

GAO

Report to the Subcommittee on Federal
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Information, Federal Services, and International
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Governmental Affairs, U.S. Senate

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FEDERAL REAL PROPERTY

Strategy Needed to Address Agencies' Long-standing Reliance on Costly Leasing



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Highlights

Highlights of [GAO-08-197](#), a report to the Subcommittee on Federal Financial Management, Government Information, Federal Services, and International Security, Committee on Homeland Security and Governmental Affairs, U.S. Senate

Why GAO Did This Study

In January 2003, GAO designated federal real property as a high-risk area, citing the government's overreliance on costly, long-term leasing as one of the major reasons. GAO's work over the years has shown that building ownership often costs less than operating leases, especially for long-term space needs. GAO was asked to identify (1) the profile of domestically held, federally leased space including the overall amount and type of space agencies lease, and any related trends; (2) the factors that drive agencies to lease space that may be more cost-effective to own; and (3) any actions taken by the administration and alternative approaches proposed to address this issue. GAO reviewed fiscal year 2006 Federal Real Property Profile (FRPP) leasing data and relevant documents and interviewed officials from the General Services Administration (GSA), the Office of Management and Budget (OMB), and the U.S. Postal Service (USPS). GAO also reviewed 10 building leases that were among those with the largest dollar value in 3 locations GAO visited.

What GAO Recommends

OMB, in conjunction with the Federal Real Property Council (established by the administration to help support reform efforts in real property), and in consultation with key stakeholders, should develop a strategy to reduce agencies' reliance on leased space for long-term needs when ownership would be less costly. OMB generally agreed with the report and GAO's recommendation.

To view the full product, including the scope and methodology, click on [GAO-08-197](#). For more information, contact Mark Goldstein at (202) 512-2834 or goldsteinm@gao.gov.

FEDERAL REAL PROPERTY

Strategy Needed to Address Agencies' Long-standing Reliance on Costly Leasing

What GAO Found

Federal agencies rely extensively on leasing, occupying about 398 million square feet of leased building space domestically in fiscal year 2006, according to FRPP data. GSA, USPS, and the U.S. Department of Agriculture lease about 71 percent of this space, mostly for offices, with the military services leasing another 17 percent. GSA is increasing its use of leased space and predicts that in 2008 it will, for the first time, lease more space than it owns.

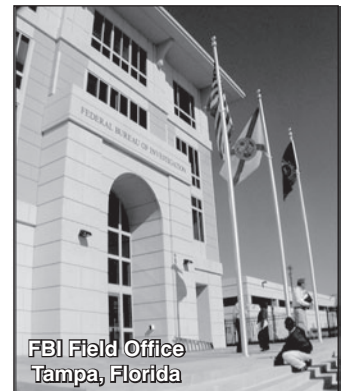
In the 10 GSA and USPS leases GAO examined, decisions to lease space that would be more cost-effective to own were driven by the limited availability of capital for building ownership and other considerations, such as operational efficiency and security. For example, for four of the seven GSA leases GAO analyzed, leasing was more costly over time than construction—by an estimated \$83.3 million over 30 years. Although ownership through construction is often the least expensive option, federal budget scorekeeping rules require the full cost of this option to be recorded up-front in the budget, whereas only the annual lease payment plus cancellation costs need to be recorded for operating leases, making them “look cheaper” in any year even though they generally are more costly over time. USPS is not subject to the scorekeeping rules and cited operational efficiency and limited capital as its main reasons for leasing.

While the administration has made progress in addressing long-standing real property problems, efforts to address the leasing challenge have been limited. GAO has raised this issue for almost 20 years. Several alternative approaches have been discussed by various stakeholders, including scoring operating leases the same as ownership, but none have been implemented. The current real property reform initiative, however, presents an opportunity to address the leasing challenge.

GSA Operating Leases for the Federal Bureau of Investigation (FBI) Field Offices in Chicago, Illinois, and Tampa, Florida



FBI Field Office
Chicago, Illinois



FBI Field Office
Tampa, Florida

Source: GSA.

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Abbreviations

Agriculture	U.S. Department of Agriculture
CAF	capital acquisition fund
CBO	Congressional Budget Office
FBI	Federal Bureau of Investigation
FRPC	Federal Real Property Council
FRPP	Federal Real Property Profile
GSA	Government Services Administration
OMB	Office of Management and Budget
TAPS	The Automated Prospectus System
USPS	U.S. Postal Service

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United States Government Accountability Office
Washington, DC 20548

January 24, 2008

The Honorable Tom Carper
Chairman
The Honorable Tom Coburn
Ranking Member
Subcommittee on Federal Financial Management,
Government Information, Federal Services,
and International Security
Committee on Homeland Security
and Governmental Affairs
United States Senate

In January 2003, we designated federal real property as a high-risk area,¹ citing the government's overreliance on costly leasing as one of the major reasons for our designation. Other reasons for the designation included unreliable data, excess and deteriorating property, and challenges associated with protecting assets against the threat of terrorism. Under certain conditions, such as fulfilling short-term space needs, leasing may be a lower-cost option than ownership. However, our work over the years has shown that building ownership often costs less than operating leases, especially for long-term space needs. For example, in 1995, we found that 55 of 73 operating leases that the General Services Administration (GSA) had entered into cost a total of \$700 million more than construction.² In 1999, we reported that for eight of nine major operating lease acquisitions GSA had proposed, construction would have cost less than leasing and saved the government \$126 million over 30 years.³

In February of 2004, the President signed Executive Order 13327,⁴ which created the Federal Real Property Council (FRPC). Real property

¹GAO, *High-Risk Series: Federal Real Property*, [GAO-03-122](#) (Washington, D.C.: January 2003).

²GAO, *General Services Administration: Opportunities for Cost Savings in the Public Buildings Area*, [GAO/T-GGD-95-149](#) (Washington, D.C.: July 13, 1995).

³GAO, *General Services Administration: Comparison of Space Acquisition Alternatives—Leasing to Lease-Purchase and Leasing to Construction*, [GAO/GGD-99-49R](#) (Washington, D.C.: Mar. 12, 1999).

⁴Executive Order 13327—Federal Real Property Asset Management, Feb. 6, 2004.

management also was added to the President's Management Agenda⁵ to address the problems we had raised in our high-risk report. The order required executive branch agencies⁶ to standardize real property data for inclusion in a governmentwide database of owned and leased space, known as the Federal Real Property Profile (FRPP). FRPP is maintained by GSA on behalf of FRPC, which controls access to the data. Shortly after signing the executive order, the President added the Federal Asset Management Initiative, commonly referred to as the real property initiative, to the President's Management Agenda. Under the executive order, the Office of Management and Budget (OMB) was given the responsibility to, among other things, review the efforts of agencies in achieving the governmentwide policies established in the executive order. In our April 2007 update on real property high-risk issues,⁷ we concluded that these efforts provided a good foundation for strategically managing federal real property, but that more progress was needed for us to remove real property management from our high-risk list.

You requested that we evaluate federal leasing trends and challenges. To do so, we addressed the following questions:

1. What is the profile of domestically held, federally leased space, including the overall amount and type of space agencies lease, and what are any related trends?
2. What factors drive agencies to lease space that may be more cost-effective to own?
3. What actions has the administration taken, and what alternative approaches have been proposed, to address agencies' reliance on costly leased space?

⁵The President's Management Agenda, announced in the summer of 2001, is the administration's strategy for improving the management of the federal government in five areas, including strategic management of human capital, competitive sourcing, improved financial performance, expanded electronic government, and budget and performance integration.

⁶The executive order applies to 24 executive branch agencies, but not to the United States Postal Service (USPS). However, USPS submitted real property information to the Federal Real Property Profile (FRPP), the centralized real property database, in fiscal years 2005 and 2006, but did not include any usable data on performance measures.

⁷GAO, *Federal Real Property: Progress Made Toward Addressing Problems, but Underlying Obstacles Continue to Hamper Reform*, [GAO-07-349](#) (Washington, D.C.: Apr. 13, 2007).

To answer the first question, we used publicly available data from FRPP, as well as additional data analyses we requested from OMB. These additional analyses used data from the three civilian real-property-holding agencies with the largest portfolios of leased building space held within the United States and U.S. territories—GSA, the U.S. Postal Service (USPS), and the U.S. Department of Agriculture (Agriculture)—to develop a more detailed analysis and assessment of FRPP data. We used data from GSA’s Public Building Service to examine trends in leasing because GSA had historical data and GSA’s tenants represent a cross-section of federal agencies. These data are different from those of FRPP. FRPP data are governmentwide, while Public Building Service data are more detailed and are only for properties that GSA controls. The FRPP data were generally reliable for describing the inventory, but data quality concerns, such as missing data, which we identified both during this review and previously,⁸ would limit the usefulness of FRPP for other purposes, such as strategic decision making. OMB is taking action to address these data quality concerns. USPS and Agriculture could not provide us with an electronic copy of historical data on their leases; therefore, we could not include information from these agencies in our analysis of trends. We determined that the FRPP and GSA Public Building Service data were sufficiently reliable for the purposes of our review by reviewing GSA’s data systems and other reports. In addition, we defined “domestic” or “domestically held” leased space as being in the United States and U.S. territories.

To answer the second question, we analyzed seven GSA and three USPS building leases to determine the estimated cost of leasing versus the cost of new construction. We visited GSA regional offices in Atlanta, Georgia; Chicago, Illinois; and Fort Worth, Texas; and USPS facility service offices in Lawrenceville, Georgia; Bloomingdale, Illinois; and Dallas, Texas, to determine the reasons that led these agencies to lease certain building space. We selected these locations because multiple agencies leased space there, the number of larger-dollar-value leases was high, and the locations were geographically diverse. The building leases we selected were among the larger-dollar-value leases within these locations. Our findings from visits to, and economic analyses of, federally leased space cannot be generalized to federally leased space nationwide. USPS provided similar data for its leases but requested that we not provide them in this report because of a Postal Regulatory Commission ruling that such data should not be disclosed to the public.

⁸[GAO-07-349](#).

To answer the third question, we analyzed administration and agency efforts to address long-standing problems in real property and past proposals for reforming federal leasing policy. For this question, we did not focus on issues related to USPS, because USPS is not subject to OMB guidance on leasing. In addressing each of the three questions, we interviewed agency officials and obtained and analyzed relevant laws and documents. Additional information on our methodology appears in appendix I. We conducted this performance audit from July 2006 to January 2008 in accordance with generally accepted government auditing standards. 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 objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Results in Brief

Federal agencies rely extensively on leasing, occupying about 398 million square feet of leased building space domestically in fiscal year 2006, according to data from FRPP. Over half of the leased square footage is used for offices, with the remaining space allocated for a mix of warehouses, family housing, schools, and other uses. GSA (which acts as a leasing agent for most federal agencies), USPS, and Agriculture were the dominant civilian agencies, leasing roughly 71 percent of this space, with the military services leasing an additional 17 percent. FRPP is a relatively new inventory, and as a result, governmentwide data on leasing trends are not available. However, GSA maintains historical data on leasing and ownership that are useful for trends because GSA's tenants represent a cross-section of federal agencies. The most striking trend in GSA-leased space is that, according to GSA, for the first time, it predicts it will lease more space than it owns in 2008. From fiscal year 2003 through fiscal year 2006, GSA increased its leased space from about 160 million square feet to about 172 million square feet while its owned space decreased from about 180 million square feet to about 174 million square feet. GSA also analyzes trends in its leased portfolio, including trends in lease extensions and vacancy rates.

In the 10 leases we examined, decisions to lease space for long-term needs that would have been more cost-effective to own were driven by the limited availability of capital for ownership and other considerations, such as security and operational efficiency. For four of the seven GSA leases we analyzed, leasing was more costly over the long term than construction—by an estimated \$83.3 million over 30 years. For example, GSA executed leases for the Federal Bureau of Investigation's (FBI) field offices in

Chicago in 2006 and in Tampa in 2005. These leases were estimated to cost \$40 million and about \$7 million more, respectively, than federal construction over 30 years. GSA officials said they entered into these leases because GSA lacked up-front capital at that time and there were security considerations. For GSA, limited funding for construction is exacerbated by federal budget scorekeeping rules, which require, for ownership and capital leases, that the full cost of the government's commitment be recorded in the budget in the first year. In contrast, for operating leases, only the amount needed to cover yearly lease payments plus cancellation costs is required to be recorded in the annual budget, thereby making operating leases "look cheaper" in any given year. This is a long-standing challenge, and overreliance on leasing is one of the major reasons we designated federal real property management as a high-risk area. Although USPS is not subject to the federal budget scorekeeping rules, USPS officials said that limited up-front capital to fund construction projects also is a hindrance for USPS.

The administration has made considerable progress in focusing on long-standing problems in the real property area, such as poor data and excess property, but efforts to address the leasing challenge have been limited. The 2004 executive order on real property management, establishment of FRPC, and other related initiatives have given greater emphasis to improving real property management and have brought a more strategic focus to fixing the problems. However, the impact of budget scorekeeping rules—though rooted in sound budget policy and designed to promote transparency—on real property costs has not been addressed. We have raised this issue for almost 20 years. Over this time, several proposals have been discussed, such as scoring operating leases the same as ownership when they are used to meet a long-term need or establishing capital acquisition funds at agencies to fund ownership. However, none of these proposals have been implemented. OMB staff said that the administration's efforts have not yet addressed the leasing challenge and that basic improvements, such as developing a reliable, governmentwide inventory of space and establishing performance measures, had to occur before OMB could take on broader, more complex policy issues such as the leasing challenge. Nonetheless, with progress being made and increased commitment by OMB and Congress to address long-standing real property problems, there is reason to be optimistic that the leasing challenge can be addressed. We are therefore recommending that OMB, in conjunction with FRPC and other stakeholders, develop a strategy to reduce agencies' reliance on leased space for long-term needs when ownership would be less costly.

OMB generally agreed with the report and its recommendation but asked that we narrow the recommendation to focus on how to identify those instances in which agencies are relying on costly leasing. A means of identifying such leases could logically be part of the strategy we are recommending and seems worthwhile pursuing. However, our report objectives did not include how best to identify costly leases, and therefore we chose not to change our recommendation. OMB also provided technical clarifications, which we incorporated where appropriate. GSA also agreed with the report and provided technical clarifications, which we incorporated where appropriate. USPS and Agriculture did not provide comments on the draft report.

Background

The federal real property environment has many stakeholders and involves a vast and diverse portfolio of assets that are used for a wide variety of missions. Real property is generally defined as facilities, land, and anything constructed on or attached to land. According to FRPP data, the federal government owned and leased 1.2 million assets with a replacement value of \$1.5 trillion in fiscal year 2006. The Department of Defense, USPS, GSA, and the Department of Veterans Affairs hold the majority of the owned and leased facility space. The makeup of the federal government's facilities reflects the diversity of agencies' missions and includes office buildings, prisons, post offices, courthouses, laboratories, and border stations.

GSA is authorized by law to acquire, manage, utilize, and dispose of real property for most federal agencies. These authorities are contained in title 40 of the U.S. Code, and GSA is responsible for its implementation. Agencies are subject to title 40 authorities unless they have their own specific real estate authority and are exempted from title 40. Under title 40, GSA is authorized to enter into lease agreements for up to 20 years that the Administrator of GSA considers to be in the interest of the federal government and necessary to accommodate a federal agency.⁹ GSA uses this authority to lease space on behalf of many federal government agencies. In 1996, GSA began a program called "Can't Beat GSA Leasing" that offered federal agencies the choice of using GSA as their leasing agent or assuming responsibility for their own leasing. Under this program, GSA delegated leasing authority for general purpose space to the heads of all federal agencies. GSA's original delegation consisted of six conditions,

⁹40 U.S.C. § 585.

which included the requirements that federal agencies acquire and utilize leased space in accordance with all applicable laws and regulations. In December of 2002, GSA revised its regulations to specifically state that all agencies must follow the budget scorekeeping¹⁰ guidelines and OMB's requirements for leases, capital leases, and lease purchases identified in appendixes A and B of OMB Circular A-11.¹¹ Federal agencies also may have their own independent statutory authority related to real property. In November 2007, GSA amended its delegations of leasing authority to acquire general purpose office space and special purpose office space. GSA said its basis for amending these delegations of authority was to increase oversight and to facilitate compliance with all applicable laws and regulations governing the acquisition of real property, since several recent audits of its delegation program found instances in which agencies had failed to meet the requirements of their leasing delegation. USPS, which is an independent establishment in the executive branch, is authorized to sell, lease, or dispose of property under its general powers and is exempt from most federal laws dealing with real property and contracting.¹²

Since 2003, we have reported that federal real property is a high-risk area due to excess and deteriorating property, reliance on costly leasing, unreliable data, and security challenges.¹³ Specifically, problems are exacerbated by underlying obstacles that include competing stakeholder interests, legal and budgetary limitations, and the need for improved capital planning. For example, agencies cited local interests as barriers to disposing of excess property, and agencies' limited ability to pursue ownership leads them to lease property that may be more cost-effective to own over time. In February of 2004, the President signed Executive Order 13327 and added real property management to the President's Management Agenda, which scores agencies on their progress in meeting performance targets. The order applies to 24 executive branch

¹⁰Budget scorekeeping rules are designed to ensure that the effects of legislation on the deficit are consistent with established conventions and comply with statute.

¹¹41 C.F.R. § 102-73.135.

¹²39 U.S.C. §§ 401 and 410.

¹³See the list of related GAO products at the end of this report.

departments and agencies,¹⁴ but not to USPS. Agencies under that executive order have, among other things, designated senior real property officers, established asset management plans, standardized real property data reporting, and adopted various performance measures to track progress. The administration's establishment of FRPC also supports reform efforts. Furthermore, OMB staff said that the administration intends to work with Congress to provide agencies with tools to more effectively manage their real property assets. To meet the order's requirement for standardized real property data reporting, FRPC worked with GSA to develop FRPP.¹⁵ The first governmentwide reporting of inventory data for FRPP took place in December of 2005, and selected data were included in the fiscal year 2005 Federal Real Property Report, published by GSA on behalf of FRPC in June of 2006. In our April 2007 update on real property high-risk issues, we reported that the administration and major real-property-holding agencies had made progress toward strategically managing federal real property and addressing some long-standing problems.

¹⁴The executive order applies to the Departments of Agriculture, Commerce, Defense, Education, Energy, Health and Human Services, Homeland Security, Housing and Urban Development, the Interior, Justice, Labor, State, Transportation, the Treasury, and Veterans Affairs; the Environmental Protection Agency; National Aeronautics and Space Administration; U.S. Agency for International Development; GSA; the National Science Foundation, the Nuclear Regulatory Commission; the Office of Personnel Management; the Small Business Administration; and the Social Security Administration.

¹⁵OMB officials told us that Federal Management Regulations require all executive branch agencies, including independent agencies, to report data for FRPP. USPS is not subject to the executive order but provided OMB with data for FRPP in fiscal year 2005 that did not include any usable data on performance measures.

Federal Agencies Rely Extensively on Leasing, Especially for Office Space Needs; GSA Predicts It Will Lease More Space Than It Owns in 2008

Federal agencies rely extensively on leasing, occupying about 398 million square feet of leased building space domestically in fiscal year 2006, according to data from FRPP. According to fiscal year 2006 FRPP information, GSA and USPS hold the majority of the federal government's leased building space, totaling about 270 million square feet, or about 67 percent of the leased inventory of space within the United States and U.S. territories. Agriculture holds 4 percent of leased space. In fiscal year 2006, GSA, which acts as a leasing agent for other agencies, had 6,750 leases and provided slightly less than 169 million square feet of leased building space to nearly every department within the federal government. Table 1 shows the amount of domestically leased space by agency, according to FRPP.

Table 1: Profile of Building Asset's Leased Square Footage in the United States and U.S. Territories by Federal Agencies, Fiscal Year 2006

Agency name	Leased square footage
GSA	168,929,552
USPS	99,527,123
Army	43,665,656
Agriculture	16,752,216
Air Force	15,800,618
Navy	9,173,844
Transportation	7,854,759
Veterans Affairs	7,589,059
Energy	6,657,275
Health and Human Services	4,160,208
Interior	4,025,243
Labor	3,776,466
Justice	3,227,893
Treasury	1,474,853
Homeland Security	1,470,675
Commerce	1,197,995
National Archives and Records Administration	545,258
National Aeronautics And Space Administration	524,029
Defense/Washington Headquarters Service	499,559
Corps of Engineers	303,769
Environmental Protection Agency	243,732
National Science Foundation	188,527
State	183,848
Office of Personnel Management	91,271

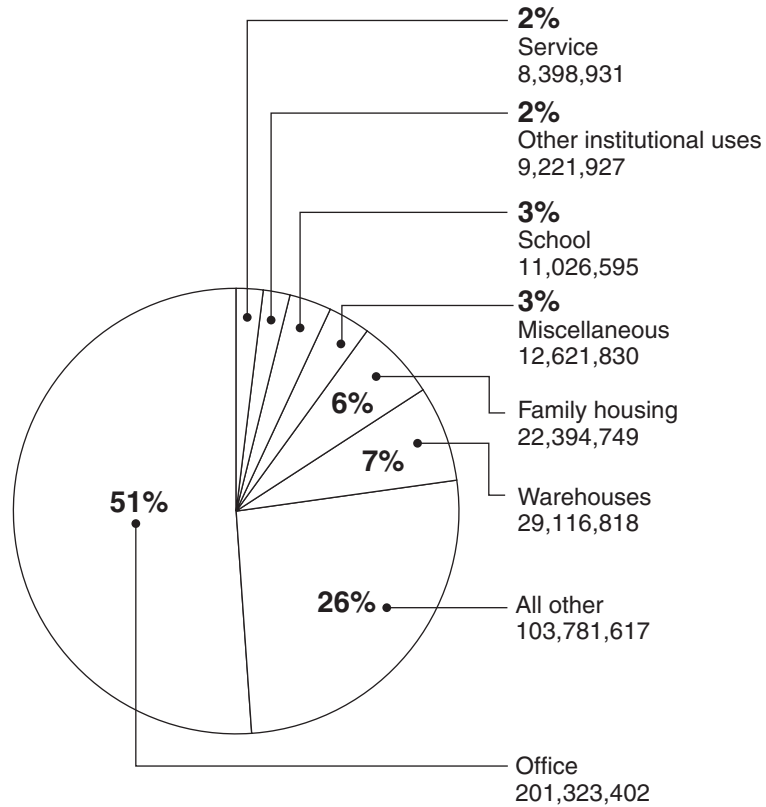
Agency name	Leased square footage
Peace Corps	18,886
U.S. Agency for International Development	3,553
Total	397,885,867

Source: OMB.

Office Space Is the Predominant Type of Federally Leased Space

According to FRPP data, over half of the space, in terms of square footage, is office space, with a mix of other uses including warehouses, family housing, and schools. The single largest category of federally leased space—office-related purposes—accounts for approximately 201 million square feet, or 51 percent of all domestic leased building space. This category includes office space and military headquarters space. The second largest category of leased space, “all other,” includes space for post offices and laboratories, as well as other buildings that cannot be classified in other categories. About 104 million square feet of leased space were reported in this category. In addition, agencies reported leasing about 29 million square feet of building space for warehouses and about 22 million square feet for family housing—a category that includes, among other things, public housing and military personnel housing. Figure 1 shows domestic leased square footage by predominant usage.

Figure 1: Federal Real Property Profile of Leased Square Footage by Predominant Usage in the United States and U.S. Territories, Fiscal Year 2006



Source: GAO.

Note: The “other institutional uses” category includes buildings such as libraries, chapels, museums, and outpatient clinics. The miscellaneous category includes the remaining leased building space predominant use categories—laboratories; dormitories/barracks; hospital, prison, and detention centers; industrial, navigation and traffic aids; communication systems; and post offices. The service category includes buildings used for service activities, such as maintenance and repair shops.

As the federal agency that leases the most space, GSA leases space for a variety of purposes, but about 152 million square feet, or 90 percent of its leased portfolio, is leased exclusively for offices. GSA also leases about 15 million square feet, or about 9 percent of its overall leased portfolio, for warehouses for agencies. Additionally, GSA leases building space for such purposes as laboratories, family housing, and other miscellaneous uses. These uses account for about 1 percent of its leased space. Agriculture had more than 3,700 leases totaling nearly 17 million square feet of building space in fiscal year 2006. About 92 percent of Agriculture’s leased space, or slightly more than 15 million square feet, is for offices. Agriculture also

has a little over a million square feet leased under the all other, warehouse, and service categories. According to FRPP data, USPS has roughly 28,100 leases, which are categorized as all other. According to OMB staff, because of a USPS data-coding error, the square footage for USPS assets was included in the “all other” category and accounts for about 95 percent of the square footage reported for this category. USPS told us that the majority of its leased buildings are used primarily for customer service post offices, and a portion of its building space is used for retail facilities and carrier annexes.¹⁶

We did not develop data on the overall yearly cost of leased space to the federal government. OMB staff said that variation in costs included in lease payments among agencies would create data consistency problems. As an indicator of asset value, FRPP tracks replacement value—or the cost to replace leased space with owned space—and the estimated replacement value of the federal government’s existing domestic leases totals \$48 billion.

Data Quality Remains a Challenge

In April of 2007, we reported that although agencies have made progress in collecting and reporting standardized real property data for FRPP, data reliability is still a challenge at some of the agencies, and agencies lack a standard framework for data validation.¹⁷ For this review, we assessed the fiscal year 2006 FRPP leasing data and found them to be generally reliable for the purpose of profiling the leased inventory. However, we noted some data quality issues that would be cause for concern if FRPP were used for more than describing the inventory, such as strategic decision making. For example, USPS categorized its 28,108 leased assets “mission dependent not critical” and did not include annual operating costs for each leased asset. The categorization of USPS’s leased facilities as “mission dependent not critical” and “not mission critical” could be questioned, since USPS’s facilities serve as the main channel for providing mail delivery service to all people residing in the United States. In our April 2007 report, we recommended that OMB develop a framework that agencies can use to better ensure the validity and usefulness of key real property data in FRPP. OMB concurred with this recommendation and has required agency-specific validation and verification plans and, according to OMB officials, has developed an FRPP validation protocol to certify agency

¹⁶Carrier annexes house the carrier routes without a retail or post office box operation.

¹⁷[GAO-07-349](#).

data. According to OMB staff, each score card agency has developed and implemented an agency-specific data validation and verification plan.

GSA's Reliance on Leasing Continues to Increase

FRPP is a relatively new inventory, a result of implementing Executive Order 13327, and therefore governmentwide data on leasing trends were not available. However, GSA, whose tenants represent a cross-section of federal agencies, maintains historical data that are useful in examining trends. The most striking trend in GSA-leased space, GSA predicts, is that for the first time it will lease more space than it owns in 2008. From fiscal year 2003 through fiscal year 2006, GSA increased its leased space from about 160 million square feet to about 172 million square feet while its owned space decreased from about 180 million square feet to about 174 million square feet.¹⁸

Besides tracking total leased square footage, as all federal agencies are required to do for FRPP, GSA captures, analyzes, and evaluates a number of other leasing trends, including trends in lease extensions, vacancy rates in leased facilities, negative net operating income leases,¹⁹ and GSA lease rates compared with market lease rates. GSA conducts trend analysis using the data from prior years that it retains, or annually archives. GSA officials stated that annually archiving data is the key to establishing baselines and conducting trend analysis because it aggregates data for similar fields over time, which allows for analyses of comparable data each year. According to GSA officials, these analyses can then be used to better anticipate and react to market changes, helping to ensure the most efficient management of the lease portfolio. GSA officials said they can use annually archived data to isolate key trends, examine the causes of these trends, and identify potential solutions. According to GSA officials, they are broadening the use of outside published data to forecast market conditions and rent for leasing activity.

GSA officials told us that trend analysis with annually archived data can identify “low- value” leases—those for which the government is currently paying above-market rates. Such analysis also can identify leases in

¹⁸GSA uses end-of-the-fiscal-year leased square footage calculations for its State of the Portfolio report, whereas its FRPP submission is based on data for the end of the calendar year.

¹⁹A GSA-leased building has a negative net operating income when the rental payments from tenant agencies generate a negative net return to GSA.

markets where rental rates are forecasted to grow quickly and the government risks paying higher lease rates in the future. Second, trend analysis of market data comparisons can indicate whether a lease extended without full competition is more expensive than a lease fully competed in the free market. GSA estimated that approximately 65 percent of its expiring leases were extended at the request of tenant agencies. GSA officials said that leases that are extended could potentially place GSA at risk, especially in areas where the agency may be overpaying because of changing market rates. According to GSA officials, information on vacancy rates is crucial for asset managers to effectively manage and minimize vacancies.

Decisions to Lease Selected Federal Properties Are Not Always Driven by Cost-effectiveness Considerations

In the 10 leases we examined, decisions to lease space that would be more cost-effective to own were driven by the limited availability of capital for ownership and other considerations, such as operational efficiency and security. To examine the cost-effectiveness of leasing decisions, we analyzed economic analyses—30-year net present value calculations—that GSA provided for seven building leases and that USPS provided for three leases.²⁰ We found that leasing was more costly over the long-term than construction for four of the seven GSA leases, and these four GSA leases were estimated to be \$83.3 million more costly over 30 years than construction.²¹ Table 2 shows the results of our analyses for the seven selected GSA lease acquisitions, the comparative cost advantages and disadvantages of construction versus leasing for these acquisitions, and the reasons cited by agency officials for leasing. USPS provided similar data for its leases but requested that we not provide them in this report because of a Postal Regulatory Commission ruling that such data should not be disclosed to the public.

²⁰A 30-year net present value analysis measures multiyear cash flows in present-dollar terms, so the value of a dollar received today can be compared against the value of a dollar received in the future. Such an analysis allows managers to compare the cost of a multiyear lease, with payments spread over a number of years, with ownership, which requires up-front expenditures of capital.

²¹GSA performed the economic analyses for the seven building leases at our request to demonstrate the long-term costs of construction versus leasing. GSA had already decided to enter into these leases and used actual rental rates for the individual leases in its analyses.

Table 2: Comparative Cost Advantages and Disadvantages of Construction versus Leasing for Selected GSA Buildings

Square feet in thousands, dollars in millions

Primary occupant and location	Total square footage	Base year for present value analysis	Estimated present-value acquisition cost for each alternative		Construction vs. lease	Acquisition decision	Reason(s) cited for decision
			Construction	Lease			
FBI, Chicago, Illinois	384.5	2005	229.8	270.1	40.3	Lease	Limited up-front capital, security considerations, consolidation of existing leases
Alcohol, Tobacco, and Firearms and Secret Service, Chicago, Illinois	99	2005	56.4	89.6	33.2	Lease	Security requirements
FBI, Tampa, Florida	130.3	2005	67.6	74.4	6.8	Lease	Limited up-front capital, immediate need for space
FBI, Dallas, Texas	210.4	2005	101.1	104.1	3	Lease	Limited up-front capital, immediate need for space
Atlanta Federal Center, various agencies, Atlanta, Georgia	1,196.1	2005	597.1	593.5	(3.6)	Lease	Leasing the most cost-effective option, immediate need for space
Centers for Disease Control and Prevention, Atlanta, Georgia	107.2	2005	54	45.8	(8.2)	Lease	Leasing the most cost-effective option, immediate need for space
Social Security Administration, Dallas, Texas	274.5	2005	134.6	111.4	(23.2)	Lease	Leasing the most cost-effective option, immediate need for space

Source: GSA.

Case Examples: FBI Field Offices in Chicago, Illinois, and Tampa, Florida

For FBI’s field office in Chicago, Illinois, the 30-year net present value cost of meeting FBI’s long-term space need with an operating lease was estimated to cost \$40 million more than construction. In this instance, GSA officials stated, limited availability of up-front capital and security considerations prevented them from pursuing ownership at that time. According to GSA officials, before deciding to enter into the lease in 2006

for the new field office, which has a 14-year term, GSA pursued other options for its tenant agency, including repair and alteration and building construction. Ultimately, these options proved unfeasible because, according to GSA officials, massive repairs were needed at one of the proposed facilities and existing facilities could not meet new building security requirements established after the September 11, 2001, terrorist attacks.

For the FBI field office in Tampa, Florida, the 30-year net present-value cost of meeting FBI's long-term space need with an operating lease was estimated at about \$7 million more than construction over a 30-year period in 2005. According to a GSA official, building construction was never considered as a viable option because of the perceived lack of necessary up-front capital. A GSA official stated that FBI had outgrown existing space in several leased facilities throughout the city and cited enhanced security requirements, anticipated expansion, and the immediacy of FBI's space need as major reasons for consolidating existing leases into one central location. The term of the lease is 15 years. Primarily because of the amount of square footage required, virtually all downtown Tampa locations were eliminated. GSA is using operating leases to help FBI meet long-term needs for field offices. For instance, GSA is using operating leases in 40 of 41 new FBI field office locations across the country. Figure 2 shows the FBI field offices in Chicago and Tampa.

Figure 2: FBI Field Office in Chicago, Illinois, and Tampa, Florida



Source: GSA.



FBI Field Office, Tampa, Florida

Case Example: Bureau of Alcohol, Tobacco, and Firearms and Secret Service, Chicago, Illinois

GSA entered into 10-year operating leases in Chicago for the Bureau of Alcohol, Tobacco, and Firearms and the Secret Service in the same building, estimated at a 30-year net present value to cost \$33 million more than construction. GSA officials said that the prior leases for both agencies, which also were housed previously in the same facility, expired and the original lessor opted not to retain the agencies as tenants for various reasons, including the need for enhanced security requirements. GSA did not have any owned federal space available in its existing inventory to meet the specialized security needs of both agencies, so finding another location that met their security needs was a major factor in choosing the new space.

Funds for Ownership Are Limited

For GSA, limited funding for construction is exacerbated by federal budget scorekeeping rules which require, for ownership and capital leases, that the full cost of the government's commitment be recorded up front in the budget. In contrast, for operating leases, only the amount needed to cover yearly lease payments plus cancellation costs is required to be recorded in

the budget, thereby making operating leases “look cheaper” in any given year.²² This is a long-standing problem, and overreliance on leasing is one of the major reasons we designated federal real property management as a high-risk area. The budget scorekeeping issue and efforts to resolve it will be discussed at length later in this report.

GSA real property officials in the regions we visited told us that for most space requests they fulfill, constraints on capital funding influenced their pursuit of ownership as a realistic option. While several of the GSA officials we spoke with noted that construction funds are available for capital projects in their region, these dollars tend to be designated for the construction of agency headquarters, courthouses, and border stations and typically are not used for federal office space, such as that needed to fulfill FBI’s field office needs. Specifically, for fiscal years 2006 through 2008, the President requested funding for GSA primarily for courthouses or border stations, although for all 3 years GSA requested funds to cover other construction and repair and alteration projects. According to GSA real property officials, these types of constraints on construction funding for federal office space often limit their ability to pursue ownership for general purpose office space.

For this review, GSA developed and provided a 30-year net present-value analysis of leasing versus ownership for the building leases we selected. When proposing a lease, GSA no longer provides this type of analysis to Congress. According to GSA officials, until the submission of the fiscal year 1995 capital investment and leasing program, GSA included the results of a 30-year net present-value analysis of housing alternatives in lease prospectuses. Now, according to GSA officials, GSA instead performs a scoring analysis for all lease prospectuses. The scoring analysis, GSA officials said, includes an estimate of construction costs. Other estimated costs include those for the proposed asset’s design, management, and inspection and site acquisition. According to GSA, these combined estimates provide a total asset value based on cost that forms the basis for determining whether the proposal scores as a capital or an operating lease. GSA officials said GSA’s authorizing committees

²²For GSA operating leases, only the budget authority needed to cover the annual lease payment is required. According to scorekeeping guidelines, for funds that are self-insuring under existing authority, only the amount of budget authority needed to cover the annual lease payment is required to be scored. In November 2005, OMB clarified its requirements by stating that the only funds that are considered self-insuring are certain revolving funds in GSA.

requested that they provide this information with lease prospectuses in lieu of the 30-year net present value analysis.

Although USPS is self-financed and not dependent on appropriations or subject to the scorekeeping rules that apply to other federal agencies, USPS officials said that limited up-front capital to fund construction projects is also a hindrance to ownership. USPS's leasing guidance states that a lease-versus-purchase analysis is to be conducted when new construction leasing or the purchase of a building is the recommended building acquisition alternative. These lease-versus-purchase analyses consider the net present value and the return on investment of acquisition alternatives. The lease-versus-purchase analysis at USPS includes the purchase of a newly constructed building, but also can include the exercise of options available in certain lease contracts to purchase a currently leased building. USPS officials at the three facilities service offices we visited said major reductions in capital funding dictated many of their decisions about leasing and ownership. In particular, USPS headquarters officials stated that they would prefer to own all of the larger facilities, such as mail-processing facilities, but that capital constraints can prevent ownership of all such facilities.

Operational Considerations Also Drive Decisions to Lease

While GSA and USPS officials emphasized that the limited availability of capital was a major impediment to building ownership, they also cited operational requirements— such as changes to an agency's mission, immediate space needs, security requirements, or a desire for flexibility— as drivers of the decision to lease rather than own space. Other factors, such as shorter-term or smaller space needs, also may influence agencies' decisions to lease space. GSA and USPS officials cited agency mission as a reason they chose to pursue leasing rather than building ownership for certain projects. For instance, USPS officials said they strive to locate postal service buildings in areas that will optimize the efficiency of mail delivery. Thus, when deciding between leasing and constructing a building, they may consider operational factors such as the size of a facility, traffic routes, access to parking, and convenience for the customer. USPS officials noted, particularly for customer service post offices, that leasing in existing retail space, rather than constructing a new facility, is usually the optimal way to reach customers. However, as we have previously reported,²³ significant challenges remain related to USPS's

²³GAO, *High-Risk Series: An Update*, [GAO-07-310](#) (Washington, D.C.: Jan. 19, 2007).

planning and implementation of its infrastructure realignment, which is designed to reduce excess capacity as well as reflect changes in operations. Further challenges persist related to USPS's identification and disposal of excess property. We previously have recommended that USPS develop a facilities plan that includes a strategy for how USPS intends to rationalize the postal facilities network and remove excess processing capacity and space from the network.²⁴ In some instances, officials told us that operational requirements take precedence over economic considerations. For instance, automation at USPS has affected operational planning requirements for future facilities by changing the expected need for square footage. GSA officials also cited changes in a tenant agency's mission as dictating an immediate need for space. For instance, expanding mission requirements for the Department of Homeland Security created additional space requirements. Faced with a changing mission and relatively immediate space needs, agencies may opt for lease construction rather than federal construction, GSA officials told us, because lease construction is perceived to take less time than federal construction. Under lease construction, an agency works with the private sector to design and build a building that the government leases to meet the agency's mission needs. The private developer finances the construction of the building and agrees to lease the finished building to the agency. This arrangement allows an agency to obtain a new building suited to its needs without having to pay the up-front costs associated with federal construction. GSA officials said that it is highly challenging to determine when a tenant agency's mission may change and what space needs may subsequently emerge.

Both GSA and USPS cited the need for flexibility in their space assignments as a reason for leasing rather than owning space. Certain agencies that GSA obtains space for, such as the Social Security Administration, try to locate their facilities close to their customers. As demographic shifts occur in certain areas of the country, customers can potentially move to new areas. GSA real property officials stated that leasing rather than ownership is frequently used to give these agencies the flexibility to relocate closer to their customers, if necessary. Postal officials also cited flexibility as a reason for leasing retail post office space. According to Postal Service officials in the Southwest Facilities Service Office, recent population increases in Texas and Northwestern

²⁴GAO, *U.S. Postal Service: Bold Action Needed to Continue Progress on Postal Transformation*, [GAO-04-108T](#) (Washington, D.C.: Nov. 5, 2003).

Arkansas may expand the need for retail postal facilities in these areas. Because the majority of the space USPS obtains in the region is small and subject to demographic shifts, leasing provides flexibility to meet changing operational needs.

Security Considerations Can Lead to Leasing

Due to the expansion of security requirements in recent years, such as those for blast-resistant building exteriors and the need for greater setbacks, GSA officials said that agency requirements have become more stringent and complex. In some circumstances, GSA officials said, these security needs cannot be met in existing federal buildings, causing agencies to pursue lease construction. When acquiring space for the FBI field office in Chicago, GSA first pursued the option of repair and alteration and then building purchase. GSA officials said that after reviewing the federal inventory and investigating the site with the most potential, GSA determined that the repairs needed to make existing federal building space comply with post-September 11 security requirements would be cost prohibitive. Given the costliness of the repair and alteration method and the limited availability of capital for construction, GSA officials selected lease construction as the method to acquire a building for FBI. Similarly, when looking for new space to consolidate FBI operations in Tampa, GSA real estate specialists told us they eliminated downtown Tampa—where existing federal buildings were located—as a site because of the difficulty of locating space with the required 100-foot building setbacks. GSA did find, however, a private developer for a lease construction project away from the downtown area on the Western Shore of Tampa.

Leasing Can Meet Short-term Needs and Is Sometimes Practical

An additional factor that may cause agencies to lease space is a customer's temporary or short-term space needs. For instance, GSA officials said that over 200 GSA-owned and leased buildings were damaged by Hurricane Katrina, necessitating the relocation of 2,600 federal employees from 28 federal agencies, many of which were GSA tenant agencies. To meet this emergency need, GSA expanded its use of leases to house agencies in temporary space to fulfill a short-term need. GSA Regional officials told us they still have a number of Hurricane Katrina-related leases in their portfolio.

Agencies also choose leasing over ownership because it is a practical way to address issues such as a limited amount of available federal space in a geographic area or a need for a small amount of square footage. GSA officials stated that in certain rural locations, construction would not be

economically advantageous. The amount of square footage needed also may dictate whether an agency chooses to lease rather than own space. For instance, more than 80 percent of GSA's leases are for 20,000 square feet or less. When agencies require less than 20,000 square feet, GSA officials stated, leasing is usually cost-competitive with ownership, and federal construction is an unlikely option. Additionally, USPS officials told us that many of their assignments are for 3,000 square feet or less and that for assignments of this size, construction is not often practical.

Various Alternatives for Addressing the Leasing Challenge Have Been Debated, but No Action Has Been Taken to Resolve This Difficult Issue

The administration has made considerable progress in focusing on long-standing problems in the real property area such as poor data and excess property. The executive order on real property management, establishment of FRPC, and other related initiatives have given greater emphasis to improving real property management and bringing a more strategic focus to fixing the problems. However, the administration's efforts to address the leasing challenge have been limited. As mentioned previously, building ownership through construction or purchase is often the least expensive way to meet agencies' long-term requirements.²⁵ For operating leases, only the amount needed to cover yearly lease payments plus cancellation costs is required to be recorded in the annual budget, thereby making operating leases "look cheaper" in any given year even though they are generally more costly over time. We have raised this issue for almost 20 years in several reports and testimonies. For example, we have reported as follows:

"Efforts to increase ownership are ... hampered by a budgetary bias against capital investment. GSA must record in 1 year's budget the total cost of a newly constructed or purchased building, but is required to record only 1 year's lease payments for a leased building. As a result, leasing appears to be less costly for the current year despite its greater long-term costs" (December 1989, [GAO/GGD-90-11](#)).

"...consideration [should] be given to revisiting the scoring of operating leases. In principle, those leases that are perceived by all sides as long-term federal commitments ought to be scored in a way that is comparable to direct federal ownership. Applying the principle of full recognition of the long-term costs to all instruments is more likely to promote the emergence of the most cost-effective alternative" (October 1993, [GAO/T-AIMD-GGD-94-43](#)).

²⁵In assessing alternatives to address the leasing challenge, we did not focus on USPS, which is not subject to OMB guidance related to leasing.

“...GSA’s economic analysis for 55 ... leases it proposed showed that federal construction would have been a less costly alternative and would have saved approximately \$700 million (present value) over a 30-year period” (July 1995, [GAO/T-GGD-95-149](#)).

“...a GSA present value cost analysis estimated that the recently leased U.S. Patent and Trademark Office-complex currently being constructed in Alexandria, Virginia, by a private company, cost taxpayers about \$48 million more to lease over the 20-year lease period than it would have cost to purchase it” (April 2003, [GAO-03-609T](#)).

“Federal real property is a high-risk area due to excess and deteriorating property, reliance on costly leasing, unreliable data, and security challenges ... Energy, Interior, GSA, State, and VA reported an increased reliance on leasing to meet space needs” (April 2007, [GAO-07-349](#)).

A complete listing of these reports appears at the end of this report in the Related GAO Products section.

It is important to recognize in any discussion about the budget scorekeeping rules that their intended purpose is rooted in sound budget principles and transparency. For Congress to efficiently allocate resources, it needs to know and vote on the full cost of any program it approves at the time the funding decision is made. Hence, the scorekeeping rules require that budget authority for the cost of purchasing an asset—whether through construction or purchase—be recorded in the budget when it can be controlled, that is, up front, so that decision makers have the information needed and an incentive to take the full cost of their decisions into account. Under current budget scorekeeping rules, the budget records the full cost of the government’s commitment in the year the commitment is made. As a result, for operating leases, only the amount needed to cover the first year lease payments plus cancellation costs need to be recorded, thereby disguising the fact that over time, leasing will cost more than ownership.²⁶

²⁶An operating lease is a lease that meets the six criteria listed in the scorekeeping guidelines in OMB Circular A-11, app. A. Specifically, (1) ownership of the asset remains with the lessor during the term of the lease and is not transferred to the government at or shortly after the end of the lease term; (2) the lease does not contain a bargain-price purchase option; (3) the lease term does not exceed 75 percent of the estimated economic life of the asset; (4) the asset is a general purpose asset, it is not for a special purpose of the government, and it is not built to the unique specifications of the government lessee; (5) there is a private sector market for the asset; and (6) the present value of the minimum lease payments over the life of the lease does not exceed 90 percent of the fair market value of the asset at the beginning of the lease term.

Scoring Can Have an Effect on Public-Private Partnerships

In addition to encouraging the use of operating leases, the budget scorekeeping rules have a clear impact on public-private partnerships. One type of partnership that agencies such as the Department of Veterans Affairs and the Department of Defense have specific statutory authority to enter into is called an enhanced use lease agreement. Such an agreement is a lease agreement for property under an agency's control or custody that the agency can (1) enter into with a public or private entity and (2) receive as payment under the lease either cash or other consideration, such as repairs of the property. According to the Congressional Budget Office (CBO), in a public-private partnership, a business entity is created by public and private parties for a single, specified purpose with activities that are predetermined by the contracts and other arrangements between the parties involved.

The scoring of H.R. 3947, the Federal Property Asset Management Reform Act of 2002, illustrates how scoring has, and will continue to have, an impact on the prospects for greater use of public-private partnerships. The bill—which was not enacted—would have authorized most federal real-property-holding agencies, including GSA, to enter into partnerships and other business arrangements with private firms to improve the government's real property. Agencies could have sold, leased, or conveyed government property as part of the business arrangements and retained or spent the proceeds without further appropriations. CBO expected that many of the ventures that agencies would enter into would be used to finance investment on behalf of the government. Because of the extent of the government's control and use of the projects likely to be undertaken, CBO concluded that spending by the ventures associated with that financing should be treated as governmental and recorded as budget authority and outlays. CBO reported that spending would increase by \$1 billion between 2004 and 2012. CBO's report contains a full explanation of CBO's conclusions.²⁷

Alternatives to the Current Budget Scorekeeping Rules Have Been Proposed

Over the nearly 20 years that we have been raising the scorekeeping issue as a problem that needs to be addressed, several alternatives have been discussed by, for example, the President's Commission to Study Capital Budgeting and us. In addition to improving capital planning overall so that the most cost-effective capital investments can be identified, other

²⁷Congressional Budget Office, *The Budgetary Treatment of Leases and Public/Private Ventures* (Washington, D.C., February 2003).

Scoring Long-term Leases Up Front

alternatives have included scoring operating leases up front and establishing capital acquisition funds at agencies to fund ownership. Although these alternatives would pose various implementation challenges, they serve to illustrate proposals that have been considered.

An alternative that could result in long-term savings for the government, proposed in the past by us, would be to recognize that many operating leases are used for long-term needs and should be treated on the same basis as ownership. This would make such instruments comparable in the budget to direct federal ownership and would foster more cost-effective decision making by OMB and Congress. Applying the principle of full, up-front recognition of the long-term costs to all options for satisfying long-term space needs—whether through construction, purchase, lease-purchase, or operating lease—is more likely to result in the selection of the most cost-effective alternative than using the current scoring rules. It is important to note that there would be implementation challenges if this option were pursued. Additionally, it would be challenging to reach consensus on what constitutes long-term space needs that would warrant this up-front budgetary treatment.

In commenting on various options for correcting the scoring issue, CBO reported that ending the distinction between various types of leases has been considered in the private sector. According to CBO, the Financial Accounting Standards Board—noting that private firms often devise leases that barely fall within the limits for operating leases—has considered requiring firms to capitalize all leases in their books, rather than maintain the current distinction between capital leases and operating leases. In the context of federal budgeting, CBO reported that capitalizing all leases could mean scoring all leases up front on the basis of the present value of lease payments over the lease term, without attempting to distinguish between leases that are equivalent to purchases—capital leases—and those that are not—operating leases.

Establishing Capital Acquisition Funds to Pursue More Ownership

The President's Commission to Study Capital Budgeting recommended in 1999 that Congress and the executive branch have one or more agencies with capital-intensive operations establish a separate capital acquisition fund (CAF) within their budget that would receive appropriations for the construction and acquisition of large capital projects.²⁸ CAFs would use

²⁸President's Commission to Study Capital Budgeting, *Report of the President's Commission to Study Capital Budgeting* (Washington, D.C., February 1999).

authority to borrow from Treasury's general fund and then charge operating units within the agency rents equal to the debt service (interest and amortization costs) on those projects. Although the Commission's discussion of CAFs was within the context of identifying measures short of capital budgeting that the government could adopt, CAFs have implications for the scoring issue because they represent a vehicle for providing up-front funding for ownership. The main advantage of CAFs, according to the Commission, is that they should improve agencies' planning and budgeting. If units or divisions within agencies are charged the true costs of their space and of other large capital items, they are likely to make more efficient uses of those assets, according to the Commission report. The report said that CAFs would not replace the Federal Buildings Fund, GSA's governmentwide revolving fund. Authority to acquire buildings through CAFs could be delegated by GSA as agencies demonstrate their effectiveness in using this instrument. In 2005, we reported that implementation issues could overwhelm the potential benefits of CAFs, which could be achieved through simpler means.²⁹

Real Property Initiative Has Not Yet Addressed the Leasing Challenge

In our April 2007 report updating our designation of federal real property as a high-risk area, we recommended that OMB, in conjunction with FRPC, develop an action plan for how FRPC will address key problems, including the continued reliance on costly leasing when ownership would be more cost-effective over the long term. OMB agreed with our recommendation and developed an action plan that included, as a priority action, "analyz[ing] real property budget scoring issues." OMB staff added that in their view, basic improvements, such as developing a reliable, governmentwide inventory of space and establishing performance measures had to occur before the administration could take on broader, complex policy issues such as how to address the leasing challenge. As a result, the current real property reform initiative has lacked a comprehensive analysis of alternatives and potential solutions to the leasing challenge. Without such an analysis, agencies' reliance on costly leasing is likely to continue and opportunities for using other instruments, such as public-private partnerships, may be limited. OMB staff said that efforts to resolve the leasing challenge could benefit from the input not only of FRPC, but also of other outside stakeholders, including Congress. At a minimum, consensus on resolving this difficult issue would involve

²⁹GAO, *Capital Financing: Potential Benefits of Capital Acquisition Funds Can Be Achieved through Simpler Means*, [GAO-05-249](#) (Washington, D.C.: Apr. 8, 2005).

analyzing current and past legislative and administration proposals that address the budget scorekeeping issue in relation to real property, gauging stakeholders' perspectives on what proposals are most viable, and determining the conditions under which leasing is an acceptable alternative even if it is not the most cost-effective option.

Conclusions

The leasing challenge—under which agencies have become overreliant on costly operating leases to meet long-term space needs—has persisted for many years. We have reported since the late 1980s that this problem has cost taxpayers hundreds of millions of dollars and needs to be addressed. Overreliance on costly leasing was, and continues to be, a major reason why real property management is on GAO's high-risk list. Trends show continued reliance on significant amounts of leased space. In particular, GSA predicts that in 2008 it will lease more space than it owns—an unprecedented situation. The predilection for leasing has been driven, in part, by federal budget scorekeeping rules, which make operating leases an attractive alternative to ownership. The scorekeeping rules, though rooted in sound budget policy and intended to improve transparency, have had this undesirable effect. Various alternatives have been proposed to remedy the problem, but it persists, and reaching a resolution will not be easy. Whatever change is under consideration—whether it involves scoring leases up front like ownership or using other methods to spur ownership—will involve making choices among competing priorities for limited federal resources. Whether to increase funding for federal real property at the expense of other programs and initiatives is properly a policy decision that only Congress and the President can make. Nonetheless, with the improvements in federal real property management made thus far and increased commitment by OMB and Congress to address long-standing real property problems, there is reason to be optimistic that stakeholders can reach a consensus on how to address the leasing challenge.

Recommendation for Executive Action

The Director of the Office of Management and Budget should direct the Deputy Director for Management, Office of Management and Budget, in conjunction with the Federal Real Property Council and in consultation with key stakeholders including Congress, to develop a strategy to reduce agencies' reliance on leased space for long-term needs when ownership would be less costly. The strategy should, at a minimum, analyze current and past legislative and administration proposals that addressed the budget scorekeeping issue in relation to real property, gauge stakeholders' perspectives on what proposals are most viable, and identify the

conditions, if any, under which leasing is an acceptable alternative even if it is not the most cost-effective option.

Agency Comments and Our Evaluation

We provided a draft of this report to OMB, GSA, Agriculture, and USPS for review and comment. OMB generally agreed with the report and concurred with our recommendation. OMB also provided technical clarifications, which we incorporated, where appropriate. OMB's comments are discussed in more detail below. OMB's letter is contained in appendix II. GSA also agreed with the report and provided technical clarifications, which we incorporated where appropriate. GSA's letter appears in appendix III without the enclosure that contained the technical clarifications. USPS and Agriculture did not provide comments on the draft report.

While generally agreeing with our report and recommendation, OMB asked us to narrow the scope of the recommendation and identified other issues inherent to the acquisition of leased space, including (1) leasing as a more practical option in certain situations, (2) the validity of the 30-year net economic analysis comparing the acquisition costs of owned and leased space, and (3) challenges associated with pursuing building ownership. OMB asked us to narrow the scope of the recommendation to identify instances in which agencies are relying on costly, long-term leasing. A means of identifying such leases could logically be part of the strategy we are recommending and seems worthwhile pursuing. However, our report objectives did not include how best to identify costly leases, and therefore we chose not to change our recommendation. Over the last decade, our work has shown that GSA relies heavily on operating leases to meet new long-term space needs and that building ownership often costs less than operating leases, especially for long-term space needs. In these reports, we cite examples of leases that were estimated to cost millions of dollars more than construction over the long-term, including operating leases for the Patent and Trademark Office in Northern Virginia and the Department of Transportation's headquarters building and the Securities and Exchange Commission building in Washington, D.C. In this report, we identify examples in which the comparative cost advantage of building ownership would result in significant financial savings over the long term, including the FBI field office buildings in Chicago, Illinois, and Tampa, Florida (see table 2). Also, OMB said that we carefully selected long-term lease arrangements in our report. Our report methodology clearly indicates that we chose GSA's regional offices in Atlanta, Georgia; Chicago, Illinois; and Fort Worth, Texas; and USPS facility service offices in Lawrenceville, Georgia; Bloomingdale, Illinois; and Dallas, Texas,

because these locations had a high number of larger-dollar-value leases and were geographically diverse.

OMB said that our report recognizes 80 percent of GSA's leases are for 20,000 square feet or less. OMB also said that when there is general purpose office space available in a competitive marketplace, leasing may be a more viable option. Our report acknowledges that leasing is a practical way to address issues such as a limited amount of available federal space in a geographic area or a need for a small amount of square footage. In addition, we cite operational requirements— such as changes to an agency's mission, immediate space needs, security requirements, or a desire for flexibility—as drivers of the decision to lease rather than own space. OMB said that the 30-year economic comparison of leasing to ownership will almost always show that ownership is more cost-effective than leasing, especially when including land values, and that the federal government may not recoup the value the 30-year comparison suggests. We believe that the 30-year net present-value analysis, which GSA has used for decades and that measures multiyear cash flows in present-dollar terms so the value of a dollar received today can be compared against the value of a dollar received in the future, remains a valid measure for evaluating long-term costs of leasing versus building ownership. Finally, OMB states that in instances where there is a long-term need or if there is a need for a special purpose facility not readily available in the leasing market, that acquisition is an appropriate strategy and that agencies should budget accordingly. Our report discusses at length GSA's and USPS's concerns that they lack the up-front capital to pursue building ownership for facilities. For example, GSA officials we spoke with in the field said that construction funds are available for capital projects in their region but these dollars tend to be designated for the construction of agency headquarters, courthouses, and border stations and typically are not used for federal office space, such as that needed to fulfill FBI's field office needs.

As agreed with your offices, unless you publicly announce the contents of this report earlier, we plan no further distribution until 30 days from the report date. At that time, we will send copies of this report to the Director and Deputy Director of OMB, the Administrator of GSA, and the Postmaster General of the United States. Additional copies will be sent to interested congressional committees. We also will make copies available to others upon request, and the report will be available at no charge on the GAO Web site at <http://www.gao.gov>.

If you have any questions about this report, please contact me at (202) 512-2834 or at goldsteinm@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report. GAO staff who made key contributions to this report are listed in appendix IV.

A handwritten signature in black ink, appearing to read 'Mark L. Goldstein', with a long horizontal flourish extending to the right.

Mark L. Goldstein
Director, Physical Infrastructure Issues

Appendix I: Objectives, Scope, and Methodology

Our objectives were to identify (1) the profile of domestically held, federally leased space, including the overall amount and type of space agencies lease, and discuss any related trends; (2) the factors that drive agencies to lease space that may be more cost-effective to own; and (3) the actions, if any, the administration has taken, and what alternative approaches have been proposed, to address agencies' reliance on costly leased space.

To identify the profile of domestically held, federally leased space, we examined the Federal Real Property Profile (FRPP), the government's real property database, and federal fiscal year 2006 leasing data and obtained breakouts of leased building space by federal agency and predominant usage. FRPP is maintained by the General Services Administration (GSA) on behalf of the Federal Real Property Council, which controls access to the data. We eliminated federal agencies from consideration that lease their building space overseas. We identified three civilian real-property-holding agencies that are the largest in terms of leased building space held within the United States and U.S. territories for a more detailed analysis and assessment of FRPP data. These agencies are GSA, the U.S. Postal Service (USPS), and the U.S. Department of Agriculture (Agriculture), which collectively hold 71 percent of domestic, federally leased space. We analyzed GSA's, USPS's, and Agriculture's fiscal year 2006 FRPP leasing data, including the data for elements such as real property type, use, legal interest, status, reporting agency, using organization, size, rate of utilization, value, condition index, mission dependency, annual operating and maintenance costs, and general location. To analyze the major trends in leased space, we were not able to use FRPP, since fiscal year 2005 was the first year federal agencies were required to submit information on their leased real property assets to FRPP. Therefore, we reviewed annually archived GSA leasing data for fiscal years 2003 through 2006, including analyses of certain aspects of the leased portfolio such as vacancy rates in leased buildings, lease extensions, and leases that are operating at a negative net operating income. Because GSA leases a variety of different space types for many government agencies, its leased portfolio provides a governmentwide perspective on federally leased building space. Issues related to collection techniques and availability precluded USPS and Agriculture from providing us with an electronic copy of annually archived leasing data, and therefore we could not include information from these agencies in our analysis of trends under this objective. We also reviewed GSA's System for Tracking and Administering Real Property and GSA-generated reports on real property, including the State of the Portfolio and the Lease Portfolio Reports. We assessed the reliability of the leasing data provided by the Office of Management and Budget (OMB) and GSA and

interviewed OMB officials because OMB oversees the implementation of Executive Order 13327, which addresses real property management and FRPP. We determined that these data were sufficiently reliable and valid for the purposes of this review.

To determine the factors that drive agencies to lease building space that may be more cost-effective to own, we focused on GSA and USPS, the two agencies that lease the most building space. To determine the major factors that guide these decisions, we interviewed GSA and USPS headquarters and regional officials with authority over leasing building space. In addition, we visited GSA regional offices and USPS facility service offices that are either in the same metropolitan area or near to it. We visited GSA regional offices in Atlanta, Georgia; Chicago, Illinois; and Fort Worth, Texas; and USPS facility service offices in Lawrenceville, Georgia; Bloomington, Illinois; and Dallas, Texas. We selected these locations because they had space leased to multiple agencies and a high number of larger-dollar-value leases and were geographically diverse. The leases we selected were among the larger-dollar-value leases within these locations. To determine the cost of leasing versus the cost of new construction ownership, we selected seven GSA and three USPS building leases. For GSA buildings, we used GSA economic analyses we requested that compared the estimated costs of leasing with the estimated costs of ownership, while for USPS buildings, we reviewed analyses previously prepared by USPS officials comparing these estimated costs. For GSA properties, we worked with budget allocation specialists from GSA's real property division to estimate the costs of leasing versus ownership over a 30-year period. We developed this estimate through a net present value analysis of both leasing and purchasing using GSA's The Automated Prospectus System (TAPS). To estimate leasing costs, we used data from the selected leases for each of the sample buildings, such as usable square footage, tenant alteration costs, services and utilities, and lease terms. If this information could not be located on a particular GSA lease, TAPS program defaults were used. Certain rental rates, such as "step rents" that increase over a period of years, were adjusted to present-value terms, as appropriate. To estimate the costs of new construction ownership, we used cost data from GSA's General Construction Cost Review Guide (for estimated construction costs), commercial real estate data from CoStar (for estimated land costs), and the Public Building Service's Design and Construction Professional Services Budget Estimating Tool (for estimated design and review and management and inspection costs). All inputs for both estimated leasing and ownership costs were adjusted to 2005 dollars using OMB inflation and interest rate data and certain TAPS program defaults from that year. We selected 2005 as the base year because it was

the most recent year for which the General Construction Cost Review Guide contained updated actual construction data, rather than estimates. After estimating the costs of both leasing and ownership, we compared these amounts to determine which method of financing would have greater financial savings over the long term. Our findings from visits to, and economic analyses of, federally leased space cannot be generalized to federally leased space nationwide.

To assess the actions, if any, the administration has taken, and what alternative approaches have been proposed, to address agencies' reliance on costly leased space, we reviewed previously issued GAO reports on real property management and leasing. We also reviewed past proposals for reforming federal leasing policy, including reports by the President's Commission to Study Capital Budgeting and by the Congressional Budget Office on budget scoring. We also interviewed OMB officials about efforts to address agencies' reliance on leasing as part of ongoing reform efforts. We conducted this performance audit from July 2006 to January 2008 in accordance with generally accepted government auditing standards. 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 objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Appendix II: Comments from the Office of Management and Budget



EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D. C. 20503

11/2008

Mr. Mark Goldstein
Director, Physical Infrastructure
U.S. Government Accountability Office
440 G Street, NW
Washington, DC 20548

Dear Mr. Goldstein:

Thank you for the opportunity to comment on the Government Accountability Office's (GAO's) draft report entitled "Federal Real Property: Strategy Needed to Address Agencies Long-standing Reliance on Costly Leasing" GAO-08-197. In general, the Office of Management and Budget (OMB) agrees with your assessment of the need for a strategy to optimize agencies' use of and spending on leased space. We recommend that GAO narrow the scope of the recommendation to more specifically address how to identify those instances where agencies are relying on costly leasing. As GAO recognized in its report, the Federal government has built a strong foundation for right-sizing the government's real property inventory since the President signed Executive Order (EO) 13327, Federal Real Property Management. Central to this foundation has been developing the tools to better manage this inventory. Since the President signed the EO:

1. all agencies established Asset Management Plans addressing acquisition, operations and maintenance, and disposition of their real property assets;
2. the Federal Real Property Council (FRPC) established a standard taxonomy and identified 24 data elements, including four performance measures, that are captured on all assets in the Federal portfolio;
3. all agencies, for the third consecutive year, reported the required constructed asset level inventory and performance data to the Federal Real Property Profile; and
4. agencies have reliable performance information to assist them in identifying underperforming assets suitable for investment or disposition.

As a direct result of these accomplishments, we know what assets we own, their location, and how they are performing. This has led to the disposal of over \$7 billion in unneeded assets since 2004. Congress also recently introduced legislation to further reform real property disposal by providing agencies needed authorities to expedite the disposal, through sale or demolition, of unneeded assets.

Now that new tools for improved asset management are in place, OMB, the FRPC, and the Congress are better prepared to address more complex policy issues such as the leasing challenges raised in this report. Our plan is to separate our analysis and effort in two distinct

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pieces. First, we will identify opportunities to improve the management of existing leases, including opportunities to optimize the leases the government currently manages. Then, we will analyze prospects for improving the acquisition of new leases.

As we perform our review, we will keep in mind a number of factors that we believe should influence the decision as to whether the Government should own or lease space. GAO's report, which is based on a review of several carefully selected long term lease arrangements, suggests that the Government is overly reliant on long-term leasing to its financial detriment. We believe there are broader considerations in evaluating the Federal government's approach to leasing that are not addressed in your report. Specifically:

- As your report recognizes, 80 percent of GSA's leases are for 20,000 square feet or less. In cases where the space needs are relatively small in scale, the economic analysis more typically points to a lease arrangement as the most practical or viable option. Therefore, for a significant percentage of GSA's lease inventory, the leasing alternative is a sensible option.
- A 30-year economic comparison of leasing to ownership will almost always show that ownership is more cost effective than leasing due to the residual value of appreciated land values. However, agencies' needs are not static: they need to grow, decline and move operations to better meet their needs. Leasing affords agencies the flexibility to adapt to changing requirements. Such flexibility is not contemplated in a 30-year comparison where value is derived from ownership.
- Further, productive ownership depends upon the owners' ability to dispose of the asset when requirements change or better economic options are available. As GAO has noted, the Federal Government faces challenges in disposing of assets. While we are making strides in improving the management of the owned inventory, historical experience suggests that there can be additional costs that may not included in the owned to leased comparison. In an ownership scenario, the Federal Government may not ultimately recoup the value that a 30-year comparison suggests.
- Ownership also requires periodic investment to maintain physical infrastructure. Agencies and Congress often defer needed maintenance to fund other needs, resulting in facilities that require greater repair and renovation costs than would have been needed if properly maintained. As an alternative, leasing can offer a consistent level of service.
- Government ownership is advantageous in cases where there is a Government need for facilities that are not available on the leasing market. However, if general purpose office space is available in a competitive marketplace, leasing is typically a cost effective option.
- Finally, the budget scorekeeping rules referred to in the draft report are modeled on the Financial Accounting Standards Boards' standards for operating and capital leases. They are designed to ensure that capital leases and purchase options are treated the same way. The scoring rules encourage agencies to seek the lower cost option when acquiring

**Appendix II: Comments from the Office of
Management and Budget**

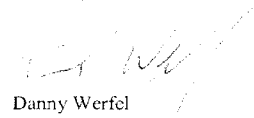
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space by requiring the full cost of capital leases to be scored upfront in the same manner as purchase and construction.

We agree with GAO that there are some instances where the Government should have pursued ownership rather than leasing an asset. However, the assumption should not be made that the information available today was known at the time the leasing decision was made. In instances where there is a long term need or there is a need for a special purpose facility that is not readily available in the leasing market, we believe that acquisition is an appropriate strategy and that agencies should budget accordingly. We believe GAO, along with the Executive branch, would be well served to consider how to identify instances where operating leases are most likely to be misused to the Government's financial detriment.

We are continuing our work to ensure that government-wide efforts will ultimately lead to improved asset management and the removal of Federal real property management from the GAO High Risk list. We want to thank GAO for the opportunity to comment on this draft report and we look forward to our continuing work in the area of improving Federal Real Property Asset Management.

Sincerely,



Danny Werfel
Acting Controller

Appendix III: Comments from the General Services Administration



GSA Administrator

January 7, 2008

The Honorable David M. Walker
Comptroller General of the United States
Government Accountability Office
Washington, DC 20548

Dear Mr. Walker:

The U.S. General Services Administration (GSA) appreciates the opportunity to review and comment on the U.S. Government Accountability Office's (GAO) draft report, "Federal Real Property: Strategy Needed to Address Agencies' Long-standing Reliance on Costly Leasing," (GAO-08-197). GAO recommends that the U.S. Office of Management and Budget (OMB), in conjunction with the Federal Real Property Council, consult with key stakeholders and Congress and develop a strategy to reduce agencies' reliance on leased space for long-term needs when ownership would be less costly.

GSA agrees with GAO's findings and recommendation, and, as appropriate, we will work with OMB and the Federal Real Property Council to support real property reform efforts. We have enclosed technical comments that update and clarify statements in the draft report.

If you would like to discuss the contents of this letter further, or if you have any additional questions or concerns, please do not hesitate to contact me. Staff inquiries may be directed to Mr. Kevin Messner, Associate Administrator, Office of Congressional and Intergovernmental Affairs, at (202) 501-0563.

Cordially,

A handwritten signature in black ink, appearing to read "Lurita Doan".

Lurita Doan
Administrator

Enclosure

cc: Mark L. Goldstein, Director, Physical Infrastructure

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1215 L Street, NW
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Appendix IV: GAO Contact and Staff Acknowledgments

GAO Contact

Mark Goldstein, (202) 512-2834 or goldsteinm@gao.gov

Staff Acknowledgments

In addition to the contact person named above, Elizabeth Repko, Susan Michal-Smith, David Sausville, Gary Stofko, and Adam Yu also made key contributions to this report.

Related GAO Products

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