

April 2006

# MILITARY HOUSING

## Management Issues Require Attention as the Privatization Program Matures



G A O

Accountability \* Integrity \* Reliability



Highlights of [GAO-06-438](#), a report to congressional committees

## Why GAO Did This Study

The Department of Defense (DOD) intends to privatize about 87 percent of the military-owned housing in the United States by 2010. As of December 2005, it had awarded 52 projects to privatize over 112,000 family housing units and had plans to award 57 more projects to privatize over 76,000 more units over the next 4 years. The program, begun in 1996, has become DOD's primary means to improve family housing and to meet its housing needs when communities near installations do not have enough suitable, affordable housing.

Because of expressed interest related to the oversight responsibilities of several committees, GAO assessed (1) whether opportunities exist to improve DOD's oversight of awarded housing privatization projects, and (2) to what extent projects are meeting occupancy expectations.

## What GAO Recommends

GAO recommends that DOD take five actions to improve the oversight of awarded housing privatization projects. In commenting on a draft of this report, DOD generally agreed with our recommendations.

[www.gao.gov/cgi-bin/getrpt?GAO-06-438](http://www.gao.gov/cgi-bin/getrpt?GAO-06-438).

To view the full product, including the scope and methodology, click on the link above. For more information, contact Barry W. Holman at (202) 512-5581 or [holmanb@gao.gov](mailto:holmanb@gao.gov).

# MILITARY HOUSING

## Management Issues Require Attention as the Privatization Program Matures

### What GAO Found

Although DOD and the individual services have implemented program oversight policies and procedures to monitor the execution and performance of awarded privatized housing projects, GAO identified three opportunities for improvement. First, the Navy's methods for overseeing its awarded projects have not been adequate to identify and address operational concerns in some projects or to ensure accurate reporting of project information. As a result, there is less assurance that Navy management could become aware of project performance issues in a timely manner in order to plan needed actions to mitigate the concerns. For example, contrary to project agreements, funds from one project had not been deposited to a Navy reserve account to provide for future project needs, and the Navy had not been reimbursed for police and fire protection services provided to another project. Compared to the Navy, the Army and Air Force had more robust and comprehensive methods for overseeing awarded projects and GAO did not find similar oversight concerns in the Army and Air Force projects it reviewed. Second, the value of DOD's primary oversight tool—the semiannual privatization program evaluation report—has been limited because the report lacks a focus on key project performance metrics to help highlight any operational or financial concerns, has not been issued in a timely manner, and does not ensure data accuracy by requiring periodic independent verification of key report elements. Third, data collected on servicemember satisfaction with housing, which is important for benchmarking and tracking of satisfaction levels over time as well as for making service-to-service comparisons, are inconsistent and incomplete because DOD has not issued guidance to the services for standardized collection and reporting of satisfaction information for all servicemembers.

Sixteen, or 36 percent, of 44 awarded privatization projects had occupancy rates below expectations with rates below 90 percent, as of September 30, 2005. In an attempt to increase occupancy and keep rental revenues up, 20 projects had begun renting housing units to parties other than military families, including 2,077 units rented to single or unaccompanied servicemembers, retired military personnel, civilians and contractors who work for DOD, and civilians from the general public. Still, rental revenues in some projects are not meeting planned levels, resulting in signs of financial stress. If lower than expected occupancy and rental revenues continue in the long term, the result could be significantly reduced funds available to provide for future project needs and renovations or, in the worst case, project financial failures. Factors contributing to occupancy challenges include increased housing allowances, which have made it possible for more military families to live off base thus reducing the need for privatized housing, and the questionable reliability of DOD's housing requirements determination process, which could result in overstating the need for privatized housing. DOD has yet to implement some previous GAO recommendations to improve the reliability of the requirements assessments supporting proposed projects.

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April 28, 2006

### Congressional Committees

The Department of Defense (DOD) intends to privatize about 87 percent of the military-owned housing in the United States by 2010. Since the enactment of the National Defense Authorization Act for Fiscal Year 1996, which provides for private-sector financing, ownership, operation, and maintenance of military housing,<sup>1</sup> privatization has become DOD's primary means for improving family housing and meeting requirements when the communities near installations do not have an adequate supply of suitable, affordable housing. Similar to servicemembers who live in the local community, servicemembers who choose to live in privatized housing receive a housing allowance that they use to pay rent and utilities. According to DOD officials, the purpose of the housing privatization program is to help improve servicemember quality of life by improving the condition of military-owned housing faster and more economically than would be achieved by the use of traditional military construction funding. By the end of December 2005, the services had awarded 52 projects to privatize over 112,000 family housing units and had plans to award 57 more projects to privatize over 76,000 more units over the next 4 years.<sup>2</sup> According to DOD, the 52 awarded projects will provide about \$13.9 billion in housing improvements, with private-sector developers and lenders providing about \$12.9 billion, or about 92 percent of the financing, and DOD providing the balance.

This report represents a continuation of our long-standing reviews of issues related to housing privatization. We initiated this engagement under the authority of the Comptroller General of the United States, and the report is addressed to you because of expressed interest related to your committees' oversight responsibilities. This report determines (1) whether opportunities exist to improve DOD's oversight of awarded housing privatization projects, and (2) to what extent awarded projects are meeting occupancy expectations.

<sup>1</sup>National Defense Authorization Act for Fiscal Year 1996, Pub. L. No. 104-106, § 2801-2841 (1996).

<sup>2</sup>This report does not include two Navy projects approved under a prior legislative authority which gave only the Navy authority to test the use of limited partnerships in order to meet the housing requirements of naval personnel and their dependents (Pub. L. No. 103-337, § 2803 (1994)).

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To address these issues, we summarized program implementation status and costs, compared the status to DOD's goals and milestones, and discussed issues affecting program implementation with DOD and service officials. In doing so, we relied on program status data provided by DOD and the services. We confirmed the status data for 12 projects, but we did not otherwise test the reliability of the data. We visited installations where 12 projects were underway to review actual project performance and to determine whether performance information and concerns were adequately captured and reported to top management in a timely manner. The installations were chosen because they contained established privatization projects, represented each of the military services, and in some cases had reported occupancy challenges. We compared occupancy rates in awarded projects with occupancy expectations; and, for the 12 projects at the installations we visited, we explored the causes, consequences, and service response when occupancy levels were below expectations. We also examined and compared DOD's and the services' policies, guidance, and procedures for overseeing awarded privatization projects. We conducted our work from July 2005 through February 2006 in accordance with generally accepted government auditing standards. A more detailed description of our scope and methodology is included in appendix I.

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## Results in Brief

Although DOD and the individual services have implemented program oversight policies and procedures to monitor the execution and performance of awarded privatized housing projects, opportunities exist for improvement. Though owned and managed by the private sector, adequate oversight of privatized housing is essential to help monitor and safeguard the government's interests and to help ensure the long-term success of the housing privatization program, and its importance has become even greater as the number of housing privatization projects has increased. We identified three areas of concern—the adequacy of the Navy's oversight methods, the usefulness of DOD's primary oversight report, and the consistency of tenant satisfaction data—which offer opportunities for enhancing the oversight of awarded privatization projects.

- The Navy's methods for overseeing its awarded projects have not been adequate to identify and address operational concerns in some projects or to ensure accurate reporting of project information. As a result, there is less assurance that Navy management could become aware of project performance issues in a timely manner in order to plan needed actions

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to mitigate the concerns. For example, we found that funds earmarked for future project needs at one project had not been deposited to a Navy reserve account and the Navy had not been reimbursed for the cost of police and fire protection services provided to another project, as specified in a project memorandum. Also, status information for five of the eight Navy and Marine Corps projects we reviewed was inaccurately reported to DOD headquarters management. Compared to the Navy, the Army and Air Force had more robust and comprehensive methods for overseeing awarded projects and we did not find similar oversight concerns in the Army and Air Force projects we reviewed. Navy officials stated that they recognized the need for improvements to their oversight methods. As such, they informed us that they have begun a review to upgrade their monitoring and oversight process to ensure consistency and completeness, and the Navy says it has taken steps to address the concerns identified at the projects we visited. However, until improvements are implemented, the adequacy of the Navy's oversight will continue to be questionable.

- Although primary responsibility for overseeing awarded privatization projects rests with the individual services, opportunities exist to improve oversight at DOD headquarters by enhancing the value of DOD's primary oversight tool—the semiannual privatization program evaluation report. The report consists of information submitted by the services on each awarded project and includes data on project contract structure, construction progress, occupancy, financial performance, and tenant satisfaction. However, the value of the report as an oversight tool has been limited because the report (1) lacks a focus on key project performance metrics to help highlight any operational or financial concerns, (2) has not been issued in a timely manner, and (3) does not ensure data accuracy by requiring periodic independent verification of key report elements.
- Improving the consistency of data collected on servicemember satisfaction with privatized housing offers another opportunity to improve program oversight. Because the overall goal of the privatization program is to improve servicemember quality of life by improving the condition of military housing, DOD requires the services to report data on servicemember satisfaction with privatized housing as an indicator of program success. However, because DOD has not issued guidance for accomplishing this task, the services have used inconsistent methods for collecting housing satisfaction data. As a result, value of the data could be improved for assessments of satisfaction levels over time,

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comparisons of satisfaction levels among projects, and identification of trends among the services. Further, because housing satisfaction information is not routinely collected on servicemembers who do not live in privatized housing, DOD lacks complete information on the impact of its overall housing program on servicemember quality of life.

Sixteen, or 36 percent, of 44 awarded privatization projects had occupancy rates below expectations with rates below 90 percent, as of September 30, 2005.<sup>3</sup> Specifically, occupancy was below expectations and below 90 percent in 6 of the Army's 19 awarded projects, 4 of the Navy's and Marine Corps' 13 awarded projects, and 6 of the Air Force's 12 awarded projects. Although the projects were originally justified on the basis of meeting the needs of military families, some projects had begun renting housing units to parties other than military families in an attempt to increase occupancy and keep rental revenues up. For example, 20 projects had rented 1,116 units to servicemembers who were single or unaccompanied by their families; 662 units to retired military personnel, and civilians and contractors who work for DOD; and 299 units to civilians from the general public. At one Air Force project, only 29 percent of the available privatized housing units was rented to military families. Still, rental revenues in some projects are not meeting planned levels, resulting in signs of financial stress. If lower than expected occupancy and rental revenues persist in the long term, the result could be significantly reduced funds available to provide for future project needs and renovations or, in the worst case, project financial failures.<sup>4</sup> Factors contributing to the occupancy challenges in some projects include increased housing allowances, which have made it possible for more military families to live off base, thus

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<sup>3</sup>According to service officials, the expected occupancy rate during a project's initial development period, when many housing units are being constructed or undergoing renovation, is usually around 90 percent of the units available for rent. After completion of the initial development period, most projects expect occupancy rates of about 95 percent. Three of the 16 projects had completed the initial development period. Also, our analysis excluded 7 projects awarded as of September 30, 2005, because 6 had been privatized for less than 2 months and 1 project had no units yet available for rent. Of the 44 projects included in our analysis, 6 additional projects were not meeting occupancy expectations but had occupancy rates of 90 percent or more.

<sup>4</sup>According to DOD officials, because privatization projects are privately owned, it is a project's developer and private lender—not the government—who would bear most of the consequences from a project financial failure. Still, DOD has an interest in each project's financial success because it has made investments in each project and, according to DOD officials, the military's housing objectives can be met only if the projects remain viable over the long term.



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reducing the need for privatized housing, and the questionable reliability of DOD's housing requirements determination process, which could result in overstating the need for privatized housing. To help ensure that the size of housing projects is accurately determined, we previously reported that DOD needed to study how increased housing allowances might affect future housing needs.<sup>5</sup> Also, we previously reported that changes were needed to improve the reliability of DOD's housing requirements process and to ensure maximum reliance on local community housing, as required by DOD policy.<sup>6</sup> Because DOD has yet to implement these steps, the planned size of future privatization projects may not be based on reliable assessments, which could result in overstated requirements and thus contribute to occupancy and financial challenges in some future projects.

We are making five recommendations to improve the oversight of awarded housing privatization projects and to help ensure that the size of future projects is reliably determined. Specifically, we are recommending that DOD require the Navy to upgrade its oversight of awarded projects, improve the department's semiannual evaluation report, provide guidance to help ensure consistent collection and reporting of housing satisfaction information for all servicemembers, determine how increased housing allowances will most likely impact future housing requirements, and expedite issuance of guidance to improve the reliability of housing requirements assessments. In written comments on a draft of this report, DOD fully agreed with three and partially agreed with two of our recommendations and stated that shortcomings identified in our draft would be addressed. We discuss DOD's comments in detail later in this report.

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## Background

In the mid-1990s, DOD became concerned that inadequate housing allowances and poor quality military housing were negatively affecting quality of life and readiness by contributing to servicemember decisions to leave military service. DOD noted that when living in private-sector housing in the local communities, servicemembers were paying about 19 percent of housing costs out of pocket, because housing allowances were

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<sup>5</sup>GAO, *Military Housing: Management Improvements Needed As the Pace of Privatization Quickens*, GAO-02-624 (Washington, D.C.: June 21, 2002).

<sup>6</sup>GAO, *Military Housing: Further Improvement Needed in Requirements Determinations and Program Review*, GAO-04-556 (Washington, D.C.: May 19, 2004).

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inadequate. DOD also noted that the quality of military-owned housing had been in decline for more than 30 years because military-owned housing was not considered a priority and because earlier attempts at solutions ran into regulatory or legislative roadblocks. DOD officials stated that much of the military-owned family housing in the United States was old, lacked modern amenities, and required renovation or replacement. DOD estimated that completing this work with historical funding levels and traditional military construction methods would take more than 20 years and cost about \$16 billion.

In response, and with the approval of Congress, DOD began two major initiatives. First, DOD began an initiative to increase housing allowances to cover the average cost of housing and utilities in each of the nation's various geographic areas, thus eliminating the average out-of-pocket housing costs paid by servicemembers. This initiative was completed at the beginning of calendar year 2005. Second, DOD began an initiative to privatize most military-owned housing to use private capital and construction expertise to replace or renovate inadequate housing faster than could be achieved using traditional funding methods at historical funding levels. At DOD's request, Congress enacted legislation in 1996 authorizing the Military Housing Privatization Initiative to allow private-sector financing, ownership, operation, and maintenance of military housing.

DOD policy states that private-sector housing in the communities near military installations will be relied upon as the primary source of family housing. However, when communities do not have an adequate amount of suitable housing, DOD intends to use housing privatization—rather than military-owned housing financed with military construction funds—as the primary means for meeting family housing requirements. As of December 2005, the services had awarded 52 projects to privatize over 112,000 family housing units and had plans to award 57 more projects to privatize over 76,000 more units by 2010. Table 1 shows implementation status by service. Also, appendix II contains more detailed status information on the 12 projects at the installations we visited during this review.

**Table 1: Privatization Projects Awarded and Planned as of December 2005**

Service	Number of projects			Number of housing units		
	Awarded	Planned	Total	Awarded	Planned	Total
Army	19	16	35	59,571	23,813	83,384
Navy and Marines	17	7	24	38,106	20,500	58,606
Air Force	16	34	50	14,615	32,133	46,748
<b>Total</b>	<b>52</b>	<b>57</b>	<b>109</b>	<b>112,292</b>	<b>76,446</b>	<b>188,738</b>

Source: DOD.

The duration of the initial development period—that is, the period when developers construct new housing units and renovate older units—varies among privatization projects, often lasting from 5 to 10 years. Thus, planned housing improvements resulting from privatization normally are not completed for several years after the projects are awarded. For all awarded projects as of September 2005, privatization developers had completed the construction of 10,911 new housing units and the renovation of 9,161 older housing units. Figures 1 through 5 show photographs of newly constructed and older privatized housing units at selected installations we visited.

**Figure 1: Newly Constructed (left) and Older (right) Privatized Housing at Fort Meade, Maryland**



Source: GAO.

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**Figure 2: Newly Constructed (left) and Older (right) Privatized Housing at Fort Stewart, Georgia**



Source: GAO.

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**Figure 3: Newly Constructed (left) and Older (right) Privatized Housing at Robins Air Force Base, Georgia**



Source: GAO.



**Figure 4: Newly Constructed (left) and Older (right) Privatized Housing at Patrick Air Force Base, Florida**



Source: GAO.

**Figure 5: Newly Constructed (left) and Older (right) Privatized Housing at the South Texas Project (Naval Air Station Corpus Christi), Texas**



Source: GAO.

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Servicemembers can choose whether or not to live in privatized housing—there are no mandatory assignments. Those who choose to live in privatized housing receive the same housing allowance (which is used to pay rent and utilities) as they would if they rented or purchased housing in the local communities.

Within the Office of the Secretary of Defense (OSD), the Housing and Competitive Sourcing Office, which reports to the Deputy Under Secretary of Defense (Installations and Environment), provides oversight of the housing privatization program, but the primary responsibility for implementing it rests with the individual services. OSD designed and uses the program evaluation plan report to oversee the effectiveness of the program and the performance of awarded projects. The report, prepared semiannually for the periods ending June 30 and December 31, is a compilation of extensive data submitted by the services for each awarded project and includes information on project contract structure, construction and renovation progress, occupancy, financial performance, and servicemember satisfaction with the housing.

This report is a continuation of a series of reports that we have issued on matters related to DOD's housing privatization program as well as DOD's process for determining housing requirements. The following summarizes key issues from these reports:

- In July 1998, we reported on several concerns as the housing privatization program began, including (1) whether privatization would produce insignificant cost savings and whether the long contract terms of many projects might cause the building of housing that will not be needed in the future; (2) whether controls were adequate to protect the government's interests if developers failed to operate and maintain the housing as expected; and (3) whether DOD would face certain problems if privatized housing units were not fully used by military members and were subsequently rented to civilians, as the contracts permit.<sup>7</sup>
- In March 2000, we reported that initial implementation progress for the privatization program was slow, the services' life-cycle cost analyses

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<sup>7</sup>GAO, *Military Housing: Privatization Off to a Slow Start and Continued Management Attention Needed*, GAO/NSIAD-98-178 (Washington, D.C.: July 17, 1998).

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provided inaccurate cost comparisons, and DOD lacked a plan for evaluating the effectiveness of the program.<sup>8</sup>

- In June 2002, we reported that DOD needed to (1) revise its housing requirements determination process to take into account greater use of community housing as well as the projected impact that the housing allowance initiative might have on military installation housing requirements; and (2) improve the value of the primary privatization oversight report by completing the report on time, including information on funds accumulated in project reinvestment accounts, and obtaining periodic independent verification of key report elements.<sup>9</sup>
- In May 2004, we reported that DOD needed to improve its revised housing requirements determination process to help ensure that housing investments, whether through military construction or privatization, were supported by consistent and reliable needs assessments. We also reported that DOD needed to survey servicemembers with dependents to update information on the housing preferences for family housing, given recent changes such as the increase in housing allowances.<sup>10</sup>

In response to each report, DOD officials have stated that they planned management actions to address our concerns.

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## Opportunities Exist to Improve the Oversight of Awarded Privatization Projects

Although OSD and the services have implemented program oversight policies and procedures to monitor the execution and performance of privatized housing projects, opportunities exist for improvement. Though owned and managed by the private sector, DOD maintains a strong interest in the operational and financial performance of privatized housing projects because it is accountable for public funds expended and because, according to DOD officials, the military's housing objectives can be met only if the projects remain viable. Thus, adequate program oversight is essential to help monitor and safeguard the government's interests and to

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<sup>8</sup>GAO, *Military Housing: Continued Concerns in Implementing the Privatization Initiative*, GAO/NSIAD-00-71 (Washington, D.C.: Mar. 30, 2000).

<sup>9</sup>See GAO-02-624.

<sup>10</sup>See GAO-04-556.

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help ensure the long-term success of the program. However, we identified three areas of concern—the adequacy of the Navy’s oversight methods, the usefulness of DOD’s primary oversight report, and the consistency of tenant satisfaction data—which provide opportunities for enhancing the oversight of awarded privatization projects. Specifically, as evidenced by issues identified in some Navy and Marine Corps projects we visited, the Navy’s oversight methods are not adequate to identify some project operational concerns or to ensure accurate reporting of project information. As a result, in contrast to the Army and the Air Force which have more robust oversight methods, there is less assurance that Navy management could become aware of project performance issues in a timely manner in order to plan needed actions to mitigate the concerns. Also, the usefulness of OSD’s primary program oversight tool—the semiannual privatization program evaluation report—has been limited because the report has not focused on key project performance metrics, has not been issued in a timely manner, and has included inaccuracies. Moreover, data on servicemember satisfaction with housing are inconsistent because DOD has not issued guidance to the services for collecting and reporting satisfaction information. As a result, data gathered to date cannot be readily tracked over time or compared among the services, and their value could be improved as a tool to more fully assess the impact of the privatization program, as well as the impact of DOD’s overall housing program, on servicemember quality of life.

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**Navy Program Oversight Did Not Identify and Address Some Project Concerns and Reporting Inaccuracies**

The Navy’s oversight program for monitoring Navy and Marine Corps projects has not adequately identified and addressed some project operational concerns, nor does it ensure accuracy in project information reported to DOD headquarters. Adequate program oversight is essential to help monitor and safeguard the government’s interests and to help ensure the long-term success of the program. However, in contrast to the Army’s and Air Force’s oversight programs, the Navy’s oversight program was less comprehensive and thus provided less assurance that Navy management would become aware of project performance issues in a timely manner. To illustrate, we found that the Army and the Air Force have robust, well-developed portfolio oversight programs to help top management monitor implementation of their privatization programs. Both of these services collected and analyzed detailed performance information on each project including construction progress, construction costs, occupancy levels, rental revenues, operating expenses, net operating income, and the debt



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coverage ratio.<sup>11</sup> These services prepared detailed project reports, which compared actual project performance data with expectations and discussed reasons for significant variances. The Army and the Air Force also prepared quarterly portfolio summary reports, which monitored project execution, analyzed trends, highlighted current and potential performance issues, and documented recent and planned actions to address any project concerns.

In contrast, the Navy's oversight program was less structured, included fewer details on project performance, and did not include summary oversight reports on portfolio performance, even though such reports were required by Navy guidance. Specifically, in February 2004, the Navy established a portfolio management group and assigned the group responsibility to oversee the Navy's and Marine Corps' housing privatization program. Although the group's charter stated that it would review project performance information and prepare consolidated portfolio summary reports, Navy officials stated that no such reports had been prepared at the time of our review in January 2006, almost 2 years after the charter was approved. Navy officials initially told us that the required summary reports were not needed because portfolio monitoring was performed in other ways, such as a review of monthly status reports from each project. They further stated that the Navy intended to eliminate the reporting requirement. Subsequently, Navy officials told us that the summary performance reports were needed and would be prepared in the future.

During our visits to Navy and Marine Corps privatization projects, we found instances where Navy oversight had not been adequate to identify and address some project operational issues and ensure accurate reporting of project performance information to OSD. For example:

- During our September 2005 visit to the Navy's Kingsville II project at the Naval Air Station Kingsville, Texas, we found that project funds had not

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<sup>11</sup>The debt coverage ratio is computed by dividing a project's net operating income by its debt service payment. Ratios above 1.0 indicate that net operating income from a project is sufficient to cover its debt service payments. Ratios below 1.0 indicate that a project's net operating income is insufficient to cover its debt service payment, requiring the use of funds from some other source, if available, to cover the debt payment to avoid default. Thus, higher ratios equate to lower risk of default while lower ratios typically signify increased default risk. According to Army officials, private-sector lenders often require that housing privatization projects maintain a minimum positive debt coverage ratio, such as 1.2.

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been disbursed in accordance with the project agreement. According to the agreement, 30 percent of the project's net cash flow—that is, the rental revenue remaining after payment of expenses and debt service—was to be deposited to a Navy-owned reserve account to be available for future project needs. On the basis of the project's net cash flow during the first and second quarters of 2005, over \$42,000 should have been deposited to the Navy's account. Yet, only \$314 was deposited. When we asked about this, Navy officials initially told us that the deposit amount was correct and consistent with original expectations. When we again questioned the deposit amount, Navy officials stated that the funds had not been appropriately disbursed and that they had asked the project developer for a complete analysis of the reserve accounts from project inception. The officials subsequently stated that a deposit was made to correct the balance in the Navy reserve account. Navy officials also stated that, in light of the shortcomings identified, the project agreement would be amended to require deposit and disbursement reports for all reserve accounts and to ensure that the project's annual audit included a compliance review.

- During our visit to the Navy's South Texas project in September 2005, we found that the project had not reimbursed the Navy for police and fire protection services, as specified in a memorandum signed by the Navy in January 2002. The memorandum stated that the project would pay the Navy for police and fire protection services provided by the Naval Air Station Corpus Christi beginning in calendar year 2002. The initial annual payment was to be \$84,756 with cost-of-living adjustments in future years. However, when we asked about the payments in September 2005, we were told that no payments had been made because the Navy had not processed the proper paperwork to bill the project for reimbursement. When we again asked about the reimbursement status in December 2005, Navy officials stated that they were working to resolve the issue. As of January 2006, 4 years after the project memorandum was initially signed, the Navy still had not billed the project for reimbursement.
- We found that inaccurate project status information was reported to OSD for five of the eight Navy and Marine Corps projects we reviewed in detail. For example, data reported to OSD on the San Diego II project showed that the project's total development cost was \$304 million, although the correct amount was \$427 million. Also, data reported to OSD for the Camp Pendleton I showed that the project's reinvestment account balance was \$725,000 although the correct balance was

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\$104,000. Further, data reported to OSD for the Marine Corps' Tri-Command project showed that no net operating funds or interest would be used to help finance the project during the initial development period even though project closing documents in March 2003 showed that \$53.6 million from net operating funds and interest were expected to be used to help finance the project.<sup>12</sup> Navy officials stated that corrections would be made in the information reported to OSD.

During our review, Navy officials stated that they had begun a top-to-bottom evaluation of the privatization oversight program. They stated that our review had been helpful in identifying items that required attention, such as those we mentioned. The officials stated that while they believed that their current procedures protected the government's interests and alerted top management to project concerns, they were conducting a comprehensive review to ensure consistency and completeness, upgrade the monitoring and oversight process, and make oversight responsibilities better defined and, perhaps, more aggressive. As part of the review, the officials stated that they intended to consider the Army's and the Air Force's oversight procedures and reports and also intended to ensure that appropriate portfolio performance summary reporting was completed in a timely fashion. The officials said that they planned to complete the review and implement oversight improvements by late spring 2006.

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## OSD's Primary Program Oversight Report Is of Limited Usefulness

OSD's semiannual privatization program evaluation report is of limited usefulness because it is unwieldy, untimely, and includes inaccurate information on some Navy and Marine Corps projects. Established in January 2001, the report is OSD's primary tool for overseeing the program's effectiveness and the performance of awarded projects. Although the report is a potentially useful tool for monitoring program implementation, the value of the report has been limited for several reasons.

First, as the number of awarded projects has increased from 7, when the report was established, to 52 at the end of December 2005, the report is not well focused, and has become unwieldy with the growing volume of data provided. The December 2004 report contained 268 pages and, unless changed, the report size will continue to increase as additional projects are awarded. A streamlined report that focuses on a few key performance

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<sup>12</sup>The Tri-Command project includes family housing at the Marine Corps Air Station Beaufort, the Marine Corps Recruit Depot Parris Island, and the Beaufort Naval Hospital.

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metrics from each project could more readily highlight any operational or financial concerns that might require management attention. Both the Army and the Air Force portfolio summary reports include such focused information and thus might provide useful insight in restructuring the OSD report.

Second, the report's usefulness has been limited because the report is not timely. Although the report is not intended to provide for real-time monitoring of awarded projects—the individual services have this responsibility—information included in the report is so dated by the time the report is issued that its value, as a tool to highlight any operational or financial concerns to top management in a timely manner, is questionable. For example, the report containing project information as of December 31, 2004, was due March 15, 2005, but it was not issued until June 2005, 3 months late, and contained data that were about 6 months old. Similarly, the report containing project information as of June 30, 2005, was due by September 15, 2005, but was not issued until February 2006, almost 5 months late, making the information in it more than 7 months old.

Third, the reports include inaccuracies because data reported by the services are sometimes incorrect. OSD officials stated that, although they review data submitted by the services for consistency and accuracy compared to other information provided to OSD, reported information has not been subjected to periodic independent verification to check accuracy.

We previously noted similar concerns about the privatization program evaluation report. In our June 2002 report, we recommended that DOD improve the report's value by completing the report on time, including information on funds accumulated in project reinvestment accounts, and obtaining periodic independent verification of key report elements.<sup>13</sup> Although the report now includes information on funds accumulated in project reinvestment accounts, concerns remain about the report's timeliness and accuracy. These concerns may be of additional importance given that the House Appropriations Committee requested in 2005 that DOD begin submitting a summary of the results of the program evaluation plan used to monitor the military housing privatization initiative to the

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<sup>13</sup>See GAO-02-624.

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committee<sup>14</sup> and that information from the report has been cited in DOD testimony on the housing privatization program.<sup>15</sup>

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## Methods for Measuring Servicemember Satisfaction with Privatized Housing Are Not Consistent

The services have adopted different methods and time frames for collecting and analyzing information about servicemember satisfaction with privatized housing, largely because OSD has not issued guidance on how or when the data must be collected. This limits the data's value for tracking occupant satisfaction over time as well as making service-to-service comparisons. Given that the overall goal of the housing privatization program is to improve the quality of life for servicemembers by improving the condition of military housing, DOD considers that one measure of program success is whether or not servicemembers are satisfied with privatized housing. To gauge servicemember satisfaction, OSD requires the services to collect and report satisfaction information from occupants at each awarded project as part of the input to the privatization program evaluation report. Specifically, OSD requires the services to survey occupants and to report the occupants' responses to the question "Would you recommend privatized housing?" Data are reported separately for occupants of privatized housing that is newly constructed, newly renovated, and not renovated. Similar satisfaction information is not routinely collected from the majority of servicemembers who live in the communities surrounding military installations.

The information required by OSD could be useful in assessing satisfaction levels over time and for comparing satisfaction levels among projects and the services to identify trends and factors attributing to higher or lower satisfaction levels. However, using satisfaction data for these purposes requires that the services collect consistent information, and this is not the case. Largely because OSD has not provided guidance on how or when the services should collect servicemember satisfaction data, the services have adopted different methods and time frames for collecting and analyzing satisfaction information.

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<sup>14</sup>H.R. Rep. No. 109-95, at 25 (2005).

<sup>15</sup>Hearing on Military Quality of Life and Veterans Affairs Before Subcommittee on Military Quality of Life of the House Appropriations Committee, 109th Congress (2005) (Statement of Mr. Philip W. Grone, Deputy Under Secretary of Defense, Installations and Environment).

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- The Army uses a contractor to survey privatized housing occupants annually between April and July. The 2005 survey asked 72 questions on various aspects of maintenance and property management services, unit condition, and amenities. Responses to most questions were requested using a 5-point scale—for example, where “1” represents very dissatisfied or no agreement and “5” represents very satisfied or extreme agreement. Prior to 2005, the Army’s survey requested most responses on a 7-point scale. Army officials stated that the change was made to be more compatible with surveys performed by the other services. However, the requested response to the “Would you recommend privatized housing?” question was “yes” or “no”, rather than a requested response on a 5-point scale. Therefore, because the Navy and the Air Force request that servicemembers respond to this question using a 5-point scale, the Army did not achieve compatibility with the other services in the responses to this key question.
  - The Navy uses a different contractor to survey privatized housing occupants at various times during the year. The survey asks 48 questions with responses requested on a 5-point scale, including the question on whether the occupant would recommend privatized housing. Navy officials stated that the Navy strives to survey each project once a year. However, surveys were not conducted at some Navy and Marine Corps privatized housing projects in 2004 or 2005, and for six projects, the Navy reported no satisfaction information to OSD for inclusion in the December 2004 privatization program evaluation report.
  - Air Force officials stated that until 2005 each privatized project conducted a local survey of occupants. However, due to disparities in the ways the survey was administered from one installation to another and because of the difficulty in achieving statistically significant response rates (for example, only nine responses were obtained from 382 tenants at the Patrick Air Force Base project in 2004), the Air Force decided to adopt a centralized approach. In June 2005, the Air Force used the same contractor as the Navy and surveyed occupants at all Air Force privatized projects. The survey asked 54 questions—mostly the same questions that the Navy asked—with responses requested on a 5-point scale, including the question on whether the occupant would recommend privatized housing.

With different survey methods, questions, and time frames, the information being collected cannot be readily used for the purposes of benchmarking, tracking, or comparing servicemember satisfaction levels. Thus, the value

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of the information to help measure whether or not the privatization program is succeeding in its goal of improving servicemember quality of life could be improved. Further, because housing satisfaction information is not routinely collected on servicemembers who do not live in privatized housing, DOD lacks complete information on the impact of its overall housing program on servicemember quality of life.

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### Lower Than Expected Occupancy Creates Concerns in Some Privatization Projects

Sixteen projects, or 36 percent, of 44 awarded privatization projects had occupancy rates below expectations with rates below 90 percent, as of September 30, 2005, raising concerns about project performance. Although the projects were justified on the basis of meeting military family housing needs, 20 projects have begun renting housing units to parties other than military families, including unaccompanied military personnel and the general public, in an attempt to keep rental revenues up. Still, rental revenues in some of the projects we visited have not met expectations, resulting in signs of financial stress such as having months where project revenues were insufficient to pay all project expenses. In the long term, if lower than expected occupancy and rental revenues persist, the result could be significantly reduced funds deposited into reserve accounts, which provide for future project needs and renovations. Or, in the worst case, there could be project financial failures. Factors contributing to occupancy challenges include poor condition of existing housing that has not yet been renovated in some projects, significantly increased housing allowances, which have made it possible for more military families to afford off-base housing thus reducing the need for privatized housing, and continued problems in DOD's housing requirements determination process, which could result in overstating the need for privatized housing. Although deployments can also contribute to occupancy challenges, they were cited as a contributing factor to lower than expected occupancy rates in only 1 of the 12 projects we reviewed. The services are monitoring occupancy and revenue concerns, and in some cases, have taken or planned steps to address the concerns. However, without additional steps to help ensure that the size of future privatization projects is reliably determined, future projects could face similar occupancy and financial challenges.

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### Occupancy Was Below Expectations in Some Projects

We found that some awarded projects, as shown in table 2, were not meeting occupancy expectations. According to service officials, the expected occupancy rate during a project's initial development period, when many housing units are being constructed or undergoing renovation,

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is usually around 90 percent of the units available for rent. After completion of the initial development period, most projects expect occupancy rates of about 95 percent. As of September 30, 2005, occupancy was below expectations and below 90 percent in 6 of the Army's 19 awarded projects, 4 of the Navy's and Marine Corps' 13 awarded projects, and 6 of the Air Force's 12 awarded projects. Although most of these projects were in their initial development periods, 1 Navy and 2 Air Force projects were not. In total, of 85,590 privatized housing units available for rent, 77,355 units or 90 percent were occupied and 8,235 units or 10 percent were vacant.



**Table 2: Awarded Privatization Projects with Occupancy Rates Below Expectations as of September 30, 2005<sup>a</sup>**

Service/Project	Expected occupancy rate (percent)	Actual occupancy rate (percent)	Housing units		
			Available	Occupied	Vacant
<b>Army</b>					
Fort Meade	94	80	2,778	2,230	548
Fort Stewart	94	79	3,089	2,433	656
Fort Hamilton	94	70	286	199	87
Fort Shafter/Schofield Barracks	94	78	7,074	5,520	1,554
Fort Leonard Wood	94	83	2,229	1,853	376
Fort Bliss	94	83	3,001	2,491	510
<b>Navy/Marine Corps</b>					
South Texas	80	78	398	311	87
Kingsville II <sup>b</sup>	97	89	150	133	17
Tri-Command	93	83	1,680	1,393	287
Pendleton II/Quantico	93	89	3,656	3,261	395
<b>Air Force</b>					
Dyess Air Force Base <sup>b</sup>	97	86	402	344	58
Hanscom Air Force Base	88	84	722	607	115
Kirtland Air Force Base	90	85	1,078	919	159
Little Rock Air Force Base	90	86	1,320	1,141	179
Patrick Air Force Base	90	73	592	433	159
Robins Air Force Base <sup>b</sup>	97	83	670	559	111

Source: DOD.

<sup>a</sup>Our analysis excluded seven projects awarded as of September 30, 2005, because six projects had been privatized for less than 2 months and one had no units yet available for rent. Also, the table includes only projects with occupancy rates below 90 percent. Six additional projects were not meeting occupancy expectations but had occupancy rates of 90 percent or more.

<sup>b</sup>The initial development period was completed at these projects.

Occupancy rates would have been lower if 20 projects had not rented units to nontarget tenants—that is, tenants other than military families. Although the projects were justified on the basis of meeting the needs of military families, project managers are allowed to offer units for rent to nontarget tenants, when occupancy rates fall below expected levels for a designated period of time, such as 2 or 3 months. Normally, project managers follow a priority list, referred to as a tenant waterfall, when renting units to

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nontarget tenants. In a typical tenant waterfall, vacant family housing units are first offered to single or unaccompanied active duty military servicemembers; then to DOD-related individuals, such as retired military personnel and civilians and contractors who work for DOD; and finally to civilians in the general public. As of September 30, 2005, of 44 awarded projects, 20 projects, or 45 percent, had rented units to individuals other than military families. More specifically, 20 projects had rented 1,116 units to single or unaccompanied military personnel; 662 units to retired military personnel and civilians and contractors who work for DOD; and 299 units to civilians from the general public. In all, 2,077 family housing units were occupied by parties other than military families.

Although renting vacant units to nontarget tenants increases rental revenue, the practice includes some associated concerns. For example, although background checks are performed on prospective general public civilian tenants, several service officials stated that additional concerns exist when civilians live on military installations, such as whether they should have access to on-base amenities available to military families. Also, when units are rented to unaccompanied servicemembers, the rental revenue is usually less than with military family occupants because the rental rate is normally based on housing allowance rates, and the allowance rates for unaccompanied servicemembers are less than the rates for servicemembers with families. Therefore, although occupancy rates increase, the increase in rental revenues usually falls short of the revenue expectations for the units.

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**Lower Than Expected  
Occupancy Causes  
Financial Stress and Could  
Reduce Funds for Future  
Reinvestment**

When project occupancy levels are less than expected, project rental revenues are less than expected, which can cause financial stress, such as having periods when revenues are insufficient to pay all expenses. If revenue shortfalls persist in the long term, the result can be reduced or no funds remaining after payment of operational expenses, debt service, and developer returns to be deposited into the reserve accounts established to pay for future project needs and renovations. In a worst—case scenario,

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there could be insufficient funds to make a project's loan payments, which could lead to a financial default.<sup>16</sup>

Although the housing privatization program is relatively young and the majority of the projects awarded through September 2005 appeared financially healthy, lower than expected occupancy rates and rental revenues in some projects were causing financial stress in some of the projects we visited. The examples below illustrate the occupancy and financial challenges facing some projects, the reasons for the challenges, and steps taken or planned in response. While many vacancies involved older housing units not yet renovated, we also found vacancies involving newly constructed and renovated units.

- At Fort Meade in July 2005, 2,044 units, or 81 percent, of the available units were occupied, compared to an expected occupancy of 2,332 units, or 92 percent. Army officials stated that the project's 491 vacant units were older units that had not been renovated. Occupancy would have been lower if the project had not rented units to nontarget parties. Of the occupied units, 205 units, or 10 percent, were occupied by nontarget tenants, including unaccompanied military servicemembers, military retirees, and DOD civilian employees. The shortfall of 288 expected occupants had caused financial stress for the project. For example, the project's net operating income was 33 percent below expectations for the quarter ending June 30, 2005. Army officials stated that lower than expected revenues had slowed the project's construction progress because funds remaining after payment of project expenses were to be used to help pay for construction costs during the initial development period. The officials stated that lower than expected occupancy was caused by three main factors. First, the poor condition of much of the privatized housing that had not yet been improved made it unattractive to military families. Second, increased housing allowances made more local community housing affordable and caused many military families to decide to rent or buy housing off base. Third, recent private-sector

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<sup>16</sup>According to service officials, it is a project's developer and private lender—not the government—who have provided the majority of each project's development funds and, consequently, who would bear most of the consequences from a project financial failure. According to service officials, the primary remedy to lenders in case of a default is to replace the project's property manager with one who could better market the rental property and thus increase financial results. At the same time, however, DOD has an interest in the financial success of each project because it has made an investment in each project and, according to DOD officials, the military's housing objectives can be met only if the projects remain viable over the long term.

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housing development in the local communities surrounding Fort Meade increased the availability of local housing. In response to the occupancy and financial concerns, Army officials stated that plans were underway to restructure the project and reduce the project's planned number of units. Army officials were optimistic that occupancy would increase as more units were renovated and additional new units were constructed, making the project more appealing to military families.

- At the Navy's South Texas project, Navy officials stated that lower than expected occupancy had been a concern since the project's beginning in February 2002. At the time of our visit in September 2005, the occupancy rate was 78 percent, with 311 units occupied and 87 units vacant. Navy officials stated that a key reason for low occupancy was that the project was still in its initial development period, and progress in improving housing conditions had proceeded much more slowly than planned. As a result, much of the privatized housing was in poor condition and unattractive to military families. However, of the 87 vacant units, Navy officials stated that only 11 were awaiting renovation or replacement, and the remaining 76 units consisted of newly constructed or renovated housing units. Other causes for low occupancy included reduced housing requirements caused by reductions in military personnel assigned to the area and increased housing allowances, which made more local community housing affordable for servicemembers. With reduced occupancy, the project had experienced signs of financial stress. For example, in July 2005, the project's rental income was 26 percent below budget and was insufficient to pay the project's operating expenses. Also, the project's debt coverage ratio was a negative number, meaning that net operating income was insufficient to cover the project's debt payment. Navy officials stated that the project faced little risk of financial failure during its initial development period because accounts were established at the project's inception to provide for debt service payments during this period. Nevertheless, Navy officials expressed concern about the project and had taken actions to address the situation. In August 2004, an agreement was reached to reduce the project's scope by 80 units, and Navy officials stated that further project scope reductions might be considered in the future.
- At Robins Air Force Base, 559 units, or 83 percent, of 670 available units were occupied in September 2005 compared to the expected occupancy rate of 97 percent. This project had completed its initial development period and consequently all available units are newly constructed or renovated. Of the occupied units, 109 units were occupied by nontarget

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tenants, including 42 civilians. Air Force officials stated two reasons for the low occupancy. First, increased housing allowances and attractive mortgage interest rates had caused some servicemembers to decide to purchase homes in the local community. Second, the project's design, which included many two-bedroom units, was less appealing to some military families. As a result of the low occupancy rates, Air Force officials stated that the project faced significant financial challenges. The Robins project was one of three Air Force projects rated as unsatisfactory in the Air Force's September 2005 portfolio summary report because of financial weakness and concerns about meeting developmental and/or financial obligations. Air Force officials stated that alternatives were being explored, which may require renegotiation of the project agreement with the developer to improve the project's long-term financial viability.

- At Patrick Air Force Base, military families occupied 172, or only 29 percent, of the 592 available units. Nontarget tenants, including 135 unaccompanied servicemembers and 126 civilians, occupied 261 additional units to make the overall occupancy rate 73 percent compared to an expected occupancy rate of 90 percent. Air Force officials attributed the low occupancy to the poor condition of the project's units, where planned improvements were far behind schedule. The project, which will consist of all new units when completed, had no new units ready for occupancy at the time of our visit in early December 2005. The officials also said that increased housing allowances had caused many military families to decide to obtain housing in the local community. Although the project's nontarget tenants had significantly reduced the financial challenges that would have occurred if only military families occupied the housing, the project still faced financial stress. For the quarter ending September 30, 2005, the project's net operating income was 28 percent below expectations. Largely because of financial issues, the project was restructured in April 2005 to increase debt and provide additional funds needed to complete the initial development period. As part of the restructuring, some funds that had initially been required to flow into the project's reserve account for future project needs and renovation were allowed to be used for construction funding. Air Force officials stated their belief that, as housing improvements are completed, both occupancy rates and the number of military family tenants will increase and the project's financial performance will improve.

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- At the time of our visit to the Marine Corps' Tri-Command project in early October 2005, the expected occupancy rate was 93 percent. However, the actual rate was 83 percent, with 1,393 of 1,680 available units occupied and 287 units vacant. Service officials stated that most vacant units were older units that had not been renovated. According to installation officials, the lower than expected occupancy rate was caused by increased housing allowances, which had led some servicemembers to decide to rent or buy housing in the local community. Also, although the project was awarded in March 2003, the project was still undergoing initial development and, with many of the planned housing improvements not yet completed, much of the on-base housing was in poor condition and unattractive to military families. With lower than expected occupancy, the project showed signs of financial stress. In September 2005, the project reported that rental revenues were 14 percent below expectations and the net operating income was 30 percent below expectations. Also, the project's debt coverage ratio was .66, meaning that the project's operations did not produce sufficient funds to cover the debt payment. Marine Corps officials stated that the project faced little risk of financial failure during its initial development period because accounts were established at the project's inception to provide for debt service payments during this period. Still, the officials expressed concern about the project's finances. In an effort to improve occupancy and financial performance, the project revised its revitalization strategy in August 2005 and obtained \$44.1 million in additional private loans to finance upgrades to more housing units than originally planned to make the units more appealing to potential renters. Marine Corps officials stated that the revised strategy should result in improved project performance.

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**Increased Housing Allowances and Unreliable Needs Assessments Contribute to Occupancy Concerns**

Increases in monthly housing allowances and unreliable estimates of housing requirements contribute to occupancy concerns in some privatization projects by reducing the need for privatized housing or possibly overstating the required size of some projects. Some causes of occupancy concerns, such as changes in personnel assignments and deployments, often cannot be predicted and are beyond the control of the services. While deployments can contribute to occupancy challenges, they were cited as a contributing factor to lower than expected occupancy rates in only 1 of the 12 projects we reviewed. Also, as the condition of privatized housing at some installations improves with the construction of new housing and the renovation of older housing units, the projects may attract more military families and the occupancy rates may improve. However,

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other factors, such as the impact of DOD's zero-out-of-pocket housing allowance initiative and the reliability of DOD's overall housing requirements assessment process, can also affect occupancy rates and are important considerations in planning for future housing privatization projects. To help ensure that the size of housing projects is accurately determined, we previously reported that DOD needed to study how increased allowances might affect future housing needs and to make improvements in its requirements process to maximize reliance on local community housing, as required by DOD policy. Yet, because DOD has yet to implement these recommendations, the planned size of future privatization projects may not be based on reliable needs assessments, which could contribute to occupancy and financial challenges in some future projects.

For example, in June 2002, we noted that uncertainties existed in the future need for military-owned and privatized housing because of DOD's initiative to increase housing allowances.<sup>17</sup> Prior to the initiative, servicemembers with families living in community housing received, on average, an allowance that covered about 81 percent of housing costs, including utilities. Servicemembers paid the remaining 19 percent of housing costs out of pocket using other sources of income. Under the initiative begun in 2001, housing allowances increased each year over a 5-year period, progressively eliminating the average out-of-pocket costs. By January 2005, the average housing allowance fully covered the average costs of housing and utilities in each geographic area with the typical servicemember paying no additional out-of-pocket costs. Table 3 illustrates the increase in housing allowances for selected military paygrades in five locations before the initiative in 2000 and after the initiative in 2006.

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<sup>17</sup>See GAO-02-624.

**Table 3: Examples of Changes in Monthly Housing Allowances for Servicemembers with Dependents<sup>a</sup>**

Location	Paygrade (E=enlisted and O=officer)	Monthly allowance in 2000	Monthly allowance in 2006	Increase in allowance (percent)
Fort Meade, Maryland	E-3	\$774	\$1,259	63
	E-6	1,148	1,605	40
	O-3	1,245	1,785	43
Naval Air Station Corpus Christi, Texas	E-3	592	979	65
	E-6	715	1,333	86
	O-3	857	1,393	63
Robins Air Force Base, Georgia	E-3	540	898	66
	E-6	673	967	44
	O-3	807	1,237	53
Patrick Air Force Base, Florida	E-3	506	1,027	103
	E-6	662	1,437	117
	O-3	817	1,531	87
Marine Corps Air Station Beaufort, South Carolina	E-3	502	961	91
	E-6	701	1,271	81
	O-3	853	1,345	58

Source: DOD.

<sup>a</sup>Changes in the housing allowance amounts reflect the impact of the zero-out-of-pocket initiative as well as changes in cost of housing at each location since 2000.

Our report further noted that increased housing allowances from the zero-out-of-pocket initiative would make a significant impact on the military housing program. First, increased allowances should decrease the requirement for military-owned or privatized houses by making local community housing more affordable to servicemembers. Second, over time, the supply of community housing available to military families could increase and reduce the requirement for military-owned or privatized housing as private developers construct new housing near military installations to profit from renting to servicemembers at market rates. Third, increased allowances should allow DOD to better satisfy the preferences of most servicemembers to live off base and reduce demand for on-base housing.<sup>18</sup> For these reasons, we recommended that DOD take into account the projected impact that the housing allowance initiative

<sup>18</sup>A 2005 Army survey showed that 80 percent of enlisted personnel and 76 percent of officers reported that they would prefer to live off base, if costs were the same. These results are similar to a previous DOD housing preference survey.



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might have on military housing requirements. Yet, as of January 2006, DOD had not conducted detailed analyses to consider the effects of increased allowances on requirements, nor had the department provided guidance to the services on how these effects should be considered in their housing requirements assessments.

We also previously reported on changes needed to increase the reliability of DOD's housing requirements determination process.<sup>19</sup> In May 2004, we noted that, although DOD had revised its process and made improvements, additional steps were needed to ensure consistency, accuracy, and maximum reliance on private housing in the communities surrounding military installations. Specifically, we noted that (1) DOD had not provided the services with timely detailed guidance for implementing the revised requirements process; (2) in the absence of detailed guidance, the services used inconsistent methods and sometimes questionable data sources and assumptions when determining family housing needs at various installations; and (3) as a result, DOD could not know with assurance how many housing units it needed and whether its housing investment decisions were justified. The report also noted that DOD's revised requirements process provided exceptions to the use of available, suitable local community housing at each installation. We noted that one exception—military mission requirements—appeared clearly justified, but the other exceptions did not and could result in the services identifying more on-base family housing requirements than were actually needed. For example, DOD's process allows installations to include in its military-owned or privatized housing requirement a quantity of housing to accommodate up to 10 percent of the projected number of families at those installations, regardless of the availability of local housing.

To address these matters, we recommended that DOD provide the military services with more detailed guidance on implementing the revised housing requirements process to help ensure that housing investments, whether through military construction or privatization, were supported by consistent and reliable needs assessments. We also recommended that DOD review the rationale supporting the exceptions to using local community housing in an effort to reduce or narrow the scope of the exceptions and help maximize use of available community housing. In response, DOD stated that it planned to include detailed guidance on implementing the requirements process in a forthcoming revision to the

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<sup>19</sup>See GAO-04-556.

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DOD housing management manual. DOD officials stated that the revised manual would also include guidance narrowing the scope of the exceptions provided to the services in the use of available community housing. Although the revised manual was originally scheduled for issuance in December 2004, the manual had not been issued at the time of our review in January 2006. DOD officials stated that they were still revising the manual and that the final version should be issued during 2006.

Upcoming changes in personnel assignments at some installations resulting from Base Realignment and Closure decisions, the return of forces from overseas bases, and the implementation of the Army's modularity program will increase the importance of reliable housing assessments. In particular, some installations stand to gain substantial numbers of military families, which could increase requirements for privatized housing and increase occupancy in current projects. Conversely, implementation of the Army's force stabilization initiative may result in reduced requirements for privatized housing because more service members may choose to purchase homes if they know that they will be assigned to the same installation for a longer period of time. However, until improvements are implemented in the housing requirements assessment process, the assessments for planned privatization projects at some installations may indicate a need for more housing units than required, which could lead to future occupancy and financial concerns. In its September 2005 portfolio summary report, the Air Force highlighted this concern. The report noted that:

The fact is that the [project] scopes are currently based on static housing requirements and market analysis. Markets are not static, as is evidenced by the speed at which the private sector has provided housing thereby reducing subsequent [housing] requirements...The Air Force should carefully consider expectations for future (2 to 5 years) housing needs when establishing the scope of new projects....Because of the delays between the date of the housing requirements and market analysis and the delivery of units, the Air Force may be building too many homes. Overbuilding in any project could pose a significant risk.

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## Conclusions

Adequate privatization program oversight is essential to help monitor and safeguard the government's interests and ensure the long-term success of the program. Unless the Navy follows through with its plans to improve its policies and procedures for overseeing its housing privatization program, Navy management will continue to lack assurance that it can become aware of project performance issues in a timely manner. Also, unless DOD streamlines its privatization program evaluation report to focus on key project performance metrics, completes the report on time, and obtains periodic independent verification of key report elements, the report's value

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as an oversight tool will continue to be limited. Further, until DOD provides guidance to the services to help ensure consistent collection and reporting of housing satisfaction from all servicemembers, the value of the information to help measure this aspect of the privatization program's success, as well as the impact of DOD's overall housing program on quality of life, will also continue to be less useful than it could be.

In the long term, if lower than expected occupancy rates and rental revenues at some privatization projects persist, the result could be significantly reduced funds flowing into reserve accounts that were established to provide for future project needs and renovations. In the worst-case scenario, the program could see project financial failures, which could affect the quality of housing available to military families. Such concerns may occur in future privatization projects unless DOD fully considers the impact of increased allowances on housing requirements and implements improvements to its requirements determination process so that the planned size of future projects is reliably determined.

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## Recommendations for Executive Action

We recommend that the Secretary of Defense direct the Deputy Under Secretary of Defense (Installations and Environment) to take the following five actions:

- Require the Navy to upgrade the monitoring and oversight of its housing privatization program to ensure consistency, completeness, and preparation of appropriate portfolio summary performance reports.
- Improve the value of DOD's privatization program evaluation report by streamlining the report to focus on key project performance metrics, completing the report on time, and obtaining periodic independent verification of key report elements.
- Provide guidance to the services to help ensure consistent collection and reporting of housing satisfaction information from all servicemembers, which would allow for benchmarking and tracking of tenant satisfaction over time as well as for making service-to-service comparisons.
- Determine how increased housing allowances from the zero-out-of-pocket initiative will most likely impact future family housing requirements and provide guidance on how the impacts should be factored into the services' housing requirements assessments.

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- Expedite issuance of the revised DOD housing management manual and ensure that the revision includes guidance to improve the reliability of housing requirements assessments and reduce the scope of the exceptions provided to the use of available community housing.

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## Agency Comments and Our Evaluation

In written comments on a draft of this report, the Director for Housing and Competitive Sourcing within the Office of the Under Secretary of Defense for Acquisition, Technology and Logistics fully agreed with three and partially agreed with two of our recommendations and stated that shortcomings identified in the report would be forthrightly addressed. Noting that our report was an important contribution to DOD's oversight of the housing privatization program to date, DOD stated that steps were already underway to streamline the privatization program evaluation report and improve the report's accuracy. Also, DOD intends to closely observe project vacancy rates in view of the increased housing allowance rates and ensure that the revised housing management manual, now scheduled for completion by the end of calendar year 2006, addresses the housing requirements issues identified in our report. DOD also stated that its privatization program evaluation report was not intended to provide real-time project oversight and that this was the role of the services' portfolio management systems. Our report does not imply that the evaluation report should provide for real-time project oversight. Nevertheless, because the evaluation report is the department's primary tool for evaluating the program's effectiveness, we continue to believe that such a report which focuses on key performance metrics and contains accurate and timely information is important for OSD in carrying out its oversight and effective stewardship of the program.

DOD partially agreed with our recommendation that the Navy be required to upgrade the monitoring and oversight of its housing privatization program to ensure consistency, completeness, and preparation of appropriate portfolio summary performance reports. DOD stated that it disagreed with our assumption that, because the Navy did not prepare summary portfolio briefings and the Navy's input to the privatization program evaluation report contained errors, the Navy was at risk of not being aware of potential problems with projects. DOD also stated that a review of other projects conducted by the Navy and a Navy consultant did not identify issues such as those we identified at the Kingsville II and South Texas projects. However, DOD stated that additional guidance was being developed for internal reviews of audits and financial data from general partners to ensure accurate monitoring and oversight of distributions.

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Finally, DOD stated that the cost of fire and police services at the South Texas project was not invoiced or reimbursed for 2 years, not for 4 years, as stated in our report.

We disagree with DOD's description of the Navy's oversight of its housing privatization program and continue to believe that, without improvement, the Navy is at risk of being unaware of potential problems with projects. First, our report notes that in contrast with the Army and the Air Force, the Navy's oversight program was less structured, included fewer details on project performance, and did not include summary oversight reports on portfolio performance, even though such reports were required by Navy guidance. Also, as noted in our report, the Navy agreed that oversight improvements were needed and had begun conducting a comprehensive review to ensure consistency and completeness, upgrade the monitoring and oversight process, and make oversight responsibilities better defined and, perhaps, more aggressive. Further, we continue to believe that inaccurate project status information reported to OSD for five of the eight Navy and Marine Corps projects we reviewed indicates a lack of adequate oversight and attention to detail. Second, while the Navy and its consultant apparently did not identify issues at other projects, the Navy was developing additional guidance for internal reviews of audits and financial data from general partners to ensure accurate monitoring and oversight of distributions. We believe that this action indicates the Navy has recognized the need for better oversight and also raises the question of why such guidance was not already in place given that the housing privatization program began in 1996. Third, regarding the reimbursement for the cost of fire and police services at the South Texas project, our report contains information provided by top management in the Navy's housing privatization program and which we revisited with the Navy officials several times over the duration of this review. For example, we posed a written question to the Navy headquarters housing officials in mid-November 2005 in which we reiterated a statement they had previously made to us earlier that Navy never billed the South Texas project for fire and police services, and asked for the status of the issue. On November 22, 2005, an official on the staff of the Assistant Secretary of the Navy for Installations and Environment, without stipulating a set number of years, provided the following written response, "Navy Region South East and the installation are working to resolve this issue. As of November 15, 2005, the project had not been billed for the services." Subsequently in a December 13, 2005, meeting with Navy privatization program officials, we again discussed this issue and were told that they were working to resolve the issue. On January 25, 2006, a senior Navy housing official told us that the

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installation had billed the project and had received payment within the last month. When we asked about the month in which the billing occurred, the same official responded 2 days later that “The billing has not yet occurred.” In view of these statements from the top Navy management officials responsible for overseeing the housing privatization program, we believe that DOD’s comment that cost of fire and police services at the South Texas project were not invoiced or reimbursed for 2 years, rather than 4 years, only helps to illustrate our point—that the Navy should be required to upgrade the monitoring and oversight of its housing privatization program.

DOD partially agreed with our recommendation that DOD provide guidance to the services to help ensure consistent collection and reporting of housing satisfaction information from all service members, which would allow for benchmarking and tracking of tenant satisfaction over time as well as for making service-to-service comparisons. DOD stated that tenant survey guidance already exists and that it would not be suitable to overlay a programwide directive because of differences among the services in the data they need to help support their specific, negotiated business structures. However, DOD also stated that it would revise its guidance to require consistent use of a 5-point numerical system to measure tenant satisfaction across the services. DOD also agreed that (1) housing preferences should be surveyed for all service members, not simply those occupying privatized housing; (2) it is important to reevaluate servicemember housing preferences driven by increased allowances and housing revitalization; and (3) a panel at the Office of Secretary of Defense has been studying how to best implement such a survey. The intent of our recommendation was not to require the services to use identical questions when assessing tenant satisfaction, but rather to ensure that the services’ methods, questions, and time frames were of sufficient consistency to allow for benchmarking, tracking, or comparing servicemember satisfaction levels. Ensuring that the services use a consistent 5-point numerical system for measuring tenant satisfaction is a step in the right direction. However, we continue to believe that DOD needs to ensure that the services use consistent time frames in order to make maximum use of satisfaction information as a tool to help measure whether or not the privatization program is succeeding in its goal of improving servicemember quality of life.

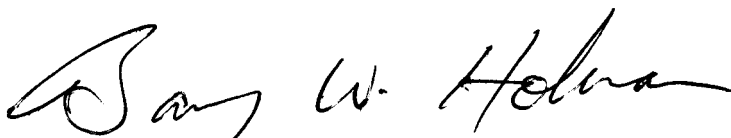
DOD’s comments are reprinted in their entirety in appendix III.

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We are sending copies of this report to other interested congressional committees; the Secretaries of Defense, Army, Navy, and Air Force; and the Director, Office of Management and Budget. We will also make copies available to others upon request. In addition, the report will be available at no charge on GAO's Web site at <http://www.gao.gov>.

If you or your staff have any questions about this report, please call me at (202) 512-5581 or email at [holmanb@gao.gov](mailto:holmanb@gao.gov). Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report. The GAO staff members who made key contributions to this report are listed in appendix IV.

A handwritten signature in black ink that reads "Barry W. Holman". The signature is written in a cursive, flowing style.

Barry W. Holman, Director  
Defense Capabilities and Management

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*List of Congressional Addressees*

The Honorable John Warner  
Chairman

The Honorable Carl Levin  
Ranking Minority Member  
Committee on Armed Services  
United States Senate

The Honorable Kay Bailey Hutchison  
Chair

The Honorable Dianne Feinstein  
Ranking Minority Member  
Subcommittee on Military Construction and  
Veterans' Affairs, and Related Agencies  
Committee on Appropriations  
United States Senate

The Honorable Duncan L. Hunter  
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The Honorable Ike Skelton  
Ranking Minority Member  
Committee on Armed Services  
House of Representatives

The Honorable James T. Walsh  
Chairman

The Honorable Chet Edwards  
Ranking Minority Member  
Subcommittee on Military Quality of Life and  
Veterans Affairs and Related Agencies  
Committee on Appropriations  
House of Representatives



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# Scope and Methodology

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To determine whether opportunities exist to improve the Department of Defense's (DOD) oversight of awarded housing privatization projects, we summarized program implementation status and costs, compared the status to DOD's goals and milestones, and discussed issues affecting program implementation with DOD and service officials. We relied on program status data provided by DOD and the services and confirmed the status data for 12 privatization projects, but we did not otherwise test the reliability of the data. We also obtained, reviewed, and compared DOD and service policies, guidance, and procedures for monitoring implementation and measuring progress in the housing privatization program. We questioned DOD and service officials responsible for the program about how they oversee project performance, how they compare performance with expectations, and what actions they take when performance does not match expectations. We obtained and reviewed applicable oversight reports and assessed the extent to which the reports included key project performance data, trends, and discussion of any performance concerns. We also compared the issue dates of DOD and service oversight reports with the due dates to determine the timeliness of the reports; reviewed and compared the services' methods and time frames used to measure servicemember satisfaction with privatized housing; and reviewed the results of DOD and service efforts to assess servicemember housing preferences.

Further, we visited selected military installations with housing privatization projects to review oversight at the local level, to examine project performance, and to determine whether performance information and concerns were adequately captured in oversight reports and provided to top management in a timely manner. Specifically, we visited Fort Meade, Maryland; Fort Stewart, Georgia; Naval Air Station Corpus Christi, Texas; Naval Air Station Kingsville, Texas; Naval Station San Diego, California; Patrick Air Force Base, Florida; Robins Air Force Base, Georgia; Marine Corps Base Camp Pendleton, California; and Marine Corps Air Station Beaufort, Georgia. These installations were chosen because they contained established privatization projects, represented each of the military services, and a balance of some with and without challenges. Together, the installations contained 12 separate privatization projects.

To determine to what extent awarded privatization projects are meeting occupancy expectations, we interviewed DOD and service officials to discuss project occupancy expectations, the factors that contribute to lower than expected occupancy rates, the financial and other impacts that result from lower than expected occupancy rates, and the responses

normally taken when occupancy is below expectations. We obtained, reviewed, and analyzed project occupancy rates and trends for all projects awarded as of September 30, 2005, and compared these data to occupancy expectations. We relied on occupancy data provided by the services and did not otherwise attempt to independently determine occupancy rates. Also, for the 12 projects at the installations visited, we reviewed project justification and budget documents to determine each project's occupancy expectations and compared actual occupancy rates with the expectations. When occupancy rates were below expectations, we reviewed project performance reports and interviewed local officials to determine the causes, consequences, and any actions taken or planned in response. We also reviewed information on the number of privatized family housing units rented to parties other than military families and discussed the associated impacts with service officials. Further, we determined the status of steps taken by DOD in response to previous GAO recommendations to address concerns in the reliability of the services' housing requirements assessments.

We conducted our work from July 2005 through February 2006 in accordance with generally accepted government auditing standards.

# Details on 12 Housing Privatization Projects

Table 4 provides details on the 12 housing privatization projects at the installations visited during this review.

**Table 4: Details on the 12 Housing Privatization Projects We Visited**

Service, project, location, and award date	Total housing units after initial development period	Total estimated initial development cost (in millions)	Estimated completion date for initial development period	Project description	At the time of our visit, was project		
					Development progress on schedule?	Meeting occupancy expectations?	Renting units to parties other than military families?
Army, Fort Meade, Maryland, May 2002	3,170	\$461.2	2012	Government conveyed existing units and leased land. Developers to construct 2,748 new units, renovate 422 units, and own, operate, and maintain all units for 50 years.	No	No	Yes
Army, Fort Stewart and Hunter Army Air Field, Georgia, Nov. 2003	3,702	\$353.4	2011	Government conveyed existing units, leased land, and contributed \$37.3 million. Developer to construct 1,868 units, renovate 1,597 units, and own, operate, and maintain all units for 50 years.	No	No	No

**Appendix II**  
**Details on 12 Housing Privatization Projects**

(Continued From Previous Page)

Service, project, location, and award date	Total housing units after initial development period	Total estimated initial development cost (in millions)	Estimated completion date for initial development period	Project description	At the time of our visit, was project		
					Development progress on schedule?	Meeting occupancy expectations?	Renting units to parties other than military families?
Navy, South Texas, Texas, Feb. 2002	585 <sup>a</sup>	\$75.4	2007 <sup>a</sup>	Government conveyed existing units, leased land, and contributed \$29.4 million. Developer to construct 470 units, renovate 114 units, and own, operate, and maintain all units for 50 years.	No	No	No
Navy, Kingsville II, Texas, Nov. 2000	150	\$14.5	Completed	Government conveyed units and land, contributed \$4.3 million, and provided \$2.5 million loan. Developer provided land, constructed 150 units, and will own, operate, and maintain the units for 30 years.	Initial development completed	No	Yes

**Appendix II  
Details on 12 Housing Privatization Projects**

*(Continued From Previous Page)*

Service, project, location, and award date	Total housing units after initial development period	Total estimated initial development cost (in millions)	Estimated completion date for initial development period	Project description	At the time of our visit, was project		
					Development progress on schedule?	Meeting occupancy expectations?	Renting units to parties other than military families?
Navy, San Diego I, California, Aug. 2001	3,248	\$328.8	2006	Government conveyed units, leased land, and contributed \$20.9 million. Developer to construct 1,400 units, renovate 1,058 units, and own, operate, and maintain all units for 50 years.	Yes	No	No
Navy, San Diego II, California, May 2003	3,217	\$427.0	2007	Government conveyed units and leased land. Developer to construct 460 units, renovate 1,072 units, and own, operate, and maintain all units for 50 years.	Yes	Yes	No

**Appendix II  
Details on 12 Housing Privatization Projects**

(Continued From Previous Page)

Service, project, location, and award date	Total housing units after initial development period	Total estimated initial development cost (in millions)	Estimated completion date for initial development period	Project description	At the time of our visit, was project		
					Development progress on schedule?	Meeting occupancy expectations?	Renting units to parties other than military families?
Marine Corps, Camp Pendleton I, California, Nov. 2000	712	\$88.3	Completed	Government conveyed units, leased land, and provided \$29.4 million loan. Developer constructed 512 units, renovated 200 units, and will own, operate, and maintain the units for 50 years.	Initial development completed	Yes	No
Marine Corps, Camp Pendleton II and Quantico, California and Virginia, Oct. 2003 <sup>b</sup>	4,534	\$590.3	2008	Government conveyed units, leased land, and contributed \$70.7 million. Developer to construct 2,040 units, renovate 2,394 units, and own, operate, and maintain all units for 50 years.	No	No	No

**Appendix II  
Details on 12 Housing Privatization Projects**

*(Continued From Previous Page)*

Service, project, location, and award date	Total housing units after initial development period	Total estimated initial development cost (in millions)	Estimated completion date for initial development period	Project description	At the time of our visit, was project		
					Development progress on schedule?	Meeting occupancy expectations?	Renting units to parties other than military families?
Marine Corps, Camp Pendleton III and Yuma, California and Arizona, Oct. 2004 <sup>b</sup>	897	\$85.5	2006	Government conveyed units, leased land, and contributed \$18.6 million. Developer to construct 253 units, renovate 257 units, and own, operate, and maintain all units for 50 years.	Yes	Yes	No
Marine Corps, Tri-Command, South Carolina, Mar. 2003	1,718	\$175.9	2007	Government conveyed units, leased land, and contributed \$26.5 million. Developer to construct 491 units, renovate 1,227 units, and own, operate, and maintain all units for 50 years.	Yes	No	No

**Appendix II**  
**Details on 12 Housing Privatization Projects**

(Continued From Previous Page)

Service, project, location, and award date	Total housing units after initial development period	Total estimated initial development cost (in millions)	Estimated completion date for initial development period	Project description	At the time of our visit, was project		
					Development progress on schedule?	Meeting occupancy expectations?	Renting units to parties other than military families?
Air Force, Robbins Air Force Base, Georgia, Sept. 2000	670	\$56.5	Completed	Government conveyed units and land, provided \$22.3 million loan, and provided a guarantee on the private loan. Developer constructed 370 units, renovated 300 units, and will own, operate, and maintain the units for 50 years.	Initial development completed	No	Yes
Air Force, Patrick Air Force Base, Florida, Oct. 2003	552	\$120.6	2008	Government conveyed units and land. Developer to construct 552 units and own, operate, and maintain the units for 50 years.	No	No	Yes

Source: DOD.

<sup>a</sup>The original scope for the South Texas project was 665 units and the original completion date for the initial development period was February 2005. The project agreement was modified in August 2004.

<sup>b</sup>We did not visit the Quantico or Yuma portions of these projects.



# Comments from the Department of Defense



ACQUISITION,  
TECHNOLOGY  
AND LOGISTICS

## OFFICE OF THE UNDER SECRETARY OF DEFENSE

3000 DEFENSE PENTAGON  
WASHINGTON, DC 20301-3000

APR 10 2006

Mr. Barry Holman  
Director, Defense Capabilities and Management  
U.S. General Accounting Office  
Washington, D.C. 20548

Dear Mr Holman,

This is the Department of Defense (DOD) response to the GAO draft report GAO-06-438, "MILITARY HOUSING: Management Issues - Require Attention as the Privatization Program Matures," dated March 1, 2006.

Thank you for allowing us to comment on your draft report. I consider the report a important contribution to our oversight of the 58 projects and 121,000 units that have been privatized to date. These projects have allowed us to tap private sector resources and initiative to eliminate over 91,000 inadequate housing units. In these projects over \$1 billion dollars of government contribution has generated over \$14 billion in housing development. The report undertook an assessment of whether opportunities exist to improve our oversight of awarded housing privatization projects and to what extent projects are meeting occupancy standards.

On the issue of oversight, the Program Evaluation Plan (PEP) and report is the Department's primary tool for evaluating the program's effectiveness in leveraging appropriations, reducing housing deficits, eliminating inadequate housing, and appropriately implementing the legislative authorities. It is not intended to provide real time project oversight. That is the role of the portfolio management systems of the military services. We are generally pleased with your assessment of how the services are implementing their systems. Where you have identified shortcomings, we will act forthrightly to address them.

Occupancy rates in privatized housing is also an issue worth addressing. The revitalization of housing through privatization and the five-year increase in housing allowances (enactment of the privatization program preceded the initiative to increase allowances) should bring about a tremendous improvement in the quality of life of military service members. It has also expanded their housing options significantly and given them more opportunity to "vote with their feet," in choosing housing. As we transition from models of government ownership of largely inadequate housing, to private ownership of largely inadequate housing, to private ownership of excellent housing, our housing requirements determination process must be informed by the actual housing preferences of the service members. A housing survey of all service members can assist this understanding. More important though is an understanding that the housing is being transferred to private ownership. Private sector landlords and the lenders



that finance them respond quickly to vacancies. Our requirements determination process must continue to understand the effects of the housing revitalization and increase in allowances and it must adjust accordingly.

If you have any questions regarding the attached report please contact me at (703) 602-3669.



Joseph K. Sikes  
Director, Housing and Competitive  
Sourcing

GAO-06-438

**“MILITARY HOUSING: MANAGEMENT ISSUES – REQUIRE ATTENTION AS  
THE PRIVATIZATION PROGRAM MATURES”**

**DEPARTMENT OF DEFENSE COMMENTS  
TO THE RECOMMENDATIONS**

**RECOMMENDATION 1:** The General Accounting Office (GAO) recommended that the Secretary of Defense direct the Deputy Under Secretary of Defense (Installation and Environment) to require the Navy to upgrade the monitoring and oversight of its housing privatization program to ensure consistency, completeness, and preparation of appropriate portfolio summary performance reports.

**DOD RESPONSE:** Partially concur. We recognize the need to improve the system to ensure accurate reporting. The Navy is striving to achieve a balance between the appropriate levels of government oversight while maintaining limited governmental involvement. The Navy had begun a comprehensive review of potential enhancements to portfolio management prior to initiation of the GAO review. Navy representatives have met with their counterparts in the Army and Air Force to review their portfolio management approaches and are working to incorporate best industry practices.

However, we disagree with the assumption that, because summary annual portfolio briefings were not prepared or that Program Evaluation Report (PEP) input contained errors, the Navy was at risk of not being aware of potential problems with projects. Senior leadership within both the Navy and Marines are frequently briefed on ongoing potential issues. The following information is provided regarding some of the specific findings cited in the draft report.

The Navy's privatized portfolio average occupancy rate for the first quarter of fiscal year 2006 was 93%. With the exception of the Northeast Region and South Texas, with occupancy rates of 88% and 78% respectively, all Navy privatization projects' occupancy rates were above 90% during this time period. The Marine Corps' privatized portfolio average occupancy rate for the first quarter of fiscal year 2006 was 92%. With the exception of Tri-Command, with an occupancy rate of 81%, all Marine Corps privatization projects occupancy rates were at or above 90%.

The GAO finding that Kingsville II project funds in the amount \$50,282.49 were not properly distributed was corrected in September 2005. The Navy's general partner has agreed to audit revisions that will permit early detection of any issues, and will provide Navy additional data in the future to ensure correct financial distributions.

The Navy's South Texas limited partner was not invoiced for fire and police services for 2004 and 2005 until February 10, 2006, and the general partner paid the full amount March 2, 2006. The GAO draft report incorrectly states that services were not invoiced or reimbursed for services provided in 2002 and 2003. The Navy's installations and

regions have worked to ensure that provisions have been established to properly invoice the general partner for all reimbursable services.

A review conducted by the Navy, and their Military Housing Privatization Initiative (MHPI) business consultant, of their remaining projects noted that the issues identified at Kingsville II and South Texas were isolated incidents and not a systemic problem. Additional guidance is being developed for internal reviews of audits and financial data from general partners to ensure accurate monitoring and oversight of distributions. Further, while we agree that PEP reports should be accurate, and will aggressively seek to improve accuracy in its reports, we believe those errors did not subject Navy projects to increased risk.

**RECOMMENDATION 2:** The GAO recommended that the Secretary of Defense direct the Deputy Under Secretary of Defense (Installations and Environment) to improve the value of DOD's privatization program evaluation report by streamlining the report to focus on key project performance metrics, completing the report on time, and obtaining periodic independent verification of key report elements.

**DOD RESPONSE:** Concur. In 2001, we initiated the semi-annual PEP report to monitor overall MHPI program performance. It has evolved over time to meet the needs of the accelerating MHPI program, as it has matured. While the PEP is intended to oversee broad program performance, the service portfolio management systems oversee the well-being of individual projects. In the summer of 2003, we implemented a work plan which improved the PEP process used to identify issues and validate observations. Under that work plan methodology, key report elements are reviewed and evaluated by consultant support. The services are asked to respond to our questions and observations via the PEP Memorandum of Observations. In 2005, with an overabundance of data we decided to streamline the PEP report and respond to a new Congressional semi-annual reporting requirement. We reduced the PEP report from over 300 pages to a PEP Executive Report of 19 pages to focus on key project performance metrics. The first PEP executive report (draft) was provided to GAO on February 8, 2006 and a final version was submitted to Congress on March 31, 2006.

**RECOMMENDATION 3:** The GAO recommended that the Secretary of Defense direct the Deputy Under Secretary of Defense (Installations and Environment) provide guidance to the services to help ensure consistent collection and reporting of housing satisfaction information from all service members, which would allow for benchmarking and tracking of tenant satisfaction over time as well as for making service-to-service comparisons.

**DOD RESPONSE:** Partially Concur. Tenant survey guidance already exists in the PEP instructions. We will revise that guidance to include a five-point numerical system, which will be consistent across the Services.

The military services collect tenant satisfaction data which supports their specific, negotiated business structures. That data is suited to their specific incentive structures and would not be suitable to overlay a program-wide directive on the individual projects.

However, we concur with the recommendation to collect information on the housing preferences of all service members, not simply those occupying privatized housing. We believe it is important to re-evaluate member housing preferences driven by increased allowances and housing revitalization; it makes sense to consistently collect housing preferences of all service members. An Office of Secretary of Defense Housing panel has been studying how to best implement such a survey.

**RECOMMENDATION 4:** The GAO recommended that the Secretary of Defense direct the Deputy Under Secretary of Defense (Installations and Environment) determine how increased housing allowances from the zero-out-of-pocket initiative will most likely impact future family housing requirements and provide guidance on how the impacts should be factored into the services' housing requirements assessments.

**DOD RESPONSE:** Concur. The five-year initiative (2000-2005) to increase housing allowances has been implemented. Every housing requirements and market analysis (HRMA) since 2003 has used the projected five-year basic allowance for housing (BAH) as the maximum allowable housing cost (MAHC), thus accounting for the zero out-of-pocket initiative. The examples cited in the report are for projects which preceded full implementation of that guidance. With more money in their pockets, military service members base their housing choices upon many factors, including their household income, the condition and affordability of available housing, the ratio of military to civilian population, and commute time. Further, member housing choices during the initial development phases of privatization projects, while housing is still inadequate, likely do not reflect actual demand. With increased housing allowances in place and housing being revitalized every day, we will closely observe vacancy rates. If vacancy rates rise, their impact could, for example, be captured by an increase in the MAHC in the requirements determination process which would tend to reduce project scope. The trend over the last two years has been a decrease in the number of units included in MHPI projects.

**RECOMMENDATION 5:** The GAO recommended that the Secretary of Defense direct the Deputy Under Secretary of Defense (Installations and Environment) to expedite issuance of the revised DOD housing management manual and ensure that the revision includes guidance to improve the reliability of housing requirements assessments and reduce the scope of the exceptions provided to the use of available community housing.

**DOD RESPONSE:** Concur. Policy for conducting requirements assessments was issued by Deputy Secretary in January 2003 and has been applied to every housing project since issuance. Housing manual revisions are underway which will address the exceptions identified by the report. Due to the increasingly important role of privatization in DOD housing, we found it necessary to do a broader revision of the manual than we had originally planned. We expect to complete the manual and issue it by the end of calendar year 2006. Notwithstanding final issuance of the manual, regular interim improvements have been made to the original housing policy. These improvements are applied in reviewing the HRMAs for every housing privatization project.

# GAO Contacts and Staff Acknowledgments

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## GAO Contact

Barry W. Holman, (202) 512-5581 ([holmanb@gao.gov](mailto:holmanb@gao.gov))

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## Acknowledgments

In addition to the person named above, Mark A. Little, Assistant Director; Janine M. Cantin; Susan C. Ditto; Gary W. Phillips; and Sharon L. Reid also made major contributions to this report.

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