



July 2015

FEDERAL REAL PROPERTY

GSA Needs to Determine Its Progress toward Long-term Sustainability of Its Portfolio

Accessible Version

GAO Highlights

Highlights of GAO-15-609, a report to congressional requesters

Why GAO Did This Study

GSA is the primary steward of the federal government's owned portfolio of buildings, many of which do not generate sufficient revenue to fund their own operations, repairs, and capital needs. In 2001, GSA developed a portfolio-restructuring strategy to identify and dispose of those buildings that were a fiscal and managerial drain on the portfolio's resources.

GAO was asked to review GSA's efforts to address buildings with poor financial performance. This report discusses (1) how GSA addresses the effects of consistently poor-performing buildings and the challenges presented by and the extent GSA has sustained losses from these buildings; and (2) the progress, if any, GSA has made toward building a portfolio of strong performing buildings, including the extent to which GSA's quantitative building measures provide useful information. GAO analyzed relevant laws and agency documentation and data for fiscal years 2002–2013—the most recent available data—and interviewed GSA officials and real estate experts representing 11 private-sector professional, industry, and trade organizations selected based on past GAO work and reviews of GSA documents.

What GAO Recommends

GSA should assess progress made toward a sustainable portfolio by identifying the gap between its current performance and the level necessary for sustainability. As part of this effort, GSA should update its tiering and core asset analysis procedures to provide more precise measures for identifying any performance gap. GSA agreed with the recommendation.

View GAO-15-609. For more information, contact David Wise at (202) 512-2834 or wised@gao.gov.

July 2015

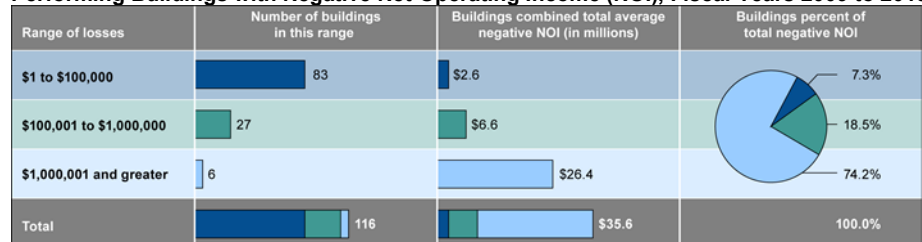
FEDERAL REAL PROPERTY

GSA Needs to Determine Its Progress toward Long-term Sustainability of Its Portfolio

What GAO Found

In 2002, the General Services Administration (GSA) implemented “tiering”—a series of quantitative tests designed to separate strong income-producing buildings from poorly performing buildings. From 2002 to 2013, almost 20 percent of GSA's buildings with at least 5 years of data were designated as poor financial performers at least 75 percent of the time they were tiered. All 11 of GSA's regions have taken steps to improve the financial performance of these buildings, including eliminating federal tenants' leases, filling vacant space, and reducing operations and maintenance costs. However, some challenges lie beyond GSA managers' ability to address, including rent limitations and poor market conditions. Average annual losses of almost \$36 million (for fiscal years 2009 to 2013) were attributable to 116 of GSA's 251 consistently poor-performing buildings; 33 of these buildings accounted for almost 93 percent of the overall loss.

Average Annual Losses among General Services Administration's Consistently Poor-Performing Buildings with Negative Net-Operating Income (NOI), Fiscal Years 2009 to 2013



Source: GAO analysis of General Services Administration (GSA) data. | GAO-15-609

Note: GAO reviewed 12 years of annual tiering data on 1,283 of GSA's buildings (those in GSA's 2014 inventory with at least 5 years of tiering data). GAO found 251 buildings that have been assessed through GSA's measures as non-performing or under-performing at least 75 percent of the time. GAO refers to this group of 251 buildings as “consistently poor performing buildings.”

GSA's progress toward a sustainable portfolio is unclear because GSA has not assessed the gap between the performance the portfolio needs to exhibit to be sustainable and its current performance. Since GSA adopted a 2001 strategy to restructure the portfolio to consist primarily of strong income producers, it has disposed of almost 370 assets comprising about 18-million square feet. However, without assessing progress made toward sustainability, GSA cannot say whether it has done enough to fully address the problem the restructuring strategy was developed to address—that of too few funds for too many buildings. In addition, GSA's quantitative building measures—tiering and core asset analysis (analysis that complements tiering and identifies assets needed long-term)—may not be sufficient for assessing progress toward a sustainable portfolio. Experts GAO interviewed identified several limitations of GSA's tiering method, including that it may be outdated and does not enable comparison of asset efficiency. Further, GSA's core asset analysis may be imprecise as in 2013, GSA managers justified categorizing as core assets about 74 percent of the 345 buildings that failed core asset tests. If GSA refined its quantitative measures—tiering and core asset analysis—the measures would be better suited to address the Office of Management and Budget's new *National Strategy for the Efficient Use of Real Property*, which emphasizes efficiency measures and the long-term sustainability of the federal portfolio.

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Abbreviations

BOMA	Building Owners and Managers Association International
FCI	facility condition index
FRV	functional replacement value

GPRA	Government Performance and Results Act of 1993
GSA	General Services Administration
National Strategy	National Strategy for the Efficient Use of Real Property
NOI	net operating income
OMB	Office of Management and Budget

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July 15, 2015

The Honorable Ron Johnson
Chairman
The Honorable Thomas R. Carper
Ranking Member
Committee on Homeland Security and Governmental Affairs
United States Senate

The Honorable John Barrasso, M.D.
United States Senate

The federal government's real property holdings are vast and diverse—comprising hundreds of thousands of buildings across the country, and we have identified federal real property management as a high risk area since 2003.¹ The General Services Administration (GSA) serves as the primary steward of the federal government's civilian real property portfolio. The buildings in this portfolio can require significant resources to construct, operate, and maintain over the course of their life cycle.² In 2001, GSA observed that many of its buildings did not generate sufficient revenue to fund their own operations, repairs, and capital needs. To promote its portfolio's long-term sustainability, GSA developed a restructuring strategy so that the portfolio would consist primarily of buildings that are strong income producers by removing from the inventory those buildings that were a fiscal and managerial drain on the portfolio's resources. In 2002, this strategy led to the practice of "tiering"—a series of quantitative tests, or measures, that GSA developed to separate strong income-producing buildings from poorly performing buildings. In this context, you asked us to review the issues that contribute to buildings' not performing financially as well as to review what GSA has done to improve the finances of those buildings.

This report focuses on (1) the steps GSA has taken to address buildings that consistently exhibit poor financial performance, challenges GSA faces from poor-performing buildings, and the extent to which GSA has sustained losses from these buildings, and (2) the progress, if any, GSA

¹GAO, *High-Risk Series: An Update*, [GAO-15-290](#) (Washington, D.C.: February 2015).

²In this report we refer to buildings that are owned by the federal government and under the custody and control of GSA as GSA buildings.

has made toward building a portfolio of strong performing buildings, including the extent to which GSA's quantitative building measures provide useful information for determining that progress.

To address the extent to which GSA has sustained losses from these buildings, we obtained GSA's tiering data from 2002 through 2013 (as long as GSA has been tiering buildings including the most recent year for which data were available) on GSA's buildings. Based on our review of documentation for each of the systems inputting data for tiering tests, our interviews with GSA officials, and our own electronic testing of the tiering data, we determined that GSA's tiering data were sufficiently reliable for our purposes. We analyzed these data to identify which of these buildings were consistently poor performers—which we defined as buildings annually categorized as financially non-performing or under-performing at least 75 percent of the time that they were tiered. We also analyzed the tiering data and compared the characteristics of 251 consistently poor-performing buildings to GSA's other buildings.³ We reviewed documents and interviewed officials at all 11 of GSA's Regional Offices and officials at GSA Headquarters to learn about how the agency manages consistently poor-performing buildings. We also identified the 33 buildings among the consistently poor-performing buildings with an average loss of \$100,000 or more each for 5 fiscal years from 2009 through 2013,⁴ and reviewed documentation and interviewed the managers of those buildings to learn about the factors contributing to the losses. We selected 11 buildings from this population for site visits based primarily on geographical distribution. These buildings were located in California, Missouri, Illinois, and the District of Columbia.

To determine what progress GSA has made toward building a portfolio of strong performing buildings and the extent that GSA's quantitative building measures provide useful information for determining that progress, we reviewed GSA documentation and interviewed GSA officials about their tiering methodology. Based on past GAO work, reviews of

³We only considered buildings that had at least 5 years of tiering data for the purposes of this review. We also used only owned buildings and excluded all other asset categories (e.g., land, structures, etc.) during our review. Once we removed the buildings without 5 years of tiering data and assets that were not GSA buildings, we divided the population into two populations that we use throughout this report. Those that were categorized as non-performing or under-performing for 75 percent or more of the time, we call "consistently poor performers" and the rest are "other buildings."

⁴For the purposes of this report, we defined loss as negative net operating income—a measure of revenue minus some expenses.

GSA documents, and external recommendations, we also identified 11 real-estate industry organizations representing a selection of domestic and international professional organizations, industry, and trade associations. We interviewed these experts and discussed the tiering methodology to obtain their views on this methodology and ideas for improvements that might be made. In addition, we reviewed 2013 data and documentation from GSA for another of its key quantitative measures—"core asset analysis"⁵—which was designed to complement tiering. We reviewed documentation on the various computerized data sources providing inputs to core asset analysis, interviewed GSA officials about how these data sources are assembled, and determined that these data were sufficiently reliable for our purposes. We also reviewed a new *National Strategy for the Efficient Use of Real Property (National Strategy)* from the Office of Management and Budget (OMB) to determine if GSA's quantitative building measures are useful for implementing that strategy.⁶ Further details on our scope and methodology can be found in appendix I.

We conducted this performance audit from June 2014 to July 2015 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Background

To provide a predictable source of revenue for funding federal buildings, the Public Buildings Act Amendments of 1972 established the Federal Buildings Fund.⁷ Revenue from GSA's owned inventory—derived from rents collected from federal tenants—is the main source of the Federal Building Fund's operating income and is used to fund repairs and alterations, new construction activities, operations and maintenance, and

⁵The quantitative portion of "core asset analysis" consists of five quantitative tests designed to measure a building's customer needs, market condition, and reinvestment needs.

⁶Office of Management and Budget, *National Strategy for the Efficient Use of Real Property, 2015–2020*: (Washington, D.C.: 2015).

⁷Pub. L. No. 92-312, § 3, 86 Stat. 216, 218 (June 14, 1972), codified as amended at 40 U.S.C. § 592.

disposal of buildings.⁸ Congress exercises control over the Federal Buildings Fund through the appropriations process, which sets annual limits on how much GSA can obligate for various activities. GSA requests amounts it can obligate—called obligational authority—from Congress as part of the annual President’s Budget Request. The budgeting and appropriations process may result in differences between the fund’s resources and GSA’s use of these funds.⁹ In 2001, GSA recognized the challenges to keeping its federal inventory in good repair—given the deteriorating condition of the federal inventory and trends in funding for federal buildings and the number of buildings in this inventory that operated at a loss. At that time, GSA proposed a strategy to restructure its portfolio to address the imbalance between the condition of its inventory and available financial resources. In this strategy, GSA noted a goal of living within its means—in other words, making its inventory self-sustaining within the boundaries of funding that GSA could reasonably expect to receive. GSA designed its tiering metrics to identify assets that drain the resources of the portfolio and should be considered for disposal. GSA continues to annually tier assets based on these same procedures from 2002 using four tier rankings—1, 2a, 2b, and 3—with 1 being the best status and 3 being the worst. The diagnostic procedures are performed in reverse order, beginning with the Tier 3 diagnostic, so that if an asset passes the Tier 3 diagnostic, then it moves successively through the remaining tests until it is placed in the category that best describes the performance of the asset. Table 1 summarizes the tier descriptions and associated diagnostic calculations of GSA’s 2014 tiering procedures.¹⁰

⁸GAO, *Federal Buildings Fund: Improved Transparency and Long-term Plan Needed to Clarify Capital Funding Priorities*, [GAO-12-646](#) (Washington, D.C.: July 2012).

⁹We reported in 2012, that the balance of the Federal Buildings Fund had increased from \$56 million in fiscal year 2007 to \$2.2 billion in fiscal year 2012 primarily due to the growing difference between the Fund’s resources and GSA’s use of these funds as determined through the budgeting and appropriations process. We also reported that in the 2 previous years, Congress provided fewer resources than requested by the executive branch and generated by the Federal Buildings Fund. However, since 2008, GSA has consistently requested less obligational authority than the total resources available in the Federal Buildings Fund. GSA officials stated then that in preparing their budget requests, they work with OMB to discuss their needs in relation to competing priorities from other executive branch agencies. Thus, budget requests for obligational authority reflect efforts to balance GSA’s needs with those of other federal agencies within the overall budget framework. See [GAO-12-646](#).

¹⁰GSA tiers are based on the results of the previous fiscal year. Thus, the 2014 tiering procedures were conducted with data from the end of fiscal year 2013.

Table 1: The General Service Administration’s 2014 Tiering Tests for Measuring Financial Performance

Tier level	Performance category	Formula test	Description
Tier 3	Non-performing asset	Net Operating Income [Note A] – 2% of Functional Replacement Value [Note B] < 0 [Note C]	Poor financial performance; the asset is unable to fund a reserve to replace itself at the end of 50 years
Tier 2b	Under-performing asset	Return on Equity [Note D] < 6%	Marginal financial performance
Tier 2a	Performing Asset	Return on Equity > 6% Facility Condition Index [Note E] > 0.10	Good financial performance, but significant capital reinvestment required
Tier 1	Performing Asset	Return on Equity > 6% Facility Condition Index < 0.10	Good financial performance, relatively small capital investment required

Source: GAO analysis of the General Services Administration data. | GAO 15-609

Note A: GSA defines net operating income (NOI) as follows: NOI = Direct Revenue – Direct Expenses – Field Office General and Administrative expenses. General and Administrative expenses are a form of overhead costs.

Note B: GSA defines functional replacement value (FRV) as follows: FRV = Cost to replace the building’s function (office, warehouse, etc.) and not the cost to replace the building as an exact replica of itself.

Note C: In this formula, if NOI less FRV is negative, the building is Tier 3, the lowest tier possible.

Note D: GSA defines return on equity as follows: NOI / Value. For most assets, value is the fair market value determined by a recent third-party appraisal. For assets that do not have a recent third-party appraisal, either the construction cost for assets built within the past 10 years, or a calculated direct capitalization method is used to determine value.

Note E: GSA defines facility condition index (FCI) as follows: FCI = Physical Condition Survey reinvestment needs / FRV. FCI is a measure of an asset’s condition. FCI is the ratio between total repair and alteration needs and the FRV of an asset (i.e., the estimated cost of needed repairs divided by the asset’s replacement value). The higher the FCI, the worse the condition of the asset. According to GSA, an FCI of less than 0.1 indicates that a building is in good physical condition, an FCI of 0.1 to 0.2 indicates that it is in fair condition, and an FCI above 0.2 indicates that a building is in poor condition.

In 2008, GSA noted that tiering had been an effective tool in changing the way it manages its portfolio. However, according to GSA, due to challenges of large reinvestment liability and limited funding, GSA still needed to “right-size” the portfolio. To do this, GSA noted that it needed more sophisticated analytical tools to become more strategic in its decision making; thus, the agency began conducting the following five additional quantitative tests, known as core asset analysis, on its inventory to identify core assets and complement tiering. According to GSA officials, GSA intends to hold its core assets long-term (longer than 15 years) while it takes a shorter view of its non-core assets, including possibly limiting maintenance and repairs and taking action to dispose of some. Core asset analysis consists of the following tests:

- *Customer tests:* The primary consideration in classifying a property as a core asset is whether there are federal tenants (customers) to fill the space. To evaluate the customer profile of an asset, GSA analyzes

both current asset occupancy and the housing needs of potential customers. An ideal customer base for an asset includes federal agencies that have a long-term need for the space as well as potential backfill candidates in the event that space becomes available. To assess the customer base of an asset, the analysis asks two questions: Does the building have an acceptable level of vacancy (Asset Occupancy Test)? If not, do opportunities exist to backfill the space with other tenants (Backfill Potential Test)? According to GSA officials, an asset can fail the Asset Occupancy Test and still be considered a core asset if it passes the Backfill Potential Test.

- *Market test:* Another consideration in classifying a property as a core asset is whether the asset is located in a market that can support its reinvestment needs. This test measures the payback period of the reinvestment needed to maintain the asset in good condition, in the context of the market (Market Payback Period Test). To pass this test, an asset's reinvestment payback period must be less than 25 years. Assets must pass this test to be considered a core asset.
- *Asset tests:* A third consideration in classifying a property as a core asset is whether the level of reinvestment needed to keep an asset functioning is acceptable. If the planned or needed reinvestments are more than 50 percent of the functional replacement value of the asset, then the reinvestment level may not be acceptable, causing GSA to consider whether reinvestment is the best alternative for the government or whether it could be more cost-effective to lease or to construct space in that market. This portion of the core asset analysis applies two tests to answer the following questions: (1) Is the asset's reinvestment level acceptable as compared to its functional replacement value (Reinvestment Level Test)? (2) Does the planned reinvestment extend the asset's life (Asset Lifecycle Test)? The asset must pass the Reinvestment Level Test to be considered a core asset. However, an asset can fail the Asset Lifecycle Test and still be a core asset.

Based on these quantitative tests, GSA gives a preliminary designation to each asset as "core" or "non-core." However, asset managers can still designate a failed asset as core, despite the results of the five tests, if managers justify it as core through a validation process guided by a series of questions to justify a strategy that does not align with the tests (e.g., retaining an asset long-term when it fails the test).

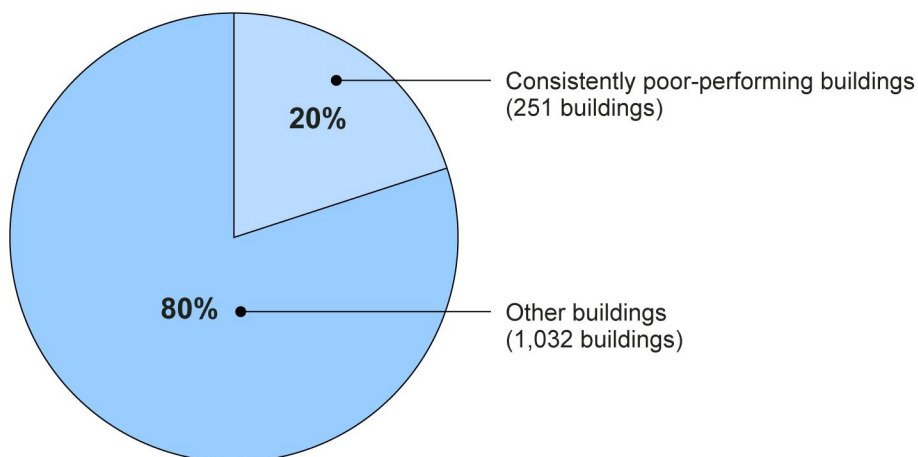
Although GSA Has Taken Steps to Address Consistently Poor-Performing Buildings, Challenges Are Difficult to Mitigate and Have Led to Considerable Losses

GSA Has Taken Some Steps to Mitigate the Effects of Consistently Poor-Performing Buildings

Based on 12 years of annual tiering data (2002–2013), we found that almost 20 percent of the buildings in GSA’s fiscal year 2013 inventory that have been tiered over time have consistently shown poor financial performance. Of the 1,283 buildings for which there was enough data for us to review, 251 (almost 20 percent) have been assessed as Tier 3 or Tier 2b at least 75 percent of the time that they were tiered.¹¹ For simplicity, in this report we refer to this group of 251 buildings as “consistently poor-performing buildings,” and the other 1,032 buildings as “other buildings” (see fig. 1).

¹¹To identify buildings that have been consistently poor performers, we considered only the 1,283 buildings that had at least 5 years of tiering data.

Figure 1: Proportion of Buildings That Were Consistently Poor-Performing Buildings versus Other Buildings, End of Fiscal Year 2013 (Percentages Rounded)



Source: GAO analysis of General Services Administration (GSA) data. | GAO-15-609

Note: We reviewed 12 years of annual tiering data on 1,283 of GSA's buildings (those in GSA's fiscal year 2013 inventory with at least 5 years of tiering data). We found 251 buildings that have been assessed through GSA's measures as Tier 3 (non-performing) or Tier 2b (under-performing) at least 75 percent of the time that they were tiered. We refer to this group of 251 buildings as "consistently poor-performing buildings," and the other 1,032 buildings as "other buildings."

While consistently poor-performing buildings can present difficulties for managers, we found that all 11 of GSA's regions have taken steps to improve the performance of these buildings, including the following:

- *Eliminating federal tenants' leases and filling vacant space:* When possible, GSA officials said that they eliminate leases and move federal tenants from leased to owned space, sometimes buying out a lease and ending it early in order to make more efficient use of owned buildings. For example, a courthouse in El Paso, Texas, became vacant when a new courthouse opened. Officials in GSA's Region 7 (Southwest U.S.)¹² arranged for the U.S. Bankruptcy Courts to move from leased space and occupy the building, which is now a financially performing building. Sometimes GSA is able to backfill vacant space with federal tenants with relative ease, as GSA officials said that some federal agencies appreciate rental rates in federal spaces that are lower than those in private spaces; however, some agencies prefer the location of leased space, particularly if the space is located in a more desirable area, even if the costs are higher.

¹²GSA Region 7, the Greater Southwest Region, covers New Mexico, Texas, Oklahoma, Arkansas, and Louisiana.

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- *Leasing vacant space to non-federal tenant:* If no federal tenants are available, GSA may “outlease” vacant space to the private sector and/or state and local governments. For example, officials in GSA’s Region 6 (Central U.S.)¹³ said that they will place ads in local newspapers and reach out to local officials whenever they have vacant space in their buildings. These officials are in the process of filling vacant office space about 100 miles north of St. Louis, Missouri, with an outlease to the State of Missouri, which will lease a few hundred square feet from GSA. However, regions also noted some limitations of outleasing. Officials in GSA’s Region 2 (near New York)¹⁴ said that outleasing should not be a long-term strategy, since GSA should ultimately dispose of buildings the government doesn’t need. Officials in Region 4 (Southeast U.S.)¹⁵ told us many buildings in Region 4 with vacant space have a heavy court presence, and for security reasons, the court will not allow certain tenants to use space in buildings it occupies. Further, GSA officials told us that many private sector tenants do not want customers to endure extra security that is required for courts and resist locating their businesses in buildings that are occupied by the courts.
 - *Reducing operating and maintenance costs:* GSA employs a number of strategies to reduce the costs of consistently poor-performing buildings. Specifically, GSA has introduced a number of energy efficiency measures, including installing more efficient plumbing and electrical fixtures, using energy rebates, educating tenants on changing certain behaviors to reduce energy costs, and exploring Energy Savings Performance Contracts with utility companies. For example, officials in Region 1 (New England area)¹⁶ have explored such a contract with the local utility company. In these contracts, the utility pays for the upfront, capital costs of installing energy-saving infrastructure. Although GSA does not receive any discount on the utility rate, GSA receives the benefit of more efficient equipment over time. GSA has also consolidated service contracts (awarding one

¹³GSA Region 6, the Heartland Region, covers Nebraska, Iowa, Kansas, and Missouri.

¹⁴GSA Region 2, the Northeast and Caribbean Region, covers New York, New Jersey, Puerto Rico, and the Virgin Islands.

¹⁵GSA Region 4, the Southeast Sunbelt Region covers Kentucky, Tennessee, North Carolina, South Carolina, Georgia, Alabama, Mississippi, and Florida.

¹⁶GSA’s Region 1, the New England Region, covers Maine, New Hampshire, Vermont, Massachusetts, Rhode Island, and Connecticut.

contract to service multiple buildings). For example, Region 8 (near the Rocky Mountains)¹⁷ officials said that they consolidated several operations and maintenance contracts in South Dakota, so that they cover all of the federal buildings in the state, and through economy of scale reduced operations and maintenance costs.

- *Renovating assets with deficiencies:* GSA officials said that if funding is available, they will renovate consistently poor-performing buildings to improve a building's condition, attract tenants, and increase rental rates. For example, the Thomas P. O'Neill Jr. Federal Building in Washington, D.C., was a Food and Drug Administration laboratory for many years. After the Food and Drug Administration vacated the building in 2002, it was consistently poor-performing and contained radioactive waste. However, GSA renovated the building, converting it into office space. GSA officials expect that this building—which achieved a Leadership in Energy and Environmental Design Gold certification¹⁸ from the U.S. Green Building Council—will be a Tier 1 performing asset after it has received a full year of rent in April 2015. Figure 2 shows the building before and after its renovation.

¹⁷GSA's Region 8, the Rocky Mountain Region covers Montana, Wyoming, Utah, Colorado, North Dakota, and South Dakota.

¹⁸Leadership in Energy and Environmental Design is a certification program for the design, construction, operation and maintenance of green buildings developed by the U.S. Green Building Council (<http://www.usgbc.org/leed>). Leadership in Energy and Environmental Design Gold is the second highest certification available, next to Platinum.

Figure 2: Renovation of the Thomas P. O'Neill Jr. Federal Building (Washington, D.C.)



Before

After

Source: General Services Administration (GSA). | GAO-15-609

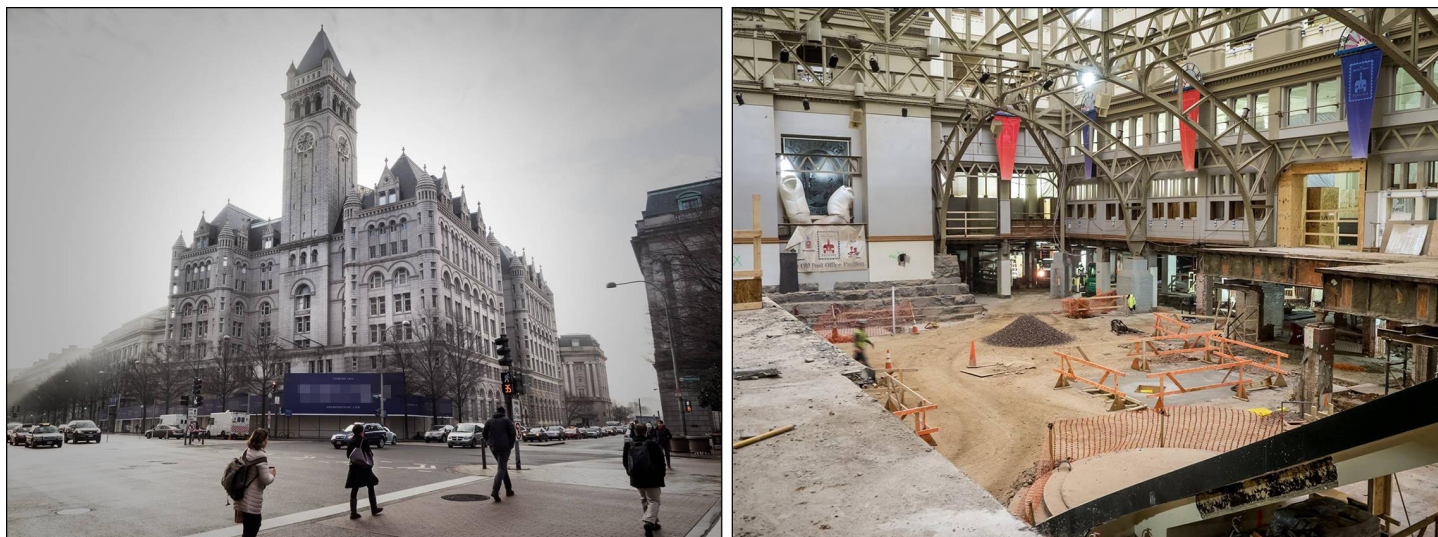
- *Public-private partnerships.*¹⁹ Although public-private partnerships are sometimes pursued as a means of addressing poor-performing buildings, none of the GSA regional officials told us that they were actively pursuing new agreements to address their consistently poor-performing buildings. According to the Congressional Research Service, these partnerships for federal real property management can be complicated arrangements, requiring knowledge of a range of disciplines, and have certain risks and limitations. Related to this situation, the Congressional Research Service noted that there are relatively few real world illustrations of these risks and limitations at the federal level because federal agencies' use of public-private partnerships for federal real property management has been relatively limited, particularly as compared to that of state and foreign governments. We did, however, find one example where GSA Region 11 (National Capital Region)²⁰ is using a public-private partnership to

¹⁹According to the Congressional Research Service, while there is no single, accepted definition of public-private partnerships, such partnerships, as they relate to federal property, can be thought of as an agreement whereby a non-federal entity acquires the right to use an asset owned and controlled by a federal agency—typically through a long-term lease—in exchange for redeveloping or renovating that property (or another property). In many cases, the agency and the nonfederal entity share the net cash flow or savings that result from the agreement. See Congressional Research Service, *Public-Private Partnerships for Purposes of Federal Real Property Management*, (Washington, D.C.: Dec. 31, 2014).

²⁰GSA's Region 11, the National Capital Region covers the Washington, D.C. metro area.

re-purpose one of the top consistently poor-performing buildings in terms of loss (see app. II). In June 2013, GSA reached an agreement with Trump Old Post Office, LLC, on the terms of a 60-year lease aimed at transforming the Old Post Office Building in Washington, D.C., into a 275-room hotel scheduled to open in 2016 (see fig. 3).²¹ Prior to this agreement, this building had been a Tier 3 non-performing asset since tiering began in 2002 and had an average annual net operating income loss of more than \$2.8 million for 5 years.

Figure 3: Old Washington, D.C., Post Office Being Renovated through Public-Private Partnership (2015)



Source: GAO. | GAO-15-609

Challenges from Consistently Poor-Performing Buildings Are Difficult to Mitigate

While GSA has taken these steps to mitigate the effects of poor performance, GSA managers encounter challenges that result in some buildings remaining consistently poor performers; some of these challenges are beyond GSA's ability to address with better management practices.

- *Rent limitations:* According to GSA officials, some tenants—including the Social Security Administration, Railroad Retirement Board, and

²¹Under section 4 of the Old Post Office Building Redevelopment Act of 2008, Pub. L. No. 110-359, 122 Stat. 4005 (2008), GSA was directed to proceed with redevelopment of the Old Post Office Building.

Centers for Medicare & Medicaid Services—in GSA’s consistently poor-performing buildings pay much less rent than comparable market rents—and, in some cases, no rent at all.²² In particular, as another example of rent limitations, GSA assesses rents at the buildings that make up the White House complex according to terms of a memorandum of understanding that expired in 2012, but they do not cover the full costs to operate and maintain these buildings.²³ GSA officials said they have had some limited success in getting more operating costs paid by the White House. For example, GSA has paid for a full-time audio-visual employee to operate equipment in an auditorium for the Executive Office of the President, but GSA officials said that they expect the new memorandum of understanding to state that the White House will cover those costs beginning in fiscal year 2016. GSA and the White House are currently in the process of developing a new memorandum of understanding, but there is no estimated date for its completion, and GSA officials do not expect that a new agreement would result in rental rates that cover the costs of operating these buildings. Further, the National Building Museum, a private non-profit entity, occupies a historic building in Washington, D.C., without any rent charged at all, in accordance with provisions in law.²⁴ According to GSA, operating costs of the building are high because the museum is only closed three days out of the year, and the air conditioning system is used 24 hours per day for sensitive

²²Consistent with language in H.R. Conf. Rep. No. 93-1489 (1974) and under the discretionary authority of the Administrator allowing GSA to determine the rental rates charged to executive agencies (40 U.S.C. § 585(b)(1)-(2)), GSA officials said the agency has long applied a special pricing policy for certain space occupied by the Social Security Administration, the Railroad Retirement Board, and the Centers for Medicare and Medicaid Services. This policy allows these agencies to pay rental rates to GSA that are less than the commercial equivalent rent for space and services, and effectively reduce rental rates at the asset level by about 30 percent. The policy was most recently defined in Memoranda of Understanding executed for the three agencies for fiscal years 2004 through 2013. GSA is currently in the process of renegotiating the Memoranda of Understanding.

²³According to GSA officials, there are several Memoranda of Understanding between GSA and the Executive Office of the President that govern, among other things, rental rates and payment of utilities, for space occupied by the Executive Office of the President and by other agencies in the complex. According to GSA officials, one of the challenges for setting White House rental rates is the lack of comparable properties on which to base the rate. In addition, the historic status, high security needs, and high operation and maintenance costs present substantial challenges. GSA officials said that since a new Memorandum of Understanding for White House complex rental rates has not been executed and because the timeframe for a new rental agreement is unclear, the White House complex continues to operate under the terms of the expired Memoranda of Understanding.

²⁴Pub. L. No. 96-515, § 306, 94 Stat 2987, 3003 (1980).

collections housed in the galleries; however, GSA receives no rent to offset these costs. The net operating income for this building is consistently negative having an average annual loss of almost \$4 million over five fiscal years (2009–2013).

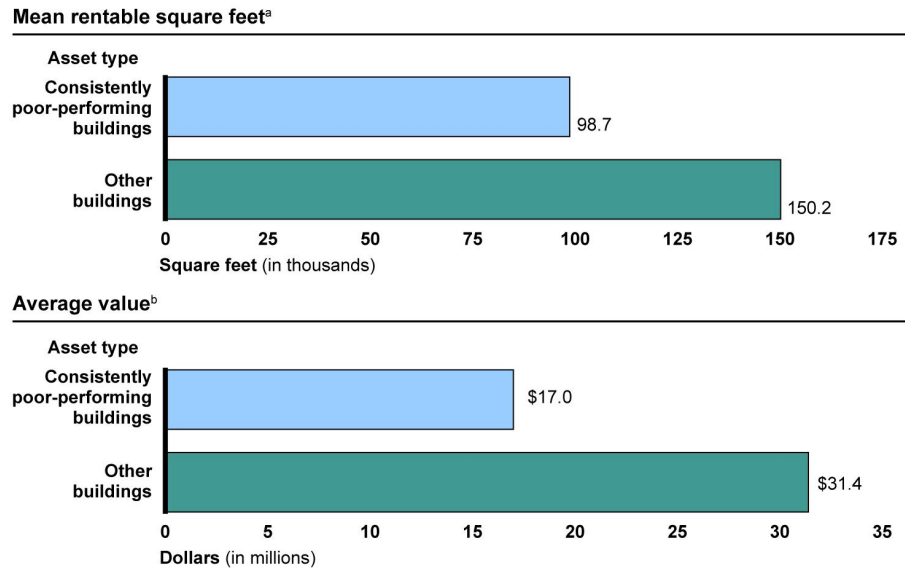
- *Market conditions:* GSA officials told us that real estate market conditions can be a factor affecting consistently poor-performing buildings. These market conditions affect GSA's ability to set rental rates and maintain good financial performance over time. For example, according to GSA officials in Region 8 (near the Rocky Mountains),²⁵ because there is often an absence of comparable properties in smaller markets, appraisals of the buildings are lower, resulting in low rental rates. In addition, officials in GSA Region 9 (Pacific Rim Region)²⁶ said that low market value appraisals are one of the most common factors driving consistent-poor performance. Furthermore, GSA officials in Region 1 (New England area)²⁷ noted that consistently poor-performing buildings are mostly smaller buildings in small communities with smaller markets. In addition to the GSA regional officials' observations, we also found that GSA's data showed that on average, across all markets, consistently poor-performing buildings are smaller by about 34 percent and less valuable by about 46 percent than other buildings (see fig. 4).

²⁵GSA's Region 8, the Rocky Mountain Region covers Montana, Wyoming, Utah, Colorado, North Dakota, and South Dakota.

²⁶GSA's Region 9, the Pacific Rim Region covers Arizona, California, Hawaii, Nevada, as well as overseas in the U.S. territories of American Samoa, Guam and the Commonwealth of the Northern Mariana Islands, Diego Garcia, mainland Japan and Okinawa, the Republic of Korea, and Singapore.

²⁷GSA's Region 1, the New England Region, covers Maine, New Hampshire, Vermont, Massachusetts, Rhode Island, and Connecticut.

Figure 4: Size and Value of General Services Administration's (GSA) Consistently Poor-Performing Buildings versus Other Buildings, End of Fiscal Year 2013



Source: GAO analysis of General Services Administration (GSA) data. | GAO-15-609

Note: We reviewed 12 years of annual tiering data on 1,283 of GSA's buildings (those in GSA's fiscal year 2013 inventory with at least 5 years of tiering data). We found 251 buildings that have been assessed through GSA's measures as Tier 3 (non-performing) or Tier 2b (under-performing) at least 75 percent of the time that they were tiered. We refer to this group of 251 buildings as "consistently poor-performing buildings," and the other 1,032 buildings as "other buildings."

Note A: According to GSA, rentable space is the area for which a tenant agency is charged rent—the measurement of the area where a tenant normally houses personnel and/or furniture plus the associated share of floor common areas and building common areas. The rentable space may include a share of common areas such as elevator lobbies, building corridors, and floor service areas (e.g., restrooms, electrical closets, etc.). The rentable space does not include vertical building penetrations and their enclosing walls such as stairs, elevator shafts, and vertical ducts.

Note B: For most assets, value is the fair market value, determined by a recent third-party appraisal. For assets that do not have a recent third-party appraisal, either the construction cost for assets built within the past 10 years, or a calculated direct capitalization method is used to determine value.

- **High vacancy:** High vacancy rates are negatively related to a building's performance. Some GSA buildings with vacant space are located in smaller communities or rural areas with a limited federal presence and thus have a low potential to backfill the space with new federal tenants. For example, the Federal Building-U.S. Post Office and Courthouse in Hannibal, Missouri, is about 33 percent vacant as of January 2015 largely because there is little potential to backfill the building with federal or other tenants (see fig. 5). GSA has outleased some of this space to non-federal tenants and is in the process of leasing some space to the state government. Further, GSA officials told us that buildings sometimes become vacant for several years

while undergoing renovation and will record large losses because much or all of the building is unable to generate rent for an extended period of time. For example, a federal office building in San Francisco has been a Tier 3 performer because it has been vacant for extensive renovations.²⁸ GSA officials expect that the building will eventually be a Tier 1 performer when they find tenants to fully occupy the building and receive a full year of revenue. On average, this building has lost more than \$730,000 annually in net operating income for 5 fiscal years (fiscal years 2009-2013), the highest for any building outside of Washington, D.C.

Figure 5: High Vacancy in a Hannibal, Missouri, Federal Office Building in 2014



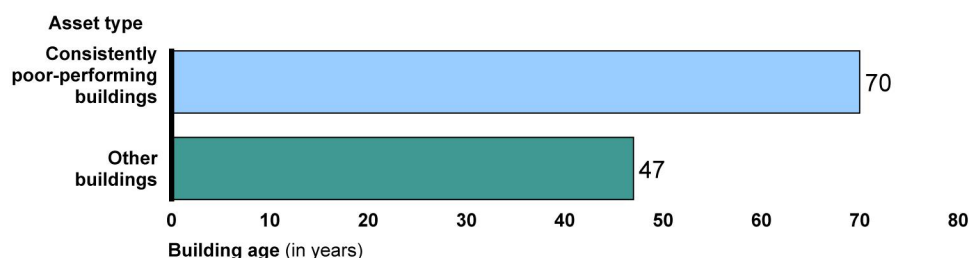
Source: GAO. | GAO-15-609

- **Age:** GSA's data confirms that older buildings, many of which are historic, may not be as attractive to tenants as newer buildings. We

²⁸In 2003, GSA proposed renovation of the building but later withdrew the proposal because of a real-estate market downturn. However, according to GSA officials, funds received from the American Recovery and Reinvestment Act of 2009 were used to renovate the building. This building was constructed in the 1930s and survived an earthquake. The extensive renovation included a seismic upgrade, environmental remediation, roof replacement, and new mechanical, electrical, lighting, and plumbing systems.

found that consistently poor-performing buildings are, on average, 23 years older than other buildings (see fig. 6) and are more likely than other buildings to have a historic designation.²⁹ In particular, we found that 27 percent of consistently poor performers have a historic designation compared to 17 percent of other buildings. GSA regional officials told us that historic buildings tend to have more vacancy (leading to lower revenue) because they can be difficult to backfill due to historic preservation requirements, which may limit the way the buildings can be modernized for today's work environment. Further, GSA sometimes faces difficulty backfilling vacant space in older buildings because of obsolescence, meaning the space itself is no longer suitable for the needs of tenants in a modern work environment. Examples of obsolescence include aging building systems and lack of adequate parking, accessibility, and "open" office plans.

Figure 6: The General Service Administration's (GSA) Consistently Poor-Performing Buildings versus Other Buildings in Terms of Average Age, End of Fiscal Year 2013



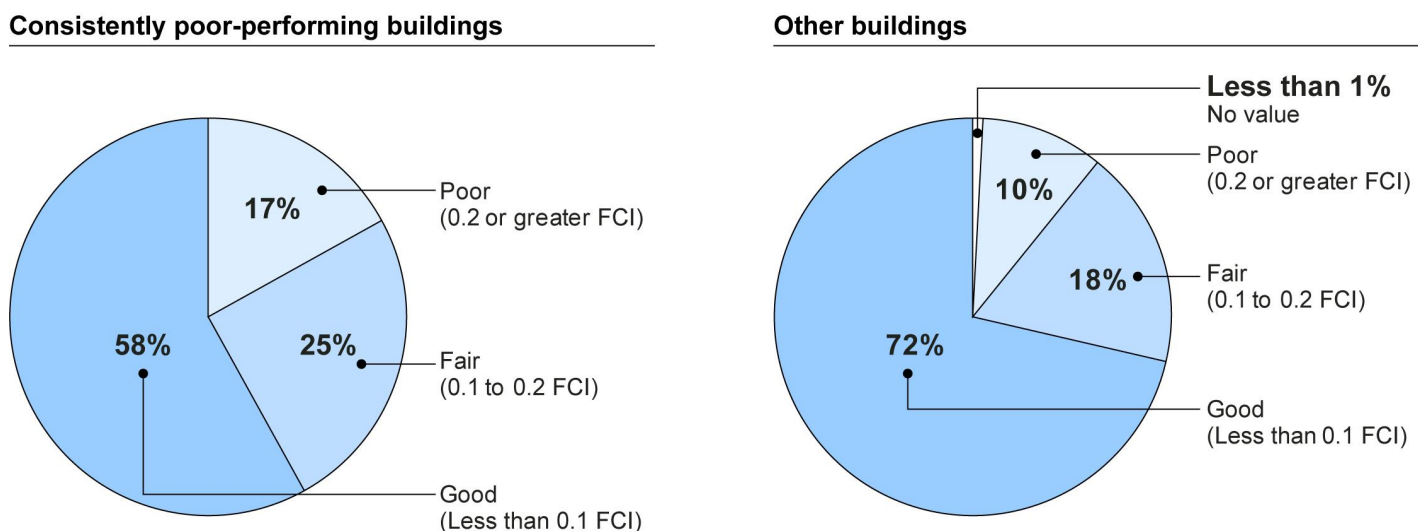
Source: GAO analysis of General Services Administration (GSA) data. | GAO-15-609

Note: We reviewed 12 years of annual tiering data on 1,283 of GSA's buildings (those in GSA's fiscal year 2013 inventory with at least 5 years of tiering data). We found 251 buildings that have been assessed through GSA's measures as Tier 3 (non-performing) or Tier 2b (under-performing) at least 75 percent of the time that they were tiered. We refer to this group of 251 buildings as "consistently poor-performing buildings," and the other 1,032 buildings as "other buildings."

²⁹The National Historic Preservation Act of 1966, as amended, requires agencies to establish a preservation program to identify, evaluate, and nominate historic federal buildings to the National Register of Historic Places and manage those buildings in a manner that considers their historic character. (Pub. L. No. 89-665, 80 Stat. 915 (Oct. 15, 1966), codified as amended at 16 U.S.C. § 470 et seq.) The National Register of Historic Places is comprised of many different types of historic properties including buildings that are significant to American history, architecture, archaeology, engineering, and culture. A building is generally not eligible for listing until it is at least 50 years old, unless its historic significance is considered exceptional. The National Register of Historic Places also includes buildings meeting the criteria for a national historic landmark. National historic landmarks are designated by the Secretary of the Interior as possessing exceptional value or quality in representing the heritage of the nation.

- **High costs:** GSA officials told us that higher than average costs for certain buildings contribute to their consistently poor performance. For example, GSA officials said that high security and housekeeping requirements add substantial labor costs to the operating budget of all White House buildings. Cleaning and maintenance are highly intensive services in these buildings, and personnel often work overtime to accommodate the President's schedule. Security requirements necessitate personnel clearances and contractor escorts that add significantly to expenses. In addition, GSA regional officials said that some consistently poor-performing buildings have higher costs related to their generally greater overall repair needs. In line with these officials' observations, we found that consistently poor-performing buildings are in worse physical condition than other buildings as measured by facility condition index (see fig. 7).

Figure 7: The General Service Administration's (GSA) Consistently Poor-Performing Buildings versus Other Buildings in Terms of Condition, End of Fiscal Year 2013 (Percentages are rounded.)



FCI: Facility condition index^a

The Facility Condition Index (FCI) is a measure of an asset's condition. It is the ratio between total repair and alteration needs and the functional replacement value of an asset (i.e., the estimated cost of needed repairs divided by the asset's replacement value). The higher the FCI, the worse the condition of the asset.

Source: GAO analysis of General Services Administration (GSA) data. | GAO-15-609

Note: We reviewed 12 years of annual tiering data on 1,283 of GSA's buildings (those in GSA's fiscal year 2013 inventory with at least 5 years of tiering data). We found 251 buildings that have been assessed through GSA's measures as Tier 3 (non-performing) or Tier 2b (under-performing) at least 75 percent of the time that they were tiered. We refer to this group of 251 buildings as "consistently poor-performing buildings," and the other 1,032 buildings as "other buildings."

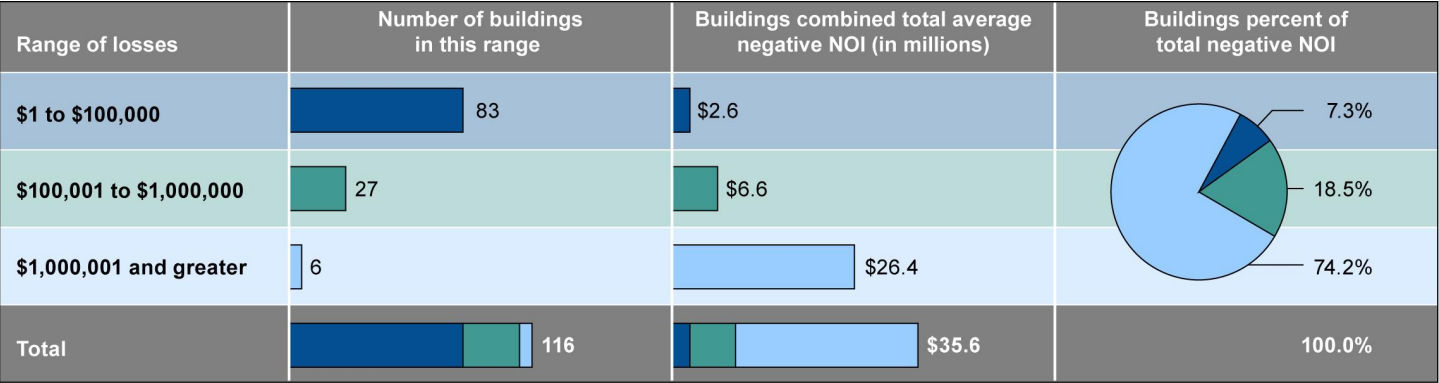
Note A: Our past work has found that the FCI may be unreliable because some agencies had a "practice of assigning no repair needs to many excess and underutilized buildings because agencies had no intention of repairing them." See GAO, *Federal Real Property: National Strategy and Better*

Data Needed to Improve Management of Excess and Underutilized Property, GAO-12-645 (Washington, D.C.: June 20, 2012). In this report, we recommended that GSA develop and implement a plan to improve the Federal Real Property Profile data (condition is included in this data). GSA agreed with the recommendation. Because GSA may be less likely to dispose of their Tier 1 and Tier 2a buildings than their Tier 2b and Tier 3 buildings, this practice of assigning no repair needs to many excess and underutilized buildings may result in condition assessments for the consistently non-performing buildings that are better than is actually the case. That is, the consistently non-performing buildings may be in worse physical condition than is shown in the data.

Most of the Losses from GSA’s Consistently Poor-Performing Buildings Are Concentrated in a Small Number of Buildings

Buildings that are consistently poor performers put a strain on GSA’s portfolio not only by generating insufficient revenue to fund the reinvestment needs of the building over time, but also, in some cases, by losing money year to year, as represented by negative net operating income. In particular, over 46 percent (116) of the consistently poor performers had, on average, a net operating income over the past five years that was negative. As figure 8 shows, these 116 buildings have a combined loss of almost \$36 million on average annually, but 33 buildings accounted for almost 93 percent of this loss, and 6 of these buildings, accounted for almost 75 percent of the loss.

Figure 8: Average Annual Losses among the General Services Administration’s Consistently Poor-Performing Buildings with Negative Net Operating Income (NOI), Fiscal Years 2009 to 2013



Source: GAO analysis of General Services Administration (GSA) data. | GAO-15-609

Note: We reviewed 12 years of annual tiering data on 1,283 of GSA’s buildings (those in GSA’s fiscal year 2013 inventory with at least 5 years of tiering data). We found 251 buildings that have been assessed through GSA’s measures as Tier 3 (non-performing) or Tier 2b (under-performing) at least 75 percent of the time that they were tiered. We refer to this group of 251 buildings as “consistently poor-performing buildings,” and the other 1,032 buildings as “other buildings.”

Appendix II, which lists the 33 buildings that have lost \$100,000 or more in annual average net operating income over 5 years (fiscal years 2009–2013), shows that many of the challenges identified by GSA officials contributed to the consistently poor performance and large losses. Twelve

of these buildings are located in Washington, D.C., including 9 of the top 10 in losses. Seven of the 33 buildings are associated with the White House, where rent limitations present challenges. Further, 4 of the buildings are located within a single facility in St. Louis, Missouri, where high vacancy presents challenges, and 10 of the buildings serve or have served as U.S. courthouses where various factors such as market conditions and high vacancy present challenges.³⁰

GSA's Progress toward a Sustainable Portfolio Is Unclear, and Its Quantitative Measures Could Be Improved

GSA Has Not Identified the Gap between Its Portfolio's Current Performance and Sustainability

In 2001, GSA adopted its strategy to restructure its portfolio because (1) it generated too few funds for reinvestment, and (2) those funds were spread too thinly among assets in the inventory. As part of its restructuring strategy, GSA intended to remove from its 185-million square foot inventory a substantial number of assets that were a fiscal and managerial drain on resources—those that were expensive to operate and maintain, and which produced little or no net income—to create a smaller but more financially viable portfolio capable of generating sufficient revenue to keep the inventory in good repair to ensure its long-term sustainability.³¹ As previously discussed, GSA adopted its tiering process in 2002 to help identify the buildings that drained the portfolio. According to GSA officials, GSA has disposed of almost 370 assets between 2001 and 2013 for a reduction of about 18-million square feet. In addition, GSA has set annual performance goals related to components of the tiering formulas. For example, GSA has set annual performance goals for the past several years aimed at achieving a positive return on

³⁰For more information on our work regarding the challenges associated with courthouse space see [GAO-14-48](#), *Federal Courthouses: Better Planning Needed Regarding Reuse of Old Courthouses*, (Washington, D.C.: November 7, 2013).

³¹In 2001, GSA noted that at the time, 97 percent of returns on investments came from only about 53 percent of the buildings in the portfolio and that many owned properties were contributing little or nothing in terms of reinvestment dollars. According to GSA, this created an unsustainable dis-equilibrium between conditions and available resources.

equity and reducing vacant space that does not produce revenue and leads to lower net operating income.³²

However, it is not clear to what extent these efforts have addressed the issues GSA identified with the long-term sustainability of the portfolio in 2001. We have found that the most effective results-oriented management takes steps beyond strategic planning (such as GSA's 2001 restructuring strategy) and performance measurement (such as GSA's return on equity and vacant space goals). The leading results-oriented organizations we have observed applied their acquired knowledge and data to identify the gaps between actual performance levels and the levels necessary to achieve desired outcomes. In fact, we have found that this is the only performance data that can be truly useful.³³ In the case of GSA portfolio management, identifying the performance gap would mean determining the level of performance the portfolio needs to exhibit to be financially sustainable long-term, as envisioned by its 2001 restructuring strategy; however, GSA has not taken this action.

More specifically, when GSA developed its 2001 strategy, the agency determined that the portfolio was too large and that a "substantial" number of poor-performing buildings needed to be removed. GSA noted that it could afford to retain some of the "fringe" assets (including certain

³²Return on equity is a component of the Tier 1, 2a, and 2b tests. Net operating income is used in determining return on equity, so it is also a component of the Tier 1, 2a, and 2b tests. In addition, net operating income is a component of the Tier 3 test. (GSA defines an asset's return on equity as its net operating income divided by its value.) GSA set a goal to achieve a 6 percent return on equity on 78.9 percent of its assets in fiscal year 2015. GSA had the same goal in fiscal years 2012, 2013, and 2014 and achieved a 6 percent return on equity on 71.8, 72.4, and 73.9 percent of its assets respectively. In 2011, GSA set a goal to achieve a 6 percent return on equity on 78.6 percent of its assets and achieved the 6 percent return on 76.1 percent of its assets. GSA also has a goal to keep vacant space at or below 3.2 percent in fiscal year 2015 and fiscal year 2016. GSA had the same goal for the previous four years. During this time, GSA met the goal in fiscal year 2012, achieving a 3 percent vacancy rate. In fiscal years 2011, 2013, and 2014, GSA's vacancy rate was 3.4, 3.8, and 3.6 percent respectively.

³³See GAO, *Executive Guide: Effectively Implementing the Government Performance and Results Act*, [GAO/GGD-96-118](#) (Washington, D.C.: June 1996). We studied a number of leading public-sector organizations that were successfully pursuing management reform initiatives and becoming more results-oriented. In particular, we studied state governments, such as Florida, Oregon, Minnesota, North Carolina, Texas, and Virginia; and foreign governments, such as Australia, Canada, New Zealand, and the United Kingdom. Many of these organizations found themselves in an environment similar to the one confronting federal managers. In this work, we identified key steps that agencies need to take toward the implementation of the Government Performance and Results Act of 1993 (GPRA), along with a set of practices that have made implementation a success in results-oriented organizations.

heritage properties for which federal ownership is a symbolic must) that are economic drains on the portfolio, but only a limited number because over-subscribing to these fringe performers would perpetuate the problem of having too few funds to address too many needs. However, because GSA has not taken further steps since it adopted the restructuring strategy in 2001 to identify how many poor-performing buildings need to be removed, which fringe buildings can be kept, and the amount of economic loss from poor performers that can be absorbed, the long-term sustainability of the portfolio is unclear. Without taking the next step in results-oriented management and assessing this performance gap or determining if one exists at all, GSA cannot say whether any improvements indicated by, for example, increased disposals and returns on equity or decreased vacancy rates are enough to fully address the problem the restructuring strategy was developed to address in 2001—too few funds for too many buildings.

Such an assessment could also enhance GSA's communication with Congress about its portfolio, which could, in turn, help Congress make more informed resource allocation decisions affecting the portfolio. This communication is particularly important in the case of funding GSA's buildings, because Congress sets annual limits on the resources GSA allocates to sustain its buildings portfolio. When discussing the performance gap with GSA officials, they noted that they have generally not received consistent levels of obligational authority which hinders them from assessing the gap between their current level of performance and the level needed for a sustainable portfolio. However, a consistent assessment of the gap between the portfolio's performance and the level that portfolio would need to exhibit for long-term sustainability would provide valuable information over time and would help GSA ensure that the obligational authority it seeks is strategically aligned with the long-term sustainability of the portfolio. Further, over time, GSA would be able to conduct a trend analysis in funding levels, and the gap between performance and funding, to determine to what extent, if any, the agency still faces the risks to the overall health of the portfolio that it found in 2001.

GSA's Quantitative Measures of Building Performance Are Limited

While assessing GSA's progress toward sustainability could provide many benefits, it is not clear that GSA's tiering and core asset analysis effectively contribute to such an assessment. We separately interviewed non-governmental real estate experts representing eleven professional, industry, and trade associations about GSA's financial measures as defined in its tiering methodology and asked them to comment on the

methodology and to identify improvements that could be made. The experts we spoke with identified several limitations with GSA's tiering method, limits that generally accorded with our analysis. Examples of limitations we heard from the experts include the following:

- *Tiering methods may be outdated.* Experts we spoke with said that financial measures—such as those used in tiering—should be updated on a periodic basis.³⁴ For example, experts from one organization told us that the market environment can change significantly over time and periodic updates would ensure that tiering is reflective of market conditions. However, although GSA has modified its approach to determining values for two components used in the tiering formulas (facility condition index and functional replacement value) the agency has not updated its tiering method since it was first introduced in 2002.³⁵
- *Tiering does not enable comparison of the efficiency of assets.* One expert observed that tiering indicates the relative financial performance of GSA's assets considered from a profit-making (net income) viewpoint, thus treating public-use buildings as commercial properties. Conceptually, this reflects GSA's financial circumstances rather than efficiency of the portfolio because, as that expert told us, the central criterion used for tiering does not reflect efficiency aspects of building performance that are critical for public assets and used almost universally in other countries, such as annual operations and maintenance expenses per square foot of building space or space consumption per employee. For example, while GSA could determine an asset to be performing well because it generates sufficient revenue, it might operate (as indicated by cost per square foot of building space) or be used (as indicated by space occupied per employee) less efficiently than comparable GSA assets in different markets or non-GSA assets. According to this expert, using efficiency measures that allow like-for-like comparisons would enable GSA to compare assets in its portfolio, set benchmarks for assets' performance, and better inform GSA's decisions related to the long-

³⁴Experts suggested reviewing and updating financial performance indicators on intervals ranging from 1 to 5 years.

³⁵According to GSA officials, GSA altered the way it interpreted facility condition index (FCI) in fiscal year 2008. In particular, GSA changed the criterion for "good" condition—from an FCI of 0.3 to an FCI of 0.1. In addition, GSA adopted in fiscal year 2011 a new methodology for determining functional replacement value by switching to the Project Cost Planning Guide (which was based on a 2010 unit cost study) as a basis for determining functional replacement value.

term disposition of individual buildings. In addition, we believe that if the tiering measures allowed comparing the efficiency of assets' performance, this step would position GSA to be responsive to OMB's recently released *National Strategy for the Efficient Use of Real Property (National Strategy)*³⁶ which emphasizes calculating performance of assets to provide valuable information on efficiency related to property costs and utilization. If GSA were to update its tiering measures in such a way that efficiency could be compared among assets, GSA's tiering would be better suited to meet this new directive and could possibly be modified for other federal agencies' use.

- *Tiering does not account for rent limitations that skew results on financial performance.* GSA charges market-based rents which determine an asset's net operating income, a key tiering formula input. However, we found in cases where GSA is precluded from charging market-based rents due to rent limitations, the associated assets may be non-performing because of their limited ability to generate income. As experts observed, this distorts the tiering analysis and limits GSA's ability to compare assets based on actual performance of the building itself. Moreover, a 2001 study commissioned by GSA recommended that GSA quantify the impact of buildings within its portfolio that are exempted from rents or enjoy reduced rents, steps that would have addressed this issue.³⁷ If GSA did quantify the impact as suggested by the study, it would provide greater transparency on the scope of GSA's responsibilities that go beyond what is commonly expected in the maintenance of GSA buildings—namely that GSA assumes costs that would normally be borne by agencies which benefit from rent limits.
- *Functional Replacement Value may be inaccurate or overstated.* Some experts observed that an asset's functional replacement value may be an inaccurate indicator of value, and our analysis shows that its use in tiering effectively precludes some assets from moving beyond a Tier 3 designation. For example, the G. W. Andrews Federal Building and U.S. Courthouse in Opelika, Alabama, has a fair market

³⁶Office of Management and Budget, *National Strategy for the Efficient Use of Real Property, 2015-2020*: (Washington, D.C.: 2015).

³⁷In addition, the same report recommended that GSA classify its buildings by economic value or value added into four categories: national treasure buildings, generic office or workplace buildings, generic warehouse or storage buildings, and special purpose buildings (laboratories, border stations, etc.). See GSA, *Agenda for Strategic Change: Report to the Commissioner of Public Building Services Prepared by the Counselors of Real Estate Consulting Corps Panel*, (Washington, D.C.: September 2001).

value of \$400,000; however, the functional replacement value used in the tiering tests is \$5.9 million (almost 15 times the building's market value).³⁸ For this building to ever move beyond a Tier 3 ranking, the net operating income would have to annually exceed \$119,000 (2 percent of functional replacement value), an amount more than 25 percent of the building's market value and unlikely to be achieved. In addition, GSA's method of measuring functional replacement value assumes assets will be replaced with same-sized buildings, but future buildings may be smaller.³⁹ Moreover, OMB has recently issued a policy that requires agencies to reduce their space⁴⁰ as well as its *National Strategy* that emphasizes agencies will use less space to accomplish their mission in the future due to technology advances and increased telework. Because future space requirements are likely to be less than current needs, using functional replacement value—that assumes a same-sized replacement—as a determinant in the tiering formula may overstate the government's future needs.

- *Reinvestment assumptions in tiering analysis could be more accurate.* GSA's Tier 3 test assumes that annual reinvestment for ongoing maintenance and repair and an asset's eventual replacement should exceed 2 percent of its functional replacement value. However, some experts observed that applying a fixed level of investment based on a building's replacement value may not accurately reflect its maintenance and repair needs. Some of these experts also said that buildings' maintenance and repair needs are dissimilar due to differences in age, physical condition, location, and building

³⁸For more information on the large difference between replacement value and market value, see [GAO-12-645](#).

³⁹GSA officials told us that they calculate functional replacement value for tiering in the same way that it is calculated in Federal Real Property Profile guidance. This guidance has directed agencies to calculate functional replacement value defined as the amount required to construct an asset of a similar size and in the same location at today's construction standards. In calculating the replacement value, agencies have been directed to assume that they will replace the asset with one of the same size. (See General Services Administration, *Federal Real Property Council, 2013 Guidance for Real Property Inventory Reporting*, (Washington, D.C.: July 2013).

⁴⁰See, Office of Management and Budget, *Management Procedures Memorandum No. 2015-01. Implementation of OMB Memorandum M-12-12 Section 3: Reduce the Footprint* (Washington, D.C.: Mar. 25, 2015). This memorandum sets policy to "Reduce the Footprint" and expands upon the "Freeze the Footprint" policy implemented in 2013, which stated that federal building space as of fiscal year 2012 could not be increased without a reduction of the same size elsewhere (Office of Management and Budget, *Management Procedures Memorandum No. 2013-02. Implementation of OMB Memorandum M-12-12 Section 3: Freeze the Footprint*, (Washington, D.C.: 2013)).

components, among other factors. As such, the Tier 3 diagnostic would provide a more accurate indication of asset non-performance if it were based on specific estimates of maintenance and repair needs as opposed to a less precise proxy measure of these needs.

- *Tiering does not consider the physical condition of all assets.* GSA describes tiering as a measure of the financial health and physical condition of its assets yet does not use condition information in a consistent manner in tiering formulas. GSA's tiering calculations for generally performing assets (Tier 1 and Tier 2a) are based, in part, on the assets' physical condition as measured by the facility condition index (see table 1). However, GSA does not use a physical condition measure in tiering calculations pertaining to poorly performing assets (Tier 2b and 3). According to one expert, using condition information in all tiering levels would make comparison across tiers more meaningful because assets in each tier would be assessed on the same indicators (financial performance and condition). Another expert noted, for example, that the Building Owners and Managers Association (BOMA) International's method of classifying buildings is based, in part, on using common measures—such as rent, building finishes, and location—that enables comparisons to be made.⁴¹

While the experts stated that financial measures such as GSA's tiering measures should be updated periodically and have identified some potential considerations when updating measures, GSA officials said that they have not updated their tiering methods because they want to be able to compare tiering results for the same assets over time. However, we question whether the benefits of keeping the tiering formulas as they are outweigh the potential benefits an update could provide. Also, in addition to experts' observations on tiering's limitations, we found that GSA does not use its tiering process in the way the 2001 restructuring strategy envisioned. In this strategy, GSA noted that the tiering diagnostic should indicate a particular approach to managing each asset. For a Tier 3 asset, for example, GSA's 2001 strategy would indicate that the building is a

⁴¹The Building Owners and Managers Association (BOMA) International—comprised of owners and managers of commercial property, including nearly 10-billion square feet of office space in the United States—is a widely recognized source of building definitions, standards and information on real estate industry trends. The Building Owners and Managers Association (BOMA) International divides office buildings into three classes: Class A, Class B, and Class C. Class A buildings are defined as the most prestigious buildings, commanding above average rents, competing for premier office users and include state-of-the-art systems, among other attributes. Class B buildings have average rents for the locale, compete for a wide range of users and include adequate building systems. Class C buildings have rents below average for the locale and compete for tenants requiring only functional space.

candidate for disposal and capital expenditures should generally be limited to fund critical repairs. However, most of the GSA regional officials we interviewed told us that tiering results are not currently used as a leading or deciding factor for consideration in their strategic asset-management decisions, such as for reinvestment in, or disposal of, assets; but rather, this factor is just one of many considerations. Furthermore, in contrast to what GSA's 2001 strategy would suggest, we found that instead of minimal reinvestment, Tier 3 assets received more reinvestment funds than assets in any other tier during the 5 fiscal years 2010 through 2014. Specifically, we found that during this period, Tier 3 buildings received 43 percent of reinvestment funds.⁴² In addition, when the average Tier 2B and Tier 3 reinvestments are combined, we found they account for the majority—or 52 percent—of reinvestment expenditures during this period (see table 2 below).

Table 2: Breakdown of the General Services Administration's (GSA) Reinvestment Funds by Tier for its Owned Buildings, Fiscal Years 2010–2014 (Percentages Rounded)

	Tier 1 ^b	Tier 2a ^b	Tier 2b ^b	Tier 3 ^b
Average reinvestment ^a expenditure per year	\$157 million 30 percent	\$94 million 18 percent	\$46 million 9 percent	\$219 million 43 percent
(Tier 1+Tier 2a)	\$251 million 48 percent			
(Tier 2b+Tier 3)			\$265 million 52 percent	

Source: GAO analysis of GSA data, GAO 15-609

^aReinvestment expenditures are comprised of minor and major repair and alteration level projects. Decisions involving minor repair and alteration projects are made within GSA and do not require a

⁴²In this context, we are referring to reinvestments as funds for minor and major repair and alteration projects. Minor projects are projects with estimated costs below the prospectus level, which in fiscal year 2014 was \$2.85 million. Major projects are projects with estimated costs above the \$2.85 million threshold. A major repair and alteration project requires GSA regional offices to submit a prospectus to GSA headquarters where it is reviewed both by headquarters staff and then by OMB. If OMB approves the project, it is included as part of GSA's budget request to Congress and the prospectuses are submitted to the Senate Committee on Environment and Public Works and the House Committee on Transportation and Infrastructure for authorization. In addition, major repairs and alterations are generally included as line items in GSA's annual appropriation, which provides the whole Congress with an opportunity to decide whether or not to authorize the project and appropriate project funds as part of the annual appropriations process.

prospectus to be sent to OMB and the Congress. Major repair and alteration projects, or projects with an estimated cost greater than \$2.85 million, require GSA to submit a prospectus to OMB and, if approved, to the Congress for funding.

^bAs noted above, the tiering process categorizes the financial performance of buildings: Tier 1 and Tier 2 buildings are buildings with good financial performance, with Tier 2A buildings requiring significant capital investment unlike Tier 1 buildings, which do not; Tier 2B buildings are financially underperforming buildings while Tier 3 buildings are financially non-performing buildings. Tier 3 buildings are distinguished from Tier 2B buildings in that they are unable to generate sufficient revenue over 50 years to cover the cost of replacement.

In describing changes to their approach to asset management since implementation of the 2001 restructuring strategy, GSA developed core asset analysis in fiscal year 2008 to address tiering's limitations. In particular, core asset analysis was designed to complement tiering and provide more sophisticated analytical tools in order to enable GSA managers to become more strategic in decision making and to "right-size" the portfolio. However, we found limitations in core asset analysis, indicating that it may be imprecise and not useful to fully inform strategic decisions and to address tiering's limitations. For example:

- Most assets that fail the overall core asset analysis are nevertheless classified as core. If an asset fails one or more of the three areas of tests included in the core asset analysis (customer, market, or asset), asset managers can complete a justification to classify the asset as core, despite the failed test(s). These justifications are used to justify holding an asset long-term, even though this does not align with the results of the diagnostic tests. While there may be instances in which it makes sense to justify the retention of an asset that fails the quantitative tests, we found that in fiscal year 2013, GSA justified 257 (over 74 percent) of the 345 buildings⁴³ (in the population of buildings that we considered in this review) that failed the quantitative core asset analysis tests. The large percentage of assets that were justified to be core assets despite failing the quantitative tests suggests that these tests are not efficiently identifying buildings that are needed over the long-term and core to federal missions. This outcome, in turn, raises questions as to whether the quantitative measures are adding the necessary sophistication to support strategic decision making and "right-sizing" the portfolio as GSA intended.

⁴³As stated previously, we considered 1,283 buildings for our review based on buildings that have had at least five years of tiering data. Of those 1,283 buildings, 133 did not have data for core asset analysis because they did not have assignable space (GSA only conducts core asset analysis on buildings with assignable space). The 345 buildings that failed the test were out of a smaller population of 1,150 buildings.

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- GSA does not apply the results of one core asset test that would lead to a comparatively greater number of buildings failing the core asset tests. As noted previously, an asset that fails the Asset Lifecycle Test—intended to measure whether reinvestment would extend the life of the asset—may nonetheless still be considered a core asset. We found that 195 buildings failed only the Asset Lifecycle Test in fiscal year 2013 and thus were still designated as “core.” If the Asset Lifecycle test were governed by the same rules as the other core asset tests—that it had to be passed for an asset to be considered “core” without a justification—and the assumption is made that all 195 buildings that failed this test in fiscal year 2013 would remain “core” assets along with the 257 other assets quantitatively determined to be non-core but justified to be core by managers’ justifications, then overall, about 84 percent of assets that fail the quantitative portion of the core asset analysis tests would be changed from non-core to core. GSA officials said the Asset Lifecycle Test is not used to determine an asset’s status because failing it may indicate that historical, political, security, or other non-quantifiable considerations may be increasing the scope of the reinvestment projects but not necessarily contributing to extending the asset’s life. However, these same considerations may also affect the other core asset tests, so it is not clear why the Asset Lifecycle Test is treated differently than the other core asset tests in determining an asset’s status.

If Strengthened, GSA’s Quantitative Building Measures Could Support Recent Government-Wide Strategic Objectives

OMB’s recently issued *National Strategy*, discussed previously, aligns in two important ways with GSA’s 2001 portfolio restructuring strategy and subsequent adoption of tiering. First, OMB’s *National Strategy* emphasizes the importance of data-driven decision making, noting that performance should be calculated in order to provide valuable information on efficiency and to help find targets for reducing space. In particular, the *National Strategy* states that measuring the performance of assets should result in the identification of inefficient locations that are “ripe for action.” This is consistent with the original intent of GSA’s portfolio restructuring strategy, which envisioned a tiering process based on measures that would identify buildings that could be disposed. However, as stated previously, GSA does not use tiering as a leading or deciding consideration in making asset management decisions the way the restructuring strategy described. Second, the *National Strategy* states that one of the desired outcomes of the strategy is to ensure the long-term fiscal sustainability of the federal real property portfolio as was also intended by GSA’s 2001 restructuring strategy and subsequent development of tiering. Hence, while important aspects of GSA’s 2001 portfolio-restructuring strategy relate closely to OMB’s *National Strategy*,

the way GSA currently uses tiering is not clearly aligned with either strategy. For example, buildings critical to government operations such as those in the White House complex exist in the same bottom tier as those that may be candidates for disposal. As a result, differences between mission-critical buildings and less-important non-performing buildings are obscured and make it more difficult to determine the efficiency of the portfolio. Further, it is not clear to what extent core asset analysis provides any greater clarity on portfolio efficiency considering that most of the assets that fail the tests are justified as core. This raises questions as to whether GSA's quantitative measures are truly data-driven as called for by the *National Strategy*.

GSA officials told us that tiering was useful in its early days to identify the “low-hanging fruit”—buildings that were clearly problematic and ones that could readily be disposed.⁴⁴ However, now that these clearly problematic assets have been disposed, those that fall into Tier 3 are not necessarily viewed as candidates for disposal for many of the reasons discussed previously in this report. In particular, we found that in fiscal year 2013, when both tiering and core asset analysis were taken into consideration, GSA designated almost 70 percent of its consistently poor-performing assets for long-term hold (greater than 15 years), including 25 of the 33 buildings with the greatest losses in net operating income (accounting for over \$31.5 million in average annual loss over 5 years, see app. II).⁴⁵ This raises questions as to whether this is the amount of “fringe” assets GSA's restructuring strategy envisions can be sustained long term by the rest of the portfolio or if more needs to be done to cull this group of poor performers—including refining tiering measures to effectively identify them—to ensure that there are not too few funds for too many buildings. Given the limitations with GSA's tiering measures identified by the experts we spoke with—including that they may be outdated and do not assess efficiency, a prime focus of OMB's *National Strategy*—GSA could update its tiering process to address those limitations and increase the precision of its financial measures. Further, core asset analysis could be updated to

⁴⁴GSA officials told us that they have disposed of almost 370 assets between 2001 and 2013; however, the officials did not track disposals according to tiering data, so GSA officials did not have data on the tier of the disposed assets.

⁴⁵As stated previously, we considered 1,283 buildings for our review based on buildings that have had at least 5 years of tiering data. Of those 1,283 buildings, 251 were considered to be consistently poor-performing buildings. Of those 251, 21 did not have data for core asset analysis because they did not have assignable space (GSA only conducts core asset analysis on buildings with assignable space). Therefore, the 70 percent is based on the 230 buildings that had core asset analysis data.

better identify “core assets” in a way that is truly data-driven. If the output of both measures—tiering and core asset analysis—were more refined, they could be more useful in assessing the performance gap in the sustainability of GSA’s portfolio and also for supporting OMB’s *National Strategy*.

Conclusions

GSA recognized in 2001 that—based on the age and deteriorating condition of its buildings and the available funding for its buildings—a new approach to managing the portfolio was needed to address issues affecting long-term sustainability. While GSA has stated its intent to transform its portfolio into one that is made up primarily of strong income-producing assets, it has not identified what such a portfolio would look like. Real property management remains a high risk area for the government, and GSA continues to face challenges with assets in GSA’s owned portfolio that have limited management options, such as those in smaller markets or with rent reductions, and therefore is likely to always have some buildings that are poor financial performers and that will need to be retained. Thus, it is important for GSA to assess any performance gap between how well the overall portfolio must perform financially to absorb the effects of these poorly performing buildings that GSA must keep, regardless of financial performance, and the portfolio’s current level of performance. Without this assessment, GSA cannot know the extent to which it still faces the grim forecast that it made in 2001 of having too few funds to address too many buildings. If GSA identified what the composition of the portfolio needs to look like in terms of financial performance to ensure long-term sustainability and compared this desired condition to the current state of the portfolio, decision makers inside GSA and in Congress would have better information to determine what further steps and resources are needed, if any, to structure the portfolio toward that end.

Distinguishing between poorly performing buildings may require more precision than GSA’s current measures provide. Private-sector real estate experts stated that GSA’s tiering measures are limited and could provide greater nuance to the information they obtain on financial performance, nuance that could facilitate a sharper evaluation of the portfolio. For example, GSA could revise its measures in such a way that they compare efficiency of assets, a step that would align with OMB’s *National Strategy*. Further, GSA’s core asset analysis was intended to help GSA right-size the portfolio, but the vast majority of assets that fail these tests are justified as core, indicating the tool could use more refinement. Better measures could also help GSA evaluate its progress toward a sustainable

portfolio in the long run and help the agency to provide better information to Congress on the scope of its challenges that may not be clear with the level of detail present in current measures.

Recommendations for Executive Action

To assist in determining progress toward a long-term, sustainable portfolio, the Administrator of GSA should identify the gap between the portfolio's current level of performance and the level necessary to sustain the portfolio. As part of this effort, GSA should review its tiering and core asset analysis measures and update them to provide more precise measures that can be used in identifying this performance gap.

Agency Comment

We provided a draft of this report to GSA for its review and comment. GSA provided written comments which are reproduced in appendix III. GSA concurred with our recommendation. As GSA explains in its written comments, it is developing a comprehensive plan to address the recommendation and intends to consult with real estate leaders to assist this effort.

As agreed with your office, unless you publicly announce the contents of the report earlier, we plan no further distribution until 30 days from the report date. At that time, we will send copies to the appropriate congressional committee and the Acting Administrator of GSA. In addition, the report will be available at no charge on GAO's website at <http://www.gao.gov>.

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

Sincerely yours,



David Wise
Director, Physical Infrastructure Issues

Appendix I: Objectives, Scope, and Methodology

This report focuses on (1) the steps GSA has taken to address buildings that consistently exhibit poor financial performance, challenges GSA faces from poorly performing buildings, and the extent to which GSA has sustained losses from these buildings and (2) the progress, if any, GSA has made toward building a portfolio of strong performing buildings, including the extent to which GSA's quantitative building measures provide useful information for determining that progress.

To address the first objective, we reviewed relevant GAO, Congressional Research Service, Office of Management and Budget (OMB), and National Research Council documents. In addition, we reviewed relevant GSA documentation, including testimony of GSA officials before Congress, GSA's State of the Portfolio documents, GSA Office of Inspector General audits, agency-wide financial reports, a rent pricing guide, and disposal guidance, among others. We also reviewed and analyzed memoranda of understanding between GSA and other agencies regarding rent limitations for diverse buildings such as the White House and regional Social Security Administration offices, and the relevant federal statutes and regulations. We obtained tiering data from GSA on its portfolio of owned buildings for the fiscal years 2002 through 2013 (as long as GSA has been tiering buildings including the most recent year for which data were available). To assess the reliability of these data, we interviewed GSA officials to identify the sources of these data and how they are collected, maintained, and processed. These officials included staff from GSA information technology, financial management, and portfolio management units. We also collected and reviewed documentation on the various computerized data systems used as inputs for the tiering process. While GSA develops the tiering data by collecting and manually entering information from various computerized data systems into an Excel spreadsheet where the tiering diagnostic is performed, GSA has a process to manually validate the data by checking for outliers in the results computed by the Excel program. Based on our review of documentation for each of the systems inputting data for tiering tests, our interviews with the cognizant GSA officials, and our own electronic testing of the tiering data, we determined that tiering data were sufficiently reliable for our purposes. We analyzed the data to determine which buildings received non-performing (Tier 3) or under-performing (Tier 2b) tiering results at least 75 percent of the time period that they

were tiered.¹ This analysis resulted in a population of 251 buildings, which we refer to as consistently poor-performing buildings. We analyzed tiering data to determine the characteristics of these consistently poor-performing buildings—such as size, age, value, condition, historical status, and location, among others—and compared them to the rest of the GSA buildings considered in our review. Finally, from this population of 251 consistently poor-performing buildings, we identified 33 buildings that had an average net loss of \$100,000 or more for five 5 fiscal years from 2009 through 2013.² We reviewed documentation for these buildings, including GSA's annual *Asset Business Plans*, among other documents. We also interviewed the managers of these buildings to learn more about the factors contributing to the large losses. We selected 12 buildings from this population for site visits based primarily on their geographical distribution for site visits. These buildings were located in California, Missouri, Illinois, and the District of Columbia.³ We also visited two additional sites—a building in the District of Columbia and a federal facility in Maryland—that were not among the 33 substantial underperformers. In addition, we reviewed documents and interviewed officials at all 11 of GSA's Regional Offices and officials at GSA Headquarters to learn about how the agency manages consistently poor-performing buildings.

To address the second objective, we reviewed GSA documents including portfolio strategic-planning documents; the 2001 document outlining the strategy for restructuring the portfolio (including tiering); the internal

¹We only considered buildings that had at least 5 years of tiering data for the purposes of this review. We also used only owned buildings and excluded all other asset categories (e.g., land, structures, etc.) during our review. Once we removed the buildings without 5 years of tiering data and assets that were not GSA buildings, we divided the population into two populations that we use throughout this report. Those that were categorized as non-performing or under-performing for 75 percent or more of the time, we call "consistently poor-performing buildings," and the rest are "other buildings."

²For the purposes of this report, we defined loss as negative net operating income—a measure of revenue minus some expenses.

³Of the 33 buildings with an average net loss of \$100,000 or more, we visited three buildings in Washington, D.C., the city where GSA is headquartered. (We did not visit buildings associated with the White House due to security limitations, and we did not visit a building managed by the U.S. Department of Agriculture that is still owned by GSA. Of the four buildings that remained, three were in the top five in terms of loss, and we visited those three.) We also visited a building in San Francisco, California, due to its location on the West Coast and because it was the building outside of Washington, D.C., that recorded the largest loss. Finally, we visited seven buildings in the central part of the U.S. (Missouri and Illinois) because all of these buildings were geographically close enough to drive in one week's time.

policies and procedures related to the tiering tests; and documents on how tiering is computed. We also reviewed OMB memorandums and documents regarding federal real property management and reporting policies. We performed “sensitivity analyses” on tiering data elements to better understand how these elements were affected by key assumptions.⁴ We also interviewed GSA Headquarters officials about their tiering methodology and officials from GSA’s 11 regional offices to determine how tiering results are used to manage the national portfolio. Based on past GAO work, reviews of GSA documents, and internal and external recommendations, we selected 11 real estate industry organizations representing a range of domestic and international professional, industry, and trade associations and asked them to identify experts within their organizations who were knowledgeable about the measurement of financial performance and could identify key measurement practices that might be applicable to GSA’s management of federal government property. We interviewed experts from the following organizations:

1. Ron Kendall and Associates
2. NORC at the University of Chicago
3. VFA, Inc.
4. International Facility Management Association
5. Counselors of Real Estate
6. Signet Partners
7. Ernst and Young, LLP
8. National Federal Development Association
9. Green Street Advisors
10. Building Owners and Managers Association (BOMA) International
11. Royal Institution of Chartered Surveyors

With GSA’s permission, we shared the tiering methodology with these individuals and interviewed them to obtain their views on the tiering methodology, and obtained their suggested improvements. In addition,

⁴“Sensitivity analysis” is a technique used to determine the effect that changing key assumptions may have on outcomes. For example, we performed various sensitivity tests on GSA’s tiering methodology including testing the effects on tiering results if 3 percent, 4 percent or 1 percent of functional replacement value were used instead of 2 percent as GSA currently uses in the Tier 3 test.

we also obtained their opinion regarding whether certain key private sector practices might help the government improve the financial performance of its buildings. In addition, we reviewed 2013 data and documentation from GSA for another key building measurement—core asset analysis. Core asset analysis was designed to complement tiering⁵ information and enhance GSA's strategic decision making. This analysis uses five additional quantitative tests that include assessing a building's customer needs, market condition, and reinvestment needs. As with the tiering data, we interviewed GSA officials to identify the sources of these data and how they are assembled, and we collected and reviewed documentation on the various computerized data sources providing inputs to core asset analysis processes. While GSA develops the core asset analysis data by collecting and manually entering information from various computerized data systems into an Excel spreadsheet where the core asset diagnostic is performed, GSA has a process to manually validate the data by checking for outliers in the results computed by the Excel program. We determined that these data were sufficiently reliable for our purposes. We analyzed core asset test results to determine how many of the assets that received non-core designations were subsequently changed to core through narrative justifications given by regional managers based on qualitative factors not captured by the core asset tests. As with tiering data, we also conducted several sensitivity analyses on core asset tests' data to understand key assumptions and test the impact their change would make on the results. We interviewed GSA headquarters and regional managers on how the combined tiering and core asset analysis results are used in making investment decisions and managing the national portfolio, and compared their statements with our analysis of GSA data on the portfolio-wide allocation of reinvestment funding by tier and core asset designation from fiscal years 2010 through 2014. We also reviewed a new *National Strategy for the Efficient Use of Real Property (National Strategy)* from the Office of Management and Budget (OMB) to determine whether GSA's quantitative building measures are useful for implementing that strategy.⁶

⁵According to GSA's 2008 State of the Portfolio, core asset analysis was created to facilitate strategic decision making with an analytic tool more sophisticated than tiering and would quantify the three facets of GSA's portfolio strategy: customer demand, market viability, and asset considerations. The quantitative portion of core asset analysis consists of five quantitative tests designed to measure a building's customer needs, market condition, and reinvestment needs

⁶Office of Management and Budget, *National Strategy for the Efficient Use of Real Property, 2015-2020*: (Washington, D.C.: 2015).

We conducted this performance audit from June 2014 through July 2015 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Appendix II: Challenges Contributing to the 33 Buildings with the Largest Average Loss (Net Operating Income), Fiscal Years 2009–2013

		Average annual net operating income (fiscal years 2009–2013)	City, state	Holding period as designated by GSA fiscal year 2013	Challenges contributing to consistently-poor performance based on interviews with GSA officials and building documents
1	Dwight D. Eisenhower Executive Office Building	– \$7,550,023	Washington, DC	Long term, > 15 years	<i>Rent Limitations</i> (White House Memorandum of Understanding); <i>High Vacancy</i> (renovations); <i>High Costs</i> (high security and operation and maintenance costs due to mission serving the Executive Office of the President).
2	Postal Square	– \$7,195,148	Washington, DC	Long term, > 15 years	<i>Rent Limitations</i> (GSA has signed a triple net lease on this building requiring the tenant (GSA) to pay for costs of operation and maintenance, building repairs, taxes and insurance until 2022).
3	National Building Museum	– \$3,836,668	Washington, DC	Long term, > 15 years	<i>Rent Limitations</i> (legal limitation – GSA receives no rent on this building from the museum—the primary tenant—per legislation); <i>High Costs</i> (high security and operation and maintenance costs due to mission of the museum).
4	White House-West Wing	– \$3,180,093	Washington, DC	Long term, > 15 years	<i>Rent Limitations</i> (White House Memorandum of Understanding); <i>High Costs</i> (mission serving the Executive Office of the President and high General and Administrative costs).
5	Old Post Office Building	– \$2,806,502	Washington, DC	Long term, > 15 years	<i>High Costs</i> (high security and operation and maintenance costs due to mission of an observation tower open to the public and the age of the building). Note: In 2013, GSA entered into a public private partnership with the Trump Old Post Office, LLC (a 60-year lease). The building is being converted into a hotel.
6	New Executive Office Building	– \$1,846,210	Washington, DC	Long term, > 15 years	<i>Rent Limitations</i> (White House Memorandum of Understanding); <i>High Costs</i> (high security and maintenance costs due to mission serving the Executive Office of the President and high General and Administrative costs).
7	Remote Delivery Site	– \$735,850	Washington, DC	Long term, > 15 years	<i>Rent Limitations</i> (White House Memorandum of Understanding); <i>High Costs</i> (high operation and maintenance costs due to mission serving the Executive Office of the President and high costs related to a ground settlement problem).
8	Federal Office Building, 50 United Nations Plaza	– \$731,743	San Francisco, CA	Long term, > 15 years	<i>High Vacancy</i> (renovations and changes in space needs). Note: GSA officials said that this building should eventually become a Tier 1 performer if GSA finds tenants to fill the space.

**Appendix II: Challenges Contributing to the 33
Buildings with the Largest Average Loss (Net
Operating Income), Fiscal Years 2009–2013**

	Building name	Average annual net operating income (fiscal years 2009–2013)	City, state	Holding period as designated by GSA fiscal year 2013	Challenges contributing to consistently- poor performance based on interviews with GSA officials and building documents
9	Thomas P. O'Neill Jr. Federal Building	– \$620,312	Washington, DC	Long term, > 15 years	<i>High Vacancy</i> (renovation). GSA officials said that this building is now a Tier 1 performer because it is fully occupied.
10	Jackson Place Complex: White House Conference Center	– \$594,198	Washington, DC	Long term, > 15 years	<i>Rent Limitations</i> (White House Memorandum of Understanding); <i>High Costs</i> (high General and Administrative costs).
11	Federal Building No 1	– \$269,304	Kansas City, MO	Short term, 0 to 5 years	<i>Market Conditions</i> (low rent revenues compared to functional replacement value). Building is being considered for disposal.
12	Federal Center Building 101	– \$256,372	St. Louis, MO	Long term, > 15 years	<i>Market Conditions</i> (low market rental rates); <i>High Vacancy</i> (building is empty and being considered for disposal); <i>Age</i> (built in 1942).
13	Silvio O. Conte Federal Building	– \$236,650	Pittsfield, MA	Mid term, 6 to 15 years	<i>Rent Limitations</i> (Social Security Administration pays less rent than comparable markets per a memorandum of understanding); <i>Market Conditions</i> (low market rental rates); <i>High Costs</i> (high General and Administrative costs).
14	Social Security Administration District Office Building	– \$236,264	Quincy, IL	Long term, > 15 years	<i>Rent Limitations</i> (Social Security Administration pays less rent than comparable markets per a memorandum of understanding); <i>Market Conditions</i> (low market rental rates); <i>High Costs</i> (high General and Administrative costs due to a coding error that did not attribute construction costs correctly). Note: This building appears in our list of top 33 performers over five years due to the coding error. Without the coding error, this building is still a consistently poor performer due to the Social Security Administration rent credit and market conditions.
15	Federal Building, U.S. Post Office and Custom House	– \$226,012	St. Albans, VT	Long term, > 15 years	<i>Market Conditions</i> (geographic location); <i>High Vacancy</i> (some of the building space is difficult to fill).
16	1724 F St., NW	– \$195,652	Washington, DC	Long term, > 15 years	<i>Rent Limitations</i> (White House Memorandum of Understanding); <i>Age</i> (built in 1911); <i>High Costs</i> (high security and operation and maintenance costs due to mission serving the Executive Office of the President and high General and Administrative costs).

**Appendix II: Challenges Contributing to the 33
Buildings with the Largest Average Loss (Net
Operating Income), Fiscal Years 2009–2013**

Building name	Average annual net operating income (fiscal years 2009–2013)	City, state	Holding period as designated by GSA fiscal year 2013	Challenges contributing to consistently- poor performance based on interviews with GSA officials and building documents
17 Gerald W. Heaney Federal Building & United States Courthouse and Custom House	– \$189,337	Duluth, MN	Long term, > 15 years	<i>Market Conditions</i> (low rent revenues compared to functional replacement value, low market rental rates); <i>High Vacancy</i> (low federal backfill potential).
18 Federal Building and United States Courthouse	– \$179,921	Port Huron, MI	Long term, > 15 years	<i>Market Conditions</i> (low rent revenues compared to functional replacement value, low market rental rates); <i>High Vacancy</i> (low federal backfill potential in that market); <i>Age</i> (built in 1877); <i>High Costs</i> (geographic location, high operation and maintenance costs).
19 Jackson Place Complex, President's Guest Residence	– \$175,446	Washington, DC	Long term, > 15 years	<i>Rent Limitations</i> (White House memorandum of understanding; no rent is collected on this particular building).
20 G. W. Andrews Federal Building-United States Courthouse	– \$173,018	Opelika, AL	Mid term, 6 to 15 years	<i>High Vacancy</i> (low federal backfill potential in that market).
21 Prince H. Preston Federal Building	– \$172,621	Statesboro, GA	Mid term, 6 to 15 years	<i>High Vacancy</i> (low federal backfill potential in that market).
22 Federal Center Building 110	– \$157,214	St. Louis, MO	Long term, > 15 years	<i>Market Conditions</i> (low rent revenues compared to functional replacement value, low market rental rates); <i>High Vacancy</i> (low federal backfill potential in that market); <i>Age</i> (built in 1942).
23 Federal Center Building 103F	– \$154,572	St. Louis, MO	Long term, > 15 years	<i>Market Conditions</i> (low rent revenues compared to functional replacement value, low market rental rates); <i>High Vacancy</i> (building was flooded and closed for an extended time); <i>Age</i> (built in 1942).
24 William H. Natcher Federal Building and United States Courthouse	– \$149,603	Bowling Green, KY	Mid term, 6 to 15 years	<i>Market Condition</i> (geographic location); <i>High Costs</i> (high operation and maintenance costs due to geographic location).
25 Minneapolis Federal Building	– \$149,361	Minneapolis, MN	Long term, > 15 years	<i>High Vacancy</i> (obsolescence).
26 Agriculture South Building	– \$145,201	Washington, DC	Long term, > 15 years	<i>Rent Limitations</i> (The U.S. Department of Agriculture stopped paying rent); <i>High Costs</i> (coding error caused costs to be listed as higher than they were).

**Appendix II: Challenges Contributing to the 33
Buildings with the Largest Average Loss (Net
Operating Income), Fiscal Years 2009–2013**

	Building name	Average annual net operating income (fiscal years 2009–2013)	City, state	Holding period as designated by GSA fiscal year 2013	Challenges contributing to consistently- poor performance based on interviews with GSA officials and building documents
27	Hannibal Federal Building, United States Post Office and Courthouse	– \$137,676	Hannibal, MO	Mid term, 6 to 15 years	<i>Market Conditions</i> (low market rental rates); <i>High Vacancy</i> (low federal backfill potential in that market).
28	Federal Center Building 107	– \$117,456	St. Louis, MO	Long term, > 15 years	<i>Market Conditions</i> (low market rental rates); <i>High Vacancy</i> (low federal backfill potential in that market); <i>Age</i> (built in 1942).
29	Albuquerque Federal Building Courthouse	– \$116,551	Albuquerque, NM	Long term, > 15 years	<i>High Vacancy</i> (obsolescence).
30	Federal Building and United States Courthouse	– \$115,410	Anniston, AL	Mid term, 6 to 15 years	<i>Market Conditions</i> (geographic location); <i>High Vacancy</i> (low federal backfill potential in that market and obsolescence).
31	Federal Building-United States Court House	– \$114,921	Selma, AL	Mid term, 6 to 15 years	<i>Market Conditions</i> (geographic location, low market rental rates); <i>High Vacancy</i> (low federal backfill potential in that market).
32	Joe Skeen Federal Building	– \$114,233	Roswell, NM	Long term, > 15 years	<i>Market Conditions</i> (geographic location); <i>High Vacancy</i> (space in the process of being backfilled).
33	Robert C. McEwen United States Custom House	– \$105,071	Ogdensburg, NY	Long term, > 15 years	<i>Market Conditions</i> (geographic location, low market rental rates); <i>High Vacancy</i> (low federal backfill potential in that market).

Source: GAO analysis of General Services Administration (GSA) data, GAO-15-609.

Appendix III: Comments from the General Services Administration



The Administrator

June 29, 2015

The Honorable Gene L. Dodaro
Comptroller General of the United States
U.S. Government Accountability Office
Washington, DC 20548

Dear Mr. Dodaro:

The U.S. General Services Administration (GSA) appreciates the opportunity to review and comment on the U.S. Government Accountability Office (GAO) draft report entitled, *Federal Real Property: GSA Needs to Determine Its Progress toward Long-Term Sustainability of its Portfolio* (GAO-15-609). GAO recommends:

To assist in determining progress toward a long-term sustainable portfolio, the Administrator of GSA should identify the gap between its current performance and the level necessary to sustain the portfolio. As part of this effort, GSA should review its tiering and core asset analysis measures and update them to provide more precise measures that can be used in identifying this performance gap.

We have reviewed this report in depth, agree with the recommendation, and are developing a comprehensive plan to address the recommendation made to GSA. We are confident that our comprehensive plan will satisfactorily remedy the concerns raised by GAO.

GSA retains and invests in Federal assets where mission need and market dynamics make Federal ownership in the best interest of the taxpayer. In some instances there may not be commercial space alternatives to accommodate an agency's mission requirement. Our Local Portfolio Planning (LPP) initiative is an example of GSA's holistic approach to market-based, portfolio planning. The LPP process balances financial performance, customer requirements, market demand, space utilization, and investment needs in order to plan Federal housing needs as economically and efficiently as possible.

For our lowest performing financial assets, GSA continually performs economic analyses to make the right decision regarding reinvestment, disposal, and exchange opportunities. Using our integrated approach to portfolio strategy, we work to ensure

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our assets are utilized to the highest and best use and continue to divest our portfolio of assets that we are no longer able to cost-effectively maintain. GSA has been diligently disposing of underutilized assets that tiering and core asset analysis are designed to identify. Since fiscal year 2010, GSA has disposed of over 135 assets which have returned proceeds of over \$110 million to the Federal Buildings Fund.

While we recognize the unique differences between private and public sector real estate organizations, GSA will consult with industry leaders to glean applicable best practices to further strengthen our asset management approach. Both tiering and core asset analysis were originally developed in consultation with private industry leadership, and we will seek private industry input to continue to improve the portfolio evaluation process.

If you have any additional questions or concerns, please do not hesitate to contact me at (202) 501-0800, or Ms. Lisa A. Austin, Associate Administrator, Office of Congressional and Intergovernmental Affairs, at (202) 501-0563.

Sincerely,



Denise Turner Roth
Acting Administrator

cc: David Wise, Director, Physical Infrastructure Issues, GAO

Appendix IV: GAO Contact and Staff Acknowledgments

GAO Contact

David J. Wise, (202) 512-2834 or wised@gao.gov

Staff Acknowledgments

In addition to the contact named above, Michael Armes (Assistant Director), Lindsay Bach, Patricia Donahue, Amy Higgins, DuEwa Kamara, Jon Melhus, SaraAnn Moessbauer, Cheryl Peterson, Minette Richardson, Amy Rosewarne, and James Russell made key contributions to this report.

Appendix V: Accessible Data

Data Tables

Data Table for Highlights Figure: Average Annual Losses among General Services Administration’s Consistently Poor- Performing Buildings with Negative Net- Operating Income (NOI), Fiscal Years 2009 to 2013

Range of losses	Number of buildings in this range	Buildings combined total average negative NOI (in millions)	Buildings percent of negative NOI
\$1 to \$100,000	83	\$2.6	7.3%
\$100,001 to \$1,000,000	27	\$6.6	18.5%
\$1,000,001 and greater	6	\$26.4	74.2%
Total	116	\$35.6	100%

Source: GAO analysis of General Services Administration data. | GAO-15-609

Note: GAO reviewed 12 years of annual tiering data on 1,283 of GSA’s buildings (those in GSA’s 2014 inventory with at least 5 years of tiering data). GAO found 251 buildings that have been assessed through GSA’s measures as non-performing or under-performing at least 75 percent of the time. GAO refers to this group of 251 buildings as “consistently poor performing buildings.”

Data Table for Figure 1: Proportion of Buildings That Were Consistently Poor- Performing Buildings versus Other Buildings, End of Fiscal Year 2013 (Percentages Rounded)

Consistently poor-performing buildings (251 buildings)	20%
Other buildings (1,032 buildings)	80%

Source: GAO analysis of General Services Administration data. | GAO-15-609

Note: We reviewed 12 years of annual tiering data on 1,283 of GSA’s buildings (those in GSA’s fiscal year 2013 inventory with at least 5 years of tiering data). We found 251 buildings that have been assessed through GSA’s measures as Tier 3 (non-performing) or Tier 2b (under-performing) at least 75 percent of the time that they were tiered. We refer to this group of 251 buildings as “consistently poor-performing buildings,” and the other 1,032 buildings as “other buildings.”

Data Tables for Figure 4: Size and Value of General Services Administration's (GSA) Consistently Poor-Performing Buildings versus Other Buildings, End of Fiscal Year 2013

Mean rentable square feet [Note A]

Asset type	Square feet (in thousands)
Consistently poor-performing buildings	98.7
Other buildings	150.2

Average Value [Note B]

Asset type	Dollars (in millions)
Consistently poor-performing buildings	17.0
Other buildings	31.4

Source: GAO analysis of General Services Administration data. | GAO-15-609

Note: We reviewed 12 years of annual tiering data on 1,283 of GSA's buildings (those in GSA's fiscal year 2013 inventory with at least 5 years of tiering data). We found 251 buildings that have been assessed through GSA's measures as Tier 3 (non-performing) or Tier 2b (under-performing) at least 75 percent of the time that they were tiered. We refer to this group of 251 buildings as "consistently poor-performing buildings," and the other 1,032 buildings as "other buildings."

Note A: According to GSA, rentable space is the area for which a tenant agency is charged rent—the measurement of the area where a tenant normally houses personnel and/or furniture plus the associated share of floor common areas and building common areas. The rentable space may include a share of common areas such as elevator lobbies, building corridors, and floor service areas (e.g., restrooms, electrical closets, etc.). The rentable space does not include vertical building penetrations and their enclosing walls such as stairs, elevator shafts, and vertical ducts.

Note B: For most assets, value is the fair market value, determined by a recent third-party appraisal. For assets that do not have a recent third-party appraisal, either the construction cost for assets built within the past 10 years, or a calculated direct capitalization method is used to determine value.

Data Table for Figure 6: The General Service Administration's (GSA) Consistently Poor-Performing Buildings versus Other Buildings in Terms of Average Age, End of Fiscal Year 2013

Asset type	Building age (in years)
Consistently poor-performing buildings	70
Other buildings	47

Source: GAO analysis of General Services Administration data. | GAO-15-609

Note: We reviewed 12 years of annual tiering data on 1,283 of GSA's buildings (those in GSA's fiscal year 2013 inventory with at least 5 years of tiering data). We found 251 buildings that have been assessed through GSA's measures as Tier 3 (non-performing) or Tier 2b (under-performing) at least 75 percent of the time that they were tiered. We refer to this group of 251 buildings as "consistently poor-performing buildings," and the other 1,032 buildings as "other buildings."

Data Tables for Figure 7: The General Service Administration's (GSA) Consistently Poor-Performing Buildings versus Other Buildings in Terms of Condition, End of Fiscal Year 2013 (Percentages are rounded.)

FCI: Facility condition index [Note A] = The Facility Condition Index (FCI) is a measure of an asset's condition. It is the ration between total repair and alteration needs and the functional replacement value of an asset (i.e. the estimated cost of needed repairs divided by the asset's replacement value). The higher the FCI, the worse the condition of the asset.

Consistently poor-performing buildings

Poor (0.2 or greater FCI)	17%
Fair (0.1 to 0.2 FCI)	25%
Good (Less than 0.1 FCI)	58%

Other buildings

No value	Less than 1%
Poor (0.2 or greater FCI)	10%
Fair (0.1 to 0.2 FCI)	18%
Good (Less than 0.1 FCI)	72%

Source: GAO analysis of General Services Administration data. | GAO-15-609

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Note A: Our past work has found that the FCI may be unreliable because some agencies had a "practice of assigning no repair needs to many excess and underutilized buildings because agencies had no intention of repairing them." See GAO, Federal Real Property: National Strategy and Better Data Needed to Improve Management of Excess and Underutilized Property, GAO-12-645 (Washington, D.C.: June 20, 2012). In this report, we recommended that GSA develop and implement a plan to improve the Federal Real Property Profile data (condition is included in this data). GSA agreed with the recommendation. Because GSA may be less likely to dispose of their Tier 1 and Tier 2a buildings than their Tier 2b and Tier 3 buildings, this practice of assigning no repair needs to many excess and underutilized buildings may result in condition assessments for the consistently non-performing buildings that are better than is actually the case. That is, the consistently non-performing buildings may be in worse physical condition than is shown in the data.

Data Table for Figure 8: Average Annual Losses among the General Services Administration's Consistently Poor-Performing Buildings with Negative Net Operating Income (NOI), Fiscal Years 2009 to 2013

Range of losses	Number of buildings in this range	Buildings combined total average negative NOI (in millions)	Buildings percent of negative NOI
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Agency Comments

General Services
Administration

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Accessible Text for Appendix III: Comments from the General Services Administration

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Denise Turner Roth
Acting Administrator

cc: David Wise, Director, Physical Infrastructure Issues, GAO

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