

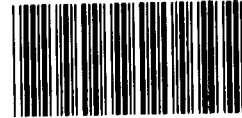
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Briefing Report to the Chairman,
Subcommittee on Federal Services, Post
Office and Civil Service, Committee on
Governmental Affairs, U.S. Senate

July 1992

POSTAL SERVICE

Decisions to Purchase Two Properties in Queens, New York



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General Government Division

B-248862

July 17, 1992

The Honorable David Pryor
Chairman, Subcommittee on Federal Services,
Post Office and Civil Service
Committee on Governmental Affairs
United States Senate

Dear Mr. Chairman:

This briefing report responds to your request that we review the United States Postal Service's (USPS) acquisition of property for and subsequent management decisions associated with the general mail facility in Queens, New York. On April 6, 1992, we briefed the Subcommittee on the results of our work. As requested, we are summarizing the information provided at the meeting in this briefing report.

BACKGROUND

For many years, USPS looked for a site on which to consolidate its mail processing operations and to resolve long-standing operational problems in Queens, New York. Finding an acceptable site in highly urbanized Queens was difficult. In April 1985, USPS said that at least 27 sites had been reviewed during the prior 3 years. A July 1986 decision analysis report prepared by the USPS Northeast Region identified two acceptable sites for the Queens facility: a former American Telephone and Telegraph, Inc. (AT&T) Western Electric manufacturing facility, and a former Phelps-Dodge Corporation metals refinery. While the AT&T site was preferred (acquisition had been approved by USPS' Capital Investment Committee), the Northeast Regional Postmaster General supported his staff's opinion that it was operationally important to have the Phelps-Dodge site as an alternative, in the event the acquisition of the AT&T property fell through.

On September 9, 1986, the USPS Board of Governors, after being told that the AT&T property was not for sale to USPS, approved the purchase of the Phelps-Dodge site (about 37 acres) and the construction at that site of the Queens mail handling and vehicle maintenance facilities at a cost not to exceed \$125.6 million including \$14.7 million for the land. Title to the property officially transferred to USPS on December 30, 1986.

Subsequent to the Board of Governors approval but before the transfer of title to the Phelps-Dodge site, negotiations for the AT&T site continued. AT&T and USPS agreed to a purchase price of \$65 million in November 1986. In May 1987, USPS purchased the AT&T property--a 548,000-square-foot building on a 24-acre site in the College Point area of Queens, New York. USPS estimated that an additional \$50.7 million would be needed to renovate the existing building and to construct a vehicle maintenance facility. This estimate was a major factor in the decision to purchase the AT&T site because, when added to the purchase price of \$65 million, the total estimated cost of \$115.7 million was \$10 million less than the purchase price and estimated cost of construction on the Phelps-Dodge site.

RESULTS IN BRIEF

USPS has invested nearly \$80 million for the purchase of two sites in Queens, New York. One site was not used and remains unusable because of hazardous waste contamination. Construction at the second site has cost more than the estimate used to justify the purchase and further investment is needed.

USPS purchased the Phelps-Dodge site with provisions in the contract of sale requiring Phelps-Dodge to clean up hazardous waste. Cleanup activities, except for testing and analysis, have been suspended since the summer of 1987, and additional hazardous waste was found at the site in 1990. Despite certifications by Phelps-Dodge's contractors that asbestos-containing materials were removed, significant quantities of asbestos were also found at the site in 1990. As owner of the property, USPS is liable for cleaning up the hazardous waste and asbestos if Phelps-Dodge is unable or unwilling to do so. If this occurs, USPS attorneys said that USPS would have a cause of action against Phelps-Dodge to regain the money expended. Presently, however, USPS has millions invested in a vacant site that it cannot use or sell without additional expenditures or price concessions.

The \$65 million paid for the AT&T site was 44 percent more than the appraised fair market value of the property. USPS justified the price by citing operational savings, competition for purchase of the property, and a cost savings of \$10 million over the purchase price and construction costs on the Phelps-Dodge site. The cost of acquisition and renovation of the AT&T property was scheduled to cost \$116 million, compared to \$126 million for Phelps-Dodge. However, additional funding has raised total costs on the

AT&T acquisition to more than \$128 million. Another funding request to make operational improvements and to correct health and safety defects is pending. The Director, Office of Real Estate, USPS, said that initial estimates were based on essential repairs needed to achieve operating occupancy and that additional operating requirements and efficiency upgrades contributed to the need for increased funding.

OBJECTIVE, SCOPE, AND METHODOLOGY

Our objective was to examine and document USPS actions in acquiring the two Queens sites. We interviewed officials from USPS and the New York State Department of Environmental Conservation, inspected the renovated AT&T property, and reviewed documents pertaining to both site acquisitions. We also spoke to officials of the Postal Inspection Service, who were also investigating the Phelps-Dodge acquisition. Appendix I contains more details on our objective and scope of work. We did our work from January 1992 through April 1992 in accordance with generally accepted government auditing standards.

AGENCY COMMENTS

We considered the comments of several postal officials, including the Directors of the Office of Real Estate and the Office of Capital Investment and Financial Analysis, on a draft of this briefing report. They suggested several clarifications, which we made as appropriate. They emphasized that the decisions to acquire the properties were greatly influenced by the need to resolve long-standing operational problems and that the overall objective of improving postal operations has been accomplished. The Director of the Office of Capital Investment and Financial Analysis said that the comparative cost analysis supporting the AT&T decision was consistent with policy and believes that the AT&T property remains the economically preferred alternative. The Director of the Office of Real Estate believes that USPS ultimately will not suffer a financial loss on the acquisition of the Phelps-Dodge property.

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As agreed with the Subcommittee, unless you publicly announce its contents earlier, we plan no further distribution of this report until 30 days from the date of this letter. At that time we will send copies of this report to the Chairman, USPS Board of Governors; the Postmaster General; and other congressional committees with

B-248862

postal oversight responsibilities. Copies will also be made available to others upon request.

The major contributors to this briefing report are listed in appendix IV. If you have any questions, please call me on (202) 275-8676.

Sincerely yours,

A handwritten signature in cursive script, appearing to read "L. Nye Stevens". The signature is written in black ink and is positioned to the left of the typed name.

L. Nye Stevens
Director, Government Business
Operations Issues

C O N T E N T S

	<u>Page</u>
LETTER	1
APPENDIXES	
I	OBJECTIVE AND SCOPE OF WORK 6
II	PHELPS-DODGE SITE 9
	Phelps-Dodge Site Summary 9
	Decision on Hazardous Waste Cleanup Changed 10
	Hazardous Waste Cleanup Not Completed 12
	Significant Amount of Asbestos Still on Site 14
	Ongoing Postal Inspection Service Investigation 16
III	AT&T SITE 19
	AT&T Site Summary 19
	Purchase Price 44 Percent More Than Appraised Value 20
	Original Cost Estimate for AT&T Site Surpassed 22
IV	MAJOR CONTRIBUTORS TO THIS BRIEFING REPORT 24

ABBREVIATIONS

AT&T	American Telephone and Telegraph, Inc.
DAR	Decision Analysis Report
GMF	General Mail Facility
NYDEC	New York State Department of Environmental Conservation
USPS	United States Postal Service

Objective and Scope of Work

- Provide information on USPS actions in acquiring the two sites
- Interviewed officials--USPS and NYDEC
- Visited Queens GMF
- Reviewed USPS documents on site acquisitions

OBJECTIVE AND SCOPE OF WORK

Our objective was to provide, as requested by the Subcommittee, information on United States Postal Service (USPS) acquisition of property for a new general mail facility (GMF) in Queens, New York. We interviewed USPS headquarters managers and attorneys who were involved with one or both of the site acquisitions; USPS staff from the Northeast Region and the Facilities Service Center in Windsor, Connecticut; and USPS staff at the Facilities Service Office in Hoboken, New Jersey, and at the Queens GMF in College Point, Queens. We spoke with Postal Inspection Service staff who were concurrently undertaking their own investigation of the Phelps-Dodge acquisition. We also interviewed staff from the New York State Department of Environmental Conservation (NYDEC).

We looked at the American Telephone and Telegraph, Inc. (AT&T) site and toured the Queens GMF to see the conditions that caused USPS officials to ask for additional funds (deviation requests) to correct health and safety defects and to make operational improvements.

We also reviewed numerous documents relating to both site acquisitions. These documents, dating back to 1985, included USPS internal and external memoranda, purchase agreements, decision analysis reports (DARs), minutes of Board of Governors meetings, environmental consultants' reports, applicable sections of USPS real estate manuals, Postal Inspection Service reports, and a copy of the Order on Consent between the New York State Department of Environmental Conservation (NYDEC) and Phelps-Dodge.

Our work was done from January 1992 to April 1992 in accordance with generally accepted government auditing standards. We obtained comments from cognizant USPS officials and incorporated their views where appropriate.

PHELPS-DODGE SITE

Phelps-Dodge Site Summary

- Decision on Hazardous Waste Cleanup Changed
- Hazardous Waste Cleanup Not Completed
- Significant Amount of Asbestos Still on Site
- Inspection Service Review Continuing

Decision on Hazardous Waste Cleanup Changed

- May 1985 study identified soil contamination
- Transfer of title before cleanup
- USPS financial liability increased

DECISION ON HAZARDOUS WASTE CLEANUP CHANGED

A May 1985 study by a USPS environmental consultant identified extensive soil contamination on portions of the Phelps-Dodge site. Because of this discovery, USPS' initial decision was to make the purchase of the property contingent upon successful cleanup of the site by Phelps-Dodge and certification by NYDEC.

Early drafts of the purchase agreement said that Phelps-Dodge agreed and understood that any and all toxic and hazardous waste found on the property would be its responsibility to remedy prior to transfer of title. This provision was revised during negotiations with attorneys for Phelps-Dodge.

The purchase agreement ultimately signed by Phelps-Dodge and USPS on August 13, 1986, said that the presence of hazardous waste on the premises would not prevent transfer of title. Why and who in USPS agreed to the less protective provisions was not documented, and we were unable to obtain an explanation from interviews.

In lieu of actual cleanup before title transferred, the signed agreement required Phelps-Dodge to develop a remedial action plan to clean up the site and get NYDEC's approval. Further, \$2 million of the purchase price was placed into an escrow account to pay for the plan's implementation, and those funds are still available. The agreement also provided that Phelps-Dodge, at its cost and expense, would indemnify, hold harmless, and defend USPS for a period of 4 years from the closing against any and all future actions by regulatory bodies and/or other third parties regarding any type of waste situated upon or within the property attributed to Phelps-Dodge during the period of its ownership.

By accepting title to the site, USPS increased its potential financial liability. Under federal law (42 U.S.C. Sec. 9607 (1988)--the Comprehensive Environmental Response, Compensation, and Liability Act of 1980), the USPS, as owner, could be required to clean up the site if Phelps-Dodge is unable or unwilling to do so. According to its attorneys, USPS would then have a cause of action against Phelps-Dodge to recapture the money expended.

Hazardous Waste Cleanup Not Completed

- Remediation plan approved by NYDEC in December 1986
 - Groundwater contamination identified in July 1987 and cleanup suspended
 - Revised remediation plan requested by NYDEC
 - No additional cleanup or approved revised plan to date
 - Additional contamination identified in 1990
-

HAZARDOUS WASTE CLEANUP NOT COMPLETED

Phelps-Dodge's plan to remediate soil contamination at the site was formally approved by NYDEC in December 1986 and was embodied in an Order on Consent between Phelps-Dodge and NYDEC executed on February 11, 1987. The Order characterized the property as an inactive hazardous waste disposal site constituting a significant threat to the environment.

The excavation and removal of contaminated soil began in March 1987. In July, excavation failed to yield uncontaminated soil before groundwater was encountered--a situation that had not been anticipated--and cleanup was suspended. NYDEC ordered Phelps-Dodge to submit a revised remediation plan for cleanup of the site. There have been no cleanup activities at the site since August 1987. In the interim, Phelps-Dodge has performed groundwater and surface water testing and analysis, held discussions with NYDEC and USPS, and submitted revised work plans to NYDEC. However, there has been no agreement on what needs to be done to complete the cleanup.

Concerned about the lack of progress in cleaning up the site, USPS, among other actions, sent letters to the Commissioner of NYDEC (1990) and New York's governor (1991) requesting that the project be given a high priority and that NYDEC enforce its legal agreement with Phelps-Dodge. Both letters stressed getting the property back on the tax rolls and its excellent potential for stimulating employment. NYDEC, however, has not declared Phelps-Dodge in default of the Order on Consent; and therefore, USPS believes that a civil suit against Phelps-Dodge over the cleanup issue would not be successful.

Additional hazardous waste contamination--not addressed by the existing remediation plan--was found at the site. A 1990 USPS study found potential contamination sources on three parcels of the property where no remedial action was planned. These sources included underground oil storage tanks, a former metal scrap storage area, and discolored soil used for fill. The study recommended a comprehensive soil and groundwater sampling program to adequately evaluate these parcels for oil and hazardous materials contamination. The results of this study were provided to NYDEC and Phelps-Dodge; the latter, however, has not accepted the responsibility for addressing these issues. The Director, USPS Office of Real Estate, told us that recent conversations with NYDEC indicate that they expect to require Phelps-Dodge to address the entire site.

Significant Amount of Asbestos Still on Site

- Early drafts of agreement assigned removal responsibility to Phelps-Dodge
 - Removal certificates furnished at time of sale
 - Asbestos identified on site in 1990 by USPS
 - Responsibility for removal not yet accepted by Phelps-Dodge
 - USPS may have to pay for removal or grant price concessions to a buyer
-

SIGNIFICANT AMOUNT OF ASBESTOS STILL ON SITE

Early drafts of the Phelps-Dodge site purchase agreement said that the company was responsible for removing all asbestos materials.¹ However, no asbestos-removal provisions appeared in the final agreement signed by Phelps-Dodge and USPS in August 1986. Instead, at the closing on December 30, 1986, USPS' Director of the Office of Real Estate requested that Phelps-Dodge provide certification with regard to asbestos removal from the site. These certifications were submitted to USPS in January 1987. USPS did not verify their accuracy.

During a visit to the site in 1990, USPS personnel identified asbestos in some structures. USPS subsequently contracted for an analysis of materials at the site. Asbestos-containing materials were found on all parcels of land having permanent structures or buildings. USPS also learned that some removal had been completed, but a poor job had been done in numerous locations. Specific management or abatement options were recommended by the contractor.

Asbestos removal is not covered by the Order on Consent between Phelps-Dodge and New York State. On July 12, 1991, USPS advised Phelps-Dodge officials that if the asbestos were not removed or USPS were not notified of their intention to begin removal within 14 days, USPS would use all means available to enforce its right to an asbestos-free site.

Asbestos removal on the site could cost millions of dollars. Phelps-Dodge, to date, has not indicated a willingness to assume this responsibility. USPS is preparing a litigation report as a basis for filing a lawsuit against Phelps-Dodge. If Phelps-Dodge does not agree to remove the asbestos or if litigation against the company is unsuccessful, the site cannot be sold or used without USPS paying for asbestos removal or granting a price concession to a purchaser willing to acquire the property as is.

The Director, USPS Office of Real Estate, believes that neither of the two events will result in a financial loss to USPS. He anticipates that any costs incurred in selling the property would be offset by appreciation or recoverable from Phelps-Dodge.

¹These materials could be friable or nonfriable, contained, wrapped, or otherwise mitigated.

Ongoing Postal Inspection Service Investigation

- USPS actions in acquiring site being questioned
- Investigation scheduled for completion on June 30, 1992

ONGOING POSTAL INSPECTION SERVICE INVESTIGATION

The Postal Inspection Service is investigating the acquisition of the Phelps-Dodge site. Answers are being sought for the following questions:

- Did the decision analysis report provided to the USPS Board of Governors prior to their approval of the Phelps-Dodge purchase contain an adequate analysis of the toxic waste problem at the site?
- Why were provisions of the purchase agreement changed to allow USPS to acquire the site without prior cleanup?
- Were legal conditions or agreements to protect USPS interest adequately enforced?

On June 11, 1992, the Assistant Chief Inspector-Audit informed us that they expect to complete their investigation by June 30, 1992.

AT&T SITE

AT&T Site Summary

- Purchase Price 44 Percent More Than Appraised Value
- Original Cost Estimate for AT&T Site Surpassed

Purchase Price 44 Percent More Than Appraised Value

- USPS influenced by competition for site purchase
 - Investigation confirmed competition
 - \$65 million purchase price not expected to increase total cost beyond \$116 million
 - Decision to purchase made by top USPS management
-

PURCHASE PRICE 44 PERCENT MORE THAN APPRAISED VALUE

In May 1987, 5 months after closing on the Phelps-Dodge site, USPS bought the AT&T property for \$65 million--\$20 million, or 44 percent, more than appraised fair market value. USPS justified this above market value price through operational savings, active competition for purchase of the site, and a "breakeven" analysis.¹ A Postal Inspection Service investigator confirmed that in 1987 at least one other party was negotiating for the property. USPS projected that, including the \$65 million purchase price, renovation of the AT&T property could be done for \$116 million--\$10 million less than new construction on the Phelps-Dodge site.

We could not document the evolution of the USPS/AT&T negotiations for purchase of the AT&T site during 1986. However, we did determine that the decision to acquire the property at the \$65 million asking price was made during a meeting on October 7, 1986, attended by the Postmaster General and senior USPS officials.

¹"Breakeven" analyses typically compare the costs of various project alternatives to determine the most preferable. In this case, the only alternatives considered were the Phelps-Dodge and AT&T sites. Decision Analysis Reports also indicated that other sites were considered and eliminated for valid reasons.

Original Cost Estimate for AT&T Site Surpassed

- Originally estimated that GMF on AT&T property would save \$10 million
- Additional funding to make GMF operational exceeds savings
- More funds requested

ORIGINAL COST ESTIMATE FOR AT&T SITE SURPASSED

The total cost of acquisition, design, and renovation of the AT&T property was initially projected to be \$115.7 million--\$10 million less than the purchase and development of the Phelps-Dodge site. However, this cost advantage has been eliminated by an additional funding request and may be further eroded by another request.

In July 1990, USPS prepared a deviation request to increase authorized funding by \$12.7 million to upgrade or replace building systems, construct a fuel island, and renovate the building. The request also provided an additional \$5 million for renovations of the AT&T property by eliminating construction of a vehicle maintenance facility.

If approved, a pending deviation request will provide funds for correction of health and safety defects and for correction of operational deficiencies. The Director of USPS' Office of Capital Investment and Financial Analysis said that expected expenditures will total less than \$5 million. Even with a total project cost of around \$133 million, the Director believes that the AT&T site is still the economically preferred alternative.

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