KANSAS
DEPARTMENT OF SOCIAL
AND REHABILITATION SERVICES

Don Jordan, Secretary

Joint Committee on State Building Construction
November 10, 2010

Office Space Management

Secretary Don Jordan

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Chairman Umbarger and members of the committee, thank you for the opportunity to discuss SRS' Overland Park lease and the topic of leasing or purchasing buildings. At your meeting in August, the Overland Park lease was presented to the committee. After initially approving the lease, the Committee reconsidered its action and asked for additional information. Specifically, the Committee requested a cost-benefit analysis comparing the lease cost with the cost to buy this particular building; the cost to purchase another building that would meet the agency's needs; and the cost for the agency to build a building to meet its needs. I am here today to ask you to approve the Overland Park lease.

Leasing vs. Purchasing State Office Space

Before discussing the specifics of the Overland Park lease, I want to offer a few observations from my own experiences in state government regarding leasing or purchasing. As you know, SRS does own and manage property at our state hospital campuses, and we take that responsibility seriously. Our state hospitals are 24/7 operations and ownership makes sense at those campuses because of the direct connection between the physical environment and patient care. The buildings are integral to the entire operation of the state hospitals, making it difficult to rely on leasing arrangements. One thing we do know from our experience at our state hospitals is that a significant amount of resources must be devoted to physical plant operations and a specific level of expertise must be developed. At our state hospitals, more than 18 percent of the operating budgets are comprised of funding associated with the physical plant. In addition to normal operating costs, we also know that repair, rehabilitation and renovation must be an ongoing focus to ensure the physical environments are maintained in a way that supports health, safety and quality of care. We are fortunate at the state hospitals to have a dedicated funding source for ongoing capital improvements, the State Institutions Building Fund, which is paid through a portion of state property tax mill levies. Even with this dedicated source of funding, it remains very difficult to keep up with the maintenance and rehabilitation needs. The state hospitals currently have over $16 million in outstanding maintenance, repair and major renovation projects.

While ownership of property is something we really must do at our state hospital campuses, we have pursued other avenues for our field operations. If the agency were to pursue ownership of our field office buildings, we would have to recreate the same type of operational capacity and expertise in our central office as well as in our larger field offices. This would include adequate staff resources with expertise in facilities operations to oversee maintenance staff and contracts for building repairs and services. It would also be essential to have an identified source of funding set aside for ongoing repair, rehabilitation and renovation.

Since the mid-to-late 1980s, SRS has committed to addressing our office space needs through lease arrangements. We have developed a strong expertise in lease procurement and management that allows the agency to secure specialized facilities expertise through our landlords. We believe our current arrangement of working with landlords to address physical structure and maintenance needs serves us and the state well. We manage our relationships with our landlords carefully and maintain a healthy partnership that leverages the strengths of both SRS and the landlords, and that is cost-effective for SRS and the state. The analysis that SRS secured regarding Overland Park lease options supports that this is a cost-effective approach.

Background on Overland Park Lease

The lease presented to the Committee at its August meeting provided for a 15 year lease beginning July 1, 2011 at a fixed rate of $9.96 per square foot, along with a five year renewal option at the same rate. The proposal selected is for the current office site and was the lowest total cost of all proposals, and a modest increase from the current base lease rate of $9.10. Other proposals submitted in response to the RFP ranged from $18.84 to $21.23 per square foot.

As discussed at your August meeting, the lease is also a good value for the organization because of the improvements the landlord has agreed to make. The proposed rate includes the construction of 14 enclosed interview rooms and relocation and remodeling of the reception and waiting room. It also includes the construction of 20 enclosed supervisor offices and restroom remodeling. Also, data and phone wiring will be upgraded and an HVAC unit will be installed in the telecommunications room. The proposed lease also includes significant energy improvements to increase the energy rating of the building. These include: reroofing the existing facility and upgrade of the roof insulation to R28 value; replacement of all exterior facility windows with energy efficient double pane low-E glass; replacement and installation of new electronic light ballasts and T-8 lams for all light fixtures; and the installation of night setbacks for HVAC units. To ensure the energy improvements are resulting in increased efficiency, the Department of Administration will request a new energy audit in 2012. These energy improvements and the previously stated building improvements total $965,000 and were negotiated into the base lease rate amount.

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Committee Request for Additional Information

SRS contracted with Jones Lang LaSalle to prepare a cost benefit analysis identifying the cost to purchase and renovate another building that would meet the agency's needs and the cost for the agency to purchase land and build a building to meet its needs. The cost to purchase the specific building in the lease was not included, because the landlord has no interest in selling the building. The full report is included as an attachment to this testimony. The analysis spans a period of thirty years and studies the market and factors in typical construction costs and building operational costs. In comparison, the cost to execute the lease proposed by the current lessor will cost on average $13.30 per square foot; while the cost to purchase an existing building and renovate is estimated to cost between $18.14 and $18.39 per square foot and the cost to purchase land and construct a building is estimated to be $20.72 per square foot.

Proposed 15 Year Lease		**30 Year Cost Analysis Comparisons**			
		Current Building	Purchase-Renovate	Purchase-Renovate	Purchase-New Build
Annual Cost per Sq Ft.	$12.07	$13.30	$18.14	$18.39	$20.72
Annual Cost	$608,629.75	$670,652.50	$851,310.20	$1,048,910.43	$1,044,806
Total Cost	$9,129,446	$20,119,575	$25,539,306	$31,467,312.90	$31,344,180

Based on the committee's request the analysis concluded the cost to purchase an existing building and renovate or to purchase land and build a building would not be cost-effective and would not allow SRS to financially break even over the thirty year period compared to the lease that was presented to this Committee in August. I would respectfully request that the committee approve the Overland Park lease. The lease will meet the needs of the agency for many years and is a good value for the state. Thank you.