ACQUIRING OFFICE SPACE FOR STATE AGENCIES

A Report Prepared for the

Legislative Finance Committee

By

Greg DeWitt , Senior Fiscal Analyst

February 21, 2008

Legislative Fiscal Division

www.leg.mt.gov/css/fiscal

INTRODUCTION

The Department of Administration is charged in statute to assist state agencies, except for the university system, in addressing their office space needs. To carry out these duties, the department manages most existing state-owned buildings and addresses needs that can not be served within the existing state-owned buildings through lease agreements with private property owners. Agency office space needs are constantly changing through a variety of reasons such as increased staffing, customer driven need changes, or existing space issues, including building-related health and environmental concerns, building owner decisions, organizational restructuring, and so forth.

Prior to the 2007 legislative session, the department received notification of Helena space needs for programs of the Department of Public Health and Human Services (DPHHS), Department of Corrections (DOC), and Montana Board of Crime Control (MBCC) that was ultimately addressed through a build-to-lease agreement with a private sector entity. The process taken and the decisions made to address the space needs for these agencies are highlighted here, but only because they bring to light more systemic concerns with the laws for allocating office space for state government. The systemic concerns are the primary focus of this report. This report focuses on the Helena state government office space allocation and does not broach the debate between locating state personnel in Helena or another community. This report does not fully analyze options available to the legislature to address the concerns raised, but requests input from the committee on its desire, time requirement, and priorities for further developing legislative options to address the concerns raised.

For the DPHHS and MBCC programs, the space needs were triggered by building environmental concerns in current facilities and a decision of the private property owner of the building currently being leased to the state to change the use from office to retail space. The DOC currently resides in a 100 year old, state-owned building that has been determined to no longer be adequate for agency occupancy due to health and environmental concerns. To address these space needs, the department took steps, which will be discussed in more detail later in this report, that have resulted in the state entering into a long-term (30 years) lease for a building that will be built by a private property owner specifically to service the above mentioned state programs. The build-to-lease building, the Nob Hill Building, has attracted the attention of some local legislators, Helena city officials, and Helena residents, which has triggered the space allocation process concerns raised in this report. Primary among the concerns is that the laws that exist to provide authority to the department to allocate space for state agencies may have unintended consequences that allows the legislature to be excluded from decisions that commit the state to long-term fiscal commitments and may cost the state more money.

PURPOSE OF REPORT

This report is being written to raise concerns over processes followed to acquire space to house state agency personnel and to solicit direction from the Legislative Finance Committee on whether staff resources should be redirected during the current interim to further pursue options to address the concerns. These concerns came to light after the department entered a long-term lease agreement with a private developer to build a building for lease to the state in the new Nob Hill subdivision of Helena. Aside from concerns raised by residents of the subdivision over building placement and property value issues, which are local government issues to address, the actions taken by the department raise legislative concerns that may not have been contemplated by the legislature when developing state laws that grant authority to the department for allocating space for state agencies. Specifically, the concerns are:

- The laws allow the department to commit the state to a long-term lease agreement and therefore commit future legislatures to funding the lease without direct legislative involvement in a build or lease decision
- The laws are silent on a requirement to determine the least cost option for the state, between constructing a state building or leasing space from the private sector, prior to entering into long-term lease agreements and therefore leaves it to the discretion of the executive whether to request funding from the legislature to build a state-owned building when that option may result in the lowest total cost for the state

- There is no hard and fast requirement for the executive to regularly determine the most cost and operational efficient space allocation for agency personnel
- Budget decisions to add staff may not fully anticipate the space impacts from the decisions

PROCESS FOR ALLOCATING SPACE

SPACE ALLOCATION AUTHORITY

Montana law currently assigns to the Department of Administration the authority for determining the space required by state agencies, other than the university system, and allocating space in buildings owned or leased by the state, based on each agency's need. The statute specifies that the space allocation shall be efficient and effective, and can include leasing additional space, or remodeling or exchanging existing space among agencies.

Short-Term Versus Long-Term Considerations

The ability to satisfy agency office space needs and the ability to obtain and occupy space have varying time constraints. One option for addressing office space needs of state government is to rent or lease space from the private sector. Assuming adequate funding is available, this option can be accomplished in a relatively short period of time. Another option is for state government to build or buy a structure. The option to acquire a state-owned building typically involves a much longer time horizon than leasing space, because of the following steps that would not typically be involved in a solicitation for lease space:

- The building needs to be planned to the point where reasonable accurate acquisition (construction or purchase) costs are known
- A request must be made to the legislature
- If funding is approved by the legislature, the structure must be designed (in the case of construction)
- A solicitation must be made and a contract awarded for a contractor to build or a building owner to sell a structure
- If the structure involves construction, time is needed to build the structure

Acquiring a state-owned building would take several years from the time the space needs are identified until the space can be occupied. This is in contrast to a several month time to acquire leased space of existing office space in a community if space is available. Depending upon the factors that necessitate the need for office space, both short-term and long-term options need to be available to the department for allocating space.

Helena State Office Space Demographics

Currently, the state owns 1,467,086 square feet of office space in Helena and leases an additional 583,303 square feet under 85 leases (not including the space that will be provided by the Nob Hill Building). The ratio of state owned to private lease space has change over the years through a growth of leased space, while the state-owned space has remained relatively constant. According to data provided by the Legislative Audit Division in conjunction with a risk assessment for a build verses lease analysis, discussed below, 250,000 square feet of leased space has been added in Helena since 1997. According to the Department of Administration, Helena's available and acceptable office lease space is saturated, which is why the department issued an RFP for space to be served by the Nob Hill Building. This is important, because for the Helena commercial market to provide additional lease space in the future, either new space will need to be constructed, existing space will need to be converted into acceptable office space, or small, decentralized spaces that may not efficiently serve the space needs for agencies may be the options available for serving state government's Helena office space needs outside of constructing a new state-owned building.

Profile of Long-range Building Program Requests

The Metcalf Building was the last Helena office building constructed with funding approved by the legislature (1983 Legislature). The following figure shows the Helena area office buildings that were: 1) requested to be included in the state Long-range Building Program (LRBP); 2) those requests that were approved by the executive for inclusion in the LRBP; and 3) the status of the LRBP after legislative action. The list of requests

included in the figure is only for office space in the Helena area and is based on staff's paring of a list provided by the department of all building requests that originally were made to the executive process for inclusion in the LRBP request to the legislature. Excluded from the list were all requests for remodeling, warehouse space, or special use buildings.

Since the Metcalf Building, several office buildings have been proposed within the Executive Branch but have not been approved by the executive for inclusion in the LRBP request and subsequently to the legislature, except for three related requests, which are described in Appendix A. This list shows that the legislature is often not presented the opportunity to consider building a state-owned building for office space in Helena.

Helena Area Office Space Funding Requests

		Executive	Legislature	
Session	Project	Agency Requested Amount	Requested in LRBP	Approved in LRBP
1983	Construct New DNRC Building	$6,692,000	$6,958,000	$6,958,000
1989	New Dept. of Commerce Building	7,000,000		
1991	New ISD Building	3,800,000		
1991	New Dept. of Commerce Building	7,455,000		
1991	Office Building, Helena	9,105,955		
1991	Construct OPI Office	2,017,500		
1993	New Dept. of Commerce Bldg.	7,500,000		
1993	Dept.of Health Building	20,000,000		
1993	SRS Building Addition	6,637,500		
1993	Dept. of Labor Building Addition	5,886,000		
1997	OPI Lease/Purchase	1,535,732		
1997	Lease Reduction Program, Helena	28,038,750	350,000	
1997	New Commerce Building	5,040,000		
1997	Expand Walt Sullivan Bldg.	2,201,700		
1997	Purchase Lottery Bldg.	700,000		
1999	Justice Bldg. Addition	1,000,000		
2001	Justice Building Addition	2,300,000		
2001	Construct New Office Building	36,000,000	Note 1	
2003	Construct New Office Bldg.	9,000,000		
2003	Justice Bldg Addition	2,300,000		
2007	ESSC Facility	24,150,000	20,150,000	14,500,000
2007	Purchase 301 S. Park	10,000,000		

Note 1: A funding request for this new office building to house DPHHS employees was included in the Governor Racicot LRBP request but was removed at the request of Governor Elect Martz.

SPACE ALLOCATION IN PRACTICE

The process that the executive has followed, at least for the last quarter century, is described below along with a listing of steps that have not been included, but would enhance the ability of the process to satisfy the efficient and effective requirements of the authorizing statute.

Process Being Used

The process the department uses for allocating space involves the following steps:

1) Agencies communicate their space needs and requirements to the department
2) The department identifies if existing space in state-owned buildings or within current leases is available to fulfill the need and requirements, and if available, works with the requesting agency to occupy the space
3) If no existing space is available, the department makes inquires to the commercial real estate market for existing space to satisfy the need and requirements, and if space is available: 1) works with the requesting agency to gain concurrence that the space is acceptable; and 2) establishes a lease agreement for the space determined to be acceptable by the agency
4) If no acceptable space is identified in the existing commercial real estate market, the department issues a request for proposal (RFP) for space to lease by the state (existing, remodeled, or new)

Nob Hill Building – An Example of Recent Process in Action

When following the process for space to house the agencies currently slated to occupy the Nob Hill Building, no existing and acceptable space in Helena was identified and an RFP was issued on January 24, 2007, for a lease for office space in an existing building or a lease in a building built to suit the needs identified in the proposal. The RFP had scoring components based on the contractor (1/7 weight), building specifications (2/7 weight), location (1/7 weight with locations closer to the capitol complex receiving higher scores), and cost (3/7 weight). The RFP was preceded by a request to the Department of Administration Long-range Building program for a new state building. In testimony before the January 7, 2008, meeting of the State Administration and Veteran's Affairs Interim Committee, the Governor's budget director stated that the executive later decided not to proceed

with this request over concerns that a new office building request would jeopardize legislative approval for a higher priority request, to build a new primary data center and a backup site. The data center proposal was subsequently funded by the May special session of the 2007 Legislature in HB 4, but without office space to house information technology personnel.

The process followed that culminated in entering into 30-year leases for the Nob Hill Building did not include several steps that would have identify if the long-term lease provided the best "bang" for the funding being committed. Although not specifically required in statute, the following steps could interject comparative analysis that would determine the most cost effective options for addressing agency space needs.

HOLISTIC PROCESS FOR ALLOCATION SPACE

Process Requirement Questions

For office space needs that are not driven by unanticipated near-term factors (no immediate urgency that can't wait until after the next legislature convenes), the question comes down to:

- What requirements should be included in the enabling statutes that provide space allocating authority to the department and that ensure that the most cost effective and efficient space allocation for the state is accomplished?
- What level of analysis and what level of legislative involvement should be required in the process?

Missing Steps

There are several issues with how the executive currently allocates office space for state agencies:

1) Although the statute directs that the department allocate space efficiently, there is no specific requirement to consolidate the offices of agencies into a single, central location if it would save costs for the state, as is the case specifically stated in statue for state agencies located in a city other than Helena.
2) There is no specific requirement to determine the least cost alternative between satisfying state agency space needs with a state-owned building or lease from the private sector. Consequently, no lease versus build analysis was conducted when evaluating how to address the space needs that will be satisfied by the Nob Hill Building. According to space allocation managers of the executive, lease versus build analyses are not regularly or typically included in the decision when deciding how to address agency space needs.
3) There have been no recent or there any foreseen plans to perform a space consolidation study or a study to determine the most efficient space allocation for agencies with staff located in Helena.

OTHER LEGISLATIVE COMMITTEES LOOKING INTO THE ISSUE

Concerns similar to those raised in this report have caught the eye of other legislative committees and staff during this interim. The following provides information of other legislative entity involvement on this topic.

Legislative Audit Committee

At its August 22, 2007, meeting, the Legislative Audit Committee heard a risk assessment performed by the Legislative Audit Division (LAD) to determine if a new audit should be performed to update a February 1997 lease versus build analysis for acquiring office space for state agencies. During the discussion of the risk assessment, which is summarized below, the committee directed LAD staff to develop recommendations for committee consideration for legislation that would require, among other things, a lease versus acquire analysis as a regular part of the biennial Long-range Building Program budgeting cycle. In addition to the work in support of the legislation options requested by the committee, two legislative information requests associated with this issue were completed and staff are developing a decision matrix for an additional request of a legislator to develop legislation to address concerns with the space allocation statutes as they relate to the Nob Hill Building lease. The responses to the completed legislative request are included in Appendix B and include: 1) response to legislative request 2601 concerning background information about the Nob Hill Building (memo only); and 2) response to legislative request 2613 regarding processes used in other states when acquiring office space.

1997 Lease Versus Build Analysis

In February 1997, a performance audit was published by LAD that documented a lease versus build analysis for Helena-area office space. The audit objective was to determine if it is less costly for state government to continue to lease or to construct a new building for office space on the capitol complex. The lease versus build analysis used two methods to determine if it is less costly to the state to build or lease: 1) present value; and 2) internal rate of return. Both methods determined that for the 90,000 square foot office space it was more cost effective for the state to build instead of lease the space. Based on the market conditions at the time of the analysis and assumptions used, the state would have saved $4.2 million to build the space versus lease the space[1].

State Administration and Veterans' Affairs Interim Committee

At its January 7, 2008, meeting, the State Administration and Veterans' Affairs Interim Committee (SAVA) heard a brief and unscheduled presentation by the Governor's budget director requesting direction from the committee on issues associated with the Nob Hill building and legislative concerns of the process followed by the department in acquiring the office space. The budget director considered SAVA the appropriate committee because it has interim oversight of the Department of Administration, the agency charged in statute for allocating state office space. SAVA requested that the budget director return with a more formal response to committee questions that were raised. The next SAVA meeting is scheduled for February 22. Any information provided by the budget director at this meeting will be provided as an attachment to this report for consideration by the Legislative Finance Committee in its deliberation of the following options.

OPTIONS

With knowledge of what other legislative staff and committees are working on regarding this topic, the committee may want to consider the following series of questions that should lead to an action plan for committee and staff involvement in addressing the concerns raised in this report.

IS THE COMMITTEE CONCERNED WITH EXISTING LEGISLATIVE INVOLVEMENT IN SPACE ALLOCATION DECISIONS?

To determine if the committee wants to take action to further investigate the concerns raised in this report, members may want to consider the following question:

- Is the committee concerned that the space allocation laws are such that the process currently being followed by the executive excludes the legislature from direct involvement in space allocation decisions, and does the committee feel this should be addressed through further investigation and potential legislative action?

In determining whether to investigate the concerns identified in this report, the committee may want to consider that the goal of the investigation would be to review the current statutory authority for allocating office space and identify legislative options for adding more specificity to the statutes to perhaps require comparative analyses for determining the least cost alternative between leasing and acquiring space for state agencies, from a long-term perspective.

IF ACTION IS WANTED, WHAT SHOULD BE THE INVOLVEMENT OF LFD STAFF?

If the committee decides to further pursue the concerns identified in this report, does the committee want to direct Legislative Fiscal Division (LFD) staff to:

- Pursue independent research and legislative options for committee action
- Follow other legislative activities and keep the committee informed on actions being taken

[1] Net present value to lease was $29.6 million and to build was $25.4 million.

If this project is undertaken, the project would likely address the following components of the space allocation process:

- Should funding for office space leases be approved by the legislature in a more formal process than that currently accomplished in the general appropriations process for tenant agencies? If so, is there a threshold lease size or lease duration term that would trigger the more formal legislative involvement?
- Should statute require a lease versus acquire (build or buy) analysis prior to entering into lease agreements for state office space? If so, what size in annual funding or square foot should trigger the analysis?
- Should statute require an occasional space allocation study to determine the most long-term cost effective space allocation for state office space needs? If so, how often should the study be done?
- What is the right amount of legislative involvement that will allow office space needs to be addressed in the long-term without inhibiting the executive's ability to provide for short-term office space needs?
- What would it cost and what resources would be needed to add requirements for regular lease versus acquire analyses and space consolidation studies?
- What changes to statute are needed to effect the desired changes?
- What additional criteria should be considered when determining how to address the long-term space needs for state agencies? Other criteria could include, among other things, state and local land use planning, polices for addressing long-term environmental concerns, energy conservation, and operational efficiencies.

Pursuit of all aspects described would likely require reallocation of staff resources. Also, if a subcommittee is deemed warranted committee member availability will also be a potential issue.

SUMMARY

A recent decision by the Department of Administration to enter into a long-term lease of a sizable office building to address state agency office space needs has raised concerns with laws that give the department authority to allocate space for state government. Of concern is that the law allows the department to enter into long-term leases without any requirements to evaluate if the lease is in the best long-term interest of the state or involve the legislature directly in the funding decision other than through the temporary general appropriations bill that funds biennium operations for state agencies. Being excluded since 1983 is a process involving the legislature to evaluate if a state-owned building would save money for the state and requests for state-owned buildings. A 1997 analysis by the Legislative Audit Division determined that building a state-owned building for offices of state agencies would save the state nearly $4.2 million for a 90,000 square foot building with a 40 year useful life over leasing the same space from the private sector.

This report identifies the concerns with the current space allocation process being followed by the department and provides options for the Legislative Finance Committee in deciding whether or not to proceed with an in-depth analysis with the objective of providing legislative options for addressing the concerns raised.

APPENDIX A

HELENA AREA OFFICE SPACE FUNDING REQUESTS INCLUDED IN LONG-RANGE BUILDING PROGRAM REQUESTS

HELENA AREA OFFICE SPACE FUNDING REQUESTS

Since 1983, the following three Helena area office space items have been included in Long-range Building Program requests to the legislature: 1) funding to plan for a program to reduce leases in Helena to the 1997 Legislature; 2) funding for a new office building to the 2001 Legislature; and 3) funding to build a data center and backup data center site for statewide computer systems to the 2007 Legislature.

Lease Reduction Program

The request for funding to plan the lease reduction program originated in the executive as a request for funding to build a state-owned building. The executive reduced the request to funding only for costs to plan a lease reduction program. The funding was not included in the LRBP when it came out of the 1997 Legislature, but the process or decisions that caused it to be removed are not apparent from a review of available documentation. So, it is not clear if the legislature denied the funding or if the request was removed at the request of the executive.

New Office Building for DPHHS

The LRBP as requested by Governor Racicot included funding to build a new office building to house personnel of the Department of Public Health and Human Services. Prior to LRBP hearings the request was removed at the request of Governor Elect Martz, so the legislature never had an opportunity to debate the funding request for the building.

Enterprise Services Support Center

A request for funding to construct a new data center and a backup site for statewide computer operations was included in a request to the 2007 Legislature. In its original form, the data center included funding for 90,000 to 100,000 square feet of office space, or roughly enough to house the Information Technology Services Division of the Department of Administration currently residing in the Mitchell Building on the capitol complex. The legislature subsequently reduced the funding by eliminating much of the office space of the original request. This is the only request for Helena office space the legislature has considered since 1983.

APPENDIX B

RESPONSES TO LEGISLATIVE INFORMATION REQUESTS ASSOCIATED WITH OFFICE SPACE ACQUISITION

LEGISLATIVE AUDIT DIVISION

Scott A. Seacat, Legislative Auditor
Tori Hunthausen,
Chief Deputy Legislative Auditor

Deputy Legislative Auditors:
James Gillett
Angie Grove

MEMORANDUM

TO: Scott A. Seacat, Legislative Auditor

FROM: Kent Rice, Performance Audit Senior

DATE: October 17, 2007

RE: New State Building (08L-2601)

This request asked for information regarding a new state building to be constructed at an Interstate 15 interchange. This memorandum provides details on information compiled.

BACKGROUND

The requestor heard a new state building was to be built at the South Helena Interchange currently under construction off Interstate 15. This interchange exits at the new Nob Hill Subdivision. I contacted personnel within the Department of Administration (DOA) to obtain information on any proposed state buildings. The first discovery made was the proposed new building will not be a state-owned building. Rather, the building will be built by a private developer and leased to the state for office space. The following sections provide details on the proposed new leased space.

Initial Development

The State of Montana leases over 600,000 square feet of space in the Helena area. Programs are growing and space needs are growing as well. According to DOA personnel, the need for additional space, as well as new space, was not being met, so the decision was made to secure new space. The process started about three years ago. State personnel in three agencies were considered a top priority for securing new space. The three agencies are:

- Department of Public Health and Human Services (DPHHS)
- Department of Corrections (DOC)
- Montana Board of Crime Control

DPHHS is co-locating employees from several locations including the City/County Building where they are being evicted, the North Gate Plaza where space is not user-friendly, the Cogswell and Sanders Street buildings, and the old Board of Investments building on Fuller Avenue. The DOC building is old and they have been looking to vacate this space for quite some time. Personnel in the basement of the DOC building were moved out due to the space being uninhabitable. The Board of Crime Control is also currently located in the North Gate Plaza. According to DOA personnel, the owner of the North Gate Plaza property is looking to convert the space back into retail space.

Room 160 · State Capitol Building · PO Box 201705 · Helena, MT · 59620-1705
Phone (406) 444-3122 · FAX (406) 444-9784 · E-Mail lad@mt.gov

DOA initially started planning to secure additional space with a proposal to build a state-owned building, but according to DOA personnel, the Governor's Office did not want to pursue a state building. DOA still needed space, and because it has statutory authority to secure space through leasing, it chose to issue a request for proposals (RFP) for leased space.

Request for Proposals

An RFP was issued January 24, 2007 and closed April 25, 2007. The RFP requested a contractor to provide a lease for office space in an existing building or a lease/build to suit building. The RFP spelled out the general details for the building including the number of FTE to occupy the space. The RFP was only a guideline for the project.

The RFP also explained the evaluation process. Proposals were to be scored using specified evaluation criteria. The evaluation criteria included the following:

- Contractor (100 points)
- Building Specifications (200 points)
- Location (100 points)
- Cost (300 points)

A total of eight proposals were received in response to the RFP. The successful proposer was SBC Archway III, LLC. As it turned out, this winning proposal was the least expensive proposal received. The successful proposer is a combination of several companies including Streeter Brothers from Billings and an architecture firm from Colorado. Streeter Brothers is currently under contract with the Board of Investments for its real estate investment portfolio. The Board of Investments is not involved with this building project.

Current Status

DOA has not finalized the specifics of the building, but estimate a final floor plan by November 2007. The building will be located in the Nob Hill Subdivision south of the South Helena Interchange. The total square footage of the building is estimated at between 150,000 and 200,000 square feet. The building will be four stories high, and will be occupied by approximately 500 FTE. Standard lease contracts between the three agencies and the contractor have been drafted and will be finalized after the floor plan is finalized. According to DOA personnel, all three agencies requested and received approval from the 2007 Legislature for increased rent for occupying the new building in the 2009 biennium. The price for the lease will be $21.85 per square foot, which is comparable to the rates charged for several other state agency locations in the Helena area. The lease rate includes everything including janitorial services and parking. The lease term is 30 years with the 20th and 30th year rent free. Groundbreaking is estimated for February 2008, with building occupation sometime in early 2009.

SUMMARY

Several state agencies required office space, so DOA issued an RFP to secure needed space. The successful proposer was SBC Archway III, LLC. The building will be located in the Nob Hill Subdivision. DOA estimates finalization of the floor plan in November 2007, with groundbreaking for the building in February 2008, and building completion by 2009.

NOTE: attachments include a preliminary plat of the Nob Hill Subdivision and two building location maps.

LEGISLATIVE AUDIT DIVISION

Scott A. Seacat, Legislative Auditor
Tori Hunthausen,
Chief Deputy Legislative Auditor

Deputy Legislative Auditors:
James Gillett
Angie Grove

MEMORANDUM

TO: Scott A. Seacat, Legislative Auditor

FROM: Kent Rice, Senior Performance Auditor

DATE: January 9, 2008

RE: Other State Processes for Acquiring Office Space (08L-2613)

This request asked for information regarding processes and analysis done by other states when acquiring office space. This memorandum provides details on information compiled.

INTRODUCTION

For this request, I reviewed information from six neighboring states including Colorado, Idaho, North Dakota, South Dakota, Washington, and Wyoming. Only two of the six states, Idaho and Washington, have formalized processes for analyzing lease versus build costs. The following sections provide summary information for each state.

COLORADO

Colorado has only general statutes and processes similar to Montana's Long Range Building Program. According to a state representative, Colorado has not had capital construction funds to build in quite some time. They plan to complete a Master Plan for the Capitol Complex in the near future which will address a potential new state office building to be constructed next to the State Capitol. The Master Plan will consider the need for adjacency and the need for the space for 100+ years. In cases where they might lease large blocks of space, they may complete a buy/build/lease analysis, but without the ability to fund a purchase or construction, it is considered "not realistic." The state representative indicates they have seen a cyclical rental market, which makes it difficult to predict future costs with certainty, and without certainty they do not place much validity on a lease versus buy analysis. With limited exceptions, all state agencies and institutions must utilize contracted real estate brokerage services when leasing or purchasing property in any of nine identified counties.

IDAHO

Title 67, Chapter 64, Idaho Code, contains the Idaho State Building Authority Act. This Act contains a declaration of policy which includes the following statements:

- It is necessary that proper provision of office space and related facilities for the many departments, agencies and commissions of state government and its instrumentalities be provided.
- It is to the economic benefit of the citizens of the state of Idaho to provide sufficient office space and the necessary related facilities for such state governmental bodies and thus provide a more efficient and more economical operation of state government.

Room 160 · State Capitol Building · PO Box 201705 · Helena, MT · 59620-1705
Phone (406) 444-3122 · FAX (406) 444-9784 · E-Mail lad@mt.gov

- It is further declared that in order to provide for a fully adequate supply of governmental facilities at costs that state government can afford, the Legislature finds it necessary to create and establish a state building authority for the purpose of constructing and operating such facilities to meet the needs of the state government.

Idaho's Department of Administration manages multi-agency facilities constructed, acquired or refurbished through the State Building Authority, and subleases the facilities to various state departments, agencies, and institutions in Idaho.

According to Title 67, Chapter 57, Idaho Code, the Director of the Department of Administration shall establish a program for evaluation of all leases of facilities. No agency may enter into or renew any lease until completing a comprehensive analysis according to Department of Administration standards and criteria. The comprehensive analysis shall address, at a minimum, an evaluation of the need for facilities, space utilization efficiency, long-term needs and objectives, and viable alternatives to meet facility needs, including acquiring facilities with appropriated funds and leasing facilities through the State Building Authority. From the analysis, agencies, in consultation with the Department of Administration, are to select the alternative that best serves long-term needs and objectives and that provides suitable facilities at the lowest responsible cost to the taxpayer measured over the time the facilities are expected to be needed, or 40 years, whichever is less. A summary of these analyses are to be included in the annual budget requests to the Governor and the Legislature.

The comprehensive analysis has two components: 1) a Lease Purchase Model, and 2) a Facilities Questionnaire. A Lease Analysis Advisory Group was formed to develop a workable system for state agencies. The Lease Purchase Model is a result of meetings with this group. The expectation is that the model will represent a dynamic tool for agencies and it is anticipated adjustments will need to be made, especially with regard to real estate market conditions. This model can also be used as a negotiating tool for agencies by providing comparative financial information to landlords for consideration in determining if they can lease space for less than what it would cost the state to build a facility. The Lease Purchase Model is a spreadsheet modeling tool containing eight worksheets. This model was designed to answer the question "Is it better for the state to lease this facility or to construct a facility through the Idaho State Building Authority or other funding sources?" The model only answers the financial, or quantitative, aspects of the facility. There are other issues which will impact choices in determining which facility meets the state's needs. These issues, which are qualitative in nature, are addressed in the Facilities Questionnaire.

The model is designed to only require "assumptions" to be inserted into one of the eight worksheets. All calculations are automatically performed from inserted assumptions. Occupancy of a purchased facility is designed to commence three years after the analysis is performed, in order to provide for an adequate amount of time for legislative approval and the construction process. In addition, current policy is the state of Idaho will not cancel leases until the leases have expired, and the model automatically allows for this timing. The analysis is intended to convert all leases to a "triple net" lease. Costs to operate and maintain facilities are removed from both the lease rate and from the cost to acquire and operate a building. The worksheet has preset base assumptions made about specific locations. Costs are compared over a 40-year period on both a cash method and a net present value basis. A break-even year, the year when the cost of leasing is equal to the cost of acquiring a facility, is also identified with the model. The model expresses a cost ratio by dividing the net present value of the purchase alternative by the net present value of the leasing alternative. If the cost ratio is below 1.00, the acquisition of a facility should be considered. For example, if the cost ratio is .56, this would mean the acquisition proposal can provide the facility for $0.56 per square foot versus the current lease expense of $1.00 per square foot. The model can be readily adapted to suit a wide variety of situations, including the purchase of an existing facility.

The model is updated annually to reflect changing market conditions and takes into account such factors as moving costs, financing rates, and building costs.

Laws also require agencies to prepare and maintain a five year facilities needs plan. These plans are to include the state agency's need to own, operate or occupy real property and improvements including administrative office buildings, structures and parking lots, to assist it in its operation as a state agency. There is a Permanent Building Fund Advisory Council which is a five-member council created by the Legislature whose members are appointed by the Governor. The council oversees the construction, renovation and repair projects of state-owned property, in addition to approving facility leases on a statewide basis. Per law, Idaho published a State Facilities Manual to assist agencies in the acquisition of functional and cost effective facilities, whether leased from private landlords or located within the various state-owned buildings. The manual indicates facilities can be owned by an agency, leased from the private sector, sub-leased from another agency, or sub-leased from the Department of Administration (generally in a state-owned office building).

NORTH DAKOTA

North Dakota does not have policies, rules, or laws requiring an analysis. Agencies have been delegated authority to negotiate their own leases. However, the Facilities Management Division (FMD), Office of Management and Budget (OMB) does track leases. The Legislature implemented statute that agencies cannot purchase or construct buildings without legislative approval as a result of the State Land Department purchasing a building. According to an FMD official, the Legislature is currently pro-leasing.

According to North Dakota's Office Space Policy, OMB is responsible for the assignment of office space within the Capitol Complex. When space is not available in the Capitol, it becomes necessary to lease or rent additional space in buildings located off the Capitol grounds. All leases for office space off the Capitol grounds must pass through OMB for approval. It is the position of OMB that any agencies needing additional office space outside the Capitol Complex must first review the various locations currently being rented and attempt to secure rental space with other existing units of government prior to securing a new location. It is the intent of this policy to collocate agencies within the same building which will help to ensure efficiency and shared services between units of state government. It is the goal of OMB to limit the number of locations for state offices in rental space to help individuals who need the services of these agencies and departments affected. The only agencies and institutions that do not come under the guidelines and procedures are the institutions under the North Dakota University System, the Adjutant General, and the Department of Transportation. All other state agencies and departments must follow the standard leasing policies as provided by OMB.

SOUTH DAKOTA

South Dakota does not have any specific laws, rules, or policies regarding lease versus build analysis. According to the Director of Office of Space Management (OSM), South Dakota operates on a case-by-case basis. Each individual written request for office space made to OSM is assessed on needs, current utilization of space, etc. Space Management provides leasing services for all state agencies, with the exception of the Board of Regents who handles its own space needs. OSM is statutorily responsible for providing space for all state agencies through utilization of leased buildings including negotiating for leased space from the private sector, researching the market to determine current lease rates, determining site selection, space allocation and usage, tenant development and overseeing construction and remodeling projects. The office is also responsible for reviewing agency needs and requirements for space and making specific recommendations to the Commissioner of Administration concerning the amount and location of available space that will most efficiently satisfy agency needs.

According to South Dakota laws, the Bureau of Administration shall, under the direction of the Commissioner of Administration, and with the consent of the Governor, arrange for procuring office

space outside of the Capitol when necessary. The Capitol Complex Restoration and Beautification Commission is authorized and directed to make all necessary plans for the enlargement of the capitol complex. The Commission shall make recommendations for the development of areas immediately adjacent to the state capitol complex and acquaint the people of South Dakota with the need and purpose of a comprehensive long-range plan for capitol complex of sufficient and proper size to serve the future needs of the state and to secure the proper growth and expansion of the city of Pierre. The zone shall be the capitol area preservation zone and shall be zoned primarily for residential purposes and for governmental purposes. According to the Director of OSM, the Legislature approves all construction, even for retrofitting an existing building.

WASHINGTON

The state's Capitol Complex Master Plan adopts an analytical approach to own-versus-lease decisions in the management of the state's real property portfolio. State agencies are to ensure decisions related to facility needs have undergone rigorous analysis by the appropriate operating and capital budgeting authorities. The Master Plan includes a leased versus owned analysis policy indicating the state shall use total cost of ownership, life cycle cost analysis, and other economic models to evaluate whether to own or lease space to meet the state's projected business and operational needs. This policy is intended to ensure acquisition of state facilities, particularly office space, is based on planning and evaluation of both owning and leasing options and opportunities. It is further intended decisions on owning versus leasing will be made with the long-term interests of the state as the foremost consideration. It recognizes the question of owning versus leasing is a fundamental question an agency has to answer before proceeding with any acquisition approach.

The State of Washington leases approximately 11 million square feet of space and owns approximately 5 million square feet of space. The owned space is mostly in the State Capitol or on the Capitol Campus. In the early 90's, the Legislature approved expansion beyond the Capitol Campus and started building space on satellite campuses. They lease space partly because of the flexibility and partly because of needs for space but having only so much space on the Capitol Complex. There was a change in administration (Legislature changed party majority) and they moved toward more leasing. This change included very little appropriations for building. As a result, they worked with cities to establish "preferred leasing areas".

JLARC (Joint Legislative Audit and Review Committee) released a December 1995 performance audit report entitled Capital Planning and Budgeting: Study of Leasing Versus Ownership Costs. The study included an analysis of several ownership and leasing decisions. Personnel created an economic model based on industry standards and benchmarks, which built upon previous economic modeling conducted in 1987 and 1988. The purpose of the economic model was to quantify all costs to the public of the alternatives being considered. The study reaffirmed conclusions of previous studies indicating government ownership can result in significant savings given similar facilities, development and operational costs. The study further states economic comparisons must be made between specific alternatives using all facts available about each. The report contains seven recommendations for providing greater accountability and quality control in the project proposal process, and better information for policy makers in choosing among alternatives. Recommendations included having the Legislature require a life cycle cost analysis, including establishing benchmarks for major assumptions, as well as requiring a review including a sensitivity analysis. As a result of the performance audit, a life cycle cost analysis model was developed.

The 2004 Legislature changed majority party again, and the new administration saw more benefits from ownership. The state is now moving more toward building space. Legislation passed in this regard directed the state to do more long-term planning as opposed to being reactive to space needs. All lease and build proposals are reviewed and approved by the Office of Financial Management (OFM), which is

the Governor's Budget Office. According to state officials, the construction market is "out of control" and costs are increasing rapidly. As a result, it somewhat impacts their ability to do long-term analysis. However, overall, they believe they should be able to bring about more consolidation and collocation under the current philosophy.

In February 2007, JLARC issued an update on the life cycle cost analysis model. According to the JLARC report, life cycle cost analysis is an economic tool used to calculate the total costs of an asset over its useful life. In the case of facility space, life cycle cost analysis looks at all quantifiable capital and operating costs of facility alternatives over their estimated useful lives and compares all costs on a same-year dollar basis. JLARC made updates and changes to the existing life cycle cost analysis model, resulting in a more comprehensive and user-friendly tool for evaluating different financing and project delivery options for state facility space. These updates and changes included the ability to:

- Compare up to six different ownership and project delivery alternatives and leasing options at the same time, and designate unique schedules and budgets for each alternative delivery method.
- Compare different financing scenarios for each of the ownership and project delivery approaches.
- Review at once all of the major cost estimates and economic assumptions used for each alternative, and conduct sensitivity analyses on the major assumptions used to determine how sensitive the outcome of the analysis is to the major assumptions.

In addition, JLARC identified key cost assumptions requiring regular updates to ensure accurate estimates when using the life cycle cost analysis model. According to JLARC, the state lacks policies and standards for conducting life cycle cost analysis in general. In addition, limited oversight and review of results of life cycle cost analyses does not ensure that analyses across projects and agencies are consistent or accurate. JLARC made three recommendations addressing these issues.

According to state law (RCW 43.82.010), the Director of General Administration shall purchase, lease, lease purchase, rent, or otherwise acquire all real estate required by state agencies. The Director sets the terms and conditions of each lease. The Director may enter into a long-term lease greater than 10 years in duration if an analysis shows the life cycle cost of leasing the facility is less than the life cycle cost of purchasing or constructing a facility. It is the policy of the state to encourage the collocation and consolidation of state services into single or adjacent facilities, whenever appropriate, to improve public service delivery, minimize duplication of facilities, increase efficiency of operations, and promote sound growth management planning. Prior to the construction of new buildings or major improvements to existing facilities or acquisition of facilities using a lease purchase contract, the Director shall conduct an evaluation of the facility design and budget using life cycle cost analysis, value-engineering, and other techniques to maximize the long-term effectiveness and efficiency of the facility or improvement.

The 2007 Legislature passed Substitute House Bill 2366, which took effect on July 22, 2007. This legislation directs OFM to strengthen its oversight role in state facility analysis and decision-making. The laws governing lease/purchase were updated and although not codified as law, the intent of the Legislature was stated as follows:

- The Legislature finds that the capital stock of facilities owned and leased by state agencies represents a significant financial investment by the citizens of the state of Washington. Capital construction projects funded in the state's capital budget require diligent analysis and approval by the Governor and the Legislature. In some cases, long-term leases obligate state agencies to a larger financial commitment than some capital construction projects without a comparable level of diligence. State facility analysis and portfolio management can be strengthened through greater oversight and support

from OFM and the Legislature and with input from stakeholders. The Legislature finds that the state lacks specific policies and standards on conducting life cycle cost analysis to determine the cost-effectiveness of owning or leasing state facilities and lacks clear guidance on when and how to use it. Further, there is limited oversight and review of the results of life cycle cost analyses in the capital project review process. Unless decision makers are provided a thorough economic analysis, they cannot identify the most cost-effective alternative or identify opportunities for improving the cost-effectiveness of state facility alternatives. The Legislature finds that the statewide accounting system limits the ability of OFM and the Legislature to analyze agency expenditures that include only leases for land, buildings, and structures. Additionally, other statewide data systems that track state-owned and leased facility information are limited, onerous, and inflexible. Therefore, it is the intent of the Legislature to strengthen OFM's oversight role in state facility analysis and decision-making. Further, it is the intent of the Legislature to support OFM's and the Department of General Administration's need for technical expertise and data systems to conduct thorough analysis, long-term planning, and state facility portfolio management by providing adequate resources in the capital and operating budgets.

Substitute House Bill 2366 included the following changes to law:

- Chapter 39.35B RCW new section:

  OFM shall:

  (1) Design and implement a cost-effective life cycle cost analysis model by October 1, 2008, based on the work completed by JLARC in January 2007 and in consultation with legislative fiscal committees.

  (2) Deploy the life cycle cost analysis model for use by state agencies once completed and tested.

  (3) Update the life cycle cost analysis model periodically in consultation with legislative fiscal committees.

  (4) Establish clear policies, standards, and procedures regarding the use of life cycle cost analysis by state agencies including:

    (a) When state agencies must use the life cycle cost analysis, including the types of proposed capital projects and leased facilities to which it must be applied.

    (b) Procedures state agencies must use to document the results of required life cycle cost analyses.

    (c) Standards regarding the discount rate and other key model assumptions.

    (d) A process to document and justify any deviation from the standard assumptions.

- Chapter 43.82 RCW new sections:

  - OFM, in consultation with the appropriate committees of the Legislature, shall prepare an implementation plan to improve the oversight of real estate procurement and management practices. The plan must identify specific steps state government can take to better manage the acquisition, ownership, lease, and disposition of office and warehouse space so state services are delivered in an effective manner. The plan was to be submitted to the Governor and the appropriate committees of the Legislature by October 1, 2007.

  - (1) OFM shall design and implement a modified predesign process for any space request to lease, purchase, or build facilities that involve (a) the housing of new state programs, (b) a major expansion of existing state programs, or (c) the relocation of state agency programs. This includes

the consolidation of multiple state agency tenants into one facility. OFM shall define facilities that meet the criteria described in (a) and (b) of this subsection.

(2) State agencies shall submit modified predesigns to OFM and the Legislature. Modified predesigns must include a problem statement, an analysis of alternatives to address programmatic and space requirements, proposed locations, and a financial assessment. For proposed projects of twenty thousand gross square feet or less, the agency may provide a cost benefit analysis, rather than a life cycle cost analysis, as determined by OFM.

(3) Projects that meet the capital requirements for predesign on major facility projects with an estimated project cost of five million dollars or more pursuant to Chapter 43.88 RCW shall not be required to prepare a modified predesign.

(4) OFM shall require state agencies to identify plans for major leased facilities as part of the ten-year capital budget plan. State agencies shall not enter into new or renewed leases of more than one million dollars per year unless such leases have been approved by OFM except when the need for the lease is due to an unanticipated emergency. The regular termination date on an existing lease does not constitute an emergency. The Department of General Administration shall notify OFM and the appropriate legislative fiscal committees if an emergency situation arises.

(5) For project proposals in which there are estimates of operational savings, OFM shall require the agency or agencies involved to provide details including but not limited to fund sources and timelines.

- OFM shall:
  (1) Work with the Department of General Administration and all other state agencies to determine the long-term facility needs of state government; and

  (2) Develop and submit a six-year facility plan to the Legislature by January 1st of every odd-numbered year, beginning January 1, 2009, that includes state agency space requirements and other pertinent data necessary for cost-effective facility planning. The Department of General Administration shall assist with this effort as required by OFM.

WYOMING

The State of Wyoming does not have laws or rules to govern facility acquisition or management. Per the Wyoming Constitution, the five state elected officials (Governor, Secretary of State, State Auditor, State Treasurer, and State Superintendent of Public Instruction) make up the State Building Commission (SBC). The SBC has authority to deal with all matters regarding state facilities. In Wyoming, most state buildings are owned and maintained by the state. Many of the buildings are older and somewhat historic in nature. Many have been renovated to better serve the state with technology and provide up-to-date infrastructure and energy efficiency. When state revenues are high, there are new buildings constructed and older ones renovated. However, the state also leases space for agencies or offices around the state as may be needed in various locations. Also, occasionally the state may purchase existing buildings if they fit a state need and opportunity to purchase, at a fair price, is available. Management of state facilities is done by SBC staff. Leasing, purchase, renovation or building of state facilities is approved by the SBC and funded by approval of the Governor and Legislature. Requests for space are submitted to the Construction Management Office (SBC staff) for review. Staff evaluates the proposal, reviews all other options and makes a recommendation to the SBC regarding the request. The review will include consideration of the most cost effective method to satisfy the need. The SBC, Governor, and Legislature have final approval of any request.

SUMMARY

The legislatures of all six states reviewed have approval authority for construction of new facilities. Both Idaho and Washington have laws requiring lease versus build analysis. Both states have developed models for use in conducting the analysis, and copies of these models are available.

S:\Admin_Restricted\DAILY\LEG-REQ.08\08L-2613 memo.doc/ah