

GOVERNMENT OF THE DISTRICT OF COLUMBIA
Office of the Inspector General

Inspector General



August 20, 2003

The Honorable Anthony A. Williams
Mayor
District of Columbia
John A. Wilson Building
1350 Pennsylvania Avenue, N.W., 6th Floor
Washington, D.C. 20004

Dear Mayor Williams:

The purpose of this Management Implication Report (MIR 03-A-03) is to inform you of the need for an analysis of alternatives to the District's Master Lease Contract and that management has agreed to consider alternatives. Although the specific issue of the Master Lease Program is not relative to all District managers, the concept of analyzing funding options for large procurements should always be considered to ensure that the District uses the most cost-effective funding mechanism.

The Master Lease Contract (the Contract) is currently in its third year and will terminate on March 30, 2004. The District awarded the contract in the amount of approximately \$75 million. The Office of Finance and Treasury (OFT) manages the contract and, at the onset of our review, was working on a Request for Proposal (RFP) with the objective of issuing a subsequent contract starting in fiscal year (FY) 2004. It is estimated that the new contract term could be 5 years, at a cost of as much as \$100 million. Given the increased economic strength of the District and the relatively low interest rates available in financial markets, OFT officials have agreed that before awarding the next contract, it would be timely and prudent to consider all available funding resources that could reduce costs.

During a review of invoices from the General Services Administration (GSA), it came to our attention that payments for equipment and supply items procured by District Government agencies were seriously overdue. We determined that the causes for late payments were varied and covered at least six District agencies.¹ It was during this review of overdue invoices that we became aware of the Master Lease Program (Program).

The Master Lease Program. The District began the Program in 1998 to provide financing for projects with short-term to intermediate-term useful lives. The program enables the District to improve its asset/liability management by matching the useful life of the asset being financed to the amortization of the liability (5 to 10 years). The District procures heavy equipment items

¹ MIR 03-A-04 will be issued shortly to address late payments to GSA.

under the Program, to include fire apparatus (trucks) and other emergency medical services equipment (ambulances); trucks and cranes used by the Department of Public Works; and vehicles used by the Metropolitan Police Department.²

Lease payment obligations are neither debt nor general obligations of the District, but they are payable from annual appropriations. As of June 25, 2003, the District financed approximately \$92 million of its capital equipment needs through the Program, and approximately \$61 million in principal was outstanding. During the year, the average interest rate used to finance equipment through the Program was 3.56 percent per annum, with payments to be made on a quarterly basis.

During our review of the Program, we found that the Contract was up for renewal. Further inquiries disclosed there were no official plans to conduct an analysis prior to award of the proposed contract to determine the most economical acquisition method. Additionally, our review of District procurement regulations disclosed that there was no requirement for such an analysis prior to contract award. We discussed this matter with OFT officials who expressed the belief that in 1997 an analysis of the contract financing methods was performed before the Master Lease Contract was awarded.

Financing Mechanism. The District government entered into a lease-purchase contract with Koch Financial Corporation (contractor) of Scottsdale, Arizona. The first contract for the Program was awarded in June 1998 for 3 years and a second contract, currently in effect, was awarded in March 2001. The current contract is valued at \$75 million (plus finance charges). Long range planning on the part of OFT officials to award the contract included writing and issuing the RFP; completing necessary documents in sufficient time to compete the award; performing an analysis of the proposal; and awarding the contract in such a manner as to preclude delays in ordering and receiving needed capital equipment.

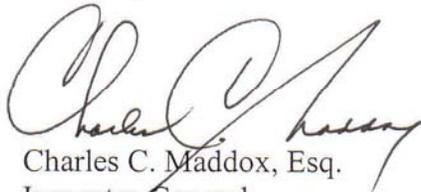
Need For An Economic Analysis. The District paid interest and administrative costs exceeding \$7.2 million under the Contract for the period 1998 to 2003. We believe that considering an option of financing capital lease projects through the issuance of bonds may result in savings to the District over the term of the new lease term. We recognize that bonds may not be the only alternative. Other financing options exist, such as paying for capital equipment out of future capital budgets, other commercial financing mechanisms, or a combination of financial mechanisms that could include the proposed contract but at a reduced value.

We also acknowledge that federal and local regulatory and budget constraints may limit available options. Although the final selection of the funding mechanism used will be made by District financial managers, we look forward to the results of the analysis performed. This analysis should assist District management in identifying the most cost-effective funding mechanism for its future equipment needs.

² Information obtained from the District of Columbia Comprehensive Annual Financial Report for FY 2002.

If my Office can be of further assistance, please contact me or William J. DiVello, Assistant Inspector General for Audits, at (202) 727-2540.

Sincerely,



Charles C. Maddox, Esq.
Inspector General

CCM/cj

cc: See attached Distribution

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