



# **PERFORMANCE AUDIT REPORT**

## **Assessing the Benefits of Leasing Versus Owning Office Space for State Employees**

**A Report to the Legislative Post Audit Committee  
By the Legislative Division of Post Audit  
State of Kansas  
March 2000**

# ***Legislative Post Audit Committee***

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## ***Legislative Division of Post Audit***

**THE LEGISLATIVE POST** Audit Committee and its audit agency, the Legislative Division of Post Audit, are the audit arm of Kansas government. The programs and activities of State government now cost about \$8 billion a year. As legislators and administrators try increasingly to allocate tax dollars effectively and make government work more efficiently, they need information to evaluate the work of governmental agencies. The audit work performed by Legislative Post Audit helps provide that information.

We conduct our audit work in accordance with applicable government auditing standards set forth by the U.S. General Accounting Office. These standards pertain to the auditor's professional qualifications, the quality of the audit work, and the characteristics of professional and meaningful reports. The standards also have been endorsed by the American Institute of Certified Public Accountants and adopted by the Legislative Post Audit Committee.

The Legislative Post Audit Committee is a bipartisan committee comprising five senators and five representatives. Of the Senate members, three are appointed by the President of the Senate and two are appointed by the Senate Minority Leader. Of the Representatives, three are appointed by the Speaker of the House and two are appointed by the Minority Leader.

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February 24, 2000

To: Members, Legislative Post Audit Committee

Senator Lana Oleen, Chair  
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This report contains the findings, conclusions, and recommendations from our completed performance audit, *Assessing the Benefits of Leasing Versus Owning Office Space for State Employees*.

The report contains an appendix which shows all the office space leased by State agencies within Shawnee County, as of December 1999.

This report includes several recommendations for the Department of Administration and one for the Legislature's Joint Committee on State Building Construction. We would be happy to discuss these recommendations or any other items in the report with you at your convenience.

  
Barbara J. Hinton  
Legislative Post Auditor



**EXECUTIVE SUMMARY**  
**LEGISLATIVE DIVISION OF POST AUDIT**

**Question 1: What's the Most Cost-Effective Way to  
Provide Office Space for State Agencies?**

**Numerous factors can come into play when deciding how best to provide office space.** ..... page 5  
*Economic factors—such as interest rates, building operation and maintenance costs, and lease rates—need to be considered. Non-economic factors include the desire to have State offices located “downtown,” flexibility of the space, and accessibility for the public.*

**It's difficult to know what factors State officials considered in the recent decisions to purchase or construct office buildings downtown.** ..... page 8  
*The Division of Facilities Management solicited proposals in 1997 for leasing office space near the Capitol. In all, 24 developers submitted proposals and a selection committee was formed to evaluate the proposals. The State ultimately decided to purchase an existing building from the Security Benefit Group, and to build 2 other office buildings—the Signature Building at 10<sup>th</sup> and Jackson, and the Myriad Building at 5<sup>th</sup> and Van Buren. We found little documentation of analyses performed on the proposals, or the rationale for the State's decisions regarding the 3 buildings selected.*

**After the Signature, Security Benefit, and Myriad buildings are filled, the State still will lease enough office space to consider constructing or buying additional buildings.** ..... page 12  
*We estimated that the State still would be leasing approximately 521,000 square feet of office space after all the newly acquired buildings are filled. Because of this, we looked at the possibility of constructing another new building or buying an existing building. In general, it appears it wouldn't be cost-effective for the State to build another major office building, unless it could be done for less cost than the Signature Building. But it may be cost-effective to consider buying an existing building where the State leases a considerable amount of space.. More complete financial information and analysis would be needed before a decision could be made.*

**Better information about State leases could help the Department of Administration in analyzing future decisions about State buildings.** ..... page 14  
*The Division of Facilities Management maintains a database that contains lease information, but we found the database had some inaccuracies. The Division recently purchased comprehensive facilities management software that will allow its staff to provide information to the Legislature about funding needs for maintenance and the consequences of deferring maintenance.*

**Kansas has used a number of methods to acquire buildings.** ..... page 15  
*Over the years, Kansas has used General Fund appropriations, issued bonds, and entered into lease-purchase agreements to acquire buildings. The 3 newest buildings acquired by Kansas were acquired through lease-purchase arrangements. Other states we contacted haven't used lease-purchase arrangements to acquire new buildings over the last decade. Instead, they used general obligation bonds, state appropriations, revenue bonds, and certificates of participation to finance building acquisitions.*

**Question 1 Conclusion:** ..... page 16

**Question 1 Recommendations:** ..... page 17

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**Question 2: Could Kansas Save Money by Having  
The Department of Administration Negotiate All Leases**

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***In Kansas, individual agencies negotiate their own leases, but those leases must be approved by the Secretary of Administration.*** ..... page 18

*The current Director of Facilities Management favors moving to centralized lease negotiations. He thinks this change could save the State money and would lead to more consistency in leases. Centralizing this responsibility would require a change in State law. Centralized lease negotiations won't necessarily eliminate differences in lease rates paid by different agencies occupying space in the same building, but it might put the State in a better position to negotiate concessions from landlords.*

***Centralized leasing offers a number of advantages that could save the State money, but there also can be some disadvantages for State agencies.*** ..... page 20  
*Some advantages include consistent space standards, potential for volume discounts, and agencies not getting into bidding wars for the same space. On the other hand, some agencies don't want to lose their ability to make their own lease arrangements and others think it might be difficult for one agency to negotiate all leases Statewide. Officials in 5 of 6 states we spoke with offered positive comments about the benefits of centralized lease negotiations. Officials from Kansas agencies were less enthusiastic—83% replied they were either uncertain or opposed to the concept of centralized lease negotiations. The concept got mixed reviews from 3 landlord representatives we talked to.*

**Question 2 Conclusion:** ..... page 22

**Question 2 Recommendations:** ..... page 22

**APPENDIX A: Scope Statement** ..... page 23

**APPENDIX B: Kansas Agencies that Lease Office Space in Shawnee County** ..... page 27

**APPENDIX C: Summary of Assumptions and Data Limitations Relevant to Legislative Post Audit's Analysis of Constructing a Second State Office Building and Acquiring the Mercantile Bank Building** ..... page 30

**APPENDIX D: Agency Response** ..... page 31

<p>This audit was conducted by Chris Clarke and Joe Lawhon. Leo Hafner was the audit manager. If you need any additional information about the audit's findings, please contact Ms. Clarke at the Division's offices. Our address is: Legislative Division of Post Audit, 800 SW Jackson Street, Suite 1200, Topeka, Kansas 66612. You also may call (785) 296-3792, or contact us via the Internet at: <a href="mailto:LPA@lpa.state.ks.us">LPA@lpa.state.ks.us</a>.</p>
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## **Assessing the Benefits of Leasing Versus Owning Office Space for State Employees**

The State has entered into more than 80 leases for about 900,000 square feet of privately owned office space in Shawnee County, much of it in the downtown core area. It also houses State employees in about 625,000 square feet of office space in the Landon, Docking, and Memorial Hall buildings, and recently contracted to build 2 office buildings and purchase an existing office building in downtown Topeka.

These transactions have raised legislative questions about how best to provide office space for State employees, and how best to finance it. Those questions have centered on the benefits of leasing versus owning State office space. Questions also have been raised about how agencies lease space. Because some State agencies negotiate their own leases in non-State-owned buildings, the State has little real leverage to negotiate volume discounts or other lease concessions.

This performance audit was approved to answer the following questions:

- 1. What factors, including costs, determine whether a State agency should lease or purchase property?**
- 2. What funding mechanisms should the State use to acquire office space for State agencies?**
- 3. What are the advantages and disadvantages of adopting a centralized approach to leasing State office space?**

A copy of the scope statement approved by the Legislative Post Audit Committee is contained in Appendix A. As that scope statement indicates, we focused our analysis on Shawnee County.

To answer these questions, we interviewed officials from the Department of Administration, from its Division of Facilities Management, and from other agencies. We reviewed current lease arrangements and associated costs, and we reviewed documentation about the three new building acquisitions in downtown Topeka. In addition, we surveyed all Kansas agencies leasing office space in Shawnee County as of December 1999, as well as officials in other states.

Our audit work answers the questions presented above. For reporting purposes, however, we've collapsed the 3 questions into 2, and re-worded them slightly.

In conducting this audit, we followed all applicable government auditing standards set forth by the U.S.. General Accounting Office, except we weren't able to verify cost information reported to us directly by agency officials because of time constraints. We have no reason to think that any of the data agencies submitted to us were intentionally misreported. If an agency did misreport a cost or square footage figure, it would affect the average lease rate we calculated for Shawnee County. Our findings begin on page 5, following a brief overview.

## Overview of Leased Office Space in Shawnee County

At the end of 1999, a total of 54 State agencies were leasing office space from private landlords at 84 different locations within Shawnee County. On average, here's how this leased space compared with the State-owned office space in the Landon, Docking, and Memorial buildings:

### Comparison of Leased and Owned State Office Space in Shawnee County

	number of sq. feet	Annual cost	Average cost/sq.ft.
<b>LEASED SPACE</b>	900,000	\$10.1 million	\$11.22
<b>STATE- OWNED SPACE</b>	625,000	\$8.7 million	\$13.95

The maps on pages 6 and 7 show where State agencies were leasing office space in Shawnee County and downtown Topeka as of December 1999. More information about each agency's leased space and costs is presented in Appendix B.

### **At the Governor's Direction, The State Is in the Process of Relocating Many State Employees To Office Space in and Around the State Capitol**

Plans to relocate many State employees into office space in the downtown Topeka area began to take shape in 1995. Then in early 1997, the Governor publicly declared his preference to consolidate State agencies into fewer locations in downtown Topeka.

**In May 1997, the Department of Administration's Division of Facilities Management solicited proposals for leasing office space in close proximity to the Capitol Area Plaza.** The primary target development area was outlined as between 4<sup>th</sup> and 14<sup>th</sup> streets, and between Monroe Avenue and Tyler Street. Besides offering existing office space, developers were encouraged to propose build-to-suit and major remodeling projects.

In all, 24 developers submitted proposals. A selection committee evaluated these proposals, six of which ultimately were discussed with the Legislature's Joint Committee on State Building Construction. Based on these discussions, the State entered into contractual agreements to do the following:

- **Build a new general-use office building at 10<sup>th</sup> and Jackson.** In December 1998, the Department of Administration signed contracts with the Topeka Public Building Commission to issue \$46.4 million in bonds to finance the construction of the 5-story, 265,000-square-foot office building with an attached parking garage. That building is called the Signature Building.
- **Build a new office building for SRS at 5<sup>th</sup> and Van Buren.** In January 1999, the Department of Social and Rehabilitation Services signed contracts with the Topeka Public Building Commission to issue \$11.4 million in bonds to finance the construction of a 3-story, 96,000-square-foot office building. That office building is called the Myriad Building.
- **Buy the existing Security Benefit Group building at 7<sup>th</sup> and Harrison.** In December 1999, the Department of Administration signed contracts with the Kansas Development Finance Authority to issue \$21.6 million in bonds to finance the lease-purchase of this 14-story, 297,000-square-foot office building.

## **What's the Most Cost-Effective Way To Provide Office Space for State Agencies?**

Whether it's more cost effective to build new buildings, lease space in existing buildings, or buy existing buildings depends on a number of economic factors in effect at the time a decision is being made. Those include the cost to build or buy and remodel a building, current interest rates, and current and expected future lease rates. A number of non-economic factors also may enter into any decision—such as a desire to centralize agencies downtown. Based on existing documentation, it was difficult for us to determine exactly what factors State officials considered in evaluating recent proposals to construct new office space and acquire the Security Benefit Group building.

After these 3 buildings come on-line, the State still will be leasing more than 500,000 square feet of office space. Our preliminary analysis showed it wouldn't be cost-effective for the State to build another major office building, but it may be cost-effective to consider buying an existing building. These and related findings are discussed in more detail in the sections that follow.

### **Numerous Factors Can Come into Play When Deciding How Best to Provide Office Space**

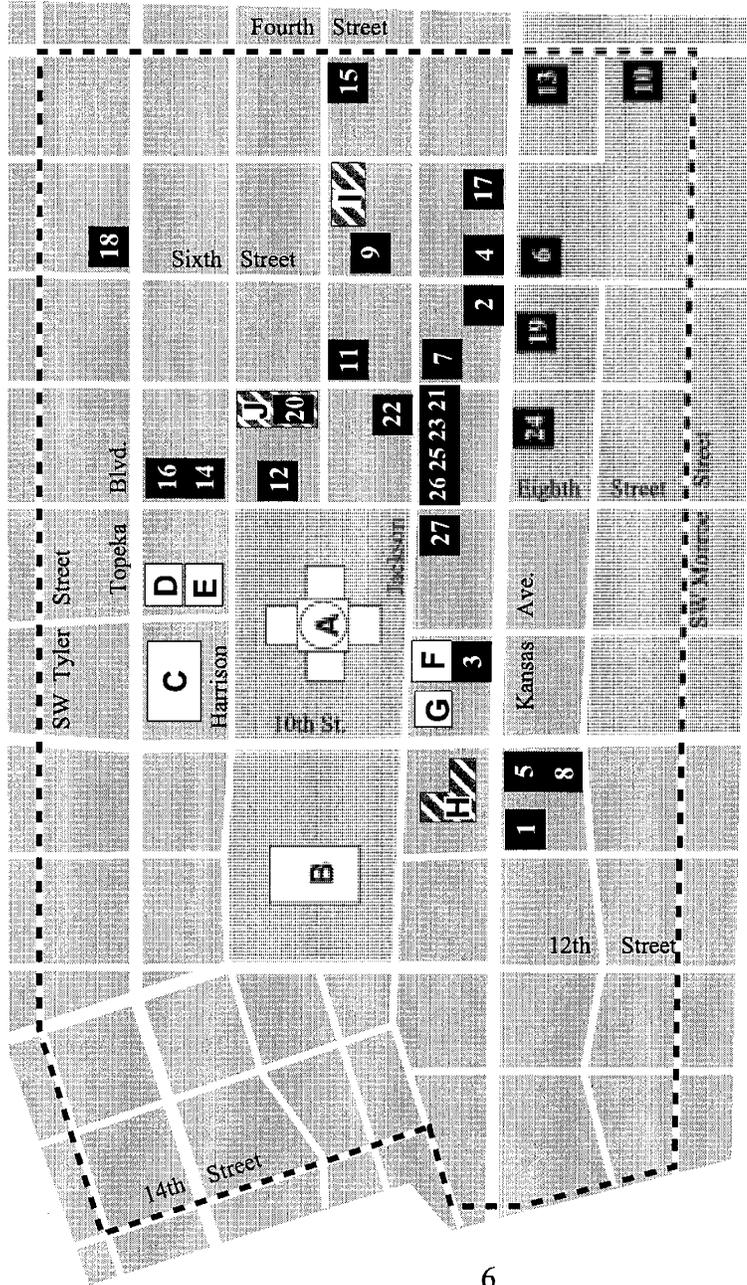
A number of economic factors need to be considered when determining the most cost-effective means of providing office space for State agencies. These factors include:

- current construction costs
- current interest rates
- the cost of buying an existing building
- remodeling costs
- projected building operation and maintenance costs
- current and projected lease rates

Typically, a number of these factors are included in an analysis called a net present value analysis that allows the cost of leasing and owning a building to be compared. With that comparison, someone can estimate which course of action will produce the lowest costs over a stated period of time.

Decisions about office space can't always be made solely on economic factors, however. A number of other considerations may enter into the picture—either as advantages or disadvantages—including those listed on page 8.

# Owned and Leased State Agency Office Space In Downtown Topeka



Boundary of downtown Topeka as defined by the Department of Administration for the 1997 RFP for leasing office space in close proximity to the Capitol Plaza.

## STATE-OWNED PROPERTIES IN THE DOWNTOWN AREA

- A = Capitol
- B = Judicial Center
- C = Docking State Office Building
- D = Insurance Department
- E = Dillon House
- F = Landon State Office Building
- G = Memorial Building
- H = Signature Building (under construction)<sup>(a)</sup>
- I = Myriad Building (under construction)<sup>(a)</sup>
- J = SBG Building (acquired)<sup>(a)</sup>

<sup>(a)</sup> The State has a lease-purchase agreement on this building

## STATE-LEASED PROPERTIES

Facility	Occupants
1 1020 S Kansas	Architectural Services
2 109 SW 6th	Emergency Medical Svcs, Bd of
3 109 SW 9th	multiple agencies
4 112-114 SW 6th	Indigents Defense Services
5 117 SE 10th	Education, Bd of
6 120 SE 6th	multiple agencies
7 122 SW 7th	Kansas Highway Patrol
8 123 SE 10th	Education, Bd of
9 214 SW 6th	multiple agencies
10 217 SE 4th	Transportation, Dept of
11 222 SW 7th	Kansas Inc
12 300 SW 8th	Health Care Stabilization Fund
13 400 S Kansas	Credit Unions, Dept of
14 400 SW 8th	Health & Environment, Dept
15 400 Van Buren	Motor Pool Garage
16 415 SW 8th	SRS
17 503 S Kansas	multiple agencies
18 512 SW 6th	Human Resources, Dept of
19 618 S Kansas	Securities Commissioner
20 700 SW Harrison	multiple agencies
21 700 SW Jackson	multiple agencies
22 701 SW Jackson	multiple agencies
23 708 SW Jackson	Animal Health Dept
24 712 S Kansas	Behavioral Sciences Reg. Bd
25 714 SW Jackson	multiple agencies
26 720 SW Jackson	Juvenile Justice Authority
27 800 SW Jackson	multiple agencies



### **Financial Considerations:**

- With leasing, costs will continue to rise subject to market conditions
- Outright ownership requires more capital outlay up-front, but can help the State control future costs
- Ownership requires on-going maintenance and upkeep expenses. State ownership removes property from the tax rolls, which can be an important political consideration

### **Flexibility Issues:**

- Ownership may lock a State agency into a particular location, and make it more difficult to respond to program changes
- At the same time, ownership can provide more flexibility in terms of moving agencies from one building to another, without worrying about when leases expire

### **Location Issues:**

- Leasing can be more practical for small agencies in rural areas
- Housing more than one agency together can offer better coordination and access to the public
- Whether space is leased or owned, adequate parking must be available for employees and for members of the public

### **Efficiencies:**

- A single agency housed in multiple locations may experience increased travel time and decreased employee productivity
- Consolidating agencies into buildings may save travel, communications, and other support costs

The analyses we present in this audit were based solely on economic considerations, which generally should be the first step in the decision-making process.

Once the cost-effectiveness of any particular method of providing office space is determined, then decision-makers can factor in any of the other relevant considerations, and assess whether the benefits outweigh any increase in costs.

### **It's Difficult to Know What Factors State Officials Considered in the Recent Decisions to Purchase or Construct Office Buildings Downtown**

As described in the overview, the Division of Facilities Management solicited proposals in May 1997 from developers to provide downtown office space. The State

<b>Characteristic</b>	<b>Security Benefit</b>	<b>Myriad</b>	<b>Signature</b>
<b>Type of acquisition</b>	Lease / purchase	Lease / purchase	Lease / purchase
<b>Square feet of usable office space --</b>	227,000	85,500	255,000
<b>Purchase or construction price</b>	\$18.5 million	\$10.5 million	\$33.1 million for building and \$9.5 million for garage
<b>Bond issuance costs</b>	\$3.1 million	\$0.9 million	\$3 million for building and \$800,000 for garage
<b>Amount of bonds issued</b>	\$21.6 million	\$11.4 million	\$46.4 million (a)
<b>Term of bond issue</b>	35 years	30 years	30 years
<b>Bonds issued by</b>	Kansas Development Finance Authority	Topeka Public Building Commission	Topeka Public Building Commission
<b>Source of revenue to pay off the bonds</b>	building rent	building rent	building rent
<b>Primary tenant</b>	Department of Transportation	Department of Social and Rehabilitation Services	Department of Health and Environment
<b>Cost to buy building when bonds are retired</b>	\$100 and reasonable closing costs	\$100 and reasonable closing costs	\$100 and reasonable closing costs
<b>Property taxes</b>	Paid by Security Benefit until they move out, then none	Annual payment in lieu of taxes of \$25,000 for 30 years	None
<b>Projected annual cost (debt service and operations) in first year of State occupancy</b>	\$3 million	\$964,000	At least \$3.5 million
<b>Projected cost per sq. ft. in first year of State occupancy</b>	\$13.19	\$11.28	More than \$15.00
<b>Estimated date of occupancy for State agencies</b>	Possibly May 2003	September 2000	September 2001

(a) doesn't include approximately \$6 million in additional bonds that will likely be issued to complete the project

ultimately decided to purchase an existing building from Security Benefit Group, and to build 2 other office buildings—the Signature Building at 10<sup>th</sup> and Jackson, and the Myriad building at 5<sup>th</sup> and Van Buren. These 3 facilities will add about 568,000 square feet of office space near the Capitol for State agencies. Some background information about each project is provided in the table on the previous page.

The proposals submitted by 24 developers were evaluated by a selection committee that included staff from the Department of Administration and its Division of Facilities Management, and representatives from the Departments of Transportation, Health and Environment, SRS, and Agriculture. These were the agencies that likely would be occupying the new facilities.

**We found little documentation to show what the selection committee did to evaluate the proposals submitted by developers.** During this audit, we expected to find written documentation showing what criteria the selection committee had used in evaluating these bid proposals, the results of the analyses performed, and the rationale for deciding which proposals to take to the Legislature. However, we found no documentation related to any cost-benefit calculations that had been performed on the proposals, nor did we find documentation of why certain proposals were rejected.

We interviewed several of the people who served on the selection committee, including the Facilities Management employee who was responsible for coordinating the committee’s analysis and documenting the decisions reached. He told us he thought he recalled using different colored paper to distinguish between proposals that had merit and those that didn’t. None of those summaries could be found. We also reviewed all the records relating to the selection committee’s consideration of these proposals that Division staff could find. However, those records essentially only contained the proposals and correspondence between the parties.

The only documentation we found was a side-by-side comparison of certain factors from the proposals for constructing a new office building at 2 different sites in downtown Topeka. This document, which was presented to the Joint Committee on State Building Construction, compared such factors as parking, square footage, and land acquisition costs, and for each factor indicated which site had an advantage over the other. This comparison contained no cost-benefit analysis, nor did it contain a recommendation about which site was better.

Maintaining documentation of what the selection committee did to evaluate the proposals would provide both a record of the State’s decisions and justification for why decisions were made, and could be extremely useful in evaluating future proposals. Although such information would have been confidential while the evaluation process was on-going, it would have become public under the Open Records Act once the awards had been made. Other information we learned about how the decisions were made on each of these buildings is contained in the box on the next page.

- **Security Benefit Group Building** This building's proposals included both a lease option and a purchase option. Several agencies expressed an interest in occupying office space in the building, including the Departments of Agriculture, Transportation, and Health and Environment. In September 1999, the Joint Committee on State Building Construction authorized the Secretary of Administration to proceed with negotiations for the Security Benefit property.

Department of Administration records indicate that four appraisals of the Security Benefit building had been performed in 1999. The three appraisals performed for the State valued the building between \$12 and \$14 million, while an appraisal performed on behalf of the Security Benefit Group valued the building at slightly more than \$25 million. At the October 1999 meeting, the Secretary of Administration informed the Committee that a sales price of \$18.5 million had been negotiated, subject to the Committee's approval. The Committee approved this purchase.

The Department of Transportation is scheduled to move into the building. Before that happens, certain renovations are planned. Currently, the planned renovations include a tunnel to the Capitol, security and telecommunications upgrades, asbestos/lead abatement, and structural upgrades. These renovations are expected to cost an additional \$15 million.

- **Signature Building** Two proposals for constructing a new State office building were being considered; 10<sup>th</sup> and Harrison and 10<sup>th</sup> and Jackson. In February 1998, the Joint Committee on State Building Construction authorized the Department of Administration to proceed with the proposal for a new building at 10<sup>th</sup> and Jackson. According to the documentation we found, the factors State officials considered in making this decision included parking issues, square footage, and land acquisition costs. In December 1998, the Department of Administration signed a lease with option to purchase agreement with the Topeka Public Building Commission. (The Commission was created by the City of Topeka, in accordance with State law. For this project, it acquired the property, is developing the site, will lease the facility to the State, and has issued bonds to finance the project.)

In considering this proposal, Department officials established a goal of having the first year's debt service and operational costs for the building not exceed \$15 per square foot. As of December 1998, the rental rate for the building was estimated to be \$14.25 per square foot. Because of certain additions to the original plans, however, Department officials told us the Building Commission probably will have to issue an additional \$6 million in bonds later in calendar year 2000 to complete the project. Given these additional debt service costs, an October 1999 estimate placed the total cost at \$15.07 per square foot. Since then interest rates have increased, so the final costs could be higher.

- **Myriad Building** According to a Department of Administration official, the Department of Social and Rehabilitation Services, as the sole tenant of the building, was responsible for bringing an affordable deal for approval to the Joint Building Committee. An SRS official told us the SRS selection committee made an effort to obtain the lowest cost, but that no price goal was established.

In June 1998, SRS executed a 30-year lease of the facility with the project developer, but that agreement was voided and replaced by a January 1999 agreement with the Topeka Public Building Commission. This new agreement was executed in order to reduce the project's financing costs. Because the Building Commission can issue bonds, it can raise the money necessary to finance the project at a lower interest rate than the private developer could obtain through private-sector financing. In addition, because the building will no longer be subject to property taxes, SRS has agreed to make an annual payment in lieu of taxes to the City of Topeka of \$25,000 for 30 years. A preliminary analysis performed by Department of Administration staff shows the new agreement should save the Department about \$8.7 million over the 30 years of the project.

**After the Signature, Security Benefit, and Myriad Buildings Are Filled,  
The State Still Will Lease Enough Office Space  
To Consider Constructing or Buying Additional Buildings**

When the 3 newly built or acquired buildings are finished, many State agencies will be moving into them and out of their existing space. For example, the Department of Transportation is expected to move out of its current State-owned space in the Docking Building and leased space in the Thatcher building, and into the Security Benefit Group building.

**Based on the information available to us at the time of this audit, we estimated the State still would be leasing an estimated 521,000 square feet of office space after all agency moves brought about by the 3 new buildings are completed.** Although agencies' actual assignments to office space could change, as could their eventual space needs, the most current information provided to us by the Division of Facilities Management is summarized below:

**Calculation of Remaining Leased Space**

Total square feet leased by agencies in Shawnee County as of 12/99	900,000
Square feet of leased space agencies will vacate by moving to new buildings	<u>(218,000)</u>
Remaining <u>leased</u> square feet	682,000
Mostly space vacated by agencies moving out of Landon and Docking that could be filled by agencies now in leased space	<u>(161,000)</u>
Approximate square feet of space State agencies still would be leasing	521,000

Because of the volume of office space still needing to be leased, we looked at the cost-effectiveness of the following 2 options for providing additional State-owned office space:

- **constructing another new office building.** Department of Administration officials told us that, of all the proposals submitted by developers in 1997, a remaining possibility was a proposal to construct an office building with parking garage on property the State owns at 10<sup>th</sup> and Harrison.
- **acquiring an existing building.** We chose the Mercantile Bank Building for this analysis because the building owner offered it to the State as one of the proposals initially submitted in response to the State's solicitation for bids in 1997. The building also has been offered for sale in the past. As a result, fairly recent data were available. The building currently houses 3 State agencies, including Legislative Post Audit, and is located directly across from the Capitol.

## Preliminary Analysis of the Cost-Effectiveness of Two Options for Housing State Employees

### Option: Building another new office building

**Bottom Line:** Over the next 40 years, the State would spend \$17.9 million more (in today's dollars) to build and operate another building downtown rather than continuing to lease privately owned space.

**For our analyses, we used the same cost data and assumptions that were used for the Signature Building.** (The major assumptions are presented in Appendix C.) We based our analysis on a 40-year time span.

Over 40 years, it would cost \$17.9 million more in today's dollars to construct a new building rather than continue to lease space in existing buildings. The State would own the building, once the bonds were paid off, but we were unable to estimate the residual value of the building at the end of 40 years.

This cash flow analysis suggests the State would pay out less money by continuing to lease office space, rather than by constructing another building the same size and cost as the Signature Building. However, other factors the State would need to consider include:

- different or more up-to-date cost figures, financing options, and assumptions could significantly change this picture. For example, the answer could be very different if building costs could be reduced, if interest rates rise, or if leasing costs escalate faster than 2% a year
- relocation costs or costs for terminating leases early would need to be considered
- whether the long-term cost savings achieved through continued leasing of office space are more valuable than having more State employees work near the Capitol
- whether the State might achieve certain non-financial benefits by having State employees work in newer office space more centrally located

### Option: Acquire the Mercantile Building

**Bottom Line:** If the State could acquire the Mercantile Building at a cost at or below the \$10.5 million figure mentioned in a 1997 proposal submitted by the building's owner, then it could make economic sense for the State to consider doing so. However, additional factors that we couldn't examine would need to be reviewed. The 1997 proposal included the office tower and garage.

**For our analysis, we used estimated operating costs and revenues for the building.** We made some assumptions about how those revenues and expenses would increase over time (See Appendix C for those assumptions) and we determined how much money would be left to pay off debt after the building's operating expenses had been paid. In essence, this told us how much the State should reasonably consider paying for the building.

**There are a number of factors our economic analysis couldn't take into account which would have to be considered in determining whether the State would want to consider acquiring this building.** Those include:

- different or more up-to-date cost figures, financing options, and assumptions could significantly change this picture.
- the structural integrity of the building which would have to be determined by engineering studies
- the cost of renovations necessary to make the building functional for State agencies
- the cost of installing fire sprinklers, which currently aren't in the building
- whether the building is useful to the State (the amount of office space on each floor is limited to about 6,000 square feet, which would make the building less attractive for larger agencies.)
- what should be done with the ground floor space, which is mostly leased to a bank
- whether there are any environmental concerns to be dealt with

**In general, it appears it wouldn't be cost-effective for the State to build another major office building, but it may be cost-effective to consider buying an existing building.** Our analyses are shown on the previous page. The reader should be aware, however, that in performing these analyses we had to use unaudited financial information, and we had to make many assumptions. As a result, our analyses should be considered only a preliminary indication of the cost-effectiveness of these options. More complete and up-to-date financial and non-financial factors would have to be included in any proper evaluation of such options.

**Better Information About State Leases  
Could Help the Department of Administration  
In Analyzing Future Decisions About State Buildings**

The Division of Facilities Management has been working for several years to collect lease data for State agencies that generally hasn't been available in the past. The only costs listed in the database are the actual lease rates. Because some agencies may have things like utilities included in their lease rate, while others may pay for them separately, the information in the database doesn't allow the true costs to be known. Also, any comparisons among agencies' lease rates based on information in the database won't be consistent and could result in erroneous conclusions.

To perform our analysis, we surveyed the 54 State agencies who lease space in Shawnee County to have them verify the information in the Department's database and to have them provide more complete information about their lease costs. Through this survey, we found the database had some inaccuracies—such as duplicate entries, and warehouse space being included in the office space category.

The Division currently is upgrading some of its information systems. For example, it has purchased comprehensive facilities management software that will allow it to establish a database of information relating to:

- facility maintenance activity tracking and reporting
- capital budget planning
- space planning and leasing services
- project and construction planning and management
- condition assessment of building components

In essence, this program will give the Division more information upon which to prioritize needs, and will allow the Division to be able to assess the condition of Landon and Docking buildings in terms of the individual components, including safety, aesthetics, outside walls, and the like. Initially, a consultant will assess all the components, but Division staff will be trained to do this in the future. The information provided will allow Division staff to update the Legislature on funding needs for maintenance, and the consequences of deferring maintenance.

## Kansas Has Used a Number of Methods to Acquire Buildings

The Docking State Office Building was purchased through bonds issued by the State Office Building Commission. The Judicial Center was built using State General Fund appropriations. The Landon Building was purchased through a loan from the Pooled Money Investment Board using idle State funds. The 3 newest buildings—Signature, Myriad, and Security Benefit—are all being acquired using lease-purchase agreements. The table below shows the advantages and disadvantages of these and other financing methods.

Type of Financing	Advantages to State	Disadvantages to State	Other states using this method
Appropriations	<ul style="list-style-type: none"> <li>• only cost is acquisition cost</li> <li>• no interest or financing costs are incurred</li> <li>• can be quick because no time needed for bond sale</li> </ul>	<ul style="list-style-type: none"> <li>• large, up-front cash outlay of State operating funds</li> <li>• takes cash away from other possible uses, including investment and funding other programs</li> </ul>	North Carolina Missouri
Obtain loan from State idle funds	<ul style="list-style-type: none"> <li>• could borrow funds at a low interest rate</li> <li>• smaller, up-front cash outlay</li> </ul>	<ul style="list-style-type: none"> <li>• State (PMIB) might be able to earn more interest through investment in the marketplace</li> <li>• idle funds would be tied up and unavailable if emergency situation occurred</li> </ul>	
Issue bonds	<ul style="list-style-type: none"> <li>• smaller, up-front cash outlay</li> </ul>	<ul style="list-style-type: none"> <li>• many costs to issue bonds are incurred up-front</li> <li>• interest costs are incurred until outstanding bonds are retired</li> </ul>	Wisconsin Minnesota Florida New York
Lease/purchase arrangement with owner financing	<ul style="list-style-type: none"> <li>• smaller, up-front cash outlay</li> <li>• property remains on tax rolls until State takes title</li> <li>• project may be eligible for certain governmental programs, such as tax abatements or tax increment financing, thus decreasing State's monthly payments to owner</li> </ul>	<ul style="list-style-type: none"> <li>• if private sector financing is used, monthly rental payments and project's total cost are increased because private sector financing is more expensive than public financing</li> <li>• interest costs are incurred over period that debt is outstanding</li> </ul>	

**Other states we reviewed haven't used lease-purchase arrangements to acquire new buildings over the last decade.** We surveyed officials from 6 other states to find out how their states financed the acquisition of office space for state employees within the metropolitan areas of their state capitals. During the 1990s, these 6 states built 17 new buildings and purchased 11 existing buildings. The most frequent financing methods they cited were state appropriations and general obligation bonds. As the table below shows, these states have used 4 different funding methods, and for a variety of reasons.

**Other States' Funding Methods for  
Acquiring Office Space for State Employees**

**Issued General Obligation Bonds (financed over 20 years)**

- |           |   |
|-----------|---|
| Wisconsin | <ul style="list-style-type: none"> <li>• state financing is cheapest method</li> <li>• G.O bonds are most desirable when considering the entire financial condition of the state</li> </ul> |
| Minnesota | <ul style="list-style-type: none"> <li>• simple and cheapest way to finance acquisitions</li> </ul>   |

(Note: Kansas is prohibited by the State Constitution from issuing General Obligation Bonds without a direct vote of the people.)

**Used State Appropriations**

- |                |   |
|----------------|---|
| North Carolina | <ul style="list-style-type: none"> <li>• state prefers pay-as-you-go basis</li> </ul>                   |
| Missouri       | <ul style="list-style-type: none"> <li>• outright ownership is preferred to lease / purchase</li> </ul> |

**Issued Revenue Bonds (financed over 20 years)**

- |         |  |
|---------|--|
| Florida | <ul style="list-style-type: none"> <li>• ownership is preferred to lease / purchase</li> </ul> |
|---------|--|

**Issued Certificates of Participation**

- |          |   |
|----------|---|
| New York | <ul style="list-style-type: none"> <li>• Governor can issue without legislative approval</li> <li>• doesn't count against bonded indebtedness of the state</li> </ul> |
|----------|---|

As the above shows, there isn't one method that stands out as the most common way states finance the acquisition of office space. The methods used seem to depend on the financial condition and particular preferences of the individual states.

**Conclusion**

With numerous State agencies scattered in so many buildings around the Topeka area, it makes sense to do some long-range planning aimed at consolidating office space and looking at the most cost-effective ways of housing State employees. There's no standard method of providing office space that will always be the most advantageous. Sometimes it will be better

to build or buy existing space, and sometimes it will be better to lease, depending on the specific economic and non-economic goals that are to be achieved at the time. However, when these decisions are made it's critical that the State have complete and accurate information about its lease costs, and that it considers all factors—both economic and non-economic—that have a bearing on a particular situation. It's also important that things such as cost-benefit analyses and rankings of proposals be fully documented and maintained so that State officials can demonstrate how they made their decisions, and that those decisions are truly in the State's best interest.

### **Recommendations**

1. To ensure that future acquisitions of office space for State employees are properly evaluated and documented, the Department of Administration should do the following:
  - a. develop procedures that specify the types of analyses—including cost-benefit analyses, proposal rankings and the like—that will be performed or considered for future acquisitions of office space.
  - b. require that those analyses be formally documented and maintained in accordance with State records retention requirements.
2. To ensure that complete and accurate information about all leases of office space is available for review and analysis, the Division of Facilities Management should work with State agencies to gather information detailing the various components of the cost of occupying that space, including utilities, custodial services, parking, security, and other applicable services.

## **Could Kansas Save Money by Having the Department of Administration Negotiate All Leases?**

In Kansas, individual agencies negotiate their own lease agreements and the Secretary of Administration approves them. Possible benefits from having a single agency responsible for Statewide leasing functions include having a consistent way of doing business, and getting volume discounts or other lease concessions. It's likely these benefits would result in some efficiencies or cost savings in Kansas. On the other hand, there's a risk that giving one agency too much authority over lease negotiations could result in some agencies' specialized needs not being fully considered.

Officials from several states with a single agency responsible for leasing office space told us they were happy with the results. An official in Minnesota told us that their lease rates average about 4% less than the asking rate. An official from Missouri told us the state had been able to significantly reduce the total amount of office space leased as a result of centralized leasing. These and related findings are discussed more fully in the sections that follow.

### **In Kansas, Individual Agencies Negotiate Their Own Leases But Those Leases Must Be Approved By the Secretary of Administration**

Centralized leasing means one agency is responsible for negotiating all State leases. In Kansas, agencies are responsible for negotiating their own leases (up to 10,000 square feet). As allowed by law, the Secretary of Administration has designated the Division of Facilities Management as the entity responsible for helping agencies with their lease negotiations and for approving the leases.

For leases involving more than 10,000 square feet, the Division of Facilities Management helps the agency prepare a request for proposals, reviews any proposals received, and votes on those proposals. The Director of Facilities Management presents the proposal to the Joint Committee on State Building Construction for final approval.

**The current Director of Facilities Management favors moving to centralized lease negotiations for several reasons.** The Director told us he thought the State potentially could save money by ensuring that lease rates are competitive to the marketplace. Also, agencies currently lease space to fit their needs independent of an overall plan. According to the Director, having one agency be responsible for space considerations may lead to underused property being made more productive, and to contracts with consistent space standards. Centralizing this responsibility within one agency would require a change in State law.

Legislators have raised questions about whether centralized lease negotiations could help eliminate variations in lease rates currently paid by different agencies occupying space in the same building. In Shawnee County, 12 buildings house 2 or more State agencies. We reviewed information about leases in 3 of those buildings, and found significant variations in 2 of them, as described in the accompanying table:

**Differences in Rates for State Tenants Within the Same Building**

Building	Tenant	Date Signed	Square Footage	Cost/Sq Foot	Possible Reasons For Differences
Mercantile	Performance Review Board	7/1/97	743	\$13.75	Differences in this building appear to be linked to volume discounts for leasing more space. As square footage increased, rental rates dropped.
	Legislative Post Audit	7/1/96	6,127	\$13.45	
	Human Resources	7/1/97	29,408	\$13.08	
701 SW Jackson	Gaming Commission	7/1/98	4,585	\$9.76	The Gaming Commission doesn't have any janitorial service, nor does it have a rate escalation clause. There was no obvious explanation we could identify for the difference between the other 2 agencies.
	Judicial Branch (Disciplinary Administration)	7/1/97	5,000	\$12.38	
	Indigent's Defense Service	7/1/98	5,000	\$14.79	
Security Benefit	Commerce and Housing	10/1/97	22,165	\$12.50	There were no significant differences in the rates paid by State agencies in this building, even though the leases began 1.5 years apart.
	Board of Regents	3/1/99	8,620	\$12.53	

Source: Data reported to LPA by individual agencies. Costs include basic rent plus utilities and other expenses.

Examples of other general factors that can result in different lease rates in the same building include:

- the inclusion of parking spaces in one agency's rent and not in another's
- charges for renovation costs one agency incurred that another agency didn't
- special security considerations one agency has that another agency doesn't

**Centralized lease negotiations won't necessarily eliminate differences in lease rates caused by the types of reasons cited above.** However, having one centralized agency responsible for negotiating all leases makes it more likely that someone will be aware of differences in lease rates in the same building. In cases where

there's no apparent explanation for the differences, this agency would be in a better position to negotiate concessions from the landlord. Also, having a central agency responsible for all the leases in a building could result in more standardized practices regarding payment for extras, such as parking, as part of lease costs.

**Centralized Leasing Offers a Number of Advantages That Could Save the State Money, But There Also Can Be Some Disadvantages for State Agencies**

To help determine whether Kansas may want to consider having one agency responsible for negotiating all office space leases, we contacted officials in 6 other states, surveyed officials in 54 State agencies in Shawnee County who lease space in privately owned buildings, and contacted the owners or managers of several of the buildings in which State agencies lease office space. They told us about a number of advantages and disadvantages that might result from having one agency negotiate all leases. Those are - summarized in the following table.

**Opinions About Centralized Leasing**

	<b>Other States</b>	<b>Shawnee County Agencies</b>	<b>Landlords</b>
<b>Advantages Cited</b>	<ul style="list-style-type: none"> <li>• consistent space standards</li> <li>• consistent way of doing business in the State</li> <li>• potential for volume discounts</li> <li>• increased knowledge and expertise</li> <li>• ease of budgeting lease funds</li> <li>• agencies don't get into bidding wars for the same space</li> </ul>	<ul style="list-style-type: none"> <li>• less work for agency officials</li> <li>• increased knowledge and expertise</li> <li>• potential to negotiate better rates</li> <li>• leases would be uniform and meet all required mandates</li> </ul>	<ul style="list-style-type: none"> <li>• easier to deal with only one State official who would be more knowledgeable</li> </ul>
<b>Disadvantages Cited</b>	<ul style="list-style-type: none"> <li>• agencies resent the loss of authority</li> <li>• hard to obtain funding for general governmental services</li> <li>• potential to take longer</li> </ul>	<ul style="list-style-type: none"> <li>• loss of control for agencies</li> <li>• agencies are in the best position to determine their own space needs</li> <li>• another layer of bureaucracy that could lead to delays</li> </ul>	<ul style="list-style-type: none"> <li>• likely to be difficult for the Division of Facilities Management to negotiate all leases Statewide</li> </ul>

Source: Data provided to LPA through interviews and surveys

**Of the people we contacted, officials from other states were the most positive about the advantages of centralized lease negotiations.** Altogether, 5 of the 6 states we contacted (Missouri, New York, Wisconsin, North Carolina and Minnesota) have a

single agency responsible for lease negotiations. Except for Missouri, all those states have had that arrangement for more than 10 years.

Florida was the only state we contacted that didn't have a single agency responsible for lease negotiation. Officials there told us a bill before the Florida Legislature several years ago that would have designated a single agency to negotiate leases failed because of heavy opposition from state agency officials who were concerned about losing their authority to enter into leases.

Although the states that have it favored the concept of a single leasing agency, most couldn't document specific savings they'd achieved. However, an official from Minnesota told us that, on average, state government in Minnesota pays about 4% less to lease space from private landlords than the asking rate. A Missouri official told us that the State now leases almost 15% less total office space than it did in the past. She generally attributed the reduction in leased space to consolidating agencies to have them share common areas such as conference rooms, training rooms, and break rooms.

**Officials from Kansas agencies were less enthusiastic about centralized leasing, citing concerns that their specialized needs might not be fully taken into account.** When we asked State agency officials if Kansas should centralize its lease negotiations, we received the following responses from the 48 agencies that answered the question:

<u>Response</u>	<u>Number of Agencies</u>	<u>Percent</u>
yes	8	17%
no	16	33%
uncertain	24	50%

Source: LPA tally of survey responses

The major concern expressed by agency officials in Shawnee County was the fear that the Division of Facilities Management wouldn't recognize their specialized space needs. Respondents to our survey said that agency officials are best able to determine their space needs. Another concern was that the Division of Facilities Management lease services would be impersonal, bureaucratic, and slow. Such concerns could be minimized by ensuring that agency officials were involved throughout the process.

**The concept also got mixed reviews from some of the landlord representatives we talked to.** One told us that it would be nice to have a single entity to deal with, and that the State could potentially have increased negotiating power because it would be dealing with large quantities of space rather than small individual agency spaces one at a time. Another landlord said he'd rather work directly with the building tenants than with the Division. A third thought the Division would have difficulties negotiating all leases Statewide.

### **Conclusion**

Based on 6 states we contacted, it appears that Kansas is in the minority in not having a central agency designated to perform lease negotiations. Although some State agency officials have expressed concern about their needs not being met or losing control of their lease negotiations under a centralized process, it appears the potential for efficiencies and benefits that could accrue from such a process outweigh the limitations. In addition, most agency concerns could be addressed by requiring the Department of Administration to work closely with agencies in determining their space needs, and by providing for an appeals process for agencies that think their needs aren't being met.

### **Recommendations**

1. The Joint Committee on State Building Construction should consider the merits of centralizing the function of leasing space for State employees. If the Committee determines that centralization would benefit the State, then it should consider introducing legislation to grant a single agency the authority to enter into lease arrangements for the State.

## **APPENDIX A**

### **Scope Statement**

This appendix contains the scope statement approved by the Legislative Post Audit Committee on March 16, 1999. The audit was originally requested by Representative Kline, and revised by Senator Vidricksen.

## SCOPE STATEMENT

### **Assessing the Benefits of Leasing vs. Owning Office Space for State Employees**

There are currently more than 50 State governmental office locations in Shawnee County. The State owns a number of buildings that house office space for State employees, and there are plans for building another State office building in downtown Topeka. In addition, the State has entered into numerous leases for additional office space. Because State agencies negotiate their own leases, in buildings like the Mercantile Bank Building that house multiple State agencies the State hasn't been able to use its leverage to negotiate volume discounts or other lease concessions.

Numerous factors can come into play when considering the advantages and disadvantages of leasing versus owning State office space. Some of the advantages of leasing can include limited liability and manageable risks, flexible occupancy, owner financing and oversight, and private-sector building management. Some of the advantages of building ownership include attractive financing rates, stable locations, predictable and systematic maintenance schedules, predictable annual budget costs, and custom-designed buildings.

Recently, the State has begun an effort to consolidate and centralize State governmental operations. In doing so, the State has used a variety of financing options, including traditional lease variations for a certain period of time, lease with an option to purchase at a pre-determined ceiling price, and lease-purchase (primarily owner-financed). The Joint Committee on State Building Construction also has adopted policies for leasing and acquiring real property designed to assure competition, cap costs, and maximize agency flexibility to ultimately own facilities.

Legislative questions have been raised about a number of the benefits of leasing versus owning State office space. A performance audit in this area would address the following questions:

- 1. What factors, including costs, determine whether a State agency should lease or purchase property?** To answer this question, we'd review relevant literature regarding leasing or purchasing property, and would interview officials from the Division of Facilities Management and from the National Association of State Facilities Administrators to identify what major factors need to be taken into account. We'd also determine whether and how the Divisions of Purchases and Facilities Management make sure all the appropriate factors are considered before approving an agency's lease for office space.
- 2. What funding mechanisms should the State use to acquire office space for State agencies?** To answer this question we'd look at some examples of current arrangements the State has for providing office space for State agencies to determine which method appears to produce the lowest long-term costs. This would include looking at costs for buildings that are owned and buildings that are leased either under a traditional lease or lease-purchase arrangement. We'd also interview appropriate State officials and real estate experts, and review literature to identify other options for providing office space that aren't currently being used in Kansas. We'd discuss these other options with State officials and the experts

we contact to determine the pros and cons of using each type of arrangement. We'd also contact a sample of other States to determine what primary methods they use to acquire office space for their agencies, and which methods they have found to be most cost-effective. We'd conduct additional work as needed.

3. **What are the advantages and disadvantages of adopting a centralized approach to leasing State office space?** We'd interview officials from the Division of Facilities Management and from a sample of other states to determine what their current practices are, and what they think the advantages and disadvantages are for centralized and de-centralized approaches to leasing office space. We'd also identify those buildings in downtown Topeka in which multiple State agencies lease space, and would compare and contrast the lease arrangements they have negotiated. We'd perform other testwork as needed.

**Estimated completion time: 6-10 weeks**



## **APPENDIX B**

### **Kansas Agencies that Lease Office Space in Shawnee County**

The table on the next 2 pages identifies the agencies that lease office space in Shawnee County and the street address for each office. The table also shows how much office space leased at each site, the annual cost for that office space, and the corresponding cost per square foot. All of this information was supplied by agency officials.

## Kansas Agencies Leasing Office Space in Shawnee County

<u>Count</u>	<u>Agency name</u>	<u>Address</u>	<u>As Reported by Each Agency</u>		
			<u>Annual Rent</u>	<u>Square Feet</u>	<u>Cost per Square Foot</u>
<b>Downtown</b>					
1	Administration	1020 S Kansas	\$201,564	18,000	\$11.20
2	Administration	400 Van Buren	\$70,526	8,700	\$8.11
3	Aging	503 S Kansas	\$372,748	31,543	\$11.82
4	Agriculture	109 SW 9th	\$406,661	46,924	\$8.67
5	Animal Health	708 SW Jackson	\$38,817	4,086	\$9.50
6	Arts Commission	700 SW Jackson	\$26,100	2,635	\$9.90
7	Attorney General	700 SW Jackson	\$106,624	10,440	\$10.21
8	Barbering, Board of	700 SW Jackson	\$10,575	922	\$11.47
9	Behavioral Sciences Regulatory Bd	712 Kansas	\$39,032	4,592	\$8.50
10	Commerce And Housing	700 SW Harrison	\$277,063	22,165	\$12.50
11	Conservation Commission	109 SW 9th	\$47,587	3,924	\$12.13
12	Credit Unions	400 Kansas	\$20,404	2,166	\$9.42
13	Education	117 E 10th	\$491,148	53,445	\$9.19
14	Education	123 SE 10th	\$27,109	2,089	\$12.98
15	Emergency Medical Services	109 SW 6th	\$24,114	2,734	\$8.82
16	Fire Marshal	700 SW Jackson	\$75,926	7,231	\$10.50
17	Fort Hays State University	214 SW 6th	\$6,646	571	\$11.64
18	Gaming Commission	701 SW Jackson	\$44,738	4,585	\$9.76
19	Health & Environment	400 SW 8th	\$314,511	20,291	\$15.50
20	Health & Environment	109 SW 9th	\$104,658	12,564	\$8.33
21	Health Care Stabilization Fund	300 W 8th	\$69,174	4,941	\$14.00
22	Human Resources	512 SW 6th	\$201,930	19,594	\$10.31
23	Human Resources	800 SW Jackson	\$384,657	29,408	\$13.08
24	Indigents' Defense Services	701 SW Jackson	\$73,943	5,000	\$14.79
25	Indigents' Defense Services	714 SW Jackson	\$62,060	6,000	\$10.34
26	Indigents' Defense Services	700 SW Jackson	\$18,063	1,412	\$12.79
27	Indigents' Defense Services	700 SW Jackson	\$76,930	6,503	\$11.83
28	Indigents' Defense Services	112-114 W 6th	\$62,790	5,250	\$11.96
29	Judicial Branch	701 SW Jackson	\$61,900	5,000	\$12.38
30	Juvenile Justice Authority	714 SW Jackson	\$107,119	8,074	\$13.27
31	Juvenile Justice Authority	720 SW Jackson	\$56,250	4,500	\$12.50
32	Kansas Development Finance Authority	700 SW Jackson	\$33,337	3,175	\$10.50
33	Kansas Highway Patrol	122 SW 7th	\$186,847	15,140	\$12.34
34	Kansas Inc	222 SW 7th	\$27,500	2,500	\$11.00
35	Kansas Real Estate Appraisal Board	120 SE 6th	\$50,784	4,232	\$12.00
36	Kansas Technology Enterprise Corp.	214 SW 6th	\$110,352	7,947	\$13.89
37	KS Governmental Ethics Commission	109 SW 9th	\$32,994	2,869	\$11.50
38	Legislative Division of Post Audit	800 SW Jackson	\$82,408	6,127	\$13.45
39	Mortuary Arts	700 SW Jackson	\$10,000	1,000	\$10.00
40	Ombudsman for Corrections	700 SW Jackson	\$7,330	733	\$10.00
41	Performance Review Board	800 SW Jackson	\$10,216	743	\$13.75
42	Regents, Board of	700 SW Harrison	\$107,750	8,620	\$12.50
43	Revenue	120 E 6th	\$124,974	10,022	\$12.47
44	Securities Commissioner	618 South Kansas	\$79,948	7,581	\$10.55
45	Sentencing Commission	700 SW Jackson	\$22,489	2,150	\$10.46
46	Social & Rehabilitation Services	503 S Kansas	\$465,672	40,579	\$11.48
47	Social & Rehabilitation Services	415 SW 8th	\$196,460	16,000	\$12.28
48	State Bank Commissioner	700 SW Jackson	\$63,000	6,000	\$10.50
49	State Bank Commissioner	700 SW Jackson	\$12,548	1,195	\$10.50
50	Transportation	217 E 4th	\$420,272	35,317	\$11.90
51	Veterans Affairs	700 SW Jackson	\$3,731	364	\$10.25
52	Veterans Affairs	700 SW Jackson	\$18,143	1,770	\$10.25
53	Water Office	109 SW 9th	\$98,711	8,315	\$11.87
<b>Downtown sub-total</b>			<b>\$6,046,831</b>	<b>537,668</b>	<b>\$11.25</b>

## Kansas Agencies Leasing Office Space in Shawnee County

			<u>As Reported by Each Agency</u>		
<u>Count</u>	<u>Agency name</u>	<u>Address</u>	<u>Annual Rent</u>	<u>Square Feet</u>	<u>Cost per Square Foot</u>
<b>Outside Downtown Core</b>					
1	Administration	610 SW 10th	\$36,875	3,706	\$9.95
2	Agriculture	Forbes Field	\$189,200	17,200	\$11.00
3	Agriculture	1643 SW 41st St	\$21,911	3,000	\$7.30
4	Agriculture	Forbes Field	\$54,000	6,800	\$7.94
5	State Bank Commissioner	150 W 30th	\$8,067	787	\$10.25
6	Board of Healing Arts	235 S Topeka	\$91,820	8,313	\$11.05
7	Citizen Utility Ratepayers Board	1500 SW Arrowhead	\$19,085	1,242	\$15.37
8	Corrections	3400 Van Buren	\$71,507	7,527	\$9.50
9	Cosmetology, Board of	2708 N Topeka	\$21,508	2,582	\$8.33
10	Dental Board	3601 SW 29th	\$11,293	708	\$15.95
11	Health & Environment	J Street 2 North	\$440,000	40,000	\$11.00
12	Human Resources	1430 SW Topeka	\$352,732	33,700	\$10.47
13	Human Resources	420 SE 6th	\$64,925	6,125	\$10.60
14	Kansas Corporation Commission	1500 SW Arrowhead	\$550,896	34,758	\$15.85
15	Kansas Correctional Industries	Forbes Field	\$33,225	7,530	\$4.41
16	Kansas Lottery	128 N Kansas	\$328,592	29,400	\$11.18
17	Kansas Real Estate Appraisal Board	1100 SW Wannamaker	\$14,594	1,081	\$13.50
18	Racing Commission	3400 Van Buren	\$93,312	7,440	\$12.54
19	Revenue	3718 & 3722 Burlingame	\$58,194	6,600	\$8.82
20	Social & Rehabilitation Services	406 SE Jefferson	\$91,028	17,061	\$5.34
21	Social & Rehabilitation Services	6023 SW 27th	\$6,185	720	\$8.59
22	Social & Rehabilitation Services	3640 - 1 SW Topeka	\$142,579	8,200	\$17.39
23	Social & Rehabilitation Services	3640 SW Topeka	\$505,395	30,528	\$16.56
24	Social & Rehabilitation Services	2914 SW Plass Ct	\$8,701	768	\$11.33
25	Social & Rehabilitation Services	235 Kansas	\$647,817	68,300	\$9.48
26	Social & Rehabilitation Services	610 SW 10th	\$13,145	1,391	\$9.45
27	Social & Rehabilitation Services	610 SW 10th	\$42,725	4,294	\$9.95
28	Social & Rehabilitation Services	2348 SW Topeka	\$51,334	4,403	\$11.66
29	State Long-Term Care Ombudsman	610 SW 10th	\$10,159	1,021	\$9.95
30	University of Kansas	715 SW 10th	\$49,307	4,133	\$11.93
31	Wildlife & Parks	3300 SW 29th	\$24,615	3,304	\$7.45
<b>Outside Downtown core sub-total</b>			<b>\$4,054,724</b>	<b>362,622</b>	<b>\$11.18</b>
<b>Shawnee County Total</b>			<b>\$10,101,555</b>	<b>900,290</b>	<b>\$11.22</b>

## APPENDIX C

### Summary of Assumptions and Data Limitations Relevant to Legislative Post Audit's Analysis of Constructing a Second State Office Building and Acquiring the Mercantile Bank Building

#### **For the construction of a second State office building:**

##### Assumptions

1. The debt service schedule would be identical to the initial debt service schedule for the Signature building.
2. The costs of operating the new building would start at a rate of \$6.35 per square foot. This rate includes 75 cents per square foot for a maintenance reserve and \$5.60 per square foot for operational costs.
3. The average rental rate paid by State agencies in non-State owned space would be \$11.32 per square foot. For those agencies that moved into this building, the State would no longer have to make rental payments to the landlords for the space they formerly occupied.
4. All revenues and expenditures would grow by 2% each year.
5. In making our estimate of the long-term costs of constructing another new office building, we didn't subtract about \$9 million in land acquisition and site improvement costs associated with the 10<sup>th</sup> and Jackson site that wouldn't be incurred if a similar building was built on property the State already owns at 10<sup>th</sup> and Harrison. The reason we didn't is that we assumed these costs would be offset by two types of costs—more than \$6 million in change orders associated with the Signature Building and increases in the cost of construction that would likely occur because the building would be built several years after the Signature building.

#### **For the acquisition of the Mercantile Bank Building:**

##### Assumptions

1. All revenues earned by the building (from office space and garage rentals, and other income) would continue.
2. All office space not leased by the Mercantile Bank would be occupied by State agencies.
3. All revenues and expenditures would grow by 2% each year.
4. The rental rate would include 75 cents per square foot for a maintenance reserve.

##### Limitations

1. The revenue and expense information we used reflected amounts budgeted rather than actual amounts for calendar year 2000. Also, the revenue and expenditure information wasn't audited.

## **APPENDIX D**

### **Agency Response**

On February 14, we provided copies of the draft audit report to the Department of Administration. The Department's response is included as this appendix. After carefully reviewing the response, we made some minor clarifications to the draft audit that didn't affect any of our findings or conclusions.



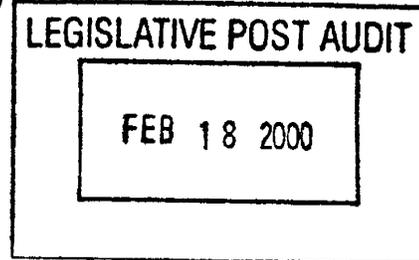
DEPARTMENT OF ADMINISTRATION

State Capitol  
Room 263-E  
Topeka, Kansas 66612-1572  
(785) 296-3011  
FAX (785) 296-2702

DAN STANLEY, *Secretary*

BILL GRAVES, *Governor*

February 18, 2000



Barbara J. Hinton  
Legislative Post Auditor  
800 SW Jackson St. Suite 1200  
Topeka, KS 66612-2212

Dear Ms. Hinton:

This will acknowledge receipt of your completed performance audit. In general, we concur with the recommendations of the Legislative Division of Post Audit. We do not find them to be out of line with the direction the Department of Administration is going. We have always attempted to present cost-benefit criteria to the Joint Committee on State Building Construction for structures we have proposed for purchase. We have chosen to look to the Joint Committee for the prioritization of projects and their deliberations are a matter of public record.

The Division of Post Audit detected flaws in our database, which have been collected this past year by 3 different individuals. We are grateful for the Division's assistance in setting this information right. We continue to seek to make our data more relevant and we have initiated the use of new forms to capture the component costs you have suggested.

We consider this endeavor and the recommendations of the Division of Post Audit to be very important and we appreciate the spirit in which this inquiry was conducted. We will use the recommendations to guide our future actions. We take some exception to a few of the conclusions drawn by your audit team and wish to offer our comments for the record as follows:

*"We found little documentation of the analyses performed on the proposals that had been submitted, or the rationale for the State's decisions regarding these 3 buildings. (SBG, Signature Building and Myriad)...Such documentation would provide a record of the State's decisions, provide justification for why decisions were made, and could be extremely useful in evaluating future proposals..."*

Barbara Hinton  
February 18, 2000  
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While it would have been nice if Deputy Director Barry Greis' notes were retained, and we agree with the recommendation that decisions should be more fully documented, there is no mystery as to what decisions led to the selection of Phase II and Phase III participants. Agency records and a phone survey of recollections of participants involved indicate that the agencies did a drive-by tour of all submitted proposals. Agencies came to the meeting with their own "short list" of favored locations. Only those projects that were considered suitable to at least one agency based on size, location and cost were invited to proceed to Phase II and III. The Joint Committee on State Building Construction made the ultimate decision between the Treanor Project, Signature Building and SBG Building in open session on Wednesday February 11, 1998, as discussed below.

*"The only documentation we found as to why that site (10<sup>th</sup> and Jackson) was chosen over the other revolved mainly around parking issues..."*

My testimony of February 11, 1998, described the findings of our Phase II analysis. I outlined the requirements by which the Signature Building and the Dunn/Treanor proposal were selected. A summary contrasting the two buildings was prepared by Thaine Hoffman, Director of Architectural Services, and presented by me on Wednesday, February 11, 1997, to the Joint Committee on State Building Construction. The decision to go forward with the Signature Building and to look into the purchase of the SBG Building was made by the Committee at that meeting.

*"Legislators have raised questions about whether centralized lease negotiations could help eliminate variations in lease rates currently paid by different agencies occupying space in the same building. In Shawnee County, 12 buildings house 2 or more State agencies. We reviewed information about leases in 3 of those buildings, and found significant variation in 2 of them...."*

The issue is not whether the rates vary. The issue is why the rates vary and whether there is an established base rate that is competitive with rates extended to other tenants within the building. There is sufficient data to establish that since 1997, master lease base rates were established for the state's largest leased buildings:

Mercantile Building	\$12.00
Jayhawk Tower	\$10.50
New England Building	\$ 9.50 (15 year rate)

These rates were established by using Benchmark full service lease rates such as \$12.00 per sq. ft. negotiated at 515 Kansas by the City of Topeka for Class A space (located just next door to the New England Building) and the lowest rates paid by any agency in the Jayhawk Towers and Mercantile Buildings.

On May 2, 1997, the Division of Facilities Management presented the attached worksheet to the Joint Committee on State Building Construction outlining their negotiations on behalf of the

Barbara Hinton  
February 18, 2000  
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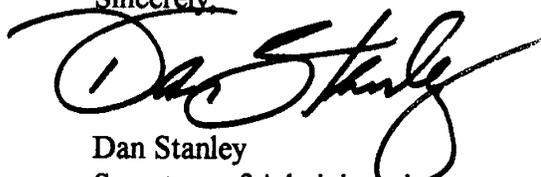
Attorney General's Office which reduced Jayhawk's proposed rate from over \$112,543 to \$100,307.64 in the first year and then established a lease rate of \$106,383 in the 2<sup>nd</sup> year (\$10.19 per sq. ft. including parking). This negotiated rate was well below the targeted base rate and well below comparable private sector rates.

The lease rates currently vary from those bases because the agencies in the Mercantile Bank and Jayhawk Tower are slated to move from those structures in the next 18 to 24 months and have not been allowed to negotiate longer leases. The base rate at the New England Building remains at \$9.55 for the 15-year duration of the lease. Adjustments were recently granted in order to accommodate the installation of additional security devices.

As the move from the Mercantile Building and Jayhawk Towers becomes imminent, the landlord has been able to override the base rates to receive compensation for improvements made with short term payback possibilities, higher than average tenant finish requirements, or for considerations made in allowing the agency to negotiate short term leases to accommodate departures from the building. These have been carefully considered. According to our sources, these rates are still around \$2.00 lower than similar leases negotiated by non-state agencies.

We appreciate the professionalism shown by your staff and thank you for the opportunity to provide these comments.

Sincerely,

A handwritten signature in black ink, appearing to read "Dan Stanley". The signature is fluid and cursive, with a large loop at the end.

Dan Stanley  
Secretary of Administration

Attachment

Dan Stanley  
 Jim Reardon  
 Art Griggs

February 9, 1998

Re: Comparison of proposed 10th street office buildings.

I have made what I think may be some "improvements". Please review and give me your comments. We need to go to press on this after lunch.

Thaine

<u>Jackson street bldg</u>	<u>Advantage</u>	<u>Harrison Street Building</u>
Cost to be paid through lease: \$38.5 million <sup>(1)</sup>	Harrison Bldg..	Cost to be paid through lease: \$36.1 million <sup>(1)</sup>
City provides site in exchange for Topeka State Hospital grounds.	Approx. equal	State provides site (value \$2.3 to \$11 million) <sup>(2)</sup>
Future development opportunities: Harrison Street lots still available.	Jackson Bldg..	Future development opportunities: Must condemn and clear area. City may not be willing to provide site at that time.
Office bldg floor area = 264,896 sf.	Approx. Equal	Office bldg floor area = 267,000 sf.
Additional parking spaces: 662 Not sufficient for Memorial Bldg..	Approx. Equal	Additional parking spaces: 701 No parking for Memorial Bldg..
Parking garage also available to Memorial building, making it more usable.	Jackson Bldg..	Parking garage not available to Memorial Building.
City will continue to own parking garage.	Harrison Bldg..	State will own parking garage after 2024. Cost to employees could be reduced
City will own and maintain parking garage.	Jackson Bldg..	State will own and need to maintain 25 year old parking garage.
Limited disruption during construction.	Jackson Bldg..	Lose 1000 parking spaces during construction.
Remove blighted area near capitol and across from Memorial Building.	Jackson Bldg..	Uses existing cleared land.
City will provide gateway improvements on Tenth Street.	Jackson Bldg..	No improvements beyond building site.

Notes:

(1) Both prices includes limestone exterior

(2) Small cleared sites sell for \$8 /sf. Purchase and clearing of Jackson Street site will cost \$38 /sf.

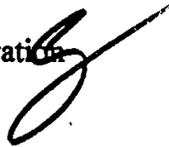


## DEPARTMENT OF ADMINISTRATION

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DAN STANLEY, *Secretary*BILL GRAVES, *Governor***MEMORANDUM**

**TO:** Joint Committee on State Building Construction

**FROM:** Dan Stanley, Secretary of Administration 

**DATE:** February 10, 1998

**RE:** Capitol Area Plaza Proposals

The State is very interested in proceeding to Phase III with the office building proposals on 10th Street. This could allow consolidation of offices in the Capitol Plaza area and provide parking for the Memorial Building. We have two potentially viable proposals on 10th Street, but neither proposal in their current form fully meets our needs.

Presently, the Eskie/Peters plan for 10th & Jackson offers inadequate parking for the Capitol Complex Area. The shortfall would be a least 200 spaces which are required for the occupants and visitors for Memorial Hall. Parking for the J.E. Dunn/Treanor plan at 10th & Harrison does not address the needs for Memorial Hall. Further, the physical separation of this location is not convenient to Memorial Hall even if additional parking is constructed. In keeping with our original concept and to be affordable, both proposals require City participation. The two proposers have suggested that the City, or its Public Building Commission, own the respective buildings and lease them to the State. I believe this concept offers the kind of approach we envisioned. We are seeking input and recommendations from the Joint Committee before we go forward. With the introduction of the Public Building Commission concept as the possible funding mechanism for these projects, I suggest the committee ask the City to become directly involved in the Phase III negotiations on these proposals or on the proposal the committee deems best suited for our needs. Further, I suggest that the committee invite the City to respond with the specifics defining the level and nature of City participation and modifications which meets the requirements stated in this memo.

1. The proposals must meet the requirements of RFP 32516 except for the provisions noted below.

2. The initial net lease rate, including land costs, must not exceed \$9.40 per square foot of rentable space (88% of gross space) with an allowable annual increase of 2%. Such rate must include the insurance costs. We estimate operating costs for which the State would be responsible would

be \$5.60 per square foot. Thus, the initial total annual costs would be in the \$15 per square foot range.

3. The office building must become the property of the State at the end of 30 years. Any garage built on City-owned land would remain property of the City.

4. Any parking garage constructed on State land must become the property of the State at the end of the lease term. The State would be willing to discuss parking and cost concessions with the City for the transfer of the current park located at 12th and Jackson to the State for use as additional parking. The City should consider closing of Harrison Street between 10th and 12th Streets so as to provide additional parking and green space in the Capitol Complex.

5. The City would be responsible for the operations and maintenance of any parking garages and be entitled to the parking revenues less any current State parking revenues lost by displacement of stalls by construction of a new building or garage. The State or state employees would be entitled to first preference for all parking garage stalls.

6. Any current parking stalls on State property lost to construction must be replaced in addition to other parking requirements. Acceptable temporary replacement parking provided during construction with fees continuing to the State. Alternate parking provisions during construction of the parking garage should be addressed. Also, a minimum of 200 parking spaces will be added to the Jackson Street proposal in addition to those required for the new building.

7. The State would lease the site for the Harrison building and garage to the City or Public Building Commission for \$1 for the term of the lease.

8. To complete the proposals, it will be necessary for the developer to meet with the individual agencies to determine their detailed requirements. In addition to their stated space requirements, a minimum of 10% additional rentable space must be provided for future needs. This space will initially house small state agencies. The number of stories or the footprint of the building may need to be adjusted to meet the space needs. The Director of Facilities Management, or his designee, should be invited to all meetings with the agencies.

9. The office building would preferably have a limestone exterior but we would consider precast panels that have the limestone appearance.

10. We would prefer additional parking in lieu of limestone exterior on the parking garage. It should be precast panels with the limestone appearance.

11. We prefer a double helix arrangement for parking garages. This is especially important at the Jackson Street location if this garage is only two bays wide and thus taller.

12. The plans and specifications for the office building(s), and any parking garage on State land would be subject to the approval of the Public Building Commission, Capitol Area Plaza Authority, and the State. The State will have access to the construction areas for inspection.

As you know, we have solicited and analyzed 28 proposals over the course of the past year. We appreciate the many thoughtful and exciting concepts that were brought to us for consideration. All of the developers, proposers, and stakeholders are to be commended for their vision and cooperation. In addition, we greatly appreciate the support and guidance the Joint Committee has provided us on this exciting project. It is now decision time. Therefore, I ask the committee's consideration of these remaining proposals and seek your guidance in how we should proceed. Specifically, you may wish to recommend that one or both of these proposals be forwarded to the City for final negotiation and a detailed response as outlined in this memorandum.