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March 2018

MILITARY HOUSING PRIVATIZATION

DOD Should Take Steps to Improve Monitoring, Reporting, and Risk Assessment

Accessible Version

GAO-18-218

GAO Highlights

Highlights of GAO-18-218, a report to congressional committees

March 2018

MILITARY HOUSING PRIVATIZATION

DOD Should Take Steps to Improve Monitoring, Reporting, and Risk Assessment

Why GAO Did This Study

In 1996 Congress provided DOD with authorities enabling it to obtain private-sector financing and management to repair, renovate, construct, and operate military housing. DOD has since privatized 99 percent of its domestic housing.

The Senate Report accompanying a bill for the National Defense Authorization Act for 2017 included a provision that GAO review privatized military housing projects and the effect of recent changes in the basic allowance for housing on long-term project sustainability. This report examines the extent to which DOD has (1) assessed and reported the financial condition of each privatized housing project; (2) assessed the effects of recent reductions in the basic allowance for housing on privatized housing; and (3) defined notification requirements for project changes and risk tolerances relative to privatized housing goals. GAO reviewed policies, project oversight reports, and financial statements, and interviewed DOD officials and privatized housing developers.

What GAO Recommends

GAO is making eight recommendations, including that DOD improve the consistency and timeliness of the information reported on the financial condition of its privatized housing projects, fully assess the effects of the reductions in basic allowance for housing on the projects, clarify when project changes require notice, and define tolerances for project risks. DOD concurred with each of our recommendations and identified actions it plans to take to implement them.

View GAO-18-218. For more information, contact Brian J. Lepore at (202) 512-4523 or leporeb@gao.gov.

What GAO Found

The Department of Defense (DOD) has regularly assessed the financial condition of its privatized housing projects; however, it has not used consistent measures or consistently assessed future sustainment (that is, the ability to maintain the housing in good condition), or issued required reports to Congress in a timely manner. Specifically:

- Some data used to report on privatized housing across the military services are not comparable. For example, there are inconsistencies among the projects in the measurements of current financial condition (for example, the ability to pay debts and maintain quality housing).These differences have not been identified in reports to Congress.
- The military departments vary in the extent to which they use measures of future sustainment, and information regarding the sustainment of each of the privatized housing projects has not been included in the reports to Congress.
- DOD's reporting to Congress has not been timely. DOD is statutorily required to report to Congress the financial condition of privatized housing projects on a semiannual basis, but it has not reported on any fiscal year since 2014.

By taking steps to improve the consistency of the information provided and meet the reporting requirement, DOD would provide decision makers in Congress with useful, timely information about the financial condition of the privatized housing projects as they provide required oversight.

DOD has not fully assessed the effects of reductions, relative to calculations of market rates for rent and utilities, in servicemembers' basic allowance for housing payments on the financial condition of its privatized housing projects. In August 2015, DOD required the military departments to review their privatized housing portfolios and outline any effects of the reductions. Each military department reported that the reductions would decrease cash flows to their long-term sustainment accounts. However, the reports did not specify the significance of the reductions on each project's future sustainment or identify specific actions to respond to shortfalls at individual projects. If DOD fully assesses the effects of the basic allowance for housing reductions on privatized housing and identifies actions to respond to any risks, DOD and Congress will be better informed to make decisions affecting the projects.

DOD has not defined when project changes require prior notice to the Assistant Secretary of Defense for Energy, Installations, and Environment or its tolerance for risk relative to its goal of providing servicemembers with quality housing, including the risk from reduced sustainment funding. Specifically, the military departments had different understandings of when project changes, such as financial restructurings, required prior notice. Additionally, DOD has not required the military departments to define their risk tolerances—the acceptable level of variation in performance relative to the objectives—regarding the future sustainability of the projects. By clearly defining the conditions that require advance notification and developing risk tolerance levels, DOD would have consistent information that would improve its oversight of privatized housing and inform its response to any future sustainment challenges.

Contents

Abbreviations

ASD (EI&E)	Office of the Assistant Secretary of Defense for Energy, Installations, and Environment
DOD	Department of Defense

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March 13, 2018

The Honorable John McCain
Chairman
The Honorable Jack Reed
Ranking Member
Committee on Armed Services
United States Senate

The Honorable Mac Thornberry
Chairman
The Honorable Adam Smith
Ranking Member
Committee on Armed Services
House of Representatives

In the mid-1990s, the Department of Defense (DOD) had designated nearly two-thirds of its domestic family housing inventory as needing repair or complete replacement. At the time, DOD estimated that it would need about $20 billion in appropriated funds and up to 40 years to eliminate the poor quality housing through new construction or renovation using the traditional military construction approach.[1] DOD became concerned that the poor quality of its housing was having a negative effect on servicemembers' quality of life and detracting from readiness by contributing to servicemembers' decisions to leave the military. To enable DOD to privatize its housing, Congress provided the department with a variety of authorities to obtain private-sector financing and management to repair, renovate, construct, and operate military housing.[2] In more than a decade since, the military departments have worked with private-sector developers who have rebuilt and renovated the housing. These developers now operate 99 percent of domestic military family housing, as well as a limited amount of housing for unaccompanied military personnel. The developers rely on servicemembers' basic allowance for

[1]GAO, *Military Housing Privatization: DOD Faces New Challenges Due to Significant Growth at Some Installations and Recent Turmoil in the Financial Markets*, GAO-09-352 (Washington, D.C.: May 15, 2009).

[2]See the National Defense Authorization Act for Fiscal Year 1996, Pub. L. No. 104-106, §§ 2801-2802 (1996), codified as amended at 10 U.S.C. §§ 2871-2885.

housing payments as a key revenue source for this privatized housing, but DOD began reducing these payments in 2015.[3]

Since 1998, we have conducted various reviews related to military housing privatization and the basic allowance for housing. In 2009, we reported, among other things, that some privatization projects with occupancy rates below 90 percent were challenged in generating enough revenue to fund construction, make debt payments, and set aside funds for future major renovations and rebuilds.[4] We also stated that turmoil in the financial markets had reduced available construction funds, resulting in more renovations relative to new construction and reduced amenities at some projects. We recommended, among other things, that DOD include information in its reports to Congress on the effects that current financial market conditions have on housing projects. DOD agreed with our recommendations, and in its February 2010 semiannual status report to Congress included more detailed information on the financial performance of ongoing projects. In 2011, we reported that DOD uses a data-intensive process to set housing allowance rates, but that enhancements related to data collection and definitions for data collection, as well as cost estimating for budget estimates, could enhance the process.[5] We recommended, among other things, that DOD assess the benefits and drawbacks of revising its definition of "available" housing for data collection purposes, and that it develop a communications process for installations to share information on housing tools. DOD generally concurred with our recommendations and took steps to implement them. In 2014, we reported, among other things, that the military services conducted several analyses and considered several other factors to determine whether to privatize housing for

[3]Beginning in 2015, DOD began reducing the basic allowance for housing payments relative to the Defense Travel Management Office's calculations of market rate rents and utilities. According to Defense Travel Management Office officials, basic allowance for housing payments are not necessarily decreasing from year to year. Instead, the average basic allowance for housing payment across the geographic areas has risen due to increases in market rate calculations, even as basic allowance for housing payments have been reduced relative to these calculations. However, throughout this report we refer to reductions in basic allowance for housing payments since the payments are being reduced relative to the market rate calculations.

[4]GAO-09-352.

[5]GAO, *Military Housing: Enhancements Needed to Housing Allowance Process and Information Sharing Among Services,* GAO-11-462 (Washington, D.C.: May 16, 2011).

unaccompanied personnel.[6] The Army and Navy concluded that privatization could be used under a narrow set of circumstances at specific installations, and the Air Force and Marine Corps concluded that privatization was not suitable for meeting any of their unaccompanied housing needs. We did not make any recommendations in that report.

The Senate Armed Services Committee report accompanying a bill for the National Defense Authorization Act for Fiscal Year 2017 included a provision for us to review privatized military housing projects and the effect of recent changes in servicemembers' basic allowance for housing on the long-term sustainability of the projects.[7] In this report, we examine the extent to which DOD has (1) assessed and reported the financial condition of each privatized housing project; (2) assessed the effects of recent reductions in the basic allowance for housing on privatized housing, and identified any other challenges and options to address those challenges; and (3) defined notification requirements for project changes and risk tolerances relative to privatized housing goals.

For objective one, we reviewed DOD guidance on the oversight and management of privatized military housing and documentation used by each military department to oversee the financial condition of each of their privatized housing projects. This included documentation on each of their portfolios as a whole through portfolio-wide oversight reports, monthly and quarterly reports on each privatized housing project, and the projects' audited financial statements from fiscal years 2013 to 2016. We also reviewed DOD's annual report to Congress on privatized housing, as well as data for privatized housing projects from fiscal years 2013 through 2016.[8] We met with officials involved in the oversight and management of privatized housing to discuss their oversight and management of the financial condition of privatized housing projects. Additionally, we examined the differences among and within the military departments in

[6]GAO, *Military Housing: Information on the Privatization of Unaccompanied Personnel Housing*, GAO-14-313 (Washington, D.C.: Mar. 18, 2014).

[7]See S. Rep. No. 114-255 at 159 (2016). The National Defense Authorization Act for Fiscal Year 2018, Pub. L. No. 115-91, § 603(c) (2017), also included a provision for us to review the management of the military housing privatization initiative.

[8]We selected this time frame because at the time we initiated our work, fiscal year 2013 was the last year for which DOD had issued a report to Congress on the financial condition of privatized military housing projects, and fiscal year 2016 was the most recent full year available. In October 2017, after we had developed the scope of our work and completed most of our analysis, DOD issued the fiscal year 2014 report to Congress.

determining the financial condition of their projects. We compared the extent of DOD's actions to assess and report the financial condition of each privatized housing project with DOD's housing policy[9] and federal internal control standards related to quality information.[10] For this and each of our objectives, we visited a non-generalizable sample of privatized housing projects.[11]

For objective two, we reviewed DOD guidance on applying reductions in the basic allowance for housing to privatized military housing, as well as other documentation on DOD's reductions in basic allowance for housing payments. Specifically, we reviewed the military departments' reports on the projected effects of the reductions in basic allowance for housing on their portfolios and quarterly project oversight reports from fiscal years 2016 and 2017 to identify challenges and options to address challenges. We interviewed officials from each military department involved with privatized housing, officials at the installations in our non-generalizable sample involved in privatized housing, and officials of five leading privatized housing developers for their perspectives on challenges to their privatized housing and options to address them. We reported examples of challenges that were identified by at least two of the three military departments. Additionally, we interviewed officials at the Defense Travel Management Office for information on the basic allowance for housing calculations and military department officials for their perspectives on the reductions in the basic allowance for housing. We compared military department reports on the projected effects of the reductions in the basic allowance for housing with federal internal control standards related to risk assessment.[12] We also reviewed policy guidance on DOD's privatized housing responsibilities to determine the level of authority needed for the options to address challenges.[13]

[9]DOD Instruction 4165.63, *DOD Housing* (July 21, 2008) (Change1, Nov. 20, 2017).

[10]GAO, *Standards for Internal Control in the Federal Government*, GAO-14-704G (Washington, D.C.: Sept. 2014).

[11]For this sample, we selected one or two projects from each of the military departments, emphasizing projects that had identified financial difficulties or were located in close proximity to military department oversight offices.

[12]GAO-14-704G.

[13]DOD Instruction 4165.63 (July 21, 2008).

For objective three, we reviewed DOD guidance on oversight and management of privatized military housing, interviewed DOD and developer officials responsible for privatized housing, and reviewed DOD documentation. Specifically, we reviewed DOD housing policies and guidance and military department guidance on overseeing privatized housing. We also interviewed officials familiar with notification processes for changes to privatized housing projects and with approaches to managing risks to privatized housing projects, and officials in the Office of Management and Budget familiar with privatized military housing. We compared the extent to which DOD has defined notification requirements for project changes and the extent to which DOD has defined risk tolerance for privatized housing with federal internal control standards related to internal communication and risk assessment.[14] Further details on our scope and methodology can be found in appendix I.

We conducted this performance audit from December 2016 to March 2018 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Background

DOD Goals, Roles, and Responsibilities for the Privatized Housing Program

DOD's policy is to ensure that eligible personnel and their families have access to affordable, quality housing facilities and services consistent with grade and dependent status, and that the housing should generally reflect contemporary community living standards.[15] It is also DOD's policy to rely on the local private sector as the primary source of housing for servicemembers who are normally eligible to draw a housing allowance, whether unaccompanied or accompanied by family. About a third of

[14]GAO-14-704G.

[15]DOD Instruction 4165.63 (July 21, 2008).

eligible servicemembers generally live on an installation, with the rest living in the surrounding local communities.

The Assistant Secretary of Defense for Energy, Installations, and Environment (ASD (EI&E)) is the program manager for all DOD housing, whether DOD-owned or privatized. In this capacity, the ASD (EI&E) provides guidance and general procedures related to military housing privatization. One responsibility of ASD (EI&E) is to provide required reports to Congress on privatized military housing projects. However, it is the responsibility of the military departments, rather than ASD (EI&E), to execute and manage privatized housing projects, including conducting financial management and monitoring their portfolio of projects. Each military department has issued guidance that outlines its responsibilities for privatized housing, such as key offices responsible for overseeing privatized housing projects.[16] For each privatized military housing project, developers maintain day-to-day operational decision making and manage each project.[17]

Military Housing Privatization Authorities and Project Structures

The military housing privatization initiative provided DOD with various authorities to obtain private-sector financing and management to repair, renovate, construct, and operate military housing. These authorities included the ability to make direct loans to and invest limited amounts of funds in projects for the construction and renovation of housing units for servicemembers and their families.[18] The projects were generally financed through both private-sector financing and funds provided by the military departments. Specifically, projects obtained private-sector financing by obtaining bank loans and by issuing bonds, which are held

[16]Department of the Army, *Portfolio and Asset Management Handbook* (Version 5.0, September 2014); Commander, Navy Installations Command, Instruction 11103.7A, *Navy Housing Roles and Responsibilities for Program Management and Finance* (Jan. 16, 2014); Air Force Instruction 32-6007 *Privatized Housing Management* (Sept. 19, 2012)(Revised by AFGM 2017-01).

[17]Privatized housing projects are run by a lead partner. For the purposes of this report, we refer to this partner as a developer or developers. Developers are alternately referred to by the military departments as project owners, private partners, or managing members.

[18]The authorities also provided DOD with the ability to provide loan and rental guarantees, make differential lease payments, and convey or lease property or facilities to eligible entities, among other things.

by the public. In addition, the military departments provided additional financing. The Army and the Navy generally structured their privatized housing projects as limited liability companies in which the military departments formed partnerships with the developers and invested funds into the partnership.[19] The Air Force generally provided direct loans to the developers. Because privatized housing projects involve budgetary commitments of the federal government, each project was scored at inception by the Office of Management and Budget to determine the amount of funds that needed to be budgeted for that particular project.[20]

The number of projects can change over time. For example, a project may be sold, and new projects can be created. As of October 2017, there were 82 privatized military housing projects, each of which can consist of one or multiple installations. The Army has 35 projects, the Navy and Marine Corps together have 15, and the Air Force has 32.[21] Most of these are family housing projects, but the Army and Navy have created a small number of privatized housing projects for servicemembers without families (that is, unaccompanied housing).

The military departments have flexibility in how they structure their privatized housing projects, but project structures share certain similarities. For a typical project, a military department leased land to a developer for a 50-year term and conveyed existing homes located on the leased land to the developer for the duration of the lease. The developer then became responsible for leasing renovated and newly constructed homes, giving preference to servicemembers and their families.

Each privatized housing project is a separate and distinct entity governed by a series of legal agreements that are specific to that project. These agreements include, among others, an operating agreement, a property

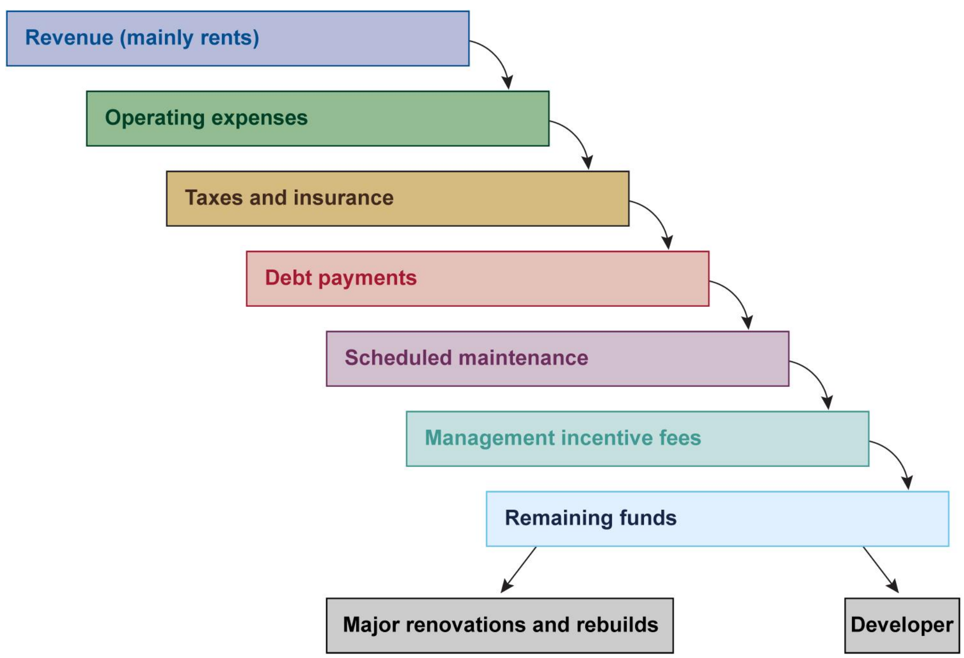
[19]A limited liability company is a company in which the liability of each shareholder or member is limited to the amount individually invested.

[20]The Office of Management and Budget uses scoring to determine the amounts to be recognized in the budget when an agency signs a contract or enters into a lease. Privatized military housing projects are scored by the Office of Management and Budget at inception to determine the amount that must be included in the federal budget for the project.

[21]The Army has a total of 35 privatized housing projects. These include 34 family housing projects, 4 of which also include housing for unaccompanied individuals, and one standalone unaccompanied housing project. For a complete list of privatized housing projects, see appendix II.

management agreement, and an agreement that describes the management of funds in the project, including the order in which funds are allocated within the project. However, while each project is distinct, there are some common elements in how projects invest and utilize funds. Every project takes in revenue, which consists mostly of rent payments. Projects then pay for operating expenses, including administrative costs, day-to-day maintenance, and utilities, among other things. After that, projects generally allocate funds for taxes and insurance, followed by debt payments. Figure 1 shows a typical funding structure for a privatized housing project.

Figure 1: Typical Funding Structure for a Privatized Housing Project



Source: GAO analysis of Department of Defense information. | GAO-18-218

In the typical privatized housing project depicted in figure 1, once debt payments are made, funds are allocated to accounts that fund scheduled maintenance. These accounts exist to fund repair and replacement of items such as roofs, heating and cooling systems, and infrastructure.[22]

[22]If a project has received a loan from the government—as is the case with many Air Force projects—the next use of funds is the payment on the government loan debt. This step is not depicted in figure 1, as Army and Navy projects generally do not include government loans.

After that, funds are allocated to a series of management incentive fees, such as the property management fee. Finally, the project divides these remaining funds according to a fixed percentage between accounts that fund major renovations and rebuilds on the one hand and go the developer on the other hand. The percentages may vary, but the majority of funds go toward the accounts funding major renovations and rebuilds.

Housing Allowance and Occupancy of Privatized Housing

DOD's Defense Travel Management Office annually calculates rent and utility rates for locations across the United States based on estimates of local market conditions, which are then adjusted for an individual's pay grade and dependency status.[23] These calculations, which can fluctuate from year to year, are then used to determine individual servicemembers' monthly basic allowance for housing payments. DOD does not require servicemembers, other than certain key personnel and junior unaccompanied personnel, to live on an installation and thus in military privatized housing. Because only about a third of eligible servicemembers generally live on an installation, the basic allowance for housing payment is designed to enable servicemembers to live off-base comparably to their civilian counterparts. Servicemembers pay their rent—whether living on the installation or off—with their basic allowance for housing payments. Therefore, DOD's privatized housing competes with available housing options in the local market.

Active-duty servicemembers are given priority for privatized military housing. However, projects can advertise and lease to tenants other than active-duty servicemembers, including civilians in some cases, generally once occupancy dips below a specific level.[24] For example, the Air Force has approved leasing to other tenants when any given project's occupancy rate falls below 98 percent.

[23]Prior to 2015, the basic allowance for housing benefit also included a component for renter's insurance, which comprised on average less than 1 percent of the total benefit. In 2015, DOD stopped including renter's insurance as a component of the basic allowance for housing.

[24]If occupancy falls below a certain level, then after military families are accommodated, projects can rent to unaccompanied military personnel, active National Guard and Reserve, military retirees, federal government civilians, and lastly civilians.

DOD Regularly Assesses Projects' Financial Conditions but Has Not Consistently Assessed Future Sustainment Needs or Issued Required Reports to Congress

DOD regularly assesses the financial condition of its privatized housing projects through recurring internal reporting by the military departments on each of their projects; however, key data on current financial conditions are not mutually comparable. Moreover, the military departments vary in the extent to which they use measures of future sustainment needs and funding to assess project sustainability.[25] In addition, DOD has not consistently issued required reports to Congress on the financial condition of privatized housing projects in a timely manner.

The Military Departments Regularly Assess the Financial Condition of Their Privatized Housing Projects

The military departments regularly assess the current financial condition of their privatized housing projects through internal, recurring monthly or quarterly financial reporting. DOD policy requires the military departments to manage their housing, including privatized housing, through financial management and reporting.[26] DOD's housing manual states that because housing privatization projects create a long-term governmental interest in privatized housing, it is essential that projects be monitored attentively, and that the military departments monitor their portfolios of projects.[27] Specifically, each military department produces—based on information provided by each project—or receives from each project quarterly or monthly reports detailing the financial condition of each individual privatized housing project. Each military department also produces

[25]The military departments use various terms to refer to types of future maintenance and reinvestment in privatized housing, and to the accounts used to fund these expenses. For the purposes of this report, we use the term "sustainment" inclusively to refer to funding both for planned maintenance and for reinvestment in projects through major renovations and unit rebuilds.

[26]DOD Instruction 4165.63 (July 21, 2008).

[27]DOD Manual 4165.63-M, *DOD Housing Management* (Oct. 28, 2010).

periodic reports on the condition of its portfolio as a whole. These reports include financial measures such as revenue and operating expenses, as well as a measure of the ability to make required debt payments, referred to as debt coverage ratio or debt service coverage ratio.[28]

In their assessments, each military department emphasizes somewhat different measures of current financial condition, although each uses debt coverage ratio as a key measure of the current financial condition of privatized military housing projects. Specifically, in its portfolio-wide reports, the Army uses three key performance metrics to measure financial condition—a measure of revenue, net operating income, and the debt coverage ratio.[29] The Air Force also rates projects' financial condition based on three metrics, but the metrics differ from those used by the Army. The Air Force's metrics are operating expenses compared with budgets, net operating income compared with the original project plan, and debt coverage ratio. In its portfolio-wide reports, the Navy provides debt coverage ratio as its measure of current financial condition. Regardless of the different metrics used, the military departments rated almost all of the privatized housing projects as having acceptable current financial conditions. Specifically:

- Army: For the quarter ending June 30, 2017,[30] all 34 Army projects generated enough cash to continue operations and make required debt payments, according to the Army's portfolio-wide reporting.[31] However, the Army rated 8 family housing and 4 unaccompanied housing projects as below or well below expectations, in terms of

[28]Debt coverage ratio and debt service coverage ratio refer to the same measure, which is generally defined as net operating income (income after operating expenses) divided by required debt payments.

[29]DOD defines net operating income as income remaining after all project expenses are paid, but before debt service and depreciation.

[30]The Army and the Air Force prepare quarterly portfolio-wide reports, whereas the Navy updates its portfolio-wide report every 6 months. For this reason we use the most recent available quarterly Army and Air Force reports, and the most recent 6-month Navy report.

[31]The Army has a total of 35 privatized housing projects. These include 34 family housing projects, 4 of which also include housing for unaccompanied individuals, and 1 standalone unaccompanied housing project. Army officials stated that the independent unaccompanied housing project also generated enough cash to continue operations and make required debt payments for the quarter ending June 2017.

current finances.[32] For example, the Army rated the project at Fort Bragg, North Carolina, as being well below expectations, due to occupancy challenges resulting from off-post competition and higher-than-expected expenses.

- Navy and Marine Corps: For the 6 months ending June 30, 2017, all 16 Navy and Marine Corps projects[33] were generating enough cash to continue operations and make required debt payments, according to the Navy's portfolio-wide reporting. However, 5 of the 16 projects were on a watch list, due to financial challenges.[34] For example, the Marine Corps' project comprising Camp Lejeune, North Carolina; Marine Corps Air Station Cherry Point, North Carolina; and Stewart Air National Guard Base, New York[35] was experiencing low occupancy rates due to local market competition, and as such was included on the watch list.
- Air Force: For the quarter ending June 30, 2017, the Air Force rated 27 of its 32 projects' current finances as acceptable or exceptional. However, the Air Force rated 2 of its 32 projects as unacceptable, and 3 as marginal, for current finances, according to Air Force portfolio-wide reporting.[36] For example, the Air Force rated the Nellis Air Force Base project in Nevada as having an unacceptable current financial condition as of June 2017. In March 2017, the Office of Management and Budget approved the budgetary scoring of a financial restructuring of the project. In the restructuring, the Air Force reduced the interest rate on the government's direct loan to the project and extended the loan's maturity date, redistributed residual project cash flows, and reduced certain returns due to the developer. In another example, the Air Force rated the Air Combat Command II project, which comprises Holloman Air Force Base, New Mexico, and Davis-

[32]The Army considers its projects below or well below expectations for finances based on a comparison of revenues, net operating income, and debt coverage ratio with baseline plans.

[33]The Navy subsequently sold one of these projects, and as of October 2017 there were a total of 15 Navy and Marine Corps projects.

[34]Navy officials stated that there are no specific criteria for inclusion on the watch list.

[35]Some Marine Corps personnel are stationed at Stewart Air National Guard Base.

[36]The Air Force rates projects unacceptable for current finances when most of the current finance metrics are unacceptable, and rates a project marginal for current finances when two or more of the current finance metrics are marginal, or one metric is unacceptable. Metrics include comparisons of operating expenses with a project's budget; net operating income with the project's plan; and debt coverage ratio.

Monthan Air Force Base, Arizona, as having a marginal current financial condition as of June 2017. Specifically, basic allowance for housing rates for the project were only 85 percent of original expectations, and the project was unable to compensate for that shortfall by controlling expenses. The Office of Management and Budget has approved the budgetary scoring of a financial restructure of the project, including a reduction in the interest rate on the government's loan to the project and a reduction in certain returns and fees previously owed to the developer.

Data on Current Financial Condition of Privatized Housing Projects Reported to the Office of the Secretary of Defense and Congress Are Not Comparable

Based on our analysis, data on the current financial condition of privatized housing projects that have been reported by the military departments to ASD (EI&E) and Congress have not been comparable because (1) there are inconsistencies in the calculation of the reported debt coverage ratios, and (2) the data requested have not followed consistent time periods. Debt coverage ratios are a key measure used by the military departments to report on the current financial condition of privatized housing projects, and the measures are also the main financial measure for privatized housing projects that DOD has previously reported to Congress. However, we found the following inconsistencies in the debt coverage ratio data reported to ASD (EI&E):

- Adjustments made to income for the purposes of calculating debt coverage ratios affect the ratios' consistency: The expenses that are or are not included in a project's calculation of the debt coverage ratio are dictated by each project's business agreements. ASD (EI&E) defines debt coverage ratio as the project's net operating income—income remaining after all project expenses are paid, but before debt service and depreciation—divided by its required debt payments.[37] However, we found that in practice, projects make various adjustments to net operating income for the purposes of calculating debt coverage ratios. These adjustments may include adding or subtracting from net operating income any of the following: sustainment fund deposits; various types of management fees,

[37]Debt service is the project's required debt payments, including principal and interest. Depreciation is an expense recorded to match the cost of an item over its useful life.

including performance incentive fees and asset management fees; certain utility costs; and taxes. Military department officials stated that the debt coverage ratios calculated using these adjustments, while different for different projects, are accurate and appropriate. However, while the calculation methods may be sufficient for any given project, the differences in calculation methods reduce the comparability of the data.

- Different project accounting methods affect the comparability of debt coverage ratios: Some projects conduct financial accounting based on the amount of cash received or paid during the period (referred to as cash basis accounting), while other projects do so based on when revenue is earned and when expenses are incurred, regardless of when cash is received or paid (called accrual basis accounting). These accounting differences can significantly affect the debt coverage ratio. For example, a cash basis project may have cash on hand to pay its debt obligations, but not enough to cover future expenses that would have been recognized under an accrual project. The specific accounting method used reflects each project's particular business agreements, but the differences in accounting methods reduce the comparability of the debt coverage ratios across the projects.

Moreover, as the program manager for all DOD housing, ASD (EI&E) requested debt coverage ratio data across varying time frames for required reports to Congress on privatized housing projects. Specifically, ASD (EI&E) has alternated between requesting annual average debt coverage ratio data and requesting data as of the end of the reporting period, thus reducing the comparability of the data over time. In instructions for its fiscal year 2014 data collection, the office requested the average debt coverage ratio over the full fiscal year; in instructions for its fiscal year 2015 data collection, it requested data as of the end of the reporting period; and in its fiscal year 2016 data collection, the office again requested data for the average over the full fiscal year.[38]

Furthermore, the instructions provided by ASD (EI&E) to the military departments for fiscal year 2015 did not specify the time period of the data to be reported. Therefore, each military department provided a

[38]In fiscal years 2014 and 2016, ASD (EI&E) requested that the military departments report the average debt coverage ratio for the period. In its instructions for fiscal year 2015, ASD (EI&E) did not request that the military departments report the average debt coverage ratio, instead requesting that the debt coverage ratio be reported as of the end of the reporting period.

different time period of data in response, further reducing the comparability of the data. Specifically, one of the military departments provided quarterly data, another military department provided data for the full year, and the other military department provided one-month data, according to military department officials.

Using data from different time periods not only reduces their comparability, but also can produce a different outlook on a project's financial condition. For example, we found that debt coverage ratios for a single fiscal quarter can be significantly different from the ratio for the same project for the full fiscal year. In some cases, a quarterly ratio showed insufficient funds to continue operations and make required debt payments, while the full-year ratio showed sufficient funds for that purpose. Conversely, another project's ratios showed the single quarter as having sufficient funds, but the full year as having insufficient funds. ASD (EI&E) officials stated that data for previous reports were collected by different staff in that office and that the current officials were not sure why the time period for fiscal year 2015 data collection was different from that of the other two fiscal years.

Standards for Internal Control in the Federal Government states that management should use quality information and externally communicate the necessary quality information to achieve the entity's objectives.[39] Information, among other things, should be complete and understandable. This involves processing data into information and then evaluating the processed information so that it is quality information. The standards also state that management should obtain relevant data from reliable sources, which provide data that are reasonably free from error and faithfully represent what they purport to represent.

However, in prior reports to Congress, ASD (EI&E) did not clarify the differences in how debt coverage ratios were calculated, resulting in information that lacked full context. Moreover, the information provided by the military departments to ASD (EI&E) and to Congress to conduct their oversight activities has not been consistent and comparable because ASD (EI&E) has not revised its guidance on privatized housing to ensure that data reported to Congress, such as data on debt coverage ratios, are consistent in terms of time periods. Officials in ASD (EI&E) acknowledged that the differences in debt coverage ratio calculation methods and

[39]GAO-14-704G.

project account methods can affect the comparability of the data. They also noted that in the future they plan to continue the annual time period for data collection and reporting, though they did not identify any additional steps they plan to take to ensure consistent and comparable data. Without contextual information on how the military departments calculate debt coverage ratios—a key measure of the current financial condition of privatized housing projects—and on the effect these differences have on comparing the data across projects, data reported to Congress may not be fully useful in supporting congressional oversight of privatized military housing. Additionally, by revising guidance to ensure that data reported to Congress are comparable (that is, across the same time frames), ASD (EI&E) will provide additional assurance that DOD and Congress will have quality information on which to base decisions regarding privatized housing projects.

The Military Departments Have Varying Methods of Assessing a Project's Sustainability

During the course of our review, we found that the military departments take different approaches in assessing a project's sustainability (that is, future sustainment needs and funding). Army officials stated that the Army validates project sustainment plans, and is developing, but has not yet implemented, a model to independently assess project sustainability. The Navy validates sustainment plans generated by the developers managing its projects. In addition to reviewing developers' sustainment plans, the Air Force conducts an independent analysis of each project's sustainment needs by conducting site tours of each project location and by using its own financial model to forecast sustainment needs, according to Air Force officials. The Air Force then compares its analysis with that of the developer. In most cases, according to Air Force officials, this comparison has shown that the Air Force's estimates of sustainment needs were greater than the developer's original estimates, which would require additional sustainment funding beyond what the developer estimated.

Moreover, the military departments do not all use measures of future sustainment for their internal portfolio-wide reports on privatized housing projects. Specifically:

- Army: The Army does not include a measure of future sustainability among the key finance performance metrics it emphasizes in its portfolio-wide oversight reports. The Army tracks the balance of funds for long-term major renovations and rebuilds as compared with expectations, but it does not include a measure of expected future sustainment needs versus funding in its portfolio-wide reports. As of June 2017, seven Army projects had fallen below expectations in current funding levels for long-term major renovations and rebuilds, according to the Army's portfolio-wide report for the quarter ending June 2017.

- Navy: In its portfolio-wide reports, the Navy includes a measure of sustainability. Specifically, the reports show modeled surpluses or shortfalls in sustainment funding through the term of each project. As of June 30, 2017, the Navy reported five projects expecting shortfalls in sustainment funding, four of which the Navy anticipated would require project plan modifications to address the shortfalls.
- Air Force: In its portfolio-wide reporting, the Air Force has adopted measures of long-term financial condition, including measures of future sustainment funding. Specifically, the Air Force gives each project a "long-term outlook" rating. This rating includes measures of projected sustainment funding levels relative to projected needs, among other measures. As of June 30, 2017, the Air Force rated 6 of its 32 projects as having "unacceptable" long-term outlooks, and another 6 as having "marginal" long-term outlooks.[40] For example, the Air Force considered the Air Combat Command II project, which comprises Holloman Air Force Base, New Mexico, and Davis-Monthan Air Force Base, Arizona, to have severely underfunded planned maintenance funds and a projected inability to meet any future needs for major renovations and rebuilds, due to lower-than-expected basic allowance for housing levels.

DOD guidance states that because privatization creates a long-term governmental interest in privatized housing, it is essential that projects be attentively monitored. DOD has recognized that a lack of sustainment funding can decrease the desirability of housing over time, thus reducing occupancy and further jeopardizing financial stability. However, DOD has not required the military departments to incorporate measures of future sustainment into their assessments of privatized housing projects. Measures of current financial condition, such as the ability to make debt

[40]The Air Force rates a project's long-term outlook unacceptable when any of the measures for projected sources and uses of funds compared with project plans, projected debt coverage ratio, or projected near-term sustainment funding is unacceptable. The Air Force rates a project's long-term outlook marginal when it has a marginal capital repair and replacement funding metric or an unacceptable metric for long-term sustainment (called reinvestment).

payments, do not necessarily indicate the ability of a project to fund its sustainment accounts sufficiently to maintain housing quality in the future. A project may generate enough revenue to cover operating expenses and make required debt payments, but the level of projected funding available for planned renovations over the course of the project may still be insufficient, as shown by Navy and Air Force portfolio-wide oversight reports. The Navy and Air Force include measures of future sustainment needs and funding in their portfolio-wide oversight. While Army officials stated that the Army regularly reviews sustainment funding levels, the Army does not include forecasts of future sustainment needs and funding in its portfolio-wide assessment reports because they are not required by ASD (EI&E). Without a requirement to include sustainment measures in their oversight of privatized housing projects, military department officials may choose to review such measures or not. If ASD (EI&E) does not require the military departments to include measures of future sustainment in their assessments of privatized housing projects, the military departments may not consistently incorporate such measures into their portfolio-wide assessments, and therefore the military departments and ASD (EI&E) may not have sufficient oversight of the projects' future sustainability. ASD (EI&E) officials agreed that such a requirement would help ensure that the military departments are consistent in their oversight of future sustainment.

DOD Has Not Met the Requirement for Financial Oversight Reports to Congress in a Timely Manner and Has Not Included Sustainability Information on Each Privatized Housing Project

DOD has not consistently provided required reports to Congress in a timely manner, and as a result Congress does not have up-to-date information on the financial condition of privatized housing. Section 2884(c) of Title 10 of the United States Code requires the Secretary of Defense to report semiannually an evaluation of the status of oversight and accountability measures for military housing privatization projects, including, among other things, information about financial health and performance and the backlog of maintenance and repair. DOD provided a report covering fiscal year 2013 to Congress in November 2014, and then did not provide another report, covering fiscal year 2014, until October

2017.[41] ASD (EI&E) officials stated that they have not provided the reports in a timely manner in recent years due to staff turnover and limited resources, as well as efforts to ensure the quality of the data included in the reports. An ASD (EI&E) official stated that DOD is planning to resume timely reporting, with a consolidated report covering fiscal years 2015 and 2016 to be submitted to Congress in the second quarter of fiscal year 2018, and a report covering fiscal year 2017 to be submitted in late fiscal year 2018.

Furthermore, in prior reports submitted to Congress, ASD (EI&E) has not reported information on the future sustainment of each privatized housing project. The statute does not require the reporting of information on future sustainability for each project. However, ASD (EI&E) has noted that long-term sustainability has become a priority as projects have completed their initial development periods, and therefore information on future sustainment has become more critical to understanding the projects' financial health.

Standards for Internal Control in the Federal Government states that management should use quality information and externally communicate the necessary quality information to achieve the entity's objectives.[42] In the past, DOD has not consistently reported on the financial condition of privatized housing projects to Congress and in cases where data were reported, the department focused its reports on measures of current financial health such as debt coverage ratios, which do not provide information about the future sustainment of the projects. An ASD (EI&E) official stated that the office will streamline the report's narrative while adding additional details to figures as a means to expedite future report submission, but the official did not provide additional details of how future reports will be completed in a more timely fashion. ASD (EI&E) officials also stated that in the past they were focused on the initial implementation phases of the privatized housing projects and are now shifting to focus on sustainment, but they have not provided sustainment information on each project to Congress. ASD (EI&E) officials agreed that it would be beneficial to include information on sustainment in their reports to Congress. If DOD does not take steps to comply with statutory time frames for reporting on the financial condition of privatized housing

[41]According to DOD officials, although the statute requires semiannual reporting, due to the effort involved DOD aims to produce one report each fiscal year, rather than two.

[42]GAO-14-704G.

projects moving forward, decision makers in Congress will not have up-to-date information about financial conditions of projects as they provide oversight of a program that represents a long-term commitment for the department. Furthermore, reporting financial information on the future sustainability of projects will help provide Congress a complete picture of the financial condition of each project.

DOD Has Not Fully Assessed the Effects of the Basic Allowance for Housing Reductions but Has Identified Other Privatized Housing Challenges and Options to Address Them

DOD has completed some analysis of the projected effects of recent reductions in the basic allowance for housing on its privatized housing portfolios, but it has not fully assessed the significance of the effects on the future sustainment of each of its privatized housing projects.[43] Moreover, DOD has not identified a course of action to address possible shortfalls resulting from the reductions in the basic allowance for housing. The military departments have also identified a variety of other challenges that could affect the financial condition of their privatized housing projects, including reductions in assigned personnel and the higher-than-expected cost of utility infrastructure. The military departments have identified options to address potential financial challenges to their privatized housing projects, including actions to increase revenue, actions to reduce expenses, and extraordinary measures to improve project financial conditions.

[43]Beginning in 2015, DOD began reducing the basic allowance for housing payments relative to the Defense Travel Management Office's calculations of market rate rents and utilities. According to Defense Travel Management Office officials, basic allowance for housing payments are not necessarily decreasing from year to year. Instead, the average basic allowance for housing payment across the geographic areas has risen due to increases in market rate calculations, even as basic allowance for housing payments have been reduced relative to these calculations. However, throughout this report we refer to reductions in basic allowance for housing payments since the payments are being reduced relative to the market rate calculations.

Reductions in the Basic Allowance for Housing Could Decrease Privatized Housing Projects' Revenue and Future Sustainment Funding

According to the military departments, reductions in the basic allowance for housing relative to market rent and utility calculations by the Defense Travel Management Office—a 4 percent reduction as of 2018—will decrease funding for future sustainment and could affect the privatized housing projects' ability to continue operations and make required debt payments. Specifically, housing developers stated that declines in revenue have already been felt by certain projects, and that any reduction in their ability to sustain the privatized housing projects over the term of their 50-year leases will result in the degradation of the housing, leaving the homes less marketable. Unlike challenges that may affect one or a few projects, the reductions in the basic allowance for housing affect all projects, since basic allowance for housing is a basis for revenue for all of the projects.

DOD has established that the amount charged to servicemembers for renting housing on base was equal to their basic allowance for housing rate.[44] Thus, the privatized housing projects were developed with the assumption that they would receive full basic allowance for housing payments as rent, according to officials from each military department. However, at DOD's request, Congress included provisions in the Carl Levin and Howard P. "Buck" McKeon National Defense Authorization Act for Fiscal Year 2015 and National Defense Authorization Act for Fiscal Year 2016 that authorized the department to reduce the housing allowance to servicemembers below the Defense Travel Management Office's typical basic allowance for housing calculations, starting with a 1 percent reduction in 2015 and reaching a 5 percent total reduction by 2019.[45] As of 2018, the department has reduced basic allowance for housing payments by 4 percent. Because of this reduction, the revenue

[44]The housing owners may set rents at an amount equal to the tenants' basic allowance for housing rate, reduced by an amount that allows the tenants to pay for their utility usage.

[45]See Pub. L. No. 113-291, § 604(a) (2014) and Pub. L. No. 114-92, § 603 (2015), codified, as amended, at 37 U.S.C. § 403(b). The National Defense Authorization Act for Fiscal Year 2018, Pub. L. No. 115-91, § 603 (2017), requires the Secretary of Defense in calendar year 2018 to pay to developers the equivalent of 1 percent of the basic allowance for housing.

that projects receive from rent payments has decreased at certain projects. However, according to officials representing the military departments, the reductions in the basic allowance for housing will not be the sole reason that any project is struggling. A project may be struggling due to other challenges the military departments identified, examples of which we describe in this report, such as aging utility infrastructure. However, officials representing each military department stated that the reductions will have a compounding effect on projects that are facing other challenges.

DOD Has Not Fully Assessed the Effects of the Reductions in the Basic Allowance for Housing That Began in 2015

An August 2015 memorandum issued by ASD (EI&E) directed the military departments to complete a thorough review of their privatized housing portfolios.[46] Additionally, the military departments were to provide a report outlining any effects of changes in the basic allowance for housing on their portfolios. However, the military departments have not fully assessed the effects of the basic allowance for housing reductions. Instead, in response to this memorandum, the military departments completed some analysis on the effects of the reductions in the basic allowance for housing and provided reports outlining the projected effects of the reductions on their privatized housing portfolios. Each military department reported that the reductions in the basic allowance for housing would decrease project revenue, and each provided estimates across multiple scenarios.[47] Specifically:

- The Army's September 2015 report projected an average decrease in long-term sustainment accounts of $104 million per project through 2039 based on a 5 percent reduction in basic allowance for housing rates.[48] Out of the 35 projects in the Army's privatized housing portfolio, the report looked at the 15 projects projected to lose 5

[46]Office of the Assistant Secretary of Defense for Energy, Installations, and Environment Memorandum, *Applying Basic Allowance for Housing Reductions to Privatized Housing* (Aug. 27, 2015).

[47]The estimates in each report were based on the assumptions and conditions of occupancy rates, among other things, at the time they were completed, which can change.

[48]This projection assumes occupancy remains at 2015 levels and that the basic allowance for housing is reduced by 5 percent in 2016 and increases 2 percent per year thereafter.

percent or more of their assigned personnel and estimated the funds available to support each project from 2015 until the end of 2039.

- The Navy's October 2015 report projected a decrease in long-term sustainment accounts across the portfolio of privatized housing projects of $2 billion based on a 5 percent reduction in basic allowance for housing rates.[49] The report also summarized any projected effects in the first year of reductions on the debt coverage ratio and specified the calendar years when sustainment shortfalls could begin to occur per project.
- The Air Force's November 2015 report projected a decrease of $48 million per year across the portfolio based on a 5 percent reduction in basic allowance for housing rates.[50] The report indicated that project ratings could begin to be affected in the same year as the reductions in the basic allowance for housing were implemented, and that funding for long-term sustainment would be diminished.

However, DOD does not have the information needed to fully assess the effects of the reductions that began in 2015, because it did not direct the military departments to specify in their reports the significance of the effects of the reductions on each individual project. The August 2015 ASD (EI&E) memorandum directed the military departments to provide reports with a "thorough review," but it did not specify the inclusion of information that would detail the extent of the effects on the sustainment of each individual project. As a result, the reports did not fully assess specific effects on each project to enable the identification of and response to specific risks. For example, generally, the reports did not include certain information for the full term of all projects, as detailed below:

- two of the reports did not include information on when deficits related to reductions in the basic allowance for housing will occur per project;[51]

[49]The report assumed a baseline using the 2015 annual operating budget but added back the 1 percent out-of-pocket expense to reflect pre-2015 forecasts. An additional adjustment was made to account for the removal of renter's insurance, an approximately 1 percent reduction.

[50]The Air Force simulated basic allowance for housing inflation rates of 0 percent, -3 percent, and -5 percent to estimate what project income would be for each project's remaining lease term. The Air Force performed this analysis in conjunction with its annual reforecast of every project.

[51]The Navy report includes this information, but the Army and Air Force reports do not.

- two of the reports did not include information on the decrease in the sustainment accounts due to reductions in the basic allowance for housing versus the amount that the project requires for planned sustainment per project;[52] and
- none of the reports included information on the likely effects of particular sustainment funding deficits (for example, how many units will forgo needed renovations or rebuilds).

In addition, the military departments did not identify specific actions in the reports to respond to particular, identified shortfalls for individual projects resulting from reductions in the basic allowance for housing. In its August 2015 memorandum, ASD (EI&E) noted that individual projects may have different solutions to address the effect of the reductions in the basic allowance for housing. The military departments did not outline solutions for each individual project but, as requested by ASD (EI&E), proposed recommendations in their reports to mitigate the overall effects of the reductions in the basic allowance for housing by charging servicemembers the out-of-pocket rate. The out-of-pocket rate reflects a servicemember cost-sharing adjustment that would require the servicemember to pay the amount by which his or her allowance was reduced.[53]

However, neither DOD nor the military departments have taken action to address the reports' recommendations, nor have they determined any other courses of action for individual projects in response to the reductions in basic allowance for housing. While the Army has a policy that would allow individual projects to propose charging servicemembers the out-of-pocket amount, subject to Army approval, the policy states that the Army strongly prefers that projects not charge servicemembers. According to Army officials, none of the projects had done so as of August 2017. Further, according to privatized housing developers representing Army projects, they have not proposed charging the out-of-pocket rate because doing so could result in a reduction in occupancy at that project, as servicemembers would begin to look for other housing. Unlike the Army, the Navy and Air Force do not have a policy that would allow developers to charge the out-of-pocket amount. According to ASD (EI&E), Navy and Air Force officials stated that their lack of policy is

[52] The Navy report includes this information, but the Army and Air Force reports do not.

[53] The out-of-pocket rate is administered using an absorption rate, which is computed to ensure that members of a similar pay grade/dependent status pay the same amount out-of-pocket, regardless of their location.

based in large part on the fact that servicemembers from all three military departments reside at nearly every installation, and that without having written assurance that the other military departments will also charge the out-of-pocket rate, the Air Force and Navy cannot agree to do so.

Standards for Internal Control in the Federal Government states that management should analyze the identified risks to estimate their significance, which provides a basis for responding to the risks, and design responses to the analyzed risks so that risks are within the defined risk tolerance for the defined objective.[54] In its August 2015 memorandum, ASD (EI&E) noted that the reductions in the basic allowance for housing could create shortfalls that in turn could lower the quality of homes in privatized housing communities. However, DOD has not fully assessed the significance of this risk by considering the magnitude of impact, the likelihood of occurrence, and the nature of the risk because, generally, the reports do not include certain information for the full term of all projects, as detailed above.[55] Specifically, DOD has not fully assessed the significance of the risk of the reductions in the basic allowance for housing by considering how the reductions will affect the quality of its housing. If DOD does not fully assess the effects of the reductions in the basic allowance for housing, DOD and Congress will not be fully informed before making decisions that could affect all of the projects. Furthermore, if DOD does not respond to the risk of reduced sustainment funds by designing specific actions, DOD and the military departments may not be well positioned to reduce any risks and meet their objective of providing quality housing for servicemembers.

The Military Departments Have Identified Various Challenges to Sustaining Their Privatized Housing Projects

The military departments have identified various challenges that could affect the financial condition and future sustainment of their privatized housing projects. Examples of these challenges include the following:

[54] GAO-14-704G.

[55] Magnitude of impact refers to the likely magnitude of deficiency that could result from the risk and is affected by factors such as the size, pace, and duration of the risk's impact. Likelihood of occurrence refers to the level of possibility that a risk will occur. The nature of the risk involves factors such as the degree of subjectivity involved with the risk and whether the risk arises from fraud or from complex or unusual transactions.

- Reductions in assigned personnel at installations have reduced occupancy rates: Information from military department officials shows that the loss of personnel assigned to an installation has reduced occupancy at some projects. Reductions in assigned personnel can occur at an installation because of large-scale troop reductions or the inactivation of units. The decrease in occupancy at some projects has led to revenue and cash flow challenges. For example, Army officials noted that the occupancy rate dropped from about 95 percent to about 70 percent at the Fort Knox project in Kentucky in 2014 when a unit was inactivated. This drop in occupancy resulted in challenges for the privatized housing project because the number and type of housing units originally built were determined on the basis of the unit's remaining at the installation.
- Aging utility infrastructure has increased sustainment costs, resulting in reduced cash flows for some projects: According to DOD and officials representing the military departments, the costs of maintaining infrastructure for utilities has reduced cash flows for some projects. In some privatized housing agreements, the military departments transferred responsibility for utility infrastructure to the projects. According to DOD and military department officials, this oversight and maintenance have been more costly than project owners had expected. Air Force officials stated that aging utility infrastructure is not something the projects are equipped to handle because there is not enough revenue in their project structures to cover the costs of maintaining the infrastructure. Air Force officials said that they noticed the challenges related to transferring utility infrastructure in the earlier projects and that they made a decision to stop transferring infrastructure to developers in later projects. Moreover, according to Air Force officials, some project owners are now asking for the military departments to take back the infrastructure. For example, the Air Force agreed to take back some of the gas and electric infrastructure at the Air Force Academy project in Colorado as part of a financial restructuring.
- Perceived disconnects between basic allowance for housing calculations and market rates: Military department officials and privatized housing developers perceive the Defense Travel Management Office's basic allowance for housing calculations as challenging because they believe that the calculations are unpredictable and do not always reflect the realities of local markets. Officials in each military department stated that the data used for the calculations sometimes do not accurately reflect the local market surrounding the project. For example, officials from the Navy's Midwest project noted that the calculation for Millington, Tennessee—

an area covered by the Midwest project—was higher than that for the Chicago area of the project in 2014—an area that they felt should have had the higher costs of the two.[56] Additionally, according to Army officials, basic allowance for housing rates fluctuate at certain projects from year to year and do not reflect the local market. For example, the average basic allowance for housing rate for Fort Huachuca in Arizona dropped 11 percent from 2014 to 2015, increased 4.6 percent in 2016, and dropped 9 percent in 2017. Army officials stated that these fluctuations did not match rental costs in the local market.

- Actual costs of utilities in some locations are not covered by the basic allowance for housing utility rates: Officials representing two military departments stated that the Defense Travel Management Office's basic allowance for housing calculations do not accurately reflect the actual costs of utilities.[57] According to Army officials, the utility component of the Defense Travel Management Office's calculations does not cover the actual cost of utilities for project homes at some locations. This difference can result when the surveys for utility costs are from homes in the local community that are not comparable to those on base.[58] For example, in Fairbanks, Alaska—where the Army's Fort Wainwright/Greely project is located—off-base homes get the majority of their heat from wood stoves that report no cost element to the surveys used by the Defense Travel Management Office. By underreporting or not otherwise adjusting for these costs, according to Army officials, the basic allowance for housing calculations fail to account for the funds necessary to cover the costs of traditional, metered utilities.
- Unexpected project expenses can reduce cash flows for some projects: Officials representing two military departments stated that unexpected expenses can be a challenge for some projects. These expenses can occur because of unexpected events, such as weather events, environmental damage, or unexpected litigation. For example, the Navy's Mid-Atlantic project has experienced unexpected expenses

[56]The Navy's Midwest project comprises Naval Station Great Lakes, Illinois; Naval Hospital Great Lakes, Illinois; Fort Sheridan, Illinois; Naval Air Station Glenview, Illinois; Naval Surface Warfare Center Crane, Indiana; and Naval Support Activity Mid-South, Millington, Tennessee.

[57]Utilities factored in the calculation include electricity, heating fuel, water, and sewer.

[58]The Defense Travel Management Office uses data from the Bureau of the Census's annual American Community Survey to determine average expenditures for utilities specific to each dwelling type in the housing area. All data are sensitive to local housing conditions, geography, and climate.

related to water intrusion and mold issues and the ensuing litigation, causing fewer funds to flow to the project's sustainment accounts.[59] There are also expenses for snow removal, hurricanes, and flooding. Navy officials stated that they did not anticipate a lot of sustainment work in the first 5 to 10 years of the projects, but needs have arisen due to these unexpected events. Additionally, according to information from the Navy's New Orleans project in Louisiana, hurricane and tropical storm damage may drain $1.5 million to $2 million from the project's sustainment accounts every 3 to 4 years.

- Determining the amount DOD must budget for a project may affect future expansions or changes to existing projects: Military department officials also noted potential challenges with the way that the Office of Management and Budget will be scoring future projects.[60] Scoring seeks to determine the cost that should be recognized and recorded as an obligation of DOD for budgeting purposes at the time a contract is signed. When the privatized housing initiative began, developers sought private borrowing, knowing that only the government funding would be scored because a 1997 Office of Management and Budget memorandum established that private funds for the projects would not be scored as government participation or activity.[61] However, according to a 2005 Office of Management and Budget memorandum, as of September 30, 2010, new privatized housing projects and expansions to existing projects using the limited liability or corporation approach are subject to traditional scoring rules. These rules require projects proposing the use of a purely private entity to be scored as a private activity, and projects proposing the use of a co-owned limited

[59]The Navy's Mid-Atlantic project comprises Hampton Roads (Naval Station Norfolk, Virginia; Joint Expeditionary Base Little Creek-Fort Story, Virginia; Naval Medical Center Portsmouth Naval Hospital, Virginia); United States Naval Academy Annapolis, Maryland; Naval Surface Warfare Center Dahlgren, Virginia; Naval Surface Warfare Center Indian Head, Maryland; Naval Air Station Patuxent River, Maryland; Naval Security Group Activity Sugar Grove, W. Virginia; Tingey House, Washington Navy Yard, D.C.; Marine Corps Base Camp Lejeune, North Carolina; and Naval Support Activity Mechanicsburg, Pennsylvania.

[60]As previously mentioned, the Office of Management and Budget uses scoring to determine the amounts to be recognized in the budget when an agency signs a contract or enters into a lease. Privatized military housing projects are scored by the Office of Management and Budget at inception to determine the amount that must be included in the federal budget for the project.

[61]Office of Management and Budget, *Scoring DOD's Military Housing Privatization Initiatives*, Director Franklin D. Raines to the Secretary of Defense (June 25, 1997).

liability corporation to be scored as government activity.[62] Some military department and developer officials have expressed concern with the uncertainties surrounding future scoring. Specifically, military department officials and developers are concerned that the reversion to traditional scoring will affect any plans for obtaining mid-term loans and any potential expansions or other changes to existing projects. Office of Management and Budget officials stated that any future federal government contributions to privatized housing projects in the form of direct loans or loan guarantees will be fully scored at the value of the loan or loan guarantee.

Privatized Housing Projects Have Various Options to Mitigate Financial Challenges

Military department and developer officials have identified various options to address financial challenges such as those previously discussed in this report. These include actions to increase revenues, actions to reduce expenses, and extraordinary measures to improve project financial conditions. As the project manager, the developer may act unilaterally in some cases, and other actions may require approval from the military department, coordination with ASD (EI&E), or notification to the Office of Management and Budget. Although these actions may improve a project's financial condition, there are limitations, such as the potential to reduce tenant satisfaction and therefore occupancy levels, or costs to the government. The extent to which any of these options will be sufficient to address a particular project's financial challenges depends on the degree of the financial challenge and the effectiveness of the option. For example, a project may seek to raise revenue by advertising to tenants to increase occupancy, but the response may be insufficient. Likewise, a project may engage in a financial restructuring to return the project to a healthy financial footing, but ongoing low occupancy or unexpectedly high expenses may continue to challenge the project financially.

Actions to Increase Revenue

Developers and military departments cited several options for increasing project revenues, including the following examples:

[62]Office of Management and Budget, *Guidance on Use of Limited Liability Partnerships and Corporations in Military Housing*, Director Joshua B. Bolten to the Secretary of Defense (Aug. 2, 2005).

Renting to tenants other than active-duty servicemembers: The military departments have the option to increase project revenues by allowing projects to rent to tenants other than active-duty servicemembers. The Navy and Air Force have policies that determine the priority ordering of types of tenants to whom a project can rent. An Army official stated that the Army does not have a department policy, but allows projects to rent to tenants other than active-duty servicemembers based on project agreements. For example, a project may offer to rent to tenant groups in the following order: active-duty personnel, reserve-duty personnel, DOD civilian employees, military retirees, and general public tenants. As of June 2017, 33 of 35 Army privatized housing projects were renting to tenants other than active-duty servicemembers; 14 of 16 Navy and Marine Corps projects were renting to tenants other than active-duty servicemembers; and 28 of 32 Air Force projects were renting to tenants other than active-duty servicemembers. While renting to tenants other than active-duty servicemembers can increase revenue, the usefulness of this action is limited when a project is already operating at a high rate of occupancy or when additional demand is limited.

Other steps to increase occupancy: Developers can take other actions to increase project occupancy, to include increased advertising, promotions, or offering rent concessions. While these actions can increase occupancy, advertising adds costs to project operations, and rent concessions lower the per-unit revenue earned for the project. Figure 2 shows an advertisement by a privatized housing project seeking tenants outside of Naval Station Norfolk in Virginia.

Figure 2: Advertisement Seeking Tenants for Privatized Housing

Source: GAO. | GAO-18-218

Charging fees for services: Developers stated that they have considered charging fees for services that had previously been provided free of charge—such as community center rentals and pet fees—as another means of increasing project revenue. However, a developer's ability to charge fees varies based on project agreements and military department policies. Developers also need to consider potentially negative effects on tenant satisfaction.

Actions to Reduce Expenses

Developers and military departments cited several options for reducing project expenses, including the following examples:

Reducing or eliminating services: Projects can reduce or eliminate project services as a means of reducing operating expenses. Officials have taken these steps at certain Army, Navy, and Air Force projects. For example, Navy officials told us that the developer cut portions of the landscaping program at the Navy's Midwest project in Illinois, Indiana, and Tennessee and eliminated one 24-hour service desk at the Navy's Hampton Roads

Unaccompanied Housing project in Virginia in order to reduce expenses.[63] While these actions reduce operating expenses, providing reduced or fewer services may make a project less marketable or desirable to tenants and can lead to declines in tenant satisfaction and occupancy.

Deferring routine maintenance: In response to financial distress, projects can curtail routine maintenance to realize savings. For example, when Nellis Air Force Base in Nevada was facing cash flow challenges, officials told us that the project curtailed its preventive maintenance program that includes the inspection and repair of heating, ventilation, and air conditioning systems; water heaters; plumbing and plumbing fixtures; roofs; and carpeting. These expense-saving measures help operating costs in the near term, but deferring maintenance can reduce the quality of the housing, reduce tenant satisfaction, and increase expenses over time by reducing the effective life of the items not being maintained.

Delaying sustainment: Another option to reduce project expenses is to delay certain sustainment actions. At the Army's Fort Knox project in Kentucky, officials stated that the sustainment plan initially included the demolition and rebuild of each unit or full renovation of historic units over the 50-year project lease; however, they no longer project that there will be funds to complete those improvements. Instead of full rebuilds, officials stated that they expect to conduct piecemeal renovations. Over time, deferred sustainment can lead to reduced housing quality, in turn reducing occupancy levels and tenant satisfaction, and thereby reducing project revenues.

Extraordinary Measures

Developers and the military departments can also take various extraordinary measures to improve the financial condition of a project. Extraordinary measures are options that can alter project agreements or project financial arrangements with the military department. These options may require approval from the military department, coordination with ASD (EI&E), or notification to the Office of Management and Budget. Examples of such actions include the following:

[63]The Navy's Midwest project comprises Naval Station Great Lakes, Illinois; Naval Hospital Great Lakes, Illinois; Fort Sheridan, Illinois; Naval Air Station Glenview, Illinois; Naval Surface Warfare Center Crane, Indiana; and Naval Support Activity Mid-South, Millington, Tennessee.

Retaining and renting excess units: Projects can earn additional revenue by retaining and renting units that were originally slated for demolition. Some project plans included the transfer of existing housing units, deemed in excess of project needs, to the developer with the intention of demolishing them. For retaining and renting excess units to be an option, a project must have some excess units slated for demolition and sufficient demand for their rental.

Reducing project scope: Projects may reduce the scope of planned work to reduce potential expenditures or improve the project's financial state. Reductions in scope may be in the form of the number of units to be built, renovated, or demolished. For example, following the inactivation of a brigade combat team at Fort Knox in Kentucky, the project made plans to eliminate 280 units due to changes in servicemember housing needs from when the project originally started construction.

Deferring fees: Developers can defer project fees due to them, such as fees for construction or management services, so that more funds are available for other project needs. Developers agreed to defer fees for several Navy and Air Force projects as a means to ensure adequate funding for the completion of project construction. Projects can defer fees to meet shortfalls in project funding, but the deferral can place additional financial strain on a project, as funds later must be used to repay the deferred fees.

Making additional investment contributions: Developers can make additional financial investments in the project to cover underfunded project expenses. For example, Air Force officials stated that developers have made additional financial investments at the Robins Air Force Base I project in Georgia to ensure that the project had sufficient funds to make debt payments. According to officials, the Air Force agreed to the additional investment contributions on the basis that they be repaid from any future excess cash flows.

Returning assets: In some instances, project assets can cost the developer more than anticipated due to the expenses necessary to maintain the asset. To alleviate the resulting financial challenges, projects can transfer ownership of the assets back to the military departments. For example, the Air Force took back five historic units from the Robins II project in Georgia that, according to officials, were not financially viable within the project and that the Air Force wanted for purposes other than housing. When assets are returned to a military department, the military department may have to begin budgeting for their costs through its annual budgeting process.

Transferring assets: The military department can transfer assets to a project that developers can sell to fund projects. For example, the Navy transferred land and units to the Navy's Midwest project with the intention that the developer would sell the land and units to supplement project funding.[64] Asset sales can be unreliable funding sources if assets sell for less than the project expected.

Financial restructurings: Military departments can seek to financially restructure projects to improve their financial condition. This process requires the military departments to renegotiate project agreements with the developer to improve financial condition. For example, the Air Force recently completed financial restructurings of the Nellis Air Force Base project in Nevada and the Air Combat Command Group II project, which comprises Davis-Monthan Air Force Base in Arizona and Holloman Air Force Base in New Mexico. Air Force and developer officials stated that the Nellis Air Force Base project began to have problems making debt payments because of declines in basic allowance for housing payments associated with falling local rental market prices. For Nellis, the Air Force and the developer negotiated a financial restructuring whereby the Air Force reduced the interest rate on the government's loan to the project and extended the loan's maturity date. The Air Force also gave the developer an additional portion of project profits. In exchange, the developer agreed to forgive an outstanding balance of payments due to them.

An ASD (EI&E) official stated that financial restructuring agreements may require notification to the Office of Management and Budget, which scores changes to privatized military housing projects. Restructurings can provide relief to projects that are facing imminent default or longer-term sustainment funding shortfalls, but they can also add financial costs to the military department. The ability to financially restructure also may be limited by the willingness of the developer to give concessions during negotiations and the ability to obtain the approvals necessary to complete the restructure.

[64]The Navy's Midwest project comprises Naval Station Great Lakes, Illinois; Naval Hospital Great Lakes, Illinois; Fort Sheridan, Illinois; Naval Air Station Glenview, Illinois; Naval Surface Warfare Center Crane, Indiana; and Naval Support Activity Mid-South, Millington, Tennessee.

DOD Has Not Defined When Project Changes Require Advance Notice or Defined Risk Tolerance Levels for Not Achieving Housing Goals

DOD has not clearly defined in its policy the circumstances in which ASD (EI&E), as the DOD-wide housing program manager, should receive advance notice of changes to address financial challenges in privatized military housing projects. In addition, DOD has not defined its risk tolerance levels for achieving its goal of providing quality housing to servicemembers that reflects community living standards—in particular, its tolerance for declining levels of funding for future sustainment that can pose a risk to this goal.

The Military Departments Have Varied Understandings of When Privatized Military Housing Project Changes Require Notification

The military departments have varied understandings of what changes to privatizing housing projects require notification to ASD (EI&E)—DOD's program manager for privatized housing. Military department officials provided somewhat differing explanations when asked about the types of project changes that require notification to ASD (EI&E). Specifically:

- Army officials stated that the Army provides notice any time there is a planned use of or change to a project involving privatized military housing authorities related to government loans and loan guarantees, the leasing of housing units, or government investments in privatized housing projects, as well as any action that requires congressional notification. The Army also notifies the office if a project's number of units is expanded relative to its approved plan.
- Navy officials stated that they provide notice any time there is an action that requires congressional notification, any time there are project changes with a potential effect on military housing privatization authorities, any time new projects or project phases are considered, and any changes to a project's previously approved scope, as well as any time ASD (EI&E) requests notification.
- Air Force officials stated that notification is required when the military department makes a material change to a project that has a financial

or scope effect relative to the details that were originally approved. Officials added that any project changes that require approval from the Office of Management and Budget would require ASD (EI&E) concurrence.

Under current DOD housing policy, ASD (EI&E) is required to notify the Office of Management and Budget of any significant changes to privatized housing projects that may require scoring consideration.[65] However, DOD policy does not establish the circumstances in which the military departments should notify ASD (EI&E) of significant project changes, and it does not define which project changes qualify as significant. DOD guidance requires ASD (EI&E) to provide guidance and general procedures relating to housing privatization. An ASD (EI&E) official also told us that the military departments are providing notification of project changes based on limited guidance, and that ASD (EI&E) is conducting oversight on a case-by-case basis. Moreover, Office of Management and Budget officials stated that they will analyze project changes to determine whether an action would constitute a project expansion significant enough to require scoring.

Standards for Internal Control in the Federal Government states that management should develop policies that address the entity's objective to achieve an effective internal control system. In addition, management should obtain and internally communicate the necessary quality information to achieve the entity's objectives, while communicating quality information down and across reporting lines to enable personnel to perform key roles. Moreover, the standards state that the oversight body receives quality information that flows up from the reporting lines from management and personnel that is necessary for effective oversight of internal control.[66] However, DOD's guidance does not clearly define the types of project changes for which ASD (EI&E) requires prior notification from the military departments, which could result in ASD (EI&E) not being notified of project changes. ASD (EI&E) has draft guidance on oversight and management of privatized military housing, which would define the circumstances under which military departments should notify ASD (EI&E) of project changes, but officials stated that they have not established a time frame for issuing this policy. An ASD (EI&E) official stated that the policy is being coordinated with the military departments,

[65] DOD Instruction 4165.63 (July 21, 2008), and DOD Manual 4165.63-M (Oct. 28, 2010).

[66] GAO-14-704G.

and this has resulted in delays to its issuance. Without issuing guidance to clearly define and communicate to the military departments the conditions that require notification, the military departments will not be able to consistently fulfill their responsibilities and ASD (EI&E) will not be able to completely fulfill its oversight function.

DOD Has Not Defined Its Tolerance for Risk to Privatized Housing Goal

Office of Management and Budget guidance on the preparation, submission, and execution of the federal budget suggests that public-private partnerships such as privatized military housing projects contain some elements of risk to the government.[67] For example, the projects are frequently constructed on government land and they include government financing in the form of direct investments or direct loans. However, the military departments have not defined their risk tolerance levels for privatized housing relative to the program's objective of providing quality housing that reflects community living standards. Specifically, the Army and Navy have not identified the level of risk they are willing to accept in their ability to fund future sustainment. Army officials stated that the Army is not responsible for taking any actions to restore a project's financial condition. Navy officials stated that they do not use a risk model, and that one is not required by DOD. The Air Force has not formally defined its risk tolerance levels for future sustainment, but it has identified the circumstances in which projected sustainment funding deficits will cause it to take extraordinary measures—specifically, to seek a financial restructuring of the project. For example, if future planned maintenance is funded at less than 85 percent of estimated needs within the next 5-year period, the Air Force may seek a financial restructuring, according to Air Force officials. Likewise, according to Air Force officials, if planned major renovations and rebuilding are funded at below 30 percent of estimated needs, the Air Force will seek a financial restructuring.

[67]Office of Management and Budget, Office of Management and Budget Circular No. A-11, *Preparation, Submission, and Execution of the Budget*, Washington, D.C. (July 2017). The circular lists the following illustrative criteria to indicate ways in which public-private partnership projects can be less governmental: there is no provision of government financing and no explicit government guarantee of third-party financing; risks incident to ownership of the asset remain with the lessor unless the government was at fault for the losses; the asset is a general purpose asset rather than being for a special purpose of the government; there is a private-sector market for the asset; or the project is not constructed on government land.

Standards for Internal Control in the Federal Government states that agencies need to define risk tolerance relative to their program objectives.[68] Risk tolerance is the acceptable level of variation in performance relative to the achievement of objectives. However, DOD has not required the military departments to define their risk tolerances regarding the future sustainability of the projects. ASD (EI&E) officials told us that they are considering establishing parameters for risk tolerance for the military departments, but have not yet done so. Officials also noted that DOD had been focused on the initial development periods of the privatized housing projects, whereas it is now shifting focus to sustainment as the projects have moved from the initial development stage. Given this focus on sustainment, if the military departments do not define their risk tolerances regarding the future sustainability of their privatized housing projects, they will lack a consistent basis on which to determine when the risks to achieving their objectives require responses, and the nature of those responses.

Conclusions

DOD's ability to maintain quality housing is critical, because housing can affect retention, readiness, and servicemembers' quality of life. Since Congress provided the department with authorities to do so, DOD has worked with private developers to improve the quality of housing available on military installations. The military departments regularly review the financial condition of their privatized housing projects, but they calculate a basic measure of current financial health—the debt coverage ratio—differently among their projects, which limits the ability of ASD (EI&E), and in turn Congress, to compare project financial health based on this measure without additional information to give the data full context. DOD has also previously reported such information for differing time periods in different reports to Congress, further limiting the data's usefulness, and has not issued revised guidance on privatized housing to help ensure consistent reporting. The military departments also vary in the extent and manner in which they oversee measures of future sustainment of their privatized housing projects. DOD has not reported measures of future sustainment to Congress, or issued a report on the financial condition of privatized housing projects, since the report covering fiscal year 2014. Without consistent and up-to-date information on the financial condition of

[68] GAO-14-704G.

projects, DOD and Congress will not be able to conduct informed and effective oversight of the projects.

The military departments have identified the reductions in basic allowance for housing as one of the various challenges affecting the financial condition of privatized housing projects. At the request of ASD (EI&E), the military departments have provided analysis on the effects of the reductions on their portfolios, but they have not been required to fully assess the significance of the effects of the reductions on the future sustainment of each of their projects, or identified specific actions to respond to the reductions, as detailed by federal internal control standards related to risk assessment. Without complete assessment of the risks of the reductions in the basic allowance for housing on each project, and developing any appropriate courses of action, DOD and the military departments will not be able to know when to take action to address deficits in the funding of long-term sustainment accounts that could lead to diminishment in the quality of military housing. Additionally, DOD and Congress will not be fully informed of the risks and possible effects before making decisions that affect all of the privatized housing projects—such as approving any further reductions in the basic allowance for housing.

The military departments have various options for attempting to improve the financial condition of their privatized housing projects, but some of these options require prior notice to ASD (EI&E). The absence of clearly defined requirements as to when this office should be notified of project changes to address financial challenges has led to varied understandings among the military departments about when notification should occur. Without a clear identification of when ASD (EI&E) should be notified of project changes, the military departments will not have consistent and clear guidance as to when this office needs to be informed prior to an action being taken by a military department regarding its privatized housing projects, and thus, the oversight office may not be fully informed on the projects it intends to oversee. In addition, DOD has not required the military departments to define their tolerances for risk to the goal of providing quality housing to servicemembers in line with community standards, including its ability to fund future sustainment needs. Without doing so, DOD will not have key information needed to determine when the risks to achieving their objectives require responses, or to determine the nature of the responses.

Recommendations for Executive Action

We are making a total of eight recommendations to the Secretary of Defense and the Assistant Secretary of Defense for Energy, Installations, and Environment. The Secretary of Defense should ensure that:

The Assistant Secretary of Defense for Energy, Installations, and Environment provides additional contextual information in future reports to Congress on privatized military housing to identify any differences in the calculation of debt coverage ratios and the effect of these differences on their comparability. (Recommendation 1)

The Assistant Secretary of Defense for Energy, Installations, and Environment revises its existing guidance on privatized housing to ensure that financial data on privatized military housing projects reported to Congress, such as debt coverage ratios, are consistent and comparable in terms of the time periods of the data collected. (Recommendation 2)

The Assistant Secretary of Defense for Energy, Installations, and Environment revises its guidance on privatized military housing to include a requirement that the military departments incorporate measures of future sustainment into their assessments of privatized housing projects. (Recommendation 3)

The Assistant Secretary of Defense for Energy, Installations, and Environment takes steps to resume issuing required reports to Congress on the financial condition of privatized housing in a timely manner. (Recommendation 4)

The Assistant Secretary of Defense for Energy, Installations, and Environment reports financial information on future sustainment of each privatized housing project in its reports to Congress. (Recommendation 5)

The Assistant Secretary of Defense for Energy, Installations, and Environment provides guidance directing the military departments to assess the significance of the specific risks to individual privatized housing projects resulting from the reductions in the basic allowance for housing and identify courses of action to respond to any risks based on their significance. (Recommendation 6)

The Assistant Secretary of Defense for Energy, Installations, and Environment finalizes guidance in a timely manner that clearly defines the circumstances in which the military departments should provide notification of project changes and which types of project changes require prior notification or prior approval. (Recommendation 7)

The Assistant Secretary of Defense for Energy, Installations, and Environment revises its guidance on privatized military housing to require the military departments to define their risk tolerances regarding the future sustainability of their privatized housing projects. (Recommendation 8)

Agency Comments

We provided a draft of this report for review and comment to DOD and the Office of Management and Budget. We initially made our recommendations to the Assistant Secretary of Defense for Energy, Installations, and Environment. We have updated our recommendations to also include the Secretary of Defense. In written comments, DOD concurred with each of our recommendations and identified actions it plans to take to implement them. DOD's comments are reprinted in their entirety in appendix III. DOD and the Office of Management and Budget also provided technical comments, which we incorporated as appropriate.

We are sending copies of this report to the appropriate congressional committees, the Secretary of Defense, and the Office of Management and Budget. In addition, the report is available at no charge on our website at http://www.gao.gov.

If you or your staff have any questions about this report, please contact Brian Lepore at (202) 512-4523 or leporeb@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report. GAO staff who made key contributions to this report are listed in appendix IV.

Brian J. Lepore
Director, Defense Capabilities and Management

Appendix I: Objectives, Scope, and Methodology

Senate Report 114-255 accompanying a bill for the National Defense Authorization Act for Fiscal Year 2017 included a provision for us to assess the solvency of each privatized military housing project in the United States and the effect of recent changes in basic allowance for housing on long-term project sustainability. This report examines the extent to which the Department of Defense (DOD) has (1) assessed and reported the financial condition of each privatized housing project; (2) assessed the effects of recent reductions in the basic allowance for housing on privatized housing, and identified any other challenges and options to address challenges; and (3) defined notification requirements for project changes and risk tolerances relative to privatized housing goals.

For all objectives, we scoped our review to include all privatized housing projects in each military department. We excluded privatized temporary lodging because its financial structure is substantially different than all other privatized housing projects. We reviewed relevant policies and collected information by interviewing officials from the Office of the Secretary of Defense (the Office of the Assistant Secretary of Defense for Energy, Installations, and Environment); the Army (Office of the Assistant Secretary of the Army for Installations, Energy, and Environment, and the Office of the Assistant Chief of Staff for Installation Management); the Navy (Office of the Deputy Assistant Secretary of the Navy for Installations and Facilities, the Commander, Navy Installations Command, and the Naval Facilities Engineering Command); the Marine Corps (Marine Corps Installations Command); and the Air Force (Office of the Deputy Assistant Secretary of the Air Force for Installations, and the Air Force Civil Engineering Center).

Additionally, we met with the five leading developers of privatized housing projects: Balfour Beatty, Corvias, Lend Lease, Lincoln Military Housing, and Hunt Companies. We also visited a non-generalizable sample of five privatized housing projects to interview on-site military department officials and tour the housing. For this sample, we selected one or two projects from each of the military departments, emphasizing projects that had identified financial difficulties or were located in close proximity to military department oversight offices. We made site visits to the following areas and installations: Norfolk, Virginia, where we met with officials of the Naval Facilities Engineering Command and visited the Homeport Hampton Roads and Mid-Atlantic Military Family Communities privatized housing projects; San Antonio, Texas, where we met with officials at the Air Force Civil Engineer Center; Las Vegas, Nevada, where we met with officials and visited the privatized housing project at Nellis Air Force Base; Fort Knox, Kentucky, where we met with officials and visited the privatized housing project at the Army's Fort Knox; and Fort Meade, Maryland, where we met with officials and visited the privatized housing project at Fort Meade.

To determine the extent to which DOD has assessed and reported the financial condition of each privatized housing project, we reviewed DOD guidance on the oversight and management of privatized military housing.[1] We also reviewed documentation used by each military department to oversee the financial condition of each of their privatized housing projects, and each of their portfolios as a whole through portfolio-wide oversight reports, monthly and quarterly reports on each privatized housing project, and audited project financial statements from fiscal years 2013 to 2016. We reviewed DOD's fiscal year 2013 and 2014 annual reports to Congress on privatized housing, as well as data for privatized housing projects from fiscal years 2013 through 2016.[2] We also met with officials involved in the oversight and management of privatized housing in the Office of the Assistant Secretary of Defense for Energy, Installations, and Environment (ASD (EI&E)), and each of the military departments to discuss their oversight and management of the financial condition of privatized housing projects. Additionally, we requested data for each privatized housing project, including audited financial statements, and examined the differences among and within the military departments in determining the solvency of their projects. For each military department, we assessed the number of projects doing financially well and those not doing financially well through correspondence with knowledgeable officials at each military department and found those department-level numbers sufficiently reliable to report the number of projects in each financial category. We compared DOD's and the military departments' actions to assess and report on the financial condition of

[1]DOD Instruction 4165.63, *DOD Housing* (July 21, 2008) (Change1, Nov. 20, 2017).

[2]We selected this time frame because at the time we initiated our work, fiscal year 2013 was the last year for which DOD had issued a report to Congress on the financial condition of privatized military housing projects, and fiscal year 2016 was the most recent full year available. In October 2017, after we had developed the scope of our work and completed most of our analysis, DOD issued the fiscal year 2014 report to Congress.

their privatized housing projects with DOD's housing policy[3] and with standards for quality information in *Standards for Internal Control in the Federal Government* to determine whether DOD has fully assessed and reported the financial condition of each project.[4]

To determine the extent to which DOD has assessed the effects of recent reductions in the basic allowance for housing on privatized housing and identified any other challenges and options to address those challenges, we reviewed DOD guidance on applying reductions in basic allowance for housing to privatized military housing and other DOD documentation on the reductions in basic allowance for housing payments. Specifically, we reviewed the military departments' reports on the projected effects of the reductions in the basic allowance for housing on their portfolios and quarterly project oversight reports from fiscal years 2016 and 2017. Additionally, we interviewed officials at the Defense Travel Management Office for information on the basic allowance for housing calculations and military department officials for their perspectives on the reductions in basic allowance for housing. We compared the military department reports on the projected effects of the reductions in basic allowance for housing with standards for risk assessment in *Standards for Internal Control in the Federal Government* to determine whether DOD has fully assessed the effects of the reductions.[5] We determined challenges identified by DOD and the military departments and options to address challenges through interviews with ASD (EI&E) officials, officials from each military department involved with privatized housing, and officials at select installations involved in privatized housing. We also met with officials of five leading privatized housing developers for their perspectives on challenges to their privatized housing and options to address them. Additionally, we reviewed quarterly project oversight reports to identify challenges associated with privatized housing. We reported examples of challenges that were identified by at least two of the three military departments. Additionally, we assessed the number of projects renting to tenants other than active-duty servicemembers by obtaining information from each military department and found those department-level numbers sufficiently reliable to report the number of projects that were renting to these tenants. We reviewed quarterly project

[3]DOD Instruction 4165.63, *DOD Housing* (July 21, 2008).

[4]GAO, *Standards for Internal Control in the Federal Government*, GAO-14-704G (Washington, D.C.: Sept. 2014).

[5]GAO-14-704G.

oversight reports to identify the options for addressing challenges, and DOD's policy guidance on privatized housing responsibilities to determine the level of authority needed for the options.[6]

To determine the extent to which DOD has defined notification requirements for project changes and risk tolerances relative to privatized housing goals, we reviewed DOD guidance on oversight and management of privatized military housing, interviewed DOD and developer officials responsible for privatized housing, and reviewed DOD documentation. Specifically, we reviewed DOD housing policies and guidance, reviewed military department guidance on overseeing privatized housing, and interviewed military department officials familiar with notification processes for changes to privatized housing projects and approaches to managing risks to privatized housing projects. We also interviewed officials in the Office of Management and Budget familiar with privatized military housing. We compared DOD's policy guidance on privatized housing responsibilities with standards related to internal communication in *Standards for Internal Control in the Federal Government* to determine the level of notification needed.[7] We also compared the extent to which DOD has defined risk tolerance for privatized housing with federal internal control standards related to risk assessment.

We conducted this performance audit from December 2016 to March 2018 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

[6]DOD Instruction 4165.63, *DOD Housing* (July 21, 2008).

[7]GAO-14-704G.

Appendix II: Complete Listing of the Department of Defense's Privatized Military Housing Projects as of October 2017

The following is a complete listing of the Department of Defense's 82 privatized military housing projects, as of October 2017. The projects can consist of one or multiple installations.

Table 1: Privatized Military Housing Projects as of October 2017

Military department	Project name	Installations/Location
Army	APG Housing LLC	Aberdeen Proving Ground, Aberdeen, Md.
Army	Carlisle/Picatinny Family Housing LP	Carlisle Barracks, Carlisle, Pa. / Picatinny Arsenal, Morris County, N.J.
Army	Fort Belvoir Residential Communities LLC	Fort Belvoir, Fairfax County, Va.
Army	Fort Benning Family Communities LLC	Fort Benning, Columbus, Ga.
Army	Fort Bliss / White Sands Missile Range LP	Fort Bliss, El Paso, Tex. / White Sands Missile Range, Dona Ana County, N.Mex.
Army	Bragg Communities LLC[a]	Fort Bragg, Cumberland County, N.C.
Army	Campbell Crossings LLC	Fort Campbell, Montgomery County, Tenn.
Army	Fort Carson Family Housing LLC	Fort Carson, El Paso County, Colo.
Army	Fort Detrick/Walter Reed Army Medical Center Family Housing LLC	Fort Detrick, Frederick, Md.
Army	Fort Drum Mountain Communities LLC[b]	Fort Drum, Jefferson County, N.Y.
Army	Fort Eustis/ Fort Story Housing LLC	Fort Eustis, Newport News, Va. / Fort Story, Virginia Beach, Va.
Army	Fort Gordon Housing LLC	Fort Gordon, Richmond County, Ga.
Army	Fort Hamilton Housing LLC	Fort Hamilton, Brooklyn, N.Y.
Army	Fort Hood Family Housing LP	Fort Hood, Killeen, Tex.
Army	Fort Huachuca – YPG Communities LLC	Fort Huachuca, Cochise County, Ariz. / Yuma Proving Ground, Yuma, Ariz.
Army	Fort Irwin Land LLC[c]	Fort Irwin, San Bernardino County, Calif.
Army	Fort Jackson Housing LLC	Fort Jackson, Columbia, S.C.
Army	Knox Hills LLC	Fort Knox, Ky.
Army	Fort Leavenworth Frontier Heritage Communities LLC	Fort Leavenworth, Leavenworth County, Kans.

Military department	Project name	Installations/Location
Army	Fort Lee Commonwealth Communities LLC	Fort Lee, Prince George County, Va.
Army	Leonard Wood Family Communities LLC	Fort Leonard Wood, Pulaski County, Mo.
Army	Lewis McChord Communities LLC	Joint Base Lewis McChord, Tacoma, Wash.
Army	Meade Communities LLC	Fort Meade, Anne Arundel County, Md.
Army	Polk Communities LLC	Fort Polk, La.
Army	Riley Communities LLC	Fort Riley, Junction City, Kans.
Army	Rucker Communities LLC	Fort Rucker, Dale County, Ala.
Army	Fort Sam Houston Family Housing LP	Joint Base San Antonio, San Antonio, Tex.
Army	Sill Communities LLC	Fort Sill, Lawton, Okla.
Army	Stewart Hunter Housing LLC[d]	Fort Stewart, Ga.
Army	North Haven Communities LLC	Fort Wainwright, Fort Greely, Fairbanks, Alas.
Army	Island Palm Communities LLC	Fort Shafter, Hawaii; Schofield Barracks, Hawaii.
Army	Monterey Bay Military Housing LLC	Presidio of Monterey, Naval Postgraduate School, Monterey, Calif.
Army	Redstone Communities LLC	Redstone Arsenal, Madison County, Ala.
Army	West Point Housing LLC	West Point, N.Y.
Army	Reece Crossings	Anne Arundel County, Md.
Navy	Camp Lejeune, Cherry Point, and Stewart (CLCPS)	Marine Corps Base Camp Lejeune, N.C.; Marine Corps Air Station Cherry Point, N.C.; Marine Corps Air Station New River, N.C.; Stewart Air National Guard Base, N.Y.; Marine Corps Air Station Beaufort, S.C.; Marine Corps Recruit Depot Parris Island, S.C.; Beaufort Naval Hospital, S.C.
Navy	Camp Pendleton (CP1)	Marine Corps Base Camp Pendleton, Calif.
Navy	Camp Pendleton and Quantico Housing (CPQH)	Marine Corps Base Camp Pendleton, Calif.; Marine Corps Base Quantico, Va.; Marine Corps Recruit Depot San Diego, Calif.; Marine Corps Mountain Warfare Training Center Bridgeport, Calif.; Marine Corps Air Station Yuma, Ariz.; Marine Corps Mobilization Command Kansas City, Mo.; Marine Corps Air Ground Combat Center 29 Palms, Calif.; Marine Corps Logistics Base Albany, Ga.
Navy	Hampton Roads Unaccompanied Housing	Naval Station Norfolk, Va.; Naval Support Activity Hampton Roads, Newport News, Va.

Military department	Project name	Installations/Location
Navy	Hawaii	Joint Base Pearl Harbor-Hickam; Joint Base Pearl Harbor-Hickam, Naval Shipyard Pearl Harbor; Pacific Missile Range Facility Barking Sands, Kauai; Marine Corps Base Kaneohe Bay.
Navy	Kingsville	Naval Air Station Kingsville, Tex.
Navy	Mid-Atlantic	Hampton Roads (Naval Station Norfolk, Va.; Joint Expeditionary Base Little Creek-Fort Story, Va.; Naval Air Station Oceana/Dam Neck, Va.; Naval Support Activity Hampton Roads/Northwest Annex, Va.; Naval Weapons Station Yorktown, Va.; Naval Medical Center Portsmouth Naval Hospital, Va.) United States Naval Academy Annapolis, Md.; Naval Surface Warfare Center Dahlgren, Va.; Naval Surface Warfare Center Indian Head, Md.; Naval Air Station Patuxent River, Md.; Tingey House, Washington Navy Yard, D.C.; Marine Corps Base Camp Lejeune, N.C.; Naval Support Activity Mechanicsburg, Pa.
Navy	Midwest	Naval Station Great Lakes, Ill.; Naval Hospital Great Lakes, Ill.; Fort Sheridan, Ill.; Naval Air Station Glenview, Ill.; Naval Surface Warfare Center Crane, Ind.; Naval Support Activity Mid-South, Millington, Tenn.
Navy	New Orleans	Naval Air Station Joint Reserve Base New Orleans, La.
Navy	Northeast	Joint Base McGuire-Dix-Lakehurst, N.J.; Naval Submarine Base New London, Conn.; Naval Station Newport, R.I.; Naval Shipyard Portsmouth, N.H.; Naval Support Unit Saratoga Springs, N.Y.; Mitchel Complex Navy Recruiting District, N.Y.; Naval Weapons Station Earle, N.J.
Navy	Northwest	Naval Base Kitsap-Bangor, Wash.; Naval Base Kitsap-Keyport, Wash.; Naval Base Kitsap-Jackson Park, Wash.; Naval Station Kitsap-Bremerton, Wash.; Naval Air Station Whidbey, Wash.; Naval Station Everett, Wash.

Military department	Project name	Installations/Location
Navy	San Diego	Naval Station San Diego, Calif.; Naval Amphibious Base Coronado, Calif.; Naval Submarine Base San Diego, Calif.; Naval Command Control and Ocean Surveillance Center, San Diego, Calif.; Naval Medical Center, San Diego, Calif.; Marine Corps Air Station Miramar, Calif.; Naval Air Facility El Centro, Calif.; Naval Air Weapons Station China Lake, Calif.; Naval Support Facility Thurmont, Md.; Joint Base Anacostia-Bolling, Md.; Naval Support Activity Washington, D.C.; Naval Support Activity Bethesda, Md. Naval Air Station Lemoore, Calif.; Naval Base Ventura County, Calif.; Naval Weapons Station Seal Beach, Calif.; Naval Air Station Fallon, Nev.
Navy	San Diego Unaccompanied Housing	Naval Station San Diego, Calif.
Navy	South Texas	Naval Air Station Corpus Christi, Tex.; Naval Station Ingleside, Tex.
Navy	Southeast	Naval Air Station Pensacola, Fla.; Naval Air Station Whiting Field, Fla.; Naval Support Activity Panama City, Fla.; Joint Base Charleston, S.C.; Naval Station Mayport, Fla.; Naval Air Station Jacksonville, Fla.; Naval Submarine Base Kings Bay, Ga.; Naval Air Station Key West, Fla.; Naval Air Station Joint Reserve Base Ft Worth, Tex.; Naval Air Station Meridian, Miss.; Naval Construction Battalion Center Gulfport, Miss.
Air Force	Air Combat Command Group II	Holloman Air Force Base, N.Mex.; Davis-Monthan Air Force Base, Ariz.
Air Force	Air Combat Command Group III	Dyess Air Force Base, Tex.; Moody Air Force Base, Ga.
Air Force	Air Education and Training Command Group I	Altus Air Force Base, Okla.; Luke Air Force Base, Ariz.; Sheppard Air Force Base, Tex.; Tyndall Air Force Base, Fla.
Air Force	Air Education and Training Command Group II	Columbus Air Force Base, Miss.; Goodfellow Air Force Base, Tex.; Laughlin Air Force Base, Tex.; Maxwell Air Force Base, Ala.; Randolph Air Force Base, Tex.; Vance Air Force Base, Okla.

Military department	Project name	Installations/Location
Air Force	Air Force Academy	Colorado Springs, Colo.
Air Force	Air Mobility Command East	Andrews Air Force Base, Md.; MacDill Air Force Base, Fla.
Air Force	Air Mobility Command West	Fairchild Air Force Base, Wash.; Tinker Air Force Base, Okla.; Travis Air Force Base, Calif.
Air Force	Barksdale, Langley, and Bolling (BLB)	Barksdale Air Force Base, La.; Langley Air Force Base, Va.; Bolling Air Force Base, D.C.
Air Force	Buckley Air Force Base	Aurora, Colo.
Air Force	Continental Group	Edwards Air Force Base, Calif.; Eglin Air Force Base, Fla.; Eielson Air Force Base, Alas.; Hurlburt Air Force Base, Fla.; McConnell Air Force Base, Kans.; Seymour Johnson Air Force Base, N.C.
Air Force	Dover Air Force Base	Dover, Del.
Air Force	Dyess Air Force Base I	Taylor County, Tex.
Air Force	Falcon Group	Hanscom Air Force Base, Mass.; Little Rock Air Force Base, Ark.; Moody Air Force Base, Ga.; Patrick Air Force Base, Fla.
Air Force	Hill Air Force Base	Northern Utah.
Air Force	Joint Base Pearl Harbor-Hickam	Pearl Harbor, Hawaii.
Air Force	Joint Base Elmendorf–Richardson I	Anchorage, Alas.
Air Force	Joint Base Elmendorf–Richardson II	Anchorage, Alas.
Air Force	Joint Base Elmendorf–Richardson III	Anchorage, Alas.
Air Force	Joint Base McGuire-Dix-Lakehurst	Burlington County, N.J.
Air Force	Kirtland Air Force Base	Bernalillo County, N.Mex.
Air Force	Lackland Air Force Base	San Antonio, Tex.
Air Force	Nellis Air Force Base	Las Vegas, Nev.
Air Force	Northern Group	Cannon Air Force Base, N.Mex.; Cavalier Air Force Base, N.Dak.; Ellsworth Air Force Base, S.Dak.; Grand Forks Air Force Base, N.Dak.; Minot Air Force Base, N.Dak.; Mountain Home Air Force Base, Idaho.
Air Force	Offutt Air Force Base	Sarpy County, Nebr.
Air Force	Robins Air Force Base I	Warner Robins, Ga.

Military department	Project name	Installations/Location
Air Force	Robins Air Force Base II	Warner Robins, Ga.
Air Force	Scott Air Force Base	St. Clair County, Ill.
Air Force	Southern Group	Arnold Air Force Base, Tenn.; Charleston Air Force Base, S.C.; Keesler Air Force Base, Miss.; Shaw Air Force Base, S.C.
Air Force	Tri-Group	Los Angeles Air Force Base, Calif.; Peterson Air Force Base, Colo.; Schriever Air Force Base, Colo.
Air Force	Vandenberg Air Force Base	Santa Barbara County, Calif.
Air Force	Western Group	Beale Air Force Base, Calif.; Francis E. Warren Air Force Base, Wyo.; Malmstrom Air Force Base, Mont.; Whiteman Air Force Base, Mo.
Air Force	Wright-Patterson Air Force Base	Green County, Ohio.

Source: GAO analysis of Department of Defense information. | GAO-18-218

[a]The Fort Bragg project includes unaccompanied housing.

[b]The Fort Drum project includes unaccompanied housing.

[c]The Fort Irwin project includes unaccompanied housing.

[d]The Fort Stewart project includes unaccompanied housing.

Appendix III: Comments from the Department of Defense

THE ASSISTANT SECRETARY OF DEFENSE
3400 DEFENSE PENTAGON
WASHINGTON, DC 20301-3400

ENERGY, INSTALLATIONS AND ENVIRONMENT

FEB 22 2018

Mr. Brian Lepore
Director, Defense Capabilities and Management
U.S. Government Accountability Office
441 G Street, N.W.
Washington, DC 20548

Dear Mr. Lepore:

This is the Department of Defense (DoD) response to the Government Accountability Office (GAO) Draft Report, GAO-18-218, "Military Housing Privatization: DOD Should Take Steps to Improve Monitoring, Reporting, and Risk Assessment" dated January 19, 2018 (GAO Code 101298). Detailed comments on the report recommendations are enclosed.

Sincerely,

Lucian Niemeyer

Enclosure:
As stated

GAO DRAFT REPORT DATED JANUARY 19, 2018
GAO-18-218 (GAO CODE 101298)

"MILITARY HOUSING PRIVATIZATION: DOD SHOULD TAKE STEPS TO IMPROVE MONITORING, REPORTING, AND RISK ASSESSMENT"

DEPARTMENT OF DEFENSE COMMENTS TO THE GAO RECOMMENDATIONS

RECOMMENDATION 1: The GAO recommends that the Assistant Secretary of Defense for Energy, Installations, and Environment should provide additional contextual information in future reports to Congress on privatized military housing to identify any differences in the calculation of debt coverage ratios and the effect of these differences on their comparability.

DoD RESPONSE: Concur. The Assistant Secretary of Defense for Energy, Installations and Environment (ASD(EI&E)) will ensure that our future reports to Congress on housing privatized under the Military Housing Privatization Initiative (MHPI) include narrative to clarify that debt coverage ratios are calculated consistent with lender requirements which may vary slightly for each project, and to explain the effect of these differences on their comparability.

RECOMMENDATION 2: The GAO recommends that the Assistant Secretary of Defense for Energy, Installations, and Environment should revise its existing guidance on privatized housing to ensure that financial data on privatized military housing projects reported to Congress, such as debt coverage ratios, are consistent and comparable in terms of the time periods of the data collected.

DoD RESPONSE: Concur. The ASD(EI&E) will revise its reporting guidance to the Military Departments to ensure that financial data on housing privatization projects that is reported to Congress is consistent and comparable in terms of the time periods of the data collected, starting with the reporting period covering October 2016 through September 2017.

RECOMMENDATION 3: The GAO recommends that the Assistant Secretary of Defense for Energy, Installations, and Environment should revise its guidance on privatized military housing to include a requirement that the military departments incorporate measures of future sustainment into their assessments of privatized housing projects.

DoD RESPONSE: Concur. The ASD(EI&E) is working with the Military Departments to determine appropriate measures of future MHPI project sustainment and will revise its guidance to require the Military Departments to incorporate such measures of future sustainment into their assessment of privatized housing projects.

RECOMMENDATION 4: The GAO recommends that the Assistant Secretary of Defense for Energy, Installations, and Environment should take steps to resume issuing required reports to Congress on the financial condition of privatized housing in a timely manner.

DoD RESPONSE: Concur. The Department submitted its most recent Program Evaluation Report (PER) on the MHPI in October 2017. The ASD(EI&E) is working to further streamline the PER format and data collection process to ensure more timely future reporting.

RECOMMENDATION 5: The GAO recommends that the Assistant Secretary of Defense for Energy, Installations, and Environment should report financial information on future sustainment of each privatized housing project in its reports to Congress.

DoD RESPONSE: Concur. The ASD(EI&E) will ensure that financial information on future sustainment of each privatized housing project is included in the Department's PER submissions to Congress starting with the reporting period covering October 2016 through September 2017.

RECOMMENDATION 6: The GAO recommends that the Assistant Secretary of Defense for Energy, Installations, and Environment should provide guidance directing the military departments to assess the significance of the specific risks to individual privatized housing projects resulting from the reductions in the basic allowance for housing and identify courses of action to respond to any risks based on their significance.

DoD RESPONSE: Concur. The ASD(EI&E) will issue guidance directing the Military Departments to annually provide a report to the ASD(EI&E) outlining their assessment of the significance of the specific risks of the BAH changes to individual privatized housing projects and identifying courses of action to respond to any risks based on their significance. This requirement will build on guidance the ASD(EI&E) issued in August 2015, which directed the Military Departments to complete a thorough review of their privatized housing portfolios and report back on any effects of the Basic Allowance for Housing (BAH) changes on their portfolios, along with planned solutions.

RECOMMENDATION 7: The GAO recommends that the Assistant Secretary of Defense for Energy, Installations, and Environment should finalize guidance in a timely manner that clearly defines the circumstances in which the military departments should provide notification of project changes and which types of project changes require prior notification or prior approval.

DoD RESPONSE: Concur. The ASD(EI&E) has coordinated draft guidance with the Military Departments and expects to issue final guidance in fiscal year 2018.

RECOMMENDATION 8: The GAO recommends that the Assistant Secretary of Defense for Energy, Installations, and Environment should revise its guidance on privatized military housing to require the military departments to define their risk tolerances regarding the future sustainability of their privatized housing projects.

DoD RESPONSE: Concur. The ASD(EI&E) will revise its MHPI guidance to require the Military Departments to define their risk tolerances regarding the future sustainability of their privatized housing projects. The ASD(IE&E) recognizes that future sustainability risk tolerance is impacted by a number of factors, to include whether the MHPI project financing includes the use of federal credit facilities.

Text of Appendix III: Comments from the Department of Defense

Page 1

Mr. Brian Lepore

Director, Defense Capabilities and Management

U.S. Government Accountability Office 441 G Street, N.W.

Washington, DC 20548

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Appendix IV: GAO Contact and Staff Acknowledgments

GAO Contact

Brian J. Lepore, (202) 512-4523 or leporeb@gao.gov.

Staff Acknowledgments

In addition to the contact named above, Kristy Williams (Assistant Director), Tracy Barnes, Ronnie Bergman, Timothy Carr, Kelly Friedman, Simon Hirschfeld, Terence Lam, Amie Lesser, Jeffrey Love, Richard Powelson, Nancy Santucci, Mike Silver, and Cheryl Weissman made key contributions to this report.

Related GAO Products

Defense Infrastructure: Army Has a Process to Manage Litigation Costs for the Military Housing Privatization Initiative. GAO-14-327. Washington, D.C.: April 3, 2014.

Military Housing: Information on the Privatization of Unaccompanied Personnel Housing. GAO-14-313. Washington, D.C.: March 18, 2014.

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