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Improved Procedures Needed For Justifying Lease Acquisitions Of Federal Buildings

General Services Administration

UNITED STATES
GENERAL ACCOUNTING OFFICE

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FEB. 13, 1975

UNITED STATES GENERAL ACCOUNTING OFFICE
WASHINGTON, D.C. 20548

LOGISTICS AND COMMUNICATIONS DIVISION

B-95136

The Honorable Arthur F. Sampson
Administrator of General Services

Dear Mr. Sampson:

This is our report on improved procedures needed for justifying General Services Administration's lease acquisitions of Federal buildings.

We want to invite your attention to the fact that this report contains recommendations to you which are set forth on page 11. As you know, section 236 of the Legislative Reorganization Act of 1970 requires the head of a Federal agency to submit a written statement on actions he has taken on our recommendations to the House and Senate Committees on Government Operations not later than 60 days after the date of the report and to the House and Senate Committees on Appropriations with the agency's first request for appropriations made more than 60 days after the date of the report.

We are sending copies of this report to the Director, Office of Management and Budget; the House and Senate Committees on Government Operations, Appropriations, and Public Works; and the Subcommittee on Treasury, Postal Service, and General Government, Senate Committee on Appropriations.

Sincerely yours,

F. J. Shafer

F. J. Shafer
Director

Contents

ABBREVIATIONS

GAO	General Accounting Office
GSA	General Services Administration
IRS	Internal Revenue Service
OMB	Office of Management and Budget
PBS	Public Buildings Service
SSA	Social Security Administration

GENERAL ACCOUNTING OFFICE
REPORT TO THE ADMINISTRATOR
OF GENERAL SERVICES

IMPROVED PROCEDURES NEEDED FOR
JUSTIFYING LEASE ACQUISITIONS
OF FEDERAL BUILDINGS
General Services Administration

DIGEST

WHY THE REVIEW WAS MADE

The General Services Administration (GSA) acquires buildings for Federal departments and agencies by Federal construction, purchase contract, or leasing. GSA is authorized to lease, for periods up to 20 years, existing buildings or buildings to be erected by private developers for Government use.

Government-leased space under GSA's control has increased during recent years. From fiscal year 1966 through 1974, leased space increased from 44.6 million square feet to 67.4 million square feet. As of June 30, 1974, the cost of leased space under GSA's management was about $323 million a year.

One of the major reasons for increased leasing has been the budgetary restrictions on GSA's construction programs. (See p. 1.)

GAO reviewed GSA procedures for justifying Federal leasing and focused on four large privately constructed facilities leased to GSA in 1970 and 1972.

The four facilities selected were the Brookhaven, New York; Fresno, California; and Memphis, Tennessee, Internal Revenue Service (IRS) data centers and the Birmingham, Alabama, Social Security Administration (SSA) payment center. GSA's long-term leases for the four facilities cost about $11.7 million a year.

GAO compared GSA's procedures for justifying leasing of the four facilities with its current procedures by reviewing two proposals sent to the Congress in 1974 justifying the leasing of buildings in Columbia, South Carolina, and Jackson, Mississippi. (See p. 2.)

FINDINGS AND CONCLUSIONS

Analyses of lease versus construction costs

To support its decision to lease, GSA furnished the Congress with present-value analyses of estimated costs of leasing versus estimated costs of Federal construction and ownership. These analyses indicated that leasing was the less costly alternative for all buildings reviewed.

GAO found that the present-value analyses sent to the Congress did not consider differences in the timing of cash payments and outlays under the lease and under

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Federal construction. In addition, some analyses contained faulty estimates.

In estimating Federal construction costs, GSA provides for expected price increases from the date of analysis to the anticipated date of the contract award. GSA does not, however, discount the construction costs to give recognition to the time when payments under a contract will be made. It assumes that payments for Federal construction would be made in a lump sum at the date of analysis.

Although it is proper to anticipate Federal construction cost increases beyond the date of analysis when award is scheduled for the future, it is inconsistent to then view all costs as occurring on the date the analysis is made.

Payments start only after contract award and continue throughout the construction period. Therefore, to provide the Congress with an accurate comparison of investment choices, future cash payments should be recognized as applicable to the years in which they actually occur and discounted to their present value. (See pp. 3 to 9.)

If the GSA analyses were adjusted to

--consider the period when future cash outlays would actually occur and

--correct computational errors,

then Federal construction and ownership, rather than leasing, would have been identified as the less costly alternative for each of the four facilities leased in 1970 and 1972. (See apps. II to V.)

When a discount rate based on the cost of U.S. Treasury borrowing as measured by the average yield on outstanding marketable long-term Treasury obligations is used in the analyses for the four facilities, Federal construction and ownership is shown as the most favorable alternative by greater amounts.

In a lease versus construction comparison, when the Government is attempting to select the least expensive way to finance an investment, the average yield on outstanding marketable Treasury obligations--with remaining maturities comparable to the analysis period--is a fair indication of the Government's cost of money and is an acceptable basis for establishing the discount rate. (See pp. 9 and 11.)

In the two analyses submitted to the Congress in 1974 justifying the proposed leasing of buildings to be constructed in Columbia and Jackson, GSA also provided for increases in Federal construction costs from the date of analysis to the anticipated date of contract award, but again it did not discount these Federal construction costs.

The analyses indicated that leasing was the less costly alternative by $5.33 million for the proposed building in Columbia and by $14.85 million for the building in Jackson.

If the GSA analyses were adjusted for differences in the timing of future cash outflows and occupancy dates, Federal construction and ownership would have been shown as the more favorable alternative by $1.2 million for the building in Columbia and leasing as the more favorable alternative by $9.06 million for the building in Jackson. (See pp. 10 and 11.)

Tax-exempt public ownership

GSA has advised the Congress that a leased building constructed and owned by a private developer, in contrast to a Government-owned building, strengthens the local property tax rolls because a privately owned building would not be tax exempt.

GSA assumes that:

--The owner of a leased building will pay property taxes, as well as local, State, and Federal income taxes.

--These taxes would be forgone when the Federal Government owns rather than leases the building.

The Brookhaven and Memphis IRS data centers and the Birmingham SSA payment center are leased to GSA by local public organizations that are exempt from property and Federal income taxes.

To finance acquisition of the three facilities, these organizations have issued, or plan to issue, tax-exempt bonds (exempt from Federal income taxes) which they propose to redeem over 20-year periods from rentals paid by GSA.

If the Federal Government had financed construction through the sale of Treasury or GSA bonds, interest on these obligations would be subject to Federal income taxes and, therefore, command a higher interest rate. (See pp. 12 and 13.)

RECOMMENDATIONS AND SUGGESTIONS

GAO recommends that, in future lease versus construction cost analyses, GSA:

--Discount cost estimates to more closely correspond to the timing of anticipated cash payments.

--Use a discount rate based on the average yield on outstanding marketable Treasury obligations with remaining maturities comparable to the analysis period. (See p. 11.)

CHAPTER 1

INTRODUCTION

The Federal Property and Administrative Services Act of 1949, as amended (40 U.S.C. 490), and Executive orders issued pursuant to the act direct the Administrator of General Services to initiate and maintain plans and programs for effectively and efficiently acquiring buildings for Federal agencies. Buildings are acquired by Federal construction, purchase contract, or lease. The act specifically authorizes the Administrator to enter into leases, not to exceed 20 years, for accommodating Federal agencies in buildings in existence or to be erected by lessors.

In fiscal year 1963 a lease-authorization procedure was established requiring the General Services Administration (GSA) to obtain prospectus approval of the Public Works Committees of the Congress for the lease of buildings for Federal agencies when the estimated construction costs exceed $200,000. In 1972 the law was amended to require prospectus approval of all leases having an annual rental in excess of $500,000. A prospectus contains information about the need for a project, estimated cost or rental information, and other data.

Government-leased space under GSA's control has increased during recent years. From fiscal year 1966 through 1974, leased space increased from 44.6 million square feet to 67.4 million square feet. As of June 30, 1974, GSA managed about 226 million square feet of space (excluding parking), of which 30 percent was leased for about $323 million a year.

Budgetary restrictions on construction have been a major reason for increased leasing. Construction expenditures are historically the first items to be eliminated when demands on the national budget are unusually great.

In September 1969 the Subcommittee on Public Buildings and Grounds, Senate Committee on Public Works, held hearings on 14 prospectuses submitted by GSA, including those covering the 4 projects we reviewed.

To justify the choice of leasing over constructing, GSA furnished to the Congress comparative analyses of the costs of Federal construction and ownership versus the costs of leasing, using the present-value method of analysis.

The present-value method of analysis is generally recommended by economists and systems analysts for evaluating alternatives, such as lease or construction. The Office of Management and Budget (OMB) also requires present-value analyses to support decisions to lease or purchase general-purpose real property, and it prescribes the discount rate for use in these analyses.

SCOPE OF REVIEW

Our review was directed toward determining whether the procedures and assumptions GSA used to compare the costs of leasing and the costs of constructing were reasonable and resulted in the most economical acquisition.

We selected for review four large buildings GSA had leased in 1970 and 1972, namely, Brookhaven, New York; Fresno, California; and Memphis, Tennessee, Internal Revenue Service (IRS) data centers and the Birmingham, Alabama, Social Security Administration (SSA) payment center. These buildings were constructed by private developers at a cost of $77 million and leased by GSA for long terms at about $11.7 million a year. We compared the procedures followed in justifying leasing of the four facilities with current GSA procedures by reviewing prospectuses submitted to the Congress in 1974 for the proposed leasing of buildings in Columbia, South Carolina, and Jackson, Mississippi.

CHAPTER 2

LEASE VERSUS CONSTRUCTION

COST ANALYSES NEED IMPROVEMENT

To justify its choice of leasing over Federal construction, GSA was required by Congress to furnish present-value analyses of the costs of leasing versus the costs of Federal construction and ownership. These analyses indicated that leasing was the less costly alternative for all buildings we reviewed.

The present-value analyses sent to the Congress did not consider differences in the timing of cash payments and outlays under the lease and under Federal construction. Some analyses contained faulty cost estimates. If these analyses were adjusted to consider the timing of cash outlays and if computational errors were corrected, leasing would not have been identified as the less costly alternative in most cases. Moreover, had the discount rate been based on the cost of U.S. Treasury borrowings, as measured by the average yield on outstanding marketable long-term Treasury obligations, Federal construction and ownership would have been shown as the more favorable alternative by greater amounts.

SELECTION OF A DISCOUNT RATE

Selecting an appropriate discount rate has been a major problem in present-value comparisons. For Federal Government program analysis and decisionmaking, arguments have been presented for rates ranging from as low as the cost of borrowing by the Treasury to as high as rates of return earned in the private sector of the economy. Because the discount rate used has a direct and overriding effect on the results and conclusions of a comparison of lease and construction costs, the choice of an appropriate rate is of great importance. As a rule, Federal construction and ownership will be more economically advantageous as the discount rate decreases; conversely, leasing normally will be more economically advantageous as the discount rate increases.

1970 AND 1972 LEASES

The prospectuses for the four facilities covered in our review justified leasing on the grounds that, because of budgetary restrictions, it was unlikely that funds for construction would be available in the foreseeable future. To further justify the choice of leasing, GSA was required by the Congress to furnish present-value analyses of the costs of leasing versus the costs of Federal construction and ownership. The analyses indicated that leasing was the less costly alternative.

In 1969 GSA initially requested and obtained approval to lease the four facilities for 20 years at a total rent of $115.9 million. (See app. I.) The GSA lease versus construction analyses submitted at the request of the Congress indicated that Federal construction and ownership costs would exceed 20-year leasing costs. However, GSA used estimated rental rates in the analyses which later proved to be greatly understated. All offers from potential lessors exceeded the estimated rental amounts approved by the Congress. Furthermore, GSA's computation errors involving two of the facilities resulted in an overstatement of $3.2 million in Federal construction cost estimates used in the 1969 analyses.

During 1970 and 1971 GSA submitted revised prospectuses to the Congress to obtain approval for higher rentals. In the revised analyses submitted with the prospectuses, GSA increased the estimated rentals (undiscounted lease cost) from $115.9 million to $237.2 million to more accurately reflect the rates it would expect to pay. (See app. I.) Leasing would no longer have been indicated as more economical than construction had GSA not increased its estimated Federal construction costs (improvements) from $76.1 million to $112.6 million--$22.8 million caused by price escalation, $3.5 million by computational error, and $10.2 million by other changes.

In the revised analyses, GSA increased Federal construction (improvement) cost estimates to provide for price escalation from the date of analysis to the anticipated date of contract award because it assumed that the contract would be awarded about 1-1/2 years after the analyses for the three IRS data centers were sent to the Congress and 2-1/2 years for the SSA payment center. However, GSA did not discount Federal construction contract payments to take into account the timing of the payments which would start after contract award and continue throughout the construction period of about 3 years. Instead, GSA assumed that payment of the full contract amounts would be made at the date of analysis.

GSA also assumed that other outlays under the Federal construction and ownership alternative--such as repairs and improvements and real estate taxes--would start at the date of analysis and continue for 20 years. Such outlays actually would begin after construction was completed, which we estimate would be about 5 years after the analyses were sent to the Congress.

GSA assumed that leasing outlays would begin at the date of analysis. However, actual rentals would start when the leased facilities were constructed and accepted for occupancy--1-1/2 years after the analysis date for the three IRS data centers and 2-1/2 years for the SSA payment center.

Leasing costs understated in 1969 analyses

In September 1969, at the request of the Subcommittee on Public Buildings and Grounds, Senate Committee on Public Works, GSA submitted present-value analyses for 11 proposed leasing projects, including the 4 we reviewed. Calculations were made at 4-7/8-, 6-, and 8-percent discount rates.

According to an OMB official, the policy of using such analysis in determining whether lease or purchase is most economical is an appropriate and wise policy. He further stated:

> "Examination of the present value analysis for the 11 lease projects at the preferred 8 percent rate shows all except one project clearly favored for leasing. With the consideration of non-economic factors in addition to the economic analysis, even the borderline project is justified for leasing."

GSA's analyses supporting its decision to lease the four facilities showed that Federal construction and ownership costs would exceed 20-year leasing costs by $30.1 million when future outlays of cash were discounted at 8 percent. (See app. I.) When 6-percent and 4-7/8-percent discount rates were used, Federal construction and ownership costs exceeded leasing costs by $15.3 million and $4.6 million, respectively.

GSA prepared the cost estimates for the four projects in August 1969. Construction costs for the Memphis IRS data center were based on a prototype. Construction costs for the Fresno and Brookhaven IRS data centers were developed by applying appropriate area cost indexes and by making other adjustments to the Memphis estimate. Federal construction cost estimates for the SSA payment center were based on past estimating procedures and building cost indexes.

Annual leasing cost estimates were based on the cost of acquiring similar facilities from 1961 to 1969 at other locations. The estimated lease costs later proved to be significantly understated. All offers from potential lessors exceeded the estimated rental amounts approved by the Congress.

Revised analyses did not consider differences in timing of cash outlays

During 1970 and 1971, GSA submitted revised prospectuses to the Congress for approval to lease the four facilities at higher rental rates. The revised prospectuses for the three IRS data centers were submitted in April 1970 and for the SSA payment center in June 1971.

We found that GSA used a different approach in estimating Federal construction costs (improvements) in the revised 1970 and 1971 analyses. These estimates included an increase expected because of price escalation from the date of analysis to the anticipated date of Federal construction contract award. The 1969 analyses did not include provision for price escalation.

In the revised analyses, GSA increased the estimated Federal construction costs by about 26 percent, or $22.8 million, to provide for price increases from the date of analysis to the anticipated date of contract award. (In its estimates for the IRS data centers, GSA used a price escalation rate of 12 percent a year from August 1969 to October 1971.) Because the scope of the SSA payment center was changed after the 1969 estimate, GSA prepared a new estimate for that facility in 1971 and also increased that estimate by about 26 percent to cover the period from the date of analysis, May 1971, to the anticipated date of contract award, October 1973. (GSA used a price escalation rate of 12 percent a year for 1971 and 10 percent a year for the remainder of the period.)

GSA's errors in preparing cost estimates caused an overstatement of Federal construction costs included in the analyses. These errors caused the 1969 estimate of Federal construction (improvement) cost of $17.7 million for the Memphis IRS data center to be overstated by about $2.6 million. The 1970 construction cost was overstated by $3.5 million because it was obtained by increasing the 1969 estimate which itself was in error. The 1969 Federal construction cost estimate of $13.4 million for the SSA payment center was overstated by about $600,000. (The 1971 estimate for the SSA payment center was not based on escalated 1969 estimates and, therefore, did not contain a similar overstatement.)

In May 1974 we brought these overstatements to the attention of a GSA official who acknowledged that the estimates were incorrect. He said the errors occurred because GSA did not have sufficient time to prepare and review the estimates.

In the analyses submitted with the revised prospectuses, calculations showing leasing as the less costly alternative were made at discount rates of 8 and 10 percent for the three IRS data centers and at 8 and 12 percent for the SSA payment center. The revised analyses showed that 20-year leasing costs were more economical than Federal construction and ownership by $10.8 million when future cash outlays were discounted at 8 percent (see app. I) and by even greater amounts at the higher percentages. However, if 4-7/8 and 6 percent had been used (as they were in the 1969 analyses), leasing would no longer have been shown as the more economical alternative.

The higher discount rates used in the revised analyses exceeded the increase in the Government's cost of money since the 1969 analyses date, as measured by the average yield on outstanding marketable long-term Treasury obligations. The average yield on long-term Treasury obligations was 6 percent in August 1969, 6.5 percent in April 1970, and 6 percent in May 1971. (As mentioned previously, in a lease versus construction present-value analysis, higher discount rates usually favor leasing.)

OMB Circular A-104, dated June 14, 1972, provides guidance to Federal agencies in preparing present-value analyses for determining whether facilities should be leased or constructed. The circular does not specifically provide for incorporating in construction cost estimates the expected price escalations for the period leading up to the anticipated date of Federal construction contract award and then discounting of construction contract payments over the construction period. However, an OMB official told us that increasing construction cost estimates for expected price increases up to the anticipated date of contract award was proper. He also stated that discounting contract payments over the construction period was consistent with the circular.

We believe that it is proper to provide for expected price increases in estimating Federal construction costs beyond the date of the analysis. It is, however, inconsistent to then view all these costs as occurring on the date the analysis is made. Rather, the cash payments should be recognized as applicable to the years in which they will occur and discounted to their present value to provide the Congress with an accurate cost comparison between investment choices.

If the GSA analyses are adjusted to consider the difference in the timing of cash outlays and to correct the computation error in the estimate for the Memphis IRS data center, Federal construction and ownership, not leasing, would be shown as the less costly alternative for the four facilities when future outlays are discounted at 8 percent. The results are shown below and in more detail in appendixes II through V.

	Analyses reported by GSA (leasing less costly)	Analyses revised by GAO (construction less costly)
	(millions)	
Memphis IRS data center	$ 0.52	$5.28
Fresno IRS data center	4.19	0.05
Brookhaven IRS data center	1.74	2.14
Birmingham SSA payment center	4.31	.10
	$10.76	$7.57

Following are explanations and reasons for certain assumptions and amounts used to adjust the preceding cost comparisons.

1. Construction (improvement) cash outlays were assumed to begin 2 years after analyses were prepared and sent to the Congress. These outlays were then discounted over a 3-year period. We assumed that 14 percent of the cash outlays would be made in the first year, 33 percent in the second year, and 53 percent in the third year. The percentage used for each year is an average amount based on the payment record for six GSA construction projects. These percentages and the construction periods would vary for individual projects.

2. Payments of real estate taxes and payments for repairs and improvements would start when Federal construction was completed, or 5 years after the analysis was prepared.

3. For the Birmingham SSA payment center, occupancy under the Federal construction and ownership alternative would take place about 3 years later than under the leasing alternative. Therefore, to make the analysis periods comparable, discounted lease payments were extended 3 years and the 3-year cost of occupying existing space as shown on the prospectus was added to the Government ownership alternative.

4. For the three IRS data centers, lease payments were discounted for 20 years starting 2 years after the analysis

was prepared--the anticipated date that the lease facility would be ready for occupancy.

The comparative analysis could be made even more accurate by discounting the lease payments for 23 years and including in the Federal construction and ownership alternative the cost of occupying existing space for 3 years. According to the prospectuses, however, no estimate of current housing costs was available because the data centers were new installations.

Discount rate based on cost of Treasury borrowing

If, in addition to the above adjustments, the revised GSA analyses are adjusted further by using a discount rate based on the cost of Treasury borrowing, as measured by the average yield on outstanding marketable long-term Treasury obligations, then Federal construction and ownership is shown as the more favorable alternative by greater amounts.

	Reported by GSA--8-percent discount (leasing less costly)	Revised by GAO: 8-percent discount (construction less costly)	Revised by GAO: Discount based on Treasury's borrowing cost (construction less costly) (note a)
	(millions)		
Memphis IRS data center	$ 0.52	$5.28	$ 8.5
Fresno IRS data center	4.19	0.05	3.3
Brookhaven IRS data center	1.74	2.14	6.2
Birmingham SSA payment center	4.31	.10	6.2
	$10.76	$7.57	$24.2

[a]In April 1970, the long-term Treasury bond rate was 6-1/2 percent, and this rate was used in the revised analyses for the three IRS data centers. In June 1971, when the analysis for the SSA payment center was sent to the Congress, the rate was 6 percent.

In a lease versus construction comparison, when the Government is attempting to select the least expensive way to finance an investment, the average yield on outstanding marketable Treasury obligations--with remaining maturities comparable to the analysis period--is a fair indication of the Government's cost of money and is an acceptable basis for establishing the discount rate.

CURRENT PRACTICE

In estimating Federal construction costs since 1970, GSA has provided for expected price increases from the date of analysis to the anticipated date of the contract award. GSA, however, has not discounted the construction costs to give recognition to the period when cash payments under a contract would be made. It assumes that such payments are made in one lump sum at the date of the analysis.

The foregoing practice is reflected in two recent examples in which there are differences in occupancy dates and timing of cash outlays for the leasing and Federal construction alternatives.

GSA submitted a prospectus to the Congress on March 15, 1974, for leasing a building to be constructed in Columbia, South Carolina. The lease was for 20 years starting January 1, 1976, at an annual rental of $2,740,163. GSA's analysis indicated that 20-year leasing was $5.33 million less costly than Federal construction and ownership. (See app. VI.)

On May 7, 1974 GSA sent a prospectus to the Congress for the leasing of a building to be constructed in Jackson, Mississippi. The lease was for 20 years at an annual rental of $2,361,600 starting January 1, 1976, the date the leased building would be ready for occupancy. The present-value analysis of alternative methods of acquisition--Federal construction, lease, or purchase contract--indicated that leasing would cost about $18.82 million less than Federal construction and ownership over a 30-year period using an OMB-prescribed discount rate of about 9 percent. Because the initial analysis contained errors, GSA submitted a revision in July 1974 which showed leasing to be more economical by $14.85 million. (See app. VII.)

In the above analyses GSA provided for increases in Federal construction costs from the date of analysis to the anticipated date of contract award--July 1975 for the building in Columbia and January 1976 for the building in Jackson. GSA did not, however, discount Federal construction costs to the contract award date and during the construction period to correspond to the timing of the construction payments.

We believe that it is proper to reflect in estimated Federal construction costs the impact of price escalations beyond the date of analysis and up to the date of contract award. Such estimates should be discounted to correspond with the timing of payments. If the analyses were adjusted for differences in the timing of future cash flows and occupancy dates, Federal construction and ownership would have been shown as the more favorable alternative by $1.2 million for the building in Columbia (see app. VI) and lease as the more favorable alternative by $9.06 million for the building in Jackson. (See app. VII.)

CONCLUSION

To provide the Congress with accurate cost comparisons of investment alternatives, GSA estimates of future costs should be discounted to more closely correspond with the timing of cash outlays. Construction cash payments start after a contract has been awarded and normally continue during the construction period. These payments should not be viewed as occurring in a lump sum at the date the analysis is made.

The present-value analysis provides the appropriate basis for evaluating lease versus construction alternatives that differ in the timing of cash requirements. One of the major problems in using present-value comparisons is selecting an appropriate discount rate. We believe that, in comparing lease and construction costs preparatory to selecting the least expensive way of financing a facility, the average yield on outstanding long-term marketable Treasury obligations is a fair indication of the Government's cost of money and is an acceptable basis for establishing a discount rate.

RECOMMENDATIONS TO THE ADMINISTRATOR OF GENERAL SERVICES

We recommend that, in future lease versus construction cost analyses, GSA:

- --Discount cost estimates to more closely correspond to the timing of anticipated cash payments.
- --Use a discount rate based on the average yield on outstanding marketable Treasury obligations with remaining maturities comparable to the analysis period.

CHAPTER 3

TAX-EXEMPT PUBLIC OWNERSHIP

OF FACILITIES

In favor of leasing, GSA has, in the past, advised the Congress that a leased building constructed and owned by a private developer, in contrast to a Government-owned building, strengthens the local property tax rolls since a privately owned building is not tax exempt. GSA assumes that (1) the owner of a leased building will pay property taxes, as well as local, State, and Federal income taxes, and (2) these taxes would be forgone when the Federal Government owns rather than leases the building.

Three of the four facilities reviewed--the Brookhaven and Memphis IRS data centers and the Birmingham SSA payment center--are leased to GSA by local public organizations which are exempt from property and Federal income taxes. The private developer who built the Memphis IRS data center and the Birmingham SSA payment center for lease to GSA sold his interest in these properties to tax-exempt local public organizations soon after GSA leased these properties. The Brookhaven IRS data center was leased by GSA directly from the town of Brookhaven.

To finance acquisition of the three facilities, the local public organizations have issued, or plan to issue, tax-exempt bonds (exempt from Federal income taxes) which these organizations propose to redeem, periodically, over the 20-year lease periods from rentals paid by GSA. If the Federal Government had financed construction through the sale of Treasury or GSA bonds, interest on these obligations would be subject to Federal income taxes and therefore command a higher interest rate. The local public organizations had an advantage over private financing and ownership because of the lower interest rate and the exemption from income and property taxes.

For the Memphis IRS data center, GSA awarded a contract to a private developer on June 26, 1970, to lease space in a building to be constructed by December 1971. This building was to be constructed in accordance with Government plans and specifications on a 50-acre site owned by the Memphis-Shelby County Airport Authority.

On September 9, 1970, the developer entered into an agreement with the Memphis-Shelby County Airport Authority (owner of the building site) whereby the Industrial Development Board of the City of Memphis and the County of Shelby would be formed to issue tax-exempt bonds to finance construction of the data center. This method of financing was contingent upon the Development Board's obtaining (1) required approval to issue tax-exempt bonds, (2) GSA's consent to the sale of the lease, and (3) rulings by IRS that the interest payable by the Board on its revenue bonds would be tax-exempt, that the income of the Board would not be subject to tax, and that the Board would not be required to file a tax return.

The Development Board was successful in obtaining required approvals and project financing. It sold $14 million in tax-exempt bonds in January 1971 at an interest rate of 5.5866 percent. The Board's official statement of December 22, 1970, relating to the bond issue showed that, over the 20-year lease period, the Board would pay from GSA rentals (1) indebtedness of $14 million, (2) interest cost of $10.47 million, (3) other expenses of $5.72 million, and (4) $9.11 million to the Airport Authority--a total of $39.3 million.

GSA's PRESENT-VALUE ANALYSIS OF FEDERAL

CONSTRUCTION COMPARED WITH LEASING

FOR FOUR FACILITIES (note a)

	Presented at Senate hearings May 1970 (note b)	Presented at Senate hearings September 1969	Difference
Construction and ownership costs:			
Improvements (note c)	$112,562,000	$ 76,098,000	$ 36,464,000
Site, design, etc. (note c)	15,065,000	11,233,000	3,832,000
Repair and improvements	4,017,000	3,008,000	1,009,000
Real estate taxes	20,044,000	15,412,000	4,632,000
Less residual value	-24,487,000	-18,777,000	-5,710,000
Present value	127,201,000	86,974,000	40,227,000
Lease payments:			
Total outlay	237,179,000	115,907,500	121,271,500
Present value	116,432,000	56,898,000	59,534,000
Leasing less costly (present value)	$ 10,769,000	$ 30,076,000	

[a]Three IRS data centers and one SSA payment center.

[b]Data for the Birmingham SSA payment center was presented by GSA to the Public Works Committees of the Congress in June 1971.

[c]Under assumption that outlays would be made at the date of the analysis, these costs are not discounted.

Note: 20-year lease and 8-percent discount rate.

PRESENT-VALUE ANALYSIS OF

FEDERAL CONSTRUCTION COMPARED WITH LEASING

MEMPHIS IRS DATA CENTER

	Presented by GSA at Senate hearings May 1970	Revised by GAO (note a)	Difference
Construction and ownership costs:			
Improvements	[b]$23,503,000	[c]$14,325,000	$9,178,000
Site, design, etc.	[b]2,091,000	2,091,000	-
Repair and improvements	814,000	554,000	260,000
Real estate taxes	5,766,000	3,922,000	1,844,000
Less residual value	-5,490,000	-3,737,000	-1,753,000
Present value	26,684,000	17,155,000	9,529,000
Lease payments:			
Total outlay	53,298,000	53,298,000	-
Present value	26,164,000	22,432,000	3,732,000
Leasing less costly (present value)	$ 520,000		
Construction and ownership less costly (present value)		$ 5,277,000	

[a]See p. 8 for an explanation of the basis used to adjust GSA's analysis.

[b]These costs were not discounted by GSA because it assumed that outlays would be made in a lump sum at the date of the analysis.

[c]Adjusted by GAO for $3.5 million error in construction cost estimates. Construction cost discounted to correspond more closely with anticipated cash outlays.

Note: 20-year lease and 8-percent discount rate.

PRESENT-VALUE ANALYSIS OF

FEDERAL CONSTRUCTION COMPARED WITH LEASING

FRESNO IRS DATA CENTER

	Presented by GSA at Senate hearings May 1970	Revised by GAO (note a)	Difference
Construction and ownership costs:			
Improvements	[b]$28,317,000	[c]$20,230,000	$8,087,000
Site, design, etc.	[b]2,851,000	2,851,000	-
Repair and improvements	814,000	554,000	260,000
Real estate taxes	5,891,000	4,009,000	1,822,000
Less residual value	-6,686,000	-4,551,000	-2,135,000
Present value	31,187,000	23,093,000	8,094,000
Lease payments:			
Total outlay	54,990,000	54,990,000	-
Present value	26,995,000	23,144,000	3,851,000
Leasing less costly (present value)	$ 4,192,000		
Construction and ownership less costly (present value)		$ 51,000	

[a]See p. 8 for an explanation of the basis used to adjust GSA's analysis.

[b]These costs were not discounted by GSA because it assumed that outlays would be made in a lump sum at the date of the analysis.

[c]Construction cost discounted to correspond more closely with anticipated cash outlays.

Note: 20-year lease and 8-percent discount rate.

PRESENT-VALUE ANALYSIS OF

FEDERAL CONSTRUCTION COMPARED WITH LEASING

BROOKHAVEN IRS DATA CENTER

	Presented by GSA at Senate hearings May 1970	Revised by GAO (note a)	Difference
Construction and ownership costs:			
Improvements	[b]$31,494,000	[c]$22,499,000	$8,995,000
Site, design, etc.	[b]3,508,000	3,508,000	-
Repair and improvements	814,000	554,000	260,000
Real estate taxes	4,584,000	3,114,000	1,470,000
Less residual value	-7,508,000	-5,111,000	-2,397,000
Present value	32,892,000	24,564,000	8,328,000
Lease payments:			
Total outlay	63,450,000	63,450,000	-
Present value	31,148,000	26,704,000	4,444,000
Leasing less costly (present value)	$ 1,744,000		
Construction and ownership less costly (present value)		$ 2,140,000	

[a]See p. 8 for an explanation of the basis used to adjust GSA's analysis.

[b]These costs were not discounted by GSA because it assumed that outlays would be made in a lump sum at the date of the analysis.

[c]Construction cost discounted to correspond more closely with anticipated cash outlays.

Note: 20-year lease and 8-percent discount rate.

PRESENT-VALUE ANALYSIS OF

FEDERAL CONSTRUCTION COMPARED WITH LEASING

BIRMINGHAM SSA PAYMENT CENTER

	Presented by GSA at Senate hearings June 1971	Revised by GAO (note a)	Difference
Construction and ownership costs:			
Improvements	[b]$29,248,000	[c]$20,895,000	$8,353,000
Site, design, etc.	[b]6,615,000	6,615,000	-
Repair and improvements	1,575,000	965,000	610,000
Real estate taxes	3,803,000	2,588,000	1,215,000
3-year occupancy cost	-	[d]1,981,000	-1,981,000
Less residual value	-4,803,000	-4,047,000	-756,000
Present value	36,438,000	28,997,000	7,441,000
Lease payments:			
Total outlay	65,441,000	[d]75,257,000	-9,816,000
Present value	32,125,000	29,095,000	3,030,000
Leasing less costly (present value)	$ 4,313,000		
Construction and ownership less costly (present value)		$ 98,000	

[a]See p. 8 for an explanation of the basis used to adjust GSA's analysis.

[b]These costs were not discounted by GSA because it assumed that outlays would be made in a lump sum at the date of the analysis.

[c]Construction cost discounted to correspond more closely with anticipated cash outlays.

[d]To make analysis periods comparable, leasing outlays were extended by 3 years and current occupancy costs for 3 years were added to the ownership alternative.

Note: 20-year lease and 8-percent discount rate.

PRESENT-VALUE ANALYSIS OF

FEDERAL CONSTRUCTION COMPARED WITH LEASING

COLUMBIA FEDERAL OFFICE BUILDING

	On GSA's prospectus	Revised by GAO (note a)	Difference
Construction and ownership costs:			
Improvements	[b]$20,223,000	[c]$16,613,000	$3,610,000
Site, design, etc.	[b]5,070,000	5,070,000	-
Management and inspection	1,382,000	1,135,000	247,000
Operation maintenance and repair	9,215,000	4,910,000	4,305,000
Real estate taxes	5,866,000	4,647,000	1,219,000
2-year occupancy cost	-	[d]1,068,000	-1,068,000
Less residual value	-4,993,000	-5,233,000	240,000
Present value	36,763,000	28,210,000	8,553,000
Lease payments:			
Total outlay	54,803,000	[d]60,284,000	-5,481,000
Present value	31,430,000	29,366,000	2,064,000
Leasing less costly (present value)	$ 5,333,000		
Construction and ownership less costly (present value)		$ 1,156,000	

[a]See p. 11 for an explanation of the basis used to adjust GSA's analysis.

[b]These costs were not discounted by GSA because it assumed that outlays would be made in a lump sum at the date of the analysis.

[c]Construction cost discounted to correspond more closely with anticipated cash outlays.

[d]To make analysis periods comparable, leasing outlays were extended by 2 years and current occupancy costs for 2 years were added to the ownership alternative.

Note: 20-year lease and 6-percent discount rate.

PRESENT-VALUE ANALYSIS OF

FEDERAL CONSTRUCTION COMPARED WITH LEASING

JACKSON FEDERAL OFFICE BUILDING

	On GSA's prospectus (note a)	Revised by GAO (note b)	Difference
Construction and ownership costs:			
Improvements	[c]$21,080,000	[d]$14,656,000	$6,424,000
Site, design, etc.	[c]3,973,000	3,465,000	508,000
Repair and improvements	1,740,000	680,000	1,060,000
Real estate taxes	8,225,000	5,024,000	3,201,000
4-year occupancy costs	-	[e]2,497,000	-2,497,000
Less residual value	-2,052,000	-1,374,000	-678,000
Present value	32,966,000	24,948,000	8,018,000
Lease payments:			
Total outlay	70,848,000	[e]80,294,000	-9,446,000
Present value	18,118,000	15,890,000	2,228,000
Leasing less costly (present value)	$14,848,000	$ 9,058,000	

[a]GSA used OMB rate of 7 percent for discounting future ownership outlays and about 9 percent for future lease outlays.

[b]See p. 11 for an explanation of the basis used to adjust GSA's analysis.

[c]These costs were not discounted by GSA because it assumed that outlays would be made in a lump sum at the date of the analysis.

[d]Construction cost discounted to correspond more closely with anticipated outlays.

[e]To make analysis periods comparable, leasing outlays were extended by 4 years and current occupancy costs for 4 years were added to the ownership alternative.

Note: 30-year lease.

PRINCIPAL OFFICIALS OF
THE GENERAL SERVICES ADMINISTRATION
RESPONSIBLE FOR ACTIVITIES DISCUSSED IN THIS REPORT

	Tenure of office	
	From	To
ADMINISTRATOR OF GENERAL SERVICES:		
Arthur F. Sampson	June 1973	Present
Arthur F. Sampson (acting)	June 1972	June 1973
Rod Kreger (acting)	Jan. 1972	June 1972
Robert L. Kunzig	Mar. 1969	Jan. 1972
Lawson B. Knott, Jr.	Nov. 1964	Feb. 1969
COMMISSIONER, PUBLIC BUILDINGS SERVICE:		
Walter A. Meisen	Oct. 1974	Present
Larry F. Roush	Aug. 1973	Oct. 1974
Larry F. Roush (acting)	Jan. 1973	Aug. 1973
John F. Galuardi (acting)	July 1972	Jan. 1973
Arthur F. Sampson	Mar. 1970	June 1972
Arthur F. Sampson (acting)	Dec. 1969	Mar. 1970
Raymond F. Myers	June 1969	Dec. 1969

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