The business of running state government operations

2019 business of running state government operations survey—
insights on real estate

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NASCA
McKinsey & Company

About NASCA

Founded in 1976, the National Association of State Chief Administrators (NASCA), is a nonprofit, 501(c)3 association representing chief administrative officers (CAOs)—public officials in charge of departments that provide support services to other state agencies. NASCA provides a forum for CAOs to exchange information and learn new ideas from each other and private partners. NASCA's mission is to help state CAOs and their teams strategically transform state government operations through the power of shared knowledge and thought leadership.

About McKinsey & Company

McKinsey & Company is the world's leading strategic management consulting firm, deeply committed to helping institutions in the public, private, and social sectors achieve lasting success. For almost a century, McKinsey has served as the most trusted external adviser to governments and private sector companies in the United States and across the globe, helping them solve their most pressing problems, and enabling them to achieve distinctive, substantial, and lasting improvements in their performance. McKinsey's governance as a private worldwide partnership ensures its independence and objectivity.

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Dear NASCA members,

State chief administrative officers (CAOs) are uniquely positioned to play a significant role in transforming the way state governments provide services. Together with our corporate partner, McKinsey & Company, NASCA conducted its second annual *Business of Running State Government Operations* survey of CAOs to identify and prioritize key issues, determine trends, and understand the perspectives of these state leaders.

NASCA conducts research with the following goals:

- **recognize the role CAOs have in driving state government operational excellence**
- **curate and disseminate best practices, success stories, and case studies in state government operations**
- **assist CAOs with the strategies and resources necessary to modernize state government operations**

The study proposal, question development, and peer communications were led by NASCA's Programs Committee, which comprises state CAOs and corporate partner volunteers. We appreciate the leadership and guidance of the Programs Committee. In addition, we thank our state members for the significant time they invested and insightful comments they provided in this survey. Finally, we are grateful for the extraordinary support and resources McKinsey & Company provided in helping us design the survey, analyze the results, and prepare this publication.

Thank you,

Dan Kim
NASCA Programs Chair
Director of the Department of Administrative Services, State of California

Executive summary

The priorities of a state's chief administrative officer (CAO) are numerous and varied: supervising critical state functions; providing services and support to other agencies; supporting innovation and change; managing budget constraints; and continuously improving administrative strategies, initiatives, and processes. To help CAOs achieve their missions, the National Association of State Chief Administrators (NASCA) and McKinsey & Company partnered for a second year to produce the *Business of Running State Government Operations* survey on key issues affecting CAOs today. The survey results are published in three separate papers that focus on real estate, digital government, and risk. Unless otherwise cited, the survey is the analytical base for all exhibits in the paper.

The 2018 survey identified real estate as a critical responsibility for CAOs, and the 2019 survey looked deeply into the challenges and opportunities CAOs face in this area.

All CAOs oversee real estate and share common concerns. The average CAO oversees upward of 2,200 owned and leased buildings. Of the buildings they own, about one-third are more than 50 years old. CAOs have 270 full-time equivalents (FTEs) working in real estate and facilities management, yet they struggle to find employees with the right technical skill set to manage their large portfolios. Indeed, they want to design buildings and spaces to improve the citizen experience and meet customer expectations, but CAOs are stymied by a median deferred maintenance backlog of almost $200 million.

This paper looks closely at four challenges CAOs face regarding real estate and facilities, and it highlights opportunities and best practices to help overcome these barriers:

- Deferred maintenance is a perennial challenge; CAOs might want to consider disposing of the state's most burdensome assets to alleviate this issue.
- Optimizing the portfolio of real estate assets can help capture synergies across tenants and allow for the best use of the space.
- Knowing which performance metrics to use and how to analyze them can be difficult, but cracking the code can lead to more productive and proactive portfolio management.
- The CAO mandate is to use real estate as a lever to enable productive and successful workspaces, but too often customer service fails to get the attention it requires; however, some CAOs are pursuing more customer-centric strategies and creating more dynamic workspaces.

CAOs can take several steps to meet their mission and address workforce needs; but to achieve transformational change in real estate management they must adopt more efficient and sustainable approaches. The suggestions and topics in this paper may be useful starting points to begin that journey.

About the survey

The *Business of Running State Government Operations* survey was conducted with NASCA state members and focused on their priorities and challenges in real estate and facilities management, digital government, and risk management. The purpose of the survey is to provide government leaders with a robust set of data and insights they can use to compare state practices and inform forward-looking strategic decisions.

Methodology

The survey questions drew from subject-matter experts on real estate and facilities management, as well as NASCA state members' experiences. NASCA convened a working group of members who are chief administrative officers (CAOs) to vet the questions to ensure CAOs' responses could yield relevant and actionable insights for NASCA state members.

The respondents

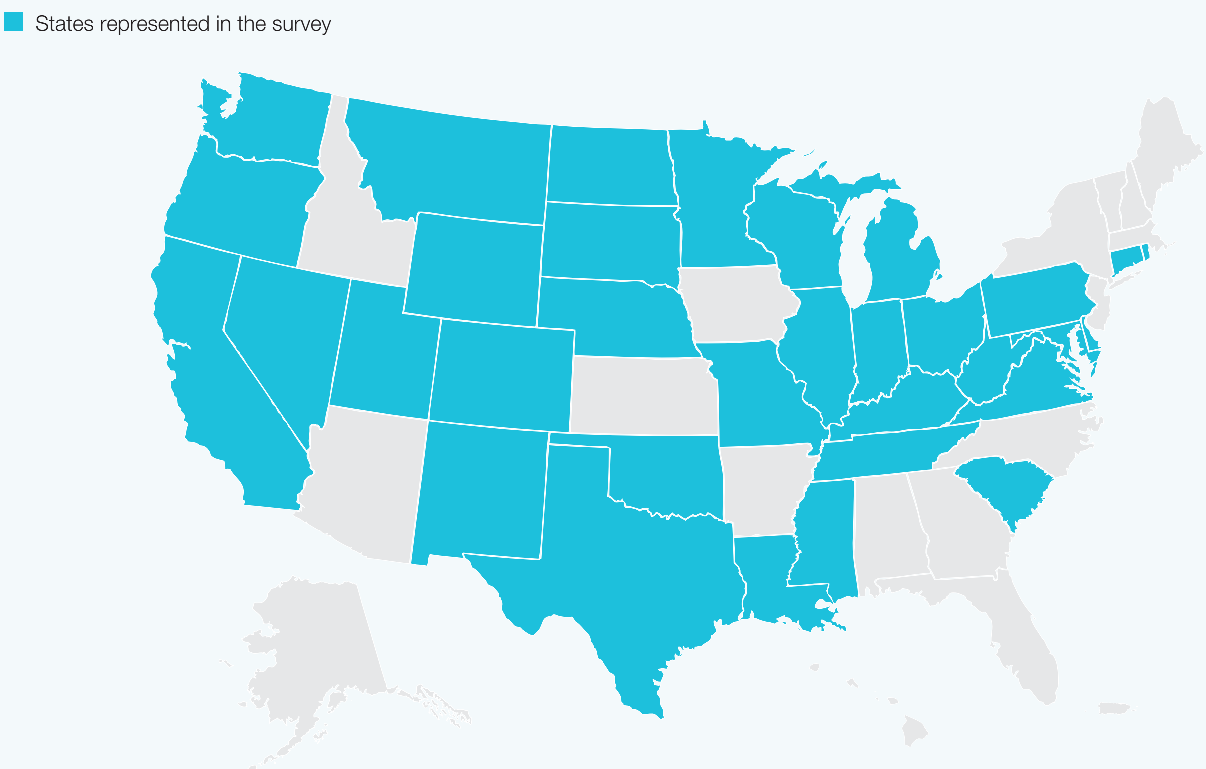
Thirty-three (33) NASCA-member CAOs participated in the survey, though not all respondents answered each question (Exhibit 1). While CAOs were the primary participants, some deputies and other officers also participated. This paper refers to all respondents as CAOs.

Anonymity

To preserve the anonymity of survey respondents, answers are not attributed to specific individuals or states.

Exhibit 1

Thirty-three NASCA-member CAOs participated in the survey.



Understanding what's at stake for CAOs across real estate and facilities portfolios

Real estate and facilities management are a core part of every CAO's job. **In fact, real estate is where CAOs spend the greatest share of their time**, about 20 percent of resource hours, relative to the full range of their responsibilities (Exhibit 2).

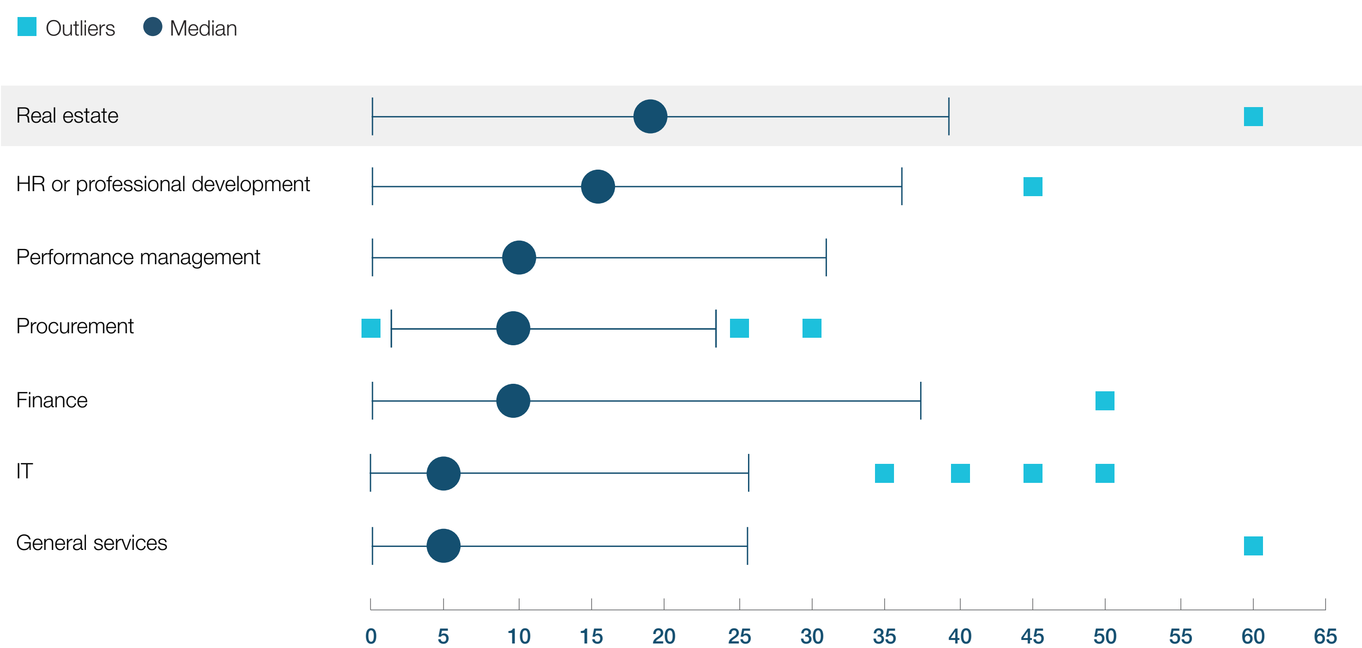
This high degree of time CAOs invest in real estate and facilities management is appropriate given the value at stake. The average state owns more than 15 million square feet of space across 2,200 buildings, much of which is managed by the CAO. CAOs, on average, spend almost $360 million a year of their annual budget and agency outlays on real estate–related activities. Most square footage managed by states is used for office space (see Infographic, on page 6).

The majority of CAOs believe their primary real estate mandate is to create a customer-focused space for state employees to conduct official business, helping them be effective and efficient at their work. However, maintaining large portfolios has become increasingly costly and challenging for CAOs, given that 80 percent of owned buildings are more than 20 years old, and nearly one-third of all buildings are more than 50 years old. With age come additional and costly maintenance needs. Therefore, active, continuous portfolio management is critical to preserving these public assets and ensuring that state facilities support productive workforces and provide high-quality service to residents.

Exhibit 2

The median CAO spends the greatest share of their time on real estate and facilities management.

% of time spent, n = 32



INFOGRAPHIC

There is tremendous value at stake in real estate for the average CAO:

72% owned buildings

Outdated and inconsistent use of performance outcomes

15	2,200	270	$360
million square feet	buildings	full-time equivalents	million annual budget

Static budget growth

1/3 of buildings are more than 50 years old

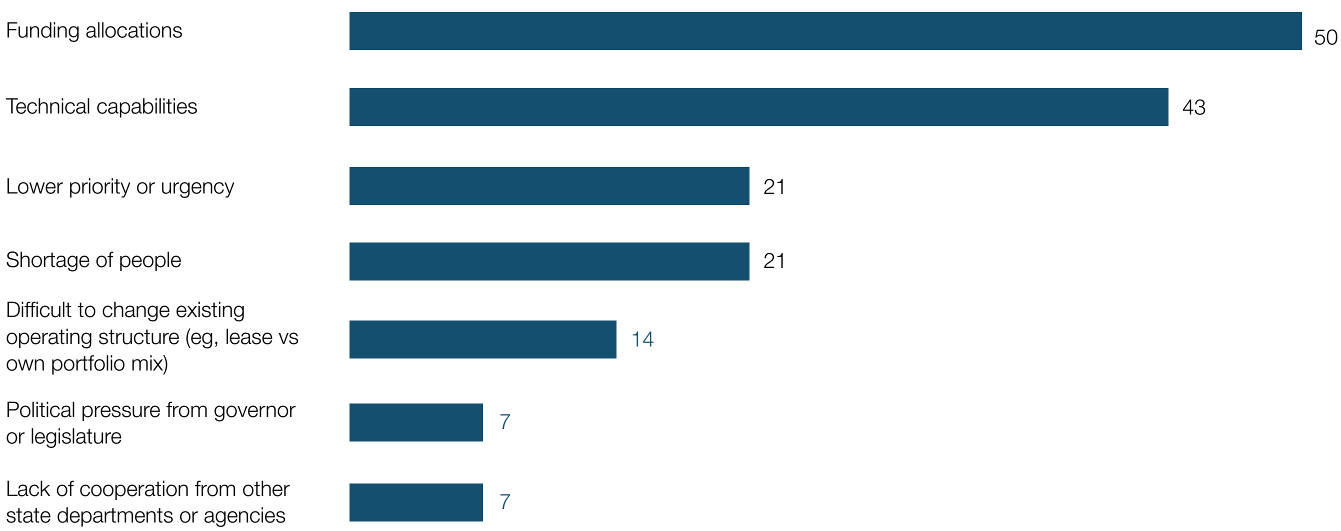
Resource constraints

Despite the importance of real estate and facilities management, most CAOs operate in a resource-constrained environment, thanks to a combination of scarce budget resources, limited technical capabilities, and competing organizational priorities (Exhibit 3).

Exhibit 3

CAOs report funding allocations and technical capabilities as their biggest constraints in real estate management.

% of respondents citing challenge, n = 14



Scarce technical capabilities

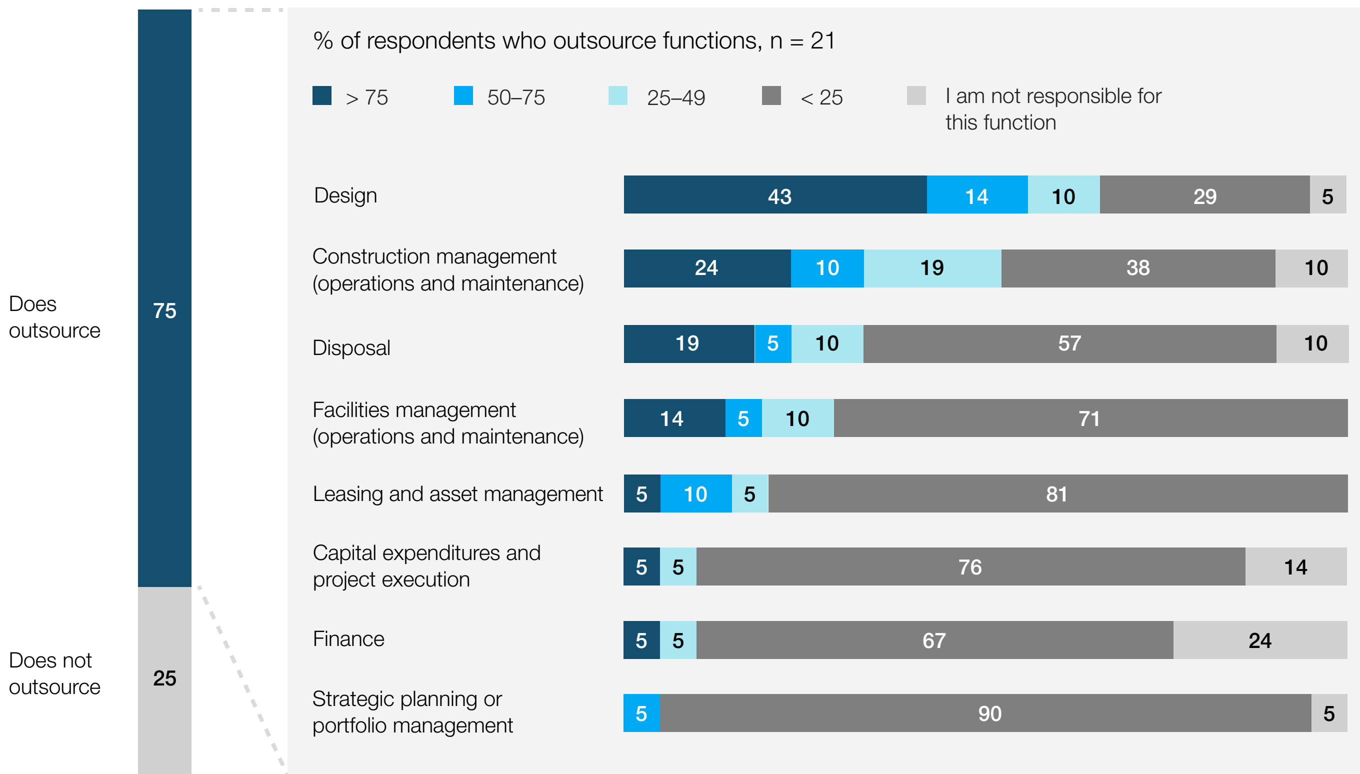
To support their portfolios, the average CAO has 270 full-time equivalents (FTEs) dedicated to real estate and facilities, with nearly 70 percent of personnel working in facilities management. Yet even with large state workforces available, CAOs struggle to recruit talent across all the technical skills required for portfolio management. **More than 60 percent of CAOs cite a shortage of people or a lack of technical capabilities as a barrier to saving money and working more efficiently**, making labor limitations the most common roadblock to effective real estate management across states. Given the importance and cost of real estate in the state, not having the right skill set in place to support that function poses a risk. As a result, CAOs outsource highly technical roles in areas such as design and construction management more than they do other functions (Exhibit 4).

Although in some cases outsourcing may provide a cost-effective solution for certain resource constraints, CAOs face the broader problem of determining whether and how to most effectively recruit, reskill, or upskill their employees. Sixty percent of CAOs believe that targeted recruitment of people with specific skills would be the best way to close the skills gap and help capture additional value in real estate management. Nearly one-third of CAOs also view training and reskilling of existing FTEs as a fundamental tool for capturing value.

Exhibit 4

The most commonly outsourced functions are highly technical roles in design and construction management.

% of respondents, n = 28



Note: Figures may not sum to 100, because of rounding.

Limited financial resources

Despite the high costs associated with deferred maintenance, most CAOs have had static budget allocations for their real estate portfolio requirements. Nearly one-third of states saw their maintenance budget go up by more than 5 percent from 2018 to 2019. Combined with significant and mounting backlogs of unfunded maintenance—the median deferred backlog across the country is $195 million—the challenge could worsen over time, with most CAOs expecting to do more in the future without a significant increase in budget (Exhibit 5).

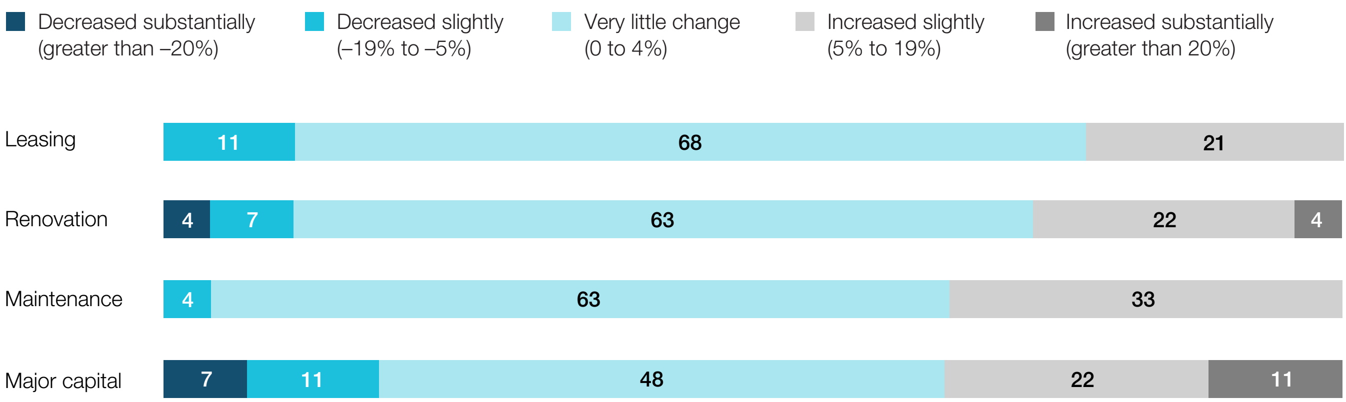
Shared priorities and challenges

Resource constraints make it more challenging for CAOs to address common real estate and facilities management challenges and create value for customers and residents. CAOs identified asset management as a priority, and nearly every survey respondent said that maintenance requirements were among their top five areas of focus (Exhibit 6). Most recognized building performance and sustainability as another top concern, while nearly half also prioritized spending and a variety of cost reduction efforts.

Exhibit 5

CAOs do not expect their budgets to change significantly in the next five years.

% of respondents, n = 27

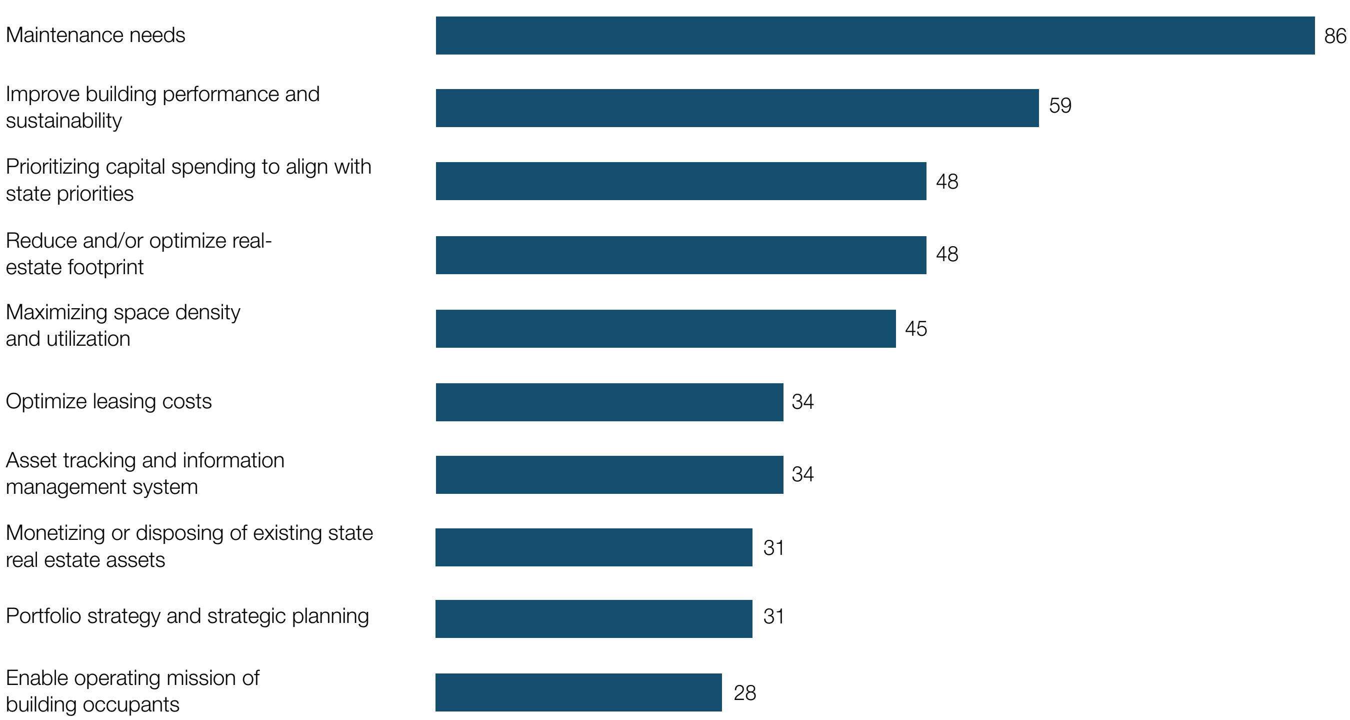


Note: Figures may not sum to 100, because of rounding.

Exhibit 6

CAOs identify maintenance needs, building performance, and aligning capital spending with state priorities as top concerns.

% of respondents listing concern as a top 5 priority, n = 29



Although these concerns are often interrelated, we distilled the survey responses into four distinct categories:

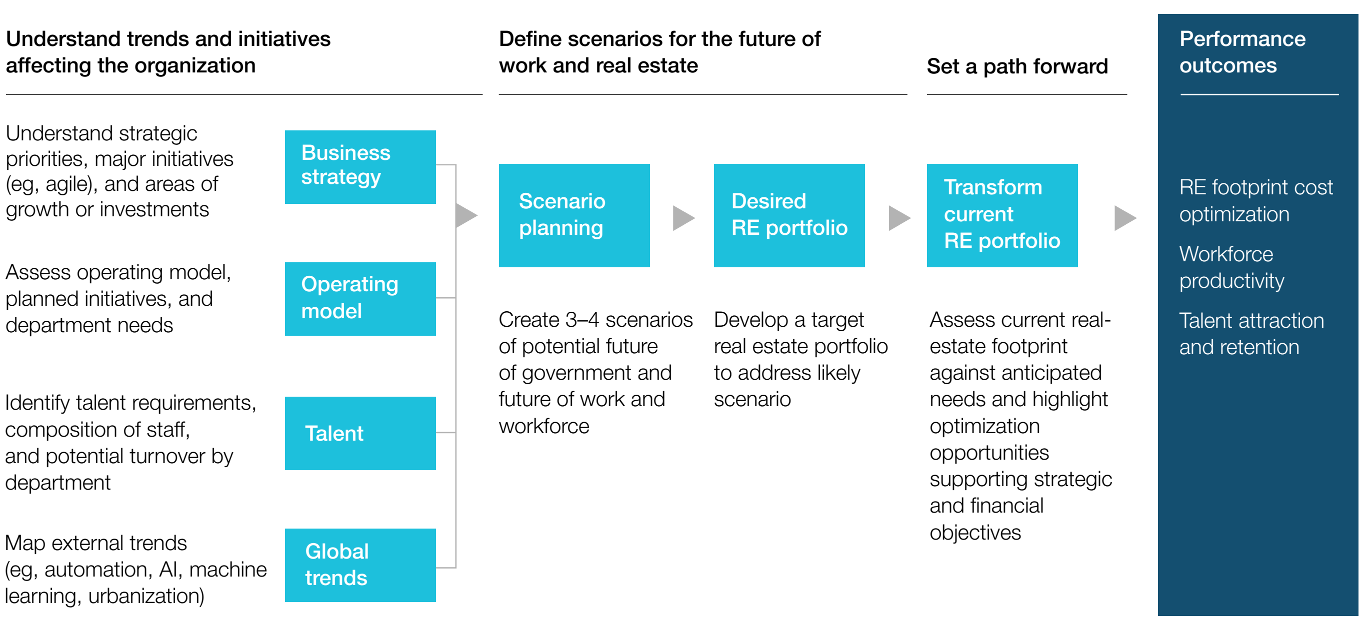
- getting ahead of deferred maintenance
- optimizing the state's real estate portfolio and associated costs
- improving the performance of state-owned buildings
- providing great customer experience to enable the mission and improve productivity

To achieve the best possible outcomes, CAOs must take an integrated approach to portfolio management, considering these four categories. An integrated approach that also takes into account trends and initiatives is useful as CAOs develop their long-term strategies, helping them to better understand future needs (Exhibit 7). For example, solving the deferred maintenance challenge in most states will require CAOs to decide which assets their states will need in the future and which can be monetized or sold. Forward-looking portfolio strategies can also help reduce footprint costs and address workforce demands.

This paper provides more detail on how real estate management challenges manifest themselves day to day. We highlight a series of case studies from innovative CAOs as well as new approaches taken by both the public and private sectors.

Exhibit 7

An integrated approach to real estate management will yield the best outcomes.



Source: McKinsey Real Estate Practice

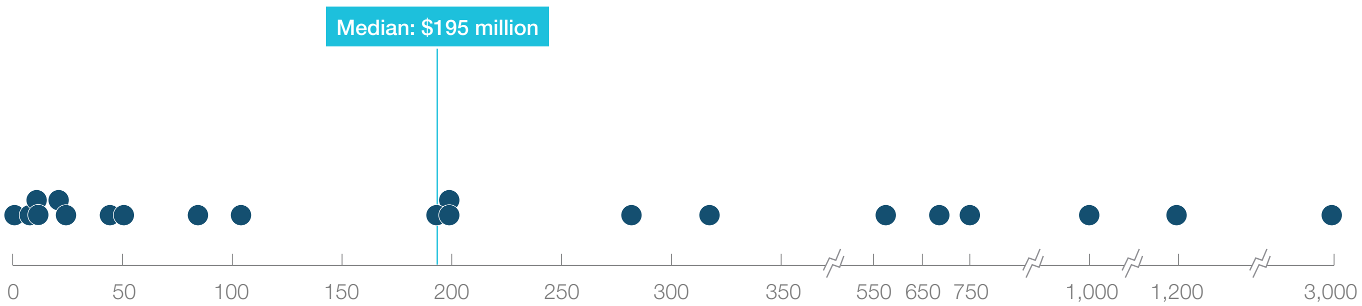
Getting ahead of deferred maintenance

Aging building maintenance is a top five real estate priority for 80 percent of CAOs— and for good reason. Deferred maintenance is a perennial problem, with a large and growing backlog of projects and persistently insufficient budgets. The median deferred maintenance backlog is $195 million (Exhibit 8).

Exhibit 8

The current value of the median deferred maintenance backlog is $195 million.

Survey responses, $ million, n = 21



Case study: A large public agency used advanced analytics to reduce its real-estate investment need by more than $1 billion

Integrating advanced-analytics capabilities into an integrated portfolio-management strategy can help CAOs work through their maintenance backlogs. One large public agency cut its overall real estate investment need in half, from more than $2 billion to less than $1 billion, by using analytics to prioritize maintenance spending and identify opportunities for asset disposal. The approach included establishing a common prioritization framework for facilities maintenance; building a shared, fact-based understanding for key decisions such as investment prioritization and divestitures; and getting buy-in from relevant stakeholders along the way.

Some of the enablers required for this work included the following:

- common fact base on facility conditions with insights from property managers, facilities conditions assessments, and customer feedback surveys
- a common valuation and understanding of zoning and redevelopment potential
- an assessment of the strategic value of the assets to the agency
- understanding of core values that needed to be upheld (for example, historic preservation)

CAOs can eliminate the maintenance backlog by prioritizing specific assets on a portfolio-wide level, investing in the productivity of those key assets, and monetizing or disposing of underused properties.

The result is not only an unfunded gap but an increased possibility of potential health and safety risks associated with underinvestment. According to the survey, 85 percent of CAOs currently use objective needs assessments to prioritize issues such as health and safety risks in their backlogs. While structured prioritization is crucial to improving outcomes, deferred maintenance challenges cannot be resolved solely through reactive measures.

CAOs can eliminate the maintenance backlog by prioritizing specific assets on a portfolio-wide level, investing in the productivity of those key assets, and monetizing or disposing of underused properties. This approach can generate capital for investment and substantially eliminate maintenance backlogs.

Disposing of assets to optimize space and reduce costs

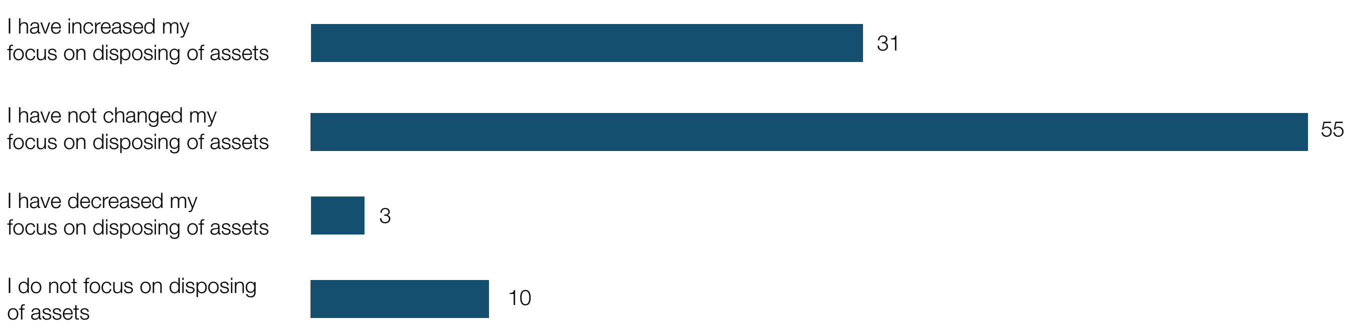
Asset disposal is one of the best tools CAOs can use to make significant headway on their deferred maintenance backlog. Liquidating burdensome assets relieves CAOs of having to make large maintenance investments in buildings that no longer meet program needs.

CAOs know this and many are already taking this approach. According to the survey, about 30 percent of CAOs have already increased their focus on asset disposal to optimize space and reduce costs (Exhibit 9). CAOs that do not currently have a strategy in place to increase asset optimization should consider implementing one.

Exhibit 9

Thirty percent of CAOs have increased their focus on asset disposal in the past year.

% of survey respondents, n = 14



Note: Figures do not sum to 100, because of rounding.

To be most effective, asset optimization should link disposition, monetization, and reinvestment. In many states, proceeds from disposition can be retained and used against other real estate needs. By leasing or selling existing real estate, CAOs can find untapped sources of value in their portfolios. Examples of asset optimization from other public agencies highlight the potential value at stake—hundreds of millions of dollars. While these cases include real estate, they also extend to adjacent assets such as energy resources, infrastructure, and parking (Exhibit 10).

Exhibit 10

Examples of public sector optimization programs demonstrate enormous value waiting to be unlocked.

Asset type	Description	Value unlocked, $ million
University energy	PPP for 50-year energy management contract, meeting university's sustainability goals	1,200
Campus parking	50-year lease of university parking lots to a private company	480
Government buildings	One-time sale of 161 buildings, with nearly 1 million square feet of space	400
Fiber optic	30-year agreement to pay annual rent to a state transportation provider in exchange for the right to install and maintain conduits to run fiber optic cables	230

Source: McKinsey analysis

Federal policy enables link between asset disposal and reinvestment

The Federal Assets Sale and Transfer Act (FASTA)[1] was instituted in 2016 to make it easier for federal agencies to dispose of real estate assets. FASTA allows revenues from sales to be connected to reinvestment requirements to reduce the overall cost of ownership for federal real property. The intent of FASTA is to increase cost efficiency in real estate management while also enabling agency missions.

[1] Garrett Hatch, "The Federal Assets Sale and Transfer Act of 2016: Background and key provisions," Congressional Research Service, October 31, 2017, fas.org.

Optimizing the state's real estate portfolio

CAOs are responsible for ensuring efficient use of their states' real estate and facilities assets while also meeting the states' strategic priorities. Taking an active approach to disposing of assets, as mentioned above, is one way to optimize the portfolio. But a strategic and comprehensive cross-agency view of the portfolio encompasses much more than offloading the most obvious problem assets. **CAOs can use advanced-analytics capabilities and other approaches to uncover opportunities to lower costs while better meeting statewide strategic goals within the remaining portfolio.** Two of the biggest opportunities for CAOs are identifying and prioritizing capital projects and rethinking the mix of owned versus leased properties.

Using advanced-analytics capabilities to reprioritize capital projects

In many cases, CAOs can respond to changes in their state's priorities without increased budget allocations. For example, by using advanced analytics to model their real estate portfolios, CAOs can assess the trade-offs between different prioritization options, helping them choose a path.

Using a long-term strategic plan to make more dynamic portfolio decisions

Nebraska

"In Nebraska we think about our real estate portfolio strategically. Our Capital Facilities Plan looks 20 years out and anticipates evolving real-estate and infrastructure needs. Working with our tenant agencies, we evaluate future mission, workforce, constituent service, accessibility, and sustainability challenges and use those inputs to make strategic choices about our long-term facility needs. With our strategic plan in place, we've been able to respond faster to acquisition opportunities that aid consolidation and co-location while sharing future state opportunities with our customers and the community in a transparent way."

— *Jason Jackson, director, Nebraska Department of Administrative Services*

However, the real estate industry tends to lag behind others in the use of advanced-analytics capabilities throughout the project life cycle. In both the private and public sectors, there is a significant opportunity to use advanced analytics more extensively during capital planning to support maintenance versus disposition decisions and to more accurately assess the lifetime value of an infrastructure development.

Optimizing the mix of owned versus leased space

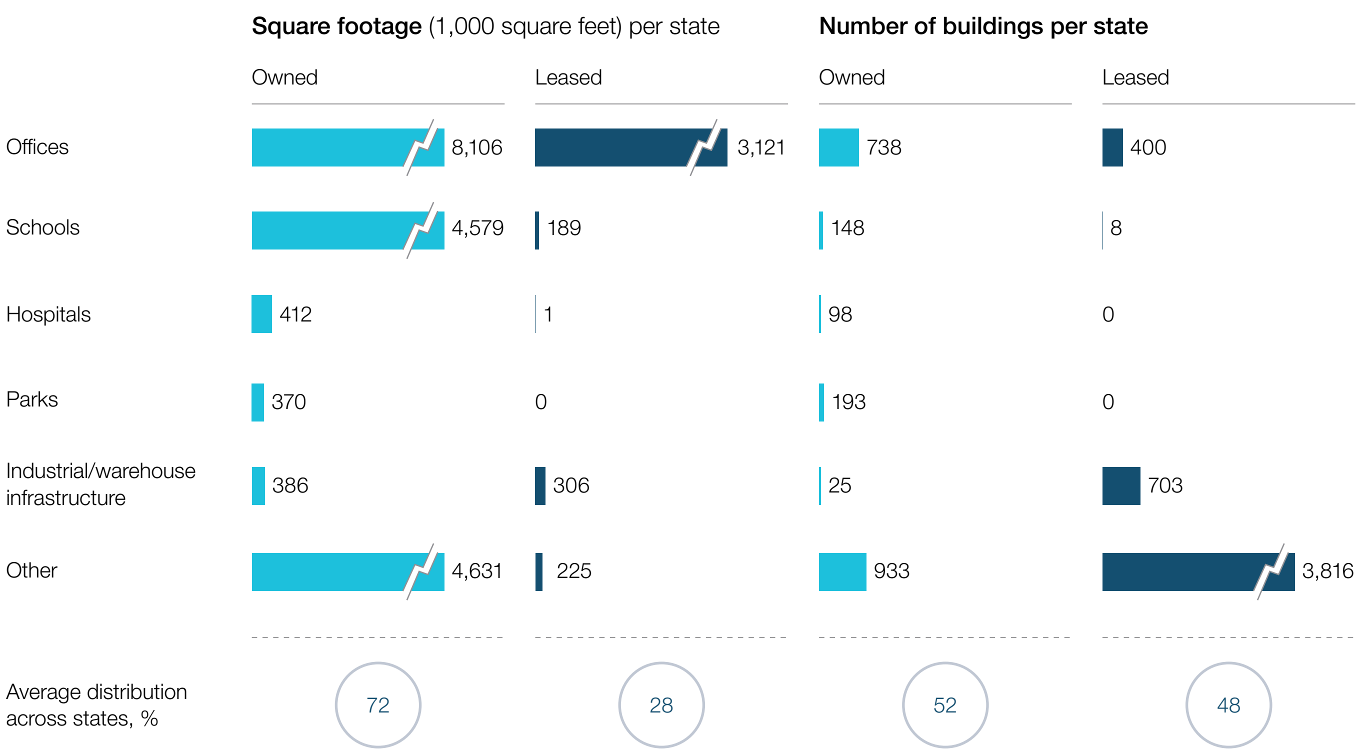
The survey demonstrated a wide range of approaches to one of the biggest decisions CAOs must make regarding their state real estate portfolios—whether to own or lease space. While the majority of CAOs reported a high proportion of owned property (on average, states have a 70/30 split of owned versus leased space), there are outliers on either side of that mean, including several CAOs who reported managing closer to 40 percent owned property (Exhibit 11).

Thirty-three percent of CAOs cited their desire to move away from leases and toward owned buildings as one of their top five approaches for capturing value. Another 33 percent of CAOs said the opposite—moving away from owned buildings and toward leases was one of their top five approaches. This divergence demonstrates **there is no universally applied best practice for addressing the decision of owning versus leasing, even after accounting for political, operational, or financial considerations.** That said, any decision on leasing or owning should be grounded in thorough, rigorous analysis of the trade-offs—rather than a mindless entropy that maintains the status quo.

Exhibit 11

Most state-managed real estate is owned.

Averages, n = 27



Case study: A public agency reprioritized its portfolio to advance its strategic objectives in housing without changing its real estate funding limit

One public agency used an advanced-analytics model to see how it could promote new housing affordability goals without changing its funding levels. By increasing the weighting of real estate projects that supported housing affordability goals in the model, the agency was able to re-prioritize its portfolio and reevaluate which projects it would fund. As a result, the agency met its new housing goals without increasing funding levels.

When deciding the right portfolio mix, CAOs should consider the following factors:

- constraints on the balance sheet, which limit the ability to make large capital outlays (in which case leasing is likely preferable), rather than constraints in the operating budget (where owning is likely preferable)
- variability of demand risk; higher variability indicates leasing is likely preferable, given the need to dispose of an owned asset if demand changes
- local market considerations, which may make it more cost efficient to own or lease
- occupancy strategies, especially how to monetize underused spaces and dispose of unused properties if necessary; determining which roles can telework; and deciding which roles need to be in the capital complex or other state offices
- legislative and gubernatorial concerns, including timelines to approve projects, sustainability targets, redevelopment goals, and support of trade or labor unions

Improving the performance of state-owned buildings

Most CAOs have clear strategic goals to guide their real estate decision making, ranging from sustainability and energy efficiency to feasibility of maintenance, yet some CAOs are concerned about their ability to achieve those goals because of a primary emphasis on cost. As CAOs themselves widely recognize, focusing solely on topline costs can obscure other factors affecting the efficiency and effectiveness of real estate decisions.

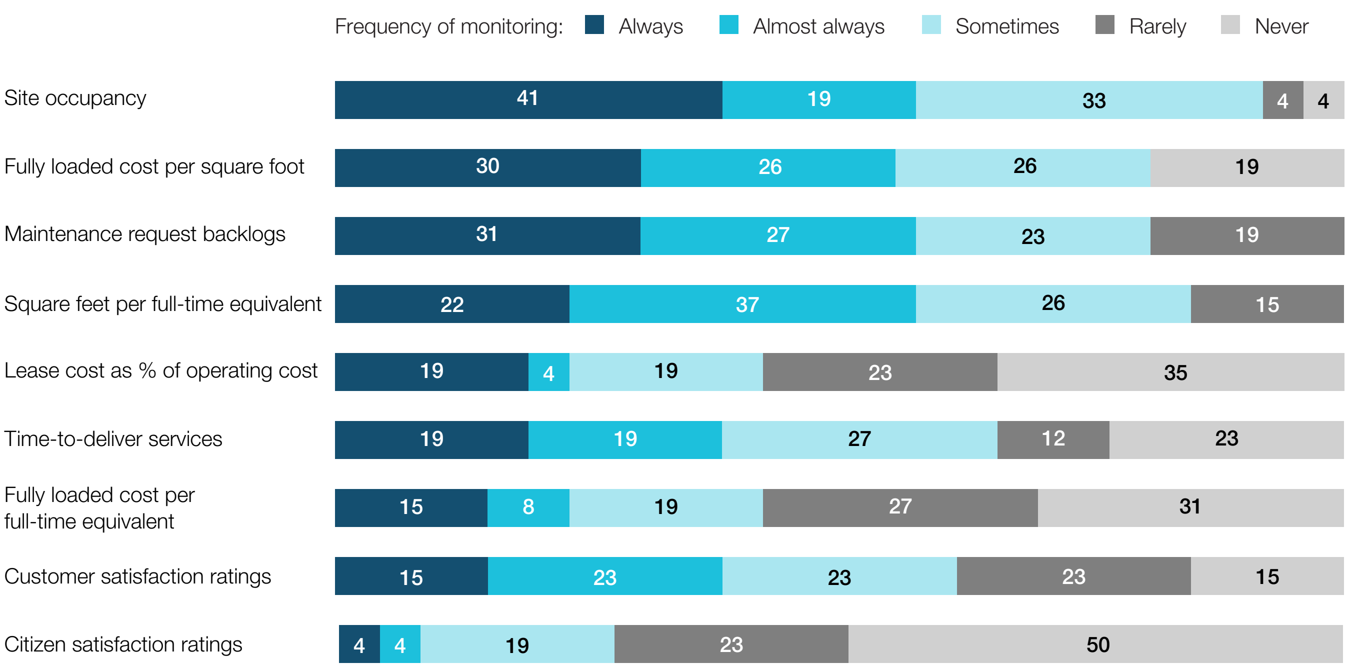
To make the most effective decisions regarding their real estate portfolios and ensure they are achieving their strategic goals, **CAOs should adopt diverse metrics, set targets for those metrics, and evaluate them on a regular basis.**

By incorporating additional building-level analytics into their real estate decision-making processes, CAOs will be better positioned to make evidence-based decisions. More than 50 percent of CAOs always or almost always use metrics such as site occupancy, fully loaded cost per square foot, square feet per FTE, and size of maintenance-request backlog (Exhibit 12). About 25 to 40 percent of CAOs always or almost always use additional metrics that include lease cost as a percentage of operating cost, time to deliver services, and customer satisfaction. CAOs not currently using these metrics (or others related to sustainability, energy efficiency, and building use) should consider tracking them to ensure they are efficiently and effectively fulfilling their organization's diverse goals and mandate.

Exhibit 12

Most CAOs monitor metrics on site occupancy, fully loaded cost per square foot, and maintenance requests.

% of respondents, n = 27



Note: Figures may not sum to 100, because of rounding.

About half of CAOs track maintenance-request backlogs and time to deliver services on a monthly or more frequent basis. Other metrics tend to be tracked sporadically—sometimes every few months, sometimes less than once a year. A better practice is to continuously collect real-time occupancy and energy-use data and assess overall building performance during regular portfolio strategy review sessions. This approach will ensure decisions are made using current data and with enough time to enable course corrections before problems become too large.

Using data to make evidence-based decisions

Washington
The Washington State Facilities Portfolio Management Tool is an IT solution that captures and retains facilities overview information, lease contract data, space use data, photos, and related documents. It allows state officials to access and use facility-inventory data collected from more than 75 state agencies and informs the state's Six-Year Facilities Plan, capital budget, leasing decisions, comprehensive emergency-management planning, and other analyses related to state facilities.

"By collecting and analyzing extensive statewide data related to our real estate and facilities portfolio, Washington State is able to make enterprise-wide strategic, forward-thinking real estate decisions. This results in increased efficiency and effectiveness in state operations and better leasing decisions, while ensuring that buildings are healthy, safe, and sustainable."

— *Dan McConnon, assistant director, Technology Services & Facilities Planning, Office of Financial Management, Washington State*

CAOs should consider conducting cost-benefit analyses that include direct costs, opportunity costs, and customer satisfaction to determine which construction model would provide the most effective and efficient use of public funds for a given capital project.

Using new construction models to reduce overall cost per square foot

CAOs can also take a more rigorous approach to performance management when undertaking large capital projects, by evaluating the right construction model for each project. Roughly 80 percent of CAOs use traditional design-bid-build construction models, and 60 percent of CAOs also use design-build models. However, a more thorough approach to assessing the impact of different models on overall costs and timeline can help CAOs select the most appropriate one.

Far fewer CAOs use public–private partnerships (PPPs) or construction manager at risk (CMAR) models on a frequent basis, though there is a desire to learn more about them. Forty-three percent of CAOs expressed an interest in learning more about PPPs, and 21 percent were interested in learning more about CMAR models. By learning about different construction models, CAOs can better match the construction model to the project, increasing efficiency in costs and schedules.

Six key performance indicators that leading organizations use to optimize occupancy costs

Initiatives such as shrinking individual workspaces and creating cross-agency shared offices have been proven to optimize space while creating more dynamic workplace environments in both public- and private-sector contexts. In the survey, about half of chief administrative officers reported a desire to reduce or optimize their real estate footprint. By identifying and tracking key performance indicators, chief administrative officers can determine the best ways to optimize their spaces. Leading organizations use the following six indicators to optimize occupancy costs:[1]

- number of full-time equivalents requiring seats
- seat utilization rate
- density, measured in square feet per seat
- rent per square foot
- facilities-management experience per square foot
- depreciation and real estate taxes per square foot

[1] McKinsey analysis.

The PPP approach can solve many problems associated with inefficient spending on large capital projects, such as poor strategic alignment, unclear roles and responsibilities, a delivery team without a sense of ownership, and poor project controls, all of which can lead to cost overruns and delays. However, these advantages do not necessarily offset the political, procurement, or revenue risks that come with PPP models. CMAR models similarly seek to navigate cost and schedule overruns by working with contractors earlier in the design phase to identify problems and manage risks from the outset of a project. **CAOs should consider conducting cost-benefit analyses that include direct costs, opportunity costs, and customer satisfaction to determine which construction model would provide the most effective and efficient use of public funds for a given capital project.**

Providing great customer experience

Most CAOs say that a core part of their real estate mandate is to provide functional space that supports their agency's mission. However, given a backlog of critical maintenance needs that can have real safety implications and high costs, few states are programmatically working toward meeting the customer-focused part of their mandate. Just fewer than one-third of CAOs list "enabling mission of building occupants" as one of their top five goals. And 38 percent of CAOs rarely or never evaluate customer satisfaction metrics (Exhibit 12).

Creating more dynamic workspaces

In the private sector, employers typically explore three approaches to achieving a more flexible, dynamic workspace: alternative worksites, co-locating, and coworking (Exhibit 13). These approaches benefit employees by making the workplace more fun and by enabling more flexible work arrangements, while simultaneously saving space or reducing space needs.

Pursuing customer-centric strategies

Customer-centric strategies in the private sector are directly linked to customer loyalty and improved bottom lines. Similarly, in the public sector, customer-centric strategies provide agencies with an enhanced ability to meet budget goals and achieve their missions.

Exhibit 13

Large employers explore three approaches to achieving more flexible, dynamic space allocations.

	Alternative worksite and smart working	Co-location	Coworking
Description	Flexible workplace program that gives employees options to work from home, shared space in offices, drop-in centers, etc Leverages hoteling space for traveling visitors	Cross-functional teams work in co-located workspace to promote collaboration and rapid iteration Fun, open environment that fosters working culture and helps to manage performance, coach team members, etc Workspace design aids the change in process and change in culture for companies moving to new dynamic/connected ways of working	Start-ups and innovators working in the same space to share ideas and capital equipment Shared office space models on flexible leases with a high community focus
Model adopted by	Companies focused on improving workforce flexibility and lifestyle Frequently used by more established companies as part of recruiting value proposition	Companies focused on building agility and collaboration where collaboration between team members is key	Companies focused on creating new ideas from outside collaboration through incubators Companies that built flexibility in their footprint and provided alternate worksites

Source: McKinsey Real Estate Practice

Putting workspaces front and center in real estate strategy

California

"We spend most of our waking hours in our office or cubicle. But our work space has often been considered an afterthought. We at DGS now recognize how important it is to get the work space right. Creating better work spaces doesn't have to mean we spend more; rather, being thoughtful about work spaces can improve recruitment and retention, foster collaboration and productivity, and promote wellness and sustainability all at once. We know this from research, and now we're putting this to practice by designing workspaces to meet the needs of a new generation of state employees. So far, the results have been overwhelmingly positive - and we are in the very preliminary stages to evaluate how workspaces impact worker productivity and wellness, not to mention retention."

— *Daniel C. Kim, director, California Department of General Services*

Although customer satisfaction is often deprioritized relative to maintenance, better alignment with tenants regarding factors that affect recruitment, retention, productivity, and morale could increase overall effectiveness and efficiency in state services. **CAOs should consider emphasizing customer satisfaction metrics in their real estate strategies.**

In addition, positive employee engagement tends to improve citizen experience, and vice versa. Across the public and private sectors, employees are often highly motivated to provide a great experience for their customers or beneficiaries, they just need the tools to do so. By removing physical workplace barriers that make work more complex, CAOs can support state employees in providing the best service to residents. At the same time, states must make it possible for residents to engage actively and efficiently with state services.[1] In other words, real estate strategies can provide CAOs with an opportunity to better serve state residents both indirectly and directly, by improving employee experience and by improving residents' experience when they visit state buildings.

Advancing a service-delivery mission through real estate strategy

Indiana

The State of Indiana co-located all of its own veterans services, as well as those provided by the federal government, local government, and nonprofits, in the same building to improve the experience of veterans seeking services.

"777 North Meridian Street is a collaborative project in which we are working with stakeholders at the federal, state, and local level, as well as those from the not-for-profit sector to make this building a one-stop-shop for veterans. The idea is that a veteran would only have to come to 777 for all of his or her needs[—]benefits, job search, health care, anything. We want to make getting services easier and less frustrating for veterans. We had this beautiful, historic building (this is where the GI Bill was signed in 1944!) and we had the chance to make it useful and meaningful at the same time."

— *Lesley Crane, commissioner of the Department of Administration, State of Indiana*

[1] Tony D'Emidio, David Malfara, and Kevin Neher, "Improving the customer experience to achieve government-agency goals," February 2017, McKinsey.com.

Setting priority initiatives and the path forward

CAOs noted that new ideas and approaches are needed to set and implement bold real estate aspirations. By applying innovative ideas and technologies, CAOs can prioritize their real estate portfolios in a manner that aligns with resident outcomes and stabilizes their expected out-year investment needs.

CAOs can take many bold steps to transform their real estate portfolios:

- building a data and analytics capability to regularly assess and optimize the total portfolio investment, including real-time data on utilization and energy use and establishing a single source for data, such as maintenance requirements, building asset values, land and redevelopment value, and strategic opportunities
- conducting a biannual strategic investment review with top state executives
- creating the structures necessary to link disposition, monetization, and reinvestment of assets
- making a state building fund to capture revenue to support sustainable maintenance
- deploying new requirements to generate more flexible, dynamic space allocations in state office buildings

CAOs also indicated in the survey that they are pursuing innovative initiatives to influence their real-estate portfolios (Exhibit 14), such as creating energy-efficiency benchmarking and increasing flexible work arrangements.

States move toward renewable energy

Several survey respondents cited efforts they're making to increase sustainability and use more renewable energy across their real estate footprint. Colorado and Oregon are two examples of states leading the way.

Colorado

In support of Governor Jared Polis' goal of setting the state on a path to 100 percent renewable energy by 2040, Capitol Complex is contracting with an energy-services company to install LED lighting across all Capitol Complex–managed buildings. The first step toward 100 percent renewables is to increase energy efficiency. In support of this effort, the Colorado Department of Personnel & Administration's Division of Capital Assets is promoting energy policies that accelerate the adoption of clean, renewable resources and energy efficiency programming in the Capitol Complex.

Oregon

Oregon state agencies greatly benefit from resources and incentives provided by Energy Trust of Oregon, an independent, public-purpose nonprofit helping Oregonians invest in energy efficiency and renewable energy. Since 2002, Energy Trust has helped state agencies meet energy goals by offering incentives for efficient lighting; heating, ventilation, and air conditioning; controls; building design; and more. In 2018, agencies received more than $890,000 in incentives and rebates for capital and operational projects projected to save more than 3.3 million kilowatt-hours of electricity and nearly 300,000 therms of gas annually.

Exhibit 14

CAOs are implementing various ongoing initiatives to meet facilities mandates.

Consolidated lease space to owned space

Created sustainability policy for rebates

High-efficiency buildings

Strengthened security of lease execution process

Requested funding to decrease deferred maintenance

Utilized building assessments for deferred maintenance needs

Requested capital for energy efficiency projects

Reorganize office space for cross-department coordination

Developed 20-year strategic plan

Automated information systems

Negotiated lease renewal options

Establish governing council

Established space standards

Public–private task force

Developed strategic plans and guiding principles

Standardized space allocation

Reviewing space standards

Implemented computerized maintenance management systemfor facilities

Co-locating state services

Focused on energy efficiency

Pursuing legislation to streamline transactions

Introduced zero-net energy policy

As CAOs develop and implement new initiatives to meet their facilities' mandates, there is an opportunity to be creative in tackling shared real estate challenges. CAOs can work across state lines to collaborate on identifying funding sources, designing next-generation workspaces, and applying advanced-analytics capabilities. An ongoing discussion of best practices and trends will help states not only identify ways to increase efficiency and effectiveness but also accelerate change across the country for the sake of taxpayers and the general public. ■

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