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Proposed Sale of Federal Land to the Columbia Hospital for Women

Statement of
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General Government Division

Before the
Subcommittee on Fiscal Affairs and Health
Committee on the District of Columbia
House of Representatives

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PROPOSED SALE OF FEDERAL LAND TO THE COLUMBIA HOSPITAL FOR WOMEN

SUMMARY STATEMENT OF RAY C. RIST DIRECTOR OF OPERATIONS GENERAL GOVERNMENT DIVISION

H.R. 2570 would authorize the sale of government-owned land at 2400 M Street NW in the District of Columbia to the Columbia Hospital for Women for $12 million. The Subcommittee on Fiscal Affairs and Health of the House Committee on the District of Columbia asked GAO to summarize its previous work on the appraised value of this land and to assess the Hospital's financial condition.

GAO had an appraisal prepared at the request of the Committee Chairman that determined the fair market value of the land was $20 million, in October 1988. In February, 1989, Columbia Hospital also obtained an appraisal which estimated the value at $9 million--less than half of GAO's appraisal estimate. The principal difference in these appraisals is that the one prepared for GAO followed federal appraisal standards, while the other did not. GAO's appraisal determined the fair market value based on the highest and best use standard and recent sales of comparable property. The Hospital's appraisal based its value on the property's proposed use as a women's health resource center, with some development rights unused. GAO cautions, however, that both appraisals are old and market conditions have changed. Only an auction or a current appraisal, using the federal appraisal standards, can determine the current fair market value of the property.

To address the Committee's concern about the Columbia Hospital's financial ability to pay for and develop the property, GAO analyzed the Hospital's financial statement for the years ending June 30, 1989 and 1990. The analysis showed that the Hospital is generally in comparable or better financial condition than the industry as a whole. However, the financial position of the Hospital deteriorated somewhat during 1990, due in part to the continuing costs of its renovation efforts. Further expansion through construction of the health center is an ambitious undertaking, particularly since financing may be difficult in the current economic environment.

GAO recognizes that there are issues associated with selling or keeping this land that are not fully encompassed by considering only the appraisals or the financial health of the hospital. For example, a below-market sale of the property would constitute a subsidy for promotion of health care. However, there may be more efficient methods for subsidizing health care which should be considered. Also, if the land is not sold, it could be used for a new federal building and reduce the government's dependence on costly leased office space in the capital, also a worthy objective.

Mr. Chairman and Members of the Subcommittee:

We welcome the opportunity to appear before you today to assist the Subcommittee in its consideration of H.R. 2570. This bill would authorize the sale of government-owned land, located at 2400 M Street NW in the District of Columbia, to the Columbia Hospital for Women. You asked that we discuss work we have done regarding the fair market value of this land and the financial condition of Columbia Hospital.

In March 1989, we issued a report to the Chairman of this Committee that discussed the results of an independent appraisal we obtained on the value of this land.[1] In December of that year we issued a follow up report contrasting the differences between our appraisal and one obtained by Columbia Hospital.[2] Our appraisal estimated the fair market value on October 31, 1988 was $20 million, while Columbia Hospital for Women's appraisal estimated the market value on February 22, 1989 was $9 million--less than half of the estimate made in our appraisal.
In May 1990, we testified on H.R. 2031 in the 101st Congress--also a bill to authorize the sale of this land to Columbia Hospital. Under H.R. 2031, Columbia Hospital would pay GSA $7 million at the time of conveyance, and $3 million 15 years

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[1] Federal Real Property: Appraisal of Land to Be Sold to Columbia Hospital for Women, (GAO/GGD-89-46, Mar. 10, 1989.)

[2] Federal Real Property: Conflicting Appraisals of Land Near Columbia Hospital for Women, (GAO/GGD-90-15, Dec. 11, 1989.)

later. We determined that the present value of this transaction was $7.8 million.

As discussed during the earlier testimony, the principal difference between our appraisal and the Hospital's appraisal is that ours followed federal appraisal standards and the Hospital's did not. Consistent with federal policy, our appraisal based the fair market value on the highest and best use of the land. Columbia Hospital's appraisal based the property's market value on the development proposed at that time--a women's health resource center.

To determine fair market value under existing federal policy, appraisal reports are to state the highest and best use that can be made of the property and then value the property on the basis of that use. Our appraisal report provided a detailed analysis of several factors considered in determining the property's highest and best use. These factors included zoning restrictions, the physical possibility for development (construction moratorium, necessary utilities, etc.), financial feasibility, and market conditions. Based on these factors, our appraiser concluded that the highest and best use of the property was for office, hotel, or mixed commercial and residential development. Columbia Hospital's appraisal report, on the other hand, did not mention the property's highest and best use.

Instead, it referred to the special and limited use proposed by Columbia Hospital which was not the highest and best use.

Federal policy also requires that the appraiser's opinion be supported by confirmed sales of comparable or nearly comparable lands having similar optimum or highest and best uses. To support the appraiser's opinion of the property's fair market value, our appraisal report provided a detailed analysis of five comparable sales that took place between December 1986 and October 1988.

In Columbia Hospital's appraisal report, the appraiser's opinion of the property value was not supported by an analysis of comparable sales. Instead, their appraiser indicated that his opinion was based on "discussions with developers and investors in the West End, as well as (his) research of recent sales...." He did not provide factual data or research that might support his opinion.

Federal policy also provides that the appraisal should not diminish or downgrade the property's value based on the purpose for which the land is to be acquired. That is, the fact that the purchaser did not plan to develop the property to its highest and best use should not have had an effect on the value of the property. Our appraisal report complied with this policy. The other appraisal report did not because it was commissioned to base the value of the property on the special and limited use proposed by the Columbia Hospital for Women, which is less than the highest and best use. I would like to caution at this point however, that both appraisals are old and market conditions have significantly changed over the last several years. Therefore, the prudent thing to do would be to get a current appraisal of this land using the federal appraisal standards.

It is also important to recognize that H.R. 2570 would sell the land at a price of $12 million, with $5 million paid at the time of conveyance and $7 million to be paid over an 8 - year period beginning in the third year after conveyance. Because GSA is to charge a market based interest rate on the outstanding balance of the purchase price beginning on the date of conveyance, the present value of the purchase price remains $12 million. These terms are a marked improvement over the sale price proposed in H. R. 2031. Specifically, the government's return has been increased by $4.2 million--the difference between the present value of $12 million and $7.8 million.

Hospital's Financial Condition

Because of your concern about Columbia Hospital's ability to both pay for the land and construct a new center, we did an analysis of the hospital's financial condition for the years ending June 30, 1990 and (reclassified) 1989. Our analysis, using the 6 building blocks of financial analysis--short term liquidity, cash flow, capital structure/long-term solvency, return-on-investment, operating performance, and asset utilization, showed that overall Columbia Hospital is generally in comparable or better financial condition than the industry as a whole. For example, we noted that:

-- Columbia's total liabilities to total equity are better than the industry average with its debt ratio at about the industry average. As of June 30, 1990 and 1989 Columbia Hospital's ratios of liabilities for every $1.00 of equity were 1.4 in 1990 and 1.7 in 1989; better than the 2.5 industry average. Columbia hospital's debt ratio, was .58 in 1990 and .62 in 1989, comparable to the industry average of .62.

-- Columbia earned above hospital industry averages on its return on total assets and total equity. For 1990 and 1989 Columbia Hospital earned 3.8 and 4.2 percent, respectively, on its total assets while the 1989 industry average was 3.9 percent. Additionally, Columbia Hospital earned 9.1 percent in 1990 and 11.1 percent in 1989 on its total equity, which is better than the hospital industry average of 7.8 percent.

-- Columbia Hospital's operating performance, based on the gross revenue writeoffs and the operating margin, is comparable to industry averages. For 1990 and 1989 Columbia Hospital wrote-off 27.1 and 25.6 percent respectively of its gross revenues which is comparable to the 1989 hospital industry average of 27.3 percent. Its operating margin, the ability to generate income to sustain operations, of 2.1 percent in 1990 and 3.1 percent in 1989 is comparable or better than the hospital industry average of 2.2 percent.

However, the financial position of the hospital deteriorated somewhat during 1990. For example, Columbia Hospital's cash flow as identified from operating, investing or financing activities decreased by $7.4 million in 1990 after a 1989 increase of $8.6 million. Cash from operations decreased to $2 million in 1990 from $6 million in 1989 primarily as a result of net income and depreciation/amortization. Cash from investing activities decreased $3.3 million in 1990 and $27.7 million in 1989 primarily due to purchases of fixed assets and contributions to the self-insurance trust fund. Cash flows from financing activities decreased in 1990 by $6.1 million primarily due to an equity payment to a healthcare group.

Furthermore, in 1990 Columbia Hospital began a major facility renovation project. The $25 million invested in this renovation significantly increased the hospital's debt load. Further expansion with the construction of the health resource center will cost an estimated $37.5 million. A portion of this construction is to be financed through a capital campaign which may be difficult to accomplish in the current economic environment. Another difficulty may be creditors' unwillingness to lend given the general stagnation of development loans in the Washington, DC area. Given these conditions, the hospital's undertaking is ambitious. The result could be the hospital obtaining the land and being unable to construct the center as planned for several years, or in the worst case, not at all.

Therefore, it may be prudent to amend the conveyance terms in H.R. 2570 to provide for the land's reversion to GSA if the center is not built within a certain number of years.

Other Considerations

We recognize, however, that there are public policy issues associated with selling or keeping this land that are not fully encompassed by considering only the appraisals or the financial health of the hospital. If enacted, H.R. 2570 could contribute to the promotion of health care. As envisioned, the proposed women's health resource center is intended to provide programs, services, and activities that will help address several of the problems associated with health care in the nation. Yet it is also important to recognize that the sale of this land at any price lower than the highest and best use value of the land would be the same as providing a subsidy for this purpose. For example, if we assume that the value of the property to the government is still $20 million, as our previous appraisal stated, and if the government sells the property for $12 million, the purchaser implicitly receives an $8 million government subsidy. We believe that consideration should be given as to whether this subsidy will return greater public benefits per dollar than alternative subsidies to other institutions offering comparable research, education and care services. In other words, the public may be better served by the government selling the property for $20 million to the highest bidder and then providing an $8 million dollar subsidy to the most deserving medical institution nationwide.

There is also an opportunity cost associated with the proposed transaction. If H.R. 2570 is not enacted, GSA would then be able to keep the land for its proposed use--the construction of a federal office building that would help reduce the government's dependence on costly leased office space in the Washington, DC area. We have issued a series of reports and testimonies documenting that this need is real.[3]

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[3]PUBLIC BUILDINGS SERVICE: GSA's Projection of Lease Costs in the 1990s, (GAO/GGD-89-55, Apr. 19, 1989.)

PUBLIC BUILDINGS: Own or lease? (GAO/T-GGD-89-41, Sept. 26, 1989.)

PUBLIC BUILDINGS: Increased Ownership Would Result in

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This concludes my prepared statement and I would be pleased to respond to any questions.

Significant Savings, (GAO/GGD-90-11, Dec. 22, 1989.)

THE DISINVESTMENT IN FEDERAL OFFICE SPACE (GAO/T-GGD-90-24, Mar. 20, 1990.)

LONG-TERM NEGLECT OF FEDERAL BUILDING NEEDS (GAO/T-91-64, Aug. 1, 1991.)

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