

CORPORATE STRUCTURES FOR GOVERNMENT FUNCTIONS

HEARING BEFORE THE SUBCOMMITTEE ON GOVERNMENT MANAGEMENT, INFORMATION, AND TECHNOLOGY OF THE COMMITTEE ON GOVERNMENT REFORM AND OVERSIGHT HOUSE OF REPRESENTATIVES ONE HUNDRED FOURTH CONGRESS FIRST SESSION

JUNE 6, 1995

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CORPORATE STRUCTURES FOR GOVERNMENT FUNCTIONS

TUESDAY, JUNE 6, 1995

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON GOVERNMENT MANAGEMENT,
INFORMATION, AND TECHNOLOGY,
COMMITTEE ON GOVERNMENT REFORM AND OVERSIGHT,
Washington, DC.

The subcommittee met, pursuant to notice, at 2 p.m., in room 2154, Rayburn House Office Building, Hon. Stephen Horn (chairman of the subcommittee) presiding.

Present: Representatives Horn, Flanagan, Davis, Tate, and Scarborough.

Staff present: J. Russell George, staff director; Mark Brasher, professional staff member; Andrew G. Richardson, clerk; David McMillen, and Matt Pinkus, minority professional staff.

Mr. HORN. A quorum being present, the Subcommittee on Government Management, Information, and Technology will come to order.

This afternoon we are holding the fifth of nine hearings on making government work. In this session we will examine three different corporate structures to assist agencies of the Federal Government in providing services more efficiently. We recognize that no single structure will be best and even necessarily good for every Federal mission and organization that we have. It is possible in some cases that none of these corporate forms will fit as well as the current structures.

With us today are experts on governmental and private and public corporate organizations with extensive management credentials in both environments. Former Secretary of Defense and White House chief of staff and current chief executive officer of the General Instrument Corp., Donald Rumsfeld, will lead off with a broad overview of public and private reorganization issues.

The second panel will be focused on the reorganization of the General Services Administration represented by its administrator, Roger Johnson, who has had extensive private corporate experience as well as distinguished public service.

Panel three will feature the Bonneville Power Administration and the Forrester Corp. as two representative corporations whose goal is to increase efficiency in Government.

The final panel will discuss an administration proposal for an air traffic control corporation. Mr. Harold Seidman, a fellow of the National Academy of Public Administration, will summarize the three

organizational types and describe how they can assist agencies to increase efficiency.

Gentlemen, we thank you all for joining us. We look forward to your testimony, and, if I might, I would like to ask the first witness, who knows the tradition, to stand and take the oath, which is the tradition on this committee. We will put in immediately after the introduction your full statement.

We limit members to summarizing essentially to 5 minutes. We might stretch it a little with you and Mr. Johnson, but we want to leave plenty of time for questions, and it will all come out, I think, in the questioning.

So if you will stand, Mr. Rumsfeld, raise your right hand.

[Witness sworn.]

Mr. HORN. Thank you, and please be seated.

Now let me ask before we begin if there are any opening statements by the vice chairman, Mr. Flanagan, the gentleman from Illinois.

Mr. MICHAEL FLANAGAN. Thank you, sir. Thank you, Chairman Horn, and all the witnesses that are here to enlighten us today on the topic of merging corporate structures and Government functions.

This is not a new idea or a cure-all solution to the problem of Government waste, this is just common sense. We are fortunate that we do not have to recreate the wheel and that there are pre-existing corporate structures that Government functions can adopt and utilize.

The House Budget Resolution contains proposals to eliminate the Federal Supply Service and the Information Technology Service. These bureaucracies are designed to save the taxpayer money. The question is, do they cost more money than they save? While the FSS may save the Government money by acquiring automobiles in large quantities at volume discounts, is this not something that each agency can do on its own when purchasing automobiles? Further, do the track records of these agencies justify their existence?

The General Services Administration has noticed concern about the ITS to the point that it has called for a time-out in some of its services. Once again, these are services that Government should continue supporting.

I also look forward to hearing the advantages of creating government corporations that could provide us with necessary services such as electricity and air traffic control while at the same time help us reach energy efficient requirements outlined in previously passed legislation by offering options to Government facilities. We have an obligation to deliver what has worked to the taxpayers of this country, and these are essential steps on the path to that success.

Thank you, Mr. Chairman.

[The prepared statements of Hon. Michael Flanagan, Hon. Cardiss Collins, and Hon. Carolyn B. Maloney follow:]

PREPARED STATEMENT OF HON. MICHAEL FLANAGAN, A REPRESENTATIVE IN
CONGRESS FROM THE STATE OF ILLINOIS

Thank you Chairman Horn and all the witnesses that are here to enlighten us today on the topic of merging corporate structures and government functions. This is not a new idea or a cure-all solution to the problem of government waste—this

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PREPARED STATEMENT OF HON. CARDISS COLLINS, A REPRESENTATIVE IN CONGRESS
FROM THE STATE OF ILLINOIS

Thank you Mr. Chairman for putting together this series of hearings on the National Performance Review. This is a particularly important hearing because it illustrates one of the problems in the rhetoric we use to talk about reinventing government. Everyone talks about making government work more like a business, and each has a different understanding of what that means.

We are all for making the government more efficient and cost less, but all too often those who would "reinvent" our government by setting up a corporation to do the work are too much like those home repair scams that work door to door. We discover after the scam artist has left town that the roof still leaks. Similarly, these reinvention specialists leave us with a function that is no more efficient, doesn't cost any less, and is outside of the government's control.

Setting up a government corporation or restructuring an agency to look like a corporation doesn't bring market forces to bear on the function. Corporations in the private sector make profits, and if they don't, the shareholders either sell their stock for fire the managers. Government corporations don't have the same incentives as private corporations, and consequently won't act like private corporations.

Too often, talk about setting up a corporate structure for government functions is doublespeak for cutting wages, firing employees, and circumventing procurement rules. I think it is all well and good to ask if a corporate structure is appropriate to a particular government function, but we must also ask what will happen to the employees in this transition. Will their wages and benefits be cut? Will their agencies be "downsized", the corporate euphemism for eliminating jobs?

Reinvention at the expense of the workers will not improve services. Instead there will be a demoralized work force which doesn't perform well. As Mr. Krasner pointed out in his testimony, it is not in our best interest to have Air Traffic Controllers or airplane mechanics who have thousands of lives in their hands every day make mistakes because of low morale.

I am particularly interested in the restructuring going on at the General Services Administration. I welcome Mr. Johnson who will testify before us a bit later today.

As I said in my letter to Mr. Johnson last February, I believe that GSA has performed an essential and effective service as a central administration agency for our Federal Government. GSA is responsible for many functions that are basic to government business—telecommunications, computer purchasing, and building management to mention just three. If GSA is unable to carry out those functions, the whole government suffers, and ultimately so does the American public.

The question is whether and how GSA can maintain responsibility for its statutory functions while at the same time propose massive cuts in personnel.

Similarly, I am concerned about the morale of those employees who are being challenged by the Administration to be more efficient, while at the same time the Congress works to cut their benefits.

I have seen the pendulum swing from building Federal buildings to leasing and back again. Throughout that period, GSA has provided the leadership necessary to deal with shifting policy priorities. If reinvention—whether it be by corporate structuring or some other scheme—causes us to lose that leadership we have made a ter-

rible mistake. The one certainty in all of this is that if we destroy the morale of government employees, reinvention will fail.

PREPARED STATEMENT OF HON. CAROLYN B. MALONEY, A REPRESENTATIVE IN
CONGRESS FROM THE STATE OF NEW YORK

Thank you Mr. Chairman. I am pleased with the continuation of these hearings and I look forward to today's testimony.

We have heard a lot about making government more like business. But we also hear a lot about stopping the government from competing with business. The President's circular A-76 makes it quite clear that the government should not compete with business.

These are two sides of the same coin. Discussions about how the government should not compete with business are really discussions about what are and what are not government functions. When we talk about corporate structures, we are talking about how the government goes about doing what it should do. It is important not to get these two things confused.

Unfortunately, the use of the term "corporate structure" is sufficiently vague to lose almost all meaning. Today's testimony illustrates this point. We have three witnesses—all talking about corporate structure—describing three very different approaches to how the government should do business. Those differences are important because some proposals cross the line from talking about how the government should work to talking about whether or not the activity is a government function.

At one end of the spectrum is the reorganization at GSA. Here we are discussing reorienting the way in which GSA does business. At the other end of the spectrum is the proposal for the Forrester Corporation, which would be a private company performing a function that was formerly done within the government. We need to ask very different questions about these two cases.

GSA has been in the forefront of reinventing government, and its reorganization along business-line functions makes sense. But GSA is quite different from other agencies. Leasing and maintaining buildings, acquiring telecommunications services and computers, and managing fleets of vehicles are all functions which can readily be compared with the private sector. It is more difficult to understand how this would help the Department of Health and Human Services or Veterans Affairs.

The Forrester Corporation seems to be about how the procurement system works. If there are problems with the procurement system, we should fix them, not create ways of going around it.

I am particularly pleased that you have invited the National Air Traffic Controllers Association and the Professional Airways Systems Specialists to testify. All too often in this process we hear from the Administration, and not from those most affected by reinvention—the employees. It would be interesting to learn if the employees at GSA are as sanguine about GSA's reorganization as Mr. Johnson is.

I am also curious about how often the Administration has looked into Employee Stock Ownership Programs. This is an excellent way to turn what is now a government activity into a corporate one, and give ownership to the employees. I hope the witnesses today will pay attention to this option as they comment on reinventing government.

Again, Mr. Chairman, thank you for putting this hearing together. And, thank you and your staff for choosing this excellent panel of witnesses.

Mr. HORN. Thank you.

The gentleman from Virginia.

Mr. DAVIS. Yes. No statement at this time, but it is a pleasure to have the Honorable Don Rumsfeld here today.

I look forward to hearing you, Mr. Secretary.

Thank you.

Mr. HORN. I might say before Mr. Rumsfeld begins that we all know that he was a very distinguished Member of Congress prior to his rise in the executive branch to almost the highest position and certainly the most complex as Secretary of Defense and his splendid record in the private sector.

So it is a pleasure to have you with us.

**STATEMENT OF DONALD H. RUMSFELD, FORMER SECRETARY
OF DEFENSE**

Mr. RUMSFELD. Thank you very much, Mr. Chairman. I'm pleased to be here.

I suppose having spent 20 years in the Federal Government with some 20 years in the private sector I do have a somewhat unusual perspective. I must say that when I served on the House Government Operations Committee many, many years ago back in the 1960's, the task we had to oversee the Federal Government was a much simpler one than today, and I recognize that. I can recall the collective gasp that took place when the Lyndon Baines Johnson administration had the first Federal budget of \$100 billion, I mean the budget, not the deficit, and it wasn't that many years ago.

I've taken a very broad interpretation of the phrase "corporate structures for Government" to include not just simply formal structures or organizations but also approaches, techniques, and the like. It seems to me that to discuss particular organizational arrangements generally is not anywhere near as useful as discussing them with respect to specific activities. I say that because it seems to me that the first place one must start is to decide what activities Government ought to conduct, rather than how they ought to be conducted. Certainly in business that is the first task. It is to determine what businesses to be in and then to focus on those and divest those assets that are secondary to those activities. My view is that it would be highly desirable for U.S. Government to do the same thing. Tinkering with structures and organizations for activities that more properly belong with the individual, private organizations or State and local governments, is misplaced effort.

It seems to me that first one must address the more fundamental question. The Federal Government ought not to continue programs that are obsolete, that have failed, or that can be better performed by other institutions; and, second, the Federal Government should only do those things that have a high national priority, not things that can be best handled by other levels of Government.

Back in the sixties when I was in Congress, it was a different world. Because of the civil rights problems, the Federal Government ended up involving itself in a host of activities because there was reasonable certainty that those activities would not be conducted at the State or local level in a nondiscriminatory manner. And so it was understandable that non-Federal activities were embraced by the Federal Government, and the regrettable thing is that that has not been readdressed really in any organized way, since the advent of so many pieces of civil rights legislation.

In any event, only after addressing the more basic questions one ought to move to considerations of specific structures, in my view.

I mention in my testimony one comment about the fact that there used to be a dairy for the Naval Academy, and every time someone talked about selling the dairy, why, everyone explained that it was terribly important to have a captive milk supply for the midshipmen. It is kind of amusing in this day and age to think about it, but in fact it was a serious debate that took place back in those days. As a disinterested observer I can say that there are many things today that strike me as equally humorous, or unfortunate, as the case might be.

I know that when taking over a troubled company a knowledgeable chief executive officer takes a quick look at the teeth to tail ratio, as they say in the military, and undertakes a review of the company's assets and resources and properly divests those that are not central to the future success of the institution.

I mention in my testimony the example of Sears Roebuck where recently they have focused on their basic businesses. This is a very large institution, \$50 billion. They sold some 20 percent of Dean Witter in an initial public offering and then spun the rest of it out. They sold 20 percent of Allstate Insurance in the second largest IPO in history, and then in June 1995 will spin off the remainder. Sears sold Coldwell Banker Residential Services. They are going to sell Homart and Prodigy as well. The effect of all of that was that Sears employees moved from 420,000 in December 1990 to an estimated 240,000 today, still a large number, but a vastly lower number. Sears stock, interestingly, went from some \$25 a share in 1990 up to what it would be equal to over \$70 a share today had Dean Witter stayed a part of the enterprise. I mention that because obviously the investors rewarded that institution for facing up to its problems.

As overseers of the Federal Government, an institution which, for the sake of discussion, I would say is arguably in Chapter 11, the Congress will need to treat the job of restructuring in the same urgent, tough-minded manner. The goal must be to earn back the confidence of the taxpayers who are the real stockholders of the Federal Government.

I read a piece by Peter Drucker where he cautioned that this isn't going to be accomplished by simply tinkering. He pointed out that in any institution other than the Federal Government the changes being trumpeted as reinventions would not even be announced except perhaps on the bulletin board in the hallway. They are the kinds of things that a hospital expects floor nurses to do on their own, that a bank expects branch managers to do on their own, that even a poorly run manufacturer expects supervisors to do on their own without getting much praise, let alone extra awards.

I read an article recently, which I cited in my testimony, which is worth mentioning by a man named Dunlop who did the skillful restructuring of Scott Paper Co. He said do it once, do it severely, and get it over with. When a company says it is going to restructure over the next 3 years, it won't happen. You end up paralyzing the company by repeated cuts that are of too small a size. I think that is sound advice for the Congress as well.

If, in fact, one happens to cut too much in a specific area—and that is almost unprecedented—it is relatively easy to add it back, but it is harmful to keep cutting repeatedly. It is like cutting a dog's tail off one inch at a time hoping it doesn't hurt so much.

The balanced budget plan drafted by the House committee I noted is certainly remarkable in its specificity and scope. In my view, however, it possibly runs the risk of ignoring the principle of cutting decisively and rapidly. In some instances it talks about phasing things out over 3 to 5 years. It seems to me that if something is outmoded and inefficient, phasing it out over a 3-year period will not make it less inefficient or less outmoded. I don't see

quite why one would want to inflict on these programs the death of a thousand cuts.

I suspect I've used up the better part of 5 minutes. I would only mention that what I'm describing at Sears Roebuck or Scott Paper is something that we did at G.D. Searle in the late 1970's and early 1980's, it is something we did at General Instrument. Incidentally, Mr. Chairman, I've left General Instrument Corp. and would want the record corrected on that. I served there from 1990 to 1993. We divested five or six businesses, sold a number of assets, downsized and focused on the core businesses, and dramatically reduced the size of corporate headquarters, with the result that investors and owners of the company moved the stock from about \$15 a share to \$50 a share, judging it the right thing to have done, and, as I say, there are hundreds of companies doing the same thing.

With that, I will be happy to stop and respond to questions.

[The prepared statement of Mr. Rumsfeld follows:]

PREPARED STATEMENT OF DONALD H. RUMSFELD, FORMER SECRETARY OF DEFENSE

THOUGHTS FROM THE BUSINESS WORLD ON DOWNSIZING GOVERNMENT

Thank you, Mr. Chairman, and members of the Committee. I was pleased to accept your invitation to discuss some corporate approaches to organization and downsizing and their possible relevance to the federal government. I believe I do have a somewhat unusual perspective on this issue, having spent roughly 20 years in the federal government and another 20 years in the corporate world.

I am pleased to be back in these chambers. As a young member of the Congress during the 1960s, I had the opportunity to serve on this Committee when it was known as the Government Operations Committee. At the beginning of my tenure, the government we oversaw was much smaller and simpler than the complex and overwhelming behemoth that so many of you in this Congress have pledged to reform.

With your permission, I thought what I would do this afternoon would be to merely summarize some of the concepts in my prepared text, which all of you have received in advance, and then allow the maximum amount of time for questions.

If my memory serves me correctly, one of the issues of my time in Congress was whether or not to close a dairy at the U.S. Naval Academy. That example may be good for a laugh today, but those who tried to sell off the dairy were accused of not understanding the importance of a captive milk supply for the Midshipmen. Heaven forbid that the Naval Academy would have to buy milk from the private sector like everyone else.

While that may seem like a trivial example compared with the sacred cows that must be challenged today if you are to balance the budget by 2002, the fact remains that the federal government is one of the few institutions that still thinks itself able to afford the luxury of sentimentality at taxpayers' expense. Businesses eventually cannot afford to hold on to activities, people, practices, divisions or subsidiaries that have become not central to the core business, outmoded, inefficient or a financial drain on the rest of the company. Rather, they have to figure out what they should and should not be doing and then take decisive action to get their financial affairs in order. If they fail to do so, they die.

When taking over a troubled company, a knowledgeable CEO checks his or her "teeth to tail" ratio, as they say in the military. It involves undertaking a thorough review of the company's assets and resources and then promptly divesting those that are not central to the future success of the institution. This forces the company to focus on its "core" business and to avoid wasting manpower, time and money on ventures that are secondary to what is vital to the long-term health and success of the company.

A good example of a corporation recently undergoing such a top-to-bottom restructuring is Sears, Roebuck and Company. Sears in recent years decided to move from a widely diversified company to a company focused on its core businesses. During this restructuring it closed a hundred unprofitable stores, took Dean-Witter, Discover, Allstate Corporation, PMI, and S.P.S. public, sold off unneeded assets and even disposed of the famed Sears Tower in Chicago. Some of the cash raised from

these sales was used to buy out thousands of middle managers and the rest was plowed back in to strengthen its basic businesses.

One of the most painful and visible aspects of their restructuring was the decision to close Sears' catalog division—the business on which Sears was built. The truth is that the catalog division was unprofitable and a drain on the company's main businesses. As difficult as it was, however, this break with the past told Sears stockholders that management was serious about fundamentally restructuring the company and putting it on a path for growth.

The experience at Sears, and the experiences at hundreds of other companies, including two I helped to downsize—G.D. Searle & Co., a pharmaceutical company, and General Instrument Corporation, an electronics company—can provide valuable lessons on how to and how not to downsize and overhaul the federal government. There is no one formula for successfully reorganizing a major corporation or the federal government, beyond the fact that it requires making tough, serious decisions, and it is often easier for someone from outside the institution who understands that this is his or her assignment to do it than it is for an insider. Also, not surprisingly, it is best done by someone who knows how to do it.

DEFINE THE "CORE" BUSINESS

As overseers of the federal government, an institution which, for the sake of discussion, is arguably in Chapter XI, Members of Congress will need to treat the job of restructuring it in the same urgent, tough-minded manner so many corporations around the country are now doing. The goal must be to earn back the confidence of the taxpayers, who are the real stockholders of the federal government. This does not mean simply "patching," as management guru Peter Drucker has characterized Vice President Gore and his associates of doing. The reason National Performance Review (NPR) efforts have received so little public attention, said Drucker, is that:

In any institution other than the federal government, the changes being trumpeted as reinventions would not even be announced, except perhaps on the bulletin board in the hallway. They are the kinds of things that a hospital expects floor nurses to do on their own; that a bank expects branch managers to do on their own; that even a poorly run manufacturer expects supervisors to do on their own—without getting much praise, let alone any extra rewards.¹

Certainly the NPR is a worthwhile effort—a good idea. But, much more is needed. Techniques such as Total Quality Management, procurement reforms, or streamlining middle management will improve government, but they will only affect the problems in government programs at the margins. Well-intended corporate managers have used the same sort of techniques and still failed or suffered. It is vital that many of these things be done, but only after one has decided and dealt with the more central issues of what businesses to be in.

The first task is to decide what the core business is. Once this decision is made, then everything else is secondary. For the federal government, the four basic departments—State, Defense, Justice and Treasury—have a solid basis for existence. The other departments were either more narrowly based, were an afterthought, or both. Some had utility when they were established, but no longer do. Others, in my view, probably did not have a need to be at the Cabinet level even when they were first established. A number of them were recommended and created less for organizational reasons and more to gain favor with a particular interest group. Once one has determined the core functions to be performed by the federal government, all other activities should be scrutinized for elimination, downsizing, reorganization, movement to state and local governments or privatization.

I begin with the conviction that the first place activities should be undertaken is with the individual citizens and private organizations; next, if government must be involved, by local governments, state governments, and only last by the federal government. In the past, this was not a workable principle in some instances because of the issue of civil rights, even though in theory it was compelling and rational. It was clear that if some activities were left to local or state governments or to individuals there would not be appropriate protection against discrimination. Given the many civil rights laws on the books today and the progress that has been made, it is no longer the problem it was in earlier periods. Today government services are being delivered to minorities in a nondiscriminatory manner.

My conviction is that as overseers of the federal government Congress ought to use federal solutions only as a last resort. The question must be asked whether a

¹ Peter F. Drucker, "Really Reinventing Government," *The Atlantic Monthly*, February 1995.

problem is truly a federal responsibility, or can it better be handled privately, by voluntary organizations, by local governments, or state governments. I understand how difficult this is in Washington, D.C., given the fact that all the institutional pressures seem to run the other direction. But I'm reminded of a sage warning former Missouri Congressman Tom Curtis once said, "Public money drives out private money." And it does.

CUT SHARPLY AND RAPIDLY

I read an article recently which set out some useful advice on downsizing from CEO Al Dunlap, who apparently did a skillful and swift job of restructuring Scott Paper Co. On downsizing, he said:

Do it once, do it severely, and get it over with. When a company says it is going to restructure over the next three years it won't happen. . . Don't do it! You paralyze the company.²

This is sound advice for the Congress as it undertakes the massive task of balancing the federal budget by the year 2002. Cut severely and rapidly. Don't wait. Whatever it is you do the odds are overwhelming that you should have done more, rather than less, and that you should have done it sooner, rather than later. There are so many pressures in Washington, D.C., to keep the status quo, that the most frequent mistake is to make too few changes or to cut too little. If in fact one cuts too much, which is very rare—indeed probably unprecedented—it is easy to add back. But, once you cut and then find you have to go back and cut again, it is harmful to an organization. Do it once. Do it well. Don't under do it. And then let people get back to work. Don't try to cut the dog's tail off one inch at a time, hoping it won't hurt as much.

And, a caution. After the reductions have been accomplished, don't turn your head for a second or you will find the waste moving right back in. It is inevitable that it will happen, and fast, unless the overseers are vigilant. As the saying goes, "If you're coasting, you're going down hill."

Although the balanced budget plan drafted by the House Budget Committee is remarkable in its specificity and scope, in my view it ignores the principle of "cutting decisively and rapidly," in that it proposes phasing out some programs and agencies over a period of three to five years. If a program or agency is outmoded and inefficient, phasing out its funding over a period of years will not make it less so. For instance, I agree with those who propose to eliminate taxpayer funding for Amtrak, the Corporation for Public Broadcasting and dozens of other programs that are not, or are at least no longer appropriate federal responsibilities. But why inflict on these programs the "death of a thousand cuts."

If Amtrak, for example, should be given the flexibility and the challenge to compete in the private sector, then why can't it be done sooner, say over the next 12 months, rather than over the next five years. My advice is to sever public ties with much greater speed.

The Small Business Administration continues to dodge reform. It was not even ten years old during my freshman term, yet, in a 1963 article on pork barrel spending, *Life* magazine exposed the SBA as a new "device for soaking up money and getting rid of it." Based upon its early track record, we should have had the good judgment to close down the SBA decades ago. I hope that this Congress will have the courage to act this year. It is never to be desired, but given the current budget situation, good intentions and throwing money at problems hoping some of it will stick and do some good is unacceptable.

DOWNSIZE

I also recommend that Congress move swiftly to cut management and get personnel costs under control. It is guaranteed that there are more managers and more staff in the federal government than are needed. In less than seven months, Scott Paper eliminated 11,200 people, one-third of the workforce. The company cut 71 percent of the headquarters staff, 50 percent of management, and 20 percent of the hourly employees. They discovered they really weren't needed.

Another example is G.D. Searle & Co., where I served from 1977 to 1985. There we reduced the centralized corporate activities down to about 20 percent of their prior size, divested some 30 to 35 businesses, sold a variety of assets, downsized the company to close to 65 percent of its prior employee base, with the not surprising result that it worked better, earned more, and investors and owners moved the stock from about \$12 a share to \$50 to \$60 a share.

² Al Dunlap, "If You're Going to be a Director . . .", *Directors and Boards*, Winter 1995.

So too at General Instrument Corporation where I served from 1990 to 1993. There we divested five or six businesses, sold a number of assets, downsized and focused on the core businesses, and dramatically reduced the size of corporate headquarters, with the result that the investors and owners of the company moved the stock from below \$15 a share to \$50 a share.

There are hundreds of companies that are doing the same thing. Some do it after they should have, others do it ahead of the curve. Some wait too long and they suffer and die. Clearly the U.S. Government is well behind the curve.

No doubt the federal government suffers even more waste on a percentage basis throughout the bureaucracy than even poorly run companies. According to the NPR, the federal government has over 280,000 persons formally classified as "supervisors, managers, and executives, all of whom perform control functions, costing billions of dollars." "At times," reports the NPR, "the federal government's management control system resembles a theater of the absurd."³ To make a point, if one used the Scott Paper model on downsizing as a guide, theoretically some 140,000 of these managers could be cut immediately, saving taxpayers billions of dollars. For example, I see fewer and fewer companies where every manager has a special assistant or two. But in government, it seems even special assistants have assistants. Don't get me wrong, I used to be one and I used to have one or two. And I suspect many of you do. Indeed, some are needed. But, the revolution in information technology has changed the way work can be done so that excessive layering of organizations can be avoided.

REORDERING THE FLOW CHART

There are a variety of ways to merge federal agencies and departments, and certainly no one way is perfect. For example, over 20 years ago, Richard Nixon and the Ash Commission recommended that there be four basic areas: defense, foreign policy, the economic, and domestic. One can find powerful reasons for either merging or terminating many of the newer departments. Some of their functions will, of course, need to continue, but certainly much of the overhead is not necessary.

While I have no special insight as to which is the preferred way to reorganize our government, I am persuaded that probably one-half to two-thirds of the non-central departments are no longer needed in their current form. For example, the Republican proposal to close down the 93-year-old Department of Commerce seems reasonable to me. It lacks a clear sense of mission and the fact that it duplicates the work of dozens of other departments and agencies is a sign that taxpayers could do without it in its present form. The same could likely be said for others of the newer departments, such as Energy, HUD, Education, Transportation and Veterans Affairs, as well as the Appalachian Regional Commission and EDA. For example, the veterans were served before the VA was made a Cabinet rank department, as they should have been. And they can be well-served, possibly better served, if it were to move out of the Cabinet and have some of its functions turned over to the private sector.

DON'T MICROMANAGE

There is no one perfect organizational arrangement. The right people can make a poor organizational structure work well, and wrong people will assure that the best possible organizational arrangement will work poorly. People are the key. That is why the delays in the Presidential appointment process have been so damaging. In many cases, cabinet and sub-cabinet posts have not been filled until after a non-trivial fraction of their entire term is over.

An important rule for a corporate board is to avoid trying to micromanage the CEO and the company. Boards need to give management the direction to be sure, but also the freedom to run the company in the most effective and profitable way they see fit, and then hold them accountable. One of the problems in government, and something that contributes to waste and mismanagement, is legislative micromanagement of the Executive branch. My recollection from my days in the Executive branch is that Congress imposes so many restrictions, requirements and requests on the Executive branch, no one of which is debilitating, but in the aggregate are like the threads the Lilliputians used to prevent Gulliver from moving. This was certainly a problem at the Pentagon and I suspect still is, because of the blizzard of requests for studies and the directives and rules generated by the multiplicity of Congressional committees and subcommittees. I want to commend you for taking

³The National Performance Review, "Streamlining Management Control," Creating a Government that Works Better and Costs Less: Accompanying Report of the National Performance Review, September 1993, p 1.

steps to reduce the number of committees and subcommittees earlier this year. It was a good start.

However, smaller government is an unachievable goal if Congress continues to try to tell the Executive branch when to turn right, turn left, speed up, or slow down. What Congress needs to do is tell the Executive branch generally the direction to go, where the sides of the road are, and what the speed limit is. Then Congress should stand back, oversee, and evaluate the administration on how well they do it, and if necessary calibrate the directions or change the drivers. Too many hands on the steering wheel will put the truck in the ditch.

BIG GOVERNMENT AND BIG BUSINESS

Anytime anyone proposes a change, there will be opposition and concern. Change is not easy for people. However, the fact that there is opposition and concern about proposed changes does not mean that the changes are undesirable. Indeed change in both people and organizational assignment can bring in fresh thinking and approaches. Certainly the entire country has seen the fresh breeze blowing through the Congress since the changes earlier this year. It is refreshing, as even a number of my friends from the new Minority agree.

In Washington, D.C., change is a particular problem for several reasons. Any change in the Executive branch tends to result in changes in people and organizational structure. The effect is that makes life less certain for people in the bureaucracy, which not surprisingly they resist. It also makes life difficult for those they deal with—Washington lawyers and lobbyists. These folks have invested many, many years in the relationships and knowledge they have achieved, which, for them, is the coin of the realm. Therefore, it should be no surprise that they often become the earliest and most effective opponents of change. This is not because they think the change is unwise or unnecessary, but because they could lose their investment in the people and the structure as currently arranged. They would have to start over again developing such relationships and knowledge. This is certainly not a reason not to change.

Further, any change proposed in the Executive branch tends to result in difficulties for Congressional committees in that jurisdictions of committees can be affected. There will be winners and losers. Therefore the predictable result of any proposed change tends to be that some Members of the Congress oppose it. Here again, it is not a reason not to change.

It is important not to lose sight of the reality that Washington, D.C. is arranged in a way that only large companies are able to hire the lawyers, lobbyists and representatives necessary to effectively interact with the Executive branch of the federal government and the Legislative branch to their advantage. Only large companies have the resources to stay the course while the Executive departments and agencies study and delay decisions on matters that directly affect them. Indeed, that is a competitive advantage large companies have—they have the resources and they have the staying power. Big businesses have the institutional capability to effectively interact with big government. That is not true of small businesses. Dealing with the federal government can suck the very life out of small companies that have to compete with big businesses in trying to avoid having government unintentionally take actions that are harmful to them.

A THOUGHT FOR CONGRESS

Thirty years ago, I testified before the Joint Committee on the Organization of Congress. One of my recommendations was to terminate the practice whereby Members of the House and Senate frequently announce federal grants, contracts and projects in their states and districts. It didn't happen.

I said then:

. . . to encourage or assist Members (of Congress) in making initial announcements of Federal grants, projects, and particularly Federal contracts, leaves at least a shadow of a question as to whether or not the contract or project was awarded solely, as it should have been, on factors such as cost, performance, and national interest. I would think that a procurement officer or Corps of Engineers' official, for example, who based his decisions on needs, cost, and performance, would not be pleased to see Members' announcements of these contracts or projects leaving the impression that they may have influenced his decision.

I suggest that government likely would shrink if Members ended this policy and thereby eliminated the incentive to have the federal government become involved in so many activities that belong in the private sector or in state or local govern-

ment. In short, implementing that recommendation would help. As long as this practice remains, the incentive will be upside down and more and more activities are likely to move toward Washington, D.C.

PRIVATIZATION INSURES ACCOUNTABILITY

"Corporocracy" is a term relating to the private sector, meaning corporate "bureaucrats running corporations for their own good and the shareholder be damned." Fortunately, and not surprisingly, the competitive marketplace punishes companies that become "corporacies." Indeed, the most valuable thing that exists in business and in the non-governmental sector is the opportunity to fail. And fear of failure focuses the mind. Government programs are effectively insulated from the rigors of the marketplace and therefore are denied the possibility of failure. The task for government is to find some substitutes or proxies for the possibility of failure—for the "bottom line"—in business. One approach would be to have more "sunset" provisions to force legislative review after a period of years. While not always appropriate, one other essential way of brining this level of accountability to the delivering of services is privatization.

Some thirty years ago, Nobel Prize Economist Milton Friedman told me that the best way of curing the problems of waste and inefficiency in the U.S. Postal System, then the Post Office Department, was to amend the law so it would no longer be a monopoly, and thereby would be forced to compete. He was correct. I have questions about some of the so-called "government-owned" corporations. One effect can be to insulate such an activity from being accountable to either the marketplace or to Congress. And, everyone needs to be accountable to someone. The U.S. Postal Service and Amtrak are two examples. Still other so-called government corporations, such as the Legal Services Corporation, aren't really corporations. All the word "corporation" in their title does is befuddle and confuse.

Certainly a number of these activities should be cut loose from the taxpayers' purse and allowed the privilege of competing in the marketplace. Competition is what brings out the best in people and organizations. As the saying goes, "it is your enemies who make you strong." I am attracted to the idea of divestiture or privatization of a number of government-owned enterprises such as the Air Traffic Control System, the Naval Petroleum Reserve, the Government Printing Office, public housing, defense stockpiles, and unneeded federal buildings and real estate. I have no view as to whether it might make sense to make some of these activities "corporatized" government agencies as an interim step toward full divestiture. In some cases, such a step might be useful in getting the some enterprise's books in order, providing time to inventory their assets, and in preparation for selling them off to people who know how to run such activities.

ASSET SALES

I have trouble understanding why the federal government should be borrowing over \$200 billion per year to cover its deficit when it is sitting on billions worth of assets that could and should be sold to the private sector to raise cash and which would then be forced to operate on a more cost-effective basis. As the Dunlap article points out:

Inside every corporation is the biggest bank one is ever going to find—its own assets. My philosophy is, before you go looking for outside funding, look inside first at what you don't need. We sold S.D. Warren, a paper subsidiary, for \$1.6 billion. It was a fine company but I believe you can't be in two capital intensive businesses and do well at both. We sold other operations and have another \$1 billion of assets on the block. We are on track to be debt-free in 1995. All this from a company that was heavily in debt, whose bonds weren't investment grade, when I arrived.

Some twenty years ago, I chaired the Property Review Board in the Nixon Administration, which supervised the review of literally hundreds of federal real properties for movement to their highest and best use outside of government. The resistance in both the Executive and Legislative branches was enormous. That opportunity is still there and, given the current budget situation, must be seized.

Unfortunately, I am told that for the past decade or so, asset sales have been seen as somewhat of a gimmick here in Washington, D.C. It is not a gimmick in the business world and need not be seen as such in government. The goal of such sales is to use unneeded or underutilized assets to reduce liabilities and to free up funds to be focused on more important needs. This is a business-like strategy I believe the U.S. Government could usefully adopt. I understand that the Majority's balanced budget plan does target a number of assets for sale to the private sector such as

the Power Marketing Administration, the Helium Program, and the Uranium Enrichment Corporation.

That would be a start, but there are billions of dollars in assets which could still be tapped to reduce government's borrowing. For example, the Heritage Foundation, in its very useful study, has suggested selling the government's \$150 billion portfolio of direct loans to the secondary market. This is an idea that could generate as much as \$100 billion in cash. Such steps could save taxpayers billions in future interest payments as well as have the advantage of moving such assets out of the government and into the more productive private sector.

CONCLUSION

As the Congress goes about the business of putting meat on the bones of the balanced budget plan passed last month, it will have to make tough decisions. I recognize the difficulty of that task, having served here in the House. But I've learned that the decisions that are made every day in the corporate world are sometimes even more difficult, because the very survival of a company can be at stake. The choices you make affect people with real careers, mortgages and families to raise, to be sure. But since you oversee an enterprise facing bankruptcy, you can have confidence that the decisions you make, however tough, can help to restore the long-term health of the government, our economy and our country.

I thank you for this opportunity to share these thoughts, and I would be happy to entertain questions.

Mr. HORN. Very good. As you can see, the green light is still on. We gave you a long 5 minutes, at the chairman's discretion.

Does the gentleman from Illinois want to begin the questioning?

Mr. MICHAEL FLANAGAN. Thank you, Mr. Chairman, for the amazingly insightful use of your discretion.

Good morning.

Mr. HORN. I knew he was from Illinois and I'd better treat him right.

Mr. MICHAEL FLANAGAN. Good afternoon, Mr. Rumsfeld, and permit me to further congratulate the chair on yet once again choosing a high-speed, superintelligent individual from the great city of Chicago to come and inform us on how to do things better, and I thank Secretary Rumsfeld for coming here today and congratulate him.

I perked up with great fascination at your comments and your opening remarks for the Federal Government to decide what businesses we should be in and what things we ought to take care of, and it was remarkable, your demonstration of this showing how the roles of the Federal Government have exploded so over the years from the first Johnson administration and \$100 billion total budget, able to run a military and everything else that happens with that. Even understanding the dollar was different then, it still is a colossal change in the scope, the drive, and actually the role of Government, and I'd agree with you also that it is amazing how it is misplaced effort to tinker on the edges with trying to help or hurt programs that we think should or should not be here.

I take small exception to phasing out programs that the Federal Government shouldn't be in. The cold turkey approach could be particularly harmful to local governments, but in theory and in practice in many portions you are absolutely right, we are devolving the power from the Federal Government to the States all at once maybe a little more harsh than we can do. But as for the areas that Government shouldn't be in the business of doing at all, you are absolutely correct.

Because I can only recognize a cow two out of three times correctly, I'll call it a dairy refinery for the purposes of our discussion, but I think in the vein of what you are talking about we have gone

from a dairy refinery to a pork slaughterhouse, and we have to look very closely at where we are going with that. Before we leave Chapter 11, hopefully we will go to fiscal solvency instead of to Chapter 13.

On the issue of accountability—and this is something we discussed with Mr. Munoz of the Treasury Department when he was in and something I would like to take up with you and hear your views on it—there seemed to be a discussion of the approach that we should take in regard to making agencies more efficient and more capable. Consequently, we are working on incentives to get agencies to collect outstanding moneys owed to the Federal Government of the United States and to make them more efficient in the disposition of the moneys which they are given.

There seem to be two approaches, one that I have championed and hope will be done, and the other which is a level of financial incentives for the agencies where their budgets will grow in proportion to the amount of money that they collect or save, and, you know, other countries have used this successfully.

New Zealand, for example, gives a bonus to its high officials when inflation rate is low and the budget is well controlled. I champion the other side; that is, to make it a mission-essential task of that agency to accomplish these fiscal goals and to decide whether the agency heads or functionaries in the agency have been successful in their jobs by whether they have accomplished these goals or not, and their having not been successful will define them as a failure and find someone who can be successful in doing these things.

I think you alluded to this in your statement when you were talking about things that most companies would leave relegated to middle or lower management and would chagrin at the thought of rewards and not even think of it but merely refer to it as a mission-essential task of their job, and I wonder if you can expand upon that, or have I got the right reading of what you are thinking about this?

Mr. RUMSFELD. No. I think that is an important issue.

It seems to me that in the private sector the general pattern is that both techniques are used, the carrot and the stick, and they are used for quite different things. Normal performance, expected performance, functioning within a job specification, is certainly not rewarded for acceptable performance of the basic job. The salary and the normal compensation handles that. Incentives are used to try to elevate people to a level that is higher. And they tend to be used only for people who are in a position to make a difference.

It worries me a bit about Government using certain business practices, and when you take business practices and put them into Government and Government still doesn't have a bottom line. It doesn't have the ability to fail, if you will, or at least to die. Government has the ability to fail and continue, unlike the private sector, which can fail and die and disappear. Both are certainly appropriate in the business world. But, I think the role for carrots are modest in Government.

User fees are something, of course, that from time to time are left to be used where they are raised and not recycled back through the Treasury into general revenues, and then the authorization and

appropriation process, and that is fair enough. It seems to me there is nothing wrong with doing that.

Mr. MICHAEL FLANAGAN. Your remarks are particularly poignant in that the carrot and the stick delineation line is at the level of expectation of the actor, and I think the expectation of Government has sunk so low that they need to be rewarded to do what we once merely assumed was their job, and I think that that is something that we have to encourage and foster and demand once again from the agencies who administer and steward our money and take care of the things that are done here and provide incentives for smarter, better action or something that would be extraordinary or extra-neous to their job. I agree.

Thank you, Mr. Secretary.

Thank you, Mr. Chairman.

Mr. HORN. Thank you.

The gentleman from Virginia, Mr. Davis, 5 minutes for questioning.

Mr. DAVIS. Thank you very much.

Mr. Secretary, before I was in Congress I was the head of a large county Government out in Fairfax, VA, where we tried different carrots and sticks. One thing we found appropriate is, we had tried earlier on, if managers could save a certain amount of money each year, giving them awards, and that didn't work. They would save money, return it to the treasury, and it would go to agencies that overspent, and there was just no cause and effect. We finally let them keep some of the money that they had saved and use it in their agencies for certain unspecified purposes, and we saved a lot of money that way. When money saved from their agency, a percent of that, could be plowed back into their agency for other items they couldn't get, it was a great incentive, and we saved millions of dollars annually on that. Managers reacted very well to that.

I don't know if that is the kind of carrot that works in this case, if the bonus system works in this case. They use it in the private sector all the time for managers to meet limits, or how you define success, which you allude to. It is tough because you don't have a bottom line to measure it by.

New Zealand has the Government Performance and Results Act where the Governor of New Zealand's central bank gets a large bonus when inflation is less than 2 percent, and of course he makes sure it is kept low for that reason. Can you think of any other incentives like that we might use in our system, result oriented?

Mr. RUMSFELD. I would be slow to use them in Government. The problem in Government is that Government is doing too many things they ought not to be doing. To the extent those things are done in the private sector or done at a level of Government where they can be more properly monitored and overseen, I think that you don't need to worry about how they are going to function. They are going to function a lot better than they will if they are in a large behemoth such as the Federal Government of the United States and remote from people who have any ability to affect them.

The problem with using incentives is that you don't have a bottom line in Government. I think that the appropriation process and the role of the Congress to appropriate funds is important. To the extent that a host of things end up being run outside of the normal

process you run the risk of having a whole lot of activities flourish while activities that don't have the ability to raise funds can't flourish in the same way, in terms of being able to use the fees or the commissions.

In terms of bonuses, I know that since I left the Federal Government they have installed various bonuses. I frankly have not used them in a Government environment. I'm modestly uncomfortable with them.

Mr. DAVIS. OK.

Mr. RUMSFELD. I think that one of the things that ought to be done is that the civil service rules for executive branch employees ought to be changed so that a manager has a better chance to manage his agency or his department. In the private sector when you have activities that aren't going right you let people go. You terminate them. If their performance isn't good enough, they leave. In the Federal Government if you try to do that you spend your whole career trying to figure out a way to rearrange people in a way that makes sense.

Mr. DAVIS. You can transfer them or do something else or fight it forever to try to get a termination.

Mr. RUMSFELD. Yes.

Mr. DAVIS. One of the Reinventing Government Initiatives was to downsize the Federal Government by I think it was 250,000 employees or whatever. But that strikes me—you talk about doing it by function as opposed to setting an artificial limit and going after it. It just seems more sensible to go after functions, decide what is important given our priorities and ability to pay, and I gather from your testimony you think that is the way we ought to go.

Mr. RUMSFELD. I think you begin first with what are the things you want the Federal Government to do, and you move everything else out to somebody else, whether it is State government, local government, or the private sector, and let them rationalize it. I wouldn't try to rationalize it before making those moves. When I do it in a company or when I've done it in Government, I've done it that way. I've taken pieces and moved them out and then let them get rationalized at the level where they are going to be operating.

Mr. DAVIS. OK. All right. Thank you very much.

I yield back.

Mr. HORN. Thank you.

The gentleman from Florida, Mr. Scarborough, did you have an opening statement you wished to submit?

Mr. SCARBOROUGH. I don't have an opening statement. Thank you, Mr. Chairman, for holding this hearing. It is certainly important. And I would also like to thank you for coming this afternoon and testifying before this committee. You certainly are preaching to the choir, and I certainly appreciate especially the need to move quickly and to be decisive in downsizing decisions.

I'm heading a task force looking into moving the Department of Education out of Washington and back home across the country, and I'm amused by those testifying against that, saying how they are downsizing and reinventing government and cutting costs, saying they are cutting \$19 billion over the next 3 or 4 years, but then

you look at their budget over the next 3 or 4 years and they are actually asking for more and more money year in and year out.

So, again, I thank you for your testimony and certainly hope that Congress will have the political will to do what you are recommending that we do.

Mr. RUMSFELD. Thank you.

Mr. HORN. Thank you.

Let me first say to the reporter of debates that I have the statement of the ranking minority member on the full committee, Cardiss Collins of Illinois, and that will go at the beginning of the record when we had other opening statements.

Let me ask you several questions, Mr. Rumsfeld, that related to your very stimulating testimony. In the rush some of your better lines were left out, and we might resuscitate them, and I thought one of them was certainly the comment, "My recollection from my days in the executive branch is that Congress imposes so many restrictions, requirements, and requests on the executive branch, no one of which is debilitating but in the aggregate are like the threads of the Lilliputians used to prevent Gulliver from moving." I completely agree with you. Part of the problem is Congress, and we need to discuss that.

You have had the unique experience of the private and the public sector. You had the second toughest job in the Government of the United States, in my humble opinion, which is being Secretary of Defense—complex organization; completely different cultures and different services. I would like your thoughts as to the type of corporate culture you have dealt with, how you compare it to the government culture, what if anything should be done, whether we are talking incentives, as has been discussed by some of my colleagues, or structural changes that might change behavior that would be in the taxpayers' interest. Do you have any thoughts on that?

Mr. RUMSFELD. There is no question but that the problem of micromanagement does not exist in the private sector in the normal environment, and it is a serious problem in the executive branch of the Federal Government. No one of the requests or the requirements is, in and of itself, unreasonable. What happens is that, when they are aggregated the effect of them is that Gulliver can't move. A senior management in an executive department spends so much time testifying, responding to Members, responding to staff members. The explosion in the number of subcommittees that took place—and I do commend the Congress for reducing the numbers of committees and subcommittees—had the effect of focusing the executive branch away from what they were doing toward the Congress, and that doesn't happen in the private sector. In the private sector you can actually decide what you want to do, do it, evaluate it, find out it was imperfect or needs to be recalibrated, recalibrate it, and then go about your business or stop it if it doesn't work.

In the Federal Government you of course can't do that. You are constantly jerked around in what you are attempting to do. They keep pulling the plant up by the roots to see how it is growing before it has had a chance to even take hold. There are hearings, and there are investigations, GAO studies, and so forth. As I say, I'm

not against oversight, I believe in it, and certainly that needs to be done, but it is a very serious problem.

I would say about the Pentagon in particular that it is a very different institution from others because of a couple of things. First, is the fact that you need civilian control. So, if in a mindless way you begin reducing at the Pentagon you may sheer off that thin layer of civilian control over the military which is not desirable.

Second, there is a certain centrifugal force that still exists in that institution among the services, a tendency to want to pull apart. There too, to the extent you reduce in a way that is not very careful, you can have a nonintuitive effect, and, in effect, contribute to the centrifugal force by reducing those things that allow for the jointness that is necessary in the modern world. So that, as an institution, is quite unlike some of the other departments and agencies, and one has to be careful in doing it.

Mr. HORN. Let me pick up on another phrase you have here with which I completely agree. You say, "For example, I see fewer and fewer companies where every manager has a special assistant or two, but in Government it seems even special assistants have assistants, and I've watched this since the Eisenhower administration." You are absolutely correct. As Professor Light, who will be testifying here later in the summer, has noted, we have got a thickening of government. I'd like you to reflect on the days when you were in the Pentagon and your observations as to why we need civilian control and people with a broad perspective that have the trust of the President over there for the Secretary, Deputy Secretary, Service Secretaries, Assistant Secretaries, and so on.

We also need clear lines of authority in communication, and what bothers me is, we have all these staff agencies which are growing like Topsy, and a lot of those are civil service, some are noncivil service, some are Schedule C political appointees, which to justify their existence, seem to be clogging up the works, and I would think a Secretary has his or her hands full when they deal with that network in their attempt to get something done. What is your view on that?

Mr. RUMSFELD. I do think that there was a pattern over the decades, particularly in the sixties and seventies and eighties, for layers of people to be added. My impression is today that the revolution of information technology has created a situation where we have the ability to do a lot more than we used to in terms of how we do our work, and it is possible today to do a lot of delayering, relatively easily, I would think, without any loss in productivity and indeed conceivably with an increase in productivity.

One example: At one company where I was chief executive we took the corporate headquarters from something like 750 people, centralized activities, down to roughly 100, and it worked better. There were fewer people sending each other notes, and there was less work to do, and people were forced to stop doing some things, the bottom 10 percent of what they were doing, which really was the lowest priority anyway, and so I think that one should take advantage of the information, the technology, that is available today, and I mean I started out as an assistant to a Congressman not too much before you did back in the 1950's here when Eisenhower was

President, so I've got nothing against assistants, but I think it has gotten a little out of hand.

Mr. HORN. Yes, we have too many up here too, and, as you know, we cut committee staff one-third, long overdue because you had a proliferation that really wasn't solving anything.

Mr. RUMSFELD. Yes.

One other thing, I'm on the boards of some small companies. This town works fine for big companies. It doesn't work well at all for a little company. Big companies have the law firms on their payrolls, they have the lobbying firms on their payrolls, they have all kinds of representatives, they have the resources to have staying power over weeks and months while discretion is being exercised by the Federal Government. So, to the extent the Federal Government has a whole lot of things it is doing, that affects the private enterprise system and has a whole lot of people doing them and a whole lot of people calling up those companies, asking for this information or to do this or to do that or come to a hearing, or, "We are going to reconsider this," then those small companies, it can suck the life out of them. Senior management spends all their time down here just trying to stay alive, and that is an unhealthy thing. They ought to be out selling or making or doing whatever it is they do. It is one of the competitive advantages that large companies have, is that they can do it relatively easily, and they don't complain. Indeed, frequently it is the large companies that like Government to be involved in something. It is the small companies that get crushed by it or drained of their energy.

Mr. HORN. I yield 5 minutes to the gentleman from Illinois, Mr. Flanagan.

Mr. MICHAEL FLANAGAN. Mr. Secretary, you have touched once again on a core issue that has to do with where we are going and what we are doing, and that is a continual devolution and abolishment of some governmental functions, and I think there is a two-step question to the paradigm that you have set up, and, first, the one that you have articulated is, should this be something that the Federal Government is doing?

I think the second question—and it is really a harder question and has to do with our prioritizing spending as much as the first question—is, should this be a function of Government at all and should this be something that Government does, period, whether it be at a State or a local level or at the Federal level, and is this something we wish to foster down, or is this something we wish to abolish while we can, and that is also on our minds as we go through that, and I offer those comments gratuitously.

We wish to work with the President, and the Vice President has talked about reinventing government on a regular basis, and the proposals are nebulous at best. Perhaps you can offer us some insight into which, in those two points, things that Government should do at all or at least things that should not be done by the Federal Government, perhaps an example or two, not to pin you down or nail you to the wall or anything like that, but perhaps maybe just major areas that we should look very hard at, either our inability to get it done right or our lack of ability to do it at all.

Mr. RUMSFELD. I must say I looked over the Heritage Foundation's study, a rather thick book, and the way they have aggregated them, in a manner not dissimilar to the way you have suggested. It has there a whole series of examples of activities that in some instances are obsolete, that are not needed any more, and there are some things that have not worked terribly well as another category. As I recall, the list must have had 10 or 15 items.

The other category is examples that I mentioned in my opening remarks where it was something that obviously was not a Federal responsibility, not a national responsibility, but it was taken under the national Government because it was not being handled well at the State or local government, partially because of the civil rights issue, and in my judgment that was a legitimate thing to have done, but it is every bit as legitimate today to denationalize those activities and move them back to the State and local governments where we know services, in fact, are being delivered in a non-discriminatory manner or people go to jail. So there are those activities.

There are some activities like the Corporation for Public Broadcasting, public television, and public radio, which is a source of debate and discussion in the Congress right now. People can come up on different sides of the issue. I happen to like public television and public radio, National Public Radio. I also happen to think that it is a perfectly legitimate thing to move that out into the private sector and that it, in fact, can be sustained on a nonprofit basis through contributions, and if it wishes to be on a privatized basis on a for-profit basis, that there are any number of activities that the two activities, radio and television, do that, in fact, could be handled on a for-profit basis. I mean there is an example of something that is currently being debated.

With respect to the departments and agencies, during the Nixon administration, as I mention in here, the Ash Commission came up and came out with the four basic departments—State, Defense, and Treasury, and Justice. The rest evolved over time, some with good reasons that were appropriate then but aren't so appropriate now, others with not so good reasons really as a way to appease some political interest group that wanted a Cabinet department. It wanted it shown that that was terribly important.

Anyone can organize things the way they want, but I think it is relatively obvious to most people that the bulk of those other departments do not need to be Cabinet departments. Whichever ones someone wanted to leave and then aggregate other pieces under is pot luck as far as I'm concerned. I don't think it makes a lot of difference.

For example, the Veterans' Administration functioned for veterans prior to the time it became a Cabinet department. Those functions—certain of those functions clearly need to be performed, and they need to be performed well for veterans, but they do not need to be performed by Cabinet-ranked department, notwithstanding the fact that people want it because they think it elevates the importance of veterans. I personally think the affairs would be handled better in a nondepartment in some other way.

Mr. MICHAEL FLANAGAN. You cut to the quick in a unique and refreshing way. Without a lot of edge talk, I think you do say what

is on most people's mind. And it is good to hear it plain from time to time without a lot of what I like to call lotus position language about where we need to go and what we need to do.

If I may ask the chairman's indulgence for just an additional 60 seconds, I would like to key in one more time and be sure that we have it clear, and that is, to what level do you believe that the Federal personnel system is a barrier and in whichever way you think it functions worst or best to actually achieving the streamlining level. Can we get to a point where we won't have 750 people in a management situation, where we can get to 100 who work better, smarter, with better technology at a significantly reduced savings who actually produce a better, if you will, product?

Mr. RUMSFELD. Well, very briefly, I have not worked full time in the Federal Government since 1977. I served as President Reagan's Middle East envoy and was involved in the mid-eighties, and I have been on a number of advisory boards and activities, so I don't pretend that I'm current, but when I was active in the Federal Government and when I compare it to what I have been able to do in the private sector, there is no question but that you spend an enormous amount of time trying to figure out how you can reduce and rearrange things in the executive branch of the Federal Government which you do not have to do in the private sector. You can move with much greater dispatch. You can, in fact, arrange things in a way that you improve productivity and efficiency, and the net effect is that people are happy and more productive themselves, and I would certainly not ignore that aspect of it.

I'm unfortunately not in a position to tell you precisely how I would address the civil service situation. There is no question there are enormous pluses to it from the spoils system, so I don't want to throw the baby out with the bath water, but I think there ought to be ways to improve it.

Mr. MICHAEL FLANAGAN. I thank you, and I offer you that I think the reputation or at least the public image of a civil servant or the civil service generally, like most things, increases with the difficulty of being able to hold on to it, and I think people say it would be nice to come to a time in our life when someone can say I worked for the Federal Government for 30 years and people will be amazed that, because of the high standards required and because of the difficulty in holding on to that job, they could say, well, you were an awesome achiever in being able to hold a job that hard that long as opposed to merely shrugging and saying, "Well, doesn't everybody?" And I think that that would be really a wonderful thing to get to 1 day.

Thank you, Mr. Chairman.

Mr. HORN. The gentleman from Florida, Mr. Scarborough.

Mr. SCARBOROUGH. Thank you.

I just have one question I would like to ask you, if you could to give us a little bit of historical perspective from your vantage point on the political feasibility of your recommendations actually making it into legislation that passes.

Given the fact that you served as a staff member in the Eisenhower administration, worked in the legislative branch as a congressman in the Kennedy and Johnson administrations, and then went over and worked for the Nixon and Ford administrations, you

certainly have a perspective on what has been going on in Washington, at least since 1957, and of course we have had the Grace Commission reports before; we now have Al Gore talking about re-inventing government, and it seems to me that we have had these impulses in the past and yet we have seen Government expanding, continuing to expand.

Do you see 1995 as providing the type of political environment that is finally required to push through some of your proposals and some of your suggestions, or do you think we may fall into the same pitfalls that we have experienced over the past 30 years when we have tried to do this?

Mr. RUMSFELD. I must say I'm enormously optimistic. I feel a fresh breeze blowing through the country and through Washington. We have a lot of evidence that a lot of the good intentions and the efforts that were put into programs didn't really work as well as people had hoped, and people are beginning to address that and accept it.

I serve as a trustee of the Rand Corp., and we do a variety of analyses, multidisciplinary analysis, rigorous policy analysis, on domestic as well as national security issues, and there are a lot of things that just don't work out the way people had hoped, and that is fair enough. There is nothing wrong with trying things. But people recognize that there have also been some nonintuitive effects where not only have things not done the good they were intended but they have done some harm. People are ready to face up to that. Particularly the people who were the intended beneficiaries of a lot of these programs have to know that they have, in many instances, done harm and not good.

The change I mentioned with respect to civil rights changes gives us the ability now to move some things to State and local governments. I feel that there is a real possibility to do that.

I also think that our Government has managed to work itself into a budget situation that creates a much more immediate incentive to get our house in order, because it is pretty clear that at a certain point, if we go down the road we are going, we are going to be imposing enormous damage on our society, on the people of this country and on generations yet to come.

So I think that the incentive is there. I think the willingness is increasingly there.

The National Performance Review—I'm not an expert on it, but I've read some materials about it—it's a good idea, it is a good thing to be doing. It isn't, in my view, anywhere near enough, and in a sense it is at the margins as opposed to dealing with the more central questions.

There are plenty of companies, for example, that have Total Quality Management and still go broke because they are in the wrong business and they weren't doing that which they ought to be doing, or they didn't engage in the kinds of asset sales and divestitures so that they could focus all their assets on what was really important.

I mention in my testimony the Property Review Board during the Nixon administration. We reviewed hundreds of pieces of property, and the to resistance to doing anything about it was just enormous. Now today that is different. Today people recognize that the Fed-

eral Government owns a lot of things it shouldn't be owning. A, it doesn't need to own them; B, they will be more efficiently and productively managed in the hands of others, whether it is Federal, State—whether it is State or local government or the private sector, and I think people see that. I'm reasonably optimistic about it.

Mr. SCARBOROUGH. Great. Well, I appreciate your testimony today.

Mr. HORN. Let me pursue the questions of accountability and responsibility. When we say some agencies should be in the Cabinet, some departments, some functions recognized and some should be independent agencies or at least not in the Cabinet, don't we have a problem where the President and the President's immediate staff are less likely to be involved with independent agencies than they are with the work of Cabinet departments? Don't we also have a problem, in trying to get the best person in the United States to head that independent agency? The Cabinet status is certainly psychologically alluring, to get some people to give up their private sector job. How do you feel about that?

Mr. RUMSFELD. Let me address that in two pieces.

First, you are right, the President's staff is less likely to be involved if an activity is not a Cabinet department, and I would say wonderful. There is no reason in this good Earth why the President's staff has to get involved in every aspect of the Federal Government. They don't bring a dadburned thing to it. I mean about all they are capable of doing frequently is telling them to turn right or turn left or hire this secretary or don't hire this secretary or hire that political appointee or don't hire that political appointee. They don't bring any value to those departments, agencies or independent commissions.

Second, with respect to status, that's right, you are right on both counts, but my attitude is, you know that you have to weigh the benefits and the burden, what are you getting for what are you giving up. In my opinion you are going to gain a lot more than you are giving up.

Furthermore, I forget who it was—Huck Finn—said you can't pray a lie. I mean you can't live a lie. Those departments that were not supposed to be departments, that were elevated agencies, are still nothing more than elevated agencies, and a trained ape knows it. When they look at it they still see exactly that. So calling it something else doesn't make it something else. It is like calling the Legal Services Corp. a legal services corporation. It doesn't make it a corporation. Just because we use corporate words to try to make a Government function seem like it's efficient, productive, and business oriented doesn't make it so.

So I wouldn't worry a bit about taking half to two-thirds of those Cabinet departments besides the four basic ones I mentioned and move the pieces into one, two, three, of them, and move some of the pieces over to the Defense Department, some of the pieces into independent agencies, and be done with it, save a lot of money, a lot of superstructure. I don't think that the status issue has a weight anywhere near the advantage that would be gained. And there is a great benefit in not having the President's White House staff horsing around with them.

Mr. HORN. Well, of course independent agency status doesn't mean the staff can't horse around with them.

Mr. RUMSFELD. That is true.

Mr. HORN. In the sense that they have got budgets for clearance, they have personnel authorization for clearance, and so forth.

You mentioned the Ash Commission, the Nixon departmental reorganization program. I'm looking at the chart, and while they started with the four basic departments that George Washington had in his day called State, Treasury, War, and Justice, or the Attorney General, and then under Nixon, State, Treasury, Defense, Justice, and the following: Agriculture, Department of Community Development, Department of Natural Resources, Department of Human Resources, Department of Economic Affairs, and of course what they did say in community development, you had urban and rural development assistance, you had housing, which of course is HUD now—and a lot of people are talking about changing that—highways, urban mass transit in transportation, since elevated separately, and Federal high risk insurance programs, which are really run by FEMA—Federal Emergency Management Agency. Then they put in natural resources, energy, and mineral resources, and of course we now have an Energy Department as well as Interior, and then some of the marine atmospheric resources which are over in Commerce, really 70 percent of Commerce, which a lot of us feel should be abolished although Herbert Hoover might not be happy with that thought since he was the great Secretary of Commerce in the twenties. But all the important functions are somewhere else, such as Mickey Kantor being the U.S. Trade Representative. That is what a Secretary of Commerce ought to be doing. One will argue, however, that it is hard for a Cabinet officer to coordinate his colleagues unless the President makes it very clear he is the straw boss.

And then Department of Human Resources. We now have HHS, and that is where Nixon's people would have put health services, income maintenance, and security. In the last Congress we made a separate Social Security Administration independent of HHS.

Education is a new department since Nixon's time. Manpower basically is the tail that wags the labor dog and is where the big money is in labor, and we have one proposal before the Congress, Mr. Gunderson of Wisconsin, to merge labor and education so you would have a continuum of formal education as well as worker retraining.

Then for social rehabilitative services, the Nixon commission proposed a Department of Economic Affairs. Domestic, international commerce, science and technology—we have a separate National Science Foundation. Social and economic information is spread over Commerce with the Census, Bureau of Labor Statistics, and Labor.

It was interesting. Once they got down to it, they got beyond the four basics that were good enough for George Washington, and a lot of people might say maybe we ought to go back to what Washington did. You could sit around the table. You actually made some collective decisions. When George went home to Mount Vernon from New York in the summer, Hamilton and Jefferson and Secretary Knox and Attorney General Randolph ran the Government, all couple of hundred at the most, and, as Jefferson said of the De-

partment of State about his inherited civil service, few die and none resign. So I understand the personnel policy. So did Thomas Jefferson.

But what do you think about how you would really get the basics right now given your philosophy, given what Ash and that group were trying to do? What would you cancel? Everything but those four basics?

Mr. RUMSFELD. No. First of all, I'm not a purist on this and I don't know that my judgment would be any better than anyone else's as to which one should be the survivor. But setting aside the four basic departments, you probably can make a case for two, three, or four of the others, and the rest clearly you can't make a case for.

It doesn't make a lot of difference which ones you leave, to me, as the survivors. You are going to end up clustering rational pieces under them, create bureaus and divisions for some activities, strip away a lot of the assistants, levels and bureaucracy that attach to a Cabinet department, and in the process move a number of activities to State and local governments, and you would be taking some activities and privatizing them. You would be reducing the span simultaneously. It is something that a handful of reasonable people could sit down and come to conclusions as to how it ought to be done and set about doing it. I would think it would be something that would be very bold and interesting from the standpoint of the President of the United States and the executive branch. I mean anyone who is down there in the White House has to know that the organizational arrangement doesn't work very well.

Now every time we try to change it this town bands together and stops it. The investment that Washington lawyers and Washington lobbyists and the Washington press have in the status quo is enormous. They know the people, they know their offices, they know their phone numbers, they play golf with them, they work with them, they like them, they respect them, they understand them. Once you start eliminating, altering organizational charts, changing people, reducing, their value diminishes.

The same thing with Congress. Every time we try to change anything, a committee's jurisdiction is affected. There are going to be winners, there are going to be losers, so they resist change. You hear all this bleating about how terribly important it is that each department stay exactly the same so congressional committee would stay exactly the same.

Well, those are not good reasons for wasting the taxpayers' money, they just aren't, and we are at the point now where people, I think—maybe it's just me, but I come into this town, I love this city, and I have lived here for a great many years, and I walk down and I see a new Federal building going up and I shudder. I say why? We don't need more space down here. We don't need it. It is not right. It's not right. And I think the American people feel that way.

Mr. HORN. One last thought because I know we are pressing the time of other panels, but it seems to me the only way to get the job done is what we tried earlier in the fifties, which was, give the President the power to reorganize and move the structures around and we vote it up or down, like the base closure process.

Mr. RUMSFELD. Just reverse the veto.

Mr. HORN. That's right. Another way is to simply put a really tough freeze where you cut out a few hundred thousand here or there, and the President has got to make some tough choices, and give him the authority to do what a President as chief executive ought to have the authority to do, and then there is a whole series of things I think you and I would agree on, on flexibility in the personnel system, which I certainly achieved in the university and you had automatically in business. Where you had overlaps, you had merit performance, and if they didn't produce they didn't have that job any more. Even though it was a State civil service, we folded all those things into broad categories, and you made discretionary decisions based on performance. We don't have enough of that in the Federal Government.

Mr. RUMSFELD. The Congress could perform a real service, Mr. Chairman, if they do what an oversight entity ought to do, and that is not say speed up, slow down, turn right, turn left, and get 15 hands on the steering wheel and drive the truck in the ditch, but instead sit back, think about it, and set out the parameters of the playing field, say here are the sides of the road, here's some criteria, we want to go from the total number of departments now to half of them, and set some goals like that, some directional leadership from the Congress for the executive branch, and then sit down and discuss how to make those kinds of organizational changes. I think reasonable people ought to be able to come to some agreement rather rapidly. The advantage is that there is no right answer, there are any number of ways that that organization chart could be cut, and the key is good people.

Mr. HORN. Exactly.

Mr. RUMSFELD. I mention in my testimony something that disturbs me. The fact of the matter is, when it takes so long to get people into place in the executive branch of the Federal Government, when you have wasted a nontrivial fraction of the entire term before people are ever confirmed, it is terribly damaging.

Mr. HORN. You are absolutely correct.

Well, we thank you greatly for taking the time to come down here. I think you have made some very perceptive and wise observations which only experience such as you have had could lead to. So thanks so much for coming.

Mr. RUMSFELD. Thank you very much.

Mr. HORN. May I say to the official reporter, we have an additional statement to put in at the opening. One will be from the ranking minority member on the subcommittee, Mrs. Maloney, the gentlelady from New York. The other will be from the vice chairman, Mr. Flanagan from Chicago, IL, and those will be given to you.

Mr. HORN. Now Mr. Johnson, if you would rise and raise your right hand.

[Witness sworn.]

Mr. HORN. Thank you. Please be seated.

Would you like to make a general opening statement, and then we will have questions.

STATEMENT OF ROGER W. JOHNSON, ADMINISTRATOR OF GENERAL SERVICES

Mr. ROGER JOHNSON. Yes, if I may, Mr. Chairman.

I came here around 2 years ago to work in the process of re-inventing government. It is why I think the President asked me to come here. Since I've come though I have been continuously amazed, I guess some disappointment and some frustration, about the basic operating structure or lack of it in the Federal Government.

The National Performance Review reports though, the analysis which I had a chance to work on from the beginning, is some of the best materials I have seen in 35 years of private enterprise, good analysis done by good people. They differ quite a bit, I think, from the Grace Commission and Ash's reports and others in the past because they were done by people who do have an understanding of business—an understanding of the Federal business.

What I would like to do is to talk just briefly about three things that I think are major barriers to real acceptance of change from my viewpoint. One of the biggest astonishments I have had since being here is that most people think—and may be so in Washington standards—that the progress that has been made has been very good. My standards say may be not so good. It may be as good as it can get.

Issues that stand in the way, I think, of making real change and progress here are: First, there is a tremendous overriding atmosphere of risk aversion and fear. Now lots of people talk about that, but I had no idea how pervasive and how self-reinforcing the issue is. It results, of course, in Government operating by process rather than results. I reject the concept that there is no bottom line in Government, I completely reject it. There are thousands of bottom lines, but we kind of hide behind the fact that there is no P&L and say that therefore we can't measure anything. I think that is nonsense.

Before we can talk incentives—and I was interested in the earlier discussion of course—you need three simple things. You need to know what it is you want to accomplish. That is called a result. It needs to be stated in end results, and although there are no profit and loss statements there are certainly dates by which time committed activities should be finished. There are amounts of money committed to be saved or to be spent, and there are customer service measurements—there are hundreds of them that can be put in place. Once you decide what you want the results to be, you then need to have a standard of performance, of what is acceptable. Once you have determined what is acceptable, then you have to have a system that can measure performance periodically. Only when you have those three things can you even begin to discuss incentives.

So I think it is quite premature to talk about incentives until we are able to talk about results.

What can we do about this? One of the things I have suggested to prior chairmen of this committee, and I'd suggest it again to you is that it needs, I think, to start with the Congress. If I were sitting there I would ask me, as administrator of GSA, to come to you with committed results, what is my plan, when will I have certain

things done. Let's take building schedules. When will they be done? How much will they cost? And it is my job to come back to you on a very regular basis and tell you how we are doing or not doing.

If we can begin to gain your confidence that we know what we are doing, then you would give us a little more room. To the degree we do not have your confidence, you will pull the rope back in more tightly. That is very different and much more productive than trying to control every single piece of the process to ensure that something gets done.

A second problem, I think, flows from that, and it also has to do with people. I have learned—I suspected it when I came here, but it has been confirmed—Federal workers are good people. They are honest, they work hard, they are well intentioned, and they are very intelligent. But the whole process that we have in Washington tends to yield managers who have very, very little diversity of background or experience, and therefore we have a situation where the thought processes of people such as those the Secretary just spoke of and myself and a very few others who have spent a lifetime in the business of results management are not here, and part of that is reinforcing, also because part of the reason we are not here is that there aren't results here, and so we either don't come in the first place or get very frustrated very quickly and leave.

It is not something that is personal. I used to think it was, and some days I have trouble convincing myself it is not, but I don't think it really is. It is just a system that doesn't know any better because it is reinforcing its own set of standards.

So what do you do about that? Well I've suggested to the President and to some others that bringing people like myself or the Secretary back one at the time isn't going to get us anywhere. Frankly, I have very few people to talk to about some things. On the other hand, if we identified maybe 50, 60, 40 jobs that are operating jobs in my agency and office of budget and measurement and personnel and Treasury and required them to be staffed by people who were—had experience in P&L, balance sheet, and multifunctional organizations, operating people, I would make the jobs 2-year jobs or 2½-year jobs. The reason is, people who have these skills and capabilities, a 4-year assignment here could truncate a career; they are not likely to come. Two years I think could be viewed as something that was a career enhancer.

I then go to CEO's of the Nation and I ask for a pool of 500 or 600 people, people they said they would supply and who have said they might come, and then come to the Congress with a particular program.

I reject the idea that these jobs are that complex that it takes 4 years to start learning them. The company I ran, Western Digital, was subject matter more complex. The process here is complex, and the mass is big, but I think in operating jobs, not policy jobs, those can be learned fairly quickly, particularly if you have a series of people with similar backgrounds.

A third area that has appalled me is the understanding and the recollection that the Federal Government has no capital planning process, per se. Now I've used the words "capital planning process" very carefully and not use the words "capital budget" because I have seen such a tremendously negative reaction to the term "cap-

ital budget." Again, I think, an example of a reinforcing atmosphere. The reason for that, most people tell me, is that we don't trust each other, that if we gave the Congress or anyone else in this town a capital budget they would abuse it to the point that we would be even more bankrupt than we are today.

Now the fact is that the private sector has had capital budgets and people trying to go around them for years, and that we have found ways to stop that from happening I think is not understood. However, I do believe that a capital planning process could begin without changing the scoring rules and we could gain 80 to 90 percent of the value.

The value of a capital planning process comes in three pieces. One, it separates and identifies at a time separate but simultaneous from the operating budget and forces commitment of future benefits from the money that is spent today, and it captures those commitments: I want 10 million today for a system, and I will return 2 million a year for the next X years and improve the following other operations. That is commitment—committed and captured.

It is important to do this because then in the succeeding years, those commitments are brought forward during the operating part of the budget preparation, and I am asked: Where is the \$2 million you said you were going to save last year? Why is it not there? Integral part of the operating plan.

It also would allow the Congress and the administration to prioritize on the basis of those projects with better returns than others. We always have limited resources, today more than ever. Therefore, you must always prioritize the moneys you have, and they should go to those things which have best returns. Failing to have a process to even identify or rank them, you are pretty well shooting in the dark of one project versus another.

And, finally, it sets up a method for rewarding those who demonstrate that they can meet their commitments and plan well, and of course it would then set up the ability to pull the string back from those who don't.

So there are three areas, I think, Mr. Chairman, that are in the way of implementing more fully the things that everyone here and I think in the country wants.

I think, coming full circle that I'd have to say that the biggest issue is this atmosphere of mistrust. It appears as though, for whatever reason—I don't know how it started—that it is assumed that people in Government, private sector people doing business with it, anyone connected with it is either a crook, stupid, or lazy, and more likely some combination of the three. That is a debilitating atmosphere for anyone to operate in. I may be old fashioned but I think we can add, and have to add, a little bit of trust and faith and understanding and add those words to the Federal vocabulary and at least give them equal time with "waste, fraud, and abuse."

Thank you.

[The GSA results-oriented mission charts follow:]

GSA's Results-Oriented Mission:

To Improve the Effectiveness of the Federal Government by Ensuring Quality Work Environments for Its Employees.

What Makes Up GSA'S \$64 Billion Financial Responsibility:

Asset Sales \$15.5 B
 Building Construction \$4.6 B
 All other \$1.7 B (\$.9 salaries)
 Purchased Materials & Services \$42.2 B (\$25 B Information Technology)
 Total \$64 B

How \$64 Billion Becomes \$159 Million:

\$159 Million In Operations Appropriations from Congress
 \$63.8 B Charged or delegated to other Agencies

"Time Out & Review" of Federal Buildings Program

192 Projects Reviewed
 154 Projects Modified
 Total Projected Savings = \$1.38 B

Other Benefits:

Federal Buildings process revised
 Greater Industry Involvement
 Partnership With Courts

"Time Out" For Major Information Technology Systems

VA/VBA \$.265 B
 DOC/AWIPS \$.514 B
 PTO/Modernization \$.666 B
 FAA/AAS \$2.1 B
 USDA/Infoshare \$2.6 B
 Total Cost Avoidance \$7.4 B

FTS 2000: Good Program, Well Managed

Long Distance Calls (per Minute):
 Government 5 cents
 Commercial 9 cents
 Citizens at Home 16 cents
 Traffic Tripled
 Overhead Costs Halved
 Half the "Trouble" Calls Vs. Commercial

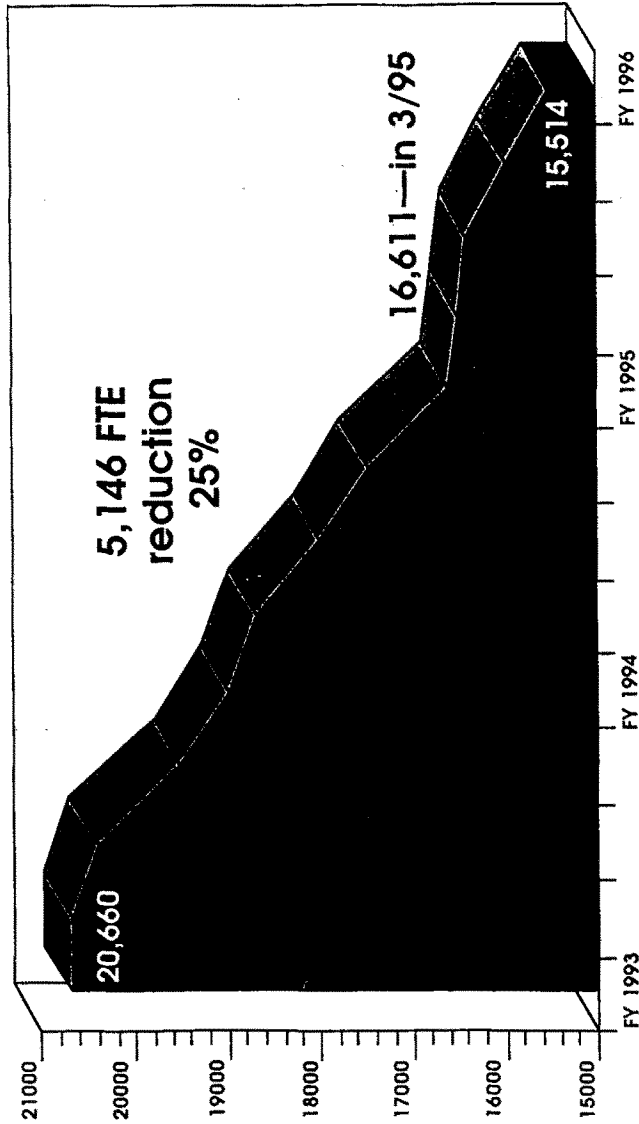
FTS 2000: Big Savings Getting Bigger

\$2.3 billion First 6-Year Savings +
 \$2.5 billion Next 4—Year Savings =
 \$4.8 billion Total Savings Over 10 Years

Projected Savings and Costs Avoidance

Federal Fleet Program \$30 M
 IMPAC Card \$475 M
 Time Out & Review of Federal Building Program \$1.38 B
 FTS 2000 \$2.5 B
 Review of Major IT Acquisitions \$7.4 B
 Total More than \$11.7 B

Employment Down With **NO** RIFs...



*Resulting from attrition, hard-freeze & buyouts.

GSA Operating Expenses Down

\$192 M FY 93
 \$174 M FY 94
 \$165 M FY 95
 \$159 M FY 96 (proposed)
 DOWN \$33 M DOWN 17%

While Customer Service is Improving:

"We always referred to GSA as GA in the past because they never had any customer service . . . the current changes are dramatic." Chuck Davis, U.S. Fish & Wild Life Service

"Reinvention has empowered GSA employees to use their best professional judgment." Chandler Peter, U.S. Army Corps of Engineers

REGO I to REGO II

Business Lines Leverage	(\$ Million)
Commercial Brokerage	2,431.2
Internal Computer Operations	34.0
Fleet Management	603.6
Federal Protective Service	95.1
Property Management	1,994.7
Govt-Wide IT Acquisitions	24,057.5
Travel	3,827.4
Property Disposal	12,133.3
Fee Developer	5,415.0
Information Technology Integration Services	344.0
Property Management (Personal Property)	3,569.3
Local Telecommunications	310.2
Portfolio Management	11.9
Supply/Management	6,667.5
IT Procurement	1,406.9
Transportation	262.7
Total	more than \$64 Billion

Mr. HORN. I thank you.

Let me pursue the capital planning, capital budget process a bit. I understand the differentiation, in both cases, to have a legitimate process you obviously need criteria that make some sense in terms of why this project and why not this particular project in terms of either a mathematical ratio of cost-benefit or long-term national plan to achieve certain goals through development of infrastructure to support those goals. In the California State budget you do not have a separate capital budget but you do have a capital budget that is funded differently than the operational budget, but in terms of the legislative review both are in one budget bill.

What we are talking about now in Congress very seriously in the next few months is a capital budget process that would have both the planning process you are talking about as well as a separate-ness from the general operational budget that we work on through appropriations committees, authorization committees, and all the rest.

What do you see as the main complaints to the capital budget as often practiced in a number of American corporations?

Mr. ROGER JOHNSON. Well, I think you have got a different situation in the corporation because you are dealing there with tax laws, so you have an issue that you need to match the expense with the revenue which is driven off the Tax Code. That is really the basic foundation now for depreciation, which is what people worry about

if you gave the accounting part of capital budgeting to the Federal Government.

I would say it is a moot issue. Since we don't have taxes in the Federal Government, you don't need to go through all that accounting, you can still score the money up front from a budgeting standpoint and eliminate the argument and the fear that evil people will just capitalize air—right?—out over 10 years and take what ought to be today's expenditure of \$10 billion and spread it out over 10 years and get us in all kinds of trouble. You don't need to do that. I think you can have all the benefits if you just put a process in place—and you could pick any one of a number of corporate or even some State capital budgeting processes and get all of the benefit without any of those concerns.

Mr. HORN. Now in your own planning process within GSA in terms of which Federal buildings would come on line first, in terms of need, you have a whole series of criteria I assume as to either need to be served, do we save money on rentals in the community, long-term amortization, et cetera. What are some of those criteria?

Mr. ROGER JOHNSON. Well, in the Federal buildings process, the way it is structured, Mr. Chairman, the process is an annual budgeting process. We don't really have the time to put that kind of a process together, so about all I can tell you is that we have reviewed those programs assuming they are needed, and we do some checking to see that they are not grossly unneeded, and then we try to assure that if the Congress wants us to build them that in fact we will build them in the most efficient manner.

One of the problems of not having a capital planning process is that there is never time to do it, because this town is in one continuous state of budgeting annually. I have tried to come forward with some kind of a process, but I am just not able to have the time to get through the process the first time. So it's a little like the chicken and the egg.

So the answer to you is, we do not have a way to prioritize on the basis of rate of return or any other way.

We tried to come through with a conversion of leased property to purchased property on that basis. In other words, we took leases that were costing us 2 and 3 times what a purchase would be over a life cycle and tried to bring forward a process that said please allow us to have X millions of dollars this year to convert these properties coming off lease and in turn we will commit to you three X savings over the period with a return. There the reverse hit us, and the scoring would not allow us to do that this year even though the long-term savings were there.

Mr. HORN. Is this essentially OMB making that decision?

Mr. ROGER JOHNSON. Well, I think it is OMB, but I think they have a lot of help.

Mr. HORN. Well, I don't know. Usually it is the budget examiner or the director that is calling that shot.

Mr. ROGER JOHNSON. Well, I think the Congress at that point was unwilling to change that also.

Mr. HORN. Really?

Mr. ROGER JOHNSON. Yes.

Mr. HORN. In other words, they talked to various people on some of the oversight committees?

Mr. ROGER JOHNSON. Yes.

Mr. HORN. Because I would think that is something we ought to do. The Corps of Engineers does it, the Bureau of Reclamation has done it, and they have both done it for 30, 50 years.

Mr. ROGER JOHNSON. Yes.

We are continuing to look at our real estate as a portfolio of course. We did stop all new office buildings when we came here, and I think Secretary Rumsfeld was correct, we don't need any more office buildings, but the next step now with downsizing would be to take a good look across the Nation and come back to you with a total real estate plan including collapsing leases, including a question of, is a Federal building built somewhere a better investment? Should we do that and plan to collapse these 10 leases into it over time? That is where I think leverage would be if you could ask us to do it. Right now it would be a wasted effort because the budgeting process wouldn't allow it to come forward anyhow.

Mr. HORN. I yield to the gentleman from Illinois, Mr. Flanagan, for 5 minutes.

Mr. MICHAEL FLANAGAN. Thank you, Mr. Chairman.

To my knowledge, you are the only CEO from a large business concern in the Federal Government or in the administration.

Mr. ROGER JOHNSON. So I'm told.

Mr. MICHAEL FLANAGAN. How do you think it would help if at all if we had more of, if not Cabinet level, certainly director level or other members who have had your similar experience and background in helping Government run better?

Mr. ROGER JOHNSON. Well, I think what would happen is, there would be a larger body of thinking that has to do with the things we were just talking about. We are no smarter, we are no more patriotic, no more well intended than people here, we just have a different experience base.

For example, in the GSA when I first came, as I would with any troubled situation, I put a hard freeze on all hiring, all replacements. It is instinctive with me because I have done it 20 times and I'm able to handle immediately and sensibly questions that say, well, how will we get the work done? Well, one way we will get the work done is to stop doing that 10 percent of the work that we shouldn't be doing anyway. That just comes from having done it, experience, and telling people. Because of that freeze, and buy-outs, we now have 4,000 fewer people than on the day I came, 20 percent less. Haven't laid off a soul, and our customers say we are doing better. That is not because I'm any particular genius, that is just because I have done this a lot of times and know how. If we had more people with that kind of experience, I think you would get many more instinctive moves based on their experience and quicker implementation of a lot of things in the National Performance Review which are very sensible, very logical, and very well analyzed. We are still missing people who really have had the background and say now here's how we are really going to get that done.

Mr. MICHAEL FLANAGAN. In the general perception it is believed that civil servants have inviolable employment, it will go on as long as they choose for it to go on, and that it cannot be terminated. Assuming that that is not absolutely correct, can you describe what

process you would go through to assess someone as ineffective at their job and consequently dismiss them from employment?

Mr. ROGER JOHNSON. Here or in a private company?

Mr. MICHAEL FLANAGAN. No, here.

Mr. ROGER JOHNSON. Here?

Mr. MICHAEL FLANAGAN. Yes.

Mr. ROGER JOHNSON. Well, first of all, I believe that the people that we have in our agency in the main are as good a work force as I have had anywhere. My job is to get stuff out of their way, so I've tried to convince them of that. It was hard in the beginning. I think they have gotten sort of convinced that this is true, and I have said to them, "Go ahead and make judgments. If you make mistakes, that's OK, just don't keep making them, and we'll judge you on the results." It gets very difficult, Congressman, because we keep coming back and I can't even get them judged on results because the whole system judges on process.

We put through a very good performance measurement based piece of legislation, I think. I think it has bipartisan support, and yet I have discovered that one of the reasons some of it isn't implemented is that there are committees around trying to figure out a process that will make sure the performance measurements are fair. I mean it is just instinctive. So that, even with a piece of legislation that is aimed at solving this problem, the process is now moving in to stop the process.

Mr. MICHAEL FLANAGAN. If I may borrow my favorite Est saying, if I hear what you are saying, you are saying that their employment is inviolable, that the process protects them, and that it is virtually impossible to eliminate someone who is not getting the job done in whatever management technique you have selected, and whether that works well or not, in your judgment as a department head or something else, that if you have some weight that you cannot move, the best you can do is transfer it, that you cannot dismiss it.

Mr. ROGER JOHNSON. Yes, Congressman, but don't get me wrong. It is my opinion that that is not the first place I go, because I don't think we have got too many people because we have got a bunch of bad performers.

Mr. MICHAEL FLANAGAN. No, and I don't mean to suggest that, that the Federal Government needs to have mass firings, but I'm saying this is not a tool at your disposal to implement management.

Mr. ROGER JOHNSON. No, but I don't really need it yet.

Mr. MICHAEL FLANAGAN. OK.

Mr. ROGER JOHNSON. The big leverage here is on things we have talked about earlier. First of all—and the whole process that this agency is going through now is to ask the first question: Why are we doing that? Is it our mission? Should we be doing it at all? If the answer turns out to be no, then we are trying to get rid of it. If it turns out to be yes, then the next question is: Well, who can do it as well? Who else does this? Do we have any measurements? Do we even know what the results are going to be? This analysis is beginning to pay off a great deal.

The Federal worker wants to do a good job. Most of them know exactly how to do it. So if we can just get this stuff out of their

way we are going to make immense progress, and if we want to reduce people my view is, well, let's just freeze the whole place and also be able to move people between agencies.

Mr. MICHAEL FLANAGAN. Thank you.

Thank you, Mr. Chairman.

Mr. HORN. Thank you.

I welcome the gentleman from Washington to the hearing.

Do you want to pass on this round and get in on questioning?

Mr. TATE. Yes. Thank you.

Mr. HORN. OK.

Let me pursue a few questions that came up in the Q&A with Mr. Rumsfeld and also with yourself, and you have given us some thoughts on comparing Government restructuring with private industry restructuring.

Having heard Mr. Rumsfeld and also realizing what you have said already in answer to questions, are there any other common patterns you think worth mentioning as to the way you would reorganize in the private sector versus the public sector, and are there any differences that we ought to be aware of in particular if we are trying to figure out a policy to suggest in relation to restructuring?

Mr. ROGER JOHNSON. Yes, Mr. Chairman. It doesn't sound very scientific, but I would certainly support from my background, I think, one of the points that the Secretary made, and that is that at some point you just have to decide and have a forcing function. I agree that it probably doesn't make much difference whether you have 5, 10, 15, or what of something. It finally comes to a point where you stop analyzing and just say I can only afford six, all right? And that is what we are trying to do in our agency. Now give me a plan to get from Y to six, whatever it is, and then begin working toward that, and out of that will come, many times, you'll see the barriers if you are doing something dumb pretty quickly. You will also see some opportunities you never even thought about.

But if we just sit and study it and say how can we do this better without any forcing function, I think you are just not going to get anywhere. People have said: Well, how small can you make the agency? My answer is, I don't know. I've said to people I think we could probably operate with half the people simply because I think I can always do anything with half the people. That, again, just comes from—but let's go find out.

I have never taken a company that was in difficulty—many of which I inherited, some of which I created myself—where I moved fast enough or deep enough—never, ever, never.

Mr. HORN. So you and Mr. Rumsfeld agree on that, don't cut the dog an inch at a time.

Mr. ROGER JOHNSON. You aren't kidding, yes. I agree with the chairman of Harley Davidson. There was a company that was really in deep trouble, about to be buried, and it was resurrected, and they asked: "How did you do that?" He said, "Well, one thing I did, I cut the headquarters staff in half and the motorcycles stopped leaking oil." That just comes from years of experience. That's all.

Mr. HORN. Do you think, looking at it from the congressional side, what can Congress do to be the most helpful to you as an executive in getting the job done? Is it a freeze approach rather than thinking we know so much?

Mr. ROGER JOHNSON. No. I think it is come at me with results.

Mr. HORN. Yes. I think one of the problems here is, some think they know so much that they will say cut this function within the agency, don't cut that, so forth.

Mr. ROGER JOHNSON. Then you don't need the CEO running the agency.

Mr. HORN. Right.

Mr. ROGER JOHNSON. I would say, Mr. Chairman, the best thing the Congress could do if you could get it anywhere pervasive would be to give me an answer if you want and say, "All right, administrator, I want you to do what you are doing with half the people and half the money." Now I won't like that, but then I have the ability the best I can to try to meet that objective. By telling me to cut this, privatize that, I think we are most likely going to cost the taxpayers money. But then make me come back with a plan, and then have me come back and tell you how I'm doing against it, and if I can't cut it in half, I will come back and logically explain to you what I can do, because one thing I'll do is find out in the process.

Mr. HORN. In the NPR process how does it work within the executive branch? Is each administrator asked to submit a plan given some particular proportionate share they are to move back to help make the savings and the employee cuts?

Mr. ROGER JOHNSON. No. I think it is a little more sophisticated than that. The National Performance Review has 32 different pieces of analysis, some of them in very functional areas, by procurement, financial measurement, budgeting, personnel policy, and some by agency. I have a personal performance commitment document with the President in which I looked across all of these various reports, activities, and suggestions, and picked the up ones that I thought were most meaningful and achievable, and so in my case I have a performance agreement with the President. He has it, and we send him periodic reports. I think this is the basis on which most of the agencies and Cabinets are working. Inside those reports there are things requiring legislation.

Of course we have come forward with suggestions of procurement reform. Chairman Clinger's bill I think is a very good bill, although if it gets in place I'm wondering—here's another one of these inescapable problems. You know, procurement reform requires people implementing it who have the background and skills, and, not the fault of our people, but pretty much all of the folks doing procurement in the Federal Government are called contracting officers. When you think about that, these are people trained in process. In my company I had one or two contracting officers and a cadre of buyers, people charged with the responsibility to know markets, understand products and technologies, so they don't need to ask people for pricing or cost data: it is their job to know that industry and the market. Here we can say you don't need it any more, and yet I'm worried a bit about the implementers who have never been asked to do that before.

Incidentally, to get buyers of that caliber, we probably couldn't get them for the salary structure. So there is still some fundamental work to do even in that case.

Mr. HORN. Well, I think you make a very excellent point. Having listened to some of the discussion the other day and being the third author on the bill, what worried me is the low amount of compensation we give to some key procurement officers making decisions that affect hundreds of millions of dollars, affect the life of an agency and a project, and it just seems to me your separation there of contracting office from buyer is exactly the analogy that we ought to be thinking about in the Federal Government. Once you get the deal struck, fine, turn it over to the contracting office to make sure all the dots—

Mr. ROGER JOHNSON. Your terms and conditions.

Mr. HORN [continuing]. The dots are over the i and the t's are crossed. But I think we are going at this in the wrong way, so maybe we can get a little reform in yet, and we would welcome your further advice on that.

You mentioned of course some of the problems we all face in personnel in a public agency as well as a private company. Now certainly when you mentioned the idea of bringing in people experienced in management of the process, not getting into the substance of the political values but making the system work, and also I think you and I have talked about some use of retirees, and we know the Senior Executive Service has had a marvelous experience helping nations all over the world.

The Hoover Commission, which proposed your agency in 1949, had also suggested the career administrative assistant secretary or assistant secretary for administration management in each of the major agencies and departments. It seems to me over the last two or so decades that has become an increasingly politicized position rather than a professional management position where people understood how the system worked and could work that system to the advantage of the department in terms of basic, simple, fundamental management processes. What has been your experience as you look at the other departments with which GSA deals, and also in GSA do we have a management cadre somewhere of professionals that know these processes, understand budgeting and all the rest, program evaluation?

Mr. ROGER JOHNSON. Yes, I think we do, Mr. Chairman, but not nearly at the levels I think they ought to be. I only brought in, I think, about half the political appointees that I would have been allowed to bring in. I also worked hard to put professional career people into senior jobs in the country in agencies such as this or wherever these responsibilities go, because one thing about this agency, regardless of what happens to the agency, the work it does has to get done, somebody has got to buy the stuff and rent the buildings, what-have-you. That work really should be done by pros.

It is probably one of the interesting arguments or discussions that we are having of why maybe having some of the employees do the business on a private basis is one of the alternatives we are looking at.

These activities that we do, and others in the Government as well, are fundamental operating activities, they are not political situations, and I think should have either political people come in who have card-carrying proven capability to do the work or they should be done by career people. That is why I had suggested the

card-carrying people as well as sort of a jump start to bring in maybe 50, instead of just one at a time.

Mr. HORN. Another thing, we have had a lot of people say as they move from industry to Government that, the balance sheet was important or, as was said by Mr. Rumsfeld, the profit and loss statement is really a disciplining force to know whether we are achieving some of the goals. I'm somewhat dubious about that because you can have a balance sheet and what makes me dubious is reading a month ago that most of American industry is cutting back on research and development funds, which is the basic investment a corporation makes to have a long-term return in new product development and all the rest, and I wonder, as you look at the Federal Government, is the balance sheet model a good one to bring discipline to the internal processes of management? What is your thinking in that area?

Mr. ROGER JOHNSON. Well, in my view, if you are running a corporation or any institution, a university or performing arts center—I have worked in all three areas—the continuous issue is, how do you tradeoff short term with long term? Do you take money out of the endowment if you head a not-for-profit situation to cover operating expenses, or how do you do that? I think you can't escape the fact that the people operating it, the executives, have to be able to make judgments. The corporations you read about, I would suggest, will not survive.

Now in Government, failing to have a result-oriented mentality—and I do reject the idea that you can't measure things in Government, you can—failing to have that, you are stopped before you begin because there is no way to even start distinguishing between what is current operations and what is long term, it is all in one big lump.

Now financially, OK, leave it there, but for goodness sake at least pull those expenditures which truly are being made today for tomorrow's benefit, a computer system for example, and at least understand that that is what it is: it is a current investment for future benefit. Now you can start to ask the question, well, if I'm in trouble currently should I curtail that expenditure, cut it back in favor of just paying salaries, or are the returns such that it would be stupid to do that and I really ought to cut the current operations and save the future investment. Until you are able to distinguish between the two, Mr. Chairman, you are dead, you can't make that distinction.

For example, just stay with this for a second because it just appalls me, talking about computer systems, and measurements and results. No one has asked me—and I hope you will soon, although I'm not sure what I'll tell you—what is my cost reduction plan for computer technologies? I come from that industry. We have been spending \$20 to \$25 billion a year for nonmilitary computer hardware and software for as long back as I can see, in an industry in which the costs have been going down 20 to 40 percent per year.

Now it doesn't take much to say, gee, if that's the case, and you spent \$20 billion 3 years ago, it seems like you ought to be able to spend 10 this year and get the same amount. So if you are spending 25, you ought to be getting three times as much. Those questions are never asked.

Incidentally, the performance of those systems is going up 20 to 40 percent per year also. How is it we are not the best computerized structure in the world? Because we don't ask those questions.

Mr. HORN. Is there a separate process in the budgeting process that perhaps OMB has that looks at computer purchases and pay-offs a little differently than the normal equipment? The State of California has that process. That is why I'm curious.

Mr. ROGER JOHNSON. Yes, and I am not banging at OMB particularly here because I think they do as good a job as they can within a structure that is a 12-month structure, and I know agencies come and make commitments and they do as good a job as they can of saying, yes, that's a good project, that's not, we'll do that, we won't do that, but the minute that decision is made, my point is, that performance, that whole set of commitments is lost. It never comes back into the budget process ever again, except when a program gets in enough trouble that it shows up in the papers, and then people jump all over it.

Mr. HORN. Such as the FAA purchase.

Mr. ROGER JOHNSON. Such as the FAA purchase.

Mr. HORN. Among others.

Let me yield to the gentleman from Illinois, Mr. Flanagan.

Mr. MICHAEL FLANAGAN. Mr. Johnson, I can tell you are chomping at the bit to tell us among other things about your computerization reduction plan. I imagine you have probably got a laundry list of stuff that you would like to testify about today, and I would just like to take the 5 minutes, hand it to you, and pretend you have been asked a question and expound for us on the stuff that you think we ought to be hearing here. Having been denied the testimony and other things, we would like very much to have you just take it and run with it.

Mr. ROGER JOHNSON. Well, we have been looking at the computer systems of the country, have recommended that we change the approach for oversight there, give most of that responsibility to interagency people, experts in computing technology, and we have them all through the Government, and they are awfully good people.

One of the things we found in our buildings program—we saved \$1.4 billion out of about \$7 billion—and not because people were dumb or crooked, but simply because we were managing the project, no matter what its size or complexity was, in the geography that it happened to be in, and whereas the private sector was bringing together the best talent in the world, we would deal with them on the basis of whoever happened to be there.

The same holds true in a lot of our computer systems. Many of the systems are dead because of the original planning, not that people are not well intentioned, but because very complex systems are getting designed, developed, and planned because they happen to be in a particular agency with certain people. I think we should be looking across the Government, ranking the systems by complexity, size, risk, and then bringing to bear, at least in the early stages of design, architecture, and layout, the very best people we can get our hands on in the Government as well as bringing in outside people. I think this could make immense changes in how well

we implement that particular part of a very critical part of the Government.

Mr. MICHAEL FLANAGAN. I have a short question about that, not to excuse or to explain the consistency in the amount of money spent yet are below the zone level of achievement in computer level, but in our endless and continuous drive to acquire the best and the most recent, are we successful in that, and does that come at a higher cost as opposed to something that will work that is older and consequently at a much lesser cost?

I mean computer technology, it seems to me to my unbaptized level of knowledge of computers, changes daily, and advances are made with such frequency that to commit to making huge dollar purchases may commit us to a path of mediocrity for a long time to come. So are the amounts of money that we are spending justifiable in that way, or is there just a colossally stupid management reason why we continue to pour these kinds of money into that?

Mr. ROGER JOHNSON. Well, I have to tell you I'm not sure what the answer to your question is. I'm very suspicious because every place I look I see a lack of control and measurement, and I don't mean it in a defalcation sense, I'm talking about just common sense approaches. I know from my own personal experience that computing technology is one area that needs to be constantly watched, to be traded off, and to have the people who know most about it on top of it continuously.

Our procurement process, in my opinion, essentially works against us there because we don't really bring in the best industry people we can get. I would not do business with the Federal Government in my computer company because of the complexities. Many of my colleagues don't either. Now you may see our companies' names here, but they are here represented by people who understand Government procurement, and one of their principal jobs is to keep the Government procurement away from the real company, and that is just what you have here.

So even there you have got industry that looks like industry that really is a part of the infrastructure here. We are unable to call in, for a lot of different reasons, the kinds of experts I would call in, in my own corporation, from other companies and say help me with this, give me some counsel and advice, and have them still able to go out and compete with each other after they have done that. That is impossible here under current procurement rules. Some of those issues are being addressed, but, again, it runs to this very basic issue of trust and motivation.

So we just kind of spin around with people trying to make progress but running up against some awfully fundamental barriers, most of which are not legislative, they are mostly attitudinal.

Mr. MICHAEL FLANAGAN. Well, your concerns have an ear and a voice here. We are going to work to fix a lot of this.

Thank you, Mr. Johnson.

I yield back, Mr. Chairman.

Mr. HORN. I yield to the gentleman from Washington.

Mr. TATE. No questions.

Mr. HORN. OK. The gentleman from Illinois doesn't have any more. Let's just pursue a few closing ones here. I know we have kept you a long time.

One question comes up when you have got Congress passing laws, a lot of which concern general management and are buried somewhere either in law or regulation or Executive order, and some would argue that certainly makes management where you are trying to get something done to accommodate your customers, who are usually other executive agencies—makes things a lot slower, less responsive than if you had to operate strictly to market conditions as a firm would, and, as a number of us have said and the witnesses have said and you have said, it is process-oriented rather than results-oriented.

Is the Federal Government really suited to run a large commercial type organization as GSA is expected to be? In other words, you are expected to get all these economies that you would get if you were in the private sector by bulk purchase and all the rest of it, which would mean your people take advantage of certain sales when they see them, thinking of Government needs to be met down the line. How do you feel about that? Is there another way to organize GSA?

We have a number of witnesses coming in here talking about Government corporations of one type or another. Should we be talking about that in relation to any of GSA that isn't already related to that?

Mr. ROGER JOHNSON. Well, I think, Mr. Chairman, we are already asking that question inside the process of this agency.

I have resisted and resist attempts to impose answers to questions that I think can get answered through a more logical process. A Government corporation for example, that's a tool; privatization, that is a tool; contracting out, that is a tool; those aren't results. The result is: Works better, costs less.

So the question becomes how do you do that? How do you know what you are doing? How do you know whether you should be doing something, and what are the best alternatives? The result may be to privatize, the result may be to contract out, but for Congress or anyone, I think, to leap out in front and conclude without going through an analysis is very, very dangerous, particularly in the complex things that we are doing.

The Government has to do the things we do one way or the other. Even if it all turns out that it should be contracted out, it needs to have some awfully good controls on how to contract it. So no matter how you look at it, you have to get through the specifics of what you are doing, and how you are doing it, if the result is going to be a lasting, efficient way to do it, and then you have got to keep looking at it even then.

Mr. HORN. Let me move to a somewhat related subject. In March we held a hearing on the privatization at which Andrew Jones, a privatization expert at Arthur Andersen who is helping GSA review its business lines, testified about his experiences with privatization. I was just curious if GSA is engaged in contracts with other experts in business or governmental organization. For example, in figuring overhead in the agency, I'm not quite sure how you do it. Do you have a charge-back system at all in relation to the Office of General Counsel or other central services that people are tapping?

Mr. ROGER JOHNSON. Yes. The system was fairly complex. One of the things that this review we are doing is driving out of course is that those analyses maybe were not as good or as timely done as they ought to be.

We are now at a point, I think, Mr. Chairman, where we do have a pretty good, accurate handle on what it costs us in terms of direct costs, which we are quite sure of and allocated costs, which you do the best job you can to perform the work we are doing.

I think what gets interesting—and I think you each have copies of these charts there—is that as we broke our business down into the 16 things we do, we also then broke it down into the kinds of leverage each of those businesses has control of or affects. It turns out that we have control of or affect about \$64 billion. That is where the focus of this administrator is in the agency. It costs us only about \$1.7 billion to manage that stuff, and, of that, only \$1 billion is salaries. So the answer is to work on how we control the \$64 billion and not chase around the \$1 billion. The accounting for that is being very helpful for us now as we try to analyze how best to do the work of that \$64 billion.

Mr. HORN. Let's get a couple of things on the record before you leave. As you are aware, the House Budget Resolution recommended within it some specific changes at GSA, and, as you and I know, those don't mean anything unless the authorizing committees and the appropriations subcommittees agree. But where their overall target is does mean something in that the rest of us have to conform. But they noted that they would like to see the abolition of the Federal Supply Service, the Federal Property Resources Service, the Information Technology Service, changes in fleet maintenance and GSA Visa IMPAC credit card.

Now as a former chief executive of a university, I happen to believe very strongly in executive flexibility, and I suspect you share that belief, and so we would like to work with you to ensure that at the very least the savings identified in the House Budget Resolution are achieved. But we would like your thinking—and maybe you want to file some of this for the record—whether these savings would be over and above the savings you announced in January 1995, and is it more important that the savings occur rather than a specific route taken, and I think earlier in this discussion we said we ought to give the flexibility to the chief executive to say here's the target, you figure out what the new configuration should be, rather than a few people sitting on a committee at midnight figuring it.

Mr. ROGER JOHNSON. Absolutely, Mr. Chairman. Please just give me a target of what you want and let me come back and tell you the best way to get it. That is what you are paying me for.

Some of the issues that are in that budget resolution I'll guarantee you will cost the taxpayer money if implemented. Some of them may well be proper, but I don't know yet. There may be even a better way to work in some of those areas than those that were suggested.

But in any event, I would say tell me what the answer is that you want and let me come back and give you the best alternative way to get there.

Mr. HORN. Very good. We will try to do that. I think the chairman of the full committee would agree with that also.

Today's Washington Post Federal Page included an article noting that a GSA union has released a report critical of GSA's handling of security at Federal office buildings. Do you have any comments on that report?

Mr. ROGER JOHNSON. Yes, I sure do. I was very saddened to see the union, particularly the union lobbyists, using what is a tough situation right now with security around the country to promote what looks to me to be a purely union versus private sector issue. I was concerned because of the condemnation there and in some other articles of private sector contract law enforcement people. I think that borders on irresponsibility.

Private contract security people are quite professional people. In fact, they are in the business of protecting people at Justice Department and prisons in the Federal Government and many State operations, certainly lots of private organizations, and it strikes me if they are going to get attacked as being incompetent, which I think was one of the comments, that is a pretty serious undermining of law enforcement, as serious as it is for others to attack the FBI or any other part. So I was quite concerned with that.

Security of the Federal workers that I have responsibility for is our top priority—very good people are looking at how we might improve that. I think we need to work together to look at the issues and work on how we might improve security, but trying to drive a wedge between whether they are union people or private people is not the way to do it.

Mr. HORN. Remind me, in terms of security services, does GSA have some set criteria that they have to meet in terms of checking their personnel, whether they have a background, criminal record, or whatever?

Mr. ROGER JOHNSON. Yes in both cases. The corporation we would hire provides the security people, but each of the security officers even so are also individually approved. They have to have a certain amount of training, they go through individual FBI background checks, and they are looked at individually. So it isn't as though we just hire a corporation and take whoever they give us. Each one is checked as well, and I think we have a long history in our country, including Pinkerton and some of the others, who go way back of being very competent people.

Mr. HORN. I think you are well aware of the security needs for the Federal buildings and some of the threats they face from either the left or the right. There are other things coming up, however, that you might wish to think about, and it came to mind the other day when I was talking to a number of government employees that were involved with Social Security.

There are changes that are being proposed in the formula by Congress in terms of SSI, the Supplemental Security Income program and the disability program. A lot of the people on the income program have been either alcoholics, substance abusers, or drug abusers of one type or another. As the funds dry up in that area, I suspect we might well have some problems in terms of them blaming the case workers involved in Social Security. So I don't

know if these agencies are working with you, but they ought to be——

Mr. ROGER JOHNSON. Yes, they are.

Mr. HORN [continuing]. Watching that the law progress to see what kind, if any, protection is needed to help some of their people from some of these nuts that are walking through the door and blaming them for the decision.

Mr. ROGER JOHNSON. Yes. We work with each of the agencies, and now of course are going back and reviewing the criteria. But each building's security is based in part on those types of assessments, depending on who is in the building, what kinds of agencies they are, and what their individual needs are, and they can also take measures themselves, so there's two or three layers here of potential security. I think the President has asked that we review that completely, and the Attorney General is heading that task force.

Mr. HORN. Very good.

Any other questions? There are no further questions. We thank you very much for coming down. We know you have achieved a lot of accomplishments in your 2 short years, or 2½ short years, at GSA, and we commend you for them.

Mr. ROGER JOHNSON. Thank you, Chairman.

Mr. HORN. You are welcome.

In the record at the beginning of the administrator's testimony we will place the GSA's results-oriented mission charts.

Mr. HORN. OK, the next panel will raise their right hands.

[Witnesses sworn.]

Mr. HORN. Please be seated.

Mr. Robertson, deputy administrator, Bonneville Power Administration, will be first.

STATEMENT OF JACK ROBERTSON, DEPUTY ADMINISTRATOR, BONNEVILLE POWER ADMINISTRATION; PAUL MAJKUT, GENERAL COUNSEL, BONNEVILLE POWER ADMINISTRATION; AND DANIEL V. FLANAGAN, JR., THE FLANAGAN CONSULTING GROUP, INC.

Mr. ROBERTSON. Thank you, Mr. Chairman.

I have submitted my testimony for the record. I'm going to try to be brief in my remarks.

I have brought with me Mr. Paul Majkut.

Mr. HORN. Please summarize it in 5 minutes. The full text is in the record at this point.

Mr. ROBERTSON. I will do that.

Mr. Majkut is from our Office of General Counsel. Bonneville has spent the last 1½ years in the region trying to put together the details of a Government corporation, and Paul has been instrumental in putting that together. If the committee has any questions, I'm sure he will be able to help you as well.

I would like to give a quick context as to what has driven our activities in the Northwest in the last few years, Mr. Chairman. For 55 years we have tried to be an exemplary Federal agency, and we are increasingly trying to deliver because of the pressures you have heard from citizens today what people are expecting from Government, and that is to deliver higher value for far less cost.

We have been hit in the electric power industry with a wave of deregulation and competitiveness that is similar to the wave that hit the electronics industry, the telecommunications industry, the natural gas industry, the airline industry, and so on, and so we are facing very severe competition in this business for the first time in the 55-year history in the Bonneville Power Administration.

For over half a century Bonneville provided power to Northwest retail utilities with little challenge. Today, there are 40 wholesale electric suppliers competing in the Northwest when just 5 years ago with us in the Northwest—when just less than 2 or 3 years ago really there were virtually none. Fifteen years ago Bonneville's price advantage was over 400 percent compared to the next competitive alternative price for electricity.

Despite the fact that Bonneville's rates have been stable—they have gone up less than half the rate of inflation for over a decade—that gap has rapidly deteriorated now because of the cost price of gas and other commodities moving down in the Northwest marketplace to where our rate is now at or even slightly above in some cases the existing wholesale power rate. This change in the marketplace has fundamentally caused us to approach Bonneville and our position in an entirely different way.

Our first and direct response was, to take swift actions to meet the marketplace by cutting costs, improving services, and becoming more flexible. We plan to cut between 1996 and the year 2000 over \$500 million per year from our budget; that is on a base budget today of about \$2.2 billion. We plan to reduce our Federal work force, which is now or was at 3,770 FTE, by 500 and our total work force by over 1,000 within 3 years.

We volunteered to be and were accepted as a reinvention laboratory under the Vice President's initiative earlier on this year, and we have received from the GSA and other Federal agencies, particularly Department of Energy, significant administrative relief from red tape and bureaucratic barriers. However, this relief is limited in scope due to significant statutory barriers and the potential limited duration being cut for the benefits that they have provided. So in 1993, in June, we asked the National Academy of Public Administration to examine alternative structures that would maximize Bonneville's efficiency and effectiveness, and you will hear today from Dr. Seidman.

NAPA described the criteria for determining whether a corporate style organization is appropriate for Government agencies, and this includes activities that, one, are predominantly business in nature; two, are revenue producing and potentially self-sustaining; three, involve large numbers of business transactions with the public.

Now Bonneville seems to conform to many of these criteria, and we carry out an electric utility function in the Pacific Northwest that meets them almost to a tee. As I said, we have about \$2.2 billion in annual revenues. We are mandated by law to recover our costs, to operate in a businesslike way, to repay a Federal investment of about \$9 billion which totals about \$850 million on average a year back to the Federal taxpayers. We serve 10 million people. We provide service to 180 direct customers, with 40 percent of the power in the region being supplied by Bonneville in the Northwest

States and 75 percent of the high voltage transmission capacity in the region owned by Bonneville.

As of right now, the administration is considering legislation to make Bonneville a wholly owned Government corporation under the Corporation Control Act. Such legislation might allow Bonneville to accomplish its mission more efficiently and effectively as outlined in organic statutes. Potentially this would increase Bonneville's flexibility over personnel, procurement, property management, budgetary, litigation, and claims settlements, functions to allow Bonneville to compete more effectively in this electric power marketplace that has become so competitive.

Such legislation might give Bonneville the flexibility to operate efficiently, including managing its work force more effectively, and we believe the savings from this could total \$30 million a year. So as was said earlier, the concept of a corporation is that it is an important tool. It can allow us to downsize and right size the organization, and it can allow us to cut overhead very quickly. But it is a tool, it is not, in and of itself, a means or an objective. It would not, for example, change Bonneville's existing power transmission, conservation, fish and wildlife duties, under its organic statutes and Federal environmental laws such as the National Environmental Policy Act and the Endangered Species Act.

There is also no reason that such legislation would change the administrator's accountability to customers through rate making, constituencies through public involvement, the Secretary of Energy, the Congress, but in day-to-day operations of the agency we would be allowed, as the management, to act as we saw fit to achieve the objective, and that is no small thing.

So to conclude quickly, Bonneville's competitiveness plays a critical role in keeping the Northwest economy thriving. The competitiveness and survival of many of the 180 utilities and large industrial customers the agency serves is closely linked to the price Bonneville charges for power. Likewise, the business and industries served by these utilities depend on an economic and a competitive power supply.

Our competitiveness is also critical to the environment as the agency funds energy conservation activities and presently invests \$400 million per year on fish and wildlife enhancement in 1995. This amount is expected to grow to some \$550 million a year in 1998, which is the largest such investment of the kind we know about in the world.

Bonneville's competitiveness is also important to the Nation's taxpayers who support construction of the Federal dams and transmission systems. To date, as I said earlier, we have paid over \$9 billion in principal and interest to the Treasury and for fiscal years 1996 through 2000 Bonneville's projected annual Treasury payment obligation averages about \$860 million, and this year's payment will be \$1.1 billion.

The Government corporation structure might enable Bonneville to save ratepayers' moneys, increase customer service, and enhance the ability to respond to changes in the marketplace. We have worked on it for over 1½ years now, Mr. Chairman, and we hope that this kind of structure can achieve the objective of creating much higher value for the citizens we serve.

Thank you.

[The prepared statement of Mr. Robertson follows:]

PREPARED STATEMENT OF JACK ROBERTSON, DEPUTY ADMINISTRATOR, BONNEVILLE
POWER ADMINISTRATION

Chairman Horn, it is my pleasure to appear before the Subcommittee on Government Management, Information, and Technology. I am Jack Robertson, Deputy Administrator of the Bonneville Power Administration (Bonneville). Today, my testimony will focus on why government corporation status might be reasonable to consider for an entity like Bonneville that is simultaneously a government agency and a business. First, I will provide a brief profile of Bonneville. Secondly, I will describe the competitive electric utility market and the importance of Bonneville's competitiveness. Thirdly, I will discuss the implications of government corporation status in light of Bonneville's situation.

PROFILE OF BONNEVILLE

Congress created the Bonneville Power Administration in 1937 to market and transmit the power produced at Bonneville Dam. Bonneville became an appropriated Bureau within the Department of Interior. The Bonneville charter focused on providing electric power at the lowest cost consistent with sound business principles. This interim structure remained unchanged until 1974. Today, Bonneville markets power from 29 federal dams and one non-federal nuclear plant in the Pacific Northwest, and has built one of the largest and most reliable transmission systems in the United States.

Bonneville sells wholesale power and transmission services to public and private utilities, and large industries, principally aluminum smelters. Bonneville's service area includes Oregon, Idaho, Washington, Western Montana, and small parts of adjoining states. Bonneville also sells or exchanges power with utilities in California and Canada.

In 1974, Congress recognized that Bonneville needed some budgetary and financial flexibility and changed it to a self-financed agency under the Government Corporation Control Act, paying for its operating costs and repaying the federal investment in the dams from the sale of electric power and transmission services. Congress gave Bonneville a permanent, indefinite appropriation and authority to borrow up to \$1.25 billion from the U.S. Treasury. That figure was later raised to \$3.75 billion.

In 1980, Congress gave Bonneville authority to acquire energy conservation and the output of generating projects to meet the needs of its customers. Also in 1980, Congress created the Northwest Power Planning Council as a state-appointed planning body to provide guidance for Bonneville's resource acquisitions, energy conservation, and fish and wildlife mitigation programs. The fish and wildlife and conservation responsibilities Congress gave Bonneville were among the most significant additions to its charter since the agency was created.

Bonneville's need for business flexibility was acknowledged by Congress in two more acts passed in the next decade. In 1985, Congress exempted the Bonneville Fund from sequestration under the Gramm-Rudman Budget Act. In 1989, Congress recognized Bonneville's need to continue to incur obligations beyond borrowing authority and cash in its Fund.

The Energy Policy Act of 1992 made Bonneville's decisions whether to provide transmission service for non-Federal power, and the prices, terms and conditions for such service, subject to Federal Energy Regulatory Commission review. The Commission was given the authority to order the Administrator to provide transmission service and establish the terms and conditions of such service. The Commission is to assure that Bonneville's transmission rates set under this authority are not "unjust, unreasonable, or unduly discriminatory or preferential." The Act also accelerated electric utility competition by opening transmission access, not only within the Northwest, but also to utilities from other regions.

COMPETITIVE ELECTRIC UTILITY MARKET

Utility restructuring has fostered a strong independent wholesale electric power production industry nationwide. In the Northwest, as elsewhere, this industry offers Bonneville customers alternative power suppliers. For 55 years, Bonneville supplied wholesale electricity to Northwest retail utilities with little challenge. Increasing Bonneville costs and restructuring of the industry, however, has opened up the market to increasingly intense competition. Today, there are at least 40 wholesale electricity suppliers competing in the Northwest alone.

At the same time the industry is being restructured, the costs of new power sources have dropped sharply, causing the gap between Bonneville's costs and the cost of alternative power sources to narrow dramatically. Fifteen years ago, Bonneville's price advantage was over 400 percent. Recently, this gap has rapidly narrowed as independent power producers and others enter the Northwest wholesale market. The closing of this gap is illustrated in the attached graph "Avoided Cost of Generation vs. BPA Average Rate" (attachment A).

Just months ago, Bonneville believed the competitive wholesale electric rate to be in the range of 2.7 cents to 3 cents a kilowatt-hour. (Bonneville's current rate is 2.7 cents.) The benchmark was derived from the cost of energy generated from a new combustion turbine. Recently, the market dropped dramatically due to plunging gas prices. Within one week this spring, Bonneville lost 200 megawatts of load to competitors at prices ranging from 2 cents to 2.4 cents per kilowatt-hour.

Gas prices have dropped so low that competitors do not need to build new combustion turbines. Thanks to these prices, the old, inefficient gas generation throughout the West can be run competitively. What we are now competing against is a large pool of surplus power from existing—not new—resources at prices lower than Bonneville's current rates.

Bonneville customers are receiving up to five year, firm power supply offers from brokers, independent power producers, and other utilities, frequently at rates equal to or lower than Bonneville's current rates.

In addition to price challenges, Bonneville must contend with large uncertainties, such as escalating fish recovery costs. Such uncertainties have led some customers to conclude Bonneville might not be competitive in the very near future. That could be true if Bonneville were to take no further action. Our Competitiveness Project has a direct relationship to our ability to fulfill our mission, including regional utility, social and environmental responsibilities that private utilities do not have.

BONNEVILLE COMPETITIVENESS IS CRITICAL

Bonneville's competitiveness is critical to the Pacific Northwest economy. The agency provides 40 percent of the electric power and 75 percent of the high-voltage transmission in the Pacific Northwest region.

Bonneville's competitiveness is critical to its customers because the competitiveness and survival of many of the 180 utilities and large industrial customers the agency serves in the region are closely linked to Bonneville's rate levels. Likewise, business and industries served by these utilities depend on an economic power supply. Bonneville is required to spread the benefits of the federal investment in the federal power and transmission system to the customers of investor-owned utilities in Bonneville's service territory. About \$2.5 billion has been distributed in the Residential Exchange program.

Bonneville's competitiveness is critical to the environment because Bonneville funds conservation activities, and presently invests roughly \$300 million per year on fish and wildlife, and that does not include \$165 million annually by fiscal year 1997 in additional fish mitigation measures recently proposed in the 1995 National Marine Fisheries Biological Opinion. With the new costs added in, the total Bonneville costs will be more than \$550 million by 1998. The rapid growth of these costs is shown in the chart titled "BPA Fish and Wildlife Investments" (attachment B). Since 1980, Bonneville has spent about \$1.5 billion to acquire energy conservation and spent or foregone over \$2 billion in revenues for fish and wildlife.

Furthermore, Bonneville's competitiveness is important to the nation's taxpayers who supported construction and operation of the federal dams and transmission system. Bonneville has paid the Treasury over \$9 billion in principal and interest. Of the original investment, about \$10 billion in principal remains to be paid and taxpayers will also receive interest on the balance as it is repaid. Bonneville's obligation to make annual payments to the U. S. Treasury is rising. For fiscal year 1996-2000, Bonneville's projected annual Treasury obligation is on average about \$860 million.

THE COMPETITIVENESS PROJECT

A cornerstone for remaining competitive is that Bonneville must improve its efficiency. Bonneville initiated the Competitiveness Project two years ago to focus on reducing costs, increasing revenues, improving services, and becoming more flexible in order to respond rapidly to changing market conditions and customer needs. The goal of the Competitiveness Project is to allow Bonneville to accomplish its mission as outlined in organic statutes more efficiently and effectively—not to change the mission itself.

Bonneville remains committed to providing high quality transmission and to the integrity of the region's environment and natural resources, and to conservation as the energy resource of first choice. As a result of the Project, planned operating expenses for fiscal years 1996-2000 are projected to be reduced by approximately \$500 million per year on average from estimates reflected in Bonneville's fiscal year 1995 Congressional budget submission. Our workforce of 3770 full time equivalent employees has been reduced by 450 full time equivalent employees, largely through the use of voluntary separation incentives. Contractors have also been reduced by 180. These reductions put us more than half-way toward our current goal of reducing the overall workforce by 1,000 by the end of fiscal year 1997.

Achieving this goal has required new agency initiatives—including removal of the barriers to becoming more business-like. With the support of the current Administration, Bonneville became a National Performance Review reinvention laboratory in 1993. As a result, Bonneville obtained administrative relief from some red tape and bureaucratic barriers, but the relief obtained is limited in scope due to significant statutory barriers and is potentially limited in duration.

ALTERNATIVE STRUCTURES

At the request of Senator Hatfield and Congressman DeFazio in June 1993, Bonneville contracted with the National Academy of Public Administration (NAPA) to look at alternative structures that would maximize Bonneville's efficiency and effectiveness. In NAPA's report, *Reinventing the Bonneville Power Administration*, December 1993, NAPA described the criteria for determining when corporate-type organization is appropriate for government agencies. Corporate form is appropriate for activities that: (1) are predominately of a business nature; (2) are revenue producing and potentially self-sustaining; and (3) involve a large number of business transactions with the public.

Bonneville seems to conform to many of these criteria. Bonneville carries out an electric utility function in the Pacific Northwest. Bonneville has about \$2.2 billion in annual revenues, and is mandated by law to recover its costs and repay the federal investment. Bonneville serves about 10 million people, providing 180 direct customers with 40 percent of the power and 75 percent of the transmission capacity in the region.

Prior legislative action has authorized Bonneville to have a revolving fund, have access to borrowing authority, and directed it to submit a business-type budget under the Government Corporation Control Act. But unlike most government corporations, Bonneville does not have full authority to independently carry out its legislative mandates. Bonneville does not control its commercial litigation, settle its own accounts, establish its own financial, personnel and procurement systems, and acquire and manage its own property.

ADMINISTRATION CONSIDERATION OF INCORPORATION

The Administration is currently considering legislation to make Bonneville a wholly-owned government corporation under the Government Corporation Control Act. Potentially, this would increase Bonneville's flexibility over personnel, procurement, property management, budgetary, litigation, and claims settlement functions and allow Bonneville to compete more effectively in electric power markets. Such legislation might give Bonneville the flexibility to operate more efficiently, including managing its workforce more effectively. The savings might amount to as much as \$30 million dollars each Year.

Corporation legislation would not change the agency's existing power, transmission, conservation, and fish and wildlife duties under its organic laws and federal environmental laws, such as the National Environmental Policy Act (NEPA) and the Endangered Species Act (ESA). There is no reason that such legislation would change the Administrator's accountability to: (1) the customers through rate-making, (2) the constituencies through public involvement, (3) the Secretary of Energy, and (4) the Congress. If, however, day to day operation of the agency would be left to Bonneville management, this would be no small-matter.

As a separate federal agency and government corporation, Bonneville could execute the laws applicable to it and other laws generally applicable to federal agencies, free of restrictions that cause difficulties for a business entity operating in a highly competitive industry. For example, the Department of Energy adopted rules to implement NEPA. Bonneville has always prepared its own analysis under that Act which the Department almost always approved with few changes. Approximately one year ago, the Department recognized Bonneville's ability to work independently in this area and, accordingly, delegated authority to the Administrator.

This delegation has expedited our processes, but the next Administration could withdraw that delegation, and others as well.

The Department of Justice represents Bonneville in all litigation, although Bonneville attorneys have actually handled most of its highly specialized litigation in the Ninth Circuit Court of Appeals. Many of these cases have involved claims for millions of dollars. Nevertheless, small claims consume significant amounts of time due to external review requirements. Personal injury claims of over \$10,000 must go through Department of Energy review before they can be paid. As required by the Federal Tort Claims Act, personal injury claims of over \$25,000 also must go through Department of Justice review before they can be paid. Under these two sets of rules, Bonneville must aggregate small claims related to the same incident to see if they may exceed the dollar limits and then seek the appropriate Departmental approvals. A corporation, in contrast, could be provided more authority.

Today, Bonneville is "self-financed" under the Federal Columbia River Transmission System Act. This Act provides for the direct use by Bonneville of operating revenues, not taxpayer revenues, and the ability to sell revenue bonds to the Treasury to finance its capital investments. Nevertheless, Bonneville is currently subject to General Accounting Office (GAO) rules, including settlement of its accounts, applicable to federal agencies that receive annual appropriations. As a result of the application of non-business oriented rules, for example, overtime pay that any private company could pay is prohibited.

Bonneville is also subject to the reporting requirements designed for federal agencies receiving annual appropriations while simultaneously maintaining its records in a conventional utility fashion using generally accepted accounting principles. As a corporation, these GAO requirements would no longer apply, although GAO could still audit and report on the agency's activities. In addition, the duality—literally the keeping of two sets of books—would be eliminated.

Another significant obstacle to competing effectively in a market environment is the civil service system designed for traditional federal programs. Under that system, it is difficult to manage its human resources efficiently. Bonneville cannot manage its organization to an efficient mix of federal and contractor staffing needed to get the job done in the most cost-effective and expedited manner. For example, Bonneville does not have the flexibility to hire temporary employees to cut brush when needed. Bonneville must wait 90 days or pay much more to have a contractor supply brush cutters.

Although Bonneville does maintain a significant contractor presence, the agency does not have the flexibility to hire maintenance and construction craftsmen directly out of union halls, to pay competitive salaries in many job categories, to fire non-productive employees in less than two to five years, or to establish incentives specifically designed to support Bonneville's mission. For example, Bonneville invests much training in, but finds it difficult to keep power schedulers because other utilities lure them away with higher salaries.

Bonneville currently lacks the tools to downsize quickly through separation incentives, early retirement or cost effective redeployment. It takes a minimum of 18 months to reduce the workforce under current law and such reductions must be based on seniority rather than business needs. Other personnel flexibility, including improved incentives, would likely improve productivity.

Procurement and the management of property, including real property, is another critical area. A corporate structure could aid in disposing of unneeded facilities and property, thereby increasing net revenues, and allow more efficient facilities management relationships with other business partners. Buying and managing computers and communications equipment would also be made easier and more efficient. In the past, the imposition of a government-wide telecommunication policy resulted in the duplication of computing and telephone equipment. Use of Bonneville's own single microwave communication system could be more efficient, reduce redundancies, and provide a more reliable power control and communication system.

CONCLUSION

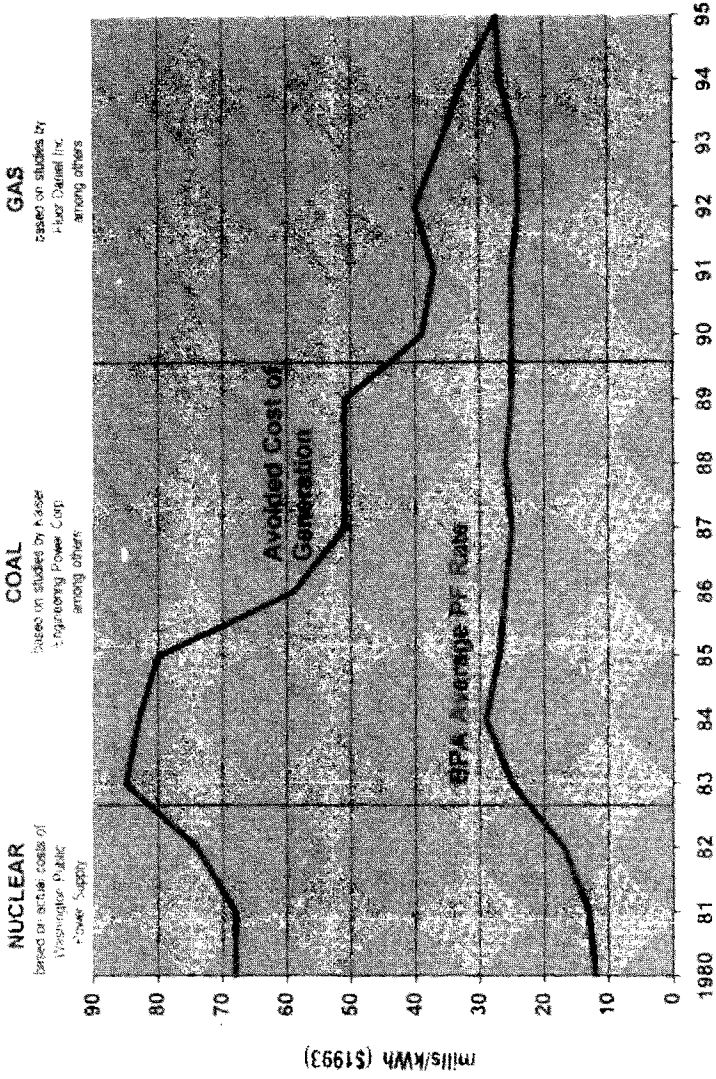
In conclusion, government corporation status:

- Can provide a structure that would allow business type agencies to remove unnecessary layers of time-consuming approval mechanisms;
- Eliminate or revise regulatory, budget or accounting directives that add costs that are not commensurate with the value provided to customers;

- Better target incentives for its work force to accomplish strategic business objectives;
 - Manage staff in the most cost-effective manner;
 - Procure and dispose of resources in a manner that produces optimal results for customers; and
 - Assume legal responsibility commensurate with a utility operation.
- This concludes my testimony, I would be pleased to respond to your questions.

Attachment A

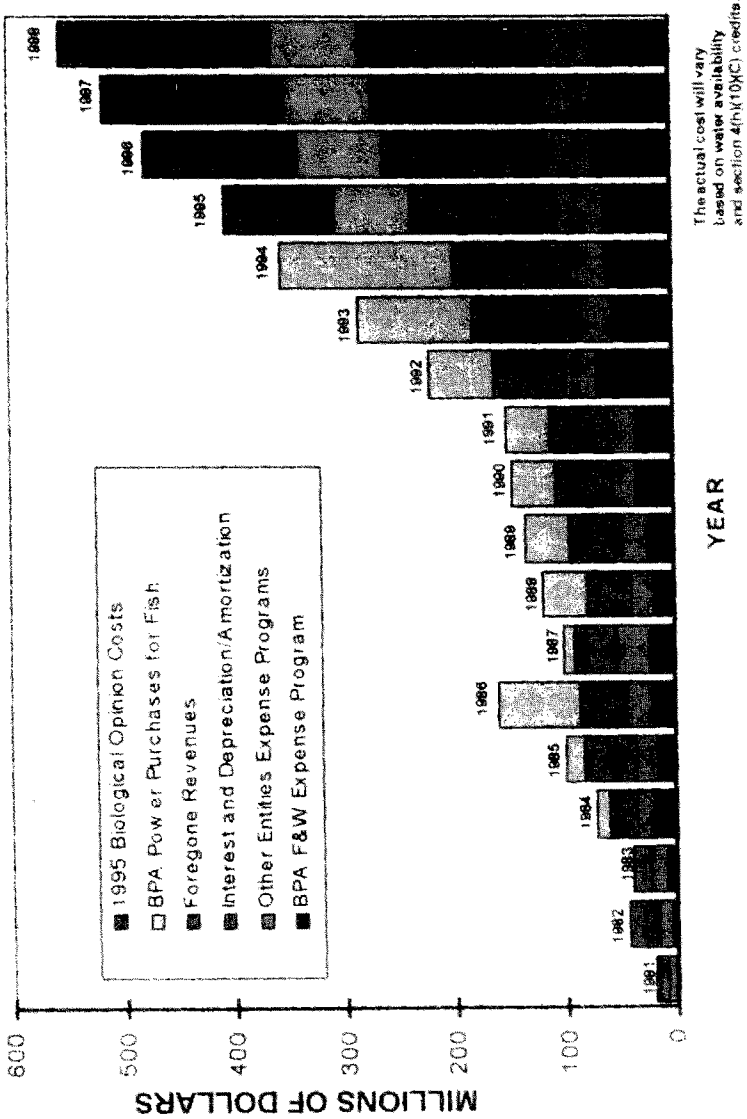
AVOIDED COST OF GENERATION VS. BPA AVERAGE RATE



Major uncertainties requiring resolution are repayment reform and fish costs

Attachment B

HFA FISH & WILDLIFE INVESTMENTS



Mr. HORN. We thank you very much.

I now yield to the gentleman from Washington, Mr. Tate.

Mr. TATE. Thank you, Mr. Chairman. And thank you for your testimony, Mr. Robertson.

A couple of questions that I have, and just start right off the bat because I think it is important that we get this on the record. Several, and many, actually, have suggested privatization of all four of the PMA's. What makes Bonneville different, and what would be the benefits and/or drawbacks of proposals such as that in trying to be more competitive and so forth?

Mr. ROBERTSON. Well, the fundamental issue I think with respect to Bonneville—the difference between Bonneville and the other PMA's is size. Bonneville is, in terms of budget, larger I think than all the other PMA's put together, and our role in the region in terms of serving 40 percent of the power supply and 75 percent of the high voltage transmission is a dominant role not comparable to any of the roles of the other PMA's in other regions of the country.

The other issue for the taxpayers that have been raised is our value in this Federal Treasury payment obligation that we have is, we calculate, worth about \$7 billion to the taxpayers right now. That is a net present value number. Given our obligations, given the fact that we have a debt ratio of 8:1, given the fact that we have this large scale fish and wildlife obligation that is growing every year, there is some serious question whether or not the taxpayers would benefit from a sale of Bonneville. That is to say, would someone purchase Bonneville with these kinds of obligations to a benefit that would exceed the \$7 billion net present value that we are now paying back to Treasury?

We also have major Endangered Species Act implications, as I indicated. We have responsibilities for fish and wildlife mitigation that other PMA's do not have. We have nuclear plant investments. We have a thing called the residential exchange. We are the entity that is designated for treaty obligations with Canada on the Columbia River. There are a number of complexities that are related to Bonneville that are not related to the other PMA's.

Mr. TATE. A followup question on that. I was looking at a few of the statistics. You know, just a few years ago we were spending \$150 million a year for fish and wildlife. Now the estimate is we would get up to \$500 million, if not \$600 million, somewhere about a 25 percent increase. Will this undermine in any way the stability of a public corporation having those sorts of uncertainties out there that—without a cap on fish? And the other part of the question is, how much of that money is directly because of the Endangered Species Act?

Mr. ROBERTSON. Of the \$550 million—well, let me start. This year we expect to spend about \$405 million on fish and wildlife, and of that amount I believe about \$260 million would be related directly to the Endangered Species Act mitigation.

In 1998, we would plan to spend, based on the requirements of fish and wildlife in the ESA, \$550 million approximately for fish and wildlife, and of that amount \$370 would be related to the Endangered Species Act.

The obligations for meeting the Endangered Species Act is carried with Bonneville whether it is a Government corporation or not. We have specifically tried to design the corporation so it achieves administrative efficiencies. We are specifically not trying to design a corporation that enhances or changes Bonneville's fundamental organic authorities because we think that would be politically complicated right now, and we are simply after the \$30 million in efficiencies we think we can get through a focused change.

Mr. TATE. Of that \$30 million, I mean what does that really mean to a ratepayer out in the Northwest region? That is actually a reduction in the overall cost?

Mr. ROBERTSON. From our perspective, the \$30 million in potential savings is savings that is now going to overhead, so slowing processes that we need to cut through in order to compete with the marketplace. If we can achieve those efficiencies, a lot of which is related to downsizing and right sizing the organization beyond what we have already done, that money should flow directly into the pockets of ratepayers of the Northwest and to our other mission purposes in the Northwest.

Mr. TATE. Would this eliminate the process of OMB and the Department of Energy's review process which is very duplicative and similar in the way that it is handled now? Would that be eliminated? Is that part of the \$30 million you are talking about?

Mr. ROBERTSON. The proposal that we are suggesting and have suggested through a regional public review process in the last year that has had hearings in the region is that we would create a corporate structure outside of the Department of Energy with the administrator of Bonneville being designated and under the supervision of the Secretary of Energy. So we would have a corporate structure outside of the Department, and that would save a great deal of overhead time and efficiencies in terms of not being a functional part of the Department of Energy.

We would still report to the Congress in the same way our budget would be submitted in the same way. We would still obviously report to the Secretary of Energy and OMB and FERC for our rate review. So everything else would stay the same, but the fact of moving the structure of Bonneville into a separate Government corporation we think would have great efficiencies.

Mr. TATE. If I may, Mr. Chairman, I have got a couple more questions.

In the area of civil lawsuits, talk to us a little bit about the advantages that you would see in dealing with civil suits under a public corporation.

Mr. ROBERTSON. Well, we have asked in the legislation that was reviewed in the region to be allowed sue and be sued status. Mr. Majkut is here, and perhaps from general counsel he can get into more details.

In simple terms, we want the ability on particularly commercial litigation areas to deal as if we were a business entity directly with our customers. For example, if we have suits exceeding \$10,000 we have to get permission to agree to that from the Department of Energy. If it exceeds \$25,000 we have to go to the Department of Justice. The ratepayers in the Northwest are paying the bills for those settlements. We are responsible to them particularly to make sure

that that is a prudent decision. We would like to be able to settle those things on the spot. That is one simple example.

But, Paul, do you want to add anything?

Mr. MAJKUT. Yes. The idea of commercial litigation being handled by Bonneville attorneys is not new. Most of our ninth circuit litigation is highly specialized, very detailed power sales contracts, so we actually do the work on that litigation now. Justice Department attorneys have specially deputized individuals in our office. We write the briefs, argue the cases, in most cases.

There are distinct kinds of litigation though. There is other commercial litigation, contract enforcement, construction contracts and tort cases, for example, which Justice generally handles, so you have to look at each discrete area.

Mr. TATE. But under these changes you folks would handle those all in house then?

Mr. MAJKUT. Well, under our proposal all commercial litigation would be handled by us. We would have without prior authorization from the Attorney General the ability to bring that litigation. In the area of NEPA, Endangered Species Act, and other environmental litigation, the noncommercial type litigation, Justice would still handle that litigation.

Mr. TATE. OK. This last quick question I asked the head of the agency, Department of Energy, Hazel O'Leary, recently, when the bill would be coming out. When can we expect a bill dealing with this particular issue to be before the Congress? When is the administration going to bring that forward?

Mr. ROBERTSON. The bill is in executive review—the executive review process right now. It has gone through OMB and is being reviewed by other agencies, and we are hoping that it will be out soon.

Mr. TATE. Soon, as in?

Mr. ROBERTSON. Weeks perhaps.

Mr. TATE. OK.

Mr. ROBERTSON. It is hard to speculate because it depends on how other agencies are reacting to it, but we are hoping—and I know the Secretary is very anxious to have it come forward.

Mr. TATE. Sure. I appreciate your work, and I yield back the balance of my time, Mr. Chairman.

Mr. HORN. Thank you very much, Mr. Tate.

I hope you can stay for Mr. Flanagan's presentation. It is rather fascinating.

We have with us Daniel V. Flanagan, Jr., the president and chief executive officer of the Flanagan Consulting Group. He is a graduate of the Naval Academy, been around Washington for a few decades, and he has a rather unique idea in the Forrestal Corp.

Please proceed and explain it.

Mr. DANIEL FLANAGAN. Thank you very much, Mr. Chairman.

I beg your indulgence to go beyond the 5 minutes, but I could stop periodically because there is a certain logic to how we explain this new concept.

It is a privilege to be here representing the Forrestal Coalition which is a number of energy-related firms and trade groups that have worked with energy infrastructure managers within the De-

partment of Defense and other agencies at their invitation to develop the legislative proposal to create the Forrestal Corp.

In addition, I was honored to serve as chairman of the Commission to Promote Investment in America's Infrastructure which was part of the Intermodal Surface Transportation Efficiency Act of 1991, where we explored how private capital can invest in our Nation's infrastructure, and I have that report with me here today. Actually, Neil Goldschmitt served on that commission as well.

This proposal to create the Forrestal Corp. is a carefully crafted and comprehensive approach that, No. 1, addresses one of the most intractable problems facing DOD today: How can the Department attract much needed private capital to finance the urgently needed modernization of its energy utility infrastructure so as to maintain the security and reliability of its existing facilities and, No. 2, to implement a successful infrastructure transition amidst base closing and realignment to a revitalized network of defense facilities having their genesis from before World War II and through the cold war. Hence the name Forrestal to commemorate the Nation's first Secretary of Defense as we approach that Department's 50th anniversary and their new path we suggest today.

The proposal would allow DOD to sponsor the Forrestal Corp. as a due diligence facilitator through which private capital could finance needed improvements. The process would be fully competitive, technologically neutral, based entirely on performance contracting, and result in no increase in the Federal budget, attracting private capital for new state-of-the-art projects to allow the Department to either make its utility programs more efficient and environmentally beneficial or to exit from these nonmission related activities altogether, leaving them to be supplied by the private sector.

In the words of Admiral Bill Owens, vice chairman of the Joint Chiefs of Staff, who pointed out in a recent Forbes magazine article, "What we need is flexibility to manage the defense resources we have. If we get proposed legislation to allow us to contract more work outside the Department it will make an enormous difference. Contracting out such things as base management, logistics, travel, and accounting processes will cut these items costs by 25 to 30 percent."

I would also like to quote the following from the Commission on Rolls Admissions of the Armed Forces Panel report which was chaired by John White, the President's nominee to replace John Deutch as deputy secretary. This report just came out the other day. "DOD should reduce the cost of support to help fund higher priority needs. Infrastructure accounts for more than half of its budget, and big opportunities for savings are available within that infrastructure. Our report is to outsource activities that need not be performed in the Government and reengineer support activities that must remain in the Government to protect the public interest. Implementation of some of our recommendations will require legislative relief from laws that inhibit efficiency. More than a quarter of a million DOD employees engage in commercial type activities that could be performed by competitively selected private companies."

Mr. Chairman, the Forrestal Corp. would expedite this investment of private capital in utility infrastructure projects by removing the two most pressing constraints that stand in the way of public/private collaboration necessary to achieve these objectives. They are:

First, the institutional constraints. Numerous studies of DOD have pointed out the various statutory, regulatory, and institutional barriers that stand in the way of greater cooperation between the public and private sector. These barriers relate primarily to the Federal Acquisition Regulations, the FAR, that were never intended to facilitate the investment of private capital into infrastructure modernization projects. The FAR exists, and rightly so, to protect the public interest in the disbursement of tax dollars to contractors.

Second, the human constraints. These same studies have revealed the general lack of personnel inside the Department with sufficient expertise, resources, and time required to structure the types of public/private relationships necessary to bring about greater utilization of private capital in meeting these infrastructure needs.

Budget constraints have made it impossible for DOD to hire and retain enough staff with sufficient expertise to keep up with the dynamic energy market that was referred to earlier and perform the essential due diligence required to ensure that DOD gets the best quality product. Unless DOD has the expertise needed to do the job, it won't get done.

Forrestal would be a private, for-profit, taxpaying District of Columbia corporation sanctioned by Congress with a required annual report to the Secretary of Defense and comptroller general audit access. It would not be an agency of the U.S. Government. It would act as an optional window between the DOD, that lacks the resources to meet its utility infrastructure modernization requirements, and the private sector, which has these resources in abundance but is discouraged from investing them in this work primarily due to the FAR.

Under the proposal, DOD utility installation managers would have the option—and that is very important; this is what they would prefer and want—of taking their requirements to the Forrestal window, which in turn would, A, solicit proposals from the private sector on a fully competitive basis; and, B, provide the necessary due diligence information to the private sector bidders and their lenders. Only in those proposals which would provide DOD with the best value, that is, price and nonprice factors, would be accorded full weight would win. The Forrestal process then would allow for the negotiation and execution of contracts between DOD and the winning bidders in a commercially oriented and timely manner.

Just as it is important to say what Forrestal is, it is important to say what it is not. Forrestal would not displace any of the development, construction, operation, or financial capabilities of the private sector. The legislation specifically requires synergistic cooperation between the corporation with neighboring energy producers and consumers, including local utilities, and requires adherence to all local and State laws governing the provision of electric utility

service. There are more than 1,000 private sector energy-related firms in the United States that are fully capable of providing DOD with the state-of-art service required to help the Department meet its targets and save taxpayer dollars. Forrestral would deploy, not displace, the best of these capabilities, nor will Forrestral usurp any decisionmaking authority that rests with the sovereign power of the Government to execute contracts.

One might ask then why would companies that compete against each other agree to work together as in our coalition to advocate the creation of this new corporation over which they would have no control? The answer is that the market created by the need of DOD to modernize its utility infrastructure is big enough that these companies think they have a good enough chance to win bids on the merits of their proposals rather than whether they have any influence in the process of awarding contracts.

Mr. Chairman, I can talk now about the needs or we can take a break for a second.

Mr. HORN. You have 2 or 3 minutes more.

Mr. DANIEL FLANAGAN. OK.

A preliminary estimate of the capital required for DOD to meet its utility infrastructure modernization requirements is about \$20 billion. This includes all the work required for the Department to comply with the mandates of Executive Order 12902 of 1994, which mandates that Government agencies—that mandates Government agency energy efficiency improvements of 30 percent or greater by the year 2005. It also includes central heating modernization, cogen, distribution improvements, and in addition to energy various waste and water treatment needs that also could be accommodated by the Forrestral process.

In the case of energy conservation need arising from that Executive order, DOD estimates an investment of about \$5 million to meet the target with projects that pay back in 10 years or less. The Department has about \$1 billion programmed subject to current congressional budgetary reductions and is attempting to develop new initiatives to secure the rest with no assurance that capital funding targets will be met without additional help from private sector initiatives.

Much of the capital funding shortfall could be accomplished using private capital via Forrestral but only if DOD could find the personnel—excuse me; I misspoke—but only if DOD could find the DOD resources necessary to develop those contracts in house.

In the area of central heating plant modernization requirements on active DOD installations, the Army construction engineering research labs recently estimated that the upgrade of 114 boiler plants would cost about \$2.1 billion and such transactions could take the form of a lease, a purchase, or a combination thereto, and DOD becomes a purchaser of electricity at a negotiated nonsubsidized market-based rate as opposed to simply being an owner. For cogeneration they suggest nearly \$900 million in investment requirements.

DOD also faces significant challenges in how to work with local communities in the ongoing base realignment and closure process. In this regard, Forrestral could help DOD arrange for the orderly upgrading, indemnification, and transfer of properties on bases either closed or to be closed to the local communities.

Beyond the goals of meeting statutory and regulatory mandates, however, is the pressing need on the part of DOD to save as much money as possible on its utility bills. DOD is the largest single customer of energy in the United States, paying nearly \$3 billion per year. The Department also has substantial expenditures for operations and maintenance and also now pollution control.

Assuming that DOD is able to meet the targets of Executive Order 12902 within the next 10 years, the Department could end up saving about \$1 billion per year of their current \$3 billion energy cost. Savings on O&M expenditures could be another \$1 billion, and savings on pollution prevention costs could be nearly \$500 million. Savings resulting from central heat plant modernization could save DOD upwards of another \$320 million per year and co-generation another \$200 million in savings. In the aggregate, potential savings on direct energy costs could total nearly \$1.5 billion per year with more than \$1.5 billion in additional savings resulting from lower O&M and pollution prevention costs.

We have not included the potential for additional savings that would result from increased worker productivity that would accompany these infrastructure improvements but believe that they would be substantial as well. Such savings, which we believe hinge on the availability of a Forrester-like process, would accrue to the Department's accounts for mission-related activities.

In addition to the energy efficiency improvement mandates of the order, these facilities must comply now with strict environmental performance mandates including those of the Clean Air Act. The infusion of capital required to meet efficiency mandates also would bring about substantial improvements in air quality.

Mr. HORN. I think we have got a pretty good picture. Can you sum it up in 30 second, and then let's get to questions.

Mr. DANIEL FLANAGAN. Very good.

Private capital is desperately needed. There are tremendous savings, but unless—from my commission activities and from working through the many, many meetings we have had at Fort Belvoir and elsewhere with installation managers, unless you have this window that can provide a due diligence opportunity for private capital and their lenders to understand they are dealing with experts, with pros, as Roger Johnson was saying, they won't bother, they'll go elsewhere, they have other places to take private capital.

The FAR, unfortunately, discriminates against that, although the FAR serves a very legitimate purpose, which is to guard public expenditures, so we suggest Forrester as the necessary facilitator but under the sponsorship of Government. It is extremely important that that sovereignty be maintained.

[The prepared statement of Mr. Daniel Flanagan follows:]

PREPARED STATEMENT OF DANIEL V. FLANAGAN, JR., THE FLANAGAN CONSULTING GROUP, INC.

Mr. Chairman, Members of the Committee, my name is Daniel V. Flanagan, Jr. I am President of The Flanagan Consulting Group, Inc. and Senior Advisor to a coalition of private sector interests that has worked with energy infrastructure managers within the Department of Defense to develop the legislative proposal to create The Forrester Corporation. In addition, I was honored to serve as Chairman of the Commission to Promote Investment in America's Infrastructure, part of the Intermodal Surface Transportation Efficiency Act of 1991. Many of the ideas developed

by the commission were utilized in the development of the Forrestal legislative proposal.

This proposal to create The Forrestal Corporation is a carefully-crafted and comprehensive approach to one of the most intractable problems facing DOD today: how can the department attract much needed private capital to finance the urgently needed modernization of its energy utility infrastructure. Private capital has never been more abundant than it is today and investment managers have said they would be most interested to see the U.S. infrastructure market become a more attractive place for investment. The Forrestal Corporation proposal is intended to make DOD utility infrastructure more attractive for private investment.

The proposed legislation would empower DOD to open The Forrestal Corporation as a new "window" through which private capital could enter into the process of financing these needed improvements. The process created by the legislation would be fully competitive, technologically neutral, based entirely on performance contracting and result in no increase in the federal budget. In fact, the purpose of the proposal is to help the federal government cut its utility bills by attracting private capital for new, state-of-the-art projects to help the department make its utility programs more efficient and environmentally beneficial.

The Forrestal Corporation would increase the investment of private capital in utility infrastructure projects by removing the two most pressing constraints that stand in the way of the public-private collaboration necessary to achieve this objective. They are:

- First, the institutional constraints. Numerous studies of the DOD have pointed out the various statutory, regulatory and institutional barriers that stand in the way of greater cooperation between the public and private sectors. These barriers relate primarily to the federal acquisition regulations (FAR) that were never intended to facilitate the investment of private capital into infrastructure modernization projects. The FAR exists to protect the public interest in the disbursement of tax dollars to contractors. Since the use of private capital involves a completely different way of doing business from the use of tax dollars appropriated to carry out federal programs, reliance on an institutional framework designed for the latter to encourage the former simply does not work.

- Second, the human constraints. These same studies have revealed the general lack of personnel inside the department with sufficient expertise, resources and time required to structure the types of public-private relationships necessary to bring about greater utilization of private capital in meeting these infrastructure needs. Budget constraints have made it impossible for DOD to hire and retain enough staff with sufficient expertise to keep up with the dynamic energy market and perform the essential due diligence required to ensure that DOD gets the best quality product. Unless DOD has the expertise needed to do the job, it won't get done.

Creation of The Forrestal Corporation will affirmatively address these two barriers. It will address the human barrier because the corporation will be staffed with knowledgeable experts who, in turn, will have the incentive to get the needed work done for DOD. It will address the institutional barrier because the corporation will be able to operate in a manner more compatible with commercial business practices than otherwise provided by the status quo. The law of commercial business would apply: If you do what the contract says, you get paid. If you do the work better than what the contract requires, you make a profit.

Forrestal would be a private special purpose corporation (SPC) sanctioned by Congress to act as an optional window between the DOD that lacks the resources to meet its utility infrastructure modernization requirements and the private-sector which has these resources in abundance but is discouraged, literally, from investing them in this work.

Under the proposal, DOD utility installations managers would have the option of taking their requirements to the window which, in turn, would solicit proposals from the private sector on a fully competitive basis. Only those proposals which would provide DOD with the best value (price and non-price factors would be accorded full weight) would win. The Forrestal process then would allow for the negotiation and execution of contracts between DOD and the winning bidders in a commercially-oriented and timely manner. It would endeavor to cut by more than half the time required to put a privately-financed deal into place, a process that can take up to as many as seven years under the regulatory status quo.

WHAT FORRESTAL IS, WHAT IT ISN'T

Just as it is important to say what Forrestal is, it is also important to say what it isn't. Forrestal would not displace any of the developmental, construction, oper-

ational or financial capabilities of the private sector. There are more than 1,000 private sector firms in the U.S. ranging in size from small 10-person energy service companies to giant worldwide corporations that are fully capable of providing DOD with the state-of-the-art service required to help the department meet its targets and save taxpayer dollars. Forrestral would deploy, not displace, the best of these capabilities. Nor will Forrestral usurp any decision-making authority that rests within the sovereign power of government to execute contracts. Rather, Forrestral's purpose will be to make the process of doing business with the government work, not fail to work as it has under the status quo. It is important to emphasize, however, that Forrestral would be an optional resource for DOD managers.

In addition, it is important to emphasize the role of the companies involved in the coalition advocating creation of The Forrestral Corporation. The companies in the coalition include CMS Energy Corporation, Consolidated Natural Gas, Ogden Power Corporation, Southern California Edison, Prudential Securities, Trigen Energy Corporation, Energy Performance Services, Dresser-Ingersoll Joint Ventures, and Dean and Associates. The Electric Generation Association, a major trade association of independent power companies, has endorsed the proposal. All the companies in the coalition advocating creation of The Forrestral Corporation are doing so because they want to compete for the business that would be brought to market by the corporation. They are not interested in having any role in the ownership or operation of the corporation. In fact, the proposed legislation contains stringent conflict-of-interest language that specifically prohibits any company bidding on a Forrestral project from owning any stock in the corporation itself. Once the corporation comes into existence, the coalition advocating its creation will disband and the companies will compete against each other and other companies for the right to develop, finance and operate Forrestral projects.

One might ask, then, why would companies that compete against each other agree to work together to advocate the creation of a new corporation over which they would have no control? The answer is that the market created by the need of DOD to modernize its utility infrastructure is big enough that these companies think they will have a good enough chance to win bids on the merits of their proposals rather than whether they have any influence in the process of awarding contracts. You can either win the competition or run the competition, not both. The companies in the coalition want to compete in, not run, the process.

The fundamental question that policy makers must answer in evaluating any legislative initiative is: Why are we doing this? We submit the following: First, there is a pressing need that is not being served by the status quo. Second, the proposal to create The Forrestral Corporation represents the best thinking of those with the greatest stake in meeting the need, those inside the Department of Defense who need to cut costs and those in the private sector who can help them do that. Third, the potential for saving money, helping protect the environment and making DOD utility infrastructure programs more efficient is big enough to justify enactment of the legislation. What follows is a discussion of these points.

I. THE ENERGY INFRASTRUCTURE NEED

A preliminary estimate of the capital required for DOD to meet its utility infrastructure modernization requirements is about \$20 billion. This includes all the work required for the department to comply with the mandates of Executive Order 12902 (March, 1994) which mandates that government agencies achieve energy efficiency improvements of 30 per cent or greater by the year 2005. It also includes central heating modernization, cogeneration, distribution system improvements and, in addition to energy, various waste and water treatment needs that also could be accommodated by the Forrestral process.

In the case of the energy conservation need arising from Executive Order 12902, the department estimates an investment of about \$5 billion to meet the target with projects that pay back in 10 years or less. The department has about \$1 billion programmed and is attempting to develop new initiatives to secure the rest, with no assurance that capital funding targets will be met without additional help from private sector investors. Much of the capital funding shortfall could be accomplished using private capital, but only if DOD could find the personnel resources necessary to develop contracts.

In the area of central heating plant modernization requirements on active DOD installations, the Army Construction Engineering Research Laboratories (CERL) recently estimated that the upgrade of 114 boiler plant upgrades would cost about \$2.1 billion. For cogeneration potential, CERL estimates the potential for nearly \$900 million in investment potential. There also is the potential for new independent power production facilities on DOD property. One estimate is that between 10

to 40 new power plants in sizes ranging up to 250 Megawatts each is possible, depending on specific needs of installations and surrounding utilities.

DOD also faces significant challenges in how to work with local communities in the ongoing Base Realignment and Closure (BRAC) process. In this regard, Forrestal could help DOD arrange for the orderly upgrading, indemnification and transfer of properties on bases either closed or to be closed to the local communities.

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Beyond the goals of meeting statutory and regulatory mandates, however, is the pressing need on the part of DOD to save as much money as possible on its utility bills. DOD is the largest single customer of energy in the United States, paying nearly \$3 billion per year. The department also has substantial expenditures for operations and maintenance as well as pollution control. Assuming that DOD is able to meet the targets of Executive Order 12902 within the next 10 years, the department could end up saving about \$1 billion per year in energy costs. Savings on O&M expenditures could be another \$1 billion and savings on pollution prevention costs could be nearly \$500 million. Savings resulting from central heating plant modernization could save DOD upwards of another \$320 million per year and cogeneration could add another \$200 million in annual savings.

In the aggregate, potential savings on direct energy costs could total nearly \$1.5 billion per year, with more than \$1.5 billion in additional savings resulting from lower O&M and pollution prevention costs. We have not included the potential for additional savings that would result from increased worker productivity that would accompany these infrastructure improvements, but believe they would be substantial as well.

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In addition to the energy efficiency improvements mandates of Executive Order 12902, these facilities must comply with strict environmental performance mandates, including those of the Clean Air Act. The infusion of capital required to meet efficiency mandates also would bring about substantial improvements in air quality.

As an illustration, one can take a typical DOD installation that uses 50,000 pounds per hour of steam from a set of old World War II boilers that require modernization. If a new cogeneration project were to be developed so that the installation could also help meet growing capacity needs of an adjacent utility (a new plant generating 80 MW of electricity and providing 50,000 pounds per hour of steam), it is possible that emissions from the old facilities could be substantially reduced. Emissions of nitrogen oxide, for example could be cut from 430,000 pounds per year to 23,000. Emissions of carbon dioxide could be cut from 1.2 million pounds per year to 57,000. If even 20 such facilities were to be developed throughout the DOD system, the reductions would be magnified accordingly.

This, in turn, would enable the U.S. government to make a significant contribution to the reduction of emissions required by the Clean Air Act and help the U.S. achieve its voluntary emissions reduction target for global warming gases as well.

II. WHY ISN'T THE STATUS QUO WORKING?

America's energy industry is undergoing a profound transformation from a set of highly regulated, vertically-integrated monopolies into dynamic, highly-competitive companies seeking to profit by delivering the best quality product in the most efficient manner possible. Empowered by the Energy Policy Act of 1992 (EPAAct), hundreds of small and large energy companies are vying for new business. In this type of market-driven environment, it's the smart consumer and the highest quality provider who come out ahead. In the private sector, energy consumers are making more educated decisions on what to buy than ever before. The federal sector, however, burdened by the regulatory status quo, lags behind the private sector in taking advantage of new products and services.

Asking why the status quo is keeping DOD from taking advantage of a highly dynamic industry is crucial to understanding why the Forrestal proposal is an effective answer. The proposal responds to the fundamental reality that DOD simply lacks the institutional and professional staff resources required to (1) keep up with trends in the evolving dynamic U.S. energy utility market and (2) take advantage of the best of what the private sector has to offer.

It's not as though the federal government hasn't tried to attract private capital for infrastructure projects. In fact, there have been about a dozen privately-financed projects (out of about 1,000 potential ones) put into place during the past 15 years. But, trying to make a privately-financed project happen in a process governed by the regulatory status quo is like trying to push a square peg through a round hole. It's not impossible, but it's so time-consuming and complicated to accomplish that

most private sector companies end up not even trying at all. Even those privately-financed projects that were completed required large amounts of time that eventually undermined the value originally envisioned by federal and private planners. In recent years, moreover, the pace of privately-financed projects has slowed even more because of DOD staff cutbacks at the very time the pace needs to be increased.

One obvious question is why couldn't DOD, even within its existing budgetary authority, simply assign personnel to a new function for the specific purpose of bringing new privately financed projects on line? In fact, DOD has done exactly that on numerous occasions, but needs still are unmet. The reason is such assignments traditionally are subject to managerial discretion, which frequently changes when "mission critical" needs assume greater priority over "non-critical" functions such as energy and other infrastructure. The situation can be compared to a police chief who has to decide between spending money on a new computer system to improve the flow of paperwork or use that money for overtime to keep officers on the street. If a crime wave hits the community, overtime to keep officers on the street always takes precedence over paperwork. Similarly, DOD will always divert funds toward mission critical needs and let the upgrade of an old boiler go for another year.

The problem is these "non-critical" needs have gone unmet for so long and budgets have become so tight that it is now virtually impossible for DOD to dedicate sufficient staff and funding for the immense task of upgrading its utility infrastructure to meet mandated energy efficiency and environmental protection goals. We submit that the best available answer is a new, dedicated, privately-financed and performance-based resource like Forrestal that will provide long-term service to DOD. Only then will the real constraints that impede the ability of the federal and private sectors to work together be effectively addressed.

I draw to your attention an excellent discussion of these constraints in a January, 1995 study prepared for DOE by Power Venture Associates.¹ The study identifies six major categories of constraints that must be understood because they form the policy justification for the Forrestal proposal:

1. Programmatic and Organizational Constraints within the Federal Government. The effort to bring about greater cooperation between the federal and private sectors is burdened by the lack of clear mandates and comprehensive programs to motivate action. The report states, "There is no central office within individual agencies, or the Federal government as a whole, whose clearly mandated mission is to pursue these projects. . . . Without a central program committed to selecting viable projects and seeing them completed, there is a higher likelihood that mixed signals will be sent to the private sector."

"Many agencies have a central energy policy and planning office that coordinates government-wide or agency-wide energy programs and usually has some budgeted funds for energy initiatives. These offices tend to be supportive of the idea of third party cogeneration projects where they are feasible, but have little ability to implement projects."

2. Resource Constraints for the Federal Government. "In the DOD the streamlining and reductions in manpower have made it impossible to develop many potential projects in-house and have left insufficient funds to hire contractors. . . . Agency personnel and private contractors alike repeatedly cite the need for additional staff trained and experienced in private sector contracting for energy services like cogeneration. The areas of expertise most often cited include integrated resource planning, project opportunity analysis, asset valuation, financial analysis and project structuring, third-party contracting techniques under the FAR, legal issues associated with negotiating these contracts and private electric power market issues. Of special concern to all is the lack of private power industry experience available within government agencies. . . . Many problems that have been encountered in the projects (attempted or undertaken) to date could have been avoided or mitigated by involvement of highly-trained, experienced staff. . . . Another source of concern is the turnover in procurement staff, particularly in the military, during the long procurement process."

3. Procurement Constraints on the Federal Government. "Key statutory authority to pursue commercially viable . . . projects is lacking. . . . For all agencies this is further complicated by the failure of the FAR Council to clarify regulations for the special energy project authorities under amendments to NECPA and EPAct. It is hard to find a participant in the third-party contracting that does not find the complexity and cost of the procurement process excessive. Even recognizing the intricacy

¹"Private Sector Financing for Power Production and Energy Efficiency Projects in Federal Facilities," by Power Venture Associates, Arlington, VA, January 26, 1995, Commissioned by the Offices of the Assistant Secretaries for Policy, Planning and Program Evaluation and Energy Efficiency and Renewable Energy, U.S. Department of Energy.

of the projects and the need to protect the public interest in a systematic manner, many Federal officials feel that the process could be improved without compromising the public's interests. . . . Mandated methodologies, contract terms, financial structures, specific equipment improvements and other inflexible terms have turned some potential bidders away from third-party contracting with the Federal government. . . . Finally, lack of ongoing involvement of the private sector in establishing a workable system for procuring their services is cited by contractors as a major barrier to future success. . . . Participation by the private sector is a way of communicating important information on the business environment in which these projects must be developed and financed."

4. Financial Issues for Private Contractors. "Government contract termination for convenience clauses (FAR Subpart 49.5) can increase the risk on many projects to the point of making them unattractive for private investment according to industry groups. These clauses allow the government to cancel the remaining term of a contract for any reason it deems fit, usually without any requirement to compensate the private developer for lost future revenues or profits. . . . Lenders and investors require some form of guarantee that will assure they can recoup their investment. . . . Some contractors have expressed the concern that government has enough authority and strength in contracting to unilaterally change or negate contracts. . . . These perceptions become more problematic with certain financing arrangements."

5. Procurement Constraints for the Private Sector Contractor. "Lack of predictability in the timing and direction of the procurement process is repeatedly cited by developers as a disincentive for their participation in competitive bids for Federal third-party projects. Similarly, the absolute length of the time elapsed in project development is a major disincentive. At many of the sites (where projects have been attempted), years elapsed before contracts could be signed and key factors changed. . . . Typically government contracting procedures are seen as dictatorial and prescriptive, not responsive in an open negotiation style to attempt to achieve a common ground."

III. THE FORRESTAL SOLUTION

It is clear, therefore, that a new alternative to the status quo is necessary if DOD, the largest single consumer of energy in America, is to take advantage of new technologies, aggressive pricing and other changes occurring in the fast-changing, dynamic energy marketplace. There are three options to be considered in helping DOD meet its energy infrastructure modernization and savings targets:

- Do nothing and hope the problem will take care of itself.
- Provide increased budget authority so that DOD can hire and retain experts in sufficient numbers to negotiate privately-financed deals.
- Use existing DOD resources in a new program to leverage private capital to get the work done. In other words, develop a new public-private partnership that will create the right incentives for the private sector to undertake the work. These incentives will be created if the private sector can (1) be confident that the people they will be working with have sufficient expertise to negotiate contracts in a manner compatible with the commercial sector and (2) that there will be adequate opportunity for reward commensurate with risk.

Obviously, the first option can be rejected out of hand. No problem can "take care of itself" if there are too many obstacles in the way of people trying to solve the problem. As to the second option, asking Congress to increase budgets is simply a non-starter in this era of government downsizing.

This leaves the third option, which we suggest is embodied most effectively and comprehensively in the legislative proposal to create The Forrestal Corporation.

Forrestal, a federally sponsored, but privately managed and financed, special purpose corporation created by Congress, would serve as an intermediary between the private sector and DOD. Forrestal would marshal experienced energy management experts in energy technology, construction and operations, environmental compliance, finance, government operations and energy law and other key areas. The proposed enabling legislation establishing The Forrestal Corporation would permit it to use a simplified procurement process which will facilitate effective response to DOD's needs and reduce costs and time delays for everyone's benefit.

The legislative design of the proposal establishes Forrestal only as an additional option available to DOD, which would retain its existing discretion with respect to utilizing its own present procurement methods or the Forrestal process. The Forrestal Corporation, like any private entity, must prove the value and benefits of its services to its customers, in this case the Department of Defense. (The proposal en-

visions, however, that other federal departments could use Forrestal on an inter-agency agreement basis.)

In addition, the Forrestal proposal is designed to be "industry friendly." That is, it would not, for example, "force" local utilities to buy power from new power plants on DOD property if there is no market for it. Similarly, there would be no requirement for a local utility to transmit, or "wheel," power if local utility franchise laws do not permit such transactions. Forrestal would be interested exclusively in "win-win" transactions that would benefit all sides.

The manner in which Forrestal would be established is particularly important to ensure that the interests of both the public and private sectors are well served. The proposal calls for the Secretary of Defense to appoint five persons from private life to incorporate Forrestal. This is to ensure that those appointed will have knowledge of the private sector, yet have the confidence of the Secretary in the early stages of the corporation. Protecting the special interests of DOD is crucial in these early stages.

Forrestal itself would be a private, for-profit, taxpaying corporation organized under the laws of the District of Columbia. Except for some initial start-up capital which, under the proposal, would be provided by DOD through the purchase of a special class of non-voting common stock, the Forrestal Corporation would be financed completely by private means. There will be no government guarantees or other use of the full faith and credit of the United States.

Once a market is determined to exist for the corporation's Class A common stock, the private shareholders who buy the stock will elect the remaining 10 directors and the original start-up capital will be returned to DOD with interest. The primary sources of the corporation's revenues would be the collection of fees for its advisory and management services.

One question that arises is why a private sector investor couldn't just capitalize the corporation without having "seed" capital provided by DOD. The answer is that a typical venture investor requires a formal business plan, a comprehensive list of property and projects to be undertaken and identified revenue streams before considering an investment. Since none of those elements exists now, the purpose of the DOD "seed" funding is to permit the development of such elements so that the sale of stock in The Forrestal Corporation itself can be accomplished. More importantly, the seed capital from DOD will enable Forrestal to be "up and running" much faster than trying to attract venture capital. Plus, a venture capitalist would insist on an extremely high rate of return that would only raise the cost of projects.

Depending on the requirements of specific DOD installations, Forrestal would be empowered to provide the following:

- Help the agency identify and assess its energy and related infrastructure needs.
- Arrange for qualified private sector companies to provide individual facility audits to determine the most economic and environmentally acceptable means of meeting such needs.
- Facilitate the development of business and financial plans for the facility.
- Develop the terms of the "sale" of steam and electricity and other utility service to the agency and for the lease or sale of the facility to a private operator.
- Issue requests for proposals (RFPs) and negotiate contracts for private sector companies to construct, upgrade, refurbish, retrofit and/or operate energy production and consuming facilities.
- Function as a central objective source of energy-related technical, financial and contracting expertise for both the federal government and the private sector.
- In addition, Forrestal could, at the discretion of DOD, carry a small equity interest in a project if DOD concluded that it would benefit the long-term viability of the project and, ultimately, DOD.

IV. HOW FORRESTAL WOULD WORK

Here is a step-by-step illustration of how Forrestal would work:

1. Under terms of enabling legislation, a military department may, at its option, enter into a "master contract" with the Forrestal Corporation enabling the department, at its option, to utilize any of the services of Forrestal. The military department then may issue task orders against the master contract to utilize Forrestal's services to complement other options available to the department.

2. The military department elects to use The Forrestal Corporation option with respect to the upgrading of the energy efficiency and environmental performance of Facility X. The department consults with Forrestal Corporation as to the depart-

ment's requirements for Facility X, including future energy needs of the department, technical requirements for upgrading and retrofitting, choice of long-term lease of facility versus outright transfer of title, security concerns (if any) and financial goals.

3. The Forrestal Corporation selects through its competitive process an energy service provider to prepare and submit a plan for Facility X as part of a report to the military department on overall feasibility analysis of the Forrestal option.

4. If the Forrestal option is deemed feasible and satisfies the military department's requirements, the department and The Forrestal Corporation may enter into contractual relationship for the Facility X upgrade in accordance with the plan agreed to by the military department.

5. Forrestal Corporation prepares and publishes RFP seeking competitive bids for the right to construct, operate, or retrofit (as appropriate) Facility X, and supply energy to the military department from such facility.

6. In consultation with the military department, The Forrestal Corporation evaluates bids.

7. If Forrestal's recommendation is accepted by the military department, a contract will be signed by the department, Forrestal and the winning bidder to undertake the project.

I would point out that, at every step of the way, Forrestal would remain fully accountable to the Department of Defense in endeavoring to bring the best of what the private sector has to offer to help DOD. This is a crucial point and was underscored by Professor Donald Kettl of the University of Wisconsin, a leading expert on government management:

The government must retain decisions over policy making. It must also retain the capacity, as the General Accounting Office put it, to 'prescribe, monitor and evaluate' the work that others (like contractors) perform on its behalf. The basic principle is this: The executive branch must be accountable for its management of government programs. To protect the public interest, it must not contract out the government's sovereign powers or its ability to exercise control over policy.²

As to the legislative proposal to create The Forrestal Corporation, Prof. Kettl said:

There are two lessons from our experience with government corporations. One is that Congress needs to take a careful review of this organizational form to ensure political accountability and financial control. The other is that the government corporation represents an unstable balance between private competition and public power. It is a model, therefore, that must be carefully tailored to the right policy problem. One intriguing proposal for a new quasi-public corporation is a plan to create 'The Forrestal Corporation.' The Forrestal Corporation would act as an intermediary between the government, which owns substantial energy facilities, and the private sector, which under the right circumstances might be interested in purchasing these facilities for operation at a profit. . . . The corporation would act as a hybrid to help bridge the gap between federal efforts to sell off government-owned facilities and private sector interest in buying them. The strategy deserves a chance to prove its worth, perhaps on an experimental basis with Department of Defense owned facilities.³

CONCLUSION

A logical question that might be asked is what is the alternative to Forrestal? All other options we have examined involve either (1) the appropriation of new federal tax dollars to set up a new federal program to work with the private sector, (2) establishment of a new government program backed by the full faith and credit of the federal government or (3) diversion of resources from functions otherwise dedicated to maintaining readiness capability to do the work. We submit that the goal of positioning the Department of Defense to respond to a changing mission in preparation for the 21st century would not be positively served by any of these options.

It is not our intent to suggest that Forrestal can solve all of DOD's utility infrastructure problems. The DOD military construction budget must remain as healthy as possible. In addition, the FAR must remain a force to protect the public interest in transactions that do not involve Private finance.

²Testimony of Donald F. Kettl, La Follette Institute of Public Affairs, University of Wisconsin-Madison, and Center for Public Management, The Brookings Institution, before Committee on the Budget, United States Senate, March 7, 1995, p. 1, "Questions for Mr. Kettl."

³Ibid.

What we do submit for your consideration is that for those projects that make the most sense in a privately-financed structure, the odds that they will be successfully undertaken are reduced if the status quo is maintained. However, the odds that projects can be successfully financed with private capital will be increased if Forrestal is created.

The proposal to create The Forrestal Corporation is offered in the context of current reality of scarce federal resources and the need to provide for a sound utility infrastructure for the Department of Defense as it positions itself to serve and protect America in the 21st century.

Thank you, Mr. Chairman and members of the Subcommittee, for your courtesies in inviting me and your kind attention to this proposal which we strongly believe is in the public interest. I would be pleased to answer questions.

THE FORRESTAL CORPORATION

- The purpose of the legislation is to enable the Department of Defense to open The Forrestal Corporation as a new "window" to attract private capital for the modernization of its environmental and energy efficiency infrastructure and help DOD save approximately \$1 billion per year on utility costs.
 - The Department of Defense is directed to appoint five persons from private life to incorporate The Forrestal Corporation to act as an optional resource for DOD to utilize in procuring service from new, privately-financed projects that will meet their objectives.
 - The Department of Defense is directed to reallocate no more than \$10 million from already appropriated programs to purchase non-voting stock in this new corporation so that it can begin to function.
 - Forrestal will not be a wholly-owned government corporation, but rather a private Special Purpose Corporation (SPC) with Congressional authorization to help DOD save money on its energy and other utility infrastructure requirements.
 - DOD will be better able to meet its energy modernization needs in an expedited manner by using Forestal's streamlined procurement and credit enhancement process to obtain the most cost effective projects from the private sector rather than the procurement process governed by burdensome federal acquisition regulations.
 - Forrestal will not displace the capabilities of private sector companies in helping the federal government meet its energy needs, but instead confine its activities to administering a streamlined process in which deals between federal agencies and private sector companies can be negotiated.
 - To guard against conflict of interest, no bidder on any Forrestal project will be allowed to own any stock in The Forestal Corporation.
 - The incorporators of this new corporation will serve as its initial directors and establish rules of procedure, develop a business plan and recruit a professional staff to carry out the functions of the corporation.
 - The corporation will be empowered to conduct its affairs as a profitable business, earn fees for its limited range of services and be able to sell stock and bonds. In no instance, however, will any of its obligations be guaranteed by the full faith and credit of the federal government.
 - It is expected that during the initial five years of its existence, the corporation will operate at a sufficient level of profitability to sell stock to the public and, therefore, return to DOD the initial funds used for its establishment and that such return will be accompanied with appropriate interest.
 - Purchasers of stock sold at public offering will be entitled to elect 10 additional persons from private life to serve on the corporation's board of directors.
 - The corporation initially will be empowered to conduct business with the Department of Defense, although other agencies will be permitted to utilize the corporation's services on an inter-agency basis.
- DOD Energy Conservation—\$5 Billion Needed for 12902 Compliance**
- \$1.1 Billion Programmed
 - \$3.9 Billion Needed from Private Sector
- 12902 Savings Targets—(Estimated Billions of Dollars-Annual)**
- \$1 Billion Energy Costs
 - \$1 Billion O&M
 - \$.5 Billion Pollution Prevention

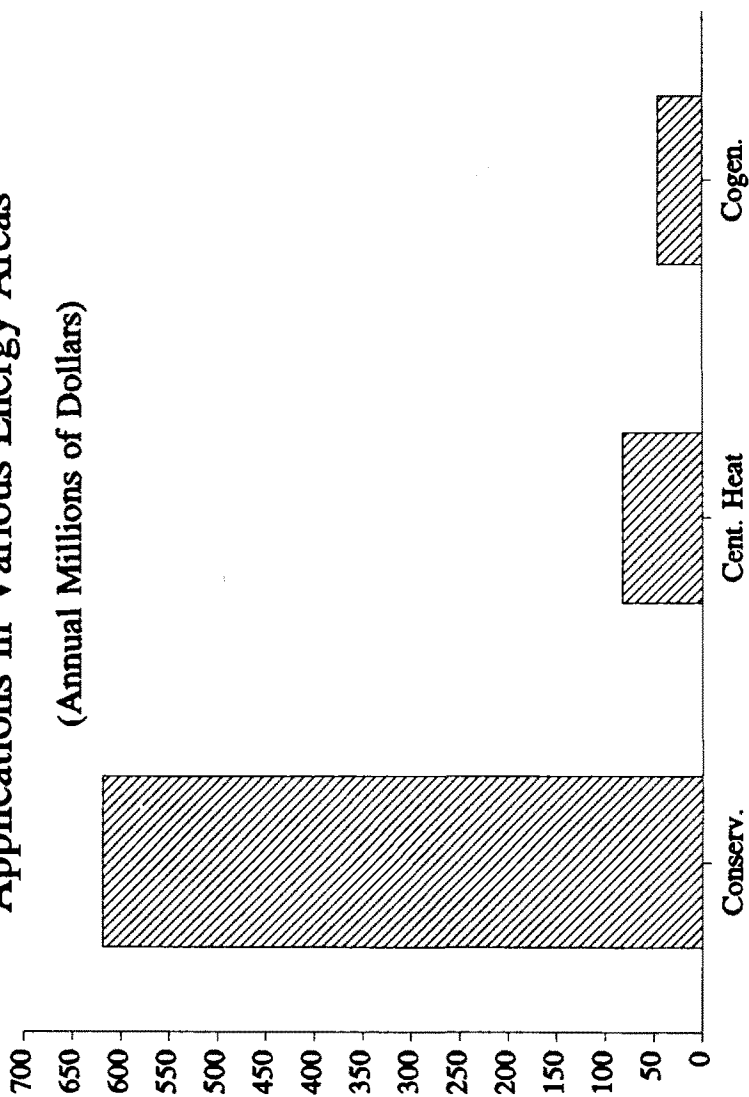
In Addition, Substantial Savings Result from Enhanced Worker Productivity

Potential Sources of Required Capital—Estimated Percentage Share

- 35% SES-ESPC (Forrestal Contracts)
- 30% Appropriations
- 25% Energy Efficiency Supply Improvement (Forrestal Contracts)
- 10% ?

Potential Forrestral Impact (Savings)

Applications in Various Energy Areas



Other Potential Benefits from Forrestal

- Independent Power Production
10–40 x 250 MW Plants
Minimum \$12 billion capital required
- Base Realignment and Closure (BRAC)
Local Development Facilitated
- Other Infrastructure—Water, Waste, Sewage
- Other Agencies on Inter-Agency Basis
DOE, NASA, VA, GSA

Federal Energy Challenge

- Federal Government Must; Modernize Its Energy Infrastructure
- Federal Agencies Lack Funds for Needed Upgrades
- Private Sector Has Capacity to Finance Upgrades
- Dynamic Energy Marketplace Provides New Technological Efficiencies
- Federal Agencies Unable to Take Advantage of Changes
- Federal Deals Too Time-Consuming for Private Sector

A New “Window” Will:

- Augment; Depleted Expertise of Federal Sector
- Reduce Risks and Costs Resulting from Time-Consuming Process

The Energy Industry—Competitive and Innovative

- Consumers Want and Are Getting More Choices Than Ever Before
- Energy Companies Responding with Intensive Marketing, Technological Development and Creative Pricing
- Consumers Are Making More Informed Decisions about Best Value
- The Best Energy Providers Profit by Helping Consumers Cut Costs

How Is the Federal Government Reacting?

- Federal Sector Lags in Taking Advantage of These Innovations
- Private Sector Consumers Are Benefitting from This Innovation, But Federal Government is Not
- Federal Energy Budgets Are Being Cut Even Though Managers Need Increased Expertise to Deal with Changing/Dynamic Market
- Even if Budgets Are Increased, Managers Still Are Burdened by Inefficient Regulations

Three Alternatives for Federal Government

- Maintain Status Quo
- Work within FAR and Boost Funding for Personnel with Sufficient Expertise for Federal Government to Take Advantage of Dynamic New Market
- Develop Alternative to FAR and Reprogram a Portion of Remaining Federal Resources to Leverage Private Sector Capital to Take Advantage of Dynamic New Market

Private Sector and the Federal Market

- Federal Sector a Vast Market to “Mine” For Profitable Opportunities amid Wasted Expenditures
- However, Private Sector Companies Find Dealing with Federal Sector Too Cumbersome Compared to Other Sectors
- Time-Sensitive Proposals Don’t Wait for Time-Consuming FAR Process
- Prospective RFPs under FAR Preclude Cost-Effective Alternatives from Being Proposed

How Forrestal Would Make a Difference

- Agencies Could Use Forrestal’s Knowledgeable Experts to Augment Depleted Staff Expertise
- Forrestal’s Expedited Process to Solicit Requirements-Oriented Proposals, Rather Than Rely on “Tunnel Vision” of Proscriptive RFPs
- Innovative Proposals Would Come Through Forrestal “Window”
- Private Companies Could Better Manage Risks on Federal Projects if Contracting Decisions Are Made in a Timely, Business-Oriented Manner

Principal Market/Beneficiary

- Department of Defense
Energy, Waste, Water Utility Infrastructure
- More Than \$20 Billion in New Capital Requirements Estimated
- Approximately \$5 Billion Required Immediately, with Only \$1 Billion Programmed
- Forrestal Proposal to be Targeted toward DOD, with Other Agencies Eligible on “Inter-Agency” Basis

Guideposts—Federal Agencies

- Use of Forrestal Must Be Optional for Agencies
- Forrestal Must Maximize Options for Agencies on a Technologically Neutral Basis
- Bidders on Forrestal Contracts Must Not Have Any Ownership in Corporation
- Agencies Must Have Ongoing “Master Contract” with Forrestal Enabling Them to Expedite Project Orders
- Forrestal Must Be Self-Sustaining with No Full Faith and Credit Backing

Guideposts - Industry

- Forrestal Must Not Displace Capabilities of Private Sector Companies
- Forrestal's RFPs Should Encourage Wide Range of Creativity to Maximize Quality Options for Agencies
- Procurement, Negotiation and Contracting Procedures Must Be Compatible with Commercial Procedures in Private Sector
- Forrestal's Fee Structure Must Insure That Bidders Place Agency's Interests Ahead of Forrestal's Interests

104th CONGRESS
1ST SESSION

H.R. ———

IN THE HOUSE OF REPRESENTATIVES

introduced the following bill; which was referred to the Committee on

A BILL

To authorize the establishment of the Forrestal Corporation to assist the Department of Defense with improving the energy efficiency, environmental performance, and operation of its energy production, consumption, and distribution facilities and to respond to the future energy needs of the Department of Defense.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

TITLE XXIX—FORRESTAL ENERGY CORPORATION

SEC. 2901. SHORT TITLE; TABLE OF CONTENTS.

(a) **SHORT TITLE.**—This title may be cited as the “Forrestal Corporation Act of 1995”.

(b) **TABLE OF CONTENTS.**—The table of contents of this title is as follows:

TITLE XXIX—FORRESTAL ENERGY CORPORATION

- Sec. 2901. Short title; table of contents.
- Sec. 2902. Definitions.
- Sec. 2903. Purpose of title.
- Sec. 2904. Establishment of Corporation.
- Sec. 2905. Powers of Corporation.
- Sec. 2906. Process of organization.
- Sec. 2907. Board of Directors.
- Sec. 2908. Governance of the Corporation.
- Sec. 2909. Ownership of the Corporation.
- Sec. 2910. Debt of the Corporation.
- Sec. 2911. Forrestal Corporation Advisory Panel.
- Sec. 2912. Authority of military departments to enter into Forrestal contracts.
- Sec. 2913. Forrestal project list.
- Sec. 2914. Annual reports.
- Sec. 2915. Conforming amendment regarding sale of electric energy at wholesale.
- Sec. 2916. Authorization of additional corporations.
- Sec. 2917. Contracting by other departments or agencies.

SEC. 2902. DEFINITIONS.

For purposes of this title:

- (1) The term “Advisory Panel” means the Forrestal Corporation Advisory Panel established by section 2911.

(2) The term "defense energy facility" means an—(A) energy production, consuming, or distribution facility owned or operated by, or leased to or from, a military department; and (B) any related infrastructure owned or operated by a military department, or leased to or from a military department, located at the same site as a facility under subparagraph (A).

(3) The term "Board of Directors" means the Board of Directors of the Corporation.

(4) The term "Comptroller General" means the Comptroller General of the United States.

(5) The term "Corporation" means the Forrestal Corporation authorized to be established by section 2904 or any additional corporation established pursuant to section 2916.

(6) The term "Director" means a member of the Board of Directors.

(7) The term "environmental study" means a study intended to satisfy the requirements of the National Environmental Policy Act of 1969 (42 U.S.C. 4321 et seq.) with respect to a defense energy facility.

(8) The term "facility audit" means a survey of a defense energy facility that provides sufficiently detailed information to allow a military department to make an informed decision whether to proceed with one or more Forrestal projects at such defense energy facility.

(9) The term "Forrestal contract" means an agreement for all or part of a Forrestal project (A) directly between the Corporation and a military department, (B) between or among a military department and one or more private parties that has been negotiated by the Corporation, or (C) among a military department, one or more private parties and the Corporation.

(10) The term "Forrestal project" means any construction, operation, refurbishing, rebuilding, upgrading, or retrofitting of a defense energy facility or any environmental study or facility audit performed by a private party for a defense energy facility.

(11) The term "military department" means the Department of the Army, the Department of the Navy, and the Department of the Air Force.

(12) The term "private party" means any entity or organization other than the Department of Defense, a military department, or the Corporation.

SEC. 2903. PURPOSE OF TITLE.

The Congress hereby declares that it is the purpose of this title to establish one or more private corporations—

(1) to help save Federal tax dollars by improving the energy, efficiency, economic performance, and environmental acceptability of defense facilities;

(2) to help the Department of Defense and the military departments identify, assess, and satisfy their energy and related defense energy facility needs by acquiring Forrestal projects from private parties;

(3) to acquire facility audits from private parties for defense facilities to determine the most economic and environmentally beneficial means of meeting such needs;

(4) to facilitate Forrestal contracts between private parties and the military departments and to enter into Forrestal contracts with the military departments and private parties;

(5) to function as a central objective source of energy-related technical, financial, and contracting expertise and advice for the Department of Defense and the military departments; and

(6) to promote commercially acceptable buying practices in the performance of Forrestal projects.

(7) to foster synergistic cooperation among defense energy facilities and neighboring energy producers and consumers, including local utilities.

SEC. 2904. ESTABLISHMENT OF CORPORATION.

(a) **ESTABLISHMENT**—There is hereby authorized to be created in accordance with section 2906 a District of Columbia business corporation to be named the "Forrestal Corporation".

(b) **TREATMENT OF CORPORATION**—The Corporation shall not be an agency, instrumentality or establishment of the United States Government and shall not be a "Government corporation" or "Government controlled corporation" within the meaning of chapter 91 of title 31, United States Code. The Corporation shall be subject to the provisions of this title and, to the extent not inconsistent with this title, to the District of Columbia Business Corporation Act (D.C. Code, sec 29-301 et seq.). Except as provided in this title, or applicable laws of the United States, the Corporation shall have all the powers of a District of Columbia business corporation.

(c) **OFFICE**—The Corporation shall maintain an office for the service of process and papers in the District of Columbia, and shall be deemed, for purposes of venue in civil actions, to be a resident thereof. The Corporation may establish offices in such other place or places as the Board of Directors may deem necessary or appropriate for the conduct of its business.

SEC. 2905. POWERS OF CORPORATION.

(a) **PERFORMANCE OF FORRESTAL CONTRACTS**—The Corporation may enter into a Forrestal contract to provide any military department a Forrestal project, through the use of private parties, except that in performing any such contract, the Corporation shall procure all subcontracts, supplies, and services involving expenditures of over \$100,000 through the use of competitive procedures approved by the Board of Directors.

(b) **NEGOTIATION**—In lieu of performing a Forrestal contract directly, the Corporation may negotiate Forrestal contracts between or among the military departments and one or more private parties and may solicit and evaluate proposals and bids for such contracts.

(c) **RELATED GENERAL POWERS**—In furtherance of its powers under subsections (a) and (b), the Corporation—

(1) may lease, sublease, purchase, accept gifts or donations of, or otherwise acquire any real, personal, or mixed property, or any interest therein, may own, hold, improve, use, or otherwise deal in or with such property, and may sell, convey, mortgage, pledge, lease, sublease, exchange, or otherwise dispose of such property;

(2) may perform management support services in connection with Forrestal projects;

(3) may charge to and collect fees for any advisory or management support services performed by the Corporation, and for any financial assistance provided by the Corporation with respect to Forrestal projects;

(4) may, only to the extent such actions have been approved in accordance with subsection (d), enter into joint ventures, partnerships, limited partnerships, and other types of contractual arrangements, and make loans, enter into guaranty agreements, and otherwise provide financial assistance to a military department or private parties, or invest in the securities of private parties in connection with the leasing, ownership, or financing of a Forrestal project;

(5) may provide or arrange for environmental indemnification of private parties for environmental hazards existing at any defense energy facility at the time the Corporation undertakes any Forrestal project with respect to such facility;

(6) may sue and be sued in its corporate capacity in any court of competent jurisdiction

(7) may issue capital stock in accordance with section 2909; and

(8) may issue notes, bonds, and otherwise incur debt in accordance with section 2910.

(d) **LIMITATIONS**—Notwithstanding this section or any other provision of this title, the Corporation shall not have the power, directly or indirectly, to invest in a Forrestal project or otherwise acquire or retain an ownership in a Forrestal project or its associated stream of revenues without the express written approval of such actions by the Secretary of Defense. In all such cases, any opportunity to invest in the Forrestal project must be available to private parties under competition procedures approved by the Board of Directors that at a minimum involve advertising such opportunity in the Commerce Business Daily. The Corporation shall not have the power to perform the facility audit, design, construction, or long-term operation of a Forrestal project, except through the use of private parties. [Note: In addition to design, construction, what about rebuilding, upgrading, etc., which are terms that appear in the definition of Forrestal project.

SEC. 2906. PROCESS OF ORGANIZATION.

(a) **INCORPORATION**—(1) within 30 days after the date of the enactment of this title, the Secretary of Defense shall appoint the Chairman of the Board of Directors and 4 additional persons, who together shall be the incorporators of the Corporation. The incorporators may not be officers or employees of the United States.

(2) Within 60 days after the completion of the appointments, the incorporators shall take whatever actions are necessary or appropriate to incorporate the Corporation, including the signing and filing of its articles of incorporation, and shall serve as the initial Board of Directors.

(b) **INITIAL OPERATIONS**—(1) Within 60 days after the incorporation of the Corporation, the Chairman of the Board of Directors shall appoint an interim Presi-

dent of the Corporation from private life who shall serve at the pleasure of the Board of Directors until the first election of a full Board of Directors by shareholders of class common stock.

(2) The interim President shall have such powers and may exercise such authority as is necessary for the proper operation of the Corporation, including the hiring of its employees, the initial issuance and sale of class B common stock to the United States for such price and upon such terms and conditions as are authorized by the Board of Directors, and, if the Board of Directors determines that a market exists for the class A common stock, the first issuance and sale of such stock for such price and upon such terms and conditions as are authorized by the Board of Directors.

(3) To assist in the startup of the Corporation, the Secretary of Defense may detail to the Corporation, upon receipt of a written request from the interim President of the Corporation, appropriate personnel as may be required for the Corporation's functioning, until such time as the first Board of Directors is elected by the holders of class A common stock and officers and employees of the Corporation are hired. No such detail of personnel shall exceed two years in length. The Corporation shall reimburse the Department of Defense for the salary and benefit costs of such detailed personnel.

SEC. 2907. BOARD OF DIRECTORS.

(a) **APPOINTMENT OR ELECTION**—The business of the Corporation shall be managed by or under the direction of the Board of Directors, consisting of 15 individuals who shall be appointed or elected as follows:

(1) a Chairman of the Board of Directors who shall be appointed by the Secretary of Defense from private life.

(2) four individuals who shall be appointed by the Secretary of Defense from private life.

(3) ten individuals who shall be elected by the holders of the class A common stock of the Corporation.

(b) **TERM**—(1) The term of each Director shall be 3 years. Any Director appointed by the Board of Directors to fill a vacancy may be appointed only for the unexpired term of the succeeded Director

(2) The members of the Board of Directors commencing on the first election of Directors by the holders of class A common stock shall have terms as follows:

(A) Three-year term: Chairman appointed by the Secretary of Defense, one Director appointed by the Secretary of Defense, and three Directors elected by the holders of class A common stock.

(B) Two-year term: Two Directors appointed by the Secretary of Defense, and three Directors elected by the holders of class A common stock.

(C) One-year term: One Director appointed by the Secretary of Defense, and four Directors elected by the holders of class A common stock.

(c) **COMPENSATION**—Directors, including the Chairman, shall serve on a part-time basis and shall be paid at a commercially reasonable rate established by the Board of Directors, after consultation with the Advisory Panel.

SEC. 2908. GOVERNANCE OF THE CORPORATION.

(a) **BYLAWS**—The Board of Directors shall adopt and may from time to time amend in accordance with the District of Columbia Business Corporation Act (D.C. Code, sec 29-301 et seq.), such bylaws as are necessary for the proper management and operation of the Corporation. Such bylaws shall not be inconsistent with the provisions of this title or the Corporation's articles of incorporation.

(b) **OFFICERS AND EMPLOYEES**—(1) The Board of Directors shall appoint a President, who shall be the chief executive officer of the Corporation, and such other offices as the Board of Directors may deem appropriate, define their duties, and establish a system of compensation for individual officer positions and other categories of employees of the Corporation. All officers appointed shall be from private life.

(2) The Corporation shall recruit and employ (on a permanent or temporary basis as the Board of Directors deems appropriate) persons with appropriate technical, financial, legal, contracting, and operational expertise to assist in the identification and acquisition of Forrestral projects and Forrestral contracts, and shall employ such other administrative personnel as the Board of Directors determines necessary or appropriate for the transaction of the business of the Corporation.

(3) Except as specifically provided in this title, Directors, officers, and employees of the Corporation, shall not be subject to any law of the United States relating to post Federal employment by reason of their employment with the Corporation.

(4) No political test or qualification shall be used in selecting, appointing, promoting, electing, or taking other personnel actions with respect to Directors, officers, agents, and employees of the Corporation.

(c) **FISCAL YEAR**—The fiscal year of the Corporation shall begin on each October 1 and end on the subsequent September 30.

(d) **INDEPENDENT AUDITS**—(1) The financial statements of the Corporation shall be audited annually in accordance with generally accepted auditing standard by a firm of independent certified public accountants of recognized national standing selected by the Board of Directors. All books, accounts, financial records, reports, files and other papers, things, and property belonging to or used by the Corporation and necessary to facilitate each audit shall be made available to the firm conducting such audit.

(2) The Comptroller General may review any audit of the Corporation's financial statements conducted under paragraph (1). The Comptroller General shall report to Congress and the Corporation the results of any such review and shall include in such report any recommendations based on such review.

(3) All books, accounts, financial records, reports, files, papers, and property belonging to or used by the Corporation and its auditing firm that the Comptroller General considers necessary to the performance of any audit or review under this section shall be made available to the Comptroller General.

(e) **CONFLICTS OF INTEREST**—(1) Except as permitted by paragraph (3), no Director shall note on any maker respecting any application, contract, claim, or other particular maker pending before the Corporation, in which, to his or her knowledge, he or she, his or her spouse, parent, minor child, partner, or an organization (other than the Corporation) in which he or she is serving as officer, director, trustee, partner, or employee, or any person or organization with whom he or she is negotiating or has any arrangement concerning prospective employment, has a financial interest

(2) Action by a Director contrary to the prohibition contained in paragraph (1) shall be grounds for removal of such Director by the Board of Directors or, if appointed by the Secretary of Defense, but any such action shall not impair or otherwise affect the validity of any otherwise lawful action by the Corporation in which such Director participated.

(3) The prohibition contained in paragraph (1) shall not apply if the Director first advises the Board of Directors of the nature of the particular matter in which he or she proposes to participate and makes full disclosure of such financial interest, and the Board of Directors determines by majority vote that such financial interest is too remote or too inconsequential to affect the integrity of such Director's services for the Corporation in that matter. The Director involved shall not participate in such determination.

(4) No person or entity (other than the Federal Government) that is an owner of the Corporation's outstanding class A common stock shall be allowed to enter into a Forrestal contract for, or to propose for or to bid on, a Forrestal contract for materials to be furnished or work to be performed pursuant to or in connection with a Forrestal contract.

SEC. 2909. OWNERSHIP OF THE CORPORATION.

(a) **VOTING CLASS A COMMON STOCK**—(1) The Corporation shall have authorized class A common stock having such par value as may be fixed by the articles of incorporation.

(2) Each share of class A common stock shall entitle its holder to one vote with rights of cumulative voting in the election of Directors as set forth in the articles of incorporation.

(3) The maximum number of shares of class A common stock that the Corporation may issue and have outstanding at any one time shall be fixed by the articles of incorporation.

(4) Each share of class A common stock shall be fully transferable only on the books of the Corporation. However, no shares of class A common stock may be purchased or held by the United States except by reason of the conversion of class B common stock under subsection (b)(5).

(b) **NONVOTING CLASS B COMMON STOCK**—(1) The Corporation shall have authorized class B common stock having such par value as may be fixed by the articles of incorporation.

(2) Shares of class B common stock shall not entitle their holders to vote in elections of Directors or any other matter except to the extent required by the District of Columbia Business Corporation (D.C. Code, sec 29-301 et seq.).

(3) The maximum number of shares of class B common stock that the Corporation may issue and have outstanding at any one time shall be fixed by the articles of incorporation.

(4) Shares of class B common stock may be purchased and owned only by the United States, acting through the Secretary of Defense, and shall be held of record the Department of Defense.

(5) At such time as the Board of Directors determines that shares of class A common stock have been sold for more than \$10,000,000, and upon the request of the Secretary of Defense, the Board of Directors shall convert such number of shares of class B common stock as may be requested by the Secretary of Defense into the same number of shares of class A common stock, in accordance with the articles of incorporation and upon such terms as the Secretary of Defense and the Board of Directors may agree. Any class B common stock; so converted into class common stock may be sold by the Federal Government at any time.

(c) **OTHER NONVOTING STOCK**—The Corporation may issue, without limitation as to amount or restriction as to ownership, such other nonvoting common, preferred, and preference stock, in such amounts, and at such times, as are authorized by the articles of incorporation.

(d) **DIVIDENDS**—Dividends may be declared by the Board of Directors and paid to the holders of outstanding shares of class A common stock as permitted by the District of Columbia Business Corporation Act (D.C. Code, sec 29-301 et seq.) and the articles of incorporation.

SEC. 2910. DEBT OF THE CORPORATION.

(a) **ISSUANCE AND SALE OF DEBT INSTRUMENTS**—The Corporation may issue, sell, and have outstanding such notes, bonds, and other debt instruments having such maturities and bearing such rate or rates of interest as may be determined by the Board of Directors.

(b) **RULES OF CONSTRUCTION**—No instrument that is issued, insured, or guaranteed by, or otherwise is an obligation of the Corporation, nor any contractual undertaking by the Corporation, shall be construed to be an obligation or undertaking which is guaranteed by the full faith and credit of the United States.

SEC. 2911. FORRESTAL CORPORATION ADVISORY PANEL.

(a) **ESTABLISHMENT**—There is hereby established an Advisory Panel to the Board of Directors which shall review the Corporation's business plans and advise the Corporation regarding such other matters as the Board of Directors may request of the Advisory Panel from time to time.

(b) **MEMBERS**—The Advisory Panel shall be comprised of the Assistant Secretary of Defense for Economic Security and such representatives from the private sector as the Board of Directors may select to ensure that the views of the financial community and the various segments of the energy industry (including the energy service companies, the independent power producers, the utilities, and architectural and engineering companies) are available to the Board of Directors. The Assistant Secretary of Defense for Economic Security shall be the Chairperson of the Advisory Panel.

(c) **MEETINGS**—The Advisory Panel shall meet with the Board of Directors not less than semiannually.

SEC. 2912. AUTHORITY OF MILITARY DEPARTMENTS TO ENTER INTO FORRESTAL CONTRACTS.

(a) **GENERAL AUTHORITY**—Any military department may enter into one or more Forrestal contracts, on a noncompetitive basis, for a period not to exceed 30 years, for the performance of a Forrestal project. Forrestal contracts may be for one or more Forrestal projects, and any military department may enter into a single Forrestal contract with the Corporation authorizing multiple Forrestal projects to be performed behalf of such military department.

(b) **EXCEPTION FROM CONTRACT REQUIREMENTS**—Except as provided in subsection (c) and in order to foster the growth of standard industry practices in Federal procurement, no Federal law, rule, or regulation dealing with the solicitation, award, execution, delivery or performance of public or Federal contracts (including chapter 137 title 10, United States Code) shall apply to any Forrestal contract or any subcontract awarded thereunder.

(c) **CONTINUED APPLICATION OF CERTAIN REQUIREMENTS**—The following provisions shall apply to every Forrestal contract any subcontracts awarded under a Forrestal contract:

(1) The Act of March 3, 1931 (40 U.S.C. 276a et seq.), commonly known as the Davis-Bacon Act.

(2) The dispute resolution procedures of the Contract Disputes Act of 1978 (41 U.S.C. 601 et seq.).

(d) **SALE OF EXCESS ELECTRIC POWER.**—Notwithstanding section 804(2)(B) of the National Energy Conservation Policy, Act (42 U.S.C. 8287c(2 B)) relating to the use of energy savings, electric power produced as a result of a Forrestral contract, and not needed by a military department, may be sold to other agencies or to private parties. However, such electric power shall not be sold to such entities in a manner inconsistent with State law governing the provision of electric utility service, including State utility commission rulings and electric utility franchises or service territories established pursuant to State law or regulation.

(e) **TERMINATION CLAUSE.**—Forrestral contracts may contain a clause authorizing the termination of a Forrestral contract for the convenience of the Government. Such clause may permit anticipatory profits and consequential damages to the extent of termination.

(f) **LEASE OF REAL PROPERTY AUTHORIZED.**—The Secretary of a military department may lease real and related personal property under the jurisdiction and control of the Secretary in connection with a Forrestral project undertaken pursuant to a Forrestral contract for a period not in excess of 50 years.

(g) **RULE OF CONSTRUCTION.**—No officer, director, or employee of the Corporation shall be construed to be a "procurement official" as such term is used in the Procurement Integrity Act.

SEC. 2913. FORRESTAL PROJECT LIST

Within 180 days after the date of the enactment of this title, the Secretaries of the military departments will develop and submit to the Corporation a list of defense energy facilities potentially suitable to the award of Forrestral contracts pursuant to the authority of this title. The Secretary of a military department may contract with the Corporation to aid in the preparation of this list.

SEC. 2914. ANNUAL REPORTS.

The Corporation shall prepare and submit to the Secretary of Defense within 90 days after the close of each fiscal year an annual report of its activities. Such report shall contain—

- (1) a general description of the Corporation's operations;
 - (2) a summary of the Corporation's operating and financial performance;
- and
- (3) a copy of the financial statements of the Corporation for the related fiscal year together with the audit report on such statements prepared pursuant to section 2908(d).

SEC. 2915. CONFORMING AMENDMENT REGARDING SALE OF ELECTRIC ENERGY AT WHOLESALE.

Section 32(a)(3) of the Public Utility Holding Company Act of 1935 (15 U.S.C. 79z-5a(a)(3)) is amended by adding at the end the following new sentence: The term also includes the provision of electric energy to an agency (as such term is defined in section 551(1) of title 5 United States Code) other than the United States Postal Service."

SEC. 2916. AUTHORIZATION OF ADDITIONAL CORPORATIONS.

No earlier than two years after the date of the enactment of this title, the Secretary of Defense shall have the authority to establish up to four additional Corporations with the same purposes, functions, authorities, powers and limitations as the Forrestral Corporation authorized to be established by section 2904. A decision to establish such additional corporation or corporations shall be based on the Secretary of Defense's written determination that such additional corporation or corporations could provide increased administrative efficiency and technical expertise to the Department of Defense.

SEC. 2917. CONTRACTING BY OTHER DEPARTMENTS OR AGENCIES.

Notwithstanding any other provision of this title, if the head of a Federal executive department or agency determines that the services of the Corporation would be beneficial in accomplishing the purposes of this title with respect to any energy production, consumption or distribution facility under such department's or agency's control, such Federal executive department or agency may enter into a Forrestral contract for a Forrestral project with respect to such facility on the same terms and using the same procedures as provided in this title for the Department of Defense and the military departments. In such case, the terms "defense energy facility", "facility audit", "Forrestral project", and "Forrestral contract" shall be deemed to refer to such Federal executive department or agency and the energy production, consumption, or distribution facilities of such Federal executive department or agency, as appropriate.

THE FORRESTAL CORPORATION

Following are questions and answers that will help explain the Forrestal concept and Process.

What is the problem facing the Department of Defense that the proposal to create The Forrestal Corporation would address?

The agency's steam and electric generating plants and transmission and distribution facilities are generally old, inadequately maintained and not in compliance with a long list of requirements, including:

- Clean Air Act Amendments
- Energy Policy Act of 1992 (EPAct) efficiency requirements
- Executive Order 12750 (April 1991) mandatory improved energy efficiency in federal buildings, facilities and vehicles
- Executive Order 12902 requiring 30% efficiency gains by 2005

Continued operation of these facilities is inefficient from the taxpayers' standpoint and inconsistent with the Administration's broad environmental policy goals, particularly global warming.

Why aren't the federal departments owning these facilities correcting this situation on their own?

First, the budgetary impact of upgrading and retrofitting these facilities is estimated at upwards of \$20 billion over the next five years. Federal appropriations of these amounts are doubtful in the present economic situation, especially if there is an alternative way to fund these costs. Second, any upgrading and retrofitting program will require expertise and experience that is not now available in each of the agencies where they are needed. Competition for this expertise in the private sector is intense and the agencies would be at a competitive disadvantage if they sought to hire their own new operating staffs.

Why wasn't the private sector utilized before to operate these facilities?

With the change in the national security situation in recent years, there is no longer a need for a totally controlled "in-house" energy supply there once was. Equally important is the 1992 passage of EPAct, allowing, for the first time, private energy companies to operate electric generating plants in more than one state without subjecting themselves to extensive federal utility regulation under the Public Utility Holding Company Act of 1935.

How can the private sector solve this problem?

Enactment of EPAct has energized the independent power industry, and those engaged in steam plant operations by opening up opportunities to operate power plants in all 50 states. A large number of experienced, highly expert organizations are interested in new opportunities to apply modern steam and electric generating technology. Upgrading, retrofitting and operating federal facilities is just such an opportunity, particularly since the federal agencies' steam and/or electric power needs provide a base load market which can be coupled with electric power sales to utilities in the same region. These companies have demonstrated their ability to raise capital for these types of projects. In addition, many utilities themselves will be interested in the potential for modernizing and operating these plants when they are located in their service area. Thus, both the money and the people are available to solve the agencies' problems.

How does the proposed Forrestal Corporation facilitate the application of modern technology and private capital to the solution to this problem?

A federally sponsored, but privately managed and financed, special purpose corporation created by Congress would serve as an intermediary between the federal agency owning the energy facility and the private energy sector. Forrestal will marshal experienced energy management experts in energy technology, construction and operations, environmental compliance, finance, government operations and energy law and other key areas. The enabling legislation establishing the Forrestal Corporation would permit it to use a simplified procurement process which will facilitate effective response to the government's needs and reduce costs and time delays for everyone's benefit.

Why is legislation needed to establish a new corporation for this purpose? Wouldn't it be better just to open a new office or hire a private contractor to do this work?

For nearly 20 years, the federal government has been opening offices and hiring private contractors to encourage more private investment in infrastructure projects. The results have been very disappointing and were set forth last year in an OTA report which said that of the limited number of energy infrastructure projects un-

dertaken so far in the 1990s, only eight per cent were privately financed.¹ The reasons cited by OTA include the cumbersome federal acquisitions, the inability of agencies to hire enough expertise to negotiate privately financed deals and the general lack of commitment from senior agency officials to get the work done. Moreover, the very programs set up for the purpose of attracting private capital are becoming more, not less, vulnerable to budget cuts. The Forrestal Corporation, however, would be a significant improvement over the status quo because it would be totally privately financed and staffed with experts with the incentive to get the work done.

Would the federal agencies be forced to use the Forrestal Corporation for all their energy projects?

No. The legislative design establishes the Forrestal Corporation only as an additional option available to the federal agencies. The Forrestal Corporation, like any private entity, must prove the value and benefit of its services to its customers, in this case the respective federal agencies. The federal agencies would retain discretion with respect to utilizing their own present procurement methods or using the Forrestal process.

What exactly would the Forrestal Corporation do for the federal agencies?

Depending on the nature of the energy project proposed, Forrestal would:

- Help the agency identify and assess its energy and related infrastructure needs.
- Arrange for qualified private sector companies to provide individual facility audits to determine the most economic and environmentally acceptable means of meeting such needs.
- Facilitate the development of business and financial plans for the energy facility.
- Develop the terms of "sale" of steam and electricity to the agency and for the lease or sale of the facility to a private operator.
- Issue RFPs and negotiate contracts for private sector companies to construct upgrade, refurbish, retrofit and/or operate energy production and consuming facilities.
- Function as a central objective source of energy-related technical, financial and contracting expertise for both the federal government and the private sector.

Forrestal would have some rather broad powers by being able to operate as a for-profit corporation apart from federal acquisition regulations. Wouldn't this give Forrestal an unfair advantage over other private corporations that would like to perform work for the federal government?

The question assumes that Forrestal would be in the same business as any other private sector company. In fact, Forrestal would be prohibited from offering or undertaking any of the developmental, contracting, operational or financial capabilities of private sector companies. Forrestal's exclusive purpose would be to bring federal infrastructure requirements to market so that private sector companies can compete for projects to serve federal needs. Forrestal's functions would be narrowly defined to simply operate as an optional procurement "window" for federal installations managers. All functions normally performed by private sector companies would be provided on a fully competitive basis.

What type of corporation will Forrestal be and who would own and finance the Forrestal Corporation?

Forrestal will be a private, for-profit, taxpaying corporation organized under the laws of the District of Columbia. Except for some initial start-up capital which might be provided by the federal government (Department of Defense) either through the purchase of a special class of common stock restricted to government ownership or a debt instrument, the Forrestal Corporation would be financed completely by private means. There will be no government guarantees or other use of the full faith and credit of the United States. As proposed, the Department of Defense will have five of the 15 directors, including the initial chairman of the corporation, and have certain special rights to protect the agencies' essential interests. Once a market is determined to exist for the corporation's Class A common stock, the private shareholders will elect the remaining 10 directors. The primary sources of the corporation's revenues would be the collection of fees for its advisory and management services. The corporation would not have the authority to invest in an energy project or retain an ownership interest in an energy project or its associated stream of revenues without the approval of the head of the Agency involved.

What is the advantage of using the Forrestal Corporation process?

¹ U.S. Congress. Office of Technology Assessment, *Energy Efficiency in Federal Facilities: Update on Funding and Potential Savings*, OTA-BP-ETI-125 (Washington, DC: March, 1994), p.9.

While Congressional action is required for the corporation to be established, it has a number of advantages over having each department or agency handle its energy facility upgrading on a plant-by-plant basis by issuing its own RFP. The advantages include the following:

- Under this proposal, federal agencies would have the option of using Forrester's streamlined procurement processes to work with the private sector in the development of new projects. This option would be an alternative to the Federal Acquisition Regulation (FAR) procedures, which were never intended to regulate the use of private sector financing in the first place and, if applied, would impede any effort to marshal private capital. Attempting to amend FAR would be counterproductive and could even compromise its original purpose of protecting the public interest in the disbursement of government funds to contractors.
- Necessary experience and expertise can be collected and made available to solving all federal agencies energy facility operating and environmental problems. The private sector will gain respect for this experience and expertise, particularly if it is assembled in an entity using commercial business practices with an accompanying rating. This will be necessary to maximize the private sector's participation.
- A broader vision of the mission to enhance the efficiency and environmental performance of all federally owned energy facilities will be applied to each federal agency and its facilities. This will greatly facilitate the attraction of private capital and modern technology to this mission. It will also provide a more rational and coordinated approach to the marketing of electricity to utilities that need to balance their total capacity and loads over extended periods of time.

Other solutions, such as having the department and agencies upgrade the plants themselves or creating a government-financed corporation to take over the energy plants, are "budget busters" that will fail to take advantage of the competitive forces which can lower energy costs and improve environmental performance with state-of-the-art technology.

Will divorcing energy management from other management functions at the government installation erode accountability?

No. One purpose of private operation of energy facilities at government installations is to allow the installations management to focus on the central mission of the installation, e.g., national security or research. The appropriate operating and lease agreements will protect the mission and establish a system to assure accountability of the operator in its support of the mission. Experience with third-party financing indicates there will be no dilution of the efforts to support the central mission.

Isn't it more risky for the federal government to set up a corporation like Forrester than it is to simply direct existing procurement programs to work harder?

To the contrary! By bringing a new privately-financed entity like Forrester into the procurement equation, the private sector would take on more risk than ever before while the federal government would take on less. There are two reasons for this. First, Forrester would be a privately-financed corporation with revenues coming from project fees, not direct appropriations from Congress. The only exception would be an initial investment of no more than \$10 million reprogrammed from existing DOD budgets to buy non-voting stock in the corporation. Once that initial capital is returned to DOD with interest, Forrester will have no further funding from any agency budget. Second, all projects brought through the Forrester window would be privately-financed, meaning that if the developer and operator of a Forrester project don't do what contracts require them to do, they don't get paid. The alternative is for the federal government to appropriate funds to hire staff, pay for contractors to build new projects and remain liable for over-budget expenditures. As we have seen, however, current budget realities make such appropriations highly unlikely if not altogether impossible.

Won't the creation of this new corporation result in the loss of federal jobs already dedicated to improving the efficiency of federal energy programs?

No. The legislation to create Forrester does not link the hiring of staff to run the corporation with any concurrent reduction in the federal work force. Nor will Forrester displace any function currently in place within the federal government. Rather, Forrester will be a complement to the range of options available to federal utility managers, thereby giving them more flexibility in gaining access to service form privately-financed projects. If anything, the existence of Forrester will enable federal workers to do their jobs faster and more efficiently. As the federal government moves toward a more performance-based system, Forrester will help federal workers add more tangible accomplishments to their performance review appraisals. Moreover, the legislation to create Forrester provides for a number of its positions to be filled by federal workers being "detailed" to the corporation.

What about the sovereign responsibility of government to make decisions on whether utility infrastructure projects are to be undertaken? If Forrestal is created, wouldn't the government, in effect, delegate to a private corporation the decision-making authority that properly lies with government?

Absolutely not. The legislation creating Forrestal clearly states that federal installations managers retain clear authority on whether to use any or all of the services provided by Forrestal.

Wouldn't the Forrestal Corporation have "monopoly" status by its Congressional authorization? Shouldn't Forrestal have some competition in the same way, for example, that Fannie Mae has to compete against Freddie Mac?

Certainly. In fact, the Department of Defense, the biggest market for utility infrastructure modernization, has suggested exactly that. Language to that effect is contained in the draft legislation.

Q & A ABOUT FORRESTAL FROM THE ELECTRIC UTILITY PERSPECTIVE

1. By its ability to operate outside the FAR, wouldn't Forrestal create an incentive for competitors to enter a utility service territory to serve a large DOD base?

DOD bases will continue to buy electricity from their local electric utilities with or without Forrestal. The issue Forrestal addresses is how DOD can work with utilities in making the most timely and cost effective choices in taking advantage of new energy-efficient technologies. New business opportunities for utilities will be opened by Forrestal.

2. Would a local utility be "forced" to wheel power to or from a DOD base under Forrestal?

No. Current federal law prohibits such transactions if they violate the laws and regulations of state and local authorities. The Forrestal legislation preserves current law. In fact, The Forrestal Coalition was asked to support a legislative proposal to change the federal law and force local utilities to wheel power to retail customers. The Coalition declined and DOD agrees with the Coalition's decision.

3. By facilitating both supply and demand-side options, wouldn't Forrestal's activities on DOD facilities result in increased competition for local utilities from "highly-leveraged" cogenerators, EWGs, etc. on bases that could "force" utilities to buy excess power?

DOD says one of its top priorities is to have better relationships with local utilities. This desire is reflected in the legislation, which says that one of the corporation's purposes is "to foster synergistic cooperation among defense energy facilities and neighboring producers and consumers, including local utilities." If the local franchised utility is seeking to acquire new power, Forrestal will recommend in cooperation with the utility that new capacity be designed to fill this need. If, however, the local utility is not seeking additional power and may, in fact, have excess capacity, The Forrestal Corporation will not make such a proposal because it would violate the statutory purpose set forth by Congress in the enabling legislation.

4. If a large number of DOD facilities opt into the Forrestal process, wouldn't that disadvantage certain utilities who have good relationships with military bases in their service territories by placing a new intermediary into the process?

No. The existing relationship between military bases and their utility suppliers that serve them both electricity and gas will remain unaffected. Indeed, proposals by neighboring utilities to acquire utility systems on both closed and surviving bases will be encouraged and transactions will be streamlined.

5. Forrestal would be fuel-neutral in its contracting process, but since many members of the Forrestal Coalition are large gas concerns, wouldn't they have the "inside track" on new projects brought to market by the corporation?

The Forrestal Coalition has electric utility representation in addition to gas utilities, cogenerators, IPPs, ESCOs, investment bankers, etc. Even so, the fact that such companies may be part of the Coalition has no bearing whatever on the corporation's fuel neutral approach. No bidder on any Forrestal contract would be permitted to own any stock or have any say in the operation of the corporation. This ban applies to all companies, whether or not they are part of the Coalition.

Mr. HORN. Well, we thank you. It is a unique idea, and it ought to be studied very carefully.

As is usual in a congressional hearing, I'm going to represent majority, minority, and skeptics generally, and the first question comes up, Mr. Flanagan, why does the Forrestal Corp., which is a private for-profit entity, need to be federally sponsored in enabling legislation?

Mr. DANIEL FLANAGAN. It is very important that the sovereignty issues be maintained. Professor Kettl testified—and actually I cite his testimony at the end of our statement here. He goes on to say—and he testified over in the Senate on privatization issues—“the Government must retain decisions over policymaking. It must also retain the capacity, as the General Accounting Office puts it, to prescribe, monitor, and evaluate the work that others, like contractors, perform on its behalf. The basic principle is this. The executive branch must be accountable for its management of Government programs. To protect the public interest, it must not contract out the Government's sovereign powers or its ability to exercise control over policy.”

He goes on to say later on that he endorses Forrestal as an interesting idea for a mission-specific purpose and suggests that it be applied to this DOD effort on an experimental basis.

Mr. HORN. Do you know of any other models such as this that are for profit and render comparable services?

Mr. DANIEL FLANAGAN. In our infrastructure investment commission report we pointed out a small agency called Connie Lee. We actually searched for such an entity. Connie Lee was created in 1985 with a \$35 million investment, I believe, by the Department of Education to focus on bringing small colleges up to a credit rating through credit enhancement to allow them to borrow in the marketplace where they did not have access. That is a minority investment by Uncle Sam. The other investors were the Pennsylvania Retirement System, AETNA, and now Connie Lee has testified before Congress that it would like to buy back from the Government their equity interest because it has essentially completed its mission and would like to enlarge its scope of activities as a private organization.

Mr. HORN. It is very interesting.

Now if Forrestal is a for-profit company, what incentive does it have to save taxpayer funds and which are really its revenue stream?

Mr. DANIEL FLANAGAN. The only taxpayer funds that come into Forrestal are at its inception. It would be very difficult to raise capital, et cetera, in terms of a plan having to be developed by Forrestal, so there would be an initial \$10 million put in as nonvoting stock by the Department of Defense. As soon as Forrestal is up and running and doing projects on an optional basis as requested by the agencies, there will be sufficient funds to repurchase from DOD, their initial investment.

We also suggest that as a for-profit it will be able to raise capital in the private marketplace a la Connie Lee, and that essentially is how that would work.

Mr. HORN. OK.

Mr. DANIEL FLANAGAN. A savings of course ensues from the involvement of Forrestal. There will be a fee structure in terms of the agencies reimbursing Forrestal for its services, and that fee stream—revenue stream along with the bidders themselves who would make a good faith deposit, which is typical in commercial competitive bidding, that is a nonrefundable deposit as part of a qualification to do business through Forrestal. These will be the various revenue streams that would go through Forrestal.

Mr. HORN. One of Forrestal powers is to sue and be sued. Will the Federal Government be protected from any legal actions directed at Forrestal?

Mr. DANIEL FLANAGAN. That is a good question. Frankly, we haven't looked into that. I was interested in the Bonneville testimony on that.

Mr. HORN. OK. Well, we might want to pursue it. If you have some thoughts, why don't you just file it for the record.

Mr. DANIEL FLANAGAN. Yes, sir.

Mr. HORN. It will be open a while. We will add it at this point.

Some of the proposed functions of Forrestal appear to be inherently governmental. For example, Forrestal will facilitate the development of business and financial plans for energy facilities. It will develop requests for proposals—RFP's—negotiate contracts for private sector companies to construct, upgrade, refurbish, retrofit, and/or operate energy production and consuming facilities.

Has the Office of Management and Budget raised any concerns over the advisability of for-profit corporations performing inherently governmental functions? Have you had a chance to discuss it with them?

Mr. DANIEL FLANAGAN. We have visited with OMB on three separate occasions, and we have been invited there again. They are intrigued by the for-profit taxpaying elements, and, as I mentioned to you earlier, there is an annual report to the Secretary of Defense.

No shareholder in Forrestal can bid on Forrestal sponsored projects and Forrestal would only be involved in the development of a project if requested by the agency. Otherwise it is principally a facilitator conducting the bidding processes, et cetera, for those who would be interested in bidding on projects that come into its purview.

Mr. HORN. Why would Federal employees be detailed to Forrestal? Would the Forrestal Corp. or the Federal Government pay the salaries and benefits of these detailees? And how many DOD employees would be detailed? And what proportion of personnel would be detailed of total Forrestal personnel?

Mr. DANIEL FLANAGAN. At the very beginning in the staffing-up process we make reference in our testimony to this detailing concept. It is something that DOD would be very willing to do, and it would be part of how they would present the project to Forrestal. They have some projects in mind already and people who have been working on them, and they would continue to be employees of DOD, et cetera. But I think it would expedite—there is already work having been done. It is merely getting it to the due diligence window so that private capital and bidders can examine and—what we are talking about is a new window as opposed to the current status quo of the Federal acquisition regs.

DOD would, at their option, place certain projects in Forrestal, and initially until Forrestal is up and running I think their staff—they would put some detailees on those projects.

Mr. HORN. Do you have any inkling as to what proportion of total personnel might be the detailees?

Mr. DANIEL FLANAGAN. Forrestal is going to be a very small organization of experts, so to speak. It is going to be 50, 100, people

officed in one place to service all over the country. It is a leverage of expertise, board of directors, five of which are appointed by the Secretary of Defense, CEO, et cetera. The detailees are really there only at the beginning to get projects moving as soon as possible. Eventually there is a scarcity, as we mention in our testimony, of these kinds of people inside Government, and that is why we need Forrestal. So they are just as anxious as we would be to get Forrestal staffed up with private sector experts in these different areas, project finance, construction, et cetera.

Mr. HORN. As proposed, Forrestal is sort of the middle man for the Federal agencies. How does Forrestal differ from what a consulting firm would do if you called in Arthur Andersen and said, "We have got a problem, what can you tell us about the private venture capital sector, and can we make a deal?"

Mr. DANIEL FLANAGAN. Well, it differs in many ways. One is, it is still subordinate to the Secretary of Defense in terms of its reports and its board makeup, et cetera, which is very important and rhymes with the testimony of Professor Kettl. On the other hand, it can have in house the kind of expertise that consultant firms and so forth normally employ. That expertise will be rewarded in accordance with the success of Forrestal and its shareholders.

But the idea of continuity is very important because these projects are, large in scale, and Forrestal's job is to be a conduit for RFP's, assessments, packaging at the request of the different agencies, and preparing the due diligence information so that the bidders and their lenders can bid on those projects. In a way, Forrestal serves as a consultant body full time to DOD and its subordinate departments.

Mr. HORN. Has anyone looked at the constitutionality or the unconstitutionality of the Secretary of Defense making appointments to the board?

Mr. DANIEL FLANAGAN. We have had some pretty good lawyers working on the legislative drafts, and from my understanding there are precedents for how they laid this out.

Mr. HORN. Are these Government corporation precedents, or do they have besides the Connie Lee example any one of a private corporation where a Government official, under very strict conflict of interest laws, is supposed to appoint part of the board of directors?

Mr. DANIEL FLANAGAN. We will research that, Mr. Chairman.

Mr. HORN. If you could, and file it. It seems to me there are constitutional problems here, but I would be curious what they say. I would be curious if OMB has consulted either with their own general counsel or the Attorney General.

Mr. DANIEL FLANAGAN. We have been relying primarily on counsel ourself in drafting this to answer those kinds of questions, but I will get back to you in writing on that.

Mr. HORN. Very good.

[NOTE.—Due to high printing costs, the above mentioned material may be found in subcommittee files.]

Mr. HORN. Well, let me move to Mr. Robertson, the deputy administrator of Bonneville, and just pursue a few questions for the record. One of them is, how does becoming a Government corporation provide more benefit to the taxpayers than privatization? In other words, do you look at the idea of privatization?

Mr. ROBERTSON. In response to Congressman Tate's question, we have looked at the benefits now to the taxpayers of the present stream of our repayment to the Treasury, and, as I indicated, it is about \$7 billion on a net present value basis. That is to say, if nothing changed, the corporation were to be put in place or in fact if Bonneville's present condition were to stay the same, it would be worth about \$7 billion to the taxpayers in today's dollars.

Given the debt that Bonneville is carrying right now and its fish and wildlife obligations along with other obligations attendant to its mission, it seems unlikely that any private acquisition of Bonneville could benefit the taxpayers beyond the \$7 billion I just described.

Mr. HORN. Let me move to another one here. Some have suggested that the personnel ceilings or caps imposed on Government corporations are not appropriate for an agency whose program is determined by economic and competitive forces. Are the personnel caps imposed by the Federal Workforce Restructuring Act of 1996 impacting Bonneville's operations? If so, how?

Mr. ROBERTSON. They are not particularly, Mr. Chairman. Because of the competitive pressures we have described and, as you point out, it is the market really that is demanding how many employees we can have or not have, and we have cut—plan to cut 1,000 of our employees in the next 1½ years and are well over half-way toward that objective, and we are driving well ahead of any of our projections on the need to cut employees.

Mr. HORN. The Office of Management and Budget and the Department of Energy review Bonneville's budget in a manner similar to that of an appropriated fund agency. That is correct, isn't it?

Mr. ROBERTSON. Yes.

Mr. HORN. This results in the Bonneville Power Administration having two separate budget submissions and maintaining two separate accounting systems, appropriated and accrual. Some think that really doesn't make much sense. How costly is it to maintain duplicative accounting and budgeting schemes, and which one as an operating officer do you think is the most helpful to you in controlling the organization and seeing what results, if any? Is it the accrual system? Is it the accounting for appropriated funds?

Mr. ROBERTSON. Hands down, the most effective management tool in that—with those choices is the accrual method, from my perspective. We devote, I'd say, about 20 full-time equivalents to the management of the two sets of books you have described, at \$70,000 per FTE, roughly \$1.4 to \$2 million per year.

Mr. HORN. And is their time split equally? Are both systems about the same to maintain, or since accrual is what I thought you would say is the best for an operating officer, should we not just go to the accrual system?

Mr. ROBERTSON. We would prefer that, strongly prefer that, because it is more businesslike and we are a function—functionally a business, and so I think my recommendation would be to you that were we to pursue—the administration to pursue the corporation, we should move to that basis.

Mr. HORN. Has that been discussed with OMB? Have they ever raised those questions as to what type of a system you ought to

try? And should they move to that in their presentations to us on the budget as well as just making their own decisions?

Mr. ROBERTSON. Yes, the budgeting process has been discussed at length with OMB in our review. I will say the administration, including OMB, has been responsive to trying to make this corporation, I think, as effective and efficient as possible. They understand the market pressures we are under, and I'm hopeful that as a result of their review now going under way that the administration will come up with something that is the most efficient possible and most effective means by which we can keep track of the books.

Mr. HORN. Now let me say that every Government corporation ought to be represented in the Cabinet by a departmental secretary. In other words, even if it is a Government corporation, it would be grouped in some way under a particular Cabinet department. Would the proposed Bonneville Power Corp. be an independent agency? Would it remain within the Department of Energy? What happens to it?

Mr. ROBERTSON. As a result of the year-long public review process we had with this in the region, the issue of Bonneville's responsiveness and where it sat and who appointed the administrator was a major issue. What was proposed—left on the table at the end of that public process last year was that Bonneville would be created—the corporation would be outside of the Department of Energy, and that gathers us a lot of the efficiencies that we talked about, the \$30 million a year we thought we could save from this, but that the head of Bonneville the administrator and CEO would be appointed by the Secretary of Energy and would report to the Secretary for purposes of national energy policy. So therefore under the construct, Mr. Chairman, just described, the Secretary of Energy would represent Bonneville at the table.

Mr. HORN. Now at one time Bonneville was under the Department of the Interior, wasn't it?

Mr. ROBERTSON. That is correct. When we were first created 50 years ago we were at the Department of the Interior.

Mr. HORN. Does anybody have a feel for how it operated then versus now, and does it matter?

Mr. ROBERTSON. When we were under the Department of the Interior we were a much smaller and more focused agency with a very specific mission to market the power off of the—first Bonneville Dam, then Grand Coulee Dam, and for many, many years we were a transitional agency, our authorities were not permanent.

With the major changes in authority that occurred in 1974 and in 1980 and then beyond that in subsequent years, Bonneville became, as I described earlier, a far more complex organization, and when the Department of Energy was created Bonneville was placed inside the structure of that Department and taken out of Interior.

Mr. HORN. Do you ever have an opportunity to share experiences with utility executives from the private sector?

Mr. ROBERTSON. All the time.

Mr. HORN. Are there any exchanges of personnel between Bonneville and the private sector in terms of the education of your middle management?

Mr. ROBERTSON. Good question. There is constant interplay between our managers and other utility managers through professional groups that we have and also system operational groups.

I was listening with interest to the Forrester Corp. suggestion. There is much experience we have had in both of those areas. And do we actually and physically exchange personnel a lot? That is to say, do we send personnel to private utilities and they send them back to us? No, not much. We do a lot of interchange intellectually and system operationally, but we do not do a lot of that type of operational, functional change.

Mr. HORN. The GSA administrator mentioned in the course of his testimony what I thought was a very good idea, bringing in people to government operations that have a management experience and are used to managing processes, not talking about the end result of do we do good for mankind or whatever, but whatever the agency is organized to do to make sure it is done efficiently, be it the budgeting, be it the legal services, be it the communications, whatever.

So I was curious if there was something we can learn from the private utilities. I remember my reading of history that TVA, Bonneville Power, and comparable operations such as that were really created in the public sector to provide a reasonable price for hydroelectric power to develop the economies of an area that many felt had been underdeveloped and that had been gouged, very frankly, by some of the private utilities, and I wonder if those conditions still exist or the fact that Bonneville is a yardstick, as is TVA, for related private utilities in the region, one can make that argument. You have got competition in what would otherwise be simply utilities by State regulation or others passing on their cost to the consumer, and if you don't like it, tough, consumer, that is the way it is going to be.

Mr. ROBERTSON. Good point. Excellent synopsis of history, I think, Mr. Chairman.

What we have in the Northwest is, I think, a very healthy mix of public and private power. We also have the fact that Bonneville, which basically takes the power of the Columbia River, which is a dominant resource in the region. We integrate with our transmission system private utility power and public power up and down throughout the Northwest and also all the way into California near your congressional district as well, trying to maximize the value of the hydropower system, to minimize air pollution, and maximize its value, and then also maximize the use of other power systems West-wide. So we are very, very experienced with dealing with private utilities.

We specifically created teams of people when we went through our reinvention process, that began about 2 years ago, that ended up in the suggestion of a corporation. We invited teams of utility managers, private and public, to come in and make suggestions to us as part of an overall reinvention. So our utility customers were involved in the changes that Bonneville suggested and in our downsizing suggestions as well and so on. We have a long way to go, but they have been part and parcel in helping us design the change that resulted in our suggestions of a corporation.

Mr. HORN. Do the private utilities that you know about, any throughout the Northwest or anywhere else, for that matter, have the obligation which you have in terms of endangered species, fish, wildlife, et cetera?

Mr. ROBERTSON. Private utilities that have—and publics that have Federal licenses or reviewed by the Federal Energy Regulatory Commission all have specific fish and wildlife responsibilities that relate to the impacts of those hydro plants.

Our responsibility is unlike any I know, frankly, in the country or in the world. We have, as I indicated, about a \$400 to \$500 million, and counting fish and wildlife obligation both for the Endangered Species Act but also to mitigate for the original damage done to the environment by the inundation caused by the dams. So we are paying the—the ratepayers of the Northwest, not the taxpayers, the ratepayers are paying for what has been, I think rightfully, described as the largest fish and wildlife enhancement program in the world. I think our budget at \$400 million is about twice, for example, the entire proposed NMFS national budget for fish and wildlife.

Mr. HORN. In other words, you are paying much more than comparable private power operations are paying, and in a sense you have assumed a governmental service obligation, and, as you suggest, are charging it to the ratepayers of the area. Now in a sense that is going to also make you not too competitive with private power interests.

Mr. ROBERTSON. In years past when we had that 400 percent rate differential we could add costs to Bonneville's base rate and still remain competitive with alternative prices. What has happened in the last 15 years is, our rates have stayed fairly flat and that differential has plummeted because this—gas prices and availability and deregulation, and so we are right at the competitive edge right now, so we cannot add a lot of costs from whatever source beyond what we are already paying for, which is considerable, in these areas. If we do that, we will become uncompetitive in the marketplace. That will leverage itself back potentially on taxpayers, because we have this year-end obligation where we pay back to the taxpayers about \$850 million a year, and if we can't make that payment the taxpayers will suffer.

So we are trying to create flat, stable rates for our customers that are competitive with these alternative rates, cut our own costs, reorganize, get Government corporation type efficiencies so that we can guarantee that flat rate and still meet our fish and wildlife missions, our energy conservation missions, and our missions to provide low-cost benchmark power and integrate the Columbia River to the rest of the region.

Mr. HORN. How many acre feet go out into the Pacific through the Columbia River?

Mr. ROBERTSON. The active storage, U.S. storage, of water is right now 20—in Bonneville system, is 22 million acre feet. That does not include storage in Canada, which is very large as well. Right now we are at the height of the spring runoff and the Columbia is probably moving 250,000 cubic feet of water per second out to the ocean.

Mr. HORN. Yes. Somewhere in my mind 35 years ago sticks the figure 300 million acre feet. Am I just dead wrong on that?

Mr. ROBERTSON. A lot of the—if you talk about the total Columbia River.

Mr. HORN. Right.

Mr. ROBERTSON. It can be that large. There's 300,000 square miles, about the size of the France is the range of the Columbia and Snake Basin. A lot of the water though that comes down the Columbia has been taken out for irrigation purposes, for example, so you start with that, then irrigation occurs, and then what is left is taken through the system, hydropower, shaped for fish and wildlife, and then makes it to the ocean. So I don't think it is 300 million acre feet. It is 300,000 square miles.

I can tell you, the Columbia, as it is moving right now, is one of the most powerful rivers in the world, and it is not completely controlled by anyone.

Mr. HORN. Well, it is a great majestic river.

Coming from Southern California, I'm just looking for 10 million acre feet of water wherever I can find it, and I thought I had it found 30 years ago as a Senate assistant, but there was a Senator who was a great man named Scoop Jackson that prohibited the study. I was curious if that water was still around should we ever have enough votes to get at it.

Mr. ROBERTSON. Thank you for reminding me, Mr. Chairman. I don't think I can talk about it legally.

Mr. HORN. OK. Well, this has been very helpful.

Mr. Flanagan.

Mr. DANIEL FLANAGAN. One quick point, Mr. Chairman.

Mr. HORN. Sure.

Mr. DANIEL FLANAGAN. I should have mentioned earlier that there would be no Government guarantees vis-a-vis Forrestal, no infringements on the full faith and credit. More importantly, the lender, in looking at the project, is going to do the due diligence and determine the viability of the project, which over the long haul will inspire in Wall Street a confidence in Forrestal and their kinds of projects.

I would also like to have our report entered into the record which has to do with a survey of these facilities.

Mr. HORN. It certainly will be.

I think there were also some charts you gave, the first one being DOD energy conservation. All those will be put in the record also as well as the different attachments. You can work that out with staff.

Mr. DANIEL FLANAGAN. Thank you.

Mr. HORN. Now let me get a feel for how this is coming to the Congress. I believe you have got a couple of authors, bipartisan, that are already interested in putting in the bill, aren't they? Or is OMB going to make a recommendation to us?

Mr. DANIEL FLANAGAN. The Department of Defense is the initiator here, and I believe that they are going to ask that this be included in the defense authorization bill this year. There may be Members of Congress that introduce the bill, but that is beyond our control. We are working with the Department of Defense.

Mr. HORN. OK. Well, you have a good army on your side. There's also some armies up here including the Majority Leader.

OK. Thank you very much for coming. We appreciate it, and it has been very helpful.

Mr. HORN. We will have the next panel, and I think we are doing well. We have Mr. Seidman, and then we have Mr. Johnson and Mr. Krasner. They are all there.

Raise your right hand, and we will swear you in.

[Witnesses sworn.]

Mr. HORN. The clerk will note that all affirmed.

We are going to start with Mr. Seidman, a senior fellow of the National Academy of Public Administration, former Assistant Director of BOB, Bureau of the Budget, for management and with a great experience in this area.

Welcome, Harold. It is always good to see you.

STATEMENT OF HAROLD SEIDMAN, SENIOR FELLOW, NATIONAL ACADEMY OF PUBLIC ADMINISTRATION; JACK JOHNSON, PRESIDENT, PROFESSIONAL AIRWAYS SYSTEMS SPECIALISTS; AND BARRY KRASNER, PRESIDENT, NATIONAL AIR TRAFFIC CONTROLLERS ASSOCIATION

Mr. SEIDMAN. It is good to see you, Mr. Chairman.

The hour is growing late. I'll try to summarize this as much as I can. It is a very short statement.

I am pleased to accept your invitation to discuss a number of issues related to Government corporations including mixed ownership Government corporations and Government-sponsored enterprises.

The Government corporation in the United States was a pragmatic response to unique problems posed by the Federal Government's increasing reliance on revenue-producing and potentially self-sustaining enterprises to accomplish public purposes. These enterprises had certain characteristics which distinguished them from programs funded through annual appropriations in that the Government was acting not as a sovereign but a marketer of services. Users rather than the taxpayer were expected to pay the cost of goods and services. Expenditures were driven by the needs of users and could not be estimated accurately in advance. Flexibility was essential to respond to fluctuations in demand, and expenditures to meet increased demand did not necessarily increase the net outlay from the Treasury.

Attempts to operate these enterprises under administrative and control systems designed for traditional agencies prevented them from functioning effectively without providing meaningful accountability. For example, traditional governmental accounting and auditing had the limited purposes of preventing the overobligation of appropriated funds and unlawful expenditures and did not provide the information essential for rate making and evaluating financial results.

The alternative was to exempt corporations completely from existing laws and regulations, with the resulting loss of public control. The Government Corporation Control Act of 1945 provided for business type budget and commercial audit systems which successfully reconciled the need for accountability to the Congress and the

President with the need for operating and financial flexibility in responding to market discipline.

In reporting the legislation, the House Committee on Expenditures and Executive Departments stated: "It has been recognized that Government corporations were created to conduct their activities with a freedom thought to be inconsistent with the types of financial control applicable to regular departments and agencies. Every effort has been made to frame this bill in such a manner as to provide for the financial control without interfering with the required flexibility of operation of the corporations affected. No purpose is served by restrictive limitations which would hinder a corporation in carrying out its statutory program." And after enactment of the Control Act, President Truman in his 1948 budget message prescribed criteria for the use of Government corporations. Accomplishment of a Government corporation was indicated for those programs which were predominantly of a business nature, revenue producing, and potentially self-sustaining and involved a large number of business type transactions with the public.

Experience in both the United States and in most developed countries has demonstrated that Government enterprises cannot function efficiently if subjected to laws and regulations intended for entirely different types of Government activities. For this reason, reports of the National Academy of Public Administration have recommended incorporation of the Bonneville Power Administration, the Federal Aviation Administration as an entity. We did not think it was sound to try to separate the safety functions from the traffic control functions. The report which was done by the Academy proposed that the FAA be established as a corporation comparable to the Tennessee Valley Authority which combines both business type functions and traditional governmental functions, and we proposed also that the Naval Petroleum Reserves the National Technical Information Service, and the Patent and Trademark Office be incorporated.

For some 25 years the provisions of the Government Corporation Control Act and the Truman criteria were consistently applied by the Congress and the executive branch. Since approximately 1970, however, legislation has been enacted and executive actions taken which ignore the established criteria and conflict with the letter and spirit of the Government Corporation Control Act. The situation today resembles that which existed prior to the enactment of the Control Act when the House Committee on Expenditures and Executive Departments found the type and degree of control has varied widely among corporations, often without regard to the real needs of the situation.

To cite some relevant examples, Government corporations have been created which are not revenue producing and potentially self-sustaining and which meet none of the Truman criteria. Government corporations have not been made subject to the Government Corporation Control Act. Wholly owned Government corporations have been improperly classified as mixed ownership Government corporations, thus exempting them from the budget provisions of the Control Act. Government corporations funded directly or indirectly by the Government and directed by Presidential appointees have been defined by law as private or nongovernment. The late

and unlamented Synthetic Fuels Corp. was defined as both an independent Federal entity and not an agency and instrumentality of the United States.

Mixed ownership Government corporations have been replaced by Government-sponsored private enterprises which are not subject to the Control Act. These retain many of the privileges of a Government entity including tax exemption and authority to borrow from the Treasury. I would say the proposed Forrestal Corp. probably would fall into the category of a Government-sponsored private enterprise.

The Control Act required that corporations chartered under the laws of a State or the District of Columbia either be liquidated or rechartered by an act of Congress because it was inappropriate to subject a Federal agency to State or municipal laws. Nonetheless, legislation has been enacted vesting in a corporation all the powers of a private corporation incorporated under the District of Columbia Business Corporation Act.

This year marks the golden anniversary of the Government Corporation Control Act. The basic principles established by the act have withstood the test of time. Amendments are required, however, to take into account significant changes that have occurred during the last 50 years and to eliminate or revise outdated provisions. Legitimate Government corporations need to be protected from laws and regulations inconsistent with the purposes of the act such as limitations on the number of employees and on corporate outlays without regard to the effect on corporate revenues.

The act's provisions now apply only to Government corporations specifically named in the act. Current law should be amended to cover all corporations which meet prescribed criteria. The section on mixed ownership corporations should be deleted in the mixed ownership corporations in which there is no private equity, and the mixed ownership corporations in which there is no private equity invested redesignated as wholly owned. A new section should be added for transitional organizations which are to be privatized and for Government-sponsored enterprises.

A wholly owned Government corporation is a Federal agency and not a quasi-government or a quasi-private institution as sometimes described in the media. The designation of some corporations as private or nongovernment places them in a legal vacuum where neither laws applicable to Federal agencies or to private institutions apply.

I might say again with reference to what I heard of the Forrestal Corp., Mr. Chairman, one of the problems of chartering a corporation by act of Congress is, there is no Federal incorporation law, and if it is a private corporation it exists in almost a legal vacuum, it is not subject to SEC. If it is chartered under State law, the State corporations law apply in a number of provisions that are applicable to those corporations both in review and control and how they are structured and protecting stockholders. If it is chartered by act of Congress, you have none of these controls because there is no Federal incorporation law.

The vesting of public functions in extraconstitutional government institutions which are defined as nongovernment by legislative fiat represents a potential threat to the constitutional powers of the

Congress and the President. In a recent decision, the U.S. Supreme Court held that statutory designation of the National Passenger Railroad Corp. as private could not alter its status as a Federal agency created for a public purpose.

The Government Corporation Control Act is sometimes mistakenly assumed to be the equivalent of a general incorporation law which enumerates the powers and provides for controls applicable to corporations chartered to law. For this reason the 1981 National Academy of Public Administration panel report on Government corporations recommended that as a supplement to the Government Corporation Control Act a new Government enterprise standards law which would prescribe criteria for the use of corporations to define their legal status and vest them with appropriate powers. I strongly urge consideration of such a law which would provide greater consistency in the treatment of revenue-producing and self-sustaining Government enterprises.

Thank you, Mr. Chairman.

[The prepared statement of Mr. Seidman follows:]

PREPARED STATEMENT OF HAROLD SEIDMAN, SENIOR FELLOW, NATIONAL ACADEMY OF PUBLIC ADMINISTRATION

Mr. Chairman and Members of the Committee:

I am, Harold Seidman, a Senior Fellow of the National Academy of Public Administration and the Center for the Study of American Government, Johns Hopkins University. As a government corporation specialist and assistant director for management and organization of the Bureau of the Budget, I was responsible for implementing the Government Corporation Control Act of 1945, and advising the President and the Congress on the organization, management, financing and control of incorporated and unincorporated government enterprises. I have served also as a consultant to the United Nations and several foreign countries on the organization and management of government enterprises.

I am pleased to accept your invitation to discuss a number of issues related to government corporations, including mixed-ownership government corporations and government-sponsored enterprises. My testimony represents my individual views and does not necessarily represent the views of the National Academy of Public Administration as an institution or its Fellows.

The government corporation in the United States was a pragmatic response to the unique problems posed by the federal government's increasing reliance on revenue-producing and potentially self-sustaining enterprises to accomplish public purposes. These enterprises had certain characteristics which distinguished them from programs funded through direct appropriations in that:

- The government was acting not as a sovereign but a marketer of services;
- Users, rather than the taxpayer, were expected to pay the cost of goods and services;
- Expenditures were driven by the needs of users and could not be estimated accurately in advance;
- Flexibility was essential to respond to fluctuations in demand; and
- Expenditures to meet increased demand did not necessarily increase the net outlay from the Treasury.

Attempts to operate these enterprises under administrative and control systems designed for traditional agencies prevented them from functioning effectively without providing meaningful accountability. For example, traditional governmental accounting and auditing had the limited purposes of preventing the over-obligation of appropriated funds and unlawful expenditures, and did not provide the information essential for rate-making and evaluating financial results. The alternative was to exempt corporations completely from existing laws and regulations with a resulting loss of public control.

The Government Corporation Control Act of 1945 provided for business-type budget and commercial audit systems which successfully reconciled the need for accountability to the Congress and the President with the need for operating and financial flexibility in responding to market discipline. The Act was the product of the collaborative effort of the Bureau of the Budget, the General Accounting Office, and the Joint Committee on the Reduction of Non-Essential Federal Expenditures.

In reporting the legislation, the House Committee on Expenditures in the Executive Departments stated: "It has been recognized that government corporations were created to conduct their activities with a freedom thought to be inconsistent with the types of financial control applicable to regular departments and agencies . . . every effort has been made to frame this bill in such a manner as to provide for financial control without interfering with the required flexibility of operation of the corporations affected . . . no purpose is served by restrictive limitations which would hinder a corporation in carrying out its statutory program." (House Report No. 856, 79th Congress, 1st Session)

After enactment of the Control Act, President Harry Truman in his 1948 Budget Message prescribed criteria for the use of government corporations. Establishment of a government corporation was indicated for those programs which were predominantly of a business nature, revenue-producing and potentially self-sustaining, and involved a large number of business-type transactions with the public. These criteria were reaffirmed by the first Hoover Commission in 1949, and the National Academy of Public Administration's 1981 "Report on Government Corporations."

Experience in both the United States and in most developed countries has demonstrated that government enterprises cannot function efficiently if subjected to laws and regulations intended for entirely different types of government activities. For this reason, reports of the National Academy of Public Administration have recommended incorporation of the Bonneville Power Administration, Federal Aviation Administration, as an entity, Naval Petroleum Reserves, National Technical Information Service, and Patent and Trademark Office. We are furnishing for the Committee's information copies of the reports on the Bonneville Power Administration and Naval Petroleum Reserves, which document fully the costs resulting from the necessity of compliance with non-value-added regulations.

For some twenty-five years, the provisions of the Government Corporation Control Act and the Truman criteria were consistently applied by the Congress and the Executive Branch. Since approximately 1970, however, legislation has been enacted and executive actions have been taken which ignore the established criteria and conflict with the letter and spirit of the Government Corporation Control Act. It was at this time that the Office of Management and Budget ceased to maintain staff capable of providing leadership and expert advice with respect to the functioning of government corporations. The situation today resembles that which existed prior to enactment of the Control Act when the House Committee on Expenditures in Executive Departments found: "The type and degree of control has varied widely among the corporations, often without regard to the real needs of the situation."

To cite some relevant examples:

- Government corporations have been created which are not revenue-producing, and potentially self-sustaining, and meet none of the Truman criteria: National Corporation for Community and Public Service, Legal Services Corporation, Oversight Board of the Resolution Trust Corporation (RTC); and U.S. Railway Association.

- Government corporations have not been made subject to the Government corporation Control Act: Legal Services Corporation, Corporation for Public Broadcasting, Oversight Board of the RTC, and Securities Investor Protection Corporation.

- Wholly-owned government corporations have been improperly classified as mixed-ownership government corporations, thus exempting them from the budget provisions of the Control Act: U.S. Railway Association, Resolution Trust Corporation, Federal Deposit Insurance Corporation; and National Railroad Passenger Corporation (AMTRAK).

- Government corporations funded directly or indirectly by the government and directed by presidential appointees have been defined by law as "private" or "non-government." The late and unlamented Synthetic Fuels Corporation was defined as both "an independent federal entity" and "not an agency or instrumentality of the United States." Others include: Oversight Board of the RTC, Legal Services Corporation, Corporation for Public Broadcasting, National Railroad Passenger Corporation; and Securities Investor Protection Corporation.

- Mixed-ownership government corporations have been replaced by government-sponsored private enterprises which are not subject to the Control Act. These retain many of the privileges of a government entity, including tax-exemption and authority to borrow from the Treasury: Federal National Mortgage Association, Federal Home Loan Mortgage Corporation, Student Loan Marketing Association, Federal Agricultural Mortgage Corporation, and Farm Credit Banks.

- The Control Act required that corporations chartered under the laws of a state or the District of Columbia either be liquidated or rechartered by an act

of Congress because it was inappropriate to subject a federal agency to state or municipal laws. Nonetheless, legislation has been enacted vesting in a corporation "all the powers of a private corporation incorporated under the District of Columbia Business Corporation Act," thus making it possible for the District of Columbia to amend a federal law. Examples: U.S. Enrichment Corporation, U.S. Railway Association; and National Passenger Railroad Corporation.

This year marks the golden anniversary of the Government Corporation Control Act. The basic principles established by the Act have withstood the test of time. Amendments are required, however, to take into account significant changes that have occurred during the last fifty years, and to eliminate or revise outdated provisions. Legitimate government corporations need to be protected from laws and regulations inconsistent with the purposes of the Act such as limitations on the number of employees and on corporate outlays without regard to the effect on corporate revenues. The Act's provisions now apply only to government corporations specifically named in the Act. Current law should be amended to cover all corporations which meet prescribed criteria. The section on mixed-ownership corporations should be deleted and mixed-ownership corporations in which there is no private equity investment redesignated as wholly-owned. A new section should be added for transitional corporations which are to be privatized, and for government-sponsored enterprises. Consideration should be given to restoring an annual audit by the General Accounting Office. The Chief Financial Officers Act vested the audit function in a corporation's inspector general or in an external auditor, as determined by the inspector general.

A wholly-owned government corporation is a federal agency and not a quasi-government or quasi-private institution as sometimes described in the media. The designation of some corporations as "private" or "non-government" places them in a legal vacuum where neither laws applicable to federal agencies or to private institutions apply. Questions have been raised as to the applicability of constitutional restraints to these corporations. The vesting of public functions in extra-constitutional government institutions, which are defined as non-government by legislative fiat, represents a potential threat to the constitutional powers of the Congress and the President. In a recent decision, the U.S. Supreme Court held that statutory designation of the National Passenger Railroad Corporation as "private" could not alter its status as a federal agency created for a public purpose. (*Michael A. Lebron v. National Passenger Railroad Corporation*, February 21, 1995).

The Government Corporation Control Act is sometimes mistakenly assumed to be the equivalent of a general incorporation law which enumerates the powers and provides for the controls applicable to corporations chartered under the law. For this reason, the 1981 National Academy of Public Administration panel report on government corporations recommended, as a supplement to the Government Corporation Control Act, a new government enterprises standards law, which would prescribe criteria for the use of corporations, define their legal status, and vest them with appropriate powers. I strongly urge consideration of such a law which would provide greater consistency in the treatment of revenue-producing and self-sustaining government enterprises.

Mr. HORN. Thank you very much.

We now turn to representatives of both the National Air Traffic Controllers Association and the Professional Airways Systems Specialists.

I believe Mr. Krasner, Barry Krasner, the president of the National Air Traffic Controllers Association, will give the primary testimony, and he is accompanied by Jack Johnson, the president of the Professional Airways Systems Specialists.

Mr. Krasner.

Mr. KRASNER. Good afternoon, Mr. Chairman.

As you may be aware NATCA, National Air Traffic Controllers Association, represents the Nation's 15,231 air traffic controllers. These men and women toil 24 hours a day, 7 days a week, 365 days a year to ensure that our system remains the safest, most efficient in the world.

PASS represents over 10,000 FAA technical and aviation systems specialists who support and sustain the safest and most efficient national air space system. The AF system specialists install, repair,

maintain, operate, and certify the entire realm of electronic, electromechanical, and environmental systems used in air traffic control. The aviation safety inspectors oversee and inspect every aspect of the commercial and general aviation industry while the AVN specialists maintain the national air space system through flight inspection.

The United States is proud to have the safest, most efficient ATC system in the world. However, the cracks in the system are starting to show, and if we intend to maintain our leadership status meaningful reform of the FAA is a must. Now within the aviation community, in the halls of Congress, and throughout the FAA there is great debate as to how this reform should occur.

The administration has had legislation introduced to restructure ATC as a Government corporation fully supported by user fees. Others in Congress have introduced less drastic measures that would reform FAA as an independent Government agency, and now the current budget crisis has forced the suggestion from the Senate Budget Committee that ATC be fully privatized.

There still remains much disparity within the aviation community as to how this reform should be accomplished, but the one thing that all agree on is that privatization is not the answer. Whatever is to happen though should happen sooner rather than later. Protracted debate over reform, impending pay cuts, proposed pension cuts, and increased pension costs have left a cloud of gloom over the agency, and employees are starting to feel the heat. The administration and Congress are in the process of creating a demoralized work force. Clearly a safety-sensitive agency like the FAA is the last place anyone would like to see that demoralized work force.

To varying degrees NATCA and PASS are on record as supporting the administration's corporation plan. Although we don't agree with the entire proposal, we find it to be the most comprehensive in the three major areas that are in dire need of overhaul—personnel, procurement, and funding. Both of our organizations stand in solid opposition to a private corporation for ATC. We believe that air traffic control and aviation safety are inherent Government functions, and we contend that continued Government ownership is a must.

We are very familiar with private enterprise infringing on public service areas. For instance, the formal training of air traffic controllers is accomplished in a privatized environment. Thankfully, we still have a very energetic and meaningful on-the-job training program that picks up the ball where the privatized formal training area drops it. Additionally, low density air traffic control towers are contracted out to private ATC companies, and what we are seeing more and more is that they do not provide the same caliber of service that is currently offered in the Federal system.

Similarly, Jack's AF work force has suffered even greater devastation as a result of privatization. In 1981 there were 11,600 system specialists to maintain 19,000 facilities. Today, there are only 6,000 specialists maintaining 31,000 facilities. To partially augment this dramatic shortage, the FAA employs 2,000 contract employees, and, much to the chagrin of the users of the system, the contractors do not provide the same quality of service that was ear-

lier performed by the Government employees that they replaced, yet the cost to the American taxpayer is considerably more.

Mr. Chairman, we fully understand the budget pressure that seems to be driving the concept of a private ATC corporation. However, prior to considering this drastic step two questions must be answered. One, can a private ATC system provide better and/or safer services? And, two, are the budget savings worth the risk? Both NATCA and PASS would contend that the answer is no.

The privatization of our ATC is a bad idea. A private ATC system would, for one, make safety answerable to the bottom line; it would double the tax on systems users; it would force general aviation out of the system, creating an insurmountable safety problem; and would provide air traffic controllers and other corporation employees the right to strike.

As I mentioned earlier, both NATCA and PASS support the concept of a Government-owned corporation because it goes along with our shared belief that meaningful reform must occur in personnel, funding, and procurement. Moreover, we believe that the ongoing budget crisis hampers the FAA's safety mission.

Today too few air traffic controllers continue to handle too much traffic. The system has fewer controllers now than we had in 1981 yet since 1981 traffic has increased by 30 percent and we are forced to work 1995 air traffic with 1960 technology. Likewise, staffing levels within PASS's AF organization have fallen disastrously low. Additionally, over 50 percent of today's work force is eligible to retire and more than likely will if the budget suggested Federal retirement changes occur.

The air traffic control system reformed as a fully user funded Government corporation would be free from the current national budget crisis, thus allowing corporate management and its unions to develop more flexible personnel and procurement systems. NATCA and PASS believe that adequate staffing allotments along with a wise technology acquisition program will enhance the safety envelope of our Nation's air traffic control system, and we don't believe these items are present in today's system.

Finally, Mr. Chairman, I would be remiss if I didn't warn you of impending trouble within our agency as it exists today. As you know, the House recently passed its budget resolution. In that resolution certain savings are realized by increasing Federal employees' contributions to the retirement, changing the formula for setting a retiree's annuity, and by eliminating the Air Traffic Revitalization Act which would amount to a 5 percent pay cut to air traffic controllers and systems specialists.

I have to ask, is this the way to reward a group of employees, who have always performed at or above 125 percent? We have to remember that air traffic controllers are working 30 percent more traffic than they were in 1981 with 1,500 fewer controllers. System specialists are maintaining 12,000 more facilities than they were in 1981 with 5,600 fewer specialists. Certainly these two groups of employees are among the most productive in or out of Government, yet the Government appears to be turning its back on them.

We fear that the proposed cuts will force eligible employees to retire as soon as possible, will make other employees seriously consider less stressful occupations, and make it difficult, if not impos-

sible, to attract high caliber individuals to these important occupations. I mentioned earlier that 50 percent of the AF work force is eligible to retire. I also need to tell you that over 2,200 of the controller work force is eligible to retire. Consequently, the American flying public would be left with a demoralized work force.

We are proud to represent these men and women who do everything humanly possible to protect the safety of the skies. We hope that you too will recognize the crucial role that our work force has played in the aviation industry.

Again, Mr. Chairman, on behalf of both our organizations we thank you for the opportunity to appear before you and we would be happy to answer any questions you have.

[The prepared statement of Mr. Krasner and Mr. Jack Johnson follows:]

PREPARED STATEMENT OF BARRY KRASNER, PRESIDENT, NATIONAL AIR TRAFFIC CONTROLLERS ASSOCIATION; AND JACK JOHNSON, PRESIDENT, PROFESSIONAL AIRWAYS SYSTEMS SPECIALISTS

Mr. Chairman and Members of the Subcommittee:

Good afternoon. My name is Barry Krasner and I am President of the National Air Traffic Controllers Association (NATCA). Joining me today is Jack Johnson, President of the Professional Airways Systems Specialists (PASS). My organization, NATCA, represents this nation's 15,231 Air Traffic Controllers. These dedicated men and women toil 24 hours per day, 7 days per week, 365 days per year to ensure that our air traffic control system remains the safest and most efficient system in the world. Meanwhile, Mr. Johnson's organization, PASS, represents over 10,000 FAA employees in three separate bargaining units. These units are: Airway Facilities; Flight Standards; and the Office of Aviation Standards. This diverse group of professional employees includes Systems Specialists, Aviation Safety Inspectors and Pilots/Procedures Specialists. They are committed to maintaining our position as world leaders in the aviation safety arena.

As you know, the U.S. is proud to have the safest and most efficient air traffic control system in the world today. However, the cracks in the system are now starting to show, and if this nation intends to maintain its leadership status in the aviation arena, meaningful reform of the Federal Aviation Administration (FAA) is a must. It is with great admiration that we thank you for having these most important hearings, and we appreciate the opportunity to appear before you today to discuss corporate structures for the FAA, both private and government-owned.

Within the aviation community, in the halls of Congress and throughout the FAA, there is much debate as to how FAA reform should be accomplished. As you know, the Clinton Administration has introduced legislation to establish a government-owned air traffic control corporation, fully supported by user-fees. Others, including Congressmen James Oberstar (D-MN) and Jim Lightfoot (R-IA), prefer a less-dramatic approach and have suggested removing the FAA from the Department of Transportation, restructuring it as an independent agency.

During the current budget cycle, a suggestion has been made by the Senate Budget Committee to fully privatize the air traffic control system. Given all of the options for reforming the FAA, there is some disparity within the aviation community as to how the reform should be undertaken. The one thing that the entire aviation community agrees on, however, is that privatization is not the answer.

With regard to FAA reform, whatever is to happen should happen sooner rather than later. Massive restructuring, pay cuts, pension cuts and increased pension costs have left a cloud over the agency and employees are starting to feel the heat. The Administration and Congress are in the process of creating a demoralized work force. Clearly, a safety sensitive agency is the last place anyone would like to see a demoralized work force.

To varying degrees, NATCA and PASS have gone on record as supporting the Administration's corporatization plan. Although we do not fully agree with the entire proposal, we find it to be the most comprehensive in the three major areas that are most in need of overhaul—personnel, procurement and funding. Whatever form the restructuring of the FAA takes, both NATCA and PASS remain ready, willing and able to assist in the development of an appropriate structure. The key to the successful revamping of the FAA or of the ATC system will be management's willing-

ness to utilize its already established cooperative processes. This will assure that the best product is developed and will go a long way toward gaining employee trust.

Both NATCA and PASS agree that we are absolutely opposed to a private corporation for air traffic control. We believe that air traffic control and aviation safety are inherent governmental functions, and we contend that continued government ownership is a must. Excellent public services are vital to the public good and to the quality of community life. The key to excellent public services is meaningful citizen and public employee involvement.

The recent tragedy in Oklahoma City has driven home the fact that public employees are on the front lines of service delivery every day. They have demonstrated their commitment to improving the quality of community life and are well situated to use their expertise to assist in the design of more efficient ways to deliver public services. Government, by selling itself to private enterprise, is destroying the integrity of public employment and the quality of public service.

Both of our organizations are very familiar with private enterprise infringing on public service areas. The formal training of Air Traffic Controllers is accomplished in a "privatized" environment. Thankfully, we still have a very energetic and meaningful on-the-job training (OJT) program that picks up the ball that is dropped in the more formal training arena. Low density air traffic control towers are contracted-out to private air traffic control companies. Unfortunately, they do not provide the same caliber of services that is currently offered in the federal system.

Similarly, Jack's AF work force has suffered even greater devastation as a result of privatization. In 1981 there were 11,600 AF Systems Specialists to maintain 19,000 facilities. Today, there are only 6,000 Systems Specialists maintaining 31,000 facilities. To augment this dramatic shortage, the FAA employs 2,000 contract employees. Much to the chagrin of the users of the system, contractors do not provide the same quality of work that was earlier performed by the government employees that they replaced; yet, the cost to the American taxpayer is considerably more.

We fully understand the budget pressure that seems to be driving the concept of a private air traffic control corporation. However, prior to considering this drastic leap, two questions must be answered. Can a private ATC system provide better and/or safer services? Are the budget savings worth the risk? Both NATCA and PASS believe that the answer to both of these pivotal questions is a resounding NO.

The privatizing of our ATC system is a BAD idea! A private corporation, either for-profit or not-for-profit, will make SAFETY answerable to the bottom line. Today, Air Traffic Controllers and Systems Specialists always place safety ahead of efficiency. In a private corporation—especially one in which the controlling Board of Directors is largely composed of airline executives—we could be forced to reverse these long held priorities.

As we understand from the Senate Budget Resolution, airline passengers and other users of the system would continue to contribute, at current levels, to the Aviation Trust Fund. The Aviation Trust Fund would remain within government, forcing the private corporation to develop its own user-fees, on top of the contribution to the trust fund. This funding mechanism of the private corporation also greatly concerns NATCA and PASS. We fear a pricing policy that would either squeeze general aviation out of the system or that would make it advantageous for them to forego air traffic services. To many, this is an economic issue—to us, it is a very real safety issue.

Before I conclude our comments on a private corporation, I would like to mention one issue that gives many cause for concern. Under a private corporation, employees have the right to strike. NATCA and PASS would expect all organized employees in the private corporation to retain this right. We understand that the Department of Defense and many airline executives have already voiced concern over this issue. While we may be willing to forego the right to strike in exchange for binding arbitration in a government-owned corporate structure, we would not be willing to accept that exchange in a private corporation.

Both NATCA and PASS support the concept of a government-owned corporation because it goes along with our shared belief that meaningful reform must occur in the personnel, funding and procurement fields. Moreover, we believe that the ongoing budget crisis hampers the FAA's safety mission.

Today, too few Air Traffic Controllers continue to be asked to manage too much air traffic. We have fewer Air Traffic Controllers now than we had at the time of the disastrous PATCO strike of 1981; yet, since 1981, traffic has increased by 30%. Of course, we are told that a technology revolution will occur in ATC and we'll be able to manage with fewer controllers. Unfortunately, that revolution has not occurred, and we are being forced to work 1995 air traffic with 1960 technology.

Likewise, as I mentioned earlier, staffing levels within PASS' Airway Facilities organization have fallen disastrously low. Additionally, over 50% of today's Systems

Specialists work force is eligible to retire. Already, the consequences of understaffing are being seen, as is evidenced by the increased number of delays and outages. Obviously, staffing is crucial and will play a decisive role in how the FAA meets its current and future aviation needs.

The air traffic control system, reformed as a government corporation, would be free from the current national budget crisis, thus allowing the corporation management and its unions to develop a more flexible personnel system and a more flexible procurement process. NATCA and PASS believe that adequate and stable staffing allotments, along with a wise technology acquisition program, will enhance the safety envelope for our nation's air traffic control system. Unfortunately, as I said, these items are not present in today's system.

Earlier, I mentioned that NATCA and PASS differ somewhat in our appreciation of the plan for a government-owned air traffic control corporation envisioned by the Clinton Administration. Because PASS will represent employees within the residual FAA and the new government corporation, they are very concerned with the disparate treatment of the two groups and rightfully question how the residual FAA and the new government corporation will interact. The important issue of how the residual FAA bureaucracy will interface with the newly created corporate bureaucracy has yet to be addressed.

Whether the FAA is reformed as a government-owned corporation or as an independent agency, PASS maintains that a well-planned strategy for internal reform will revamp the FAA into an agency that will be able to provide better services to our users, the flying public. Our position at NATCA is, if it is not possible to make the bold move to a government-owned corporation, then we should follow the lead of PASS and make the best independent agency possible.

Mr. Chairman and Members of the Subcommittee, I would be remiss if I did not warn you of impending trouble in our agency. As you know, the House recently passed its Budget Resolution. In that Resolution, certain savings are realized by increasing federal employee contributions to their retirement; by changing the formula for setting a retiree's annuity from high-three to high-five; and by eliminating the Air Traffic Control Revitalization Act which would amount to a 5% pay cut for Air Traffic Controllers and Systems Specialists. I ask you, "Is this the way you reward a group of employees who have always performed at 125%?" Please remember, Air Traffic Controllers are working 30% more traffic today than they were in 1981 with 1500 fewer Controllers and without additional technology. Systems Specialists are maintaining 12,000 more facilities than they were in 1981 with 5,600 fewer Specialists. Certainly, these two groups of employees are among the most productive in or out of government. Yet, the government is turning its back on them.

NATCA and PASS fear that the proposed cuts will force eligible employees to retire as soon as possible; will make other employees seriously consider less stressful occupations; and will make it difficult to attract high caliber individuals to these most important professions. Consequently, the American flying public will be left with a demoralized work force. NATCA and PASS are proud to represent the dedicated men and women who do everything humanly possible to protect the safety of the flying skies. We hope that you too will recognize the crucial role that our work forces play in air traffic control.

Thank you for allowing us to testify. Jack and I would be happy to answer any questions that you might have.

Mr. HORN. Thank you.

Is there anything you want to add, Mr. Johnson, at this point?

Mr. JACK JOHNSON. No, sir. Thank you. I think that Barry summed up our remarks quite well.

Mr. HORN. Very good.

Let me ask a few questions of Mr. Seidman.

There are a number of proposals to create new government corporations. And this is one of them that you have just heard about. With the decline in management staff at OMB which are exercising oversight over these prolific entities, you have criticized a number of these proposals. Do you have any advice as to how Congress and the administration can exercise better oversight regarding the creation of government corporations? Is it self-restraint? Is it more staff we need that have the background and experience you have?

Mr. SEIDMAN. I think it takes some staff. I think the situation has changed from when I started to administer the Government Corporation Control Act. There was a special Subcommittee on Government Corporations of the House Appropriations Committee who had expertise, there was a Government corporations audit division in GAO, and you had the small staff which I had. It was never more than two people who kept track of Government corporations, who knew they were different, who would read a financial statement, which is one thing most budget examiners can't do. That isn't the way you do a budget. You change the numbers, you don't read financial statements, look at depreciation.

I think part of it is the decline in the management side in OMB, and a number of us feel that the time has come to set up an office—separate office of Federal management.

Under present circumstances the way OMB is organized—and, unfortunately, I was pulled off of the grand jury to do the reorganization plan that put the M in OMB, and it has not turned out that way. The M has been subordinated to the budget and the assumption that you need the clout of the budget to do the management job is just a misconception.

I never, ever, when I was assistant director, was in a position of saying if you don't do what we are recommending we are going to get you 18 months from now in the budget. I think you provide leadership, you provide incentives, you don't use clout to get management improvement.

But there is no place. It was in the early 1970's that the last person in the OMB who took any interest in Government corporations disappeared. I gather they are trying now to regroup it. In our current dealings with OMB, I get as many different positions on Government corporation as their resource divisions, and they are not compatible with each other. The deputy for management is trying, I understand, to develop a coherent position, but they do not have one at the moment.

So I would say it takes a very small staff of a couple of knowledgeable people at the executive office level and development, some staff at the appropriate committee level who understand how a business operates.

Mr. HORN. Some people look at government corporations and see that they have few attributes that are similar to those in private corporations, and they assume from that that government corporations are simply an intermediate step toward full privatization. Is that a correct characterization?

Mr. SEIDMAN. That is not a correct characterization at all. It is for some. In fact, in our proposed Government Enterprises Standards Act we would replace the mixed ownership category with a new one which we would call the transitional corporations. We have one which we were involved with. The U.S. Enrichment Corp. is one that it is intended to demonstrate its capacity to become private. We recommended a corporation for the Naval Petroleum Reserves for the identical reason, because until it operates as a business there is no way the Government can develop what a fair price should be for a Naval Petroleum Reserve.

Mr. HORN. Let me explore the issue of accountability on the part of government corporations. Does the lack of annual appropriations

as a regular, ongoing means of reviewing funding levels and policy goals lead to oversight problems with Government corporations?

Mr. SEIDMAN. It does not, because the annual appropriation process is meaningless when applied to an enterprise which is operating out of its revenues, and in fact it is self-destructive. The Government—that was the whole purpose of the Government Corporation Control Act, provided for a business type budget which provided there would be annual review by the Office of Management and Budget, the President, and the Congress, of those things which are important, of the program, of those things which really could affect the potential cost to the Government, and in that process they do not appropriate money. What the Congress does is approve the expenditure of the available resources of the corporation for the programs approved by the Congress. If the review is done right, it is effectively accountability. The annual appropriation process provides no accountability whatsoever when applied to a business type enterprise which is operating out of its own revenues.

Mr. HORN. Well, you might well have answered the next question, but let me go through it and get it on the record.

Before a government corporation issues obligations to the public, the Secretary of the Treasury must prescribe the form, the denomination the maturity, conditions of sale. Further, the Secretary of the Treasury must approve a purchase or sale of any direct obligation of the United States on which the principal or interest exceeds \$100,000. Have these requirements proven workable both in terms of allowing Government corporations access to capital and ensuring that public funds are protected?

Mr. SEIDMAN. They have, and although some of that language is slightly obsolete, I think debt management is very critically important, because if you have Government corporations going into the market without coordination with the Treasury they can affect the interest rates on U.S. Government obligations.

Since then, we have had created the Federal Financing Bank, which basically is the funding agency for most of the Government corporations which borrow for the Treasury or from the Federal Financing Bank. Some, such as TVA, issue their own obligations directly to the public. I think that is also true of the Enrichment Corp. They pay a slightly higher interest rate on their obligations than they would if they were issued through the Treasury or through the Federal Financing Bank, but we have been successful in coordinating the financial activities of the corporations with the Treasury debt management activities.

Mr. HORN. You happened to mention the Truman criteria in 1948, and I thought as I read that, that is probably the Seidman criteria. Is that true?

Mr. SEIDMAN. That is correct.

Mr. HORN. I thought so. Well, that's quite a day to celebrate around here. We will look to 1998 and have a golden anniversary on it.

But I was trying to remember the great line Adlai Stevenson had when he gave his speech in the early fifties and he said that, "This hasn't been said to this group since it was said by Secretary so-and-so," and he said, "I happened to write that speech also." But I thought those criteria might be yours.

Mr. SEIDMAN. Well, they were endorsed by the President and were accepted by the Congress, and they remained in force and effect more than 30 odd years.

Mr. HORN. Reflecting back to 1948 are there any criteria you would add to that list now that you have seen it in operation?

Mr. SEIDMAN. I think one thing I would change, because when we see it in the Patent and Trademark Office is that it doesn't have to be commercial in the traditional sense. It is meant for programs that are intended to be revenue producing and potentially self-sustaining enterprises. The European Patent Office does describe itself as a business, I think the issuing and granting of patents does not really fit quite the category that you would normally call a commercial enterprise.

But, on the other hand, the case for the Patent Office being a Government corporation is an exceedingly strong one since it has now been not only put on a 100 percent self-sustaining basis. Unfortunately, those who apply for patents are also contributing to the general tax revenues since it goes into a surcharge fund which is supposed to be reappropriated to the Patent Office but is not. It is now \$57 million.

Mr. HORN. And their budget is what?

Mr. SEIDMAN. It is about \$100 million, but \$57 million that they have, their rates—these cover all their operations, and then the Congress incurred a surcharge where the money goes into a surcharge fund, where it is supposed to be earmarked for reappropriation to the Patent Office but has not been reappropriated, and the amount of money in that fund at the present time is \$57 million.

Mr. HORN. Interesting.

Well, if you think of some criteria you would like to add, we will keep the record open, and just supply us with it.

Can you supply us with a copy of the draft Government Enterprise Standards Act which you mention in your testimony? Or we can get it? But give us the rough citation.

Mr. SEIDMAN. I think we have a draft. We have done it at the request of staff of the Senate Governmental Affairs Committee. We have shown it to them. I asked one of the staff. I said they will probably ask for it. Any objection? I said no. We will be very happy to supply it, and we would like to see it. I think it is badly needed for a lot of the reasons, and I think, Mr. Chairman, you may find it of some interest. We will be very happy to supply it for you.

Mr. HORN. Good. Maybe we can get a joint effort going over here.

[The draft follows:]

DRAFT
June 12, 1995

A BILL

To Promote The Capacity And Accountability Of Government Corporations And Government Sponsored Enterprises

Be it enacted by the Senate and House of Representatives of the United States of America in Congress Assembled, that this Act may be cited as the "Government Corporation and Government Sponsored Enterprise Standards Act."

Title I. Purposes; Definitions; Classifications

Sec. 101. Purposes—

The purposes of this Act are to assure that government corporations and government sponsored enterprises are established and conduct their operations in conformance with consistent standards as to the applicability of Federal laws and are fully accountable for their financial soundness and programmatic activities, and further to provide an orderly process for privatizing selected government corporations.

Sec. 102. Definitions—

for the purposes of this Act:

(a) **"Government Corporation"**—Means an agency of the United States within the Executive Branch that (1) is designated by law to have corporate form; (2) carries out business type operations to provide goods or services in response to economic demand; and (3) produces revenues, potentially on a self-sustaining basis.

(b) **"Government Sponsored Enterprise" or "GSE"**—Means an instrumental-ity chartered under the laws of the United States to provide specialized financial services in furtherance of public purposes and that (1) is owned wholly or in part by private equity owners; and (2) has ties to the federal government, such as authority to borrow directly or indirectly from the Treasury of the United States, that create a perception of implicit federal backing of its obligations or-guaranteed securities.

(c) **"Newly Established Wholly Owned Government Corporation"**—Means a Wholly Owned Government Corporation which is established pursuant to any law enacted after December 31, 1994.

(d) **"Newly Established Transitional Government Corporation"**—Means a Transitional Government Corporation which is established pursuant to any law enacted after December 31, 1994.

(e) **"Newly Established Government Sponsored Enterprise"**—Means a Government Sponsored Enterprise which is established pursuant to any law enacted after December 31, 1994.

(f) **"Transitional Government Corporation"**—Means a Government Corporation which is intended to operate on a profitmaking basis and to be converted to private ownership when feasible.

(g) **"Wholly Owned Government Corporation"**—Means a Government Corporation that is wholly owned or controlled by the Federal Government. A Transitional Government Corporation shall be considered a Wholly Owned Government Corporation for purposes of this Act except as otherwise provided by law.

Sec. 103. Classification—

The Director of the Office of Management and Budget shall maintain a current list of all Government Corporations and Government Sponsored Enterprises classified according to the definitions of this Act and shall publish such list as a part of the annual budget of the United States Government. The Director of the Office of Management and Budget shall make recommendations to the Congress as to changes in law that would be appropriate to assure that the provisions of this Act apply to entities established under laws that are enacted or amended after December 31, 1994.

Title II. General Provisions

Sec. 201. Reservation—

The Congress expressly reserves the right to alter, amend or repeal any law establishing or governing the activities of a Government Corporation or Government Sponsored Enterprise.

Sec. 202. Affiliates—

Each Newly Established Government Corporation or Newly Established Government Sponsored Enterprise may establish, acquire or control the activities of a subsidiary or other affiliate only by or under a law of the United States expressly authorizing the action.

Sec. 203. Application of this Act—

After the effective date of this Act no entity established under federal law shall be a government corporation or government sponsored enterprise without meeting the requirements and conforming to the definitions of this Act.

Title III Wholly Owned Government Corporations

Sec. 301. Applicability—

This title applies only to Newly Established Wholly Owned Government Corporations.

Sec. 302. Government Corporation Control Act—

Each Wholly Owned Government Corporation shall be subject to the provisions of the Government Corporation Control Act, chapter 91 of title 31, United States Code, that are applicable to wholly owned Government corporations under that act.

Sec. 303. Sunset—

Each Wholly Owned Government Corporation shall have succession for a period of ten years from the date of enactment of its enabling legislation, subject to review by the Congress and extension for additional periods of ten years, unless otherwise provided by law.

Sec. 304. General Powers—

In order to accomplish its statutory purposes and in addition to any other powers that may be authorized by law, each Wholly Owned Government Corporation:

- (a) may adopt, alter, and use a corporate seal, which shall be judicially noticed;
- (b) may sue and be sued in its corporate name and be represented by its own attorneys in all administrative and judicial proceedings, including, with the prior approval of the Attorney General, appeals from decisions of federal courts;
- (c) may indemnify directors, officers, attorneys, agents and employees of the corporation for liabilities and expenses incurred in connection with their corporate activities;
- (d) may adopt, amend, and repeal bylaws, rules, and regulations governing the manner in which its business may be conducted and the powers granted to it by law may be exercised and enjoyed;
- (e) may determine the rates or prices of goods or services that it provides, subject to applicable provisions of law;
- (f) (1) may acquire, purchase, lease, and hold real and personal property including patents and proprietary data, as it deems necessary in the transaction of its business, and sell, lease, grant, and dispose of such real and personal property, as it deems necessary to effectuate the purposes of this Act;
- (2) shall make purchases, contracts for the construction, maintenance, or management and operation of facilities and contracts for supplies or services, except personal services, after advertising, in such manner and at such times sufficiently in advance of opening bids, as the corporation shall determine to be adequate to insure notice and an opportunity for competition: Provided, that advertising shall not be required when the corporation determines that the making of any such purchase or contract without advertising is necessary in the interest of furthering the purposes of this Act, or that advertising is not reasonably practicable;
- (g) with the consent of the agency or government concerned, may utilize or employ the services, records, facilities or personnel of any State or local government agency or instrumentality, or voluntary or uncompensated personnel to perform such functions on its behalf as may appear desirable;
- (h) may enter into and perform such contracts, leases, cooperative agreements, or other transactions as may be necessary in the conduct of its business on a reimbursable basis, with any agency or instrumentality of the United States, or with any State, territory or possession, or with any political subdivision thereof, or with any person, firm, association, or corporation;
- (i) may determine the character of and the necessity for its obligations and expenditures and the manner in which they shall be incurred, allowed, and paid, subject to the provisions of this Act and other provisions of law specifically applicable to wholly owned government corporations;
- (j) may retain and utilize its revenues for any of the purposes of the corporation, including research and development and capital investment. Corporate funds shall not be subject to apportionment under the provisions of subchapter II of Chapter 15 of Title 31, United States Code;
- (k) may settle and adjust claims held by the corporation against other persons or parties and claims by other persons or parties against the corporations; provided however, that, for purposes of the Contract Disputes Act of 1978, the corporation shall be deemed to be the agency head with respect to contract claims arising with respect to the corporation;
- (l) may exercise, in the name of the United States, the power of eminent domain for the furtherance of the official purposes of the corporation;

(m) shall have the priority of the United States with respect to the payment of debts out of bankrupt, insolvent, and decedents' estates;

(n) may define appropriate information as "Government Commercial Information" and exempt such information from mandatory release pursuant to section 552 (b) (3) of Title 5, United States Code, when it is determined by the corporation that such information if publicly released would harm the corporation's legitimate commercial interests or those of a third party;

(o) may obtain from the Administrator of General Services such services as he or she is authorized to provide to agencies of the United States, on the same basis as those services are provided to other agencies of the United States;

(p) may accept gifts or donations of services, or of property, real, personal, mixed, tangible or intangible, in aid of any purposes herein authorized;

(q) may execute, in accordance with its bylaws, rules and regulations, all instruments necessary and appropriate in the exercise of any of its powers;

(r) may provide for liability insurance either by contract or by self-insurance; and

(s) shall pay any settlement or judgment entered against it from the corporation's own funds and not from the judgment fund (31 U.S.C. Section 1304). The provisions of the Federal Tort Claims Act (28 U.S.C. Sections 1346(b) and 2671 et seq.) shall not apply to any claims arising from the activities of the corporation.

Sec. 305. Officers and Employees—

Officers and employees of a Wholly Owned Government Corporation shall be officers and employees of the United States. The corporation shall appoint and fix the compensation of such officers and employees (including attorneys) and agents of the corporation as are deemed necessary to effect the provisions of this Act, define their authority and duties, and delegate to them such of the powers vested in the corporation as the corporation may decide, without regard to any administratively imposed limits on the number or grade of personnel, and any such officer, employee or agent shall be subject to the supervision only of the corporation.

Sec. 306. Obligations and Guarantees—

The full faith and credit of the United States is pledged to the payment of all obligations issued or guaranteed by each Wholly Owned Government Corporation.

Sec. 307. Contributions to Retirement and Disability and Employees' Compensation Funds—

Each Wholly Owned corporation shall contribute to the civil service retirement and disability fund, on the basis of annual billings as determined by the Office of Personnel Management, for the Government's share of the cost of the civil service retirement system applicable to the corporation's employees and their beneficiaries. The corporation shall also contribute to the employees' compensation fund, on the basis of annual billings as determined by the Secretary of Labor, for the benefit payments made from such fund on account of the corporation's employees. The annual billings shall also include a statement of the fair portion of the cost of administration of the respective funds, which shall be paid into the Treasury as miscellaneous receipts.

Sec. 308. Financial Statements—

Each Wholly Owned Government Corporation shall maintain a system of accounts and publish its financial statements annually on the basis of generally accepted accounting principles and shall be subject to audit on the basis of auditing standards that are consistent with the private sector's generally accepted commercial auditing standards, except as otherwise provided by law.

Sec. 309. New Activities—

No Wholly Owned Government Corporation shall engage in new types of business activities before such activities are included in the annual budget program that is approved by the Congress.

Sec. 310. Revenues Foregone—

There are authorized to be appropriated to each Wholly Owned Government Corporation each year such sums as are determined by the corporation to be equal to revenues foregone by the corporation as a result of the operation of laws that direct the corporation, for reasons of national policy to provide goods or services at prices or rates below a reasonable estimate of the cost of production.

Sec. 311. Budget Limitations—

The funds, accounts, receipts and outlays of Wholly Owned Government Corporations are exempt from any general budget limitation imposed by statute upon expenditures and net lending (budget outlays) of the United States, sequestration

order or discretionary spending limit, including application of the Balanced Budget and Emergency Deficit Control Act of 1985 or similar laws.

Sec. 312. Payments in Lieu of Taxes—

Wholly Owned Government Corporations, including their franchises, property and income, shall be exempt from all taxation imposed in any manner or form by any State, county, municipality or local taxing authority, or any subdivision thereof, except as otherwise provided by law, and except that each such corporation shall make payments to State and local governments in lieu of property taxes upon real property of the corporation. The corporation shall make such payments in the amounts, at the times and upon the terms that the corporation deems appropriate, and the corporation's determination in these matters shall be final.

Title IV. Transitional Government Corporations

Sec. 401. Applicability—

This title applies only to Newly Established Transitional Government Corporations.

Sec. 402. Sunset—

Each Transitional Government Corporation shall have succession for a period of five years from the date of enactment of its enabling legislation, unless otherwise provided by law.

Sec. 403. Privatization Planning

(a) **Strategic Plan**—within four years after the date of enactment of its enabling legislation, and within four years after the date of any extension of its enabling legislation, each Transitional Government Corporation shall prepare a strategic plan for privatizing the corporation and shall transmit such plan to the President and Congress. The plan shall provide that proceeds from the return of capital to the United States shall be deposited in the general fund of the Treasury.

(b) **Consideration of Alternative Means of Transferring Ownership**—The plan shall include consideration of alternative forms of privatization, including consideration of the relative benefits and costs of complete or partial sale of corporate assets or of the going concern in one or more units to one or more privately owned entities established under the laws of a state or of the District of Columbia.

(c) **Consideration of Factors**—The plan shall include consideration of relevant factors including assessment whether privatization will:

- (1) result in a return to the United States at least equal to the net present value of the corporation;
- (2) not result in ownership, control or domination of the assets or of the acquiring entity or entities, as the case may be, by an alien, a foreign corporation, or a foreign government;
- (3) not be inimical to the health and safety of the public or the common defense and security; and
- (4) contribute to the competitive structure of the relevant market.

(d) **Evaluation and Recommendation**—The plan shall evaluate the relative merits of the alternatives considered and the estimated return on the Government's investment in the corporation achievable through each alternative. The plan shall include the corporation's recommendation on its preferred means of privatization.

(e) **GAO Evaluation**—Within 60 days of submission of the plan to the Congress, the Comptroller General shall submit a report to Congress evaluating the extent to which:

- (1) the privatization plan would result in any ongoing obligation or undue cost to the Federal Government; and
- (2) the revenues gained by the Federal Government under the privatization plan would represent at least the net present value of the corporation.

Title V. Government Sponsored Enterprises

Sec. 501 Applicability—

This title applies only to Newly Established Government Sponsored Enterprises.

Sec. 502 Sunset—

Each Government Sponsored Enterprise shall have succession for a period of 10 years, subject to review by the Congress and extension for additional periods of ten years, unless otherwise provided by law. The Secretary of the Treasury shall consider the applicable sunset period in determining the maturities of obligations that each Government Sponsored Enterprise may issue. The Secretary of the Treasury

shall issue any regulations that the Secretary deems to be appropriate for the implementation of this title.

Sec. 503 Safety and Soundness—

(a) **Required Provisions**—The law establishing any Government Sponsored Enterprise shall address issues of financial safety and soundness by including provisions for:

- (1) effective federal supervision of safety and soundness and a significant cushion of capital; and
- (2) a requirement that such GSE achieve and maintain a high investment grade rating, as prescribed in subsection (b) below, throughout its existence.

(b) **Rating—**

(1) **In General**—Not later than 1 year after the effective date of the law creating each new GSE subject to this Act, the Secretary of the Treasury shall, for each such GSE, contract with 2 nationally recognized statistical rating organizations:

(A) to assess the likelihood that the GSE will not be able to meet its obligations from its own resources with an assumption that there is no recourse to any implicit government guarantee and to express that likelihood as a traditional credit rating; and

(B) to review the rating of the GSE as frequently as the Secretary determines is appropriate, but not less than annually.

(2) **Reimbursement**—A Government Sponsored Enterprise shall reimburse the Secretary of the Treasury for the full cost of activities under this title, as determined by the Secretary of the Treasury.

(3) **Comments**—The Secretary of the Treasury shall submit comments to the Congress on any difference between the evaluation of the rating organizations and that of the Secretary, with special attention to capital adequacy and shall report on any actions the Secretary deems appropriate to assure that each GSE continuously maintains a high investment grade rating

(4) **Requirement**—Each such GSE shall achieve and maintain throughout its existence one of the two highest investment grade ratings awarded by each statistical rating organization described in paragraph (5). The Secretary of the Treasury may waive the requirements of this paragraph by published order on such terms and conditions and for such periods of times as the Secretary deems appropriate.

(5) **Definition**—For the purposes of this section, the term 'nationally recognized statistical rating organization' means any entity effectively recognized by the Division of Market Regulation of the Securities and Exchange Commission as a nationally recognized statistical rating organization for the purposes of the capital rules for broker-dealers.

(c) **Reports**—The Comptroller General of the United States and the Office of Management and Budget each shall report to the Congress upon the adequacy of provisions for effective federal supervision of safety and soundness, including the adequacy of capital standards, contained in any bill to create a Government Sponsored Enterprise. Each report shall also recommend provisions to be included in such bill to assure compliance with subsection 503 (b) of this Act.

Sec. 504 Annual Report on Impact of Borrowing by Government Sponsored Enterprises on Public Debt—

(a) **General Requirement**—The Secretary of the Treasury shall annually prepare and submit to the Congress a report assessing the financial safety and soundness of the activities of all Government Sponsored Enterprises and the impact of their operations on federal borrowing.

(b) **Access to Relevant Information**

(1) **Information from GSEs**. Each Government Sponsored Enterprise shall provide full and prompt access to the Secretary to its books and records, and shall promptly provide any other information requested by the Secretary.

(2) **Information from Supervisory Agencies**. In conducting the studies under this section, the Secretary of the Treasury may request information from, or the assistance of, any federal department or agency authorized by law to supervise the activities of any Government Sponsored Enterprise.

(3) **Confidentiality of Information.**

(A) **In General**. The Secretary of the Treasury shall determine and maintain the confidentiality of any book, record, or information made available under this subsection in a manner generally consistent with the level of confidentiality established for the material submitted by the Government Sponsored Enterprise involved.

(B) Exemption from Public Disclosure Requirements. The Department of the Treasury shall be exempt from section 552 of title 5, United States Code, with respect to any book, record, or information made available under this subsection and determined by the Secretary to be confidential under subparagraph (A).

(C) Penalty for Unauthorized Disclosure. Any officer or employee of the Department of the Treasury shall be subject to the penalties set forth in section 1906 of title 18, United States Code, if:

(i) by virtue of employment or official position, he or she has possession of or access to any book, record, or information made available under this subsection and determined by the Secretary to be confidential under paragraph (A); and

(ii) he or she discloses the material in any manner other than:

(I) to an officer or employee of the Department of the Treasury;

or

(II) pursuant to the exception set forth in such section 1906.

(c) Assessment of Risk. In assessing the financial safety and soundness of the activities of Government Sponsored Enterprises, and the impact of their activities on federal borrowing, the Secretary of the Treasury shall quantify the risks associated with each Government Sponsored Enterprise. In quantifying such risks, the Secretary shall determine the volume and type of securities outstanding which are issued or guaranteed by each Government Sponsored Enterprise, the capitalization of each Government Sponsored Enterprise, and the degree of risk involved in the operations of each Government Sponsored Enterprise due to fact such as credit risk, interest rate risk, management and operations risk, and business risk. The Secretary shall also report on the quality and timeliness of information currently available to the public and the Federal Government concerning the extent and nature of the activities of Government Sponsored Enterprises and the financial risk associated with such activities.

(d) In assessing the impact on federal borrowing, the Secretary shall report upon the impact of the issuance or guarantee of securities by Government Sponsored Enterprises upon:

(1) the rate of interest and amount of discount offered on obligation issued by the Secretary each year; and

(2) the marketability of such obligations

(e) Deadline—The report required by subsection (a) shall be submitted to the Congress by October 1 of the 1st calendar year beginning after the date of the enactment of this section, and by each October 1 thereafter.

Sec. 505 Audits—

(a) Each Government Sponsored Enterprise shall have an annual independent audit made of its financial statements by an independent public accountant in accordance with generally accepted auditing standards. In conducting an audit under this subsection, the independent public accountant shall determine and report on (1) whether the financial statements of the Government Sponsored Enterprise are presented fairly in accordance with generally accepted accounting principles, and (2) each transaction or undertaking which the auditor believes' was carried out or made without authority of law.

(b) The programs, activities, receipts, expenditures, and financial transactions of each Government Sponsored Enterprise shall be subject to audit by the Comptroller General of the United States under such rules and regulations as may be prescribed by the Comptroller General. The representatives of the General Accounting Office shall have access to such books, accounts, financial records, reports, files, and such other papers, things, or property belonging to or in use by the GSE and necessary to facilitate the audit, and they shall be afforded full facilities for verifying transactions with the balances or securities held by depositories, fiscal agents, and custodians. A report on each such audit shall be made by the Comptroller General to the Congress. The GSE shall reimburse the General Accounting Office for the full cost of any such audit as billed therefor by the Comptroller General.

(c) To carry out this subsection, the representatives of the General Accounting Office shall have access, upon request to the GSE or any auditor for an audit of the GSE under subsection (a), to any books, accounts, financial records, reports, files, or other papers, things, or property belonging to or in use by the GSE and used in any such audit and to any papers, records, files reports of the auditor used in such an audit.

(d) At least every three years the Comptroller General shall conduct program audits of each Government Sponsored Enterprise under this section. Each audit and report by the Comptroller General shall include specifically each transaction or un-

dertaking which the Comptroller General believes was carried out or made without authority of law.

Sec. 506 Shareholder Rights—

To the extent consistent with federal law, shareholders in an investor-owned Government Sponsored Enterprise shall have the rights vis-a-vis the GSE and its management that are accorded to shareholders under the Business Corporation Act of the District of Columbia.

Sec. 507 Jurisdiction—

All securities issued or guaranteed by a Government Sponsored Enterprise shall be subject to the laws administered by the Securities and Exchange Commission.

Sec. 508 Equity Securities—

No equity securities issued by a Government Sponsored Enterprise shall be lawful investments (1) for any institution whose deposits or other liabilities are insured or otherwise guaranteed by an agency of the federal government or for (2) any Government Sponsored Enterprise other than the Government Sponsored Enterprise that issues the equity securities.

Sec. 509 Federal Investments—

No securities issued or guaranteed by a Government Sponsored Enterprise shall be lawful investments or accepted as security for any fiduciary, trust and public funds, the investment or deposit of which shall be under the authority and control of the United States or any officer or officer thereof.

Sec. 510 Taxation—

Each Government Sponsored Enterprise, including its activities, holdings and income, and income from securities issued or guaranteed by a Government Sponsored Enterprise, shall be subject to all taxation imposed by federal, state and local governments and taxing authorities to the same extent as other business organizations, and income from their securities, are taxed.

Sec. 511 Report to the Congress—

A Government Sponsored Enterprise shall submit an annual report to the Congress containing the following information:

(a) A list including the name and address of each contractor, consultant, agent, or employee hired by the Government Sponsored Enterprise to engage in:

- (1) grass roots organizing or campaigning;
- (2) public relations, media consulting, or image advertising; or
- (3) lobbying, including the direct and indirect lobbying of the Congress.

(b) An itemization of all costs associated with activities described in paragraph (1) whether incurred by the Government Sponsored Enterprise or by any of its contractors, consultants, agents, or employee listed pursuant to such paragraph, including entertainment expenses, travel expenses, advertising costs, salaries, billing rates and the total amount billed for services.

(c) A description of any lobbying of the Congress or the executive branch by employees, board members, or officers of the Government Sponsored Enterprise.

(d) A description of any effort by the Government Sponsored Enterprise or its agents to encourage others to lobby the Congress or the executive branch.

(e) A list of all charitable donations paid by the Government Sponsored Enterprise on behalf of Members of Congress or members of the executive branch.

(f) A list of the salaries and other compensation (including the present value of stock options) and benefits paid to the officers and board members of the Government Sponsored Enterprise.

(g) A list of all Government Sponsored Enterprise employees who have been employed by either the Congress or the Federal Government in the five years preceding the report, and such employees' salary prior to being hired by the Government Sponsored Enterprise and their current salary.

Title VI. Government Corporation Control Act

Sec. 601—

Section 9101 (1) of title 31, United States Code, is amended to read as follows:

- (1) "Government corporation" means a wholly owned government corporation and a government sponsored enterprise as defined in this section."

Sec. 602—

Section 9101 (2) of title 31, United States Code, is amended to read as follows:

(2) "government sponsored enterprise" means the Federal Home Loan Banks, the Farm Credit Banks, the Banks for Cooperatives of the Farm Credit System, and such other government sponsored enterprises as the Secretary of the Treasury may designate from time to time.

Sec. 603—

Section 9101 (3) of title 31, United States Code, is amended by adding at the end thereof:

"(O) the National Railroad Passenger Corporation.

(P) the Federal Deposit Insurance Corporation.

(Q) the National Credit Union Administration Central Liquidity Facility.

(R) the Rural Telephone Bank.

(S) the Resolution Trust Corporation."

Sec. 604—

Section 9105 of title 31, United States Code, is amended to read as follows:

"Audits

(a) The programs, activities, receipts, expenditures and financial transactions of each wholly owned Government corporation shall be audited annually by the Comptroller General of the United States under such rules and regulations as may be prescribed by the Comptroller General. The representatives of the General Accounting Office shall have access to such books, accounts, financial records, reports, files and such other papers, things, or property belonging to or in use by the corporation and necessary to facilitate the audit, and they shall be afforded full facilities for verifying transactions with the balances or securities held by depositories, fiscal agents, and custodians. The representatives of the General Accounting Office shall have access, upon request to the corporation or any auditor for an audit of the corporation under this section, to any books, financial records, reports, files or other papers, things, or property belonging to or in use by the corporation and used in any such audit and to papers, records, files, and reports of the auditor used in such an audit. In conducting such audit, the Comptroller General may make a contract, without regard to section 3709 of the Revised Statutes (41 U.S.C. 5), for professional services with a firm or organization for a temporary period or special purpose.

(b) The Comptroller General shall make a report to the Congress on each audit conducted pursuant to this section. The report to the Congress shall contain such comments and information as the Comptroller General may deem necessary to inform the Congress of the financial operations and condition of the corporation, together with such recommendations as the Comptroller General may deem advisable. The report shall also show specifically any program, expenditure, or other financial transaction or undertaking observed or reviewed in the course of the audit which, in the opinion of the Comptroller General, has been carried out or made without authority of law. A copy of each such report shall be furnished to the President, the Secretary of the Treasury, and to the corporation at the time submitted to the Congress.

(c) A Government Corporation shall reimburse the Comptroller General for the cost of the audit as determined by the Comptroller General. An audit under this section is in place of an audit of the financial transactions of a Government Corporation the Comptroller General is required to make in reporting to the Congress or the President under another law."

Sec. 605—

Subsection 9107 (c)(3) of title 31, United States Code, is amended by striking the words, "Federal Intermediate Credit Banks, the Central Banks for Cooperatives, the Regional Banks for Cooperatives, or the Federal Land Banks" in the first sentence and substituting in lieu thereof the words, "Government Sponsored Enterprises".

Title VII. Separability

Sec. 701—

If any provision of this Act or the application thereof to any person or circumstances is held invalid, the remainder of this Act, and the application of such provision to other persons or circumstances shall not be affected thereby.

Mr. HORN. Now let's see. I think that about does it on some of the questions I had for you. Let me move to the Air Traffic Control Corp.

Well, before going to that, I would like your view, Harold, on, what do you think about what has been proposed by Secretary Pena in terms of an Air Traffic Control Corp?

Mr. SEIDMAN. I must say, I was an advisor to them. They did not take my advice. I have also been an advisor to the Air Transport Association, and I concur in the views that I think of almost all the former administrators of the FAA. It makes no sense. It is really retrogressive. We created the FAA to bring the air traffic control and safety functions together. We did not think it was desirable at the time we did the study in the Academy to create a situation where you would have first and second class citizens there.

You see, in TVA everybody works for the authority. They have the same status whether they are on the governmental side or whether they are on the corporate side, the power side. We thought that was the model which would be best suited to meet the problems of air traffic control, of capital investment, of the flexibility in dealing with personnel which was talked about, and the standards of bringing in, so the air traffic controllers do have equipment that is geared for the 1990's and not the 1960's, and we think that would be where to go.

So the principle of corporation we agree with. We disagree with the fact that taking air traffic control and separating it from safety. We do not think that is feasible, and we certainly would oppose privatizing air traffic control. That was brought up when I was Assistant Secretary of the Bureau of the Budget, and at that time I thought it had no merit whatsoever.

Mr. HORN. Would the corporation be levying user fees on the planes as they land and take off? How do they plan to pay the bills?

Mr. SEIDMAN. The bills would be paid by landing fees, as on most of the airports abroad, which are authorities. The air traffic control, they pay fees for it, which would be charged to the airports that use the air traffic control system. That is done in other countries. That is no particular problem.

Mr. HORN. Would the fees essentially go up with privatization of that corporation, of even a government corporation? Would the fees really go up?

Mr. SEIDMAN. Mr. Chairman, what happens there, one of the things—and this has come up with the question of the Patent Office—is that in any corporation you do not leave it—you have a formula set out as to what the elements of cost are that will get into it, and you have a procedure by which you go under the Administrative Procedures Act where you have this reviewed, an opportunity to protest and ultimately to go to the court to question any, and, as I found, to give you an example what happened here, it was on the Panama Canal Co. when I set that up, they had a statutory toll rate which was between 90 cents and \$1. The Appropriations Committee said to increase the rate to \$1. They had come up as a noncorporation. Well, the rate ought to be \$1.60 after it was a corporation, and they got rid of things they shouldn't have been doing.

In fact, there was a good question whether 90 cents was too high. In fact, there was a Supreme Court case where they were sued, the

General Accounting Office, over the overcharge. There was no increase.

At the present time, because it is done by Congress, the users of Patent Office, or customers, are paying really a special tax which is just going for general purposes, not for providing services. So you do have review when you have elements of cost which are reviewable and identifiable which you don't have today.

Mr. HORN. One of the issues in creating the Air Traffic Control Corp. is the placement of the safety regulation function, that crucial component, and I think Dr. Seidman's testimony you would agree with, that represent the two associations, that these should not be separated and they ought to remain together. I take it that is the brunt of your testimony too, is it not?

Mr. KRASNER. Absolutely.

Mr. SEIDMAN. That is the brunt, and that would have been the testimony of my associate, Alan Dean, who wasn't with us because his oldest grandson is graduating today. He is a former associate administrator of FAA. As you know, Mr. Chairman, he points out one of the reasons that the FAA was created was to bring these two functions together which had been divided in CAA and CAB and didn't work.

Mr. HORN. I take it, Mr. Krasner and Mr. Johnson, you agree with that. Is that correct?

Mr. KRASNER. Mr. Chairman, we—and I won't speak for Jack—we do agree with Mr. Seidman on that. In our initial discussions our initial proposal was that the FAA as a whole be taken out and made into a Government corporation, and it was the administration's position, for whatever reason, that they did not want to do that, and it ended up as the proposal that you see today. So we certainly do agree with him on that.

The other point I want to bring out is on the fees, on the fees for the privatizing under the Senate proposal of the Senate budget resolution. The fees would actually double because the privatized company would be—the way they are outlining it, the privatized corporation would be responsible for the setting of fees to run the private corporation, but the money that currently goes into the Aviation Trust Fund which comes from ticket tax and fuel tax would continue to go into the Aviation Trust Fund, so it would go toward the Government, so you would virtually have to double your fees to run the corporation.

Mr. HORN. According to the National Performance Review the Federal Aviation Administration's new computer system is 10 years behind schedule, 32 percent over budget, and using obsolete technology. How would a government corporation change that disaster? I have visited the disaster when I was on the Aviation Subcommittee in the last Congress.

Mr. KRASNER. We think a lot of it has to do simply with the thought process. A company has to think more like a business in order to be able to act like a business. We also need freedom in procurement procedures to allow us to buy up-to-date equipment.

What you are dealing with now and what the agency has always done, they have gone out to develop their own equipment, and they have determined what their needs were and then went into re-

search and development to figure out how they were going to meet those needs, and essential that is fifties kind of thinking.

In this day and age, we should be determining what our needs are, going out to companies who sell this stuff off the shelf, and see who comes closest to meeting your needs. What you really do is, you develop software and buy hardware, and I think the days are gone when you develop your own hardware because then what happens is, by the time you get it developed, you know, you are way behind schedule.

So I think it is a combination of the procurement laws as well as the corporate thought process that might actually get you where you need to be.

Mr. JACK JOHNSON. Mr. Chairman.

Mr. HORN. Yes, Mr. Johnson.

Mr. JACK JOHNSON. From the PASS perspective, we agree with the idea that the safety functions should be also in the corporation should there be a corporation.

On the issue that we just talked about with Mr. Krasner, we feel like the idea of having a corporation be able to go out and procure the equipment that they need based on what their thoughts are for today, you would agree that 10 years ago when they were talking about the new computer systems they had no idea it would be 10 years before they were able to even think about maybe rethinking their original idea and looking to 2002 for implementation of that system. So they had no idea what the new technology was going to bring about, and they are still buying the same thing they talked about buying 10 years ago for the most part. So that is one of the problems, if they had the ideas 10 years ago they are certainly not relevant to today's world.

Mr. HORN. That is a good point.

In your testimony you all noted the increase in the facilities FAA is responsible for. You noted the corresponding decrease in employees. Do you have any figures on the management to line ratio change over that period?

Mr. JACK JOHNSON. The management to line ratio has been steadily decreasing; in other words, more managers per employee for that period of time.

Mr. HORN. You are saying there are more employees per manager?

Mr. JACK JOHNSON. No, the other way around.

Mr. HORN. The other way around.

Mr. JACK JOHNSON. And the GPRA has mandated changes in that which will be coming into effect with the reorganization realignment of AF to 10-to-1 and 15-to-1. Right now we are looking at something less than 4-to-1 as far as supervisor to employees.

Mr. HORN. OK. Let's ask the FAA administrator to furnish for the record the latest information on that so we can have it at this point in the record.

[The information referred to follows:]

FAA Airway Facilities Workforce	Supervisors	Non-Supervisory Employees
Systems Maintenance	1,032	9,851

FAA Airway Facilities Workforce	Supervisors	Non-Supervisory Employees
Flight Inspection	51	588

Mr. JACK JOHNSON. On that particular subject, I would also like to comment that with the most recent buy-outs that the FAA underwent they are still backfilling all those supervisory positions, so that is taking people directly out of the safety-related work force, putting them temporarily into the supervisory positions that were bought out, so therefore there is no change, we still have the same ratio, less than 4-to-1.

Mr. HORN. In your joint testimony, gentlemen, you asserted that contractors do not provide the same quality of work that was performed by government employees. You also assert that these contractors cost more than government employees. Now that is not the first time I have heard that from union leaders who obviously are proud of their members' achievement. That is your job.

Now what I want to get to is, the administration in the National Performance Review report on the Department of Transportation notes that the Federal Aviation Administration's experience with hiring contractors to operate low-activity airport towers has been positive. FAA employees running these operations cost about \$450,000 a year while contractors operating in the absence of Federal personnel rules cost \$250,000 per year. Now I'm not sure, and maybe staff is, whether that is per person 24 hours or what the figure is there, and we need to get that straightened out. I'm just curious to let you comment on that since that is what I'm told the NPR finding is.

Mr. KRASNER. In the case of the contract towers, the low-level activity towers, you are correct as showing a cost savings, and I guess realistically it is a matter of \$450,000 versus \$250,000 roughly, on an average. Some of them don't necessarily reflect that. But then it is a matter of getting what you pay for.

We are finding situation where you have—and what is happening is, the air carriers, they are only affected to a very limited amount, they don't fly into those low-activity airports, but you have general aviation pilots who number—well AOPA represents about 345,000 of them, and we are finding there are airports where flight schools are moving out because they don't feel they are getting the level of service. We are hearing stories from pilots on the information highway, on Internet, where we hear horror stories all the time about not even getting proper landing clearances.

As you are aware, air traffic controllers are drug tested and alcohol tested on a random basis, as are all transportation type employees, while apparently in the contract towers you are only drug tested for I believe it is 2 years, and if you don't test positive within 2 years you are never tested again, while Government employees are tested for their entire career.

So you can generate cost savings if you want to generate cost savings, and additionally a lot of them have shorter hours, you are also working with a lot less people, whereas you may have seven or eight people—you may have seven or eight people manning a level one tower under Government, under a contractor they will go

down to maybe three people, and people work 6, 7, 8 hours a day without a break, and so I guess it is just a matter of what you are willing to pay for and what kind of services you want in return.

Mr. HORN. Very good.

In the testimony you also noted your desire that the Federal Aviation Administration be altered into a government corporation and your opposition to privatization. Now in the past hearings—and his name was mentioned by Dr. Seidman—Alan Dean, who is a real expert on both Government corporations and the FAA and was long time Assistant Secretary over in the Department of Transportation, stressed that air traffic control and safety regulation functions should be vested in the same entity.

Apart from the air traffic control and safety regulation, what would remain in the FAA once these very significant functions departed either into a Government corporation or privatization, as far as you are concerned? I'm just interested in your views.

Mr. JACK JOHNSON. Is the safety portion of the FAA—safety regulation proportion?

Mr. HORN. Yes, that air and air traffic control were removed, what is really left over there?

Mr. JACK JOHNSON. Very little. Most of the rest of the FAA is administrative that would be left there.

Mr. HORN. Airport improvement grants?

Mr. JACK JOHNSON. Airport improvement, certification.

Mr. SEIDMAN. Flight standards, licensing of pilots.

Mr. KRASNER. It are designed to be about 20 percent of what it is today, I believe.

Mr. HORN. Yes.

Mr. JACK JOHNSON. Flight standards actually is the safety regulating portion. They are the folks that we represent, and our argument would be that they would be better placed with the rest of the FAA in a corporation.

As far as the cost of using contractor maintenance, the government itself, through GAO, did a study, and the study came back and said that it would save \$40,000 per year per person by using in-house staffing as opposed to using contractor staffing, and, having seen a lot of the data through AF executive boards and so on, I've seen that it does cost somewhere between \$70,000 and \$100,000 per person to hire a contractor to do the same function that an FAA employee does now.

Mr. HORN. And you say that quote you gave was from a General Accounting Office study?

Mr. JACK JOHNSON. Yes, sir.

Mr. HORN. We ought to have the staff put that in at this point. [The study follows:]

Mr. Chairman and Members of the Subcommittee:

We appreciate the opportunity to testify on the Federal Aviation Administration's (FAA) fiscal year 1993 budget request for \$9.4 billion. This includes \$4.6 billion for operations; \$2.7 billion for facilities and equipment (F&E); \$1.9 billion for grants-in-aid to airports; and \$230 million for research, engineering, and development (RE&D). With the support and guidance of this Subcommittee, FAA has made significant progress over the last decade in the face of enormous challenges. This year, as the Appropriations Committees deliberate FAA's budget request, the Congress is also considering reauthorization levels for the agency for the next several years. To assist in these deliberations, our testimony provides an update on FAA's major activities and an assessment of the agency's future plans. Our testimony is based on

a report we are issuing today about the status of FAA's modernization effort and on work we have done over the last several years. A listing of the relevant reports and testimonies appears in an appendix to our statement.

Our testimony today will cover FAA's management of air traffic controllers, maintenance technicians, and aviation safety inspectors; modernization of the air traffic control (ATC) system; changes related to satellites, support services, and the consolidation of ATC facilities; and the need for FAA to establish measurable goals for its programs. Our four main points are as follows:

- Total air traffic controller staffing has improved dramatically during the last decade. FAA had about 16,200 controllers in July 1981, lost 11,400 in the strike, and now has nearly 18,000. According to its staffing standards, FAA has enough controllers overall but has staffing shortfalls at some ATC facilities. The agency is now analyzing its requirements for controllers at each facility as directed by this Committee. Staffing levels are a problem for the field maintenance work force as well. During the 1980s, FAA did not have a sufficient number of field maintenance technicians, and the current level of about 8,900 personnel in the field maintenance work force is well below the 11,700 called for by the staffing standard. The shortfall can be expected to continue since delays in modernizing equipment keep the demand for maintenance technicians high. Finally, FAA has doubled its aviation safety inspection work force since 1983 and now has about 2,600 safety inspectors. We have previously recommended that FAA needs to better target its inspection resources.

- In the past 2 years, FAA has initiated major reforms in its modernization program. FAA has required that needs be defined and approved by top management before projects can start and that operational testing be conducted before commitments to production are made. FAA is also aligning its budget with the acquisition process so that development and production are funded separately. However, these reforms have the most potential for a positive impact on new projects. Problems are still occurring in ongoing modernization projects. Of the 12 major acquisitions that we have reviewed, 4 have had both cost increases and delays over the past year, 3 have had only cost increases, and 3 have had only delays. The cost increases ranged from 4 to 21 percent. FAA completed 6 projects in the past year, for a total of 36 completed projects, and still has about 200 projects to complete. The total estimated cost for modernizing the system in fiscal years 1982 through 2000 is \$31.9 billion, about \$600 million more than it was last year. Through fiscal year 1992, the Congress has appropriated about \$13.4 billion, or 42 percent of this amount.

- FAA faces three major modernization issues, each involving significant funds. First, FAA has not determined how many consolidated ATC facilities it needs, despite this Committee's February 1992 deadline. FAA's cost estimates for increasing the number of consolidated facilities range from \$2.5 billion to \$4 billion. Second, satellites have the potential to enhance the ATC system and significantly affect the modernization program. FAA has just released a report for integrating satellites into the current land-based ATC system. We intend to evaluate the report and provide our views to your Committee. Third, FAA plans to expand the number of support contractors assisting with modernization when the agency's \$1 billion support contract with Martin Marietta is finished in 1994. However, FAA did not consider using in-house staff, which the agency estimates would save about \$45,000 per staff year compared to using contractor staff, and has not clearly identified in the budget the costs for the new contracts.

- As we have testified in recent months, FAA could improve its operations through the increased use of measurable goals in its program plans. Goals, such as reducing flight delays by a specified percentage either systemwide or within geographic regions, would better guide decision-makers in choosing among competing priorities, such as which airport development projects to fund. Measuring progress toward specific goals also would help congressional oversight go beyond considering staffing levels, the number of completed projects, and schedules and would better focus attention on the results of federal spending. Three of FAA's major program plans that guide a significant portion of the agency's budget do not have adequate or reasonable goals. Neither the modernization plan nor the airport development plan includes measurable goals. Although the draft research and development plan includes measurable goals, such as increasing the aviation system's capacity by 20 percent before the year 2000, they cannot be achieved through research alone and should be integrated with other plans.

OPERATIONS ACCOUNT

FAA's requested appropriation of \$4.6 billion for operations represents a 6-percent increase over the amount in the fiscal year 1992 appropriation. The operations account funds the salaries, benefits, and training of FAA's major work forces—air traffic controllers, maintenance technicians, and aviation safety inspectors. FAA continues to face challenges in meeting its staffing needs and effectively distributing these work forces to operate and maintain the ATC system and to conduct safety inspections.

FAA Faces Challenges in Managing Its Controller Work Force

FAA had 16,244 controllers in July 1981, lost 11,400 in the strike, and now has 17,958 controllers. The current number of controllers exceeds the staffing standard overall. Staffing standards are formulas or mathematical models for determining the number of employees needed at each facility on the basis of the work load.

Despite an adequate number of controllers systemwide, staffing levels at particular facilities differ substantially from the levels prescribed by the facility staffing standard. For example, as of August 31, 1991, one center had 96, or about 38 percent, more controllers than called for by its standard, while another center had 58, or about 14 percent, fewer controllers than called for by its standard.

In 1991 we found, at both centers and terminals, that the placement of FAA Academy graduates was inconsistent with the standards. Some graduates were placed at facilities that had more staff than called for by the standards rather than at equivalent facilities, in the same region, that had fewer staff than the standards indicated. Specifically, we found that FAA placed Academy graduates at six centers with more controllers than the standards prescribed. FAA headquarters officials believe that many deviations from the staffing standards are based on the regions' special knowledge of operational needs. For example, regions might explain placing more staff at a facility than the standard indicates because of a higher than anticipated attrition rate, a greater work load than anticipated, or the facility's special ability to train controllers.

FAA expects the number of controllers to decrease through attrition to 17,721 by the end of fiscal year 1992. In fiscal year 1993, FAA is requesting funds for only 17,871 controllers, although its staffing standard indicates that 18,128 are needed. An Air Traffic official said FAA requested about 250 controllers fewer than the standard indicates because (1) the agency is revising its screening process for hiring new controllers and wants to take on relatively few controllers during this transitional year and (2) the number of controllers planned for fiscal year 1993 meets FAA's goal to maintain staffing levels to within 5 percent of the standard. We suspect that this shortfall will make it harder for FAA to meet staffing needs in subsequent years. Reaching the fiscal year 1994 staffing standard of approximately 18,500 controllers would require FAA to add over 600 controllers in 1994.

We believe that FAA does not currently have sufficient information to know whether differences in actual staffing and the standards are justified. FAA has not analyzed either the staffing or the training capabilities at specific facilities despite being tasked by this Committee to analyze its controller requirements for each facility. FAA was to report by December 31, 1991, on these staffing requirements for the next 3 fiscal years, the number of controller candidates needed to meet these requirements, and its actions to correct disparities between the actual staffing and the staffing needed at facilities. FAA has contracted for a study of its staffing requirements for controllers, but the study will probably not be completed until 1993. Furthermore, FAA is planning to inventory facilities' training capabilities this year. Until these tasks are complete, FAA cannot be sure that its regions are making the best decisions about placing controllers.

FAA is reforming its screening and training process. The new process is intended to reduce the unacceptably high washout rate at the Academy, reduce the relocation costs associated with moving controllers as they become more experienced, and improve recruiting since the screen can be administered at multiple sites. Under the new process, candidates will be screened for up to 5 days to determine their aptitude for controlling air traffic, rather than the 9 weeks that screening currently takes. Training would then take place at the FAA Academy for 4 or 5 months. Full implementation of the plan is scheduled for fiscal year 1994.

In testimony last year, we discussed a concern about the new screening and training process. The new screening process places greater reliance on FAA's ability to accurately determine candidates' aptitude because the agency intends to train candidates who pass the screen for the entire 4 or 5 months, after which the candidates will take a "performance verification" test. An Air Traffic official has said FAA would provide the test results for the screening process, but we have not received

them yet. Without the test results, we cannot assess the accuracy of the screening process for predicting the aptitude of candidates to become controllers.

Maintenance Work Force Is Insufficient to Meet Needs

FAA currently has a field maintenance work force of about 8,900 to service ATC equipment at over 28,000 facilities across the country. However, the staffing standard for the field maintenance work force shows that a work force of about 11,700 is currently needed, which is 24 percent larger than FAA has now. By fiscal year 1995, the standard indicates that a field maintenance work force of about 11,900 will be needed—an increase of 3,000 over the present number. Airway Facilities officials expressed concern about the staffing situation, but said funding constraints limited their ability to hire more staff. The fiscal year 1993 request level will fund the same work force level as in fiscal year 1992.

As recently as 1989, FAA expected to need fewer maintenance technicians in the near future. Staffing standard projections in 1989 called for a field maintenance work force of about 9,700 in fiscal year 1992 and about 8,600 in fiscal year 1995. The 1989 projections were based on a decreasing maintenance work load. However, FAA now expects maintenance requirements to increase because of the slower than anticipated replacement of aging equipment, an expected increase in the number of facilities, and an increase in the number of services performed by maintenance staff.

FAA's efforts to reduce the gap between the field maintenance work force and the work load have not succeeded. FAA estimates that about 38 percent of the field maintenance work force will be eligible to retire by 1995 and had hoped that the Federal Employees Pay Comparability Act of 1990 (P.L. 101-509) could help retain staff. On a case-by-case basis, the act (1) permits agencies to pay allowances of up to 25 percent of employees' base pay in order to retain the employees and (2) permits rehired retirees to receive both a full salary and retirement benefits. However, since the act was passed, applications have been approved for only three engineers. Several FAA officials said that the process is cumbersome and not well understood in the field. A personnel official said field maintenance staff would be receiving more information about the program and instructions on completing the paperwork.

Although equipment redundancy and the excellent efforts of technicians have kept overall system availability at about 99.8 percent, the effects of staffing shortfalls are being felt. The mean time to restore component equipment within the ATC system increased 35 percent between calendar years 1988 and 1991. Also, FAA increased its use of overtime to about 250,000 hours in fiscal year 1991, which is a 36-percent increase from fiscal year 1988. Until now, FAA believed it was adequately performing its maintenance duties related to safety with less staff than requested by deferring in the short term maintenance activities not related to safety. FAA now believes it needs more staff and is developing options for alleviating the shortfall that still exists. Options include continuing to have contractors provide the maintenance for new systems and deferring training so staff can conduct maintenance.

More Effective Use of Safety Inspectors Could Provide Better Coverage

FAA has taken positive steps to address some of the identified shortcomings in its aviation safety inspector programs. The inspector work force is responsible for routine surveillance of airlines, certification of airlines' operations, accident and incident investigations, and safety promotion. FAA has increased its inspector work force from 1,300 in fiscal year 1983 to 2,600 currently; developed and is now updating a staffing standard to determine the number of inspectors needed; improved hiring and training processes; institutionalized a program to perform in-depth inspections of selected airlines; and developed national guidelines for its inspection program that establish the number and frequency of inspections that must be undertaken.

Notwithstanding these positive steps, FAA could do considerably more to maximize the use of its inspector resources. FAA's fiscal year 1993 budget request holds the level of inspectors constant at its current level. We recently recommended that FAA develop an effective inspection information system to help assess how inspection resources are used. Currently, FAA's management cannot determine if inspectors are spending sufficient time on surveillance—their number-one priority. Analyzing fiscal year 1990 inspection data, we found that (1) FAA's district offices did not conduct about 28 percent of the approximately 19,000 required inspections; (2) about 25 percent of about 3,600 airlines—mostly air taxis—did not receive at least one operations, maintenance, or avionics inspection as required; and (3) inspectors spent 23 percent of their time performing inspections—falling short of FAA's requirement to spend 35 percent.

Furthermore, we reported that FAA inspectors had identified more than 9,000 problems that were, or had the potential to be, in noncompliance with safety regula-

tions or other operating practices. Since it had not analyzed its inspection data, FAA could not determine whether inspectors had followed up to ensure that the airlines corrected identified problems. We also found that in some instances, FAA's routine inspections were not effective in discovering safety violations that led to emergency orders revoking commuter and air taxi operating certificates. In these cases, FAA became aware of the safety violations as the result of tips or accident investigations.

Lastly, FAA does not have a system to target its inspection resources to airlines that pose the greatest safety risk. Using a system developed for the Department of Defense to assess airlines' performance, we found that for 97 airlines, FAA's inspection coverage was too great for 17 and too little for 17. FAA is developing the Safety Performance Analysis Subsystem, which will assess all airlines' safety risk and help the agency better target FAA's inspections. FAA plans to evaluate a prototype system by fiscal year 1993.

FACILITIES & EQUIPMENT ACCOUNT

FAA's requested appropriation of \$2.7 billion for facilities and equipment (F&E) represents a 13-percent increase over the amount in the fiscal year 1992 appropriation. The F&E account funds the modernization of the ATC system. FAA has taken some positive steps to reform its acquisition process for equipment. However, these reforms have not yet alleviated problems with costs and delays in modernization projects.

FAA Is Reforming Its Management of ATC Modernization

To solve the long-standing problems in its modernization projects, over the past 2 years FAA has begun to institute major reforms to its acquisition process. For example, FAA now requires at the start of projects mission needs statements, which are to identify goals, capabilities, required resources, and potential risks for these projects. Another reform is to thoroughly and independently test systems, the "fly before buy" concept, before committing to production. Acquisition reform has already made a difference by preventing the agency from prematurely awarding a contract for production of the \$1.4 billion Voice Switching and Control System.

However, following through on these reforms is critical for success, though this task is made difficult for FAA because of projects it has to track. Projects added since the original modernization plan now account for about half of FAA's F&E budget. Furthermore, the leadership at FAA has changed several times during the evolution of the modernization effort. Over the modernization plan's 10-year history, FAA has had seven different Administrators and Acting Administrators. We believe the new FAA Administrator's support for reforming the acquisition process will be a vital element in the modernization program's success.

We noted last year that contrary to its own internal order, FAA included several acquisitions in its fiscal year 1992 budget request that did not have approved statements of mission needs. This year, however, our review of the budget indicates that FAA is complying with this important requirement. Beginning with its fiscal year 1994 request, FAA is requiring that all modernization projects have an approved statement of mission needs before the projects are included in the Capital Investment Plan (CIP) and the budget.

Despite these positive steps, our work to date indicates that some improvements are still needed in the mission needs process. FAA's acquisition order states that mission needs statements should include quantitative support, such as the results of studies, data analyses, or air traffic forecasts. However, most of the statements we have reviewed do not include such support. The statements generally do not quantify shortfalls of the current system or the extent to which the new projects are intended to alleviate the shortfalls. Without quantifying shortfalls and objectives, it will be difficult to revalidate the mission needs statements throughout the acquisition, develop appropriate operational requirements, and measure the extent to which completed projects improve the ATC system.

At the direction of the House and Senate Appropriations Committees, FAA is also taking action to align its budget process more closely with the acquisition process delineated in "Office of Management and Budget Circular A-109." This reform will show acquisitions' progression through development and production, phases in which the prior budget presentation often blurred distinctions. Our review of the new budget categories indicates that FAA's budget will comport more closely with A-109 by having separate development and production categories. However, FAA has not yet established an order, as directed by this Committee, that clearly describes the criteria under which funding is to be budgeted.

Cost Increases and delays in F&E Projects Persist This Year

Our annual status report shows FAA's latest financial plan for modernization requires \$31.9 billion of total F&E appropriations for fiscal years 1982 through 2000.¹ The Congress has already appropriated \$13.4 billion, or 42 percent of this amount. The total cost estimate for modernization is about \$600 million more than it was last year.

Last year, 8 of the 12 major acquisitions that we reviewed had increases in total estimated costs. This year, 7 of the major acquisitions had cost increases ranging from 4 to 21 percent and totaling about \$400 million. The major acquisition with the largest cost increase was the Advanced Automation System (AAS). AAS increased in cost by about \$219 million primarily because of changes needed to improve interfaces between controllers and the portion of the system to be installed in ATC towers.

Last year we reported that 8 of the 12 major acquisitions we reviewed had slipped behind schedule. This year, delays occurred in 7 of the 12 major acquisitions that we reviewed in detail. A project with a major delay since last year is the Central Weather Processor. The last-site implementation date slipped 2 years because of questions raised by an FAA team's review of the usefulness of the project's Real-time Weather Processor component. However, this schedule slip accommodates a thorough analysis of requirements that we believe is more important than implementing a system that does not meet users' needs.

Delays cause FAA to rely longer on its old ATC equipment and postpone much of the benefits expected to accrue from modernization. These benefits include reduced delays for flights, pilots being able to fly their preferred routes, and a reduced risk of accidents. FAA estimates that users of the ATC system have realized \$24 billion in benefits through fiscal year 1991 from completed and partially completed modernization projects. However, delays postpone much of the \$258 billion in benefits FAA expects from the remaining projects.

FAA notes that virtually all of the originally planned modernization projects are under contract, but the signing of contracts is clearly not a good measure of success. For example, the Mode S contract was signed about 8 years ago, and FAA still does not have one operational system. Another way to view progress is to consider the number of projects completed and the number of new projects added to the modernization plan each year. FAA completed 6 modernization projects this past year, for a total of 36 completed projects. These projects account for about 3 percent of the estimated cost of modernization through fiscal year 2000. FAA added 5 projects to its modernization plan this year, compared to 94 last year. The plan now includes about 200 projects.

UNCERTAINTIES CAUSED BY MAJOR MODERNIZATION CHANGES ON HORIZON

FAA faces three major issues in its modernization effort, each involving significant funds. First, FAA is considering more than doubling the number of consolidated facilities that form the basis of its modernization plan. Second, FAA is planning to integrate satellite technology into its land-based ATC system. Third, FAA is revising its system of support contracts for modernization. We will address each issue in turn.

As you know, FAA has become concerned about the operational feasibility of consolidating all 202 terminal radar approach control and en-route centers into 23 facilities. FAA vulnerability studies indicate that if a consolidated facility failed, adjacent facilities could not adequately manage the airspace. As a result, FAA is considering having 53 or 54 consolidated facilities. Last year we emphasized the importance of deciding on the number of consolidated facilities, and this Committee directed FAA to report its consolidation plan, including an implementation schedule and funding estimates, by February 1, 1992. However, FAA has not met this deadline and plans to ask for an extension.

Without a finalized consolidation plan, it is not clear what additional funds will be needed over the next few years. Also, FAA cannot take the steps needed to allow consolidation to commence by 1997, as planned. These include planning for new buildings, exercising options in existing contracts for additional equipment, and preparing to relocate as many as 6,000 controllers and technicians. Options for procuring the terminal portion of AAS, for example, expire in April 1994. FAA is currently working on its fiscal year 1994 budget request and needs to know how many terminal AASs will require in order to avoid renegotiating the options. In addition, the AAS contractor, IBM, has emphasized the need for a decision before this fall, when

¹ Air Traffic Control: Status of FAA's Modernization Program (GAO/RCED-92-136BR, Apr. 3, 1992).

the design of the area control computer complex phase of AAS is finalized. The design depends on the number of ATC facilities involved and their size.

A change in FAA's consolidation plans will have a major impact on F&E funding levels over the next few years. FAA's March 1992 reauthorization proposal states that \$200 million may be needed in fiscal years 1994 and 1995 to establish more area control facilities than currently planned. However, previous estimates of the cost to establish additional area control facilities suggest that the total cost would be much higher. FAA has estimated needing an additional \$2.5 billion during the next decade over and above the amount in its current funding plan. FAA also estimated, in 1988, a \$4 billion increase for another plan that included about 10 fewer facilities.

Regarding satellites, there is wide recognition that this technology has the potential to enhance the ATC system and significantly affect the modernization program. The House and the Senate Committees on Appropriations tasked FAA to develop an aggressive transition plan that (1) examines the potential savings in modernization costs from an early transition to satellites and (2) assesses the benefits the Department of Defense's satellite navigation system could have for commercial airlift. In recent testimony on FAA's F&E reauthorization, the Air Transport Association emphasized that FAA's transition plan should include the key technical decisions that will have to be made, milestone dates for accomplishments, and projected costs and benefits of the proposed transition. This information would be very useful from a budgetary perspective and for tracking FAA's progress in applying satellite technology to ATC. On March 25, 1992, FAA transmitted its report to the Appropriations Committees addressing the integration of satellites into the ATC system. We intend to evaluate the report and provide our views to the Committees.

Another major change in FAA's management of its modernization effort involves the Systems Engineering and Integration Contractor (SEIC). In addition to handling overall systems engineering and integration, the SEIC handles field support work and technical assistance. Martin Marietta's Air Traffic Control Division has been FAA's SEIC for the last 8 years, but its \$1 billion contract with FAA ends in January 1994. FAA has decided to split the SEIC contract into several smaller contracts. FAA officials told us that the primary reasons for this new approach are to (1) increase competition from splitting the contract into specific areas of expertise and (2) improve management efficiency by having smaller contracts to manage. FAA plans a total of seven new support contracts to cover the SEIC's responsibilities, at an estimated cost of least \$1.5 billion over the next 7 years. We have two concerns about FAA's plans: (1) FAA's budgeting for support contracts does not facilitate congressional oversight, and (2) FAA has not thoroughly analyzed all possible alternatives.

FAA has not clearly identified the costs associated with the new support contracts in its fiscal years 1992 and 1993 budget estimates. The costs for most of the new contracts are included in the budgets of the systems being procured. However, FAA generally identifies major acquisitions such as these support contracts separately in its budget to allow for the most effective oversight by this Subcommittee and the rest of the Congress.

FAA's policy is to assess the benefits and costs of high-cost F&E efforts. However, when FAA considered three alternatives to the current support contract, the agency did not analyze the benefits and costs of the alternatives. FAA also did not consider a fourth alternative—conversion of contract support to in-house staff. FAA officials estimate that in-house support would cost about \$45,000 less per staff year, on the average, than contractor support. In-house support has the potential for cost savings and is appropriate since modernizing the ATC system is a continuous rather than finite program.

GOALS NEEDED TO ESTABLISH PRIORITIES AND MEASURE PERFORMANCE

FAA could improve its operations by making better use of measurable goals in its program plans. Although significant plans exist in three of FAA's major program areas—ATC modernization; airport planning; and research, engineering, and development (RE&D)—the agency has not established nor included in these plans appropriate goals and objectives. Together, these programs account for between \$4 billion and \$5 billion of annual congressional appropriations from the Airport and Airway Trust Fund. These funds are entrusted to FAA for effective administration. Establishing specific goals for increased productivity by controllers or reduced flight delays for each of these programs would allow decision-makers in FAA and the Congress to better determine the program's direction, progress, and accountability.

Guiding FAA's spending of the F&E appropriation, which is intended to modernize the nation's ATC system, is the Capital Investment Plan (CIP). Although FAA included measurable goals in the CIP's predecessor—the National Airspace System

(NAS) Plan—FAA has not developed such goals for the CIP. As stated in the NAS Plan, the purpose of establishing a plan with specific goals and objectives was to end the “series of piecemeal adjustments and improvements” that had marked the modernization effort until then. The 1988 NAS Plan included such a goal when it proposed to reduce operational errors in the ATC system by 80 percent between 1984 and 1995. Reestablishing goals would form a basis for measuring the progress and benefits of the roughly \$2.5 billion per year modernization effort beyond simply counting completed projects and reporting whether projects are on schedule and within budget. Congressional oversight would be able to focus more on the results of federal spending.

As we testified in February of this year, FAA also has not established goals for its National Plan of Integrated Airport Systems (NPIAS).² This plan forms the initial basis for guiding the spending of \$1.9 billion in grants-in-aid authorized for developing public-use airports. The NPIAS includes estimates for needed development in 5 basic categories at almost 3,300 public-use airports that are eligible for federal aid. The current plan identifies \$40 billion of development costs over a 10-year period. Because FAA’s budget request and authorization usually represent only about five percent of that amount, decision-makers must work hard to determine which of the many competing projects to fund. However, because the NPIAS establishes no measurable national goals, such as the number of new runways to be constructed or the amount flight delays should be reduced, it provides little guidance for making funding choices among airport improvement projects or distinguishing among the projects on the basis of their potential to improve the national airport system. FAA officials have concurred with our conclusion that establishing measurable goals for its national airport plan would produce operational benefits and have stated their intention to develop such goals.

Finally, FAA has requested \$230 million for RE&D in fiscal year 1993. After reviewing FAA’s draft RE&D plan, we reported that the plan establishes goals so ambitious that research and development alone could never hope to achieve them.³ For example, these goals include increasing airspace and airport capacity at least 20 percent by 1999, increasing capacity an additional 20 percent by 2005, and reducing runway incursions by 80 percent by the year 2000. However, only in combination with ongoing capital investment and airport development projects can RE&D projects be expected to achieve these goals.

CONCLUSIONS AND RECOMMENDATIONS

In conclusion, Mr. Chairman, FAA has made great strides in the last decade in improving the nation’s ATC system and ensuring safety. We believe future progress will depend on FAA’s actions to address concerns, as raised in our testimony, about the adequacy of staffing levels, targeting of resources, modernization cost increases and delays, and uncertainties about consolidation and satellites.

We believe that FAA needs to improve its planning in such areas as the modernization of the ATC system, airport development, and research and development. Good planning involves a reasonable vision of the future and the ability to break that vision down into measurable increments or goals. We believe that through its planning, FAA needs to commit itself to appropriate goals that will help guide funding decisions and also act as benchmarks for measuring progress.

Accordingly, we recommend that the Secretary of Transportation direct the FAA Administrator to (1) include measurable goals in its CIP; (2) establish goals for each development project category in the NPIAS; and (3) develop goals for the RE&D plan that are appropriate for that plan.

Mr. Chairman, this concludes my statement. We will be happy to respond to any questions you might have at this time.

Mr. KRASNER. Mr. Chairman, I also want to point out on that issue that there is a little bit of a shell game in the contracting out of level one towers because—due to the budget enforcement and the reduction of appropriated funds each year to run the agencies when they let the contract, and then they have appropriated funds to pay for these contracts, but the appropriated funds reduce every

² Airport Development: Improvement Needed in Federal Planning (GAO/T-RCED-92-30, Feb. 19, 1992).

³ Aviation Research: Progress Has Been Made but Several Factors Will Affect Program Success (GAO/T-RCED-92-39, Mar. 10, 1992).

year, the contract costs go up every year. I mean they have no choice; most costs do go up every year.

So the FAA is forced to take the shortfall out of their existing operating account, and what is going to happen, you are going to find in 2, 3, 4 years, they are going to find that they can no longer support the contract tower operation and they are going to throw it back on municipalities, and they are going to end up saying if you want a tower, well, go ahead and support it because we can no longer do it, we are going to shut it down, and they are going to find you are going to have an economic impact on the municipalities who can no longer afford to have those contract services there, and I don't think they are looking—well, the FAA is following the lead of Congress on this one, but I'm not sure everyone is looking way out there and seeing what is going to happen to the communities.

Mr. HORN. Sort of an unfunded Federal mandate.

Mr. KRASNER. Sort of.

Mr. HORN. That we hear a lot of talk about.

Well, I thank you. Unless there are some other points you want to make in conclusion, or anything you have heard today you want to respond to, feel free.

I see no response to that question. I thank you all for coming. It has been very helpful testimony. We appreciate it. Sorry to keep you so late.

Let me thank, before we formally close, the professional staff that was involved in this hearing: Mr. Brasher to my left, your right, professional staff member on the subcommittee; Russell George, the subcommittee staff director; Anna Young, professional staff member on the subcommittee; and then Mr. Richardson, the clerk of the subcommittee; our two counsels, Mark Uncapher and Michael Stoker; and I thank the minority staff too, David MacMillen; and we thank of course, our recorder, Alma Kristoffersen. So thank you, Alma.

And with that, this hearing is adjourned.

[Whereupon, at 5:40 p.m., the subcommittee was adjourned.]

[Additional material submitted for the record follows:]

PREPARED STATEMENT OF DAVID R. HINSON, FEDERAL AVIATION ADMINISTRATOR

Mr. Chairman and Members of the Subcommittee:

Throughout government, we are examining how we can best serve the American people. This is especially true of services that affect our economy and safety. The American people want a better, more efficient government, and understand that change is necessary to reach this goal.

The air traffic control (ATC) system, operating under the constraints of a traditional government agency, is simply unable to keep pace with the industry that it very literally controls. This is the only 24-hours-a-day, 365-days-a-year government operation that is directly and actively involved in the minute-by-minute activities of an \$80 billion industry. Therefore, the inefficiencies that flow from the current government structure quickly become this industry's problems.

It is estimated by the airlines that ATC system delays today cost them and their passengers in excess of \$3.6 billion a year. This comes at a time when this industry is struggling to regain its financial footing. The \$3.6 billion in delay costs are more than the industry has ever made in profits in a single year. These types of losses can mean the difference between an industry that can make ends meet and one that cannot.

THE NEED FOR CHANGE

In spite of differences of opinion over what should be done to address the problems of the ATC system, there is considerable agreement on the need for change. The challenge and responsibility that we all share is to ensure that the projected growth of aviation—over 300 million more enplanements in this country within the next decade—can be handled safely and efficiently. But, when we look at the state of today's system, and at growing passenger demand and especially at the budget outlook, we cannot assure the American people or the Congress that we will be able to provide the level of service that we have today unless we make fundamental changes to our system.

WHAT IS WRONG WITH TODAY'S ATC STRUCTURE

To be able to handle this country's air traffic safely and efficiently, we need a system that can:

- 1) take advantage of new technologies;
- 2) place and retain people where we need them;
- 3) be flexible enough to respond to change;
- 4) use borrowing to finance major capital programs; and
- 5) plan for the future, and be able to implement that strategy in a timely manner.

Unfortunately, as studies for the last decade have indicated, the FAA does not have those tools. First, we have a procurement system that makes it virtually impossible to keep pace with new technology. The evidence is found throughout the system.

- At Washington's National Airport, the computer that supplies critical information to controllers is a 1960's Univac.
- Virtually all of the 2300 radar displays in our en route centers are over 23 years old.
- We have more than 500 landing systems that are between 15 and 30 years old.
- We have close to 400 radars that are between 15 and 30 years old.
- Nearly all of the largest communications switches in our en route centers are over 29 years old.
- And, in an age when generations of computer technology are measured in months, we still must purchase vacuum tubes, a technology invented at the time of the Wright Brothers' first flight.

For many of these systems, the original manufacturer no longer exists. Spare parts are not available. In order to avoid shut-downs, FAA technicians must cannibalize other equipment, or go to machine shops to custom-build old technology.

Second, the personnel system is, in a word, inflexible. It is unable to match resources with real personnel needs. It makes it far too difficult to reward good work, to deal with poor performance, or to staff high-cost, busy facilities.

Third, the budget system is one that simply does not support long-term, business-like planning or timely acquisition. It is a system that requires the FAA to set aside the funds needed for a contract, even if the money will not actually be spent for several years. It is an environment in which the FAA gets its budget in over 160 specific line items, with limited ability to make changes. It is a budget process that forces the FAA to try to plan for the future without knowing how much money will actually be provided, or what strings will be attached. More importantly, as long as FAA funding is appropriated through the traditional government process, pressures to balance the budget will make it impossible to obtain the money necessary to modernize and operate the ATC system—no matter how much users pay into the trust fund.

To understand this fully, we must recognize that the FAA's air traffic control services are directly related to the size and activities of the aviation industry. Accordingly, as demand on the system grows, so does the cost of operating the system. But as we look to the immediate future, we see those two lines—growth in demand and funding—going in opposite directions. Over the next seven years, commercial airline operations are projected to grow by close to 20%. General aviation activities will grow by another 7%. But, under the budgets now being considered by the Congress, the FAA would be forced to meet this demand with budgets at least 20% smaller than today's.

That simply won't work. The result of this outlook is a system that won't be able to keep pace with demand. So, choices will have to be made: either to accept this and possibly compromise the safety and efficiency of the system, or to make major changes to the system, scaling back or eliminating many of the services provided today.

There is a third alternative, and it's the best of the three: take air traffic control out of this situation and put it on a sound business footing. The Administration's corporation proposal does this.

BRINGING ABOUT CHANGE

Over the years, both Congress and the FAA have tried to work within the existing structure to bring change. Just in the last decade, the FAA has reorganized itself over two dozen times to try to address these problems. But, clearly, those attempts have not "solved" the problems facing the ATC system.

In the last two years, this Administration has taken major and, frankly, unprecedented steps to address management problems at the FAA. In programs such as the Advanced Automation System (AAS) and Microwave Landing System we have made the tough decisions, cutting out elements that would have wasted hundreds of millions of taxpayer dollars. The top managers responsible for the AAS program have been replaced. We will continue to work to improve management and bring about necessary change, and we have made significant progress. But internal management changes alone cannot address the fundamental structural problems facing the ATC system. That is why, as we have continued to do what we can administratively, we have also proposed to remove legislative barriers to efficiency.

ADMINISTRATION PROPOSAL

The Clinton Administration proposal specifically and clearly addresses the problems facing the air traffic control system. It would establish a wholly-owned, not-for-profit government corporation, freed from the federal budget, personnel, and procurement systems. It would be financed by users, and have the ability to finance capital programs the way any private sector company would. There would be no General Fund contribution to the ATC system, which today accounts for about \$2 billion annually.

Importantly, it would leave the critical safety regulatory functions in the FAA, an agency that is fully accountable to the Congress, the Executive, and the American people.

SAFETY MODEL

Our proposal recognizes that ATC is fundamentally different from the regulatory functions of the FAA. It is modeled on the successful regulatory structure now in place for the literally thousands of corporate entities overseen by the FAA.

The safety record of U.S. aviation is the product of a partnership that recognizes the roles of government and the private sector. The reality is that government agencies just are not designed to run a business. And, in no other case do they try to. Suggestions that a corporatized ATC system could compromise safety simply do not hold up, for several key reasons. First, entirely private corporations are entrusted with major aviation safety responsibilities every day. When you take a trip, you board an aircraft that was designed and built by a private corporation, and is maintained and flown by private sector employees. The FAA regulates the safety of these corporations and employees. That is the reality of how our system works.

Second, we do not have to speculate about safety in a corporatized ATC system. A number of other countries (including the UK, which changed its structure over 20 years ago) have corporatized their systems. Even more to the point, we have air traffic control towers in this country that have been contracted out to private operators, and are operating safely and efficiently. In fact, the aviation community has supported this effort. Aircraft Owners and Pilots Association President Phil Boyer testified in support of contract towers before the House Aviation Subcommittee in February, 1995. Last December, a cross-section of aviation groups, including the National Business Aircraft Association (NBAA), sent a letter to me calling for expanded use of privatized towers. That letter makes the case well, and let me quote it.

As you know, the safety record of this program during the past decade has been exemplary, according to the FAA and the people who fly into these smaller airports. FAA requires the same level of training and safety oversight at contract towers as at FAA-operated facilities, and individuals at these facilities have worked an average of 18 years as controllers. Letter from John Olcott for NBAA (Dec. 21, 1994)

Small airlines, airports, pilots, and general aviation have gone on record in support of—and, in fact, calling for the expansion of—air traffic control facilities that are run not by the FAA, but by private sector contractors working under federal regulation. That goes beyond what we are proposing.

Third, some commenters, including the National Academy of Public Administration, have expressed a concern with "breaking up" ATC operations from the regulatory arm of the FAA, citing the history behind the formation of the FAA in 1958 as their rationale.

According to the Congressional Record, the 1958 FAA Act was prompted, in part, by a mid-air collision between two commercial airliners over the Grand Canyon in 1956. At the time, Congress found that establishment of an airway over the Grand Canyon was being delayed by a dispute between military and civilian aviation officials. In addition, at that time, the military and the Civil Aviation Administration were engaged in a dispute over navigation aid technology. Consequently, a primary objective behind the FAA Act was to "eliminate divided responsibility and conflicts of interest that exist . . . between civil and military agencies in the field of electronic aids to air navigation." (emphasis added, cited in Congressional Record, August 4, 1958, page 16084).

Today, nearly 40 years later, that problem has been solved. Military and civilian aviation officials work closely with one another, and in fact, military aviation officials took an active role in developing the Administration's ATC corporatization proposal.

In testimony before the House Aviation Subcommittee, Dr. Clinton V. Oster of Indiana University, a noted aviation safety expert, said,

It has not been necessary for the FAA to build, operate, or maintain aircraft for them to fly safely. Instead, very high levels of safety have been achieved through regulatory oversight. Similarly, it should not be necessary for the FAA to build, operate, or maintain the air traffic control system for it to operate safely either. Here again, very high levels of safety should be achievable through regulatory oversight. "Restructuring Air Traffic Control and Aviation Testimony" (Feb. 15, 1995)

Fourth, it is inappropriate to suggest that the very people who make this the safest system in the world would advocate a change that would compromise the safety record that they have built. The air traffic controllers suggested this concept three years ago, and they and the system technicians have consistently echoed the calls for fundamental reform.

We have compelling proof of what such fundamental change can bring—right in this area—at the Metropolitan Washington Airports Authority, which runs National and Dulles airports. Until 1987, those airports were part of the FAA. They suffered from decades of underinvestment. But, in the few years since Congress "spun-off" those airports in 1987 to the regional authority, the airports have embarked on a \$2 billion capital improvement program which would have been utterly impossible under the previous status quo.

We now have an excellent opportunity to act to finally correct these problems. The Administration has put forward its proposal, and we think we have developed a solution that works. But we respect the fact that others may have different ideas about how best to address specific issues. It is time to put those ideas on the table, and get a productive dialogue under way, so that we can find a way to improve the ATC system for its ultimate users, the American people.



