CONGRESSIONAL BUDGET OFFICE
COST ESTIMATE

December 6, 2013

H.R. 3521
Department of Veterans Affairs Major Medical Facility Lease Authorization Act of 2013

As ordered reported by the House Committee on Veterans' Affairs on November 20, 2013

SUMMARY

H.R. 3521 would authorize the Department of Veterans Affairs (VA) to enter into leases to obtain the use of major medical facilities at 27 specified locations. Based on VA's long-established practice, CBO expects that the department would implement that authorization by awarding contracts for the construction and long-term use of those facilities without recording the full amount of the government's commitment as an obligation of its appropriated funds. Thus, H.R. 3521 would effectively be providing budget authority for an amount of obligations that exceeds what we expect VA initially would charge against its appropriation. By CBO's estimate, that additional budget authority would amount to $1.4 billion.

Hence, CBO estimates that enacting this bill would increase direct spending by about $1.4 billion over the 2014-2023 period. Because the bill would affect direct spending, pay-as-you-go procedures apply. We also estimate that, assuming appropriation of the necessary amounts, implementing the bill would have a discretionary cost of $124 million over the 2014-2023 period. Enacting H.R. 3521 would not affect federal revenues.

H.R. 3521 contains no intergovernmental or private-sector mandates as defined in the Unfunded Mandates Reform Act (UMRA) and would not affect the budgets of state, local, or tribal governments.

ESTIMATED COST TO THE FEDERAL GOVERNMENT

The estimated budgetary impact of H.R. 3521 is shown in the following table. The costs of this legislation fall within budget function 700 (veterans benefits and services).

	By Fiscal Year, in Millions of Dollars											
	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2014-2018	2014-2023
CHANGES IN DIRECT SPENDING												
Estimated Budget Authority	41	0	1,378	0	0	0	0	0	0	0	1,419	1,419
Estimated Outlays	2	11	83	382	459	345	137	0	0	0	937	1,419
CHANGES IN SPENDING SUBJECT TO APPROPRIATION[a]												
Estimated Authorization Level	0	0	124	0	0	0	0	0	0	0	124	124
Estimated Outlays	0	0	87	31	6	0	0	0	0	0	124	124

a. Changes in spending subject to appropriations exclude $3 million that CBO expects would be paid from currently available appropriations.

BASIS OF ESTIMATE

For this estimate, CBO assumes that the legislation will be enacted early in 2014 and that outlays will follow historical spending patterns for major construction projects carried out by VA.

CBO's Assessment: VA's Long-Term Obligations as Purchases

Section 2 of H.R. 3521 would authorize VA to acquire the use of 27 medical facilities and would set a limit on the cost of each lease. VA classifies its contracts for acquiring similar facilities as operating leases. However, on the basis of information from VA regarding those transactions, CBO has concluded that most of them are akin to government purchases of facilities built specifically for VA's use—but instead of being financed by the U.S. Treasury, they rely on third-party financing (that is, funds raised by a nonfederal entity), which is generally more expensive.[1] That conclusion is based on those leases having many of the following key features:

- The facilities are designed and constructed to the unique specifications of the government;
- The facilities are constructed at the request of the federal government;
- The leases on the newly constructed facilities are long term—usually 20 years;
- Typically, payments from the federal government are the only or primary source of income for the facilities;

[1] For more information on the budgetary treatment of third-party financing, see Congressional Budget Office, *Third-Party Financing of Federal Projects* (June 2005), www.cbo.gov/publication/16554.

- The term of the contractual agreements coincides with the term of the private partner's financing instrument for developing and constructing the facility (that is, a facility financed with a 20-year bond will have a 20-year lease term);
- The federal government commits to make fixed annual payments that are sufficient to service the debt incurred to develop and construct the facility, regardless of whether the agency continues to occupy the facility during the guaranteed term of the lease; and
- The fixed payments over the life of the lease are sufficient to retire the debt for the facility.[2]

Thus, although those transactions are structured as leases, they are essentially government purchases. Following the normal procedures governing the budgetary treatment of such purchases, budget authority should be available and obligations should be recorded up front when the acquisitions are initiated in amounts equal to the development and construction costs of the medical facilities. Instead, VA records a small fraction of the costs as obligations when it awards the contracts for such transactions.

To the extent that the full costs of developing and constructing the facilities exceeds the relatively small amount that VA would initially record as obligations against its appropriation, CBO treats the legislative authorization for those transactions as contract authority—a type of budget authority that allows an agency to enter into a contract and incur an obligation before receiving an appropriation for those activities. Because the contract authority would be provided in authorizing legislation, H.R. 3521, rather than in an appropriation act, the resulting spending is categorized as direct spending (as distinguished from discretionary spending, which results from appropriation acts).

CBO's estimate of direct spending for H.R. 3521 shows the additional budget authority needed for the costs of developing and constructing the facilities when the contracts would be awarded, over and above the $127 million that CBO estimates would be charged against VA's discretionary appropriations at those times. (VA would obligate those appropriations for certain special features of the facilities; the initial annual lease payments would begin later, after the facilities were constructed.) CBO expects that $3 million of the $127 million would be paid from already enacted appropriations for the special features of two facilities for which the contracts would be awarded in 2014. That amount is not included in this estimate.

Documentation for the projects indicates that contracts for the rest of the facilities would be awarded in 2016. Thus, CBO estimates that the bill would create $41 million of additional

[2] See the Statement of Robert A. Sunshine, Deputy Director, Congressional Budget Office, *The Budgetary Treatment of Medical Facility Leases by the Department of Veterans Affairs*, before the House Committee on Veterans' Affairs, (June 27, 2013), www.cbo.gov/publication/44368.

budget authority in 2014 for the first two projects, and another $1.4 billion in 2016 for the others. Outlays are estimated to occur over the 2014-2020 period, when the facilities would be constructed. All told, the bill would increase direct spending by about $1.4 billion over the 2014-2023 period, CBO estimates.

VA's Categorization: Long-Term Obligations as Leases

VA considers its long-term agreements for medical facilities to be straightforward operating leases (and not effectively purchases). Even if that was the case, however, it appears that the department generally has not been properly recording its obligations for such leases. Circular A-11 issued by the Office of Management and Budget specifies that operating leases require up-front budget authority in an amount equal to total payments over the full term of the lease or an amount sufficient to cover first-year lease payments plus cancellation costs.[3] But for lease contracts that do not permit early cancellation, VA has only recorded obligations for payments due in the year the lease was awarded; as a result, the government's actual obligations for contracts have exceeded the amount the agency has recorded.

H.R. 3521 would not require VA to change its current practices. Section 3 of the bill would require VA to record an obligation at the time a contract is signed in an amount equal to either the total payments that would be made under its full term, or an amount equal to the sum of the first annual lease payment and any specified cancellation costs. That requirement, however, would be contingent upon the availability of sufficient appropriations to record those amounts. Moreover, the amounts specified for the leases in section 2 of the bill are consistent only with the up-front payments for certain design features of the facilities and for the first annual lease payment. Appropriations of those amounts would not be sufficient to cover the contractual obligations under either recording method specified in section 3. Nevertheless, VA's authority to enter into the leases under section 2 would not be constrained if appropriations were not sufficient to cover the full amount of the lease obligations as properly recorded.

VA has not indicated whether it would interpret H.R. 3521 as requiring it to increase the amount of the obligations it records when it awards such contracts. CBO expects that when VA awards contracts for the authorized projects, the department might well determine that sufficient appropriations were not available to record those larger amounts, and it would continue its practice of recording obligations equal only to the payments due in the year a contract is awarded.

Thus, even if the contracts for the 27 facilities were to be considered operating leases, CBO believes that enacting H.R. 3521 would have the effect of providing VA with the authority

[3] See the Office of Management and Budget, *Preparation, Submission, and Execution of the Budget*, Circular A-11 (August 2012), Appendix B.

to enter into those leases without sufficient appropriations to cover the obligations as required by Circular A-11. If the new leases did not specify cancellation costs (as was the case for the past leases CBO has reviewed), obligations recorded for these 27 contracts if they were considered operating leases should be the total payments due over the term of the lease. CBO estimates that those obligations would total $2.3 billion. Hence, the additional budget authority provided by this bill—that is, the full cost of the leases other than the first-year payments—would amount to $2.2 billion. The outlays would be spread over the term of the leases, so that the additional outlays would come to about $670 million over the 2014-2023 period, with the remaining $1.5 billion occurring in subsequent years. However, because CBO views the leases as essentially government purchases, this estimate does not reflect those amounts but instead reflects the amounts described in the previous section.

PAY-AS-YOU-GO CONSIDERATIONS

The Statutory Pay-As-You-Go Act of 2010 establishes budget-reporting and enforcement procedures for legislation affecting direct spending or revenues. The net changes in outlays that are subject to those pay-as-you-go procedures are shown in the following table.

CBO Estimate of Pay-As-You-Go Effects for H.R. 3521 as ordered reported by the House Committee on Veterans' Affairs on November 20, 2013

	By Fiscal Year, in Millions of Dollars											
	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2014-2018	2014-2023
NET INCREASE IN THE DEFICIT												
Statutory Pay-As-You-Go Impact	2	11	83	382	459	345	137	0	0	0	937	1,419

INTERGOVERNMENTAL AND PRIVATE-SECTOR IMPACT

H.R. 3521 contains no intergovernmental or private-sector mandates as defined in UMRA and would not affect the budgets of state, local, or tribal governments.

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