OFFICE OF
INSPECTOR
GENERAL
UNITED STATES POSTAL SERVICE

Spending Trends for Maintaining Postal Service Facilities

Audit Report

November 27, 2013

Report Number SM-AR-14-002

OFFICE OF INSPECTOR GENERAL
UNITED STATES POSTAL SERVICE

HIGHLIGHTS

November 27, 2013

Spending Trends for Maintaining Postal Service Facilities

Report Number SM-AR-14-002

BACKGROUND:

The U.S. Postal Service's Facilities organization manages more than 32,000 facilities with more than 280 million square feet of space. Postal Service Finance and Planning allocates an annual budget to Facilities to fund repairs, alterations, and capital improvements. From fiscal years (FYs) 2009 to 2012, financial challenges have led to a $382-million decrease in the budget. Our objective was to determine the impact of budget constraints on the Postal Service's ability to fund facility repairs, alterations, and capital improvements.

WHAT THE OIG FOUND:

Budget constraints have affected the Postal Service's ability to fund repairs, alterations, and capital improvements. In FY 2012, the Postal Service spent $266 million (29 percent) below the industry average on facility repairs — spending $2.69 per square foot versus $3.81 per square foot. As a result, during FYs 2011 and 2012, Facilities did not complete 19,033 repairs (18 percent) estimated to cost $271 million. Fifty percent of these incomplete repairs represented safety, security, and potential future major repairs. Future costs for these unfunded repairs could reach $1.4 billion.

Sixteen percent of these repairs represented potential Occupational Safety and Health Administration violations, which could result in fines estimated at about $2.9 million.
In addition, Facilities can improve its repair prioritization process to ensure repairs are accurately prioritized. Misclassified repairs led to critical repairs being identified as low priority and repair prioritization lists were not reconciled to prior years' lists annually. This occurred because Facilities did not have documented procedures to ensure accurate repair classification and annual reconciliation of incomplete repairs.

Facilities ensures the safety and security of Postal Service properties by identifying, prioritizing, and completing repairs to meet operational needs. However, given the Postal Service's financial challenges, funds to complete all repairs were limited. Additionally, the Postal Service did not develop a strategy to complete all repairs and did not reallocate funds to unallocated critical repairs. By not accurately prioritizing and completing repairs, the Postal Service increased its safety and financial risks.

WHAT THE OIG RECOMMENDED:

We recommended management develop a strategy and reallocate funds to complete repairs and establish written procedures to accurately classify repairs and reconcile prioritization lists annually.

Link to review the entire report

November 27, 2013

MEMORANDUM FOR: TOM A. SAMRA
VICE PRESIDENT, FACILITIES

SHAUN MOSSMAN
ACTING VICE PRESIDENT, FINANCE AND PLANNING

E-Signed by Michael A. Magalski
VERIFY authenticity with eSign Desktop

FROM: Michael A. Magalski
Deputy Assistant Inspector General
for Support Operations

SUBJECT: Audit Report – Spending Trends for Maintaining Postal Service Facilities (Report Number SM-AR-14-002)

This report presents the results of our audit of Spending Trends for Maintaining U.S. Postal Service Facilities (Project Number 13YG005SM000).

We appreciate the cooperation and courtesies provided by your staff. If you have any questions or need additional information, please contact Monique P. Colter, director, Supply Management and Facilities, or me at 703-248-2100.

Attachment

cc: Corporate Audit and Response Management

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Introduction

This report presents the results of our audit of Spending Trends for Maintaining U.S. Postal Service Facilities (Project Number 13YG005SM000). This audit was the result of a value proposition[1] between the OIG and the vice president, Facilities. Our objective was to determine the impact of budget constraints on the Postal Service's ability to fund facility repairs, alterations, and capital improvements. See Appendix A for additional information about this audit.

The Postal Service's Facilities organization manages more than 32,000 facilities with more than 280 million square feet (SF) of space.[2] Postal Service Finance and Planning allocates an annual budget to Facilities officials to fund repairs and capital improvements. From fiscal years (FY) 2009 to 2012, financial challenges have led to a $382-million decrease in the budget for repairs, alterations, and capital improvements.

The Facilities organization identifies facility repairs through two methods: the annual prioritization list and the Facilities Single Source Provider (FSSP) system.[3] The prioritization list is created based on facility inspections at the beginning of the year and the FSSP system monitors repair requests that occur throughout the year. Funding is allocated to the highest priority repairs.

Conclusion

Budget constraints have affected the Postal Service's ability to fund repairs, alterations, and capital improvements. In FY 2012, the Postal Service spent $266 million (29 percent) below the industry average on facility repairs, spending $2.69[4] per square foot versus $3.81 per square foot. As a result, during FYs 2011 and 2012, Facilities did not complete 19,033 repairs (18 percent) estimated to cost more than $271 million. Fifty percent of these incomplete repairs represented safety, security, and potential future major repairs. Future costs for these unfunded repairs could reach $1.4 billion.

Sixteen percent of these repairs represented potential Occupational Safety and Health Administration (OSHA) violations, which could result in fines estimated at about $2.9 million. In addition, Facilities can improve its repair prioritization process to ensure repairs are accurately prioritized. Misclassified repairs led to critical repairs being

[1] An agreement between the U.S. Postal Service Office of Inspector General (OIG) and a Postal Service vice president agreeing to a specific body of work. The agreement identifies the area of focus, objectives, goals, scope of work, and anticipated value.
[2] Facility inventory as of December 11, 2012.
[3] FSSP was administered by the Facilities organization and was established for Postal Service personnel to record facility-related repairs and alterations. FSSP call centers respond to Postal Service facility repair and alteration needs, which are categorized as emergency, urgent, or routine.
[4] Benchmarked statistics did not include capital expenses. Because of the variations in company capitalization processes, determining the nature of the expenses to include in the calculation was not feasible. As a result, we took a conservative approach to our cost per square foot estimation that included capital expenses. Repair expense costs per square foot excluding capital expenses is $1.82.

identified as low priority and repair prioritization lists were not reconciled to prior years' lists annually.

Spending Below Industry Average

The Postal Service spent $266 million (29 percent) below the industry average on facility repairs[5] in FY 2012 — spending $2.69 per square foot versus the industry average of about $3.81 per square foot. As a result, Facilities did not complete 19,033 of 106,615 repairs (18 percent) during FYs 2011 and 2012. These repairs were needed at 8,800 facilities with an estimated cost of more than $271 million. Fifty percent of these incomplete repairs represented safety, security, and potential future major repairs; and 16 percent of these repairs were potential OSHA violations.

Facilities ensures the safety and security of Postal Service properties by identifying, prioritizing, and completing repairs to meet the needs of operations. However, given the Postal Service's financial challenges, funds to complete all repairs were limited. Despite budget constraints, Facilities could have reallocated funds for repairs and alterations by presenting a business case to Postal Service Finance and Planning. Facilities did not present a business case in FYs 2011 and 2012 to reallocate funds to complete repairs and avoid increased repair costs in future years. According to Finance and Planning, budget reallocations for safety and security-related repairs are more likely to succeed. For the FY 2014 budget, Facilities submitted a business case for the reallocation of $180 million in repair funding; however, a strategy has not been developed with Finance and Planning to complete all repairs in order to adequately maintain facilities.

By not completing necessary repairs, the Postal Service exposes itself to increased costs in future years. One of the nation's largest real estate firms recommends De Sitter's "Law of Fives" as a method of estimating the future costs of deferred repairs. The "Law of Fives"[6] concludes that if repairs are not performed, repair expenses can reach five times the repair costs in subsequent years. Based on this formula, future costs of incomplete repairs could reach $1.4 billion. However, we conservatively classified assets at risk of at least $271 million related to the future costs of not performing repairs.[7] In addition, these incomplete repairs could result in potential OSHA fines of up to $2.9 million. See Appendix B.

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[5] This estimate is conservative, because it does not account for the Postal Service's facilities that were open 24 hours, 7 days a week. Operational hours directly impact the useful life and repair needs of a facility. Based on the Postal Service's operational requirements and the age of its facilities, spending for repairs should be more comparable to industry averages.
[6] De Sitter's "Law of Fives" is an industry theory for estimating deferred maintenance costs. De Sitter theorizes that deferred maintenance is more than the current costs of the repair and includes the compound effect of deferring maintenance from 1 year to the next.
[7] At a minimum, future costs of repairs are equivalent to the current estimated costs of repairs.

Repair Prioritization Process

The Facilities organization could improve its repair prioritization process to ensure repairs are accurately prioritized. Misclassified repairs led to critical repairs being identified as low priority and repair prioritization lists were not reconciled annually. Postal Service policy[8] requires a ranking of repairs based on priority level and annual preparation of repair prioritization lists. Funding is then allocated to the highest priority projects.

Misclassified Repairs

Nine percent (1,136 of 12,258) of lower priority repairs should have been classified as high priority during FYs 2011 and 2012. This misclassification was a result of system controls that automatically rank repair needs identified during the year as low priority. The Facilities organization attempted to correct misclassified repairs by performing manual reviews; however, no formal process was in place to identify or correct misclassified critical repairs. Because the prioritization ranking was inaccurate and no formal review process existed to monitor repair classifications, there is increased risk the Postal Service may not be completing critical repairs.

Reconciliation of Prioritization Lists

Facilities did not include all incomplete FY 2011 repairs on the FY 2012 repair prioritization list. Although Facilities attempted to manually carry over incomplete repairs from prior years, it did not perform a complete reconciliation of the annual lists because there was no requirement to do so. As a result, there was a substantial risk that necessary repairs were not identified and prioritized in the subsequent year.

Recommendations

We recommend the vice president, Facilities and acting vice president, Finance and Planning:

1. Develop a strategy to complete all repairs in order to adequately maintain Postal Service facilities.

We recommend the vice president, Facilities:

2. Provide Finance and Planning with a business case to reallocate funds to critical repairs in order to mitigate future repair costs.

[8] The Postal Service Facility Inspection Program Review, dated October 19, 2010.

3. Establish written procedures to ensure repair classifications are accurate each year and to reconcile prioritization lists yearly to identify incomplete repairs to carry forward.

Management's Comments

Management agreed with our recommendations; however, they did not state whether they agreed or disagreed with the findings. Regarding recommendation 1, management will continue to allocate funding on an annual basis for repairs that impact employee safety, security, or potential future major repairs through the established business case and capital reallocation processes. In subsequent correspondence, management agreed to develop a strategy to address unfunded repairs should more funds become available in the future by March 31, 2014. In regard to recommendation 2, management will request reallocation of funds for critical repairs through the business case process on an as needed basis. With regard to recommendation 3, management will develop written procedures for repair classifications and prioritization list reconciliation by January 17, 2014.

Management did not agree with representations that supported our cost per square foot analysis. Specifically, management stated the total expenses for account classification codes 3B and line 63 in the Postal Service's Financial Performance Report (FPR) for FY 2012 did not include capital improvements attributed to operations with unique finance numbers and, therefore, were not included in the report data. Management also stated that the total salaries and benefit dollars did not include expenses associated with maintenance management. Finally, management stated that a thorough check of the 180 unfunded repairs in our review revealed that all projects classified as safety- or security-related have been completed or are active projects.

Management stated that, given the current financial and liquidity challenges facing the Postal Service, the agency enforced a capital commitment plan that was below average historical levels. Further, they stated that they initiated an ongoing capital freeze in 2009 to conserve cash and there was a decrease in Facilities planned repair dollars during the audit. Facilities agreed that there have been exceptions granted from the freeze to expend funds on projects that address health, safety, security, and continuity of operations projects. See Appendix C 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.

Additionally, the OIG contends that representations in the report adequately support the analysis performed as follows:

- Management stated that our analysis did not include total FY 2012 expenses for lines 3B and 63. We did not include the total expenses for lines 3B and 63 because many transactions associated with these line items (such as capital improvements related to Information Technology and Retail Operations) did not specifically relate to repairs, alterations, and capital improvements performed by Facilities. We excluded such transactions from our analysis and stand by our calculation of $370 million in expenses for repairs, alterations, and capital improvements.

- Management stated that our analysis did not include salaries for Maintenance management; however, to account for such variables, we included capital expenditures in our calculation, which represented more than half ($207 million of $370 million) of the expenses. The industry averages used in our report did not include capital expenditures because industry standards measure capital projects separately from repair projects. Because of our conservative methodology, we believe our analysis adequately represents FY 2012 spending for Postal Service repairs and alterations.

- Management stated that our calculations for safety, security, and potential future major repairs, as well as repairs representing potential OSHA fines, were based on a review of 180 repairs, the vast majority of which have been completed or are active projects. During the time of our audit, these repair projects had not been completed.

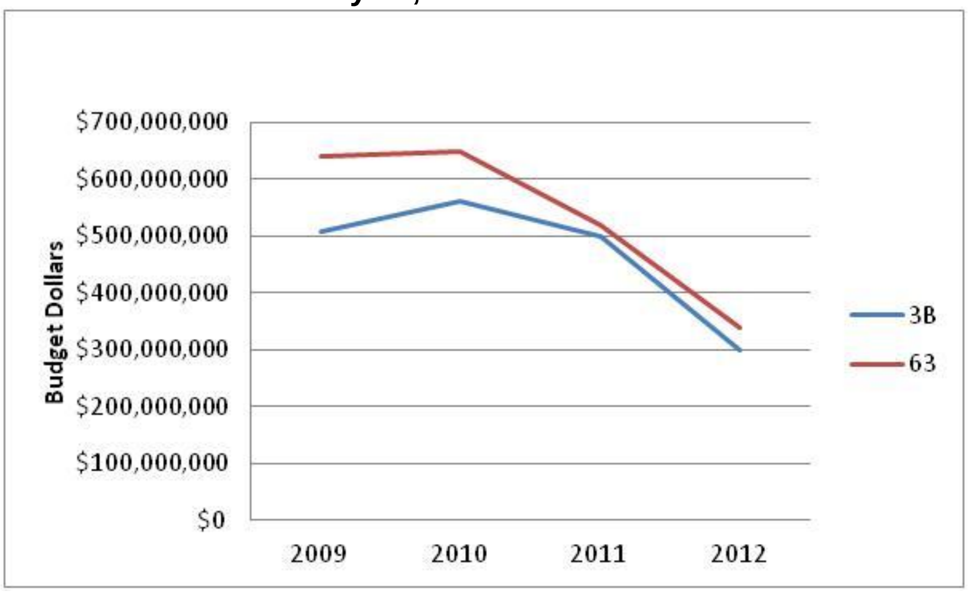
The OIG considers all the recommendations significant and, therefore, requires OIG concurrence before closure. Consequently, the OIG requests written confirmation when corrective actions are completed. Recommendation 2 can be closed with the issuance of this report. Recommendations 1 and 3 should not be closed in the Postal Service's follow-up tracking system until the OIG provides written confirmation that the recommendations can be closed.

Appendix A: Additional Information

Background

The Postal Service Facilities organization manages more than 32,000 facilities with more than 280 million SF of space.[9] Postal Service Finance and Planning allocates an annual budget to Facilities officials to fund repairs and capital improvements. From FYs 2009 to 2012, financial challenges have led to a $382-million decrease in the budget for repairs and capital improvements. The Postal Service accounts for facility repair and alteration expense under account classification code 3B in the Postal Service's FPR. Capital repairs and alterations are categorized under Code 63 in the FPR. See budget trend analysis in Table 1:

Table 1. Repairs and Alterations (3B) and Capital Expense (63) Budget Trend Analysis, FYs 2009 to 2012



Source: OIG analysis.

The Facilities organization identifies facility repairs through two methods: the annual prioritization list and FSSP. In anticipation of the upcoming year's budget, a prioritization list was created based on facility inspections and assessments. Identified repairs were ranked by priority level, and funding was allocated to the highest priority projects. Projects were prioritized as critical, high, medium, and low.

Additionally, repairs were identified throughout the year via FSSP as emergency, urgent, or routine and budget funds were allocated to these repairs. FSSP was supported and administered by the Facilities organization and was established for Postal Service personnel to record facility-related repairs. FSSP call centers respond to Postal Service facility repair needs.

[9] Facility inventory as of December 11, 2012.

Objective, Scope, and Methodology

Our objective was to determine the impact of budget constraints on the Postal Service's ability to fund facility repairs, alterations, and capital improvements.

To accomplish our objective we:

- Analyzed a random sample of data from the annual priority list for budget years FYs 2011 to 2012 and repair calls not completed in the FSSP system for FYs 2009 to 2012 to identify safety and security issues, potential OSHA violations, lack of preventative maintenance, and potential future major repairs. In addition, we reviewed the status of repairs and the repair history of applicable buildings in the electronic Facilities Management System (eFMS).

- Interviewed management and staff from Postal Service Headquarters Facilities and Finance to determine the current processes for budgeting for facility repairs.

- Obtained benchmarking data for facility repairs from Whitestone Research to determine the industry standard for cost per square foot for facility repair. The data were aligned with the Postal Service's facility inventory and provided more direct square footage comparisons. For example, Whitestone provided detailed spending and costs per square foot for various facility types that directly correspond to the Postal Service's building inventory. These facility types were manufacturing plants, post offices, and retail facilities.

- Through the Enterprise Data Warehouse (EDW), we analyzed Postal Service budget and funding for facility repair, alteration, and capital improvement for FYs 2009 to 2012 to determine trends and compare to industry standards.

We conducted this performance audit from October 2012 through November 2013 in accordance with generally accepted government auditing standards and included such tests of internal controls as we considered necessary under the circumstances. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective. We discussed our observations and conclusions with management on August 26, 2013, and included their comments where appropriate.

We assessed the reliability of computer-generated data by comparing source documents to data in eFMS and EDW to validate monetary amounts and the certifying official. We determined that the data were sufficiently reliable for the purposes of this report.

Prior Audit Coverage

The OIG did not identify any prior audits or reviews related to the objective of this audit.

Appendix B: Other Impacts

Recommendation	Impact Category	Amount
1	Assets at Risk[10]	$271,509,594
1	Assets at Risk	2,932,812
Total		**$274,442,406**

Minimum Costs of Not Performing Repairs

One industry practice for estimating the costs of deferred maintenance is De Sitter's "Law of Fives." This approach considers deferred maintenance as more than the current costs of the repair and incorporates the compound effect of deferring maintenance from 1 year to the next. De Sitter asserts that if repairs are not performed, repair expenses can reach five times the current repair costs in subsequent years. Based on this formula we calculated the potential future costs of deferred repairs by multiplying repairs not completed in FYs 2011 and 2012 by a factor of five. The total future costs of incomplete repairs for these fiscal years ranged from $271,509,594 to $1,357,547,970. The lowest range represents the current estimated costs of the repairs and, as a result, the minimum cash outlay for the repairs in the future.

OSHA Fines

We calculated average FY 2012 fines of $62,437 for 33 of 180 repairs in our sample, using an average cost of OSHA fines per incident. Based on this amount, we projected potential OSHA fines of $2,932,812 based on the lower limit of a 95-percent confidence for about 3,171 projected repairs in our universe that relate to safety, security, or potential future major repairs.

[10] Assets or accountable items that are at risk of loss.

Appendix C: Management's Comments

UNITED STATES
POSTAL SERVICE

November 18, 2013

JUDITH LEONHARDT
DIRECTOR AUDIT OPERATIONS
OFFICE OF INSPECTOR GENERAL

SUBJECT: Draft Audit Report–Spending Trends for Maintaining Postal Service Facilities
Report Number – SM-AR-14-DRAFT

Thank you for the opportunity to respond to the recommendations from your Facilities Spending Trend Audit. The Facilities and Finance and Planning offices generally agree with the recommendations noted in the draft audit report. Given the current financial and liquidity challenges facing the Postal Service, management enforced a capital commitment plan which was below average historical levels. A capital spending freeze was initiated in 2009 to conserve cash and has continued to the present date. Priority was given to projects: 1) needed for safety and/or health or legal requirements; 2) required to provide service to our customers; and 3) initiatives with a high return on investment and a short payback period. There were decreases in Facilities planned repair dollars at the time of the audit, which was conducted from October 2012 through October 2013 and a discussion of findings was provided to the HQ Finance group in quarter 4 of fiscal year (FY) 2013. Facilities agrees that there have been exceptions granted from the freeze to expend funds on projects that address health, safety, security and continuity of operations projects.

The following are data issues represented in the draft audit report that will or do affect the analysis in its current form:

- Total expenses for line 3B and line 63 for FY2012 – Actual expenses for Line 3B and Line 63 for FY2012 exceed the $370M noted in the report backup spreadsheet. This difference is largely driven by capital improvements attributed to Information Technology, Retail Operations, etc., that have unique finance numbers and are not included in the report data.

- Total salaries and benefit dollars for Building Systems Equipment (LDC 37) and Maintenance Planning Control & Stores (LDC 39) – On the OIG supplied spreadsheet the expense for maintenance labor is $255M. The salaries and benefit dollars at 50 percent for Maintenance Management (LDC 35) is not included in the maintenance labor total. The impact is an additional $140M.

- Fifty percent of incomplete repairs represented safety, security, and potential future major repairs – Apparently this calculation was based on a review of 180 unfunded repairs out of the 19,033 total. The OIG finding was that approximately 50 percent of the 180 unfunded repairs were potential safety, security or future major repair projects. A thorough check of the 180 unfunded repairs reveals that virtually all the projects classified as safety or security have been completed or are active projects. As stated previously, funding has never been withheld on projects associated with safety or security.

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- Sixteen percent of these repairs were potential OSHA violations – Same comments as the paragraph above.

Recommendation #1:
Vice Presidents of Facilities and Finance and Planning develop a strategy to complete all repairs in order to adequately maintain Postal Service facilities.

Management Response/Action Plan:
Management agrees with the recommendation as stated above. Finance and Planning will continue to allocate funding on an annual basis for repairs that impact employee safety, security, or potential future major repairs through the established Decision Analysis Report (DAR) Business Case process. Management will continue to address additional funding needs as they occur through the established Capital Reallocation process.

Target Implementation Date:
Ongoing

Responsible Officials:
Manager, Finance for Infrastructure and Manager, Facilities Repair and Alteration

Recommendation #2:
Vice President, Facilities provides Finance and Planning with a business case to reallocate funds to critical repairs in order to mitigate future repair costs.

Management Response/Action Plan:
Facilities agrees with this recommendation. Facilities is aware of the DAR Business Case process and the Manager, Facilities Repair and Alteration will request reallocation of funds for critical repairs on an as needed basis.

Target Implementation Date:
Ongoing

Responsible Official:
Manager, Facilities Repair and Alteration

Recommendation #3:
Vice President, Facilities establishes written procedures to ensure repair classifications are accurate each year. Establish written procedures to reconcile prioritization lists yearly to identify incomplete repairs to carry forward.

Management Response/Action Plan:
Facilities agrees with this recommendation. Currently repair classifications default to standard ratings in order to ensure integrity of the system. Prior to the annual budget request, each project is reviewed and classifications are manually adjusted as appropriate. Prioritization lists are reviewed annually and high priority projects are manually pulled into the FY where it appears funds will be available. The Manager, Facilities Repair and Alteration will develop written procedures for repair classifications and prioritization reconciliation.

Target Implementation Date:
January 17, 2014

Responsible Official:
Manager, Facilities Repair and Alteration

This report and management's response do not contain information that may be exempt from disclosure under the FOIA.

Tom A. Samra
Vice President, Facilities

Shaun E. Mossman
A/Vice President, Finance and Planning

cc: Sally K. Haring, Manager, Corporate Audit Response Management