

DOCUMENT RESUME

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General Services Administration's Practices for Altering Leased Buildings Should Be Improved. LCD-78-338; B-118623. September 14, 1978. Released September 18, 1978. 29 pp. + 3 appendices (7 pp.).

Report to Rep. Jack Brooks, Chairman, House Committee on Government Operations; by Elmer B. Staats, Comptroller General.

Issue Area: Increase in the Amount of Govt. Leased Space Despite Congress' Emphasis on Federal Construction. (710).

Contact: Logistics and Communications Div.

Budget Function: General Government: General Property and Records Management (804).

Organization Concerned: General Services Administration.

Congressional Relevance: House Committee on Government Operations. Rep. Jack Brooks.

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The General Services Administration (GSA) leases about 91.3 million square feet of space to accommodate Federal departments and agencies at annual rents of \$455 million. In fiscal year (FY) 1977, obligations for alterations to leased buildings were in excess of \$36 million. Findings/Conclusions: The following deficiencies in GSA's contracting practices for altering leased buildings were identified: excessive use of sole-source contracting with the building owners for alterations; not preparing independent Government estimates to aid in negotiating contract prices; a single organizational unit responsible for preparing estimates, negotiating contracts, approving payments, and inspecting work; performing major alterations before lease expiration without attempting to renegotiate the lease period or the rent; failure to adequately consider purchase for construction of alternate space; paying rent while space was not available for occupancy; and failure to document inspections of alteration work. As a result of reviews and investigations, GSA instituted a new policy requiring competitive procurement and issued new procedures for inspecting alteration work. If properly implemented, these actions may correct some of the deficiencies. The Economy Act of 1932 limits the amount that may be expended on alterations in a leased building, but it has not been effective in accomplishing this. Requiring specific congressional authorization of alterations would be more effective. GSA funding practices for alteration work have not always been sound, and yearend obligations for FY 1977 may be invalid or misclassified. Recommendations: The Administrator, GSA, should: obtain certificates of current cost and pricing data for lessors for negotiated lease alteration

contracts over \$100,000; insure that independent cost estimates are prepared and prices negotiated for contracts and change orders before work starts; establish a procedure to insure that consideration is given to renegotiating the rent and lease period prior to contracting for major alterations; require a cost comparison of alternatives before investing large sums in alterations; limit the use of letter contracts as a means of obligating yearend fund balances; and take steps to insure that accelerated yearend spending is avoided, yearend obligations are valid, and budgetary controls and contracting procedures are followed. The Congress should amend the Public Buildings Act of 1959 to require congressional authorization of alterations which involve a total expenditure in excess of \$500,000 and amend the Economy Act of 1932 to eliminate provisions relating to the 25% limitation on alterations to rented buildings. (Author/HTW)

REPORT BY THE

Comptroller General

OF THE UNITED STATES

General Services Administration's Practices For Altering Leased Buildings Should Be Improved

The House Committee on Government Operations asked GAO to review alterations made to buildings leased by the General Services Administration. In fiscal year 1977, obligations for such alterations were in excess of \$36 million.

GAO found various deficiencies in General Services' contracting practices—sole-source contracting; not adhering to sound contracting procedures and practices; failure to consider purchase or construction prior to major alterations; and performing major alterations before lease expiration without attempting to renegotiate the lease period or rent.

In the agency's rush to obligate funds, several yearend obligations may be invalid or misclassified. GAO also found that the Economy Act limitation is not effective in limiting and controlling alterations to leased buildings.



LCD-78-338

SEPTEMBER 14, 1978



COMPTROLLER GENERAL OF THE UNITED STATES
WASHINGTON, D.C. 20548

B-118623

The Honorable Jack Brooks
Chairman, Committee on
Government Operations
House of Representatives

Dear Mr. Chairman:

This report is in response to your February 28, 1978, request that we review alterations made to buildings leased by the General Services Administration.

At your request, we did not take the additional time needed to obtain written agency comments on the matters discussed in this report. As arranged with your office, we are sending copies of this report to Representative Berkley Bedell. Unless you publicly announce its contents earlier, no further distribution of this report will be made until 10 days from the date of the report.

Sincerely yours,

A handwritten signature in black ink, appearing to read "Thomas B. Stebbins".

Comptroller General
of the United States

COMPTROLLER GENERAL'S
REPORT TO THE
COMMITTEE ON
GOVERNMENT OPERATIONS
HOUSE OF REPRESENTATIVES

GENERAL SERVICES
ADMINISTRATION'S PRACTICES
FOR ALTERING LEASED BUILDINGS
SHOULD BE IMPROVED

D I G E S T

This report concerns various deficiencies found in the contracting practices of the General Services Administration for altering buildings it leases. General Services leases about 91.3 million square feet of space at annual rent of \$455 million to accommodate Federal departments and agencies. Obligations for alterations to leased space were in excess of \$36 million in fiscal year 1977 and GAO found various deficiencies in the General Services' contracting practices. These included:

- Excessive use of sole-source contracting with the building owners for alterations. (See p. 3.)
- Not preparing independent Government estimates to aid in negotiating contract prices. (See p. 5.)
- A single organizational unit responsible for preparing estimates, negotiating contracts, approving payments, and inspecting work. (See p. 8.)
- Performing major alterations before lease expiration without attempting to renegotiate the lease period or the rent. (See p. 8.)
- Failure to adequately consider purchase or construction of alternate space. (See p. 11.)
- Paying rent while space was not available for occupancy. (See p. 13.)
- Failure to document inspections of alteration work. (See p. 14.)

General Services justified sole-source contracting on the basis that it would be impractical for it to contract for work which affects building systems (heating, air-conditioning, etc.) and continue to hold the building owner responsible for the maintenance of these systems.

General Services should avoid contracting for alterations on a sole-source basis with building owners. Alteration contracts should, if possible, be awarded on an advertised competitive basis or the owners should be required to obtain bids from contractors and subcontractors. Then the owners could contract with the lowest responsible bidder acceptable to General Services.

When GAO completed its fieldwork in June 1978 General Services had underway various reviews and investigations of procurement functions and allegations of fraud. According to the agency these reviews and investigations indicated a need to strengthen procedures for accomplishing alteration projects in leased buildings. The Administrator of General Services issued a policy memorandum on June 29, 1978, which requires the agency to award contracts and make sales only as a result of formal advertising or competitive negotiations. Also GSA issued new procedures for inspecting alteration work. If the revised policy on contracting and new procedures for inspections are properly implemented, they will correct many of the deficiencies cited in this report. (See pp. 15 to 17.)

The Economy Act of 1932 limits the amount that may be expended on alterations in a leased building to 25 percent of the first year's rent. This amount may be exceeded if justified by the agency.

The Economy Act limitation on alterations to leased buildings should be repealed because it is not an effective mechanism for limiting and controlling the amount expended for building alterations. The limitation is easy to exceed and sizable amounts are spent on alterations. For example, the 25-percent limitation was exceeded and extensive alterations were made

to a leased building at a cost of \$2.15 million to convert it to a laboratory facility. The alterations required almost 2 years to complete during which time the building was unoccupied and General Services paid rent of about \$407,800. The total cost of the alterations, including rent paid while the building was vacant, was about \$2.55 million or about \$61 a square foot, which exceeded the appraised value of the building when leased of \$1.57 million, or \$37.50 a square foot.

Requiring specific congressional authorization of alterations to leased buildings would be more effective and consistent with the law which requires congressional approval of alterations to Government-owned buildings in excess of \$500,000. Alterations to a leased building requires closer scrutiny because they (1) may increase the value of the leased building which the Government does not own and (2) weaken the agency's negotiating position for follow-on leases. (See pp. 19 to 22 and pp. 30 to 34.)

General Services had too much flexibility in funding alteration work in leased buildings in fiscal year 1977. In addition to funds made available by tenant agencies, several Federal Buildings Fund accounts were used. Greater emphasis seems to have been placed on obligating available funds balances by the end of fiscal year 1977 than on adhering to sound contracting practices and effective budgetary controls. Several yearend obligations may be invalid or misclassified. In April 1977 the Commissioner of the Public Buildings Service notified the regions that he was concerned about large unobligated balances in three accounts. The regions were urged to obligate available funds before the end of the fiscal year. The regions responded to the push and the level of obligations increased significantly in September, the last month of the fiscal year. For example, in Region 3, obligations for alterations and major repair funds increased from a monthly average of \$4.4 million for 11 months to \$9.3 million in September, an increase of 11. percent. For another account,

about \$4.1 million, or 51 percent of the total amount, was obligated for alterations in September 1977, with \$3.1 million during the last 15 days of the fiscal year.

GAO is currently considering a question raised by General Services on the propriety of using rental funds for alterations in leased buildings.

RECOMMENDATIONS

The Administrator of General Services should:

- Obtain certificates of current cost and pricing data from lessors for negotiated lease alteration contracts over \$100,000. (See p. 18.)
- Insure that independent cost estimates are prepared and prices negotiated for contracts and change orders before work starts. (See p. 18.)
- Establish a procedure to insure that consideration is given to renegotiating the rent and lease period prior to contracting for major alterations. (See p. 18.)
- Require a cost comparison of alternatives--purchase, construction, or lease--before investing large sums in leased building alterations. (See p. 18.)
- Limit the use of letter contracts as a means of obligating yearend fund balances consistent with the criteria in the Federal Procurement Regulations. (See p. 29.)
- Take appropriate steps to insure (1) that accelerated yearend spending is avoided, (2) that yearend obligations are valid, and (3) that budgetary controls and contracting procedures are followed. (See p. 29.)

The Congress should:

--Amend section 7 of the Public Buildings Act of 1959 (40 U.S.C. 606) to require congressional authorization of alterations to leased space which involve a total expenditure in excess of \$500,000. This change will make the law consistent with the approval process required for alterations in Government-owned buildings. (See p. 22.)

--Amend the Economy Act of 1932 (40 U.S.C. 278a) to eliminate the provisions relating to the 25-percent limitation on alterations, improvements, and repairs to rented buildings. (See p. 22.)

Upon request, GAO will furnish suggested language for changing the law. As the Committee requested, GAO did not take the additional time necessary to ask the agency for comments on this report.

C o n t e n t s

DIGEST	<u>Page</u>
CHAPTER	i
1 INTRODUCTION	1
Scope of review	2
2 QUESTIONABLE PRACTICES FOLLOWED IN ALTERING LEASED BUILDINGS	3
Excessive sole-source contracting for alterations	3
Procedures followed by the State of California	5
Independent Government estimates not prepared	5
Cost estimates prepared after prices were negotiated or work done	6
Contracts awarded after alterations were substantially completed	6
GSA estimates prepared from lessors' proposals or not at all	7
Alteration functions performed by the same organizational unit	8
Performing major alterations before lease expiration	8
Crystal Plaza No. 2 Arlington, Virginia	9
Gramax Building Silver Spring, Maryland	10
Pershing Point Plaza Atlanta, Georgia	11
Failure to adequately consider purchase or construction of alternate space	11
Bureau of Alcohol, Tobacco and Firearms laboratory, Rockville, Maryland	12
Mat Land Office and Laboratory Building, Glenn Dale, Maryland	12
E-1 Building, Reston, Virginia	13
Computers and laboratories in leased buildings	13
Paying rent while space was not available for occupancy	13

CHAPTER		<u>Page</u>
	Willste Building	
	Silver Spring, Maryland	14
	Lack of documentation for alteration inspections	14
	GSA revised procedures for alterations in leased buildings	
	GSA's new procedures for alteration inspections	15
	Conclusions	16
	Recommendations	17
	Conclusions	18
3	LEGAL LIMITATION ON ALTERING RENTED SPACE	19
	Economy Act limitation is not effective in limiting alterations in leased buildings	19
	Certificate of determination	19
	Alteration cost not recorded	20
	Congressional approval of alterations in Government-owned buildings	21
	Conclusions	21
	Recommendations to the Congress	22
4	YEAREND SPENDING FOR ALTERATIONS	23
	Reprogramming of funds	23
	Budget Activity 53 - Rental of Space	23
	Budget Activity 54 - Alterations and Major Repairs	24
	Budget Activity 61 - Real Property Operations	24
	Accelerated yearend obligations	27
	Invalid obligations	27
	Conclusions	29
	Recommendations	29
 APPENDIX		
I	Leased building 1401 Research Boulevard Rockville, Maryland	30
II	Schedule of rental and alterations for selected GSA-leased buildings	35
III	Letter dated February 20, 1978, from the Chairman, House Committee on Government Operations	36

ABBREVIATIONS

GAO General Accounting Office
GSA General Services Administration
FPR Federal Procurement Regulations
PBS Public Buildings Service
SMD Space Management Division
OMB Office of Management and Budget
BATF Bureau of Alcohol, Tobacco and Firearms
NRC Nuclear Regulatory Commission

CHAPTER 1

INTRODUCTION

The General Services Administration (GSA) leases about 91.3 million square feet of space at an annual rent of about \$455 million to accommodate Federal departments and agencies. Leasing operations are carried out in 10 regional offices under policy and procedural direction from the GSA Central Office in Washington, D.C.

GSA contracts for alterations (also referred to as improvements, repairs, and alterations) in leased buildings to adapt the space to the tenant agency needs upon initial assignment or to meet changing agency requirements in existing space. This work includes items such as (1) converting office space to computer or laboratory space and (2) space alterations, including partitions, electrical, telephone, lighting, air-conditioning, heating, and ventilating work. Generally alterations to leased buildings have been accomplished by the lessor (owner) who is reimbursed by a lump-sum payment or by increased rent payable throughout the term of the lease.

According to information provided by GSA, obligations for alterations in leased space in fiscal year 1977 were in excess of \$36 million as follows.

	<u>Million</u>
Budget Activity 54--alterations and major repairs	
Reimbursable by tenant agencies	\$16.3
Direct (funded by GSA)	1.7
Budget Activity 53--rental of space (direct)	<u>18.9</u>
Total	<u>\$36.9</u>

The above obligations were for lump-sum payments to building owners and do not include alterations paid through increased rent. In addition, lump-sum alterations were funded from Budget Activity 61--real property operations. GSA identified \$11.5 million obligated from this activity that was used for alterations and overtime services. It could not readily determine what amount was applicable to alterations in leased space. The three activities--alteration and major repairs, rental of space, and real

property operations--are listed as separate line items in the annual appropriation acts and budget submissions.

SCOPE OF REVIEW

By letter dated February 28, 1978 (see app. III), the Chairman, House Committee on Government Operations, requested that we review alterations in leased buildings. He suggested that the review cover

1. the practice and policy of adding major alterations to leased buildings and the effect of these alterations on subsequent lease renewals, and
2. the extent of the practice of the GSA Public Buildings Service (PBS) authorizing the owners of leased buildings to provide alterations rather than PBS procuring alterations through a competitive bid process.

Our review focused on the points raised by the Chairman with emphasis on the timing of alterations, method of contracting, negotiation of prices, use or non-use of Government estimates, method of inspection, compliance with and effectiveness of the Economy Act limitation on alterations, and the push to obligate available funds by the end of fiscal year 1977.

We made our review at GSA Central Office, Washington, D.C.; Region 3, Washington, D.C.; Region 4, Atlanta, Georgia; and Region 9, San Francisco, California.

CHAPTER 2

QUESTIONABLE PRACTICES FOLLOWED

IN ALTERING LEASED BUILDINGS

We found deficiencies in GSA's practices for altering leased buildings. These deficiencies included:

- Excessive use of sole-source contracting with building owners for alterations.
- Not preparing independent Government estimates to aid in negotiating contract prices.
- A single organizational unit responsible for preparing estimates, negotiating contracts, approving payments, and inspecting work.
- Performing major alterations before lease expiration without attempting to renegotiate the lease period or the rent.
- Failure to adequately consider purchase or construction of alternate space.
- Paying rent while space was not available for occupancy.
- Failure to document inspections of alteration work.

EXCESSIVE SOLE-SOURCE CONTRACTING FOR ALTERATIONS

GSA contracted for most alteration work in leased buildings on a sole-source basis with the building owners (lessors). In the absence of competition there was no assurance that the Government received fair and reasonable prices.

GSA's justification for contracting on a sole-source basis was that under the lease terms, the lessor is responsible for maintenance and operation of building systems (heating, air-conditioning, electrical, etc.) and it would be impractical to perform or contract for work which affects those systems, and continue to hold the lessor responsible for the maintenance and operation. Its leasing procedures state that normally the best interests of the Government

will be served by having alterations accomplished by the lessor by increased rental or a lump-sum payment under the original lease or supplement thereto.

Section 302(c) of the Federal Property and Administrative Services Act of 1949, as amended (41 U.S.C. 252) provides that all purchases and contracts for property and services shall be made by advertising. Fifteen exceptions to the use of formal advertising are set forth in the law permitting contracting officers to negotiate contracts. GSA cited one of these exceptions as a basis for contracting without advertising--"(10) for property or services for which it is impracticable to secure competition."

Federal Procurement Regulation (FPR 1-18.102-1) states that construction shall be procured by formal advertising whenever such method is feasible and practicable. When negotiating prices without formal advertising, FPR 1-3.801-1 states:

"It is the policy of the Government to procure property and services from responsible sources at fair and reasonable prices calculated to result in the lowest ultimate overall cost to the Government."

However, the FPR provisions do not apply to leases of real property except in specific cases relating to standard clauses.

The GSA files were not documented in many cases to indicate if meaningful negotiations were conducted with lessors. GSA awarded alteration contracts in many cases in the same amount as the lessors offer. Although lessors did submit offers, they contained varying degrees of detail ranging from a lump-sum amount to itemized schedules. The lump-sum offers did not contain sufficient detail to enable the negotiator to evaluate the reasonableness of prices. GSA did not require lessors to use a competitive process and obtain bids from contractors or subcontractors.

FPR 1-3.807-3 provides that for any negotiated contract over \$100,000 the contractor is to submit written cost or pricing data and certify that to the best of his knowledge and belief that the data submitted is accurate, complete, and current. Since this FPR provision does not apply to negotiated alterations contracted for in leased buildings, GSA did not request certificates of cost and pricing from lessors.

Procedures followed by
the State of California

The State of California uses different methods of contracting for alterations in leased buildings. In some cases involving alterations to existing leased space, the State requires the lessor to obtain competitive bids and then the lessor contracts with the lowest bidder acceptable to the State. In other cases, the State contracts direct for the alterations.

In response to a congressional inquiry, the State outlined briefly the procedure it followed in contracting for alteration work on nine projects.

	<u>Frequency</u>
Lessor acted as general contractor and secured 3 competitive bids for subcontracting parts of the project.	1
Lessor contracted and managed alteration project by competitive bid solicitation.	1
State awarded contracts directly to contractors other than lessors.	3
Lessor acted as his own contractor. State reviewed all alteration costs to verify that they were competitive.	4

In fiscal year 1977, lump-sum payments by the State for alterations were only about \$290,000. GSA spent in excess of \$2 million in California.

INDEPENDENT GOVERNMENT
ESTIMATES NOT PREPARED

GSA's Regions 3 and 9 frequently did not prepare detailed independent cost estimates to aid in negotiating contract prices. This practice, in our opinion, placed the GSA negotiators at a disadvantage in negotiations since it limited their ability to question contractor proposals and evaluate the reasonableness of prices.

FPR 1-18.108 requires that an independent Government cost estimate be prepared for each proposed construction contract (including alteration contracts) with a cost of

\$10,000 or more. The estimate is to be in as much detail as the contractors bid. Although this FPR provision does not apply specifically to alterations in leased buildings, GSA leasing procedures provide that a written staff engineering estimate be prepared for all alteration work. An exception is when the cost does not exceed \$2,500 and the work is to be performed at a remote location or under conditions where it is impracticable to obtain an estimate.

Cost estimates prepared after prices were negotiated or work done

There were several instances where cost estimates were prepared either after the price had been negotiated or the work was done. Details on examples follow. For the Mat Land building in Glenn Dale, Maryland, the lessor performed alteration work under eight work orders at a negotiated price of \$89,406. Estimates were prepared and prices negotiated in March 1978 after the work was completed. GSA regional officials said this was done because staff was not available to prepare cost estimates when needed.

Contracts awarded after alterations were substantially completed

Alterations in a building at 215 Fremont Street, San Francisco, California, involving three contracts, were complete or substantially complete before the lessor submitted his offers to do the work and contracts were awarded. One contract totaling \$63,250 involved overtime services for electricians and related crafts. The overtime services were necessary to meet the telephone company's requirement for installation of service in the leased space. The lessor's offer was dated September 15, 1977. A review of the file and comments from a GSA official indicate the majority of the work was complete by September 30, 1977, the date of the contract award.

In the second contract, the lessor submitted his offer of \$57,397 on November 22, 1977. Again, on December 15, 1977, the lessor wrote to GSA stating that the work had been done prior to October 1, 1977, and requested payment.

In another case, a \$586,890 contract was awarded on September 30, 1977, for alterations to this building. Less than a month later, on October 28, 1977, the lessor wrote GSA requesting payment of \$513,196 for about 87 percent of work completed. Most of this work was completed prior to contract award.

Negotiation of prices after the work is completed could result in "cost plus a percentage of cost" contracting which is prohibited by law.

On another alteration project, GSA negotiated a price of \$45,000. Records indicate that the price was negotiated before March 6, 1975, but they do not show the exact date. The cost estimate was not prepared until March 7, 1975. To make the estimate equal to the negotiated price, it appears that an extra \$4,000 was added for overhead. GSA's procedures allow overhead and profit of 20 percent of labor and material costs, but in this case, the GSA estimate for overhead and profit was 33 percent.

GSA estimates prepared from lessors' proposals or not at all

Several GSA estimates were not truly independent since they were based wholly or in part on lessors' proposals. Independent estimates were not made. GSA estimators recorded their estimates on the lessors' proposals. In other cases, they spot checked selected items for reasonableness. Officials in Regions 3 and 9 stated that staff shortages precluded them from making detailed estimates in all cases.

In connection with the \$586,890 contract for alterations to the building at 215 Fremont Street, the estimate prepared by the Construction Management Division's estimator was based on information obtained directly from the lessor, not on plans and specifications. The estimator visited the lessor's office and reviewed the information available, but he did not prepare an independent Government estimate. GSA Region 9 officials stated that the estimator did not copy the lessor's information exactly, but "massaged" the data he obtained in preparing the Government estimate.

The offer from the lessor did not contain adequate detail. Only line items such as "Plants - \$76,055," "Conference Room Changes - \$20,355," and "Light Fixtures Added - \$45,885" were included. No quantities or unit prices were listed.

In other instances, there was no documentation in the files showing that an estimate was prepared. In the rush to enter into contracts and obligate available funds by the close of fiscal year 1977, GSA did not have the time to prepare independent estimates. (For further discussion see ch. 4.)

ALTERATION FUNCTIONS PERFORMED
BY SAME ORGANIZATIONAL UNIT

The Alterations Branch in GSA Region 3 prepared cost estimates and conducted negotiations for lease alterations in excess of \$10,000 generally using a team approach with one estimator specializing in the electrical aspects of the alteration costs and another preparing mechanical estimates. For 13 of the 15 buildings with Government estimates, one or more alteration contracts were negotiated by two or three negotiators, one of which was the same person who prepared the estimate. The branch was also responsible for making inspections and approving partial and final payments. While a few of the inspections were made by personnel from other branches, most of the inspections and all of the other functions were performed by the same branch.

For alterations under \$10,000, one person, the building manager, not only performed cost estimates and negotiated prices but also awarded contracts, inspection work, and approved payments prior to September 1977. The performance of all these functions by one organization unit or by one person is not good internal control. The assigned duties and functions should be appropriately segregated to provide proper internal checks and insure adherence to sound contracting procedures and practices.

Currently, the functions and responsibilities of the Region 3 Alterations Branch and the building managers offices are under review by GSA. Organizational changes have been made and others contemplated.

PERFORMING MAJOR ALTERATIONS
BEFORE LEASE EXPIRATION

GSA performed major alterations before leases expired without attempting to renegotiate the lease period or the rent. As stated in our prior report (LCD-77-354, January 24, 1978), alterations made shortly before expiration of the lease is poor strategy and weakens GSA's negotiating position on follow-on leases. We reported that competition was almost nonexistent on follow-on leases. GSA usually justified continued occupancy of existing space on the grounds that a move would involve relocation costs, interruption of agency activities, and alteration costs for new space when the Government had already spent considerable amounts of money to make existing space compatible with occupying agencies' operational requirements.

We concluded that GSA should allow sufficient time prior to lease expiration for developing an alternative space plan. This would strengthen GSA's position in negotiating a follow-on lease for continued occupancy of currently leased space.

It is obvious the lessor has an advantageous negotiating position for follow-on leases when he knows the Government is reluctant to move because of alteration costs. The following are examples of major alterations contracted for within 2 years of lease expiration.

Crystal Plaza No. 2
Arlington, Virginia

The space in Crystal Plaza No. 2 is presently occupied by part of the U.S. Patent Office. The lease currently in effect is for 160,700 square feet at a gross annual rent of \$731,185 and it expires on December 7, 1978. GSA plans to negotiate a follow-on lease.

On August 18, 1977, the Patent Office notified the GSA building manager that they were issuing a Request for Proposals for the acquisition of a major computer system and extensive site preparation would be required.

The site renovation plans were delivered to GSA Region 3 on January 26, 1978. On January 31, 1978, a Region 3 official notified the Patent Office they would not approve the plans or the expenditure since the lease rental exceeds \$500,000 and has to be approved by the Congress and the lease expires in December 1978. In a February 3, 1978, letter to the PBS Commissioner, the Department of Commerce asked for help in getting the site renovation plans approved so alterations could begin.

The Director of the Space Management Division (SMD), Region 3, requested guidance from the Central Office as to whether the request made by the Department of Commerce should be approved prior to entering into a new lease.

GSA's Central Office, on April 6, 1978, replied that they had no objection with starting procedures to begin the alterations provided disclosures were not made to the lessor which would compromise the Government's position in the current negotiations for a succeeding lease. Central Office suggested that Region 3 complete as much in-house preparation as possible, pending completion of negotiations. Upon

completion of negotiations for the succeeding lease, SMD should proceed with the project on a competitive basis, including the lessor as a participant. However, on March 9, 1978, about 1 month before the Central Office letter, Region 3 had obtained a detailed cost estimate from the lessor for performance of the alterations. On April 19, 1978, a final alteration price was negotiated with the lessor. On May 7, 1978, the PBS Commissioner gave the approval to begin the alterations prior to negotiating the new lease. Approval was given by the Commissioner because:

- If the computer system was not installed by August 16, 1978, a penalty clause would be invoked which would cost the agency an estimated \$45,000 a month.
- There was no alternative location available to which to move the agency.
- The lessor had agreed to a negotiated price for the first phase of alterations.

GSA issued alteration contracts totaling \$160,756 to the lessor on May 23, 1978. As of June 23, 1978, GSA had not negotiated a new lease with the lessor. Based on the prospectus sent to Congress, the annual net rent could be as high as \$926,000, an increase of \$410,000 (79 percent) over the current net rate.

In this case, GSA will not have an opportunity to develop an alternative space plan to strengthen its negotiating position for the follow-on lease. We believe that prior to contracting for the computer alterations in May 1978, GSA should have attempted to renegotiate the rent rate and lease items.

Gramax Building
Silver Spring, Maryland

The space in the Gramax Building is presently occupied by the National Oceanic and Atmospheric Administration of the Department of Commerce.

The initial lease expired on April 10, 1976. Less than a year before the lease was to expire, GSA contracted with the lessor for \$75,000 of alterations in May 1975. The alterations were for the installation of a computerized weather monitoring facility. The work was completed in

September 1975. GSA did not renegotiate the rent rate prior to contracting for the alterations. GSA entered into a succeeding lease agreement with the lessor to begin on April 11, 1976, for 5 years, with no renewal options. The annual net rent is \$640,094, a 68-percent increase over the previous annual net rent of \$381,107.

Pershing Point Plaza
Atlanta, Georgia

Over \$245,000 was spent for alterations during the last 3 years (January 1, 1974, to November 18, 1976) of a 5-year lease which expired November 30, 1976. A 20-month follow-on lease was then negotiated. During the term of this lease, additional alterations of about \$119,000 were performed by the lessor. Neither of the leases had renewal options.

The GSA Region 4 realty specialist said that an impending reorganization of the tenant agency was the reason for the alterations during the short leases, but that GSA was probably going to continue to lease the space regardless. At the time of our review in June 1978, GSA was negotiating another 12-month extension to the lease.

FAILURE TO ADEQUATELY CONSIDER PURCHASE OR
CONSTRUCTION OF ALTERNATE SPACE

Substantial alterations were made to leased buildings, with alteration costs exceeding buildings' appraised fair market value in two cases. GSA did not prepare comparative cost analyses prior to leasing buildings to determine if purchase or construction of facilities would have been more advantageous to the Government. Section 7 of the Public Buildings Act of 1959, as amended (40 U.S.C. 606), requires GSA to obtain prospectus approval from two congressional committees for leases with net rental in excess of \$500,000. Office of Management and Budget (OMB) Circular A-104, issued June 1972, requires the prospectus to contain a cost analysis comparing leasing to construction or purchase of space. However, the prospectuses for the two buildings reviewed in Region 3 with rentals in excess of \$500,000 did not contain detailed cost analyses.

GSA Region 3 officials indicated construction also was not considered for space with rental less than \$500,000, because GSA does not have sufficient construction funds or enough time for building construction. These officials

stated GSA has approximately \$20 million for construction nationwide, which might only fund one building. Also, the minimum time period from request through completion of construction is 5 years. Purchasing is not a viable alternative because of the substantial funds outlay required in the initial year of purchase, according to the official.

The Federal Property Management Regulations (Part 101-19.002) state that:

"To the maximum extent practical, GSA will plan the construction and alteration of Federal facilities when such action can be shown to be the most prudent and economic means of meeting Federal space requirements."

The following are examples of buildings with substantial alteration costs in relation to appraised value for which cost analyses were not prepared.

Bureau of Alcohol, Tobacco and Firearms
laboratory, Rockville, Maryland

As discussed in appendix I, the Bureau of Alcohol, Tobacco and Firearms laboratory in Rockville, Maryland, had an appraised market value of \$1.57 million. Alterations costing \$2.1 million (contracted with the lessor) and rental during construction of \$400,000 resulted in a total renovation cost of \$2.5 million. Thus, GSA invested \$2.5 million in a leased building that was appraised at \$1.57 million prior to renovation.

Mat Land Office and Laboratory Building
Glenn Dale, Maryland

GSA negotiated a follow-on 20-year lease for the Mat Land Office and Laboratory Building for April 1, 1976, to March 31, 1996, with an option to terminate the lease after 10 years.

The appraised fair market value of the building was \$1,475,000 in May 1967. In January 1976, GSA reviewed the building and confirmed the market value was at least \$1,475,000 but did not state an exact amount. Alterations were required to prepare the space for the Soil Conservation Service. From April 1, 1976, to present, GSA has contracted with the lessor for alterations of \$1,005,000 and plans to award another contract for \$485,000.

Thus, alterations in the Mat Land Office and Laboratory Building will equal \$1,490,000 which exceeds the appraised 1967 market value of \$1,475,000.

E-1 Building, Reston, Virginia

In May 1968, GSA leased the E-1 Building, Reston, Virginia, for occupancy by the U.S. Geological Survey. The lease was from December 1, 1968, to November 30, 1978, with a 5-year renewal option.

The appraised market value of the E-1 Building was \$600,000 in August 1970. Since the lease has been in effect in 1968, alterations costing \$428,000, including \$229,000 for preparation of a computer site, have been performed by the lessor. This is 71 percent of the building's appraised market value of \$600,000.

Computers and laboratories in leased buildings

The Director of SMD, Region 3, indicated that GSA's informal policy requires computer and laboratory facilities to be located in Government-owned buildings whenever possible. Seven of the 18 leased buildings reviewed in Region 3 contained either computer or laboratory facilities. In each case, GSA had determined no adequate Government space was available. However, a cost analysis comparing purchasing or construction to leasing of a building by the Government was not prepared.

PAYING RENT WHILE SPACE WAS NOT AVAILABLE FOR OCCUPANCY

For five Washington area buildings with unoccupied space being altered, GSA paid rent of \$1.8 million. Four of these buildings were vacated by one agency and then converted for occupancy by another agency. GSA paid rent, while the buildings were vacant, of \$223,000 to \$627,000. The other building was leased for initial occupancy for the Bureau of Alcohol, Tobacco and Firearms (see app. I), and rent was paid for approximately 2 years while the space was being converted to a laboratory. Details on one example follow.

Willste Building
Silver Spring, Maryland

GSA leased 117,811 net usable square feet of space in the Willste Building, Silver Spring, Maryland. The lease began on January 10, 1972, through January 9, 1977, at a gross annual rent of \$518,368, with one 5-year renewal option at the same annual rental subject to tax and operating escalation.

The building was occupied by the Federal Bureau of Investigation until August 13, 1975, when they vacated the entire building.

From November 13, 1975, to July 18, 1977, GSA contracted with the lessor to modify the leased space for a new tenant. The space remained totally vacant from August 14, 1975, through June 18, 1976, about 10 months. On June 19, 1976, the Nuclear Regulatory Commission (NRC) began backfilling the vacant space in incremental moves while alterations converting the space for the occupant agency were being completed. On September 14, 1976, GSA exercised its 5-year renewal option beginning January 10, 1977, through January 9, 1982. NRC did not attain total occupancy until July 6, 1977.

Thus, GSA paid rental of approximately \$627,184 during the 23-month period from August 14, 1975, to July 6, 1977, while space was vacant and extensive alterations costing \$705,871 were being completed in the Willste Building.

In a prior report (LCD-77-354, January 24, 1978), we reported similar findings regarding GSA's payment of rent during alterations to unoccupied space.

LACK OF DOCUMENTATION
FOR ALTERATION INSPECTIONS

GSA files lacked documentation for many alteration inspections it claimed to have performed. PBS regulations (PBS P 1600.1) state that progress inspections are necessary when a lessor is required to perform alterations either for rental consideration or on a lump-sum or installment payment basis. Inspections should be scheduled in accordance with the extent of the work involved to ensure the work is performed and progress reports should be submitted regularly to the contracting officer.

According to a GSA official in Region 3, alterations exceeding \$10,000 were usually inspected by a realty specialist during the construction phase and prior to partial payments and always prior to final payment. If the project involved a sophisticated installation, such as a computer, one or more of the estimating engineers from the Alterations Branch would assist in the inspection.

In Region 3, the Chief of the Alterations Branch required that an inspection form be completed after each visit. The form required the inspector to estimate the dollar amount of alterations adequately completed. These forms were not prepared for all inspections. For example, a GSA official stated they performed inspections twice a week, for alterations of \$736,000 at the Friendship 1 Building, Baltimore, Maryland. GSA, however, could not provide documentation that any of the weekly inspections were performed.

According to a GSA official, inspection reports were only prepared when major problems were noted. Without inspection records, GSA cannot properly assess the effectiveness of its inspection program.

The Reimbursable Work Authorization (Form 2957), which authorizes payment of agencies' funds for alterations, requires a signature by a GSA official certifying physical completion of the alterations. This certification implies a final inspection was conducted.

Reimbursable Work Authorizations were usually signed. However, in one building, GSA did not make an inspection prior to approving final payment.

On June 15, 1977, GSA contracted for a conference room costing \$21,692 at the Casimir Pulaski Building in Washington, D.C. GSA made final payment for the conference room without making a final inspection. Subsequently, the lessor's representative informed GSA that the space designated for a conference room was converted to office space before final payment was made. This highlights the need for GSA to make inspections before final payments.

GSA REVISED PROCEDURES FOR ALTERATIONS IN LEASED BUILDINGS

At the completion of our fieldwork in June 1978, GSA had underway various reviews and investigations of procurement

functions and allegations of fraud. According to GSA, these reviews and investigations indicated a need to strengthen procedures for accomplishing alteration projects in leased buildings. On June 29, 1978, the Administrator of General Services issued a policy memorandum which stated in part that:

"* * * it is the policy of this agency to award contracts or to make sales only as the result of formal advertising or competitive negotiation. Sole source procurements or sales are to be avoided except under the most extraordinary circumstances * * *."

Also, on June 29, 1978, the Commissioner of PBS issued instructions to the regions on the revised procedures for alterations in leased buildings. According to these procedures, it is the policy of GSA that all alterations performed in leased buildings be accomplished in accordance with the procurement procedures which generally apply to alterations performed in Government-owned buildings. Alterations in leased buildings, unless performed by force account, will be procured on a competitive basis, either by formal advertising or by competitive negotiations, as appropriate, in accordance with the Federal Procurement Regulations. In extraordinary circumstances where noncompetitive, sole-source contracts with lessors are required, they are to be approved in writing by the Regional Administrator.

Some lessors may object to GSA contracting directly for alterations in their buildings. Several lessors have informed Region 3 that they will not be responsible for the building systems if GSA contracts directly for the alteration work.

GSA's new procedures for alteration inspections

At a May 1978 news conference, the GSA Administrator stated that the agency organized an independent inspection unit to oversee fulfillment of every contract over \$10,000. He said that until recently, it was a common practice to leave the responsibility for inspection to the official who awarded the contract in the first place--a situation which permitted ready abuse.

As of June 1, 1978, inspection of alterations over \$10,000 require a final inspection by a professionally qualified representative of the Construction Management Division. For projects over \$50,000 one unannounced progress inspection in addition to a final inspection by the representative is required. On May 11, 1978, GSA issued procedures stating alterations of less than \$10,000 are to be inspected by at least two members of the cognizant field office. The number of inspections to be conducted by the two field office members is not stated.

The instructions require only two inspections for alterations in excess of \$50,000 and only one inspection for alterations under that amount. In many alterations, the contractor receives several progress payments from GSA during the alterations work. To assure the contractor is not paid for work prior to its accomplishment, inspections prior to progress payments are necessary.

CONCLUSIONS

We believe that GSA should avoid contracting for alterations on a sole-source basis with building owners. Alteration contracts should be awarded on an advertised competitive basis or the owners should be required to obtain bids from contractors and subcontractors. Then the owners could contract with the lowest bidder acceptable to GSA. If properly implemented, the revised GSA policy should accomplish this objective and also correct many of the deficiencies cited in our report.

We believe that the FPR requirement for the furnishing and certification of cost and pricing data should apply to negotiated alteration contracts over \$100,000. In addition independent Government estimates should be prepared before negotiations to aid negotiators to question contractors' proposals and evaluate the reasonableness of prices. To avoid "cost plus a percentage of cost" contracting, contracts and change order prices should be negotiated before the work starts.

The practice of centralizing responsibility for cost estimates, price negotiations, inspections, and payment approvals in one organizational unit does not lend itself to good internal control. GSA's internal control procedures should be strengthened by recent changes in GSA's Region 3 organizational structure and assigned responsibilities.

It is not always possible to avoid paying rent for unoccupied space in cases where alterations are needed following initial occupancy by the Government. However, GSA should minimize the payment of rent for unoccupied space during alterations. In situations such as the BATF laboratory (see app. I), GSA could have avoided paying rent for unoccupied space and obtained more offers by contracting for a completed facility to meet the agency's requirement rather than using a piecemeal approach.

RECOMMENDATIONS

The Administrator of General Services should:

- Obtain certificates of current cost and pricing data from lessors for negotiated lease alteration contracts over \$100,000.
- Insure that independent cost estimates are prepared and prices negotiated for contracts and change orders before work starts.
- Establish a procedure to insure that consideration is given to renegotiating the rent and lease period prior to contracting for major alterations.
- Require a cost comparison of alternatives--purchasing, construction, or lease--before investing large sums in leased buildings alterations.

CHAPTER 3

LEGAL LIMITATION ON

ALTERING RENTED SPACE

The Economy Act of 1932 (40 U.S.C. 278a) limits the amount that may be expended for alterations, improvements, and repairs of rented buildings to not more than 25-percent of the first year's rent. In accordance with section 210 of the Federal Property and Administrative Services Act of 1949, as amended, the 25-percent limitation may be exceeded if a certificate of determination is prepared indicating that work in excess of the limitation is advantageous to the Government in terms of economy, efficiency, or national security. The 25-percent limitation applies to net rent and only to those alterations which are considered to be permanent in nature. The limitation does not apply to temporary alterations.

ECONOMY ACT LIMITATION IS NOT EFFECTIVE IN LIMITING ALTERATIONS IN LEASED BUILDINGS

The Economy Act limitation is not an effective mechanism for limiting and controlling the amount expended for alterations to leased buildings. The limitation was exceeded on most of the leases we reviewed. Automatic approval of certificates of determination and noncompliance with procedures made the limitation ineffective.

Certificate of determination

The certificate of determination justifies expenditures in excess of the 25-percent limitation and explains why alterations are necessary and preferable to other alternative space. Generally, alternative space was not specifically identified.

In practice, the approval of certificates of determination is an automatic process. We did not find any case where one was disapproved.

In Region 3, alterations in excess of the limitation were made to 12 of the 18 leased buildings reviewed. One or more certificates were approved for each building. However, most of the certificates were not approved by the Regional Administrator as required by GSA procedures. Authority

to approve certificates is delegated only to the Regional Administrators.

In Region 9, we reviewed 24 certificates, and found that 9 were approved after alteration contracts were awarded. We found two cases in Region 3 where the certificates were dated after alteration contracts for \$845,000 were awarded.

There was an inconsistency in the application of the act between Regions 3 and 4. Certificates for laboratory alterations were prepared in Region 3 but not in Region 4. In 1969, the Region 4 counsel ruled that to have the Economy Act limitation apply, improvements had "to increase the value of the property." GSA Region 4 leased a laboratory in Miami, Florida, at an annual net rent of \$153,015. Therefore, the 25-percent limitation was \$38,254. About \$700,000 was obligated for alterations to the building in 1976. In the opinion of Region 4 personnel, the alterations did not increase the value of the building and were therefore not subject to the provisions of the Economy Act. The alterations included structural, mechanical, electrical, and plumbing changes that appeared to be permanent in nature. These changes were of the type, we believe, that should increase the value of the building.

Alteration cost not recorded

GSA procedures require that alteration costs be maintained on GSA Form 1626, Record of Expenditures. The purpose of this form is to monitor the expenditures for alterations on each lease and to insure that expenditures do not exceed the 25-percent limitation. The form shows the amount that may be expended before exceeding the limitation. If the balance shown on the Form is less than the amount to cover the planned alterations, the alteration work should either be canceled or justified on a certificate of determination approved by the Regional Administrator.

We found several instances where alteration costs were not recorded and in some cases permanent alterations were misclassified as temporary on the GSA Form 1626. Regional officials recognize that the forms are poorly maintained. They indicate that one of the reasons for not keeping the records current is that the individual responsible for maintaining the record does not always receive notification of the expenditures. All source documents are not processed through the responsible individual. Since the Record of

Expenditures forms are not complete, there is no assurance that the limitation had not been exceeded in many cases. In prior reports, we reported similar findings about inaccurate and incomplete control records maintained by GSA.

Congressional approval of alterations in Government-owned buildings

In accordance with section 7(a) of the Public Buildings Act of 1959, as amended (40 U.S.C. 606), congressional approval is required for the alteration of a public building (Government owned) which involves a total expenditure in excess of \$500,000. In order to secure approval, GSA submits a prospectus justifying the proposed alteration to the House Committee on Public Works and Transportation and the Senate Committee on Environment and Public Works. In accordance with section 11(a) of the act, GSA submits an annual report to the Congress on the status of each approved project.

There is no requirement in the 1959 act for congressional approval of, or reporting on, alteration projects in leased buildings.

CONCLUSIONS

We believe that the Economy Act's 25-percent limitation on alterations to leased buildings should be repealed. Although considerable effort is devoted to preparing justifications for exceeding the limitation and in maintaining records for monitoring compliance, the limitation is not effective. It is easy to exceed, and sizable amounts are expended for alterations to leased buildings.

We believe that congressional authorization of alterations in leased buildings would be a more effective control than the Economy Act limitation. Moreover, such authorization would be consistent with the 1959 act which requires congressional approval of alterations to Government-owned buildings in excess of \$500,000. Alterations to a leased building require closer scrutiny, because some increase the value of the building. Since the alterations are permanently affixed to the building, they cannot be removed when the lease expires. In effect, privately owned buildings are improved at Government expense. In those cases where alterations can be removed, the cost to do so might exceed their residual value. Also, the timing of alterations in leased buildings requires close scrutiny because

of the affect such alterations have on GSA's negotiating position for follow-on leases.

RECOMMENDATIONS TO THE CONGRESS

We recommend that the Congress amend section 7 of the Public Buildings Act of 1959 (40 U.S.C. 606) to require congressional authorization of alterations to leased space which involve a total expenditure in excess of \$500,000. This change will make the law consistent with the approval process required for alterations in Government-owned buildings.

We also recommend that the Congress amend the Economy Act of 1932 (40 U.S.C. 278a) to eliminate the provisions relating to the 25-percent limitation on alterations, improvements, and repairs to rented buildings.

CHAPTER 4
YEAREND SPENDING
FOR ALTERATIONS

In the rush to spend available fiscal year 1977 funds for alterations in leased buildings, several yearend obligations may be invalid or misclassified. Also, poor procurement practices were employed. The GSA Washington and San Francisco regional offices did not, in many cases, conduct meaningful negotiations or prepare independent estimates before contracts were awarded.

REPROGRAMMING OF FUNDS

In fiscal year 1977, GSA used about \$19 million of budget activity 53--rental of space--funds to make lump-sum payments for alterations in leased buildings. GSA did not disclose in its budget justifications or in the appropriation hearings that it would use the funds for this purpose. GSA officials could not cite any authority for the reprogramming of fiscal year 1977 rental of space funds for lump-sum payments. They state that use of rental of space funds is proper for alterations that are amortized over the lease term as part of the rent.

In accordance with GSA procedures, space alterations in Government-owned or leased space over \$200 should be funded from the alterations and major repairs activity and under \$200 from real property operations.

During the fiscal year 1976 hearings, GSA listed projects to be funded from its alteration and major repair activity. These projects included modernization of space, tenant alterations, aids for the handicapped, and other alterations. These projects were the same type as those funded in fiscal year 1977 from budget activity 53--rental of space.

GSA had flexibility in funding fiscal year 1977 alterations to leased buildings. Funding was made available from three budget activities which were described in the budget hearings as follows.

--Budget Activity 53 - Rental of Space. This activity provides for all costs related to the acquisition of

leased space, including payments for existing leases, projected new leases, rental rate increases, and related services furnished by the lessors. It also provides for the payment to the U.S. Postal Service for space occupied by Federal agencies in Postal Service buildings.

--Budget Activity 54 - Alterations and Major Repairs.

This activity provides for alterations and repairs of both Government-owned and leased facilities under the control of GSA. These alterations include initial tenant (space) alterations, fire prevention, and life safety alterations, and alterations to aid the handicapped.

--Budget Activity 61 - Real Property Operations. This activity provides for the operation of GSA-controlled Government-owned and leased facilities. Services furnished include items such as cleaning, minor maintenance, utilities, and fuel.

During the first 3 months of fiscal year 1977 (October thru December 1976), there was a freeze on budget activity 53 funds. Apparently, GSA overestimated the amount it would need to pay in rent in fiscal year 1977. We were told that the freeze was imposed because the manual records system projected that all funds appropriated for rental of space in fiscal year 1977 would be obligated. In January 1977, however, the automated accounting system records showed that all available rental funds would not be obligated and there would be large unobligated balances. At that time, the Assistant Commissioner for Space Planning and Management requested the Commissioner of PBS to approve a change in policy and permit the funding of "lump-sum payments for tenant alterations from the rental of space account"--budget activity 53. The Commissioner approved the request on January 19, 1977.

On February 24, 1977, the Assistant Commissioner for Space Planning and Management informed the regions about the Commissioner's approval of use of rental of space funds for alterations in leased space in fiscal year 1977. He stated that this would permit the reprogramming of alterations and major repair funds to provide for additional alterations in Government-owned space.

The Commissioner of PBS notified the regions in April 1977, that he was concerned about the large unobligated balances in budget activities 53, 54, and 61. The regions were urged to obligate available funds before the end of the fiscal year. His letter to Region 3 stated in part that:

"I have reviewed your region's fund status report, and have found large unobligated balances. Should your present rate of obligations continue unadjusted, there will be a definite adverse impact on the services provided to our tenant agencies. These projected unobligated balances through the second quarter indicate that basic program requirements are not being accomplished.

"For example, based on the FBF [Federal Buildings Fund] Fund Status Reports of February 28, 1977, the following unobligated balances and projections are shown:

Budget Activity	Obligations Through 2/28/77	Estimated Obligations 3/1/77 to 3/31/77	Estimated Cumulative Obligations as of 3/31/77	Allotted To Date	Estimated Unobligated Balance 3/31/77
Rental of Space	\$72,552,146	\$14,510,429	\$87,062,575	\$90,729,400	\$3,666,825
A&MR (Alterations and Major Repairs)	14,645,294	2,546,406	17,193,600	24,011,500	6,817,900
Real Prop. Op.	63,230,550	13,599,250	76,829,800	88,301,100	11,471,300
Program Direction	2,933,644	581,956	3,515,600	4,029,700	514,100

"Rental of Space

The Rental of Space Program (Budget Activity 53) for Region 3 had a projected unobligated balance of \$3,666,825 as of March 31, 1977. This unobligated balance reflects both delays in input into the FBF/AS and delays in the space acquisition program pending assessment of agency priorities * * *.

"Drawing upon your program experience during the first months of this fiscal year, you have had an

opportunity to assess your space acquisition program and that of Federal agencies in your region. I urge you to take every action necessary to achieve a full program for the Rental of Space * * *.

"The funding of space alterations in leased space has been revised so that when it is in the best interest of the Government such alterations may be funded from Budget Activity 53. It is suggested that you (1) carefully examine those space actions which provide the opportunity to reduce future year costs by making lump sum initial space alterations, (2) review and find those known leased locations which require alterations for the handicapped, and/or safety, and (3) identify and fund those locations in which vacant leased space can be altered and assigned. Because these latter two items are closely related to the assignment and utilization program, you may wish to consider rotational assignments for some assignment and utilization personnel to assist the Acquisition Branch. Such action would permit the personnel in acquisition to aggressively pursue the delivery of all pending lease actions. * * *.

"Alterations and Major Repairs

After reviewing your Repair and Alterations Program, I note that you have a projected unobligated balance of \$6,817,900 as of March 31, 1977. I am concerned over the possibility that the funds for projects that you have scheduled for the remainder of the current year may not be obligated. I will be monitoring this situation closely and I may consider reprogramming funds to a region which can obligate the funds this fiscal year * * *. I am planning to call you soon, at which time I will discuss with you the scope of this problem and its potential adverse impact on PBS's program integrity as reviewed by Congress, OMB, and other Federal agencies which look to us for service * * *."

In December 1977 the Commissioner of PBS instructed the regions to fund alterations in leased buildings from budget activity 54, alterations and major repairs. Rental funds are not to be used for lump-sum payments to cover alterations.

We are currently considering a question raised by GSA on the propriety of using rental of space funds for alterations in leased buildings.

ACCELERATED YEAREND OBLIGATIONS

Regions responded to the push to obligate available funds and the level of obligations increased significantly in September 1977. Extensive use was made of letter contracts. For example, in Region 3, the obligations for budget activity 54--alterations and major repairs--increased from a monthly average of \$4.4 million for 11 months to \$9.3 million in September, an increase of 111 percent. This region obligated about \$8.1 million for alterations to leased space from budget activity 53, rental of space. About \$4.1 million, or 51 percent of the total amount, was obligated in September 1977, with \$3.1 million obligated during the last 15 days of the fiscal year.

In Region 9, San Francisco, about \$3.1 million was obligated in September 1977 from budget activity 53 for alterations to leased space, about 91 percent of the total obligations in that region for fiscal year 1977.

Region 4, Atlanta, did not respond to the push to obligate funds in the same manner as Regions 3 and 9. In April 1977, the Commissioner of PBS notified Region 4 that it had an estimated unobligated balance of \$1.2 million in budget activity 53, per the automated accounting system records. The region did not obligate this amount because its manual records showed that virtually all monies in this account were obligated. The manual records were incorrect. At September 30, 1977, Region 4 had an unobligated balance in budget activity 53 of \$1.3 million. Regional officials said that greater expenditures would probably have been made if they were certain that funds were available for obligation.

Invalid obligations

Many of the yearend obligations may not be valid because (1) letter contracts used did not contain the criteria

as required by FPR or (2) contracts were not entered into by September 30, 1977. FPR 1-3.408 states that letter contracts provide for " * * * The immediate commencement of performance of the contract * * *." We found that six Region 3 letter contracts awarded in September 1977, for \$1.6 million did not require immediate commencement of work. These contracts contain clauses which stated:

--A firm fixed price contract will be negotiated at a later date.

--Upon completion of negotiations, this office will issue you a notice to proceed.

In these cases, lessors could not start work until the price was negotiated and a notice to proceed issued by GSA. The Director of Finance, Region 3, stated that the validity of the obligations for the six contracts was questionable.

We also noted that two other GSA letter contracts for \$308,710 contained the clause: "Please acknowledge your acceptance of this contract by signing a copy and returning it to this office."

The letter contracts were dated September 12 and 14, 1977, but were not accepted (signed) by the lessor until November 1977.

In Region 9, five fiscal year 1977 obligations totaling \$122,071 for alterations work were invalid because (1) they were not supported by valid contracts as of September 30, 1977 or (2) the Government had not accepted the lessors offers by that date. Funds totaling \$252,792 for three contracts entered into in July and September 1977 were not obligated as of September 30, 1977. Details on one of these cases for \$131,814 follows:

--On September 16, 1977, GSA authorized the lessor to install art work costing \$131,813.82 in a leased building at 215 Fremont St., San Francisco. On September 30, 1977, GSA contracted for alterations at a cost of \$650,140. It obligated \$650,140 of rental of space funds but it neglected to obligate the \$131,814 to pay for the art work.

In October 1977, the lessor billed GSA \$131,814 for the art work and \$513,396 for part of the alteration work. GSA combined the bills and paid

the lessor \$645,210 with fiscal year 1977 rental of space funds previously obligated. At this time, the obligation balance was \$4,930 (\$650,140 - \$645,210).

When the lessor subsequently billed GSA for the balance of the alteration work, it became apparent that GSA failed to obligate \$131,814 for the art work. On March 22, 1978, GSA obligated \$131,814 of fiscal year 1978 funds from budget activity 61, real property operations, to pay for the remaining portion of the alterations. We believe that this amount should have been charged to alterations and major repairs.

Regional officials agree that alterations and major repair funds should have been charged but at that time budget activity 61 funds were the only available funds to charge.

CONCLUSIONS

GSA had too much flexibility in funding alteration work in leased buildings in fiscal year 1977. In addition to funds made available by tenant agencies, several Federal Buildings Fund accounts were used. GSA, in effect, could pick the account to use. Greater emphasis seems to have been placed on obligating available funds by the end of the fiscal year than in adhering to sound contracting practices and effective budgetary controls.

The practice of using letter contracts as a means for obligating yearend fund balances should be discontinued. Use of these letter contracts should be limited to situations where (1) work has to start immediately and (2) it is not possible to negotiate a definitive contract before the work starts.

RECOMMENDATIONS

The Administrator of General Services should:

- Limit the use of letter contracts as a means of obligating yearend fund balances consistent with the criteria in the Federal Procurement Regulations.
- Take appropriate steps to insure (1) that accelerated yearend spending is avoided, (2) that yearend obligations are valid, and (3) that budgetary controls and contracting procedures are followed.

LEASED BUILDING1401 RESEARCH BOULEVARDROCKVILLE, MARYLAND

On April 20, 1976, GSA leased an entire office building containing 41,867 net usable square feet located at 1401 Research Boulevard, Rockville, Maryland. The lease is for a term of 10 years, starting July 1, 1976, with an option to renew for an additional 10 years. The annual rent is \$209,335 which excludes all services and utilities. The building is used as a laboratory facility by the Bureau of Alcohol, Tobacco and Firearms.

Extensive alterations were made to the building at a cost of \$2.15 million to convert it to a laboratory facility. The alterations required almost 2 years to complete during which time the building was unoccupied and GSA paid rent of about \$407,800. The total cost of the alterations, including rent loss, was about \$2.55 million or about \$61 a square foot, which exceeded the appraised value of the building when leased of \$1.57 million, or \$37.50 square foot.

The basic lease was negotiated based on a single offer. The design and alteration contracts of \$1.7 million were also negotiated and awarded to the lessor on a sole-source basis. The cost consequences of alternatives--purchase, new construction, or lease--were not studied and considered prior to the award of either the lease or the alteration contract.

Congressional approval was not required for this transaction because (1) the annual rent did not exceed \$500,000 and (2) alterations in leased buildings over \$500,000, unlike alterations in Government-owned buildings, do not, in accordance with law, require congressional approval.

Considering the total alteration costs of \$2.55 million, and the rent payable during the lease term, we believe that purchase or construction of a new facility would have been the more favorable alternative. We also believe that when the decision was made to acquire the facility by lease, GSA should have, as one procurement, advertised for and acquired a completed facility ready for Government occupancy rather than procuring it piecemeal on a sole-source basis--first awarding a lease and then contracting for alterations. Details follow.

On June 17 and 18, 1974, GSA's Accident and Fire Prevention Branch of Region 3, made a safety survey of the BATF laboratory then housed in the Internal Revenue Building, 1111 Constitution Avenue, Washington, D.C. In its survey report of July 9, 1974, GSA said that the BATF facility should not be located in buildings used primarily for offices and that consideration should be given to relocating the facility to a building designed for this type of occupancy. The report cited several physical conditions in the facility that created a potential hazard for building occupants. Earlier inspections by BATF in 1973 also disclosed fire hazards for the occupants in the building. On April 10, 1975, BATF submitted a Space Request to GSA for about 40,000 square feet to accommodate the requirements of its laboratories (32,055 square feet) and support facilities (7,945 square feet). BATF stated that it needed the space immediately.

On August 1 and 2, 1975, GSA advertised for listings for 40,000 square feet of modern air-conditioned warehouse or light industrial space that could be conditioned (converted) for laboratory use. This was not a solicitation for offers to lease. In response to advertising, GSA received 11 listings of which it considered 2 to be responsive. GSA and BATF personnel inspected available locations to determine which met the requirements of BATF. On September 18, 1975, BATF informed GSA that two locations (Rockville, Maryland, and Edsall Road, Alexandria, Virginia) are the most acceptable sites visited. GSA was asked to commence negotiations favoring these locations as soon as possible.

Four of the 11 listings were for nonexistent buildings. One was under construction and construction was planned for the other 3. BATF informed GSA that all sites under construction should be eliminated due to the urgency of relocating the laboratory facility and because the proposed buildings were of typical warehouse design which was unsuitable for BATF operations.

GSA complied with BATF's request although this was inconsistent with GSA's advertisement for a modern air-conditioned warehouse or light industrial space that could be conditioned for laboratory use. Moreover, the office building leased at 1401 Research Boulevard resembled a warehouse when all partitions and ceilings and most of the ductwork were removed prior to alteration. We believe that GSA could have leased warehouse space, if available, at a lower rent rate than office space.

One of the buildings GSA eliminated for further consideration was under construction with a scheduled completion of January 1, 1976. It was completed and occupied in March 1976 which was prior to the April 20, 1976, lease award date for the building at 1401 Research Boulevard. We believe that this building should not have been eliminated from further consideration.

GSA prepared a solicitation for offers dated September 29, 1975, which requested offers for 40,000 square feet of space for occupancy "120 days after delivery of approved layout plans on or about June 1976." The solicitation stated GSA would submit the layout plans to the successful lessor who would then renovate the space to laboratories. The lessor was required to submit a lump-sum estimate for this work.

According to GSA records, the solicitation was only sent to owners of the Rockville and Edsall Road properties. The owner of the Edsall Road property withdrew from the solicitation on October 30, 1975, because the building did not provide all of the square footage specified in the GSA solicitation.

Negotiations were conducted with the sole remaining offeror and a lease was awarded on April 20, 1976, which was a year after BATF submitted its Space Request to GSA and almost 2 years after GSA recommended that the BATF facility be relocated.

After the building was leased, GSA incurred about \$2.55 million to convert it to a laboratory facility suitable for BATF, as follows:

	<u>Amount</u>	<u>Cost per square foot (41,867 net usable square feet)</u>
Design work	\$ 60,682	\$ 1.45
Alterations	1,631,346	38.96
Laboratory equipment	384,236	9.18
Moving and other expenses	<u>70,684</u>	<u>1.69</u>
Total alterations	\$2,146,948	\$51.28
Rent paid while building was vacant during altera- tions for almost 2 years	<u>407,773</u>	<u>9.74</u>
Total cost	<u>\$2,554,721</u>	<u>\$61.02</u>

Of the total cost, the tenant agency funded about \$1.27 million and GSA \$1.29 million.

On July 20, 1976, GSA contracted with the lessor, on a sole-source basis, for laboratory design work for alterations of the building. The final cost including change orders was \$60,682.05. Plans and specifications were completed in early 1977. GSA awarded an alteration contract, on a sole-source basis, to the lessor for \$1,507,000 on April 29, 1977. As a result of nine change orders, the contract was increased by \$124,346 to \$1,631,346 on February 17, 1978. GSA officials said that some of the change orders were completed before the prices were negotiated.

During the period July 1, 1976, to June 11, 1978, GSA paid rent of \$407,773 while the building was vacant and alteration work was being done. Generally, rent is not paid until such time as the space is available for occupancy. Therefore, a lessor has an incentive to make necessary alterations quickly.

The solicitation for offers for this lease contained the following standard clause, which is generally incorporated in leases: "Rental shall not be paid by the Government until the entire premises or suitable units therefore have been made ready for use and occupancy * * *."

GSA deleted this clause from the lease. The Statement and Certificate of Award prepared by GSA Region 3 prior to lease award did not contain any justification for deleting this clause.

Delays were encountered in procuring the laboratory equipment. The lessor's architect with the assistance of a laboratory equipment supplier wrote the plans and specifications for the laboratory equipment (casework). These plans and specifications were restrictive because they were written around a given supplier's equipment. Another supplier complained that the Federal Procurement Regulations were being ignored because the equipment specifications were restrictive and therefore precluded other potential suppliers from bidding competitively. A decision was then made that GSA, rather than the lessor, would procure the equipment and that GSA would remove any restrictive language in the plans and specifications. GSA revised the plans and specifications and procured equipment through its Federal Supply Service. As a result, there were delays in the procurement and the delivery of the equipment. At

the completion of our fieldwork in June 1978, not all of the equipment had been procured.

As discussed in chapter 3, the Economy Act's 25-percent limitation on alterations to this building was \$52,333.75. Prior to the alteration contract award, GSA did prepare a certificate of determination in March 1977 justifying exceeding the 25-percent limitation. This certificate was prepared almost a year after the building was leased. Although sizable costs were incurred, none were recorded on Form 1626, Record of Expenditures. As discussed in chapter 3, this form is used to monitor expenditures in leased buildings to insure compliance with the Economy Act.

SCHEDULE OF RENTAL AND ALTERATIONS
FOR SELECTED GSA-LEASED BUILDINGS

<u>Building</u>	<u>Net annual rent</u>	<u>Fiscal year 1975 to Mar. 31, 1978 amount of alterations</u>	<u>Description of alterations</u>
E-1 Reston, Virginia	\$ 72,166-	\$ 229,244-	Space alterations for computer installation.
Casimir Pulaski 20 Mass. Ave. Washington, D.C.	1,211,642-	1,054,502-	Space alterations including photo laboratory equipment and library. An additional \$2.1 million of alteration work is planned.
Railway Labor 400 - 1st St. N.W. Washington, D.C.	246,427-	240,349-	Space alterations.
Friendship No. 3 Baltimore, Maryland	710,764-	1,624,137-	Space alterations to medical facility and polygraph room, fence and sidewalk alterations.
Twinpark Rockville, Maryland	189,774-	372,060-	Space alterations including laboratory facilities.
Gramax Silver Spring, Maryland	640,094-	75,000-	Weather computer facility alterations.
Crystal Plaza No. 2 Arlington, Virginia	515,847-	140,356-	Computer site alterations.
Friendship No. 4 Baltimore, Maryland	1,342,540-	705,749-	Space alterations and driveway resurfacing. An additional \$1.4 million of alterations work is planned.
Union Center Plaza North Bldg. Washington, D.C.	905,103-	526,747-	Alterations including data processing center.
Columbus Miami, Florida	153,015-	715,763-	Space alterations for laboratory facilities.
1401 Research Boulevard Rockville, Maryland	209,335-	2,146,948-	Conversion of office space to laboratory (See app. I).
Mat Land Glenn Dale, Maryland	188,961-	1,005,481-	Conversion to laboratory and office space including computer facilities. An additional \$485,000 of alteration work is planned.
1800 G. St. N.W. Washington, D.C.	1,753,180-	180,309-	Space alterations including computer facilities.
Parklawn Rockville, Maryland	3,197,980-	1,303,093-	Space alterations including computer facilities.
Professional Services Washington, D.C.	242,535-	712,065-	Space alterations including carpeting.
Willate Silver Spring, Maryland	414,695-	705,871-	Space alterations.
Fullerton Industrial Park Springfield, Virginia	285,660-	418,915-	Space alterations including pistol range.
Northrup Page Vienna, Virginia	456,633-	791,035-	Space alterations.
Federal Center No. 2 Hyattsville, Maryland	879,516-	1,948,679-	Space alterations.
Friendship No. 1 Baltimore, Maryland	272,236-	771,394-	Space alterations including new raised floors with new pedestals for computer room.
211 Main Street San Francisco, California	3,062,247-	2,202,167-	Space alterations.

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NINETY-FIFTH CONGRESS

Congress of the United States
House of Representatives

COMMITTEE ON GOVERNMENT OPERATIONS

2157 Rayburn House Office Building

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February 28, 1978

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MAJORITY—228-8081
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The Honorable Elmer B. Staats
 Comptroller General of the United States
 Washington, D. C. 20548

Dear General:

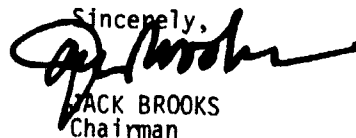
Congressman Bedell has recently brought to my attention that the Public Buildings Service of the General Services Administration is spending large sums of money each year to pay for alterations to buildings leased from the private sector. In some cases, these one year alteration costs have been several times greater than the annual rent for the building.

The Government Operations Committee is presently doing a study of the leasing practices of the Public Buildings Service. In connection with this study, I request the General Accounting Office to initiate an investigation of the alteration of leased buildings. In particular, it would be helpful if the investigation would deal with these matters:

- 1) The practice and policy of adding major alterations to leased buildings and the effects of these alterations on subsequent lease renewal decisions;
- 2) The extent of the practice of the Public Buildings Service authorizing the owners of leased buildings to provide alterations rather than the PBS procuring alterations through a competitive bid process;
- 3) Other related matters of concern which may develop during the investigation.

It would be helpful if we could have this report by September 15, 1978, but the Committee may need information and/or testimony on this investigation for hearings which may occur before that date. I would also request that this report not be submitted to the General Services Administration for comment.

Thank you for your prompt attention on this matter and with best wishes, I am

Sincerely,

 JACK BROOKS
 Chairman

(945154)