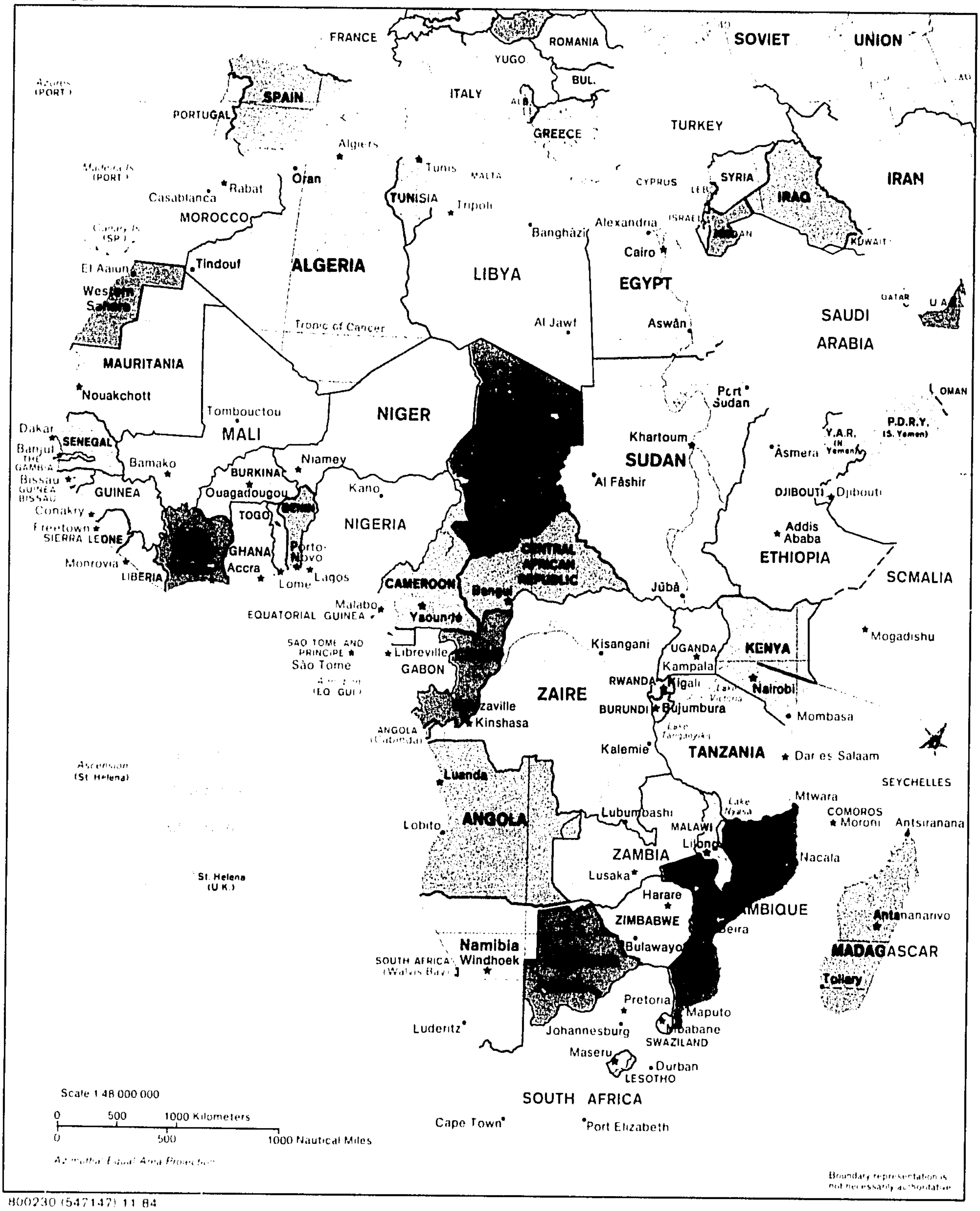
PDAAZ-463

ISN 61873

AUDIT OF
A.I.D. MANAGEMENT OF OWNED
AND LEASED PROPERTY IN KENYA

AUDIT REPORT NO. 3-615-89-14
July 12, 1989

Africa



800230 (547147) 11-84

UNITED STATES OF AMERICA
AGENCY FOR INTERNATIONAL DEVELOPMENT
REGIONAL INSPECTOR GENERAL/AUDIT

UNITED STATES POSTAL ADDRESS
BOX 232
APO N.Y. 09675

INTERNATIONAL POSTAL ADDRESS
POST OFFICE BOX 30261
NAIROBI, KENYA

July 12, 1989

MEMORANDUM FOR DIRECTOR, USAID/Kenya, Steven W. Sinding

Richard C. Thabet

FROM: RIG/A/Nairobi, Richard C. Thabet

SUBJECT: Audit of A.I.D. Management of Owned and Leased Property in Kenya

The Office of the Regional Inspector General for Audit, Nairobi has completed its audit of A.I.D. management of owned and leased property in Kenya. Five copies of the audit report are enclosed for your action.

The draft audit report was submitted to you for comment and your comments are attached to the report. The report contains one recommendation which is resolved but will not be closed until completion of planned or promised actions. Please advise me within 30 days of any actions taken to implement the recommendation.

I appreciate the cooperation and courtesy extended to my staff during the audit.

Background

The Foreign Affairs Manual (FAM) Volume 6, Sections 720 and 731 set forth the Uniform Department of State/A.I.D./United States Information Agency regulations for leasing residential quarters and acquiring real property abroad. The manual stated that A.I.D. had authority under section 636(a) of the Foreign Assistance Act of 1961, as amended, to lease offices, buildings, grounds and living quarters for up to ten years. Missions were delegated authority to enter into leases not exceeding $25,000 a year or 5 years in duration. Leases exceeding these limits had to be submitted to Management Operations/Overseas Operations, AID/W for prior approval. Section 636(c) of this Act, authorized A.I.D. to spend up to $6 million annually to renovate, construct or purchase real property facilities. However, A.I.D. missions had to compete for 636(c) funds and these were controlled by AID/W. Further, the regulations authorized A.I.D. missions to acquire property, with AID/W concurrence, through lease purchase options.

On September 30, 1988, USAID/Kenya had (a) 71 residential leases at a yearly total rental cost of $902,031; (b) 11 office leases at a yearly rental cost of $372,594; and (c) a warehouse subleased from the Embassy at a cost of $23,127 per year. Four of the residential leases were under lease/purchase agreements. Also, the Mission was negotiating for the lease/purchase of 17 more residential housing units. Real property was managed by USAID/Kenya's Executive Office.

Audit Objectives and Scope

The staff of the Regional Inspector General for Audit/Nairobi conducted an audit of A.I.D. management of owned and leased property in Kenya. The objectives of the audit were to determine whether (a) leased/owned properties were appropriate for A.I.D.'s needs and (b) the alternative used (leasing or acquisition) was the best for acquiring the required space.

The audit was made at USAID/Kenya during January to March 1989. The audit staff reviewed relevant documents and interviewed Mission officials. The audit scope included $1,274,625 used in fiscal year 1988 for the rental of the Mission's 71 leased residences and 11 offices. Thirty three leases which amounted to $531,600 in rental costs in fiscal year 1988 ($429,267 for 27 residential leases and $102,333 for 6 office leases) were tested. The reviews of internal controls and compliance were limited to the finding presented in this report. The audit was made in accordance with generally accepted government auditing standards.

Results of Audit

The audit found that USAID/Kenya's leased/owned property did not exceed its needs in terms of quantity. However, there was no assurance that leasing was the best alternative for acquiring residential housing.

USAID/Kenya did an excellent job in managing leased properties by achieving high occupancy rates. For the 71 houses that USAID/Kenya leased, the occupancy rates for 1986, 1987 and 1988 were about 90 percent. Thus, USAID/Kenya's leased properties were appropriate for its needs.

However, Mission attempts to acquire properties in Kenya rather than to lease them were not successful. The report recommends that USAID/Kenya prepare a cost analysis to support a request for acquiring additional housing.

1. USAID/Kenya Could Save On Operating Expense Funds By Acquiring Residential Housing - Although A.I.D. has authority to renovate, construct or purchase real properties abroad, USAID/Kenya has not purchased any residential housing. The Mission attempted to acquire housing but their requests for funds were not successful. USAID/Kenya could save about $11.3 million over a 15-year period by acquiring a third of their housing requirements.

Discussion - Section 636(c) of the Foreign Assistance Act of 1961, as amended, gave A.I.D. the authority to spend up to $6 million annually to renovate, construct or purchase real property facilities abroad. Each proposed acquisition or construction was to include a comparison of acquisition/construction costs against the estimated leasing costs for a 15-year period. As an alternative, A.I.D. missions had the authority, with AID/W review and concurrence and the availability of funds, to acquire property through lease purchase options. A portion of the funds for exercising an A.I.D. purchase option would be provided from operating expense funds designated as section 636(c) funds and the balance would come from ordinary operating expense funds. When a Mission desired to exercise an approved purchase option, it had to notify AID/W at least 6 months in advance. Further, a factor in AID/W apportionment of 636(c) funds for fiscal year 1989 was that A.I.D.-owned Mission property did not exceed 33 percent of staff needs.

At September 30, 1988, USAID/Kenya had four leases with purchase options but did not own any residential housing. The Mission was leasing 71 units to house its own staff and other A.I.D. regional personnel. During the period fiscal year 1983 through fiscal year 1988, the Mission paid over $4.6 million in leasing costs. In contrast to A.I.D., foreign embassies in Nairobi owned substantial quantities of their housing requirements. For example:

-- the British Embassy owned 69 percent of their 58 houses,

-- the Canadian Embassy owned 40 percent of their 20 houses; and

-- the Australian Embassy owned 27 percent of their 15 houses.

Prior to 1980, the Mission made three formal 636(c) funding requests as follows:

-- On March 23, 1979, the Mission submitted a 636(c) funding request for $214,765 to purchase the Director's residence. The request was approved on May 23, 1979 by AA/SER with A/FBO concurrence. However, the prospective seller later asked for more money than had been requested/authorized. Consequently, the house was not purchased.

-- On September 10, 1979, the Mission submitted another 636(c) funding request for $1.25 million to acquire 9 lots, 5 houses, and construct the Director's residence. AID/W rejected that proposal because of lack of funds and other Africa Bureau real estate requirements which had precedence over the Mission's proposal.

-- On January 21, 1980, the Mission, on Africa Bureau's advice, submitted to AID/W a third 636(c) funding request for $243,243 to acquire the Director's residence. However, a later Mission inspection of the residence concluded it did not meet the basic representational requirements and the request was withdrawn.

Since 1980, no formal cost analyses have been prepared to justify the need to acquire residential housing in Nairobi. AID/W has discouraged the Mission's efforts to prepare such analyses by stating in their annual plans for 636(c) requirements that funds would not be available.

If an analysis had been prepared at the time of our review, it would have shown that rental property in Kenya was at a premium and that rental rates were escalating. For example, the average lease in the audit sample increased by about 54 percent during 1988. The increases were expected to be even higher in 1989, ranging from 25 to 117 per cent.

The analysis would also have shown that the U.S. dollar enjoyed a favorable exchange rate with the local currency. The local currency had been devalued to only 40 per cent of its 1980 value compared to December 1988. Therefore, acquisition costs in Kenya were lower than in other countries where the value of the U.S. dollar had declined.

Based on (a) USAID/Kenya's and three local real estate agents' current estimates of $183,784 for purchasing a standard sized four bedroom executive house, (b) $19,460 in annual rent payments, and (c) a continuous 10.7 percent annual inflation rate in leasing costs (rate obtained from an Economist with the Regional Economic Development Services Organization for East and Southern Africa), A.I.D. would recoup its outlay for purchase costs (from no rental payments) in seven years. Over a 15-year period, A.I.D. would save about $469,898 per unit less increased maintenance costs and the Federal Government's cost of money required for the construction outlay or lease purchase options.[1/] If only a third of the units (say 24) were purchased, the savings would be about $11.3 million in the 15-year period. See Exhibit 1.

In conclusion, it was advantageous to the U.S. Government to acquire residential housing in Kenya. A comprehensive cost analysis will assist USAID/Kenya to demonstrate to AID/W that the U.S. Government could save millions of dollars by acquiring real property in Kenya.

Recommendation No. 1

We recommend that the Director, USAID/Kenya prepare a cost analysis to support a request to:

(a) obtain section 636(c) funds to purchase residential housing; or

(b) enter into additional lease/purchase agreements.

In responding to the Record of Audit Finding (RAF), USAID/Kenya officials agreed with the finding and recommendation. However, they stated that the problem was with the 636(c) program itself and that the report recommendation should have been directed to AID/W. The Inspector General's Office may issue a world-wide recommendation to AID/W, in the future, but we consider the recommendation to the Mission necessary so that they can make use of any unexpected 636(c) funds.

In responding to the draft report, management officials stated that they supported the audit conclusion that it was advantageous to the U.S. Government to acquire residential housing. They further stated that they would forward to M/SER/MS a cost analysis justifying acquiring residential

---

1/ The audit did not perform computations of increased maintenance costs and the Federal Government's cost of money required for the purchase outlay. Increased maintenance costs would include only structural maintenance such as roof repairs, since lease practices in Kenya require the tenant to pay for day-to-day maintenance. Further, the Federal Government's cost of money would be less under a lease purchase option as compared to an immediate purchase. These computations should be included in the cost analysis called for by this report recommendation. Also, to be included in this cost analysis would be investment risk factors such as political instability.

housing in Kenya along with a recommendation that a high priority be given to revamping and expanding the housing acquisition program of the Agency. The officials pointed out that fundamental problems with the 636(c) program were strong disincentives to the preparation and submission of real property acquisition proposals. The problems cited by these officials included; (1) low priority, hence little or no funding, (2) a low ceiling of $6 million for world-wide acquisition of residences and office buildings, and (3) short deadlines for end of year, use-or-lose funding for sometimes complicated projects. They also stated that AID/W in their ABS instructions had given the impression that there would probably be no 636(c) money for at least two years. In addition, they stated that a new AID/W directive that lease purchase contracts should have prior OMB approval and be included in the Mission's ABS further dimmed the prospects for future real property acquisition.

We applaud the Mission's past attempts to acquire residential housing and their plans to prepare and forward to M/SER/MS the recommended cost analysis together with a recommendation to AID/W that high priority be given to revamping and expanding the 636(c) program. The new OMB requirements, in fact, require the type of analysis recommended by this report before approval for real property acquisition can be considered. It is our hope that the recommended cost analysis together with the Mission's recommendation will demonstrate to AID/W that there is an opportunity to save on operating expense funds by acquiring residential housing in Kenya.

Based on the Mission's comments, and planned actions we consider recommendation No. 1 resolved. The recommendation will be closed when the recommended cost analysis is prepared and forwarded to M/SER/MS.

<u>Other Pertinent Matters</u>

1. A.I.D. missions had the authority, with AID/W review and concurrence and the availability of funds, to acquire property through lease purchase options. These options establish firm fixed prices for the houses to be paid annually by A.I.D. to the seller at a certain rate over a specified period of time. Consequently, in December 1987 USAID/Kenya entered into lease purchase agreements to purchase four houses at an average cost of about $83,000. This price was less than half the current market value of about $184,000. The options to purchase these four houses would expire on March 30, 1994 and involve final payments of 10 Kenya Shillings ($0.50) which would come from Section 636(c) funds. USAID/Kenya did not plan to exercise these options prior to that date. However, if USAID/Kenya were able to obtain about $65,000 (the current balance necessary to purchase each house) in Section 636(c) and other operating expense funds before November 30, 1989, they could save about

$27,500 per house in future rental payments (or about 58 percent of the rental costs) over the remaining period of lease purchase agreements. Potential savings from early exercising of all four lease purchase options would be about $110,000. We therefore suggest that USAID/Kenya utilize any unexpected surplus of Mission operating expense funds and/or query AID/W regarding the possibility of obtaining additional operating expense funds to exercise one or more of the options under its lease purchase agreements.

In responding to this matter, USAID/Kenya officials stated that they would submit an acquisition request during fiscal year 1990 should the climate for 636(c) purchases be favorable.

2. Under Foreign Building Office (FBO) housing guidelines, USAID/Kenya was classified as a No.2 locality for housing. This entitled occupants to 1320 square feet of living area for two-bedroom, 1580 square feet for three-bedroom, 2100 square feet for four-bedroom and 2360 square feet for five-bedroom units. USAID/Kenya Mission Order No. 5-3 established the policy, criteria and conditions governing the assignment of quarters for U.S. direct-hire and other employees assigned to regional components of A.I.D. located in Kenya. Basically, the Mission Order allowed one bedroom for the employee and each dependent.

Except for three-bedroom houses which averaged about 1675 square feet, USAID/Kenya was within the FBO size limitations. However, because of the family make-up of employees, the Mission's portfolio of housing cumulatively exceeded the criteria for numbers of bedrooms established under the Mission Order. For example, singles and married couples without children were often living in three and four bedroom units. Mission officials stated that due in large part to the existing rental housing environment in Kenya, there was a shortage of one and two-bedroom houses that would meet A.I.D. standards to house singles or married couples without children. At the time of audit, USAID/Kenya had only one two-bedroom residence under lease. They also mentioned that it was difficult to know from year to year their exact requirements because family sizes changed periodically. USAID/Kenya could possibly save operating expenses funds by leasing units with fewer bedrooms which in turn would also reduce furnishings and utility costs. The Mission was conscious of the goal to acquire a housing portfolio consistent with good business practices and projected mission housing requirements which would conform to FBO and Mission guidelines. We, therefore, suggest that USAID/Kenya lease smaller housing units whenever possible.

In their response to this matter, the Mission indicated that they would continue to look for good quality smaller units with reasonable rental rates.

AUDIT OF
A.I.D. MANAGEMENT OF OWNED AND LEASED
PROPERTY IN KENYA

EXHIBITS AND APPENDICES

. 4'

Analysis Showing It Is Advantageous To The U.S. Government To Acquire Residential Housing in Kenya

Year	Yearly Rental Increase Compounded @ 10.7 Percent Annually (US Dollars)	Cumulative Rental Payments (US Dollars)
1	$ 19,460	$ 19,460
2	21,542	41,002
3	23,847	64,849
4	26,399	91,248
5	29,224	120,472
6	32,350	152,822
7	35,812	188,634 a/
8	39,644	228,278
9	43,886	272,164
10	48,582	320,746
11	53,780	374,526
12	59,534	434,060
13	65,904	499,964
14	72,956	572,920
15	80,762	653,682 b/

---

a/ Based on an estimated $ 183,784 cost of purchasing a four bedroom house, the breakeven point would occur during year 7.

b/ Over a 15-year period, the Mission would save $ 469,898 ($ 653,682 - 183,784) per unit.

c/ See footnote in the Discussion section of the report for additional assumptions used in the analysis.

UNITED STATES GOVERNMENT

memorandum

DATE: May 24, 1989

REPLY TO ATTN OF: Steven W. Sinding, Director, USAID/K

SUBJECT: Audit of A.I.D. Management of Owned and Leased Property in Kenya

TO: Richard C. Thabet, RIG/A/Nairobi

We have reviewed the subject draft audit report and offer the following comments in response:

Recommendation no. 1: USAID/Kenya strongly endorses the audit report contention that it would be financially advantageous to the U.S. Government if some, or all, of our residential housing units were purchased instead of leased. Indeed, virtually every Mission in the world would agree. As noted in our comments to the previous Record of Audit Finding, however, we believe fundamental problems with the real property acquisition program are strong disincentives to the preparation and submission of time-consuming 636(c) proposals. These problems include the fact that the program has: (1) low priority, hence little or no funding, (2) a low ceiling of $6 million per year for worldwide acquisition of residences and office buildings, and (3) short deadlines for end of year, use-or-lose funding for sometimes complicated projects.

I am attaching two directives we recently received from AID/W which further dim the prospects for any real property acquisition in the foreseeable future. As you know, there has been a virtual worldwide freeze on 636(C) purchases in FY 1989. Attachment A is taken from our current ABS instructions and advises that there will probably be no 636(C) money for at least the next two fiscal years. Attachment B states that any lease/purchase contracts now must have prior OMB approval and must be included in the Mission's ABS. Such projects must meet very tough seven year payback criteria and even then, there is no assurance that they will be approved. The practical effect of these changed procedures will be a drastic reduction in lease/purchase opportunities.

Nevertheless, we concur with the auditor's analysis of potential cost savings for purchased versus rented residential units. This analysis will be forwarded to M/SER/MS along with our recommendation that a high priority be given to revamping and expanding the housing acquisition program for the Agency.

Deleted - Relates to Matter Not
Included in Final Report

Deleted - Relates to Matter Not
Included in Final Report

ATTACHMENT A

The FY 1989 and FY 1990 dollar mission allowance funding levels shown in your Table VIII MUST reflect the funding level allocated by your bureau, including any limitations imposed such as for Official Residence Expenses, Representation Allowances, and dollar funded 636(c) purchase/construction. ANY BUDGET RECEIVED REFLECTING A FUNDING LEVEL IN EXCESS OF THAT AUTHORIZED BY THE BUREAU WILL BE RETURNED FOR RESUBMISSION.

You are authorized to include operating expense funds for 636(c) purchase and/or construction activities ONLY if you have received specific authority in an Advice of Budget Allowance for such activities for FY 1989. No 636(c) activities are to be included in your FY 1990 or FY 1991 budget estimates, nor should you plan on obtaining appropriated funds in FY 1990 or 1991 for these purposes.

Your budget must include all mission financial resources required to operate the mission, whether funded from dollar mission allowances or trust funds.

The overseas Workforce and Operating Expenses section of the FY 1991 ABS consists of:

-- Table VIII, Detailed Budget Tables;
-- Table VIII(a), Narrative;
-- Table VIII(b), Information on U.S. and F.N. PSC Costs;
-- Table VIII(c), Manpower Contract Detail;
-- Table VIII(d), Contractual Services/Special Studies/All Other Code 25 Detail;
-- Table VIII(e), ADP Hardware Purchases;
-- Table VIII(f), Mission Human Resource Table;

All overseas organizations must provide, at a minimum, the information required by the above tables. Individual bureau Controllers and/or EMS offices may require supplemental information.

In addition to the normal ABS distribution, one copy of each of the following tables must be sent directly to PFM/FM/BUD, Room 801, SA-2:

1) All Workforce and O.E. Tables listed above
2) Table I, Long Range Plan by Appropriation
3) FAAS-1, Post Administrative Support Agreement
4) Trust Fund Agreement

RIG and RHUDO budgets - While mission controllers are encouraged to assist RIG and RHUDO personnel in the preparation of their budget submissions, final decisions regarding these budgets are to be made by appropriate RIG and/or RHUDO personnel.

INSTRUCTIONS FOR PREPARING DETAILED BUDGET TABLES:

There are several changes to the basic Table VIII for the FY 1991 ABS:

ATTACHMENT B

EXO

OFFICIAL FILE

UNCLASSIFIED STATE 145715

GRS-6

ACTION: AID 5

VZCZCNAO366 13-MAY-89 TOR: 04:12
RR RUEHNR CN: 18059
DE RUEHC #5715 1292016 CHRG: AID
ZNR UUUUU ZZH DIST: AA
R 092016Z MAY 89 ZEX ADD:
FM SECSTATE WASHDC
TO AID WORLDWIDE
BT
UNCLAS STATE 145715

RECEIVED
10 MAY 1989
EXO
USAID/KENYA

ADM AID

ACTION COPY
Action taken:
No action necessary

E.O. 12356: N/A
TAGS:
SUBJECT: LEASE/PURCHASE PLANNING

REF: STATE 234294

PARAGRAPH 6 OF REFTEL COVERS LEASE PURCHASE OPTIONS AND A NEW REQUIREMENT THAT THE OFFICE OF MANAGEMENT AND BUDGET (OMB) APPROVE SUCH ARRANGEMENTS FROM THE OUTSET.

M/SER/MS, PFM/FM AND GC REVIEWED THE REQUIREMENT ON ENTERING INTO LEASE PURCHASE ARRANGEMENTS, AND HAVE INTERIM GUIDANCE FOR MISSIONS PENDING ANY FURTHER CHANGES/INTERPRETATION IN THIS POLICY. AID/W CANNOT APPROVE NEW LEASE/PURCHASE ARRANGEMENTS, EVEN ON A CASE-BY-CASE BASIS UNLESS THE SPECIFIC LEASE/PURCHASE HAS BEEN AUTHORIZED TO BY OMB DURING THE BUDGET PROCESS. ACCORDINGLY, ALL NEW LEASE PURCHASE REQUESTS MUST BE INCLUDED IN THE ANNUAL BUDGET SUBMISSION (ABS) EFFECTIVE IMMEDIATELY WITH THE FY 1991 ABS CURRENTLY UNDER PREPARATION IN OVERSEAS MISSIONS. THIS OMB REQUIREMENT ACTUALLY WENT INTO EFFECT IN OCTOBER, 1988 WITH THE SUBMISSION OF THE FY 1990 AGENCY BUDGET, RATHER THAN WITH THE FY 1991 BUDGET. HOWEVER, USAIDS HAD ALREADY SUBMITTED THEIR FY 1990 ABS'S PRIOR TO THIS NEW REQUIREMENT. M/SER/MS RECOGNIZES HOW DIFFICULT IT WILL BE FOR MISSIONS TO MAKE DEFINITIVE COMMITMENTS ON STARTING DATES FOR SUCH ARRANGEMENTS. IN ADDITION, A CLEAR ADVANTAGE TO THE U.S. GOVERNMENT (I.E., THE 7 YEAR PAYBACK LEASE VERSUS BUY ANALYSIS) MUST EXIST BEFORE APPROVAL WILL BE CONSIDERED FOR ANY MISSIONS ENTERING INTO A LEASE PURCHASE ARRANGEMENT. HOWEVER, USAID MISSIONS SHOULD NOT ASSUME THAT A 7 YEAR PAYBACK, OR EVEN A SHORTER PAYBACK, WILL AUTOMATICALLY RESULT IN OMB APPROVAL. FINALLY, MISSIONS HAVING POTENTIAL LEASE/PURCHASE PLANS MUST PROVIDE JUSTIFICATIONS AS TO THE BENEFITS OF LEASE/PURCHASE VERSUS OUTRIGHT PURCHASE.

PLEASE CONTACT M/SER/MS IF FURTHER INFORMATION OR ASSISTANCE IS NEEDED. EAGLEBURGER

DATE REC'D	5-10
REPLY DUE	5-16
ACTION TO	EXO
	INFO
DIR	
D/DIR	
RRDFO	2
RHUDO	
RIG/A	
RIG/I	
RFMC	
PROG	
HRD	
PRJ	
PH	
AGR	
EXO	
FHR	
GSO	
RF	
REDSO	
GEN	
RIES	
RMO	
	13

APPENDIX 2

REPORT DISTRIBUTION

American Ambassador to Kenya	1
Director, USAID/Kenya	5
AA/AFR	1
AFR/EA/KUTRB	1
AFR/CONT	1
AA/XA	2
XA/PR	1
LEG	1
GC	1
AA/M	2
AA/PFM	1
PPC/CDIE	3
M/SER/MO	1
M/SER/EOMS	1
M/AAA/SER	1
RFMC/Nairobi	1
REDSO/ESA	1
IG	1
DIG	1
IG/PPO	2
IG/LC	1
IG/ADM/C&R	12
AIG/I	1
RIG/I/N	1
IG/PSA	1
RIG/A/C	1
RIG/A/D	1
RIG/A/M	1
RIG/A/S	1
RIG/A/T	1
RIG/A/W	1