned property at least annually to determine whether there are any properties the Postal Service no longer needs and report that excess property through the Facilities Database. Section 517.34 states that installation heads, district managers, and vice presidents of Area Operations should report all excess space in Postal Service-owned or leased buildings.
[2] 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.
[3] Funds that could be used more efficiently by implementing recommended actions. This amount does not include excess square feet that are part of an approved node study.

Management's Comments

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

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

1. Unusable space such as basements and corridors. The audit treats every square foot as usable and leasable.

2. Existing functions not included in standard designs.

3. Inefficiencies in current building layouts and support space due to code requirements.

4. Historic property.

5. Parking and dock space requirements.

6. Large inflexible retail lobbies.

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

- Amount of facilities within the district.

- Level of approved optimization studies reported.

- Square foot value assigned to excess space.

- Build out cost factors.

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

Finally, management expressed the challenges facing the Postal Service when disposing 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 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 audit report. With respect to the methodology used to calculate excess space, we did not determine whether the excess space identified was usable, in part because Postal Service systems do not identify usable areas. We agree 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 utilize basement space. We did not include allowances for existing functions, building layout inefficiencies, and inflexible spaces because the Postal Service's current space standards did not specify these allowances. Our audit focused on interior excess space and thus excess parking and dock space was outside the scope of the audit.

Postal Service management also conveyed that we did not consider the historic nature of buildings and that they are possibly restricted in making changes to these buildings. While we agree that there are properties held by the Postal Service that are historic in nature, we do not feel this 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 one percent of their properties. Also, while the Postal Service is required to consult with historical organizations, they are not bound by those consultations or decisions.

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

Postal Service management asserted that the audit team did not consider all the node studies from FY 2009. We considered all the "approved" node studies, rather than "completed" node studies. An "approved" node study represents concurrence by area office management and therefore is an active consolidation effort. A "completed" node

[4] www.boma.org

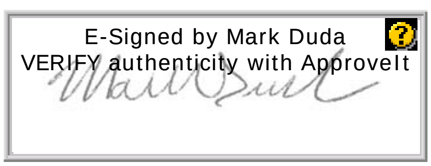
study is merely a study of consolidation options in which the area office management has yet to agree to a specific course of action.

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

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

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

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



Mark W. Duda
Deputy Assistant Inspector General
for Support Operations

Attachment

cc: Steven J. Forte
Tom A. Samra
Henry Burmeister
Corporate Audit Response Management

APPENDIX A: ADDITIONAL INFORMATION

BACKGROUND

The Northern New Jersey District leases or owns 432 facilities with over 7.8 million interior SF to move the mail. The consolidation or closure of facilities is a widely discussed topic due to declining mail volume and the resulting financial condition of the Postal Service. In response, Postal Service Facilities and Retail Management organizations have implemented initiatives to optimize space, namely, initiation of the Facility Optimization Program and the Station and Branch Optimization Consolidation (SBOC) program.

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

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

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

Table 1. Risk Metrics

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

The Northern New Jersey District ranked as second most at risk of all 74 districts as of Quarter 2, FY 2010.

OBJECTIVE, SCOPE, AND METHODOLOGY

Our objective was to identify opportunities for the Postal Service's Northern New Jersey District to optimize existing real estate. We visited 52[5] of 432 facilities in the Northern New Jersey District, which represents 64 percent of OIG-calculated total excess space. The scope of the audit included main post offices, carrier annexes, stations, branches, and mail processing facilities. To accomplish our objective we visited selected facilities, conducted interviews, and examined other relevant materials.

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

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

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

- We established thresholds to remove post offices with less than 100 SF of excess space and carrier annexes with less than 300 SF of excess space.

[5] In our sample of 52 facilities, the Kilmer and Newark retail facilities were located within their respective processing and distribution centers (P&DCs), which we had also selected for review. For purposes of determining the OIG-calculated excess square footage and total earned building size per matrix, we combined the retail site with the P&DC.
[6] We used Postal Service criteria established in March of 2007 outlined in a letter issued by the senior vice president of Operations.
[7] Interior square footage obtained from the electronic Facilities Management System (eFMS).
[8]. In support of newly established criteria, the Headquarters Facility Group, Planning and Approval, designed matrices to assist with space requirements for planned facilities. We used the Space Requirements Matrix for Non-Flat Sequencing System (FSS) offices.
[9] WebBATS Monthly Summary Data for issued P.O. Box information, Intelligent Mail and Address Quality (IMAQ) Delivery Statistics Summary for route information, and Retail Data Mart for earned peak modeled window staffing.
[10] SBOC and Facilities Optimization Program.

- We used Non-Flat Sequencing System building standards for customer service sites.

- We provided additional support space by calculating retail and delivery space requirements separately.

- We provided additional delivery space for facilities with more than 51 routes. The additional routes received the space designated for a separate total facility instead of following the Postal Service's practice of adding an additional 123 SF per route.

- At facilities with unique functions, we either subtracted the space dedicated to that function from our metric or relied on Postal Service expertise to provide us with an accurate account of the building's excess space.

- Furthermore, we reduced our total monetary impact by 14 percent to address the difficulty in achieving a 100 percent realization of optimization efforts. The reduction correlates directly to the national vacancy rate for commercial real estate.

We conducted this performance audit from September 2009 through August 2010 in accordance with generally accepted government auditing standards and included such tests of internal controls as we considered necessary under the circumstances. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective. We discussed our observations and conclusions with management officials on June 14, 2010 and July 15, 2010, and included their comments where appropriate.

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

PRIOR AUDIT COVERAGE

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

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

APPENDIX B: DETAILED ANALYSIS

Excess Space is Significant in the Northern New Jersey District

Based on facility space requirements,[11] we calculated that the Northern New Jersey District maintains 1.98 million SF more than what is required for its current operational workload, thus, can be considered potential excess space. As depicted in Chart 1, excess space was 41 percent of the total interior square footage.

Chart 1 – District Interior and Excess Space Comparison

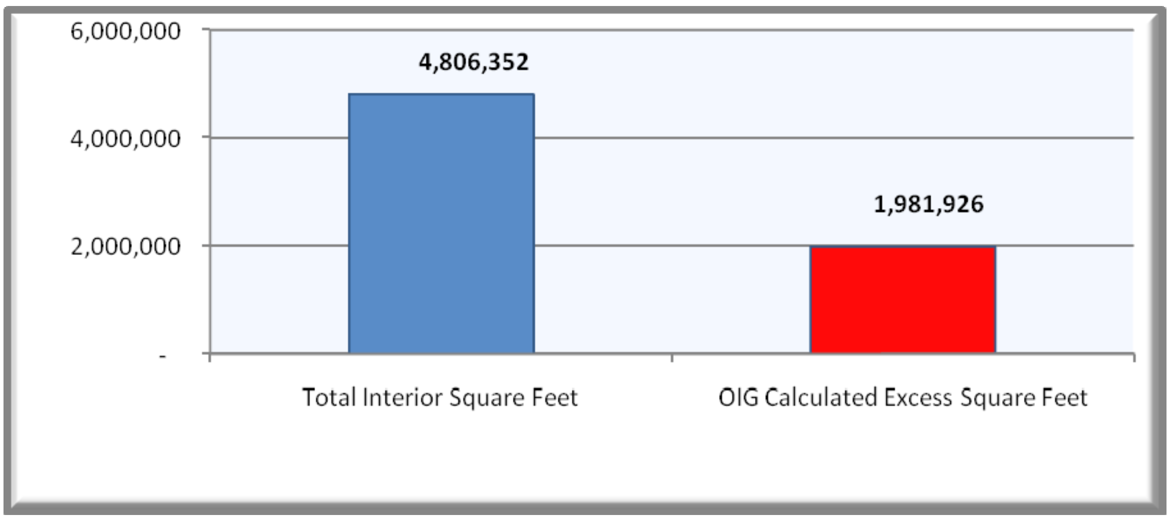


Table 2 shows the breakdown of interior square footage and OIG-calculated excess for the 52[12] visited facilities in the Northern New Jersey District. Main post offices contributed 46 percent of the excess space, while plants (35 percent) and branches (8 percent) followed to a lesser degree.

[11] We used Postal Service criteria established in March of 2007 outlined in a letter issued by the senior vice president of Operations. In support of this newly established criteria, the Headquarters Facility Group, Planning and Approval, designed matrices to assist with the space requirements of planned facilities.
[12] As mentioned previously, the Kilmer and Newark retail facilities are co-located within their respective processing and distribution centers (P&DCs), thus we combined them with the P&DC when calculating excess space.

Table 2. Excess Space by Facility Type Visited

Facility Type	Facility Type Count	Percentage of Count	Percentage of Excess	OIG Excess Square Footage	Interior Square Footage
Main Post Office	17	34%	46%	493,136	676,036
Plant	4	8%	35%	375,567	1,884,072
Branch	9	18%	8%	84,546	128,069
Carrier Annex	3	6%	6%	66,142	104,142
Station	7	14%	3%	32,187	83,960
Finance Station	10	20%	1%	10,430	24,152
Grand Total	**50**	**100%**	**100%**	**1,062,008**	**2,900,431**

To highlight excess space in the Northern New Jersey District, Illustration 1 depicts two facilities with excess interior space. The South Hackensack Branch is Postal Service-owned with one predominantly vacant floor. The Cranford Main Post Office is another Postal Service-owned facility, which houses delivery and retail operations with a vacant sub-basement. Both are located near other Postal Service facilities also maintaining excess space.

Illustration 1 – Examples of Excess Space

South Hackensack Branch
Interior SF: 86,155
Earned SF: 17,000
OIG Excess SF: 69,155

Cranford Main Post Office
Interior SF:35,608
Earned SF:9,500
OIG Excess SF: 26,108

See Appendix D for detailed earned space information on each of the facilities visited during fieldwork.

Causes for Excess Interior Space

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

- Postal Service policy requires installation heads to report excess space, but does not provide the necessary guidance to effectively accomplish this task.

- Facility systems do not track metrics such as dates identified or space conditions to allow effective management of excess space.

Guidance Can Be Improved

A review of the *Facility Database User Guide* shows it does not provide sufficient guidance for identifying excess space using the workload-driven space requirements. For example, the facility database space survey asks installation heads to objectively answer "*Do you have any vacant space in your facility that is in leasable condition and has access that does not compromise the security of the operation?*" without providing further guidance or referencing space standards. While we identified excess space at 285 of the 432 Postal Service facilities, only five locations answered "yes" to the vacant leasable space survey question. Further, our interviews revealed that Operations employees were unaware of the method used to identify excess space at their facility.

Facility Systems Do Not Allow for Effective Management of Excess Space

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

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

The GSA's Public Buildings Service also manages its leased portfolio by focusing on four primary areas: reducing vacancy, managing lease administration expenses, managing customer requirements, and analyzing market trends.[13] Similarly, owned facilities are monitored and analyzed using performance metrics such as revenue, funds from operations, operating costs, vacancy, net operating income, and return on equity. The Postal Service facility management systems are not able to manage property in this manner. For example, rents from leases or subleases are tracked manually using electronic spreadsheets.

[13] State of the Portfolio FY 2008 at: http://www.gsa.gov/Portal/gsa/ep/channelView.do?pageTypeId=8199&channelPage=%2Fep%2Fchannel%2FgsaOverview.jsp&channelId=-24880

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

We estimate if the Northern New Jersey district initiates disposal actions, there is a potential opportunity to realize $157,963,990 over typical and remaining lease terms. We consider this amount funds that could be used more efficiently or put to better use. See Appendix C for the monetary impact calculation and assumptions.

APPENDIX C: MONETARY IMPACTS
FUNDS PUT TO BETTER USE

Excess Interior Space Monetary Impacts

Project year	0	1	2	3	4	5	6	7	8	9	10
Fiscal year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Facilities											
Owned** Sublease Value	($53,395,621.20)	$28,371,006.72	$28,371,006.72	$28,371,006.72	$28,371,006.72	$28,371,006.72	$28,371,006.72	$28,371,006.72	$7,092,751.68		
Utility Savings		$2,866,431.60	$2,923,760.23	$2,982,235.44	$3,041,880.15	$3,102,717.75	$3,164,772.10	$3,228,067.55	$807,016.89		
custodial savings		$2,266,480.80	$2,266,480.80	$2,266,480.80	$2,266,480.80	$2,266,480.80	$2,266,480.80	$2,266,480.80	$566,620.20		
Leases Expiring FY 2009***											
Sublease Value	($2,204,792.55)	$1,171,485.28	$1,171,485.28	$1,171,485.28	$1,171,485.28	$1,171,485.28					
Utility Savings		$118,359.65	$120,726.84	$123,141.38	$125,604.21	$128,116.29					
custodial savings		$93,586.70	$93,586.70	$93,586.70	$93,586.70	$93,586.70					
Leases Expiring After 10/1/2010											
Sublease Value	($23,775,723)	$12,632,893	$10,605,463	$5,386,989	$4,731,502	$2,837,050	$1,685,844	$1,371,283	$918,615	$710,709	$543,023
Utility Savings		$1,276,350	$1,092,941	$566,257	$507,302	$310,266	$188,055	$156,025	$106,611	$84,132	$65,567
custodial savings		$1,009,207	$847,241	$430,352	$377,987	$226,644	$134,677	$109,548	$73,386	$56,777	$43,381
Subtotal	($79,376,136.30)	$49,805,800.38	$47,492,690.80	$41,391,533.99	$40,686,833.68	$38,507,353.33	$35,810,836.29	$35,502,411.56	$9,565,000.30	$851,617.86	$651,970.84
Cash Flows @ Sub Lease Efficiency Rate	($68,263,477.22)	$42,832,988.33	$40,843,714.08	$35,596,719.23	$34,990,676.97	$33,116,323.86	$30,797,319.21	$30,532,073.94	$8,225,900.26	$732,391.36	$560,694.92
Discounted at USPS cost of borrowing	($68,263,477.22)	$41,384,529.78	$38,128,044.14	$32,106,201.26	$30,492,353.48	$27,883,056.08	$25,053,639.02	$23,997,934.13	$6,246,843.72	$537,378.23	$397,487.18

Net Present Value: $157,963,990

Build-Out Costs SF	**$40.05**	**Utilities Savings SF per Year**	**$2.15**
Lease Savings SF per Year	**$21.28**	**Utility Cost Escalation Rate**	**2.0%**
USPS Cost of Borrowing	**3.5%**	**Custodial Rate SF**	**$3.40**
Sub-lease Efficiency Rate	**86%**		

Assumption: **Weighted Average Lease Years = 7.3

Value Assigned to Excess Space

The lease cost per square foot for the Northern New Jersey District is $21.28. Using Facility Inventory Reports from the eFMS, we calculated this figure by dividing total interior square footage by total lease costs. The value is similar to $19.34,[14] the average square foot cost for leasing commercial retail and office space in the district.

Utility Costs Associated with Excess Space

The utility cost per square foot for the Northern New Jersey District is $2.15, with a cost escalation rate of 2 percent. Using the Financial Performance Report (FPR), Line 42, we calculated this figure by dividing total annual utility expenses for FY 2009 by the district's total interior square footage.

Maintenance Costs Associated with Excess Space

The maintenance cost per square foot for the Northern New Jersey District is $3.40. We calculated this figure by dividing the total annual maintenance expenses[15] (FY 2009) by the district's total interior square footage. However, we reduced the cost by 50 percent based on previously identified savings in a custodial maintenance audit.[16]

Build-Out Costs Associated with Implementing Optimization Actions

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

Ownership of Facility and Term Years

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

We calculated leases expiring before the end of FY 2010 based on the assumption the leases would be renewed for the standard 5-year period. We calculated leases expiring after October 1, 2010 for the remaining lease term; and calculated Postal Service-owned facilities over a period of 73 years, which was the historical national average lease term.

Sublease Efficiency Rate

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

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[14] Realtor.com analyzes comparable private sector commercial retail and office space properties to determine average square footage costs.
[15] eFlash (Labor Distribution Code 38, Salary and Benefits) + FPR, Line 3F, Contract Cleaners Costs
[16] *Custodial Maintenance Audit Report*, (Report Number DA-AR-09-011, dated August 13, 2009).

APPENDIX D: FACILITIES VISITED

Facility Name	Type of Facility	Interior Square Footage	Total Earned Building Size From Matrix	Square Footage Identified in Node Studies	Potential Excess Square Footage
Allwood	Finance Station	2,640	3,000		-
Ampere	Finance Station	711	700		-
Bayway	Finance Station	1,264	900		364
Belleville	Branch	6,115	3,000		3,115
Belleville Annex	Carrier Annex	49,000	15,000		34,000
Bergen North	Station	13,020	8,000		5,020
Bergen South	Station	21,459	10,000		11,459
Bogota	Branch	1,000	2,000		-
Clifton	Main Post Office	49,500	19,500		30,000
Cranford	Main Post Office	35,608	9,500		26,108
Dominick V. Daniels	Plant	874,556	-		188,600
East Orange	Main Post Office	27,000	9,500		17,500
Edison	Main Post Office	23,477	15,000		8,477
Elizabeth	Main Post Office	69,800	25,000		44,800
Elmora	Finance Station	1,111	700		411
Fort Lee Annex	Carrier Annex	21,340	6,500		14,840
Garfield	Main Post Office	12,321	7,000		5,321
Hackensack	Main Post Office	12,118	3,900		8,218
Hasbrouck Heights	Branch	7,900	6,000		1,900
Highland Park	Main Post Office	2,470	2,000		470
Hoboken	Main Post Office	32,891	11,000		21,891
Home News Row	Carrier Annex	33,802	16,500		17,302
Jersey City	Main Post Office	90,517	12,000		78,517
Journal Square	Station	8,897	9,500		-
Kearny	Main Post Office	26,250	10,000		16,250
Kilmer Processing & Distribution Center	Plant	286,950	1,500		31,080
Leonia	Branch	2,996	4,000		-
Little Ferry	Main Post Office	6,500	5,000		1,500
Lyndhurst	Branch	4,691	6,000		-
Main Avenue Station	Finance Station	5,184	4,000		1,184
Newark P&DC	Plant	382,224	9,500		140,812
Nixon	Station	6,065	5,000		1,065
North	Finance Station	5,614	2,000		3,614
North Arlington	Branch	1,836	2,000		-
North Elizabeth	Finance Station	3,288	700		2,588
Northern NJ Metro	Plant	340,342	-		15,075
Nutley	Branch	11,100	2,000		9,100
Passaic	Main Post Office	41,128	9,500		31,628

Facility Name	Type of Facility	Interior Square Footage	Total Earned Building Size From Matrix	Square Footage Identified in Node Studies	Potential Excess Square Footage
Paterson	Main Post Office	159,536	13,000		146,536
Plainfield	Main Post Office	37,500	12,000		25,500
Ridgefield Park	Main Post Office	7,420	5,000		2,420
River Street	Station	14,436	2,900	14,436	-
Riverfront Plaza	Finance Station	1,779	700		1,079
Roseville[17]	Station	840	5,000		4,900
South Hackensack	Branch	86,155	17,000		69,155
Springfield Ave	Station	19,243	9,500		9,743
Union	Main Post Office	42,000	14,000		28,000
Union Square	Finance Station	871	2,000		-
Washington Park	Finance Station	1,690	500		1,190
Wood Ridge	Branch	6,276	5,000		1,276
Totals		**2,900,431**	**352,000**	**14,436**	**1,062,008**

[17] In eFMS, Roseville is shown as an 840 square foot facility. During fieldwork, we measured the facility as 9,900 square feet, which we used to calculate the OIG excess.

APPENDIX E: MANAGEMENT'S COMMENTS

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NORTHEAST AREA

UNITED STATES
POSTAL SERVICE

August 17, 2010

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

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

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

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

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

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

1. Methodology

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

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of the SSBD (earned) and calls the delta "excess". However, this methodology does not include allowances for[1]:

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.

Hoboken Office: Multi story

Patterson Office: Historic

Management Recommended Methodology

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

2. Inaccurate Data and Cost Factors

The audit states that 1,981,926 square feet of excess space exist in the Northern New Jersey with a potential to realize $157,963,990 over typical and remaining lease terms. The OIG also provides two specific recommendations for the $157,963,990 whereby, "Funds could be used more efficiently by implementing recommended actions."

Management disagrees with these findings because of the following:

A. Page 3 of the audit states, "The Northeast FSO has 27 approved optimization studies..." That number actually is 23 and those studies were approved in 2010. It did not include the optimization studies completed in 2009 which were 25 more.

[1] We excluded DVD, Kilmer, Newark, Northern NJ P&DC's from our analysis because the OIG obtained excess space measurements from respective industrial engineers and no methodology was applied.

B. The amount of usable excess square footage is not correct due to the methodology as described in Section 1 Methodology above.

C. The OIG states that the Value Assigned to Excess Space is $21.28. This was calculated by "dividing the total interior square footage by total lease costs" and reaching a number of $21.28. However, when Facilities calculated this number based on OIG formula, we find the number to be $27,356,403 (total lease cost) / 7,873,668 (total interior square footage) = $3.47. We believe the correct method to calculate leased per square foot cost is $27,356,403 (total lease cost) / 3,314,169 (total interior LEASED square footage) = $8.25.

D. Build-Out Cost: To build out the excess space and make it available to sublease, the number utilized was the total line 63 budget numbers from completed node studies divided by the square footage reduction. This is not an accurate method for determining the construction cost, because the node studies are based on terminating leases, selling owned buildings, and minimum renovation for the facilities gaining carriers and building alternate retail. The average square foot cost for this work cannot be used for build out cost for subleasing buildings, because the scope of work is completely different in these two scenarios. Management recommends that the OIG review each specific building to determine the following:

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

Potential Revenue:

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

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

Then adjust for the values of maintenance and utility savings.

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

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

Since the $157,963,990 over typical and remaining lease terms was not calculated according to our formula, we are unable to agree or disagree with this number.

Market Conditions:

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

Facilities engaged the largest 6 real estate brokerage firms in the country and all have confirmed that the property values are dropping, lease rates and demand are declining. As a result in general, our landlords are not accepting early lease terminations and our excess space must compete in a saturated market. Under this scenario, it makes it impossible for us in most cases to achieve any positive financial results by subleasing due to the capital improvement required to make the excess space available and the high demand for tenant improvement.

Conclusions:

A. Regarding the audit recommendations:

1. Management will develop a more accurate process and proper documentation for identifying and reporting excess space.
2. Management will include additional metrics to track dates and conditions of excess space. This will be part of a national process.

Both of these actions will be completed by the end of Quarter 2 , Fiscal Year 2011.

B. Actions already taken by management:

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

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

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

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

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

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

a. Establish and schedule a node study to analyzes all alternatives and associated costs/savings and complete schedule for all tasks.
b. Review all market conditions to determine financial viability of utilization of the space, disposal of the facility or sublease excess space.
c. Visit potential sites to verify all applicable costs.
d. Determine best financial alternative for utilization or disposal of the excess space and obtain all necessary management approvals.
e. Track time durations from final study approval of the action to ebuy notification for disposal.
f. Establish and track disposal schedule.

Generated out of optimization studies nationwide, we currently have over 120 properties on the market for sale and have scheduled to terminate 250 leases.

As a positive outcome of node studies in the New Jersey District, 20 of the 45 buildings on the audit list have been reviewed. Nine are currently in ongoing nodes studies, nine did not produce a positive NPV, one is gaining additional operations and one is having the lease 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.

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